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# When Can Companies Recoup Advancement of Executives' Criminal Defense Costs? A Recent Decision Highlights Some Limits

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When corporate executives are charged with crimes, their companies often foot the bill for their defenses. Sometimes those bills can be hefty. And while companies sometimes seek to recoup the expenses when the executives are convicted, a recent decision from the influential Judge Jed Rakoff of the Southern District of New York makes clear that the criminal restitution process may not be their best approach. More broadly, it casts doubt on companies' efforts to casts themselves as "victims" of their executives' misconduct, at least in legal terms.

In *United States v. Petit,* 19-CR- 00850 (S.D.N.Y.), the defendants—Parker Petit and William Taylor—were respectively the CEO and President of MiMedx Group Inc., a publicly-traded biotechnology company. In November 2019, a grand jury in the Southern District of New York indicted them for securities fraud. According to the indictment, the two executives entered into secret deals with several business partners to falsely boost the company's 2015 revenue figures, leading to an increase in the company's stock price. Both executives profited personally because the value of their own holdings in the company stock increased.

Petit and Taylor fought the charges, and retained major law firms for their defense. Under the company's articles of incorporation, bylaws, and indemnification agreements, as well as applicable state law, the executives demanded that the company advance their defense costs, including attorney fees. Those costs eventually ran into the tens of millions, including (by the company's account) nearly $30 million in fees. After both executives were convicted at trial in November 2020, the company refused to pay millions of dollars in outstanding fees, and the executives' law firms sued for the balance.

In an attempt to seek reimbursement of the defense costs, MiMedx asked the court to find that it was a "victim" entitled to restitution in the criminal case under the Mandatory Victim Restitution Act (MVRA) and the Victim and Witness Protection Act (VWPA), 18 U.S.C. §§ 3663 and 3663A. The company argued that in executing the fraud, Petit and Taylor had gone behind the

backs of others at the company and acted without authorization. In particular, it said, they had demoted the company's controller, who had raised questions about the accounting practices.

Judge Rakoff rejected the company's claims. As to Petit, the issue was straightforward: the statutory provision on which Petit was convicted, part of the Securities Exchange Act of 1934 (15 U.S.C. §§ 78j(b) and 78ff, and 17 C.F.R. § 240.10b-5) was not one of the laws for which restitution was permitted under the MVRA and VWPA. While Petit was convicted of aiding and abetting the Exchange Act violations under 18 U.S.C. § 2, Judge Rakoff agreed with other courts and held that the aiding-and-abetting statute did not provide an independent ground for restitution. And while the court was permitted to award restitution as a condition of supervised release (akin to probation following a prison term), it had already declined to order supervised release for Petit.

As to Taylor, the decision was more involved and instructive. The court explained that under the doctrine of *respondeat superior*, the criminal acts of a company's agents "taken on behalf of the corporation and within the scope of the agent's authority" could be imputed to the company itself, "unless the conduct solely furthered the employee's interests at the employer's expense." It then found that although Taylor may have been motivated by a desire to boost the value of his own MiMedx stock holdings, he had in effect acted to *benefit* the company by increasing the stock price, even if only temporarily. Thus, not only could MiMedx not be considered a "victim" entitled to restitution, it could have been charged criminally in the case. The court distinguished cases involving insider trading by corporate executives, which benefited only those executives at the company's expense.

Notably, Judge Rakoff rejected MiMedx's argument that Taylor had concealed his actions from the rest of the company. As the court put it, "MiMedx's efforts to root out misconduct, however extensive, do not immunize the corporation from liability when its employees, acting within the scope of their authority, fail to comply with the law." Thus, the court said, "the mere fact that the defendants may have misled other employees or agents of MiMedx does not relieve MiMedx of its criminal liability under the principle of *respondeat superior*, especially where, as here, the wrongdoing was committed by company's highest officers."

There are several takeaways from this decision:

1. Companies should be aware that illegal conduct by officers, employees, or other agents, if tending to benefit the company in any way, can subject the company to criminal liability even if the conduct is concealed from others in the company and even if the company has taken steps to prevent the conduct. Compliance programs should be designed and enforced with this standard in mind.

2. If a company advances criminal defense costs and fees for a current or former officer or employee charged with an offense that involved benefit to the company, it should not expect to recoup those costs and fees via a restitution order if the executive is convicted.

3. If a company intends to seek restitution for an offense, it should intervene in the case before the sentencing and advocate that, at a minimum, restitution be ordered as part of a term of probation or supervised release.

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