UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO. 16-20549-CR-LENARD/OTAZO-REYES(s)(s)

UNITED STATES OF AMERICA,

Plaintiff,

v.

PHILIP ESFORMES, *et al.*,

Defendant.
_____/

DEFENDANT PHILIP ESFORMES' MOTION TO STRIKE AND EXCLUDE EVIDENCE CONCERNING CIVIL SETTLEMENT AND INCORPORATED MEMORANDUM OF LAW

The Defendant, PHILLIP ESFORMES, through undersigned counsel, respectfully moves this Court, pursuant to Fed. R. Crim. P. 7(d), 12(b)(1) and (b)(3), Fed. R. Evid. 401, 402, 403 and 408, and the Due Process Clause of the Fifth Amendment, for an order: (1) striking ¶ 11 of the "Manner and Means" section of Count 1 of the Second Superseding Indictment; and (2) excluding all evidence at trial of the December 2006 civil Settlement Agreement between Mr. Esformes (and others) and the United States in *United States v. Michel*, Case No. 04-2157-CIV-JORDAN (S.D. Fla.). In support of these requests, Mr. Esformes states the following:

1. On June 29, 2004, the Government filed a civil Complaint in this Court against Mr. Esformes, his father Morris, and 21 co-defendants alleging violations of the False Claims Act, 31 U.S.C. §§ 3729(a) ("FCA"), and related torts. *See Michel*, No. 04-2157 (ECF 1).[1/] The Complaint covered two distinct time periods. First, the Complaint alleged that from March 1 through December

[1/] Rather than clutter the record with exhibits, Mr. Esformes requests that the Court take judicial notice of the pleadings and orders in *Michel*.

1997, Larkin Community Hospital, Inc. ("Larkin") and its principals (not including Mr. Esformes) paid kickbacks to various physicians in violation of the Anti-Kickback Statute, 42 U.S.C. § 1320a-7b(b), and related statutes. Second, the Complaint alleged that after Larkin was sold, between January 1, 1998 and December 31, 1999, Larkin began "churning" patients from various skilled nursing and assisted living facilities owned by Mr. Esformes and his father, Morris. *Michel,* EFC 1, p. 5.

2. In October and November 2006, the parties executed a Settlement Agreement, attached hereto as **Exhibit 1**.[2/] In return for the government abandoning its damage claim, the defendants jointly agreed to pay the United States $15.4 million. The funds were paid, the settlement was accepted by the Court, and the Complaint was dismissed *with prejudice*. *See Michel*, EFC 248, 248-1, 249.

3. Section II(H) of the Settlement Agreement provides: "This Agreement is ***neither an acknowledgment of the validity of the claims alleged*** by the United States (as joined by the State of Florida), ***nor an admission of liability*** by the Defendants." *Id.* at p. 6 (emphasis added); *see also id.* at p. 9 ("Defendants specifically reserve and do not waive any defense or claim in any criminal prosecution or administrative action" except double jeopardy and statute of limitations defenses). Similar language in settlement agreements has consistently been construed to not constitute any kind of "admission" by the parties. *See, e.g., State Farm Mutual Augo. Ins. Co. v. B&A Diagnostic, Inc.*, 145 F. Supp. 3d 115, 1169 (S.D. Fla. 2015) (citation omitted); *Muzuco v. Re$ubmitIt, LLC*, No. 11-

[2/] The Government already attached a copy of the Settlement Agreement to one of its detention-related pleadings. *See* EFC 9-2.

62628-Civ-Scola, 2014 WL 11531784, at *3 (S.D. Fla. June 25, 2014). *Cf.* Fed. R. Evid. 408 (prohibiting the evidentiary use of offers or agreements to settle claims).[3/]

4. Since Mr. Esformes was first arrested, the government has been trying to use the Settlement Agreement as a sword against him. Thus, in its Motion For Pre-Trial Detention and Supporting Memorandum (EFC 9), the government characterized Mr. Esformes as essentially a repeat-offender for having not "halt[ed] ***his illegal activities.***" EFC 9, p. 14 (emphasis added). During the detention hearings that followed, counsel argued that any reliance on the Larkin settlement was improper because the government's allegations were "never tested, never proven, never agreed to" and that Mr. Esformes, in fact, did not contribute to any of the $15.4 paid by the defendants as a condition of the settlement. *See* Transcript, August 1, 2016 (DE74), at pp. 19, 42.

5. In the First Superseding Indictments in this case, the government nonetheless falsely alleged in the "Manner and Means" section of Count 1: "On or about December 18, 2006, PHILIP ESFORMES signed a civil settlement agreement with the United States Department of Justice ***admitting*** *that he paid kickbacks to physicians to cycle patients unnecessarily between the Esformes Network and Hospital 1*." First Superseding Indictment (EFC 198), at p. 10, ¶ 11 (emphasis added). That allegation was subsequently incorporated by reference into virtually every count.

6. Undersigned counsel drafted a motion to dismiss or to strike that allegation because it was false under the express terms of the Settlement Agreement. Before filing the motion, we contacted the government and expressed our concern that the Superseding Indictment falsely stated that Mr. Esformes had admitted to paying kickbacks and cycling patients, when the settlement

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[3/] While the Settlement Agreement states that it does not release the defendants from "[a]ny criminal liability," it did not purport to allow its existence or terms to be used as evidence in *any* future proceeding.

agreement expressly stated that it did *not* constitute an admission by any of the defendants to any of the allegations. After initially refusing to change or delete the "admission" allegation, the government chose to supersede a second time, now alleging:

> On or about October 18, 2006, PHILIP ESFORMES ***signed a civil settlement agreement*** with the United States Department of Justice, ***resolving allegations*** that he, and others, paid kickbacks to a physician to admit Medicare and Medicaid patients from the Esformes Network into Hospital 1, ***where they received medically unnecessary services***. In the settlement, ***PHILIP ESFORMES did not acknowledge the validity of the claims*** alleged by the United States or admit liability.

Second Superseding Indictment (EFC 200), at p. 10 (emphasis added.)

7. The existence of a settlement in which neither side admits anything is simply irrelevant under Fed. R. Evid. 401 and 402 and, therefore, not admissible. Moreover, evidence of settlements is directly barred by Fed. R. Evid. 408. The language used by the government in the Second Superseding Indictment is prejudicial insofar as it creates the misconception that Mr. Esformes *should have* "acknowledge[d] the validity" of the government's allegations that patients "received unnecessary services."

8. Codefendant Barcha has also moved for a severance, in part, because of the prejudice caused by the settlement allegations. EFC 240, pp. 3-4.

9. Accordingly, these allegations should be stricken from the Second Superseding Indictment as prejudicial surplusage under Rule 7(d) and all evidence relating to the settlement should be excluded under Fed. R. Evid. 401, 402, 403 and 408.

MEMORANDUM

INTRODUCTION

The Settlement Agreement will prejudice Mr. Esformes' jury through slights and innuendos drawn from the existence of a settlement agreement tied to allegations of kickbacks and patient cycling that were never proven nor admitted. The government seeks to adopt a construction of Rule 408 that is contrary to the weight of authority and would contravene the purposes of the Rule, which are to exclude non-probative evidence and to encourage settlements. While Rule 408 permits settlements to be used for limited "other purposes," that is just a Trojan horse in this case to get evidence concerning the settlement before the jury and argue that it represents an implied concession of liability or a reason for the jury to convict Mr. Esformes for allegedly continuing the conduct that was at issue in the Larkin litigation. This misuse of the "other purposes" exception to circumvent the Rule 408 prohibition on the use of settlement agreements should be rejected by the Court.

I. RULE 408 PROHIBITS USE OF SETTLEMENT EVIDENCE IN SUBSEQUENT LITIGATION INVOLVING SIMILAR CLAIMS

Rule 408 of the Federal Rules of Evidence provides:

> (a) Prohibited Uses. Evidence of the following is not admissible--on behalf of any party--either to prove or disprove the validity or amount of a disputed claim or to impeach by a prior inconsistent statement or a contradiction:
>
> > (1) furnishing, promising, or offering--or accepting, promising to accept, or offering to accept--a valuable consideration in compromising or attempting to compromise the claim; and
> >
> > (2) conduct or a statement made during compromise negotiations about the claim--except when offered in a criminal case and when the negotiations related to a claim by a public office in the exercise of its regulatory, investigative, or enforcement authority.

> (b) Exceptions. The court may admit this evidence for another purpose, such as proving a witness's bias or prejudice, negating a contention of undue delay, or proving an effort to obstruct a criminal investigation or prosecution.

In *United States v. Arias*, 431 F.3d 1327 (11th Cir. 2005), the Eleventh Circuit held that Rule 408 applies in criminal cases. The Court acknowledged the two justifications for the exclusions that Rule 408 requires: (i) the evidence is irrelevant, as the compromise at issue may have been motivated by a desire for peace rather than any concession as to the merits of the party's position; and (ii) the exclusion promotes settlement of disputes." 431 F.3d at 1337. The Eleventh Circuit explained why these principles should apply in criminal cases:

> It is self-evident that a defendant in a civil suit is far less likely to offer to settle a claim if evidence of that offer can later be introduced to prove criminal liability for the same conduct. Limiting Rule 408 to civil proceedings thus undermines the public policy in favor of compromise that the Rule aims to further. Moreover, while the . . . . interest in accurate determinations in criminal trials [may outweigh] the interest in promoting civil settlements, this rationale overlooks a basic premise underlying Rule 408: evidence of compromise is not necessarily probative of liability. Indeed, the [Federal Rules of Evidence] advisory committee's notes indicate that evidence of a settlement offer is often irrelevant to liability for the charged conduct, because "the [settlement] offer may be motivated by a desire for peace rather than from any concession of weakness of position." [Citation omitted]. In this light, permitting the admission of civil settlement offers in subsequent criminal prosecutions actually compromises the accuracy of the jury's determination.

Id. at 1338. The Eleventh Circuit then quoted a passage from the Fifth Circuit's opinion in *United States v. Hayes*, 872 f.2d 582, 890 (5th Cir. 1989): "It does not tax the imagination to envision the juror who retires to deliberate with the notion that[,] if the defendants have done nothing wrong, they would not have paid the money back." *Cf. United States v. Bailey*, 327 F.3d 1131, 1145 (10th Cir. 2003) (recognizing "the dramatic effect [that] evidence of an admission of liability could have upon a criminal defendant").

Courts have thus routinely rejected artful attempts to circumvent the rule. For example, in *Kramas v. Security Gas & Oil, Inc.*, 672 F. 2d 766, 772 (9th Cir. 1982), the Ninth Circuit affirmed the exclusion of a consent decree entered in an SEC enforcement proceeding because the decree "involved no finding of culpability and no judgment of wrongdoing, and contained a recitation that it did not constitute evidence of wrongdoing in the enforcement proceeding or in any other proceeding." The court noted that the probative value of the evidence was limited because it related to different transactions and different alleged misrepresentations, but "the prejudicial impact of the evidence upon the jury was obviously substantial. Moreover, admission of the evidence would have opened large areas of proof on collateral matters." *Id. See also Laserdynamics, Inc. v. Quanta Computer, Inc.*, 694 F.3d 51, 77 (Fed. Cir. 2012) (settlement agreement entered several years after hypothetical negotiation date and reached on the eve of trial should have been excluded as it was the least reliable for demonstrating economic demand for the patented technology and its probative value was greatly outweighed by the risk of unfair prejudice, confusion of the issues and misleading the jury); *Bradbury v. Phillips Petroleum Corp.*, 815 F.2d 1356, 1363 & n.10 (10th Cir. 1987) (excluding evidence of prior settlement); *Hanson v. Alpine Valley Ski Area, Inc.*, 718 F.2d 1075, 1078-79 (Fed. Cir. 1983) (finding that "since the offers [were] made after the infringement had begun and litigation was threatened or probable, their terms 'should not be considered evidence of an established royalty ...") (citation omitted); *Gribben v. UPS, Inc.*, 2006 WL 1600378, *2 (D. Ariz. June 5, 2006) (court properly excluded consent decree between the EEOC and defendant in plaintiffs ADA case as unfairly prejudicial based on concern "that a jury may use this evidence to conclude that UPS acted in conformity with this other 'wrong'...); *Ake v. Gen. Motors Corp.*, 942 F. Supp. 869, 880 (W.D.N.Y 1996) (excluding evidence of NHTSA investigation that was closed by settlement because

"the fact that an investigation occurred would be unduly prejudicial to [defendant], and would prove nothing"); *Scaramuzzo v. Glenmore Distillers. Co.*, 501 F. Supp. 727, 733 (N.D. Ill. 1980) (excluding evidence of prior settlements of "related claims"); *Citibank N.A. v. Citytrust*, No. CV-84-3786, 1988 WL 88437, at *2 (E.D.N.Y. Aug. 23, 1988) (excluding evidence of prior settlements to prove invalidity of trademark claims); *Abundis v. United States*, 15 Cl. Ct. 619, 621 (Cl. Ct. 1988) (evidence of settlement agreements concerning claims similar to those in present dispute inadmissible); *Playboy v. Chuckleberry Publishing, Inc.*, 486 F. Supp. 414, 423 (S.D.N.Y. 1980) (excluding evidence of prior settlements to prove likelihood of confusion).

The government's gambit also contravenes the rationales underlying Rule 408 – that settlements are not probative of underlying rights or liability, and that settlements should be encouraged as a matter of public policy (*see* Fed. R. Evid. 408, 1972 Advisory Committee Notes). Evidence of settlements is non-probative, irrelevant and therefore inadmissible because settlements may be motivated by factors other than a concession of wrongdoing or "weakness of position." *Id.*

Rule 408's prohibition on the use of settlement evidence also seeks to encourage the voluntary settlement of disputes. *See* Fed. R. Evid. 408, 1972 Advisory Committee Notes. "The fear is that settlement negotiations will be inhibited if the parties know that their statements may later be used as admissions of liability." *Central Soya Co. v. Epstein Fisheries*, 676 F.2d 939, 944 (7th Cir. 1980). When the pending claim and the settled claims are plainly similar or related, this concern is not obviated merely because the two claims are not identical – particularly when they both arise from a seemingly similar set of allegations. To admit such evidence would have precisely the same effect as admitting evidence of offers to settle the *pending* case – chilling a party's willingness to settle. *Abundis*, 15 Cl. Ct. at 621 (admitting evidence of prior settlements of similar claims "would give any

litigant pause before settling"); *see also* 2 Weinstein's Federal Evidence § 408.04, at 408-17 (use of such evidence in later litigation is "against public policy").

The facts of the present case fall squarely within the scope of Rule 408. Moreover, since the government claims that the present criminal case simply "represent[s] the continuation of the feud between the [parties]" which was settled, it "[e]ssentially ... arose out of the same transaction" and thus "there is even more reason to exclude such [settlement] evidence when [it is] between the same parties to the suit at hand." *Fiberglass Insulation, Inc. v. Dupuy*, 856 F.2d 652, 655 (4th Cir. 1988).

II. THE SETTLEMENT EVIDENCE CANNOT BE ADMITTED ON THE PRETEXT THAT IT IS NEEDED FOR "OTHER PURPOSES"

While it is true that evidence of settlement offers may be admissible if introduced for "other purposes," it must be for other *valid* purposes. *See Sawyer v. Southwest Airlines Co.*, Nos. Civ.A 01-2385 and 01-2386, 2003 WL 1741417, at *4 (D. Kan. Mar. 31, 2003); *Bradbury*, 815 F.2d at 1363. And even when a valid purpose exists, if introduction of such evidence would have the unavoidable effect of raising an inference of liability on the part of the settling party, the evidence must be excluded. Thus, when the "other purpose" for which evidence of a settlement is offered is "closely intertwined" to the issue of criminal culpability, admission of the evidence frustrates Rule 408's policy of encouraging settlements and the evidence must be excluded. *Trebor Sportswear Co. v. Limited Stores*, 865 F.2d 506, 510 (2d Cir. 1989); *Baltimore Therapeutic Equip. Co. v. Loredan Biomedical, Inc.*, No. 589-1085, 1993 WL 129781, at *36 (E.D. Cal. 1993) (same). As Judge Weinstein explains: "[C]are should be taken that an indiscriminate and mechanistic application of this 'exception' to Rule 408 does not result in undermining the rule's public policy objective .... The

[court] should weigh the need for such evidence against the potentiality of discouraging future settlement negotiations." 2 Weinstein's Federal Evidence ¶ 408 [05], at 408-31.

Trebor illustrates the proper balance between an alleged need for the evidence of a settlement offer and the potential harm caused by its use at trial. In *Trebor*, the plaintiffs sought to introduce evidence of the parties' settlement discussions to prove that their claims were not barred by the statute of frauds. *Trebor*, 865 F.2d at 510. Invoking Rule 408, the district court refused to consider these documents, and the Second Circuit upheld the exclusion of the evidence on appeal because the so-called "other purpose" – meeting the statute of frauds requirement – was too "intertwined" with the merits. *Id.*

Any claim by the government of a legitimate "other purpose" for injecting the earlier settlement into this case will be nothing more than a pretext. The government's true agenda is to parade the Settlement Agreement before the jury as some kind of indirect admission of liability. Indeed, the government has already misused the Larkin settlement by mischaracterizing it as a *direct* "admission" of guilt in the Superseding Indictment and during the detention litigation. The Court should reject the government's latest, thinly-veiled attempt to influence the jury indirectly by misusing the settlement agreement.

III. WHEN THE ISSUE IS "CLOSE," PUBLIC POLICY STRONGLY ENCOURAGES THE EXCLUSION OF SETTLEMENT EVIDENCE

"When the applicability of Rule 408 is a close call," courts should lean toward exclusion. *Dow Chemical Co. v. United States*, 250 F. Supp. 2d 748, 804 (E.D. Mich. 2003). Settlement evidence is excluded because (i) "settlement offers may be motivated by a desire for peace rather than any concession of weakness of position," and (ii) "public policy favor[s] compromise and settlement of disputes." Fed. R. Evid. 408, Advisory Committee notes on 1972 proposed rules.

Because of this strong public policy in encouraging settlements, even "when the issue is doubtful, the better practice is to exclude evidence of compromises or compromise offers." *Davis v. Rowe,* No. 91C 2254, 1993 WL 34867, at *5 (N.D. Ill. Feb. 10, 1993). *See also E.E.O.C. v. Gear Petroleum, Inc*., 948 F.2d 1542, 1546 (10th Cir. 1991); *Bradbury*, 815 F.2d at 1363; *Chase Manhattan Bank v. Iridium Africa Corp*., No. A 00-564 JJF, 2003 WL 22928042, at *2 (D. Del. Nov. 25, 2003); *Pharmastem Therapeutics. Inc. v. Viacell Inc*., No. C.A. 02-148 GMS, 2003 WL 22387038, at *3 (D. Del. Oct. 7, 2003); *Bower v. Stein Eriksen Lodge Owners Assoc., Inc*., 201 F. Supp. 2d 1134, 1140 (D. Utah 2002).

IV. THE SETTLEMENT EVIDENCE SHOULD ALSO BE EXCLUDED UNDER RULE 403

Additionally, any evidence concerning the 2006 Settlement Agreement and the underlying False Claims Act case is barred by Fed. R. Evid. 401, 402 and 403. As discussed above, Rule 408 is based on the premise that evidence of prior settlements is not probative of, and in fact *prejudicial* as to, the issue of liability. Thus, evidence concerning the settlement and the underlying dispute is barred by Rules 401-403 because that evidence would unfairly prejudice Mr. Esformes, confuse the issues, and mislead the jury. *See Williams v. Chevron USA*, 875 F.2d 501, 504 (5th Cir. 1989) (evidence of settlement for a purpose arguably allowed by Rule 408 was inadmissible under Rule 403 due to possibility "that the jury would have confused its purpose for that precluded by Rule 408"); *Kemper/Prime Indus. Partners v. Montgomery Watson Americas, Inc*., No. 97 C 4728, 2004 WL 725223, at *5 n.3 (N.D. Ill. Mar. 31, 2004). To admit evidence concerning the circumstances of the parties' settlement or of the underlying dispute would inevitably and unavoidably open the door to a wholesale discussion of the litigation and settlement, including that Mr. Esformes did not pay any part of the $15.4 million. The practical effect of permitting the presentation of such evidence would be to tempt the jury mercilessly with making the very inferences that Rule 408 seeks to

prevent. The prejudice to Mr. Esformes is obvious. In part for these same reasons, co-defendant Barcha has moved for a severance. *See* EFC 240, opp. 3-4.

And without a full discussion before the jury, the jury would be left with trying to draw inferences from stray fragments of the story concerning the parties' earlier dispute. The jury would be confused and misled by the introduction of partial evidence concerning that dispute without sufficient context or explanation, and might infer culpability in the present case based on an incomplete understanding of the facts concerning the earlier dispute. Mr. Esformes would be unable to set the record straight without opening the door to a wholesale discussion of the prior litigation, *i.e.*, precisely what Rule 408 was written to avoid. Putting Mr. Esformes on the horns of such a dilemma would be unfairly prejudicial and would skew the fair weighing of relevant evidence by the jury as it performs its role in the trial process.

CONCLUSION

For all of the foregoing reasons, the Court should grant the instant motion and (1) strike the allegations in the Second Superseding Indictment concerning the settlement, *see Marshall v. Qunicy Compressor, LLC*, No. 15-458-CG-C, 2016 WL 879311 (S.D. Ala. 2016) (striking paragraph from civil complaint citing to settlement agreement); and (2) exclude all evidence at trial concerning the settlement.

CERTIFICATION PURSUANT TO LOCAL RULE 88.9

Pursuant to the Local Rule 88.9, in a good faith effort was made to resolve the issues raised in the instant motion but opposing counsel indicated that the Government opposes the relief sought.

CERTIFICATE OF SERVICE

WE HEREBY CERTIFY that on April 13, 2017, this pleading was electronically filed with the Clerk of Court using the CM/ECF and that this document is being served on all counsel of record by transmission of Notices of Electronic Filing generated by CM/ECF.

Respectfully submitted,

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