No. 13-1491

IN THE
Supreme Court of the United States

ANTHONY CUTI,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONER

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

TABLE OF AUTHORITIES—Continued

OTHER AUTHORITIES

ARGUMENT

Federal Rules of Evidence 701(c) and 702 clearly require all opinion testimony based on specialized knowledge to satisfy the disclosure and reliability requirements for expert testimony. A majority of circuits applies that requirement faithfully, but a minority—including the Second Circuit below—does not, to the serious prejudice of parties and contrary to the text and purpose of the Rules. Indeed, the loophole developed by the minority circuits revives the very division of authority that Rule 701(c)'s promulgation sought to end. The Court's intervention is needed to close that loophole and ensure uniformity in the Rules' application.

The government does not dispute the basic premises of the petition:

- that Federal Rule of Evidence 701(c) forbids non-expert witnesses from offering opinion testimony "based on" specialized knowledge;
- that a certified public accountant's mastery of Generally Accepted Accounting Principles (GAAP) is specialized knowledge;
- that lay witnesses Kevin Hallinan and John Henry gave extensive testimony, over Mr. Cuti's objection, using their accounting expertise to assess trial evidence and answer counterfactual hypothetical questions about proper GAAP treatment for various transactions; and
- that absent this Court's review, the government will continue to circumvent Rule 702 using the "expert in lay witness clothing" strategy condoned here.

Instead, the government offers sweeping justifications for the admission of accounting or similarly specialized testimony from lay witnesses. Those arguments only reinforce the need for this Court's review by illustrating how thoroughly the loophole adopted by the minority circuits undermines the gatekeeping mandated by Rule 702 and *Daubert* v. *Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993).

This issue is neither fact-bound nor case-specific, as demonstrated by the government's categorical, *legal* assertions as to when Rule 701(c) supposedly permits lay witnesses to testify "based on" specialized knowledge like accounting rules. Given the importance of the issue, especially when a criminal defendant's liberty hinges on its resolution, the petition should be granted.

I. THE SECOND CIRCUIT CHOSE THE WRONG SIDE OF THE SPLIT

Echoing the court below, the government argues that the accounting evidence at issue was (1) factual testimony or (2) lay opinion testimony admissible under Rule 701. The government offers a single argument for both conclusions: that an expert who has some personal knowledge of the case may offer wide-ranging opinions based on specialized knowledge, including answering counterfactual hypothetical questions. Neither conclusion is correct: such evidence is inadmissible under Rule 701(c), as at least five circuits have ruled.

A. The Circuits Are Divided

The majority of circuits addressing the issue holds that opinion testimony based on specialized knowledge must be qualified as expert testimony under Rule 702, even if the witness has some personal connection to the

case. Pet. 18-21. A minority of circuits, including the Second Circuit, takes an impermissibly contrary view. *Id.* 21-23. This divergence cannot be reconciled by blanket claims about "context-specific analysis" (Opp. 16), because the split occurs at the *conceptual* level.

The majority rule properly focuses on whether the testimony requires witnesses "to apply knowledge and familiarity … beyond that of the average layperson." *United States* v. *Ganier*, 468 F.3d 920, 926 (6th Cir. 2006). It permits lay opinion testimony only insofar as "the opinions or inferences do not require any specialized knowledge and could be reached by any ordinary person." *James River Ins. Co.* v. *Rapid Funding, LLC*, 658 F.3d 1207, 1214-1215 (10th Cir. 2011) (internal quotation marks omitted); *see also United States* v. *Conn*, 297 F.3d 548, 553 (7th Cir. 2002) ("[A]ll testimony based on scientific, technical or other specialized knowledge is subjected to the reliability standard of Rule 702.").

In these circuits, the admissibility of "testimony involv[ing] technical expertise" under Rule 701(c) does not depend on it being within "the realm of [the witness's] particularized experience" as the government asserts (Opp. 17), but rather on it being within "'the realm of *common* experience,'" *James River*, 658 F.3d at 1214-1215 (emphasis added). Revenue recognition under GAAP lies well outside the realm of the common knowledge of an "ordinary person." *Id.* Thus, had Mr. Cuti been tried in one of the majority circuits, the accounting testimony central to his conviction would have been excluded.

The government's failure to recognize this distinction dooms its cursory attempt to reconcile the circuit split. It asserts that the majority circuits exclude opinion evidence only when the witness's expertise was not,

at least in part, derived from personal knowledge of the facts of the case. But that theory does not withstand scrutiny: in many of the cited decisions, the excluded testimony actually did fall within the witness's "particularized experience," as the government puts it. Opp. 17-18.[1] For instance, the Sixth Circuit excluded testimony from Medicare auditors about reimbursement procedures despite acknowledging that the witnesses were "personally involved in the factual underpinnings of the case," having audited the transactions at issue. *United States* v. *White*, 492 F.3d 380, 401 (6th Cir. 2007). And the Tenth Circuit excluded an opinion about an allegedly defective pressure cooker despite the witness's knowledge of device design obtained through his years "servic[ing], clean[ing], and operat[ing] pressure cooker machines similar to, *and including*, the one [at issue]." *Randolph* v. *Collectramatic, Inc.*, 590 F.2d 844, 847 (10th Cir. 1979) (emphasis added).

Nor is the government's position supported by the advisory committee's explanation that Rule 701(c) permits businesspeople to testify to "the value or projected profits of the business" because such witnesses have "particularized knowledge" of their business. Fed. R. Evid. 701, 2000 advisory committee's notes (contrasting such testimony with the testimony of "an accountant, appraiser, or similar expert" who testifies "because of experience, training or specialized knowledge within the realm of an expert"). If anything,

[1] Because the majority circuits apply a categorical rule excluding lay opinions based even in part on specialized knowledge regardless of "particularized experience," it is immaterial that some decisions by these courts exclude testimony that would also be excluded under the government's test. *See, e.g.*, *United States* v. *Wilson*, 605 F.3d 985, 1026 (D.C. Cir. 2010).

the invocation of "particularized knowledge" to justify this testimony's admission only accentuates the circuit split and the need for this Court's review.

The minority courts, led by the Eleventh Circuit, have radically expanded the concept of "particularized knowledge" far beyond lost profits testimony to encompass testimony by a company's employees on any business-related topic, even when opinions are based on "years of experience within the field" instead of common experience. *See Tampa Bay Shipbuilding & Repair Co.* v. *Cedar Shipping Co.*, 320 F.3d 1213, 1220-1223 (11th Cir. 2003). Following suit, the Fifth Circuit held that Rule 701 broadly permits "testimony by business owners or officers on matters that relate to their business affairs." *Texas A&M Research Found.* v. *Magna Transp., Inc.*, 338 F.3d 394, 403 (5th Cir. 2003). These circuits have continued to expand the "particularized knowledge" loophole since then. *See, e.g.*, *United States* v. *Graham*, 643 F.3d 885, 896-899 (11th Cir. 2011) (allowing lay opinion testimony on fraudulent loan transactions based in part on witness's knowledge of some of the transactions at issue and in part on his "knowledge of mortgage fraud, which he had acquired through his experience as a former real estate closing attorney who had engaged in fraudulent transactions of that nature").

In contrast, the majority circuits reject the notion that "any witness can talk about his job" if specialized knowledge is involved. *Rodriguez* v. *General Dynamics Armament & Technical Prods.*, 510 F. App'x 675, 676 (9th Cir. 2013). Indeed, under the majority approach, even lost profits testimony by business owners is inadmissible when it "requires more than applying basic mathematics." *James River*, 658 F.3d at 1214. Consistent with the plain text of Rule 701(c), opinions

"based on specialized knowledge" are excluded, irrespective of whether they are also based on "pertinent" job experience (App. 12a). The Second Circuit's acceptance of such testimony, so long as it is not "'rooted exclusively [in the witness's] expertise'" (*id.*), squarely adopts the minority interpretation of Rule 701(c).

B. The Decision Below Is Wrong

The government defends the Second Circuit's ruling as "correct" (Opp. 9, 12), but that is not a basis to deny certiorari where there is circuit disagreement over the legal principle. It is for this Court to decide which side of the split is "correct." In any event, the Second Circuit was wrong.

The government asserts (at 10-11) that a witness's testimony "explain[ing] his own actions" or "state of mind" is factual. But the accountants did not simply testify to their own state of mind; such testimony would have been irrelevant here. Indeed, the district court steered the witnesses away from testimony about their own state of mind and instructed them to assess trial evidence from the purportedly objective "accounting point of view." App. 62a, 64a. The Second Circuit accordingly acknowledged that the witnesses applied "reasoning" to "hypothetical[s]" based on "earlier admitted testimony and exhibits." *Id.* 8a. That is paradigmatic opinion testimony.

In any event, testimony about whether "'withheld information would have affected' [the witnesses'] own actions" (Opp. 11), is decidedly *non*-factual. *See Washington* v. *Department of Transp.*, 8 F.3d 296, 300 (5th Cir. 1993) (witness testimony "as to what he would have done had he seen the warning label" was improper opinion testimony evaluated under Rule 701). The gov-

ernment's cases all involve witnesses asked to explain decisions they made in the past, not (as here) to speculate for litigation purposes about how they would apply technical principles in light of facts they supposedly did not consider. *See United States* v. *Giovannetti*, 919 F.2d 1223, 1226 (7th Cir. 1990) (witness permissibly explained his prior conclusion about defendant's gambling operation; the witness "was not being asked … to formulate an opinion in litigation—but rather to explain the basis on which he had drawn an inference in the past"); *United States* v. *Morton*, 391 F.3d 274, 277 (D.C. Cir. 2004) (officer permissibly explained the basis for his decision not to arrest someone).

The fact that the Second Circuit called the accountants' testimony "factual" is not a "case-specific holding" that makes this case an "inappropriate vehicle." Opp. 12. The court's holding depends on the asserted *principle* that testimony like that of the accountants here is "factual"—a principle that, if allowed to stand, creates a significant loophole in the Rules. That is not a vehicle problem; if anything, it underscores the breadth of the decision below and offers an additional reason for this Court to grant review to prevent circumvention of Rule 702.

Likewise, the fact that the parties did not dispute the tenets of GAAP in the abstract does not make the *application* of those tenets a matter of fact or lay opinion (Pet. 26-27), nor does it transform it into something "'straightforward and transparent to the jurors'" or a "'process of reasoning familiar in everyday life.'" Opp. 11, 13 (quoting App. 8a, 12a). Any such suggestion is utterly belied by the disputes among the accountants themselves about the proper application of GAAP. *See* C.A. Reply 29-30. And the notion that application of technical rules in this specialized area is proper fodder

for lay witnesses is equally inconsistent with this Court's recognition of the complexity of GAAP (Pet. 25-26), to say nothing of the multibillion-dollar accounting industry that depends on ordinary people being *unable* to use their own reasoning to apply GAAP. If anything, the fact that the specialized knowledge at issue here is accounting expertise—undoubtedly "within the scope of Rule 702," Fed. R. Evid. 701(c)—makes this case an especially good candidate for review.

Rule 701(c) contains no exception allowing testimony "'based on … specialized knowledge'" when the witnesses applying that knowledge are "following a fixed and 'undisputed' … set of rules." Opp. 13. Indeed, it would make little sense if the admissibility of lay opinion evidence turned on whether the parties agreed about the rules the witness should be applying. Even if parties stipulated to the laws of quantum mechanics, a witness applying those laws to the facts of a case would obviously be testifying as an expert.

Nor is there any basis to claim that the jury could "'readily discern whether the responses given were reliable.'" Opp. 11, 14 (quoting App. 8a). *Daubert* and the subsequent rule amendments emphasize the trial court's gatekeeping role precisely *because* jurors deciding matters involving specialized fields are easily misled by a witness's credentials and therefore cannot effectively assess reliability. 509 U.S. at 595. That risk was plainly realized here: GAAP did not specifically address income recognition for the type of real estate transactions at issue; industry practices were evolving at the time; and the accounting treatment was constantly debated by accountants in Duane Reade's Finance Department and the outside auditors. *See* C.A. Reply 29-31. Without a disinterested defense accounting expert to explain the uncertainty surrounding the

relevant transactions, the jury had no choice but to accept the oversimplified testimony of Hallinan and Henry based only on the aura of expertise their accounting credentials conferred. The Second Circuit's ratification of that approach was legal error.

II. THE ERROR WAS NOT HARMLESS

The Second Circuit did not hold that admitting the accounting testimony was harmless, despite the government's strenuous argument on that score. Nor did it hold that Henry and Hallinan could have testified as experts under Rule 702; the government abandoned that theory on appeal, and this Court should disregard the eleventh-hour attempt to resuscitate it. Besides the fact that their testimony was entirely self-serving, neither Henry nor Hallinan had done the work needed to offer reliable expert opinions. Pet. C.A. Br. 79-82. On the contrary, they formed most of their opinions on the stand. *See, e.g.*, App. 48a-49a (Hallinan noting his "predisposition" on the proper accounting treatment based "just upon hearing the facts at [a] high level").

The prejudice caused by the accountants' surprise expert testimony was not mitigated by the government's inadequate pretrial disclosures. Although the material Mr. Cuti received—primarily FBI reports documenting pre-indictment proffers with the witnesses—indicated that they had ventured some accounting opinions in interviews with investigators, that material was sent under cover expressly disclaiming any intent to call expert witnesses. CAJA 330-331. Given that Mr. Cuti's indictment was based solely on alleged sham transactions, not allegations of improperly-timed income recognition, and the prosecution stated in its opening statement that Hallinan would discuss the transparency of the transactions, not their accounting

treatment (*id.* 400), these disclosures gave no notice of the government's intent to elicit counterfactual accounting opinions from these witnesses.

Had Mr. Cuti been given proper notice, he would have retained an accounting expert to explain the complexity and subjective judgments involved in accounting for the transactions at issue. For example, with respect to one $400,000 concession, Hallinan concluded that GAAP required amortization, but Henry disagreed and recorded the income immediately. C.A. Reply 29. Two years later, Hallinan's successor concluded that Henry's approach was correct. *Id.* 29-30. At trial, however, Hallinan and Henry gave the misleading impression that there was one correct "accounting treatment" for the various transactions and that any contrary action was due to misrepresentations or withheld information. A disinterested expert would have countered Hallinan's and Henry's unreliable testimony.

In any event, the government cannot meet its burden to prove harmlessness. *See Kotteakos* v. *United States*, 328 U.S. 750, 764-765 (1946) (reversal required unless it is "highly probable" the error did not contribute to the verdict). The prosecution leaned heavily on the accountants' testimony to prove the principal disputed element of the securities fraud charges—"misstatements in the company's financial statements" (App. 4a)—as well as causation and scienter. *See* Pet. C.A. Br. 69-79.

The government's conjecture that the jury would have convicted even without the impermissible accounting testimony is premised on an oversimplified formulation of the case. Had Mr. Cuti's prosecution turned, as the government now claims, simply on whether a secret side agreement existed (Opp. 20), Mr.

Cuti should have prevailed. What constitutes a "side agreement" preventing immediate income recognition is an accounting question; Henry himself testified that a side agreement is an "obligation or requirement that Duane Reade had to perform." CAJA 2367; *see also id.* 2717-2725 (expectation of future business not a "side agreement"). Crucially, the government's only witness for the broker, WRG, denied that Duane Reade had any binding obligation to reimburse WRG for the concession payments. *Id.* 995-999. Based on that testimony, an objective accounting expert would have reasonably concluded that no side agreement existed. It was only through vague hypothetical questions posed to self-interested accountants that the government successfully advanced its unindicted theory of incorrectly-timed revenue recognition. Pet. 11-15, 31-32.[2] Had that testimony been excluded, the result would in all probability have been different.

* * *

The government concedes that it could not have proffered the challenged testimony via "an accountant unfamiliar with Duane Reade." Opp. 16. If the decision below stands—that a witness with specialized knowledge who made some "relevant decisions" in the past (*id.*) may then apply his expertise to draw *new* conclusions on the stand, without submitting a report, proffering any methodology, or giving the other side notice and opportunity to proffer contrary testimony—then

[2] *E.g.*, CAJA 2460 ("Q. … What accounting treatment would apply if [WRG] was being reimbursed for some or all of the costs of doing a deal? A. [T]hat would create a side agreement[.] … And in my opinion on the accounting treatment side, that would take away the ability to recognize this as upfront income."); *id.* 2477 (if WRG merely lacked "interest in buying [a] particular set of rights," that supposedly prevented income recognition).

the protections this Court announced in *Daubert* and safeguarded through Rule 701(c) are readily circumvented. The government has used this tactic before in other criminal cases, and no doubt will continue to attempt it whenever it can. *E.g.*, *United States* v. *Goyal*, 2008 WL 755010, at *3, 7 (N.D. Cal. Mar. 21, 2008) (mem.). The practice has not found favor in all circuits, however, and Mr. Cuti should not be disadvantaged simply because he was tried in New York.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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