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What do the Decisions in *U.S. v. Skilling* and *U.S. v. Black* Really Mean for Corruption Prosecutions?

In *United States v. Skilling*, No. 08-1394, and *United States v. Black*, No. 08-876, the Supreme Court limited the government's ability to prosecute people for the intangible fraud of failing to provide "honest services" to the public or an employer. The honest services fraud statute's core purpose, to prosecute public and private corruption involving persons who accepted bribes or kickbacks, had morphed into a catch-all "moral compass" statute. Prosecutors used it to target conduct that may have been unappealing or unethical, or just "seemed wrong," but where there was little if any proof of personal financial gain from the conduct at issue. Additionally, prosecutors favored charging the honest services fraud statute rather than federal bribery and gratuity statutes because the latter carry lesser penalties and have more demanding elements of proof. More often than not, however, the government used the honest services fraud statute as an add-on count or alternative fraud theory to enhance indictments, increase the likelihood of convictions, and ultimately raise the stakes for defendants.

The Court's decisions¹ would appear to require federal prosecutors to refocus on core corruption and tangible fraud cases and resist the temptation to stretch the law to support prosecutions where a defendant receives no personal financial benefit. What remains to be seen, however, is whether the government will seek to amend the law to support broad criminalization of undisclosed conflicts of interest. In this regard, the Supreme Court in *Skilling* cautioned Congress that there are limits to the government's power and authority to proscribe such conduct without violating the Due Process Clause of the Constitution.

I. The Rulings – The Return to the Core Purpose of the Statute

Prior to *Skilling* and *Black*, the government pursued an expansive definition of fraud under federal law. In brief, the government alleged as a fraud a scheme by a public employee or corporate officer which allegedly deprived the public or company of "the intangible right to honest services."²

¹For a more in-depth discussion of the impacts on the business community of these and other recent decisions by the Supreme Court, see the *K&L Gates Global Governmental Solutions 2010 MidYear Outlook* at http://www.klgates.com/files/Publication/a1f110c4-bc91-4dc5-9c31-016decf2bbf9/Presentation/PublicationAttachment/c5d41a80-bace-4376-ae85-02bd0bc2633e/GGS_2010_MidYearReport.pdf.

² 18 U.S.C. § 1346 (2010) (including within the definition of a scheme or artifice to defraud "a scheme or artifice to deprive another of the intangible right of honest services").

In practice, this theory knew few bounds, and has been questioned for years.³ The statute's uneven application across the federal circuits after its 1988 enactment caused it to be, according to Justice Scalia, in a state of "chaos."⁴

Skilling was a high-profile prosecution arising from the Enron collapse in which Jeffrey Skilling was convicted of, among other crimes, a conspiracy based on three fraud theories – securities fraud, money or property fraud, and honest services fraud (depriving Enron of Skilling's honest services) – all related to Skilling's alleged scheme to disseminate false information regarding Enron's business performance.

Black was equally high-profile. Conrad Black was convicted of three counts of mail fraud which were based on both a money or property fraud and an honest services fraud theory, and obstruction of justice in connection with an alleged scheme involving "non-compete fees" that were paid to executives of Hollinger International.

In *Skilling*, the Court held that a limiting construction should be applied to the honest services fraud statute in order to avoid finding that it was unconstitutionally vague. It did so by applying it to its "core" application – schemes to defraud that

³ Dick Thornburgh, *Overcriminalization and the Need for Legislative Reform*, One Nation Under Arrest (Rosenzweig and Walsh, eds.), 2010; see also Lisa L. Casey, *Twenty-Eight Words: Enforcing Corporate Fiduciary Duties Through Criminal Prosecution of Honest Services Fraud*, 35 Del. J. Corp. L. 1 (2010); Randall D. Eliason, *Surgery with a Meat Axe: Using Honest Services Fraud to Prosecute Federal Corruption*, 99 J. Crim. L. & Criminology 929 (Fall 2009); Barry M. Hartman and Brian W. Stolarz, *Time and Place are Everything: When an "Honest Day's Work" Becomes "Honest Services Fraud"*, Newsletter of the ABA Criminal Justice Section's White Collar Crime Committee, August 2008; Daniel Cleveland, *Once Again, It is Time to "Speak More Clearly" About §1346 and the Intangible Rights of Honest Services Doctrine in Mail and Wire Fraud*, 34 N. Ky. L. Rev. 117 (2007) (stating that "Congress' attempt to restore order ostensibly muddied the water further," and cited other commentaries regarding the statute).

⁴ *United States v. Sorich*, 129 S. Ct. 1308, 1311 (2009) (Scalia, Dissent) (stating that "[t]hrough it consists of only 28 words, the statute has been invoked to impose criminal penalties upon a staggeringly broad swath of behavior, including misconduct not only by public officials and employees but also by private employers and corporate fiduciaries").

involve bribery and kickbacks.⁵ The Court reviewed pre- § 1346 enactment honest services fraud case law and held that "[t]he vast majority of the honest-services cases involved offenders who, in violation of a fiduciary duty, participated in bribery or kickback schemes."⁶ Therefore, the Court held that "there is no doubt that Congress intended §1346 to reach *at least* bribes and kickbacks."⁷

The Court also rejected the government's argument to preserve conflict of interest cases by noting the "relative infrequency" of conflict of interest prosecutions in comparison to bribery and kickback cases and the "intercircuit inconsistencies they produced."⁸ The Court also cited the rule of lenity to resolve statutory ambiguity in determining that a "reasonable limiting construction of §1346 must exclude this 'amorphous category of cases.'"⁹

The Court specifically cautioned Congress on creating further honest services statutes, stating that "it would have to employ standards of sufficient definiteness and specificity to overcome due process concerns."¹⁰ The Court noted that it had significant questions about a potential criminal statute based on an undisclosed self-interest (*i.e.*, "how direct or significant does the conflicting financial interest have to be?"), and ultimately advised Congress to use "particular care" if it chose to create further criminal prohibitions in this area.¹¹

In a shorter opinion, *Black* followed *Skilling*'s lead, and held that honest services fraud, when "properly confined, criminalizes only schemes to defraud that involve bribes or kickbacks."¹² Therefore, the jury instructions that were given on the broader

⁵ *Skilling v. United States*, No. 08-1394 (June 24, 2010), 2010 U.S. LEXIS 5259; see also *Black v. United States*, No. 08-876 (June 24, 2010), 2010 U.S. LEXIS 5253.

⁶ *Skilling v. United States*, No. 08-1394 (June 24, 2010), at slip op. 43.

⁷ *Id.* at 44 (emphasis in original).

⁸ *Id.* at 46.

⁹ *Id.*

¹⁰ *Id.* at 47.

¹¹ *Id.*

¹² *Black v. United States*, No. 08-876 (June 24, 2010), at slip op. 5.

definition of honest services fraud were erroneous.¹³ The Court also held that the objection made by Black at trial to the jury instructions was not forfeited by the refusal to agree to a special-verdict form for the jury to state whether the fraud it found was money or property fraud or honest services fraud.¹⁴ Ultimately, the Court expressed no position on whether the jury instruction error was harmless, and remanded for that purpose.¹⁵

II. The Impact for Skilling, Black and Beyond

The ruling did not require reversal of Skilling's or Black's convictions – the Court remanded each case to determine what, if any, impact there would be on any of the counts of conviction. For Skilling, honest services fraud was one of three objects of his conspiracy conviction; he was also convicted of twelve counts of securities fraud related to false statements to securities analysts, rating agencies, and auditors. For Black, his convictions were for both money and property fraud and honest services fraud, as well as obstruction of justice. Because both defendants were convicted of other counts, and the government's prosecution theory did not rely solely on the honest services fraud concept, the practical impact of this favorable ruling to either defendant is unclear. Additionally, although some post-conviction petitions may be filed by defendants in other cases in response to the ruling, the presence of other independent counts of conviction or other non-honest services fraud theories may preclude relief.

Beyond the potential impact to the defendants personally, *Skilling* should curtail aggressive prosecutors from charging crimes for conduct that could previously have been charged as honest services fraud. However, the government will still be able to charge bribery and gratuities offenses involving federal officials or even those state officials involved in programs that are federally funded.¹⁶ Further, prosecutors may be able to expand the limits of the broad definition of kickbacks that was cited by the Supreme Court in

Skilling – “any money, fee, commission, credit, gift, gratuity, thing of value, or compensation of any kind which is provided, directly or indirectly, to [enumerated persons] for the purpose of improperly obtaining or rewarding favorable treatment in connection with [enumerated circumstances].”¹⁷ Additionally, the government can still charge individuals by availing itself of the now-limited honest services statute as well as traditional money and property mail and wire fraud statutes, securities fraud, false statements, obstruction of justice, false certification of corporate reports, criminal regulatory violations, criminal conflicts of interest, money laundering, and other offenses, including potential new crimes arising from the Dodd-Frank financial reform legislation.¹⁸

There are two additional potential impacts that may affect and limit how prosecutions under these and similar broadly worded statutes are brought. First, criminal cases that might have alleged an honest services fraud-type violation with no bribes or kickbacks may now be brought instead as civil matters by both governmental and self-regulatory enforcement authorities. FINRA, for example, has a broad rule that states that “[a] member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.” See FINRA Rule 2010. That type of case is far better handled, and resolved, in a civil regulatory forum with monetary penalties and administrative sanctions rather than criminal convictions. Additionally, honest services fraud violations with no bribes or kickbacks may be handled in civil lawsuits, internal employment disputes, and, perhaps most importantly for elected public officials, at the ballot box once such allegations become public.

¹⁷ *Skilling v. United States*, No. 08-1394 (June 24, 2010) at slip op. 48-9 (citing 18 U.S.C. §§ 201(b); 666(a)(2); 41 U.S.C. § 52(2)); see also Randall D. Eliason, *supra* note 3, at *936-937 (stating that the term “anything of value” is interpreted broadly to include “virtually anything of subjective worth to the intended recipient” including promises of future employment, loans given on favorable terms, and even sexual favors or companionship).

¹⁸ K&L Gates has drafted a series of alerts on the Dodd-Frank Act and its very broad impact. To view the series of alerts, please see <http://www.klgates.com/practices/ServiceDetail.aspx?service=139&view=5>.

¹³ *Id.*

¹⁴ *Id.* at 8.

¹⁵ *Id.*

¹⁶ See, e.g., 18 U.S.C. § 666.

Second, the Court's opinion may cause prosecutors to use more caution in developing and applying aggressive theories of criminal liability under other statutes – theories that may not be plainly apparent to the public.¹⁹

III. Conclusion – The Core Still Remains

Skilling and *Black* provide needed clarity to the honest services fraud statute. That said, the statute's core remains, and public and private individuals who receive a bribe or a kickback clearly remain within its scope.

¹⁹ See, e.g., *United States v. Santos*, 553 U.S. 507 (2008), *superseded by statute* as stated in *United States v. Morris*, 2010 U.S. Dist. LEXIS 26133 (S.D. Ky. 2010) (court rejected government's interpretation of "proceeds" in money laundering statute, holding that the requirements "will unquestionably require proof that is more difficult to obtain," but "we interpret ambiguous criminal statutes in favor of defendants, not prosecutors"); *United States v. Hodge*, 558 F.3d 630, 632 (7th Cir. 2009) (court denied government's "preposterous understanding" of net receipts in money laundering statute and reversed conviction); *United States v. Radley*, 659 F. Supp. 2d 803 (S.D. Tx. 2009) (court rejected novel approach to criminal manipulation provisions of the Commodity Exchange Act, finding law vague as applied).

Even without financial gain, criminal prosecutors and other federal regulators still have a full arsenal of weapons at their disposal to address core corruption cases. Congress may also weigh in again as it has in the past to try and undo much of the Court's underlying holding,²⁰ but with a watchful Court ready to critically analyze any statute.

²⁰ See, e.g., *McNally v. United States*, 483 U.S. 350 (1987) (stopping the development of the intangible-rights doctrine, and stating that "if Congress desires to go further . . . it must speak more clearly"); 18 U.S.C. § 1346 (Congress' response to *McNally*); see also *United States v. Santos*, 553 U.S. 507 (2008), *superseded by statute*.

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