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Honest Services Fraud

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CRIMINAL JUSTICE

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Introduction

At the time of this writing, two of the three cases pending before the United States Supreme Court challenging the validity of so called "honest services fraud" have been orally argued. A third will be argued later this term.

In this month's *Criminal Justice* column, we will look at the history of the "honest services fraud" statute, why it was enacted, what it purports to regulate, how it has been applied and why it is before the Supreme Court. We will look at the three pending cases and how these cases could have an impact on not only criminal prosecutions but on how civil and criminal practitioners advise their clients.

McNally and the Legislation

In June of 1987, the United States Supreme Court decided the case of *McNally v. United States*, 483 U.S. 350 (1987). It dealt with one of the most common criminal code sections in the arsenal of federal prosecutors, mail fraud. The federal mail fraud statute, 18 U.S.C. § 1341, prohibits the use of the mails to execute "any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises." As such, it extended federal jurisdiction to virtually every kind of fraud prosecuted in state courts as long as the mails were used in the execution of the scheme.

McNally, a private citizen, along with two other individuals, a former Kentucky public official and the former head of the Commonwealth's Democratic Committee, were prosecuted for mail fraud. The issue was whether or not the text of the mail fraud statute had been properly expanded by the court to include the "intangible right" to have the Commonwealth's affairs conducted honestly. The jury convicted the defendants and the Sixth Circuit Court of Appeals affirmed, holding that § 1341 proscribes schemes to defraud citizens of their intangible rights to honest and impartial government.

The United States Supreme Court granted *certiorari*. In an opinion by Justice White, the Court reversed, holding that, "The mail fraud statute clearly protects property rights, but does not refer to the intangible right of the citizenry to good government." The decision was based strictly on statutory construction going back to the legislative intent in 1870, 1872 and 1906 and the subsequent legislative history when the section was amended. It was not based on a constitutional analysis. The dissent, offered by Justice Stevens, who is still on the Court, also focused on the language of the statute and its interpretation but came to the opposite conclusion.

The next year, in 1988, the United States Congress passed a new statute, 28 words in length, designed to overrule the Supreme Court's *McNally* decision. It is codified at 18 U.S.C. § 1346 and reads in its entirety: "For the purposes of this chapter, the term "scheme or artifice to defraud" includes a scheme or artifice to deprive another of the intangible right of honest services."

The Effect of § 1346

Since its enactment, the language of a "right of honest services" has been invoked to make behavior criminal that would have never come under the original language of the mail or wire fraud statutes (18 U.S.C. § § 1341 and 1343). There has been significant commentary on this phenomenon from conservative organizations, academic writers and criminal justice organizations. Instead of having to prove bribery or the violation of a state statute, or the actual defrauding of a public entity of money or property, this federal statute has been used to police just about any conduct. In fact, it has been used to prosecute people who have not been accused of attempting to defraud the government at all.

Justice Scalia dissented from a denial of *certiorari* in a case last term which would have reviewed this law. In *Sorich v. United States*, 129 S.Ct. 1309 (*Mem.* 2009), Justice Scalia listed some of the wide ranging uses of the statute. He said, "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 employees and corporate fiduciaries." He goes on to give examples and points out that there has been an attempt to limit the broad language by judicial interpretation but the decisions have not been consistent. Generally, the courts have tried to limit the conduct to that which was, at least, in violation of state law or to conduct from which there was some expectation of private financial gain. Even with these purported limitations – and they are not adopted uniformly throughout the circuits – Justice Scalia found the statute to be offensive. This part of the dissent is worth quoting:

"First, the prospect of federal prosecutors' (or federal courts') creating ethics codes and setting disclosure requirements for local and state officials. Is it the role of the Federal Government to define the fiduciary duties that a town alderman or school board trustee owes to his constituents? It is one thing to enact and enforce clear rules against certain types of corrupt behavior, e.g., 18 U.S.C. § 666(a) (bribes and gratuities to public officials), but quite another to mandate a freestanding, open-ended duty to provide "honest services"-with the details to be worked out case-by-case. [Citation omitted]

"Second and relatedly, this Court has long recognized the "basic principle that a criminal statute must give fair warning of the conduct that it makes a crime." [Citation omitted]. There is a serious argument that § 1346 is nothing more than an invitation for federal courts to develop a common-law crime of unethical conduct. But "the notion of a common-law crime is utterly anathema today," [Citation omitted],

and for good reason. It is simply not fair to prosecute someone for a crime that has not been defined until the judicial decision that sends him to jail. “How can the public be expected to know what the statute means when the judges and prosecutors themselves do not know, or must make it up as they go along?” . . . [Citations omitted]”

The significance is that he is taking on this excessive allocation of federal power and discretion as a matter of constitutional law. First, it is a matter of federalism, that is, the states have the right to set the standards for conduct in government and other relationships, not the federal prosecutors. Second, it is also a matter of due process and the right to have criminal conduct defined by statute in advance, not defined after the fact by prosecutors and courts.

Black, Weyhrauch and Skilling

This brings us to the grants of *certiorari* in the three cases pending this term before the United States Supreme Court. Two cases came on for oral argument on December 8, 2009. One involves Conrad M. Black. He is the newspaper executive who was convicted of defrauding his media company, Hollinger International. He is arguing that his conviction should be reversed because he did not contemplate “economic harm” to the company. The second, involves Bruce Weyhrauch, a former Alaska state legislator, who was convicted of failing to disclose a conflict of interest. His primary argument is that he did not violate state law and that, as a matter of federalism, this general grant of power to federal prosecutors should not be permitted. The third case will be argued later in the term. It involves Jeffrey K. Skilling, the former Enron executive. He is arguing that the statute is unconstitutionally vague.

During the oral arguments on December 8, 2009, when the Black and Weyhrauch cases were before the Court, the main focus of the Justices’ questions was on whether the statute is unconstitutionally vague, as opposed to the more narrow arguments advanced by the defendants in their briefs. Although it is dangerous to conclude too much from the questioning, Justices Scalia and Breyer, in particular, seem ready to find the secton unconstitutional. Breyer was persistent in asking the government lawyer to explain how the statute is not vague and why it could not be used to prosecute someone for lying to the boss to go to a baseball game or giving the boss the impression that one is working when actually reading the Racing Form.

Justice Scalia flatly rejected the position that the pre-McNally cases could offer guidance in terms of how to limit the statute. He said those cases do not offer any clarity and he does not understand them. There was questioning by other Justices as well. We will probably have to wait for the Skilling case to be argued before the trilogy will be decided.

There is considerable interest in the outcome of these cases for a variety of reasons. For one, there have been and are in the pipeline a large number of cases which have been tried or which are scheduled for trial in which § 1346 is the lynchpin. The statute has been particularly popular with the United States Attorneys Office in Chicago where it has been used repeatedly in so-called political corruption cases (including a case we are handling in Chicago scheduled for trial later in 2010). The code section is also alleged in current cases which have gained national attention such as those against former Illinois Governor Rod Blagojevich, former New York State Senator Joseph L. Bruno and former Alabama Governor Donald E. Siegelman.

In addition to concern about people who have been indicted, there is considerable interest among the lawyers advising individuals, corporations, government contractors and anyone else who might now or in the future come within the sweep of this law. One way or another, the Supreme Court's decisions in these three cases will have a profound impact.

Conclusion

Perhaps these three cases signal a trend to reign in creative prosecutions. Depending on how they are decided, we could return to the model of clearly defining the proscribed behavior before allowing a criminal prosecution. It could also represent a swing of the pendulum back toward more traditional law enforcement and away from what has been perceived as an over criminalization under the federal law.