

# Behind Scrushy's Courtroom Defense, Shifting Teams and Feuding Lawyers

HealthSouth Founder Taps A Birmingham Attorney In Unorthodox Strategy

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BIRMINGHAM, Ala. -- When Richard Scrushy went on trial last week in federal court here, the lawyer standing up to defend the former HealthSouth chief executive was James "Jim" Parkman III. With his good-ole-boy manner and deep southern drawl, Mr. Parkman is more accustomed to representing defendants accused of driving drunk than executives facing 58 counts of corporate corruption.

But he has help. Sitting at the defense table is the real legal mastermind of the case: Donald V. Watkins, a wealthy attorney, banker and entrepreneur from Birmingham. Although Mr. Watkins hasn't regularly practiced law since 1999, he has spent the past 20 months overseeing Mr. Scrushy's defense. Working closely, the two men have pursued an aggressive, and often unorthodox, defense strategy that has cost more than \$23 million so far.



## **Richard Scrushy**

Along the way Mr. Scrushy has retained -- and then shed -- more than four teams of lawyers, including some of the nation's most prestigious law firms. He and Mr. Watkins have tangled with their counsel over money and strategy. Warring sets of lawyers have locked horns for control of the high-profile case and hefty legal fees. Left in the wake of this legal confusion is a bitter ethics and fee dispute between Mr. Scrushy and the powerful law firm Jones Day.

In an interview last spring, before a federal judge issued a gag order in the case, Mr. Watkins likened the defense team to a football squad, in which the coach changes players depending on the skills required on the field. "We will do substitutions in a heartbeat," Mr. Watkins said. "The prime strategy is to win."

Victory may depend on whether Mr. Parkman and his small band of supporting lawyers, including Mr. Scrushy's son-in-law, can do the kind of heavy lifting more often handled by a large law firm with a deep bench of white-collar criminal experience. And that, in turn, may hinge on whether Mr. Parkman has sorted through the colliding strategies of his predecessor lawyers and the more than six million pages of financial and other documents that have been dumped on his desk since he was substituted on to the team in September. (See a [related article](#).)

"I've never seen a case of this profile involve a shift from law firm to law firm and accounting firm to accounting firm," said accountant Michael Mulligan, the executive director of FCL Advisors International LLC, Great Falls, Va., who was replaced as a forensic accountant on Mr. Scrushy's team. The turnover, he added, "in some ways is even bizarre."

Through a spokesman, Mr. Scrushy, 52 years old, says that he has not directly dismissed any of the law firms that have worked for him and that various attorneys have withdrawn in response to the addition of other firms or changes in strategy.

Mr. Scrushy was indicted in October 2003, after eight months of investigations into one of the biggest of the wave of business scandals that erupted after the late 1990s stock-market bubble burst.



***Donald V. Watkins***

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Raised in Selma, Ala., Mr. Scrushy worked as a gas-station attendant as a young man and eventually became a respiratory therapist. He dreamt up the idea that rehabilitative health care could be a big business and founded HealthSouth Corp. in 1984. With a domineering style, Mr. Scrushy built a chain of clinics that later expanded into surgery and operated in 50 states. In 1998, the company reported

revenue of more than \$4 billion. Mr. Scrushy led a flamboyant life, acquiring homes, cars and art. He started a country band and had buildings named for him.

The government claims that Mr. Scrushy led subordinates in a six-year, \$2.7 billion accounting scheme to defraud HealthSouth. Mr. Parkman will try to convince the jury that Mr. Scrushy's lieutenants committed the fraud without his knowledge. At least three of HealthSouth's former chief financial officers -- among 15 former employees who have pleaded guilty in connection with the financial fraud -- are expected to testify that Mr. Scrushy knew exactly what was going on.

Even before HealthSouth's troubles blossomed into a full-fledged scandal, Mr. Scrushy proved himself to be a nettlesome legal client, given to hiring multiple lawyers with overlapping responsibilities. In the late summer 2002, HealthSouth announced that a change in Medicare billing rules would result in a \$175 million reduction in its earnings. The company's stock plummeted 44% in a day, and questions surfaced about whether Mr. Scrushy had known of the impending announcement when he'd sold nearly \$100 million of stock beforehand.

With the help of one of HealthSouth's Washington lobbyists, Mr. Scrushy contacted Michael Deaver, former deputy chief of staff to President Reagan, and Jody Powell, spokesman during the Carter administration, both of whom went on to briefly advise him on public relations. Mr. Scrushy also contacted Lanny Davis, a former White House special counsel to President Clinton. Then a partner at Patton Boggs, a politically connected Washington law firm, Mr. Davis signed on to represent both Mr. Scrushy and HealthSouth. Mr. Davis promised Mr. Scrushy in an e-mail, made public during Congressional hearings, that he would represent the executive "personally even if a conflict arises in representing the company and you at the same time."

Immediately he moved to secure his position among a growing list of advisers including Haskell, Slaughter, Young & Rediker, HealthSouth's longtime Birmingham law firm, and Alston & Bird, a large Atlanta law firm retained to help with the mounting shareholder litigation in the wake of the stock's collapse.

In September 2002, just after Mr. Davis had been retained, Mr. Scrushy asked if he really needed all those law firms. Mr. Davis answered in the e-mail that, "I do not believe we need Alston & Bird at this time." He told Mr. Scrushy that he needed "a clear statement from you tomorrow concerning my role as counsel or co-counsel in all the litigation."

Despite Mr. Davis's opinion, Alston & Bird continued to represent HealthSouth until March 2003 and continues to represent some of its past and current officers and directors, according to a company spokesman.

Mr. Davis then brought in attorney Hal Hirsch, of Houston-based Fulbright & Jaworski, to conduct an independent review of the insider-trading allegations. Six weeks later, HealthSouth declared that the law firm had "cleared" Mr. Scrushy.



Mr. Hirsch had seen the press release before it went out, according to his later Congressional testimony. But after it went out, he demanded that the company issue a statement that it had overstated Fulbright's findings, according to e-mail correspondence at the time, made public during Congressional hearings.

Mr. Scrushy was incensed. "Hal you may not have noticed but I built this great company from an idea and a business card," the executive fired off from his BlackBerry e-mail device on a Saturday morning in November 2002. In a subsequent e-mail also made public, Mr. Scrushy wrote: "I need to give you a little advice about winning friends and influencing people."

Mr. Davis also blasted Mr. Hirsch, writing in an e-mail that his own firm believed that Mr. Hirsch's demand was "neither necessary nor adviseable."

HealthSouth ultimately issued a statement that backtracked from the claim that Mr. Scrushy had been cleared. Mr. Hirsch cautioned Mr. Scrushy in an e-mail that the chairman was "relying upon the promise of Lanny Davis that the media and his vision will be your magic bullet. He seems to tell you what you want to hear and when it does not work out he seems to find a fall guy. He has convinced you now that it is me."

Mr. Davis told Mr. Hirsch to cease communications with Mr. Scrushy. In an e-mail statement in response to questions last week, Mr. Davis said, "sadly Mr. Hirsch appeared to be blaming the messenger." Mr. Hirsch declined to comment.



Left to right, attorneys Donald Watkins, Thomas Sjoblom and Lewis Gillis with their client Richard Scrushy in front of the federal courthouse in Birmingham, Ala.

By February 2003, Mr. Davis was gone as well, dismissed by a letter from HealthSouth's in-house lawyer. "It breaks my heart, actually, because I would have expected you to be sensitive at least as a friend on a better way to do this," Mr. Davis told Mr. Scrushy in an e-mail also made public during the Congressional hearings. He now speculates that he might have been dismissed because he had been pushing the company to cooperate more with the Securities and Exchange Commission. "All I expected was a gracious thank you after working sometimes seven days a week, virtually around the clock," he wrote in an e-mail response to questions from The Wall

Street Journal. "Yet he not only never said [thank you] -- he abruptly cut off all communications. Which disappointed me."

Mr. Scrushy was subpoenaed by the SEC in February 2003, and when he met with the agency about a month later, he had another lawyer at his side, William Clark, a Birmingham criminal attorney who had little experience on complex SEC issues. Mr. Scrushy testified for eight hours.

That came back to haunt him when HealthSouth's top finance executives began pointing the finger at him as the architect of a massive fraud. On March 19, the SEC filed civil-fraud charges against Mr. Scrushy and HealthSouth and won a court order freezing an estimated \$250 million of Mr. Scrushy's assets. In the criminal case he faces charges that he made false statements to the SEC.

Holed up at his father's condominium in Orange Beach, Ala., with a spectacular view of the gulf, Mr. Scrushy was visited by attorneys from the Washington, D.C., law firm Baise & Miller, which had represented him in the past. The lawyers told Mr. Scrushy that he needed new lawyers to take on the SEC. They later also argued that Mr. Clark and Mark White, another criminal lawyer from Birmingham working on the SEC problem, weren't making sufficient efforts to have the asset freeze lifted. In the coming week, Mr. Scrushy spoke to other lawyers who fed his fears, according to a person familiar with the discussions.

"This was not their expertise," Mr. Scrushy said last year in an interview. "If I killed somebody, maybe they'd have been good attorneys." Mr. Scrushy made it clear that he was not happy and on April 3, the two lawyers resigned.

Mr. Clark declined to comment for this article. Mr. White said in a recent interview, "In a short period of time, we were very active in our representation."

At that point Mr. Scrushy made an unusual move for a white businessman in Alabama. He turned for advice to former Birmingham mayor Richard Arrington. As mayor in the early 1990s, Mr. Arrington had been the target of a corruption investigation by the federal government. Mr. Arrington, an African-American, waged a provocative and racially charged fight, orchestrated by Mr. Watkins. Mr. Arrington, whose supporters argued that he was being targeted because he was black, was never indicted.

Throughout Mr. Arrington's ordeal, Mr. Scrushy was one of the few white business leaders in Birmingham to publicly support him. Mr. Scrushy over time built an unusual level of goodwill among African Americans. His HealthSouth clinics had brought sports and rehabilitative medicine to some communities for the first time and the company had sponsored a promotional show of big-time athletes including former football and baseball star Bo Jackson. Mr. Scrushy also was known to be a fan of Birmingham black televangelist Bishop Jim Lowe.

After federal agents raided HealthSouth's offices in March, Mr. Arrington told Mr. Scrushy to phone Mr. Watkins. "It was Arrington who got me on the line with Scrushy

and notified me that it was my time to stand with Scrushy,” Mr. Watkins, 56, said in an interview.

The son of a prominent African-American family in Birmingham, Mr. Watkins was a well-known political figure in town who sometimes held court at Lou’s Pub, a smoky establishment. He’d founded Alamerica Bank and had tried unsuccessfully to buy the Minnesota Twins.

Mr. Watkins was interested in taking Mr. Scrushy’s case. But he told his prospective client that it would distract from his other projects, including his efforts to purchase the Anaheim Angels baseball team. Therefore, he required a \$5 million retainer. Mr. Scrushy agreed.

Mr. Watkins warned that the price tag for Mr. Scrushy’s defense would be steep. During one meeting, a lawyer involved projected that the tab might run to \$10 million. Mr. Watkins disagreed, predicting that the costs would run to between \$20 million and \$40 million, according to a person familiar with the conversation.

Mr. Watkins told Mr. Scrushy that he would follow the same strategy he had pursued in defending the former Birmingham mayor, according to people involved. The idea was to swiftly answer every allegation made by the government or other defendants either in court or on the nightly news. Immediately, Mr. Watkins began publicly lashing out at prosecutors and the credibility of former HealthSouth employees striking plea bargains.

Mr. Watkins quickly reassembled the team he had relied on for Mr. Arrington’s defense, including Jonathan Rose, a partner in the Washington office of Jones Day, a roughly 2,200-lawyer firm. Mr. Rose, a former aide to President Nixon, represented Mr. Watkins in his efforts to acquire a Major League Baseball team. Mr. Watkins also brought in another firm from the Arrington fight: Thomas, Means, Gillis & Seay, which has offices in Birmingham and Montgomery, Ala.

The final senior member of the team was Thomas Sjoblom, a partner at Chadbourne & Parke, a century-old New York firm. The understanding of the lawyers was that if Mr. Scrushy’s assets were unfrozen by the SEC, each of the three firms would receive \$5 million.

Mr. Sjoblom, 55, had recently joined his firm after 20 years with the SEC. His goal was to help build the firm’s SEC enforcement and white-collar criminal practices, and Mr. Scrushy was a showcase client. Hired less than a week before a hearing on the asset freeze, Mr. Sjoblom closeted himself to prepare in a building behind Mr. Scrushy’s home on his estate in Birmingham.

After 11 days of testimony, Judge Inge Johnson released all of Mr. Scrushy’s cash, ruling that the SEC had failed to establish that he was involved in the fraud. Mr. Scrushy and his lawyers celebrated with a visit to Mr. Scrushy’s wine cellar. A week later, in May 2003, Mr. Scrushy paid more than \$21 million in fees to Mr. Watkins and three law firms, according to an Internal Revenue Service affidavit.

Mr. Scrushy continued to closely manage his case, along with Mr. Watkins. "After reviewing last month's bills, which came to more than \$1 million, I am sick," Mr. Scrushy wrote to his attorneys several months later. "I see tremendous waste and abuse. ...Please be responsible and efficient and do not let this happen to me. I am not an Enron or WorldCom."

Despite his victory in May, Mr. Sjoblom soon became a second-string player, as Mr. Watkins turned to Jones Day's Mr. Rose, with whom he had a closer relationship. On Sept. 7, at Jones Day's Washington office, Mr. Watkins met with Mr. Rose, Mr. Scrushy and Mr. Sjoblom to polish a 100-page report they delivered to the Justice Department the next day. "Several cooperating witnesses are known to have engaged in unsavory conduct, such as sexual misconduct involving children, adultery, wife-swapping, drinking and drug use," the memo stated. "The government will rely on such witnesses at its peril."

As Mr. Watkins and Mr. Rose continued to pursue what they called the "indictment avoidance" plan, Mr. Sjoblom spent time in Birmingham, working on civil suits filed against Mr. Scrushy and cozying up to his client. He soon had additional work when Mr. Scrushy dismissed Baise & Miller, which had been handling civil cases in Delaware and Alabama. The firm was terminated in a September 2003 e-mail from a Scrushy staffer, who told them Mr. Scrushy believed that Mr. Sjoblom needed "to be the one man controlling every piece of paper, every comment, and every response" in the civil cases.

Mr. Sjoblom also didn't like Jones Day's strategy of revealing its trial strategy to the Justice Department, according to a person familiar with his thinking.

Mr. Sjoblom occasionally spent the night in Mr. Scrushy's guesthouse. The two men watched African-American evangelical church services on TV and talked about their faith. "We found out very early on that we shared those common beliefs," says Mr. Sjoblom.

Mr. Sjoblom introduced Mr. Scrushy to Abbe Lowell, the Democratic counsel during the impeachment hearings of President Clinton and a well-known criminal defense lawyer. Mr. Lowell was planning to join Chadbourne, and the three men discussed whether the firm "might be able to do more for him than they might be doing at the time," says Mr. Lowell.

On Nov. 4, 2003, the indictment avoidance scheme collapsed when the government unsealed an indictment of Mr. Scrushy. That morning, Mr. Sjoblom drove Mr. Scrushy to the Federal Bureau of Investigation office in Birmingham so that he could turn himself in.

At Mr. Scrushy's arraignment, he was represented by a lawyer from Jones Day's Atlanta office. But Jones Day was on the verge of being benched.

In the wake of the indictment, Mr. Scrushy decided to change horses. "I liked Abbe," he later said of Mr. Lowell. Mr. Watkins demanded that Jones Day turn over its files

and the legal team's downtown Birmingham office space to Chadbourne & Parke. That firm quickly issued a press release headlined, "Richard M. Scrushy Names Trial Team to Defend Him."

It was not an amicable divorce. Mr. Watkins demanded that Jones Day return a portion of the fees Mr. Scrushy had already paid the firm. Jones Day insisted to Mr. Watkins that the money had been earned and argued that Mr. Scrushy still owed the firm an additional \$2 million. Jones Day refused to return any money, according to people familiar with the situation.

On Dec. 1, 2003, Mr. Watkins filed an ethics complaint on Mr. Scrushy's behalf with the D.C. Court of Appeal's arm that investigates ethics complaints. In a prepared statement, Mr. Rose said that his firm believes that Mr. Watkins's tactics in seeking the return of fees are "improper," and that the ethics investigator suggested to Mr. Scrushy that it was not the correct forum for resolving a fee dispute. However after wrangling by both sides, the dispute remains before the ethics investigator.

"Until Mr. Scrushy decided to discharge us, Mr. Watkins had nothing but praise for our work and was fully supportive of our efforts. However, his conduct since that time has been both surprising and mystifying on a professional as well as on a personal level," Mr. Rose wrote.

The relationship between Mr. Watkins and Chadbourne & Parke soon deteriorated, too. In late 2003, Mr. Lowell took the lead in the case, and Mr. Watkins became somewhat less involved. The two quarreled over strategy, say people familiar with the case. Mr. Watkins pushed for a vigorous public-relations offensive. Mr. Lowell preferred a quieter approach.

The tension peaked in March 2004, when the defense became convinced that prosecutors were concealing evidence that might be helpful to Mr. Scrushy. Mr. Lowell wanted to file a motion, under seal, in an attempt to learn more.

But Mr. Watkins's strategy won out. He, Mr. Scrushy and Mr. Sjoblom held a news conference on the courthouse steps in Birmingham, accusing the Justice Department of concealing evidence.

Mr. Lowell watched the action from behind a pack of cameras and reporters, visibly uncomfortable. Later that spring, the judge hearing the case issued an order restricting what the parties could say outside of court.

Meanwhile, Mr. Scrushy was coming to believe that Mr. Lowell wasn't dedicating enough time to his defense, say people familiar with the situation. Chadbourne withdrew from the case. A firm spokesman says that Mr. Lowell was always available to handle Mr. Scrushy's case. "No disagreement caused this withdrawal," said a firm spokesman. "It was a mutual decision."

That leaves Mr. Parkman as chief trial lawyer. The team had long considered bringing in Southern trial counsel and retained Mr. Parkman's four-lawyer firm in September. Mr. Parkman is being assisted by a lawyer in his firm, Martin Adams, Mr. Scrushy's

son-in-law; Art Leach, a former assistant U.S. Attorney from Georgia; Lewis Gillis of the Birmingham law firm Thomas Means and, of course, Mr. Watkins.

Through a spokesman, Mr. Scrushy says that he trusts Mr. Watkins and that "he is a friend." He called Mr. Parkman "a winner."

—Evelina Shmukler, Douglas A. Blackmon, Chad Terhune and Dan Morse contributed to this article.

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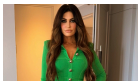
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