Litigation Law Alert

Congress and DOJ Move to Restore Breadth of Honest Services Fraud Statute

October 4, 2010

On September 28, 2010, Lanny A. Breuer, Assistant Attorney General for the U.S. Department of Justice's Criminal Division, testified before the Senate Judiciary Committee, urging Congress to enact legislation to overturn the Supreme Court's decision in *Skilling v. United States*, 130 S. Ct. 2896 (2010), and recriminalize all forms of so-called "honest services" fraud. That same day, Senator Patrick Leahy (D-VT), joined by Senators Sheldon Whitehouse (D-RI) and Ted Kaufman (D-DE), proposed the Honest Services Restoration Act (S. 3854), an act designed to fill the gap left by the *Skilling* decision.

The honest services fraud statute made it a crime to use the mails or wires to engage in a "scheme or artifice to deprive another of the intangible right of honest services." 18 U.S.C. § 1346. In the 22 years since passage of the honest services statute, the United States has used it to prosecute public officials and corporate officers for "accepting bribes or kickbacks" and for "engaging in undisclosed self-dealing."[1]

In *Skilling*, the Supreme Court held that the statute was unconstitutionally vague, except to the extent that it prohibited the deprivation of honest services through bribes and kickbacks. In short, *Skilling* eliminated the government's ability to prosecute "undisclosed self-dealing," a vague standard that prosecutors employed with near impunity to prosecute public officials and corporate executives for any appearance that the defendant personally profited from his or her official position.[2]

Breuer urged Congress to "act quickly" to "fill the void" left by the *Skilling* decision. Breuer limited his recommendation to acts of undisclosed self-dealing by public officials. In his live testimony, Breuer acknowledged that, even after *Skilling*, the government has been able to address "most" cases of private-sector self-dealing through the securities fraud statutes and other available federal criminal provisions.[3] Nevertheless, he pledged to work with Congress to craft appropriate measures to reach "corrupt private sector actors as well." In response to concerns by Senator Jeff Sessions (R-AL) that prohibiting "undisclosed self-dealing" still may be too constitutionally vague to provide adequate notice of what constitutes prohibited conduct, Breuer testified that any new

legislation should include as an element the specific intent to defraud.

The Honest Services Restoration Act, which would amend the mail and wire fraud statutes by adding a Section 1346A, seeks to fill the *Skilling* "void" as to both public officials and corporate executives. Thus, the Act prohibits both "undisclosed self-dealing" by public officials and "undisclosed private self-dealing" by "officers and directors." (Proposed Sections 1346A(a)(1)-(2).) Self-dealing in both the public and private arenas is generally defined as the defendant using his or her official position (as a public official or an officer or director) to, in whole or in part, benefit the financial interest of certain associated parties.[4] The Act also requires that the defendant knowingly falsify, conceal, cover up, or omit "material information that is required to be disclosed regarding that financial interest by any Federal, State, or local statute, rule, regulation, or charter applicable to the [defendant]."[5] (Proposed Sections 1346A(b)(1)(A)(ii), (b)(2)(A)(ii).) And, finally, in the private arena, the self-dealing must also cause or be intended to cause actual harm to the officer's or director's employer. (Proposed Section 1346A(b)(2)(A)(i).)

While clearly more specific than the old Section 1346, the Act raises several questions. ***First***, by basing liability on the falsification of, or failure to disclose, material information that is otherwise required to be disclosed "by any Federal, ***State, or local*** statute, rule, regulation, or charter" (emphasis added), the Act potentially creates dozens of different standards of criminal conduct. Different states and local jurisdictions may have different disclosure requirements; thus, conduct that is a federal crime in one jurisdiction could be entirely legal in another—all under the same federal statute. This could lead to just as much confusion—and disparate case law—about what conduct is sufficient to violate the federal criminal laws as exists under the current honest services fraud statute.

Second, while it defines who is a "public official" (Proposed Section 1346A(b)(1)(B)), nowhere does the Act define "officers and directors." Presumably, the Act intends to reach only certain corporate executives and members of the boards of directors of publicly traded companies operating in the United States, but the Act is unclear.

Finally, the Act is unclear as to the requisite level of intent. While it requires a defendant to "knowingly" falsify, conceal, cover up, or omit material information that is required to be disclosed regarding the relevant financial interest, the Act does not define "knowingly." Although Breuer suggested that any legislation should require the specific intent to defraud, courts have routinely held that "knowingly" has different meanings in different contexts. In the securities context, for example, "knowing" can mean either actually knowing the truth or recklessly disregarding the truth. In other contexts, actual knowledge is required and recklessness is insufficient to show intent. The Act here is unclear.

It remains to be seen whether either house of Congress will act on Senator Leahy's bill, or whether some other version will be proposed. It seems likely, however, that Congress will take some action to "fill the gap" created by the *Skilling* decision. And it further seems likely that the "fix" will involve some specific provisions designed to reach the conduct of corporate executives. In that event, officers and directors will need to re-evaluate corporate policies, as well as personal practice, to ensure continued compliance with the law. We will continue to provide updates as the debate moves forward.

If you have any questions about this update, please contact:

Per A. Ramfjord at (503) 294-9257 or paramfjord@stoel.com
Jamie S. Kilberg at (503) 294-9274 or jskilberg@stoel.com

----

[1] Testimony of Assistant Attorney General Lanny A. Breuer before the Senate Judiciary Committee, Sept. 28, 2010. Breuer's written testimony is available here.

[2] George J. Terwilliger III, a former Deputy Attorney General under President George H. W. Bush, testified at the Senate Judiciary Committee hearing that one of the problems with Section 1346

was that, in vaguely outlawing the deprivation of honest services, it permitted the *prosecutors* to determine what constituted criminal self-dealing and to set the standards for what ought to be disclosed. A webcast of the hearing, including Terwilliger's live testimony, can be found here.

[3] By contrast, Duke University School of Law professor—and former member of the Department of Justice's Enron Task Force—Samuel W. Buell testified that the securities laws are insufficient to reach all forms of private honest services fraud. He urged a broad legislative fix.

[4] The relevant parties include the official; the official's spouse or minor child; the official's general partner; a business in which the official is serving as an employee, officer, director, trustee, or general partner; or an individual or business with which the official is negotiating for prospective employment or other financial compensation. (Proposed Sections 1346A(b)(1)(A)(i), (b)(2)(A)(i).) These categories of interested parties track the federal conflict-of-interest statute, 18 U.S.C. § 208, which currently applies to the executive branch. In the private arena, the intended benefit to one of these parties must exceed $5,000 in value. (Proposed Section 1346A(b)(2)(A)(i).)

[5] The Act, therefore, does not itself criminalize ***disclosed*** self-dealing. Nor does it criminalize undisclosed self-dealing for which there is no separate obligation to report the related financial interest.

If you currently subscribe to Stoel Rives client alerts, click here to update your contact information and preferences. To join the Stoel Rives mailing list and ensure direct delivery of future alerts, click here to subscribe.

Stoel Rives LLP 1-800-88-STOEL (887-8635) | www.stoel.com

Anchorage, AK | Boise, ID | Lake Tahoe, CA | Minneapolis, MN | Portland, OR | Sacramento, CA

Salt Lake City, UT | San Diego, CA | San Francisco, CA | Seattle, WA | Vancouver, WA