



Portfolio Media, Inc. | 111 West 19th Street, 5th floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

Libor Reversal Draws Fine Line Between 'Wrong' And Fraud

By **Dean Seal**

Law360 (February 1, 2022, 11:18 PM EST) -- The Second Circuit's controversial decision last week to overturn convictions for two former Deutsche Bank traders accused of rigging Libor has drawn criticism from some former government attorneys and underscores the proven challenges of prosecuting fraud on Wall Street.

A unanimous three-judge panel **ruled on Jan. 27** that the U.S. Department of Justice had not presented enough evidence to support the fraud convictions of Matthew Connolly and Gavin Black, former Deutsche derivatives traders charged with pressuring bank employees to falsify lending estimates submitted for the calculation of the London Interbank Offered Rate, or Libor.

Deutsche Bank's Libor submitters testified at trial that they knew altering the submissions was "wrong" and intended to benefit the bank's derivatives positions, but according to the appellate panel, the government failed to show that those alterations resulted in submissions that were actually false or out of compliance with Libor submission instructions, since banks often made subjective choices when calculating their daily lending estimates for Libor submissions.

"The government failed to produce any evidence that any DB LIBOR submissions that were influenced by the bank's derivatives traders were not rates at which DB could request, receive offers, and accept loans in DB's typical loan amounts; hence the government failed to show that any of the trader-influenced submissions were false, fraudulent, or misleading," the opinion said.

The appellate judges emphasized in their order that the federal fraud statutes on which the government based its case "are not catch-all laws designed to punish all acts of wrongdoing or dishonorable practices."

Experts say the head-turning decision effectively undercuts the overarching theory of the government's long-running probe into Libor manipulation: that the traders involved were breaking the law.

"Some would still view it as wrong, but there's a line between wrong and criminal," Robertson Park, a partner at Murphy & McGonigle PC, told Law360. "That may be where the rubber is meeting the road."

What's This All About?

This is the second time the Second Circuit has reversed the convictions of bank employees charged with rigging Libor, the long-used interest rate benchmark that has fallen from grace following a series of scandals and revelations that bankers had been manipulating the rate in their favor.

While financial behemoths such as Deutsche Bank have **paid billion-dollar settlements** to resolve Libor-rigging claims from U.S. and U.K. regulators, the DOJ's attempt to hold individual bank employees liable for criminal charges has generally resulted in either guilty pleas or, more recently, convictions that have been overturned on appeal.

The Second Circuit **overturned the fraud convictions** of two former Rabobank employees in 2017

on evidentiary grounds, finding that prosecutors had relied on self-incriminating testimony gleaned from foreign authorities that couldn't be used in U.S. criminal cases.

The **trial convictions** of Connolly and Black more than a year later were a resounding victory for the federal government, which has struggled to deliver on its stated intention of prosecuting individuals for corporate crimes.

But the former traders, who were **sentenced to home confinement** in 2019, have maintained that their conduct was not unique and, moreover, never rose to the level of fraudulence. Their appeal to the Second Circuit was supported by the New York Council of Defense Lawyers, which said in May 2020 that the trial court had "watered down" the fraud standard to excuse prosecutors from proving that efforts to influence Deutsche Bank's Libor submission resulted in a submission that was actually false.

"Bad intent, even fraudulent intent, does not establish the crime of fraud," the group wrote in an amicus brief.

That argument won the day on Jan. 27, when the Second Circuit handed down a ruling that attorneys for Connolly and Black are celebrating as a full exoneration for their clients.

What Does It Take?

Attorneys who spoke with Law360 have offered mixed reactions to the reversal and the court's analysis in particular.

Park, who specializes in white collar defense at Murphy & McGonigle, was an assistant chief of the DOJ's criminal fraud section during its investigation of Barclays PLC's alleged Libor manipulation. Acknowledging that he might carry some bias from that experience, he nonetheless found the Jan. 27 order to be a "contortionist opinion."

"All power to the extraordinary work of the attorneys who got the convictions overturned for these individuals, but I did not really follow the logic of the opinion, of how they came to the conclusion that there was nothing in the setting of the numbers that was a lie," he told Law360. "It seems to me that it was a result that the court wanted to reach, and when you read the opinion, logically to me, it doesn't make a lot of sense."

A pair of former regulatory attorneys were more damning in their critiques. Tyler Gellasch, who previously served as counsel to Commissioner Kara Stein at the U.S. Securities and Exchange Commission, called the opinion "a head scratcher in every respect," and pondered what else prosecutors would have needed to do to secure a conviction.

"There isn't a reasonable dispute over whether the rates were manipulated. But the court suggests that as long as it's theoretically possible a knowingly false statement could be true, then somehow you may not be committing fraud," Gellasch, executive director of the investor trade group Healthy Markets Association, told Law360. "This outcome strains common sense and the law."

Salman Banaei previously served as senior counsel and policy adviser to Commissioner Bart Chilton at the U.S. Commodity Futures Trading Commission, which ran a civil investigation into Libor manipulation in tandem with the DOJ.

Now a co-head of public policy at blockchain data firm Chainalysis, Banaei said the evidence in the case clearly showed the traders had an intent to defraud and pushed Libor in a direction that benefited their trading book, yet the Second Circuit adopted a "disingenuous" reading of the fraud statutes.

"It seems like they wanted to acquit and came up with this new technicality to come up with the acquittals," he told Law360. "What does it take, really?"

But other attorneys say the decision is consistent with other rulings in manipulation cases and

correctly adheres to the limited scope of federal fraud statutes.

Tom Gorman, a Dorsey & Whitney LLP partner and former senior counsel for the SEC's enforcement division, told Law360 that the government bore the burden of "negating or eliminating various possibilities under which" the submissions at issue were not false.

"Rather than do this, it appears that the government tried to use experts to narrow the scope of required proof by narrowing what pricing was considered to the 'one true price,'" he said. "That, the court said, was not sufficient."

What's The Impact?

The Second Circuit's ruling is not necessarily final, with several attorneys telling Law360 that they expect the DOJ will at least seek a rehearing before the full Second Circuit.

But speculation already abounds about the impact of the appellate court's analysis on the world of white collar prosecution and defense.

One of Connolly's attorneys, Kenneth Breen of Paul Hastings LLP, told Law360 on Monday that the court's decision is not only a "repudiation of the DOJ's entire Libor manipulation theory," but also a significant pushback to the government's frequent use of federal fraud statutes to "punish all of the conduct that they themselves judged to be dishonorable and dishonest, or unfair."

Phara Guberman, Breen's colleague on the case, echoed that sentiment, saying, "That's what the government has really been trying to do with a lot of its recent wire fraud prosecutions — finding something that feels wrong or that they may think is unethical and trying to pigeonhole that into a wire fraud charge."

"The government has been trying to work backward and find something that feels wrong and then try to say that it was against the law," Guberman, a Paul Hastings partner, said Monday.

Ford O'Brien LLP partner Kevin O'Brien, a former federal prosecutor-turned-white collar defense attorney who isn't involved in the case, said he only sees the order as a positive since reversals "keep the government honest and sensitive to the possibility of error, which is always a good thing."

"Prosecutors should be especially careful before they bring market manipulation charges because the underlying facts are usually extremely complex and susceptible to self-serving hindsight," O'Brien told Law360. "In any case, given that the sentences imposed by the district court were extremely light — essentially time served plus modest fines — it is hard to argue that serious wrongdoing has now gone unpunished."

But critics of the Second Circuit's ruling raise concerns about the adverse effect it could have on prosecutions of corporate financial crimes.

Gellasch argues that the Manhattan federal appeals court has cast significant doubt on the government's ability to bring fraud and manipulation cases going forward.

"Hamstringing the government's ability to bring cases against obvious market manipulators sends a terrible message to investors and severely undermines the integrity of the markets," he said.

Banaei is similarly concerned that the appellate court's ruling is a "one step forward, two steps back" situation for pursuing white collar crime. Manipulation cases often don't entail a lot of direct evidence, because banks have become adept at training employees to limit what they put in communications that could be discoverable, he said; the Connolly and Black case, meanwhile, involved plenty of direct evidence — including emails and chats between the traders and Libor submitters, as well as cooperating witness testimony — and even their convictions didn't stand up.

"If you're going to make it this hard to convict employees that engage in fraudulent wrongdoing inside of our very powerful financial institutions, that has a bigger public policy impact than I think

the Second Circuit has taken into account," Banaei told Law360.

For its part, the DOJ said in response to the Second Circuit's ruling that its "unwavering commitment to prosecuting individuals and corporations responsible for white collar crimes is unchanged" and that it was still confident in its "ability to detect, investigate and prosecute market manipulation crimes to the fullest extent."

Park of Murphy & McGonigle said he doubted the decision would affect the dynamics of the DOJ's current investigations, although it may lead prosecutors to consider bringing manipulation cases in other venues outside the Second Circuit.

Waymaker LLP partner Keri Axel, a former federal prosecutor, said she also doesn't expect the ruling to upset the DOJ's institutional appetite for bringing complex cases that carry a high deterrence value, even if those cases might be difficult to prevail on.

"When you walk into the Southern District of New York, you see sketches throughout the lobby of judges officiating over various high profile white collar and national security cases," she told Law360. "I would say that has a profound impact on creating a culture where prosecutors want to bring these kinds of cases. This ruling won't change that."

--Editing by Emily Kokoll and Jay Jackson Jr.

All Content © 2003-2022, Portfolio Media, Inc.