Law

The Civil Justice System
Civil Litigation

- Beginning the Civil Action
- Filing the Complaint
  - Jurisdiction
  - Grounds for relief (what are you suing for, how did the defendant harm you?)
  - Demand for judgment (how have you been damaged; how much money do you want?)
Discovery

- Taken on any matter, not privileged, that is relevant or may lead to relevant evidence

1. Oral Depositions
   - Sworn testimony under oath

2. Interrogatories
   - Can only be served on parties to the action
   - May object to question
   - Sworn to under oath
   - Can be used to impeach

3. Requests to Produce Documents
Discovery (cont.)

- Electronic Discovery
- Litigation Hold Procedures
  - Begins when lawsuit is “reasonably anticipated”
- Counterclaim
- Cross-claim
Simultaneous Civil and Criminal Actions

- Parallel Proceedings (civil and criminal proceeding at the same time)
- In a civil case, the Fifth Amendment privilege against self-incrimination is very limited
Alternative Dispute Resolution

- Mediation
  - Impartial third person assists parties in reaching a settlement

- Arbitration
  - Decision on the merits made by an arbitrator
  - Can be binding or nonbinding
Trial of a Civil Case

- Jury does not have to be 12 people
- Need not be unanimous
- Preponderance of the evidence
  - 51%—more likely than not
- Fifth Amendment self-incrimination is limited
- Judge may sanction parties, including entry of judgment
- Both sides may appeal
Trial of a Civil Case

- Plaintiff who obtains money judgment must often take additional steps to collect
- Post-judgment discovery
- Fidelity insurance (bond) claims
1. In U.S. federal civil cases, either party may take discovery on any relevant, nonprivileged matter.

A. True
B. False
Correct Answer: A

- Discovery refers to the formal process whereby the parties collect evidence and learn of the details of the opposing case. Under U.S. federal rules, either party may take discovery regarding any matter, not privileged, which is relevant to the subject matter of the action, or which may lead to admissible evidence.
2. In the United States, both sides may appeal from an adverse verdict after a civil trial.

A. True
B. False
Correct Answer: A

- Both sides may appeal from an adverse verdict, either as to liability or damages. As in the U.S. criminal system, the appellate court is largely limited to reviewing the legal decision of the court rather than the factual determination of the fact finder. The appeals court may reverse and remand for a new trial on some or all of the issues, may order that a certain portion of the awarded damages be remitted, or may enter final judgment, if legal grounds are clear, in favor of either party.
Sample Prep Question

3. Which of the following statements concerning interrogatories in a U.S. federal civil trial is MOST ACCURATE?

A. Interrogatories are for initial discovery purposes only, and responses may not be used as evidence at trial.
B. Interrogatories need not be sworn to under oath by the responding party.
C. Interrogatories can only be served on parties to the suit.
D. Interrogatories may not be used to impeach a witness at trial.
Correct Answer: C

- Interrogatories are questions that are submitted to an opposing party in a suit; they are something like a written deposition. Therefore, interrogatories cannot be given to any witness or potential witness who is not a party to the lawsuit. Interrogatories are submitted to the party in writing. All answers to interrogatories must be sworn to under oath.

- Responses to interrogatories are not binding, meaning the responding party may offer testimony that is inconsistent with its responses to interrogatories. However, the inconsistent response to an interrogatory can be used to impeach (discredit the testimony of) the witness at trial.
Sample Prep Question

4. Under the U.S. Federal Rules of Civil Procedure, an organization’s duty to issue a “litigation hold” that suspends the destruction of potentially relevant documents arises at the point when litigation is reasonably anticipated.

A. True
B. False
To comply with the legal obligations to preserve information relevant to litigation, such as those under Rule 26 of the Federal Rules of Civil Procedure, organizations should create “litigation hold” procedures. These are the steps taken to notify employees to suspend the destruction of potentially relevant records. The duty to issue a litigation hold arises when litigation is “reasonably anticipated.”
Law

Securities Fraud
Federal Regulation

- Securities Act of 1933
  - Regulates public offering, issuance

- Securities Exchange Act of 1934
  - Regulates trading
  - Rule 10b-5
  - *To employ any device, scheme, or artifice to defraud*
  - *To make any untrue statement of a material fact or to omit to state a material fact*
  - *To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security*
SROs

- Government delegates significant regulatory authority to “self-regulatory organizations” (SROs).
- Financial Industry Regulatory Authority (FINRA): FINRA, which is overseen by the SEC, regulates all firms selling securities in the United States.
- National Futures Association (NFA): The NFA, which is overseen by the CFTC, regulates the commodities and futures industry.
State Regulation

- State securities laws are often referred to as “blue sky laws.”
- Uniform Securities Act for states:
  - Registration of the security
  - Registration of the professional (broker-dealer)
  - Full and fair disclosure of all material information
What Is a “Security”?  

- Default definition is an “Investment Contract”
- The “Howey” Test
  - Investment
  - Common enterprise
  - Expectation of profits
  - Efforts of others
Types of Securities

- Traditional Securities
  - Stocks, bonds, CDs
- Futures and options
- Investment Contracts
  - Ponzi, pyramid schemes, oil and gas interests
Securities Fraud Schemes

- Churning
- Unsuitable Recommendations
- Operating Without a License
- Insider Trading
- Disclosures (Misrepresentations and Omissions)—must be material
  - Would a reasonable investor wish to know this information to make an informed decision?
Sample Prep Question

1. One type of securities fraud involves brokers who engage in excessive trading of a customer account to create commissions for themselves and their firm. This type of fraud is called which of the following?

A. Conversion
B. Parking
C. Front running
D. Churning
Correct Answer: D

- *Churning* is the excessive trading of a customer account to generate commissions while disregarding the customer’s interests. Specifically, churning occurs when an investment professional excessively trades an account for the purpose of increasing his commissions instead of furthering the customer’s investment goals.
2. According to the U.S. Uniform Securities Act of 2002, a model act from which many state securities laws are based, certain conditions must be in place before a security can be sold or offered for sale. Which of the following correctly lists those conditions that must be present?
Sample Prep Question

A. A registration in place to cover the security, the listing of the security on a national stock exchange, and a registered broker-dealer

B. A registration in place to cover the security, a registered securities professional, and full and fair disclosure of all material information

C. A registration in place to cover the security, the listing of the security on a national stock exchange, and an administration agency to arbitrate securities lawsuits

D. A registration in place to cover the security, full and fair disclosure of all material information, and an administration agency to arbitrate securities lawsuits
Correct Answer: B

- The U.S. Uniform Securities Act of 2002 provides that, unless certain exemptions apply, a security cannot be sold or offered for sale until all of the following requirements are satisfied:
  - There is a registration in place to cover the security.
  - The securities professional is registered.
  - There is full and fair disclosure of all material information.
Sample Prep Question

3. For a financial instrument to be classified as an investment contract, and therefore, a security, under the U.S. *Howey* test, the instrument must be purchased by investors who display management activity in the instrument’s enterprise and have expectations of making profits that are to be derived from their own efforts.

A. True
B. False
Correct Answer: B

- Under U.S. law, the default definition of a security is the term investment contract, which was defined in the case of SEC v. Howey Co. In Howey, the Supreme Court established a four-factor test, which is known as the Howey test, to determine whether a financial instrument is an investment contract. The leading global definition of investment contract parallels the Howey test and requires the following four elements to be met:
  - There is an investment of money or other asset.
  - The investment is in a common enterprise.
  - The investment was made with expectations of making a profit.
  - The profits are to come solely from the efforts of people other than the investor.
Sample Prep Question

4. Which of the following is prohibited with regard to the purchase or sale of securities under Rule 10b-5 established by the U.S. Securities and Exchange Commission (SEC)?

A. Employing any device or scheme to defraud
B. Making any untrue statement of material fact
C. Engaging in any act, practice, or course of business that would operate as a fraud against any person
D. All of the above
Correct Answer: D

- Rule 10b-5 states that: “It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange:
  - To employ any device, scheme, or artifice to defraud,
  - To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
  - To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.”
Law

Money Laundering
Introduction

- *Money laundering* is the disguising of the existence, nature, source, control, beneficial ownership, location, and disposition of property derived from criminal activity.
Introduction

- **Placement**
  - Most legislation aimed at this step
  - Most often detected at this stage
- **Layering**
- **Integration**
Methods

- Using a Front Business to Launder Funds
- Provides cover for people, delivery, transportation
  - Overstating Reported Revenues and Expenses
  - Depositing, But Not Recording, Revenue
Favorite Businesses

- Bars, Restaurants, Nightclubs
- Vending Machine Operations
- Wholesale Distribution Businesses
Emerging Payment Methods

- Mobile Payments
  - Funds stored on mobile phones
  - Regulations not as sophisticated
  - Anonymity

- Digital Currencies
  - Bitcoin
  - Less strict (or no) regulations
  - Promote anonymity
Other Methods

- Money Service Businesses (MSBs)—regulations less strict
  - Currency exchangers
  - Check cashers
  - Issuers, sellers of traveler’s checks, money orders
  - Money transmitters
  - Prepaid access providers or sellers
Other Methods

- Insurance Companies
  - Redemption schemes
  - Prepayment schemes
  - Canceled policy schemes

- Alternative Remittance Systems
  - Lack of physical or digital transfer of currency
  - Parties form a local network and keep a ledger of amounts owed
  - Transferring funds is NOT necessarily illegal
  - Lack of identity makes them attractive to money launderers
Federal and State Law

The Bank Secrecy Act
- “Financial institution” definition broadly
- Currency Transaction Report (CTR)
  - Cash of more than $10,000 in or out
- Currency Reports by Nonfinancial Business (Form 8300)
- International Transportation of Currency or Monetary Instrument (CMIR)
  - Physical transportation of cash or checks of more than $10,000
- Report of Foreign Bank Accounts (FBAR)
  - Balance of more than $10,000 during the year
- Suspicious Activity Report (SAR)
  - Used to disclose known or suspected criminal offenses or transactions that involve money laundering
Federal and State Law

- PATRIOT Act of 2001
- Anti-Money Laundering Program
  - Internal policies, procedures, and controls
  - Designation of a money laundering compliance officer
  - Ongoing training program for awareness
  - Independent audit function to test the programs
- Office of Foreign Assets Control (OFAC)
  - SDN list
  - Financial Action Task Force on Money Laundering (FATF)
    - International recommendations
Sample Prep Question

1. __________ is a method of disguising money from illegal nonbusiness sources by recording more income on the books of a business than is actually generated by that business.

A. Overstating revenues
B. Integration
C. Depositing, but not recording, revenue
D. Churning
Correct Answer: A

- Overstating revenues occurs when the money launderer records more income on the books of a business than is actually generated by that business. The fictitious revenue accounts for the illegal funds that are secretly inserted into the company.
Sample Prep Question

2. Over time, Herman stole $500,000 dollars in cash from his employer. He deposited the cash in small increments into a bank account to avoid reporting requirements. He then transferred the stolen funds to an overseas account and proceeded with several additional transfers and bogus loans to foreign entities that he controlled. Finally, he moved the funds back home, disguising them as profits from investments. Which of the following stages of money laundering was Herman performing when he engaged in transfers and bogus loans to foreign entities?
Sample Prep Question

A. Placement
B. Layering
C. Integration
D. Structuring
Correct Answer: B

- The three stages of money laundering are placement, layering, and integration. *Layering* involves the creation of numerous transactions to prevent detection, such as moving funds between bank accounts, transferring funds from one form of currency to another, or transferring money between businesses. This is the stage Herman was engaged in when he created additional transfers and bogus loans involving foreign entities that he controlled.
Sample Prep Question

3. Which of the following financial institutions is NOT considered a money services business?

A. A prepaid access card provider
B. A depository investment bank
C. A currency exchange
D. A check cashing company
Correct Answer: B

Money services business (MSB) is a term used to define a regulatory class of non-depository financial service providers that transmit or convert money. MSBs generally include any business that operates in one or more of the following capacities:

- Currency exchangers
- Check cashers
- Issuers, sellers, or redeemers of traveler’s checks, money orders, or stored value
- Money transmitters
- Prepaid access providers or sellers