AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

S. HRG. 111–906

RESTORING KEY TOOLS TO COMBAT FRAUD AND CORRUPTION AFTER THE SUPREME COURT'S SKILLING DECISION

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

SEPTEMBER 28, 2010

Serial No. J–111–111

Printed for the use of the Committee on the Judiciary

U.S. GOVERNMENT PRINTING OFFICE

64–789 PDF WASHINGTON : 2011

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00001 Fmt 5011 Sfmt 5011 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

COMMITTEE ON THE JUDICIARY

PATRICK J. LEAHY, Vermont, *Chairman*

HERB KOHL, Wisconsin
DIANNE FEINSTEIN, California
RUSSELL D. FEINGOLD, Wisconsin
ARLEN SPECTER, Pennsylvania
CHARLES E. SCHUMER, New York
RICHARD J. DURBIN, Illinois
BENJAMIN L. CARDIN, Maryland
SHELDON WHITEHOUSE, Rhode Island
AMY KLOBUCHAR, Minnesota
EDWARD E. KAUFMAN, Delaware
AL FRANKEN, Minnesota

JEFF SESSIONS, Alabama
ORRIN G. HATCH, Utah
CHARLES E. GRASSLEY, Iowa
JON KYL, Arizona
LINDSEY GRAHAM, South Carolina
JOHN CORNYN, Texas
TOM COBURN, Oklahoma

BRUCE A. COHEN, *Chief Counsel and Staff Director*
MATTHEW S. MINER, *Republican Chief Counsel*

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00002 Fmt 5904 Sfmt 5904 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

CONTENTS

STATEMENTS OF COMMITTEE MEMBERS

	Page
Feingold, Hon. Russell D., a U.S. Senator from the State of Wisconsin, prepared statement	44
Leahy, Hon. Patrick J., a U.S. Senator from the State of Vermont	1
prepared statement	45
Sessions, Hon. Jeff, a U.S. Senator from the State of Alabama	3

WITNESSES

Breuer, Lanny A., Assistant Attorney General, Criminal Division, U.S. Department of Justice, Washington, DC	5
Buell, Samuel W., Professor, Duke University School of Law, Durham, North Carolina	13
Seigel, Michael L., University of Florida Research Foundation, Professor of Law, Fredic G. Levin College of Law, Gainesville, Florida	16
Terwilliger, George J., III, Partner, White & Case, Washington, DC	18

QUESTIONS AND ANSWERS

Responses of Lanny A. Breuer to questions submitted by Senator Leahy	28

SUBMISSIONS FOR THE RECORD

Breuer, Lanny A., Assistant Attorney General, Criminal Division, U.S. Department of Justice, Washington, DC, statement	31
Buell, Samuel W., Professor, Duke University School of Law, Durham, North Carolina, statement	39
Lowell, Abbe David, Potomac, Maryland, letter	48
National Association of Criminal Defense Lawyers, Timothy P. O'Toole, Washington, DC, statement	55
Seigel, Michael L., University of Florida Research Foundation, Professor of Law, Fredic G. Levin College of Law, Gainesville, Florida, statement	62
Terwilliger, George J., III, Partner, White & Case, Washington, DC, statement	65

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00003 Fmt 5904 Sfmt 5904 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

RESTORING KEY TOOLS TO COMBAT FRAUD AND CORRUPTION AFTER THE SUPREME COURT'S *SKILLING* DECISION

TUESDAY, SEPTEMBER 28, 2010

U.S. SENATE
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Committee met, pursuant to notice, at 10:07 a.m., in room SD–226, Dirksen Senate Office Building, Hon. Patrick J. Leahy, Chairman of the Committee, presiding.

Present: Senators Leahy, Whitehouse, Kaufman, and Sessions.

OPENING STATEMENT OF HON. PATRICK J. LEAHY, A U.S. SENATOR FROM THE STATE OF VERMONT

Chairman LEAHY. Good morning. Good morning, Mr. Breuer.

We are going to consider another in a series of recent cases in which the Supreme Court appears to have undermined Congressional efforts to protect hardworking Americans from powerful interests. In *Skilling* v. *United States*, the Court sided with an Enron executive who had been convicted of fraud and gutted a statute vital to combating public corruption, corporate fraud, and self-dealing.

Now we have to explore the kinds of problematic conduct that may go unchecked in the wake of the *Skilling* decision and consider what Congress should do or could do to fill those gaps and bring strong enforcement against corrupt and fraudulent conduct. I thank Assistant Attorney General Lanny Breuer for coming in to share the Justice Department's focus on this important case, and I look forward to hearing from our panel of experts.

In recent years, the stain of corruption has spread to all levels of Government. It is an issue that both parties have to address. This is a problem that victimizes every American by chipping away at the foundations of our democracy and the faith that Americans have in their Government.

Too often, loopholes in existing laws have meant that corrupt conduct goes unchecked. Senator Cornyn and I introduced the Public Corruption Prosecution Improvements Act last year to try to address some of these gaps. Obviously, a bipartisan piece of legislation, with Senator Cornyn of Texas and myself introducing it. And it was passed by this Committee, and I would hope the Senate would pass it now. The honest services fraud statute has in the past served to fill in some of the gaps in corruption laws, but with the *Skilling* case, of course, it is greatly limited. I think we have

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00005 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

to act aggressively but we also have to act very carefully to strengthen our laws to root out the kind of public corruption that resulted in convictions of high State officials, Members of Congress, and many others.

We have seen in recent years a plague of financial and corporate frauds. They have robbed people of their savings, their retirement accounts, college funds for their children, and so forth. Congress acted by passing the Fraud Enforcement and Recovery Act to give prosecutors and investigators more tools. The honest services fraud statute has allowed prosecutors the flexibility to keep up with corporate criminals.

For decades, courts and prosecutors agreed that the Federal mail and wire fraud laws could be used to prosecute individuals for "deprivation of honest services," including cases in which public officials acted to benefit their own hidden financial interests or in cases in which corporate executives secretly enriched themselves at the expense of their own corporations.

In 1987, the Supreme Court, over Justice Stevens' dissent, overturned those decades of case law, and the Congress responded quickly, explicitly adding in 1989 a provision for prosecuting deprivations of honest services under the mail and wire fraud cases. In the 21 years following that action, every single circuit court upheld the honest services fraud statute. No court limited it in the sweeping way the Supreme Court chose to in *Skilling*.

The honest services statute was used to prosecute lobbyist Jack Abramoff, Congressman Bob Ney, many corrupt State and local officials, and corporate wrongdoers like Enron executive Jeff Skilling and multi-millionaire Canadian publisher Conrad Black, whose conviction for blatant self-dealing was called into question by the Supreme Court's decision.

The Court in *Skilling* ruled that the honest services fraud statute may be used to prosecute only bribery and kickbacks, but no other conduct. Of course, there were already statutory tools to go after bribery and kickbacks, so the honest services fraud statute was more important in other areas.

It allowed prosecutors to go after corporate executives who acted to benefit themselves financially at the expense of the shareholders and the employees of their company. But those cases now are at risk. I understand the concerns in many circles about vague or undefined Federal laws which could leave some public officials or executives uncertain about what kind of conduct could leave them susceptible to criminal charges. But that is no reason to let corrupt or fraudulent conduct go unchecked. So let us identify the gaps in current law after *Skilling*.

We should be clear about what conduct is unacceptable. I would hope we could all agree that undisclosed self-dealing by public officials and corporate executives is not acceptable. We should figure out the best way to fill in those gaps, and I thank the Senators, both Republican and Democratic Senators, who have been working with me to find the best way to restore our fraud and corruption laws. And because I know we have a vote coming up, I will put my whole statement in the record.

[The prepared statement of Chairman Leahy appears as a submission for the record.]

Chairman LEAHY. Senator Sessions.

STATEMENT OF HON. JEFF SESSIONS, A U.S. SENATOR FROM THE STATE OF ALABAMA

Senator SESSIONS. Thank you, Mr. Chairman, and thank you for this hearing. I do believe it is an important hearing, and we are wrestling with very significant issues. I prosecuted public officials personally for weeks at a time. They probably took a year off my life, those cases. One good criminal lawyer who was representing one of the witnesses said, "Jeff, if you lose this case, you and I are both going to have to leave town."

So these are very important tough cases with powerful forces out there, but the Supreme Court I do not think is trying to further illegal activity when they have rendered several cases that tell us that you have got to have criminal statutes that are clear and mean something and have real definitions.

When I go back and look at it, when I was a prosecutor, perhaps I did not think it particularly bad. We will see what Mr. Terwilliger used to think when he was a prosecutor. He probably thought this was a good statute. He may have helped write it. But I see now he is not so happy with it. But it says a "scheme or artifice deprives"—an amendment to the mail fraud statute "includes a scheme or artifice to deprive another of the intangible right of honest services."

Now, what kind of statute is that? I mean, think about that. The United States Congress—and we are all, I know proud of what we do, and if a court sometimes overturns it, we think they have overreached. But we wrote a statute that is going to make it a Federal crime to deprive somebody of an intangible right of honest services. I do not know what that means. Historically, robbery was the taking of a thing of value from a person with force or violence. The elements were crystal clear, and a prosecutor knew precisely what had to be proven, and precisely the defendant knew what he could or could not do.

So I am worried about that. I think Justice Ginsburg was correct in saying that if Congress were to take up the enterprise of criminalizing "undisclosed self-dealing by a public official or private employee," it "would have to employ standards of sufficient definiteness and specificity to overcome due process concerns."

I think that is a legitimate observation by the Supreme Court. You have got to be careful when you write these kinds of statutes. And when I see Mr. Breuer from the Department of Justice's opinion, I am little bit concerned. I think it is more specific than the mail fraud statute. The Supreme Court has found that insufficiently broad, too broad. It seems to me it is sort of taking a State ethics law that may be a 1- or 2-year penalty, converting it to a Federal—converting the State ethics law into a Federal offense. And if you do not disclose—undisclosed self-dealing, that is a pretty broad statute. Give me a break. It really is.

So I think "undisclosed self-dealing by a public official or a private employee" I think is the phrase that is being suggested as an appropriate statute here, well, let us talk about it. Let us see where we go from here. But you are tying, I think, Mr. Chairman, an awful lot to the exact language that a State may have in their

ethics law. You have got the Hobbs Act, 1951, where a politician extorts a kickback or a thing of value for themselves or another in exchange for doing their official duty, that is a pretty broad statute in itself, and it has got more seriousness to it. I always felt that you needed a clear threat and a clear benefit, and I prosecuted a number of those cases, and sometimes you live and die by the words in a statute. You have to argue to the judge. If you do not meet the statute definition, you are out. You are done. And you have to know that.

So I believe it is an important issue. The Supreme Court has raised these issues. I do not think they were trying to benefit criminals and crooked politicians or crooked CEOs, but I do think that they correctly raise a concern that a Federal criminal statute should be clear; it should tell the court precisely what it is the prosecutor must prove; and the rights of defendant certainly depend on clarity in knowing what they are charged with and what the law is.

Thank you.

Chairman LEAHY. Thank you, Senator Sessions. It is helpful in this Committee that we have a number of former prosecutors like Senator Sessions, Senator Cornyn, Senator Whitehouse, Senator Klobuchar, and others, and it is very helpful.

We have a number of statements, one from Senator Feingold, which will be placed in the record, and I will keep the record open all day for any other statements that will automatically without objection be placed in the record.

[The prepared statement of Senator Feingold appears as a submission for the record.]

Chairman LEAHY. Mr. Breuer is the Assistant Attorney General for the Criminal Division at the Department of Justice. He started his career as an assistant district attorney in New York City, prosecuted offenses ranging from violent crime to white-collar crime, later joined Covington & Burling where he served as co-chair of the White-Collar Defense Investigations Group. He served as Special Counsel to President Clinton from 1997 to 1999; undergraduate degree from Columbia, a law degree from Columbia Law School, well known to this Committee.

Please, Mr. Breuer, go ahead. And your whole statement will be made part of the record, but go ahead and emphasize whatever you would like.

Senator SESSIONS. Mr. Chairman, could I just say one more thing I forgot to mention.

Chairman LEAHY. Sure, of course.

Senator SESSIONS. I do believe that anyone who is familiar with the reality of criminal prosecutions knows that it is very difficult for a local district attorney to bring a complex case against a bank or financial institution or powerful politicians in the community. They are, you know, overwhelmed with murders and robberies and that kind of things, and it takes months preparing a case frequently as not. So I do believe a legitimate Federal role in prosecutions and a dramatic limitation on the ability of the Federal Government to prosecute clear criminal acts by State and local officials would be bad policy for the country.

Thank you.

Chairman LEAHY. Thank you.
Mr. Breuer.

STATEMENT OF HON. LANNY A. BREUER, ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE, WASHINGTON, DC

Mr. BREUER. Thank you, Mr. Chairman and Senator Sessions, and thank you for this opportunity to speak with you about the Supreme Court's recent decision in *Skilling* v. *United States* and its impact on the Justice Department's ability to prosecute certain honest services fraud cases.

Protecting the integrity of our Government institutions and the American marketplace is among the highest priorities for the Department of Justice. The Department is committed to using all available tools to combat fraud and corruption in the public and private sectors, and our enforcement efforts in these areas are vigorous.

The Supreme Court's recent decision in *Skilling*, however, has without doubt impacted our ability to prosecute certain honest services fraud cases. In order to restore our ability to prosecute the full range of public corruption and fraud cases, we believe that legislation to remedy the effects of *Skilling* is needed, and we urge Congress to pass such legislation quickly.

As early as the 1940s, Federal prosecutors began to use the mail and wire fraud statutes to charge public and private officials who acted in their own financial interests rather than in the interests of their constituents. These officials were prosecuted on the theory that they were defrauding the public of its right to their honest services. That is back since the 1940s.

In 1987, however, the Supreme Court in *McNally* v. *United States* held that the mail and wire fraud statutes do not cover honest services fraud schemes and instead apply only to schemes to deprive victims of money or property. The next year, in response to the legislative gap created by *McNally*, Congress enacted what we now know as the honest services fraud statute, 18 U.S.C. 1346, which expressly criminalized schemes, as Senator Sessions said, to deprive another of the intangible right to honest services.

Between the enactment of the honest services fraud statute in 1988 and the Supreme Court's recent decision in *Skilling*, the statute has proved extremely valuable to the Justice Department's efforts to attack corruption and fraud. Congressmen William Jefferson and Robert Ney, Illinois Governor George Ryan, and lobbyist Jack Abramoff, among others, were all convicted of honest services fraud or conspiracy to commit honest services fraud.

The honest services fraud statute has been valuable because it gets at two core types of corrupt behavior by public officials and corporate officers; one, accepting bribes or kickbacks and, two, engaging in undisclosed self-dealing. In *Skilling*, however, the Supreme Court limited the reach of the statute to bribery and kickback schemes only. Simply put, after *Skilling*, the statute can no longer be used to prosecute undisclosed self-dealing, thereby, in our view, leaving a gap that must be filled.

Let me provide you with a concrete example of what this means. After *Skilling*, if a corrupt mayor solicits bribes in return for giving

out city contracts to unqualified bidders, our prosecutors could still charge that mayor with bribery under Section 1346. But if that same mayor created his own company and then used his office to funnel city contracts to that company without disclosing his financial interest in that company, we would no longer be able to charge the mayor with honest services fraud even though his undisclosed self-dealing is every bit as corrupt as bribe taking. Furthermore, I am unaware of another criminal statute that we could use to reach that mayor's conduct.

In light of *Skilling*'s impact on our efforts to combat this particular type of criminal conduct, the Department urges Congress to pass legislation that would restore our ability to prosecute officials who engage in such undisclosed self-dealing.

I have provided suggestions for such legislation in my accompanying written testimony, emphasizing in particular the public sector remedy. We believe that legislation along the lines described in my written testimony would restore our ability to address the full range of corrupt conduct by Federal, State, and local officials. The Department is also open to a private sector remedy, and we would be happy to work with the Committee in finding an appropriate legislative solution.

The Department of Justice is committed to protecting the integrity of our Government institutions and our markets. Our citizens are entitled to know that their public servants are making decisions based upon the best interests of the citizens who elect them rather than for their own personal gain. Likewise, investors and shareholders are entitled to know that corporate officers and fiduciaries are acting in the investors' and shareholders' best interests and not attempting to secretly benefit themselves.

Thank you for this opportunity to address the Committee, and I would, of course, be happy to answer any questions that you may have.

[The prepared statement of Mr. Breuer appears as a submission for the record.]

Chairman LEAHY. Thank you, Mr. Breuer.

You know, my concern, the reason we have these hearings, is that for decades we have used the honest services fraud provision. As I mentioned earlier, circuit courts have always upheld it, and it was a major tool in a prosecutor's ability to go after criminals. And one of the key types of conduct that may be difficult to go after now is what you and others call undisclosed self-dealing.

Do you want to just explain it in layman's language what is undisclosed self-dealing Why is it important for prosecutors to be able to go after it.

Mr. BREUER. Absolutely, Mr. Chairman. So under a typical example of money or property fraud, the fraudster has a victim, and that victim loses money or property because of the fraud. So his intention is directed at his victim.

In honest services fraud, the victim is not necessarily himself or herself out money. What the victim is out is the honest services of the public official. So if I am a public official, that mayor who I referred to in my opening, and I receive bribes for taking official conduct, the citizens themselves are not necessarily out any money, but I have benefited, I have profited because I have received

money. And by doing so, I have corrupted the system, and the citizenry has been defrauded in that circumstance.

Chairman LEAHY. What we have is pretty clear—no, not bribery. I mean, we have statutes, specifically statutes on bribery. Those have not been touched by *Skilling*. But if you have this undisclosed self-dealing—and just so we can maybe be more specific in my question, how do we go about prosecuting that? But, also, how do we make sure that we are not just going after an inadvertent oversight or somebody does not do their paperwork correctly? They were perfectly honest, but they just did not fill out the papers properly.

Mr. BREUER. I will. And, Mr. Chairman, just for 30 more seconds on what I was saying, we do have a bribery statute. But, of course, our Federal bribery statute deals with Federal employees. And in my example, we were talking about a local mayor. And so I think we have to have an interest in reaching that.

But the second part of it, Mr. Chairman, is the circumstance where I am not receiving a bribe, but I have an undisclosed interest. I have created my own company or I have a company that my spouse has an interest in, and I take an official action not for the benefit of my constituents in my city, but I take an official action that benefits my wife's or my own secret company. That, too, corrupts the process, and that, too, is a fraud. It is a fraud on my citizens and my constituents because I am not doing something for the purpose of serving them. I am personally benefiting from my official conduct. And if we do not have an honest services statute that addresses this self-dealing, Mr. Chairman, then, of course, that kind of conduct is absolutely right now something that we cannot reach.

Chairman LEAHY. You know, most of our public servants—and you are talking beyond the Federal area, but into State and local. A lot of local governments, the mayor, the board, are either paid a nominal amount or nothing in a lot of small towns. It is not like the community in California where the chief of police is paid, I think, two or three times what the President of the United States is paid. But, I mean, those are pretty obvious on the point. But if you have got somebody who owns a local car dealership and serves on the board of aldermen and gets paid $100 a year, is he precluded from voting on anything if the city is buying a fleet of cars?

Mr. BREUER. Well, if the mayor has a car——

Chairman LEAHY. I am assuming everybody knows he is the local——

Mr. BREUER. Right. So the mayor of a small community is also a car dealer, and it is known that he is a car dealer, and he has not surreptitiously hid the fact that he has an ownership interest, then there is absolutely nothing wrong, presumably, with what he is doing.

Chairman LEAHY. So what you are saying, however, if he was—but if he was a privately—or he was a silent partner in that car dealership and all of a sudden the cars being bought by the city at his direction went only there, that would be a different situation. Am I correct?

Mr. BREUER. It could be a different situation. To address Senator Sessions' excellent points, I think what we have to do after *Skilling*

is to address this conduct, but to address it in a way that is fair and gives notice.

So in the first instance in your hypothetical, there needs to be some sort of pre-existing requirement that the mayor disclose his interest. It can be a city ordinance. It can be a State statute. It can be a regulation. But there has to be something in this situation that there is notice that there is a pre-existing disclosure requirement, and that I think is essential.

And then, second, I think we have to show, if we were to go forward, that that mayor knowingly concealed his interest—not that he forgot. It should be the burden of the Government to prove in addressing *Skilling* that it was a knowing concealment, he did it on purpose; and in addition, we believe, that we have to establish that that mayor had the specific intent to defraud.

So it cannot be accidental that he forgot. It must be the purpose for what he was doing. But our view is if there is a pre-existing requirement and we can show that the mayor in your case knowingly concealed his interest and specifically intended to defraud because he took an official action not for the benefit of the people of his city but, frankly, to benefit his or his wife's private interests, that is the kind of conduct that we think goes to the core of the integrity of Government and we think needs to be addressed.

Chairman LEAHY. My time is up, but we are trying and we will try to get a bipartisan piece of legislation out of here. I would urge you and the Department to work closely with both Republicans and Democrats in our effort to draft such legislation. I assume that you have no problem with working with us on that.

Mr. BREUER. Mr. Chairman, we are absolutely committed to working with both sides of the aisle on bringing forth this kind of legislation as quickly as we can.

Chairman LEAHY. Thank you.

Senator Sessions.

Senator SESSIONS. Well, thank you.

Mr. Breuer, if a mayor takes a series of bribes and, that is, bribery being a predicate act under RICO, the mayor can be charged with RICO—right?—a racketeering charge, which I have prosecuted before. And two is generally sufficient if there is a pattern shown. So that is prosecuted. Well, what about if a mayor on his way to work goes by a local grocery store and steals groceries That is not a Federal offense, is it

Mr. BREUER. I do not think it is. I do not think——

Senator SESSIONS. You would not make that a Federal offense, would you

Mr. BREUER. I do not think in your scenario we would, Senator. I do not think we would do that.

Senator SESSIONS. Well, let us go beyond "think." If an individual, the mayor, picks up a rock in Alabama and murders someone, that is just not a Federal crime, is it?

Mr. BREUER. That is not a Federal crime, Senator.

Senator SESSIONS. It cannot be prosecuted in Federal court.

Mr. BREUER. Well, based on the limited facts you have given me, I think that is right.

Senator SESSIONS. Right, cannot be prosecuted in Federal court. One of the things we need to understand and I have always

learned from being a Federal prosecutor is that every crime is not a Federal crime. Every crime is just not a Federal crime. Interstate transportation of stolen motor vehicles has to be interstate transportation of the vehicle, interstate shipment. The Mann Act is taking a person in interstate commerce for the purpose of prostitution, not a local prostitute. This is one of the things we do have to recognize. There are limits on Federal reach historically and constitutionally, I think, but certainly historically.

Now, this is a pretty broad phrase, would you not agree, that a public official can go to jail for undisclosed self-dealing All right. So that is the broad—so you define that in your legislation. I do not know that—it did not say willfully. The public official knowingly fails to disclose material information regarding the financial interest, that is required to be disclosed by Federal, State, or local statute, rule, or regulation. So let us say we are having a tax debate. I put money in a dividend fund, and the question is: Should the dividends be taxed at 15 percent or normal income rate of 35 percent? And if I failed to disclose that on my ethics form somehow, would that be a violation by a State legislator or a U.S. Senator?

Mr. BREUER. Senator, in your hypothetical I think not. But if I could work with you on that for a moment or two, I could share my thinking.

If you were a State legislator, and you were supposed to disclose your interest in some sort of a fund, and we could establish that you knowingly failed to do that on purpose, and, moreover, you took an official action that was——

Senator SESSIONS. Well, knowingly is just—you just—that is not with intent to defraud. Knowingly is just——

Mr. BREUER. Well, I was going to take——

Senator SESSIONS. [continued] That you did not mistake—you did not see the form somehow. I do not——

Mr. BREUER. So I have two parts to it. The first part is simply I think it would be our obligation in the first instance to establish, right, that you knew that you had this obligation, the local official knew he had the obligation, we would have to establish, and knowingly did not fulfill that obligation. And then, in addition, we would have to show that that same person, that same official had the specific intent to defraud, that he took an official action, let us say, to support the fund somehow. He did some——

Senator SESSIONS. Where is that specific intent to defraud element in the legislation?

Mr. BREUER. Well, Senator, we have not proposed yet specific legislation; rather, we have discussed principles that we think are required in any kind of legislation that we think would address your concerns, which is not to be overly broad and to survive the test of time. And so we are very much guided, I should say, by what you referred to, Justice Ginsburg's footnote in the *Skilling* decision. And there the Justice, I think, gives us all guidance that if we are not going to have the same problem that we have had with the former honest services fraud statute, we need to address those due process concerns. And in doing that, I think we tried very much to narrow it and be very, very specific. I can go into it if you want, but it is really more principles——

Senator SESSIONS. OK. Well, let us stay at the larger principle question, and the panelists maybe should also discuss this. Let us take a situation in which a State has said you should disclose certain things in order for an individual city councilperson to be able to perform their duties, and they set a penalty for that. Let us say it is 6 months in jail. And so the person violates that. They do not disclose an interest. They vote on a matter that has some potential, even a small part of it could impact them favorably. You now could prosecute it as a mail fraud Federal felony of 5 years in jail. Is that right?

Mr. BREUER. So the way I would address that, Senator, is the following: That disclosure requirement simply in your hypothetical situation is a disclosure requirement that says that something needs to be disclosed.

Senator SESSIONS. This is what the local people have felt public officials, standards they ought to be held to, and they set a penalty.

Mr. BREUER. Exactly. But that is just a disclosure requirement. We are not going to prosecute the mere failure to disclose. That is a local or a State decision that the mayor or the legislator has to disclose something.

What we will prosecute is if that person, one, does not fulfill or disclose what is required, that deals with our notice requirement. That deals with our goal of fairness because that local official knew that he or she had to disclose because the municipality or the State required it.

We then are going to look to see if there is a scheme or artifice to defraud under the mail and wire fraud statutes. And in looking at that, in looking to see if there is a scheme or artifice to defraud, we both have, first, a failure in the first instance to disclose, but now what we look for is to see did you knowingly do that and did you specifically intend to defraud by on purpose taking advantage of your concealed interest. That is the difference. And if you took advantage of your concealed interest by engaging in a scheme to defraud by, let us say, acting on legislation that benefited you that no one knew about, that would be the circumstance very specifically where we would want to address that component of honest services fraud. And that is why we think we are not simply duplicating or Federalizing a local or a State statute.

Senator SESSIONS. So you have a different element, an additional element.

Mr. BREUER. Yes, exactly, Senator.

Chairman LEAHY. Thank you. Thank you very much.

Senator Kaufman.

Senator KAUFMAN. Thank you, Mr. Chairman. Welcome.

Mr. BREUER. Thank you, Senator.

Senator KAUFMAN. You talked about the problems with prosecuting under security law. Can you go through some of the problems with using security laws to prosecute the honest services fraud?

Mr. BREUER. So in the private situation, Senator, we do believe that, unlike in the public sector, we probably have more resources to go after securities fraud. Where we have concerns about honest services being used in the securities fraud setting is that if I am a mayor, I am a local official, my official actions are not intended

to benefit me personally. They are just not. They are meant 100 percent to benefit the people who elected me.

But if I am a corporate official, it is part of the free enterprise system that if I take steps that benefit my company, they inure to my own personal benefit as well. So it is just something that if we do have a private sector fix, I think we have to address.

And, similarly, we have to—so that is the first. And the second issue is I just think we have to look very hard at what the securities laws require with respect to disclosure. And some disclosure requirements are more disclosure requirements that are aimed at the corporation as opposed to the individual. That is not to say that there cannot be a private sector piece. It is just we think that there are more issues involved. And as of now, we feel for the most part—for the most part—we have been able to address most circumstances in the private sector where we see a wider gap of circumstances post *Skilling* that we cannot address in the public sector.

Senator KAUFMAN. But what about the case—just like the mayor, the mayor is really 100 percent right to help the citizens of the town that he or she represents. What about the case where you have someone in a corporation Aren't they there to represent the shareholders? So, really, if they do something that benefits themselves but disadvantages the shareholders, wouldn't that be a similar case

Mr. BREUER. It would. The difference is that in most circumstances we looked at—and, again, I do not want to be exhaustive, but in most circumstances that we have looked at, those actions, if they inure to the personal benefit of, let us say, the officer, there is more likely a chance that it is a direct money or property fraud in a sense and that it has hurt directly the shareholders; whereas, in the mayor's context it is harder typically to find that direct nexus. And it could very well be that the mayor benefits, but we cannot show a money or property loss to the constituents.

Senator KAUFMAN. All right. For a legislative fix to *Skilling*, it is important as a matter of constitutional law to place a significant minimum monetary value in order to constitute fraud. Do you agree with that?

Mr. BREUER. I do think that if we put a monetary limit with respect to the private sector, that helps to address that issue, yes.

Senator KAUFMAN. And do you have a preference as to whether Congress enacts this legislative response to *Skilling* in the fraud statute, Section 1346, as opposed to the conflict of interest statute, Section 208?

Mr. BREUER. So, yes, we do. We really would urge the Congress to deal with this under 1346. First, there is now quite a bit of case law with respect to dealing with honest services in the context of wire and mail fraud, and so we do think 1346 is appropriate.

Also, it gives us as prosecutors a greater ability to describe and prosecute the crimes because, of course, we are talking about a scheme or artifice to defraud, and those are well-understood terms.

And, last, frankly, we just think it more appropriately deals with the gravamen of the situation. The penalties are higher, and we think they are more appropriate in that context than in the conflict of interest.

Having said that, though, we do think the conflict of interest statute, 208, addressing Senator Sessions' point, is a very good way of dealing with the issue of notice or the scope. Justice Ginsburg asks, "So what is going to be the scope of this? Who is involved?" And 208, I mean, obviously Congress might decide to change it, but 208 right now tells us who are the people who a Federal employee cannot take actions on behalf of because of conflict of interest. And so we think that is well established, too, and would give the kind of notice that we think after *Skilling* is required.

Senator KAUFMAN. Great. Thank you.

Thank you, Mr. Chairman.

Chairman LEAHY. Senator Sessions, do you have anything further?

Senator SESSIONS. Well, I think before we go forward, we would like to see statutory language, and I think the fundamental question we all need to ask is: Is this an area of prosecution that the Federal Government needs to prosecute We have certain other tools in statutes that allow prosecutions. There are no problems, Mr. Breuer, are there, with regard to Federal officials who violate the laws, because we have ethics and other statutes that cover this kind of self-dealing and conflicts of interest and Senate ethics rules that apply. It is only a weakness you find as a result of this opinion in *Skilling*. It eliminated some ability to prosecute State and local officials. Is that right

Mr. BREUER. That is correct, Senator.

Senator SESSIONS. Thank you, Mr. Chairman.

Chairman LEAHY. Thank you. I will probably have some follow-up questions for the record, but we are somewhat limited in time with the votes coming up, and many of us are going to the burial ceremony at Arlington for our former colleague Ted Stevens. I especially want to be there. Senator Stevens was not only a very, very close friend; he was one who followed the old school. He always kept his word. I mentioned to Senator Sessions last night on the floor that he follows that rule, too, but I recall when I first came to the Senate, the first thing that Senator Mansfield, who was then the Leader, Mike Mansfield, told me, he said, "We may disagree on issues, and that is fine. Just keep your word." And Senator Stevens was the epitome of that. You could go to the bank with whatever he told you, and I think it is good that—I understand there is going to be a very large number of Senators from both parties who will be at the burial. I served with him for 36 years, and we will be there.

Anything further?

Senator SESSIONS. No. Thank you.

Chairman LEAHY. Mr. Breuer, thank you very much. I just would add, as we said, we are trying to put together statutes which address what I think all of us instinctively know is criminal conduct, and we will look forward to working with the Department of Justice in doing that.

I am also well aware of those things that should be handled by the local authorities, and I do not want to go to a situation where we are taking on things that local authorities should be able to do. But there are some major areas where only the Federal Government has the ability to do it, and we will work with you on that.

Mr. BREUER. Well, thank you, Mr. Chairman. Thank you, Senator Sessions. We very much at DOJ look forward to working with you. Thank you.

Chairman LEAHY. Thank you.

Chairman LEAHY. Good morning. We are joined first by Samuel Buell, who is a professor of law at Duke Law School. Prior to that he was lead prosecutor for the Department of Justice's Enron Task Force. During his time at the Department, he also served as a prosecutor in New York, Boston, Washington, and Houston. He twice received the Attorney General's Award for Exceptional Service that I would note for others is the Department's highest honor. Immediately prior to coming to Duke, he was a visiting assistant professor at the University of Texas School of Law and an associate professor at the Washington University School of Law. He received his undergraduate degree from Brown University and his law degree from New York University School of Law.

Following our normal procedure, we will hear from each of you, and then we will ask questions. Professor Buell, please go ahead, and your full statement will be made part of the record.

STATEMENT OF SAMUEL W. BUELL, PROFESSOR, DUKE UNIVERSITY SCHOOL OF LAW, DURHAM, NORTH CAROLINA

Mr. BUELL. Chairman Leahy, Ranking Member Sessions, members of the Committee, and staff, I will express two points this morning.

First, the problem of defining criminal fraud is both difficult and important. This is not a new problem, and it is not limited to the particular formulation that Congress chose when it enacted the honest services statute.

Second, the worries raised by the Court's narrowing of the mail and wire fraud statutes in the *Skilling* decision include the possible loss of serious cases of fraud involving breaches of fiduciary duty.

Allow me to begin with a quote: "[B]ecause fraud and deceit abound in these days more than in former times . . . all statutes made against fraud should be liberally and beneficially expounded to suppress . . . fraud." The date of this quote? 1601. Its author? The famous English jurist Sir Edward Coke, reporting a decision interpreting an Elizabethan statute.

Fraud is, by definition, a form of wrongdoing that evolves rapidly and is committed by actors who design their behaviors with one eye on the constraints of the law. This was true in the 1600s—at the dawn of the Anglo-American legal system and the beginnings of modern markets. It has never been more true than now after we have witnessed a decade marked by massive and elaborate financial deceptions.

Current U.S. law is, without controversy, full of highly general prohibitions against fraud, nowhere more prominently than in our law of securities regulation—a pillar of which is Rule 10(b)(5)'s edict against any and all schemes to defraud in connection with the purchase or sale of a security.

There is thus a somewhat unrealistic quality to what the Supreme Court said in the *Skilling* case. There is nothing novel, or unworkable, or imprudent about the idea of Congress passing general prohibitions on fraud and the courts working out how to apply

those general concepts to new forms of harmful deception as they arise.

What, then, explains the particular controversy over the honest services statute? This brings me to the second point. What has distinguished this statute is its effort to target frauds that involve less tangible harm than simple and direct deprivations of money or property.

This legislative effort alone should not be especially controversial. As our society and economy have become more sophisticated and complex, it has become more and more apparent that information is critical and valuable, and that fiduciary and other trust relationships are both essential to the functioning of a highly specialized economy and subject to harmful abuse. The legal concept of fraud must be permitted to adapt, as it always has, with such changes in society.

The Court's somewhat arbitrary decision in *Skilling* that frauds inflicting less tangible or less measurable harms can only be prosecuted when they involve a bribe or kickback payment risks leaving important forms of abusive deception outside the scope of Federal criminal law.

Suppose a senior officer of a company uses a loan program, approved in general terms by the board of directors, to spend lavishly and abusively on real estate, art, and luxury goods for him and his family. I am thinking here of the former Tyco chief Dennis Kozlowski.

Or suppose that the financial officer of a large public company obtains general approval to run a private investment partnership in order to engage in hedging transactions with the company, and then arranges those transactions to line his own pockets, often with undisclosed and mischaracterized payments. I am thinking, of course, of former Enron CFO Andrew Fastow.

How are these cases to be prosecuted? One might say these are securities frauds because they involve public companies. But these are not traditional accounting fraud cases. They are cases of self-dealing, hidden conflicts of interest, and looting of corporations.

Some of the requirements of the law of securities fraud, such as its particular doctrine of materiality, could pose problems for prosecutors in such cases.

Perhaps more significantly, the law of securities fraud is limited to fraud in connection with the purchase or sale of a security. These forms of harmful and deceptive self-dealing and looting can arise, with equal seriousness, in institutions and relationships ranging from law firms to hospitals to accounting firms to major nonprofit organizations.

One might also argue that these kinds of cases can be reached through property theories under the mail and wire fraud statutes and are thus unaffected by the *Skilling* case. But a prosecutor can often be confronted in such cases with defenses asserting that the general form of the conduct had been approved and that any property obtained by the defendant was within the bounds of such approval.

In addition and as importantly, abusive self-dealing is not always engaged in directly for profit. A defendant's objective may be to enhance his power or prestige or his control over an institution or re-

lationship in which others are depending importantly on him not to engage in abuse and are counting on transparency to allow them to prevent and sanction such abuse if it occurs.

The honest services statute became controversial not so much for its conceptual structure but because of the occasional but worrisome exercise of prosecutorial discretion to apply the statute to marginal cases that most people would readily identify as not belonging in Federal court.

The concern about vagueness, I submit, was really a concern about overbreadth. I thus want to conclude by suggesting some ways Congress might retain a fraud prohibition flexible enough to deal with serious, novel forms of intangible harm but confined enough to allay fears about overbroad application in the hands of imprudent prosecutors.

First, it has long been a hallmark of criminal fraud prohibitions that they have demanding mental state requirements. Not only do such laws generally require proof beyond a reasonable doubt of the defendant's specific intent to defraud, but they have often been interpreted to require that the defendant act with consciousness of wrongdoing.

One might draft a statute that applies only to willful violations and include within the statute an explicit definition of willfulness that embodies the requirement that violators must know that what they are doing is wrongful.

Second, a new statute might be limited to important fiduciary and trust relationships and made inapplicable, for example, to ordinary employment and contractual relationships.

Third, and finally, Congress might consider thresholds for identifying serious cases of harm. One might choose, for example, to require that the relationship in which the intangible harm occurs be one involving a single transaction or a course of conduct in which the victim had at risk something of value of at least $50,000.

I urge this Committee and Congress to uphold the centuries-long commitment of our legislatures, courts, and other legal institutions to deal with the ever challenging and evolving problem of fraud.

Thank you for the opportunity to testify today.

[The prepared statement of Mr. Buell appears as a submission for the record.]

Senator WHITEHOUSE [Presiding.] Thank you very much, Professor Buell. I did not have the chance to be here when you began your testimony, so let me highlight the most important part of the materials that I have on you, which is you were born in Rhode Island.

[Laughter.]

Senator WHITEHOUSE. Delighted to have you with us.

Mr. BUELL. I was raised in the great State of Rhode Island, yes, Senator.

Senator WHITEHOUSE. Thank you.

Professor Michael Seigel is professor of law at the University of Florida's Levin College of Law, where he specializes in criminal law and white-collar crime. Mr. Seigel has also served as an AUSA in Tampa, Florida, and Philadelphia. During his time in Philadelphia, Mr. Seigel worked on the Department of Justice's Organized Crime Strike Force. Mr. Seigel received his bachelor's degree from Prince-

ton University and his law degree from Harvard Law School, and we are delighted to have him with us today.

Professor Seigel.

STATEMENT OF MICHAEL L. SEIGEL, UNIVERSITY OF FLORIDA RESEARCH FOUNDATION AND PROFESSOR OF LAW, FREDRIC G. LEVIN COLLEGE OF LAW, GAINESVILLE, FLORIDA

Mr. SEIGEL. Thank you, Senator Whitehouse, Senator Sessions, and distinguished members of the Committee. I am going to limit my remarks to issues surrounding the impact of *Skilling* on the prosecution of public sector honest services fraud only.

I do not take issue with the Supreme Court's conclusion in *Skilling* that the concept of honest services found in Section 1346 was unconstitutionally vague. As the Court held, the term was so general that it did not provide citizens with fair notice of potential criminal conduct; it allowed for the potential abuse of prosecutorial discretion, both by vindictive prosecution and by the waste of precious resources, law enforcement resources, on trivial cases; and it risked intrusion, as Senator Sessions has indicated, on the rights of States to regulate their own politics.

However, the solution that the Court devised—it was really limited in devising because it cannot legislate—limiting the application of the statute to cases involving bribery and kickbacks is far from ideal. In fact, the newly narrowed statute suffers from the very same ills as before. One example will suffice to prove this point. Even after *Skilling*, Federal prosecutors could charge a State Department of Motor Vehicles employee with honest services fraud for taking a $20 bribe to allow a driver's license applicant to cut in line. I think we would all agree that making a Federal case out of such minor conduct would be an improvident use of DOJ's resources in an area in which the State would surely be equipped to handle the infraction itself.

At the same time, the *Skilling* limitation has made the scope of honest services fraud considerably too narrow, causing serious malfeasance meriting the attention of Federal law enforcement to be beyond its reach. As noted by Assistant Attorney General Breuer and also by Professor Buell, one of those main areas is failure to capture undisclosed self-dealing by a public official. But it has other failures as well that I would like to point out.

I think one of its greatest failures is in not defining bribery and kickbacks. Lacking direct guidance, lower courts are likely to import the definitions of these terms from the Federal bribery statute, 18 U.S.C. Section 201. According to the Supreme Court's decision in the *Sun Diamond Growers* case, conviction for an illegal bribe or gratuity requires proof of a quid pro quo—in other words, proof that the bribe or gratuity was paid in connection with a specific official act. Sometimes, despite obviously corrupt behavior, this element is impossible to prove beyond a reasonable doubt.

For example, a State legislator might secretly be on the payroll of a corporation that has an interest in a wide variety of matters that are the constant subject of legislation. The employer and employee use all kinds of deception to conceal the illicit income, which, say, adds up to half a million dollars a year. Although the

legislator is a routine champion of causes that benefit the company, there is no evidence of a direct link between any particular official act and his undisclosed conflict of interest. Under the post *Skilling* status quo, this arrangement, so obviously antithetical to a healthy political environment, lacks a Federal criminal remedy.

Unless Congress acts, two other categories of public sector honest services fraud cases will likewise go unaddressed. The first is composed of cases involving a public employee or official who receives a non-monetary benefit as a result of an undisclosed conflict of interest. Cases falling into this category might include a prosecutor whose purposeful failure to reveal his ties to the victim in a murder investigation leads to an overturned conviction requiring retrial at taxpayer expense; or a legislator—and, unfortunately, this is alleged in Florida, my home State—who secretly directed an appropriation to his alma mater by disguising the recipient's identity through deceptive language in the legislation that was buried pretty deep; or a judge who failed to disclose that he was negotiating with a party to a case that is before him while the case is going on if that relationship never comes to fruition.

The last type of undesirable conduct that is now beyond the reach of the mail and wire fraud statutes is a public employee's use of outright deception to obtain something other than money or property. Consider, for example, a disturbed employee of the Department of Homeland Security who exaggerates a threat for the sheer evil pleasure of causing a public panic; or a civil servant who has repeatedly falsified test scores to secure the promotion of one racial or ethnic group over another. It might be that these actions violate some other Federal law, but honest services fraud, properly construed, would be a useful and straightforward means of punishing and deterring this antisocial conduct.

Congress should, when it enacts legislation in reaction to the *Skilling* case, follow the principles suggested by Justice Ginsburg, Justice Scalia, and others here to make sure that the legislation is not vague.

In short, the new legislation should define each of its terms with precision; it should require that, to be cognizable, the conduct of the public official must violate a Federal, State, or local law, rule, or regulation; it should impose a minimum, though flexibly measured, level of intended or caused benefit or harm; it should spell out in clear terms the mens rea involved, whether it be willful or some other kind of specific intent. And this all should be done before the prosecution can prove that the statute was breached.

Properly redrafted, the mail and wire fraud statutes can continue to serve a very important role in the constant battle against serious and corrosive public corruption.

Thank you.

[The prepared statement of Mr. Seigel appears as a submission for the record.]

Senator WHITEHOUSE. Thank you very much, Professor Seigel.

Our final witness in this panel is George J. Terwilliger III. Mr. Terwilliger is currently a partner at White & Case, LLP, where he is head of the white-collar practice group. Previously, Mr. Terwilliger served for 5 years as the United States Attorney in Vermont and as Deputy Attorney General of the United States. Mr.

Terwilliger received his undergraduate degree from Seton Hall University and his law degree from Antioch School of Law, and we are delighted to have him here today.

Mr. Terwilliger.

STATEMENT OF GEORGE J. TERWILLIGER III, PARTNER, WHITE & CASE, WASHINGTON, DC

Mr. TERWILLIGER. Thank you, Senator Whitehouse. I appreciate that. Senator Sesions.

Public corruption investigations and prosecutions continue to deserve to be among the highest priorities of Federal prosecutors. Public corruption is an insidious wrong that engenders in our citizens disrespect for the rule of law and cynicism about the rectitude of public institutions. When the legislative process is corrupted by personal financial gain or the deliberative process is warped by corrupt practices, fundamental guarantees made to the people by law are thwarted and the democratic process itself is undermined.

To briefly relate some aspects of my professional experience that inform my testimony today, during the time that I was privileged to serve as Deputy Attorney General of the United States, I was called upon on several occasions to make final judgments concerning recommended prosecutions of Members of this body and other public officials. In private practice, I have been counsel to Members of this body and the other House of Congress, as well as for appointed officials in the executive branch and high-ranking State officials.

I have seen firsthand the toll that investigations and accusations alone, short of indictment, can exact on an individual. I am thus especially grateful to have the opportunity you have afforded me today to participate in the Committee's consideration of further anti-corruption legislation.

I agree with the Committee's apparent goal of providing Federal prosecutors the tools they need to address certain conduct by corporate and other private officers and employees. When such persons deal to themselves under the table, all the attributes of a free market are put in jeopardy.

As to all aspects of the matter under discussion, I respectfully urge the utmost care in defining clearly that conduct which is to be proscribed by Federal law. Justice Ginsburg's observation concerning the need for clarity I think is indeed a warning. Ambiguous statutory terms and requirements present interpretive problems that can require substantial judicial and other resources to resolve and, frankly, are unfair to public officials and others who deserve to be able to refer to and abide by clear lines between what is lawful and unlawful behavior.

Perhaps most relevant to the legislation on the table for discussion today are issues that arise where public or corporate officials have private or personal financial interests which may affect, or be affected by, their execution of their official duties. These circumstances present an even greater challenge in trying to write clear laws that both recognize the complex financial and regulatory world we live in today and nonetheless provide the clarity necessary to delineate conduct which could subject individuals to criminal conviction. Given the complexity of determining corporate

and other disclosure obligations, heeding Justice Ginsburg's admonition may well suggest that further study and consideration be taken before the legislative action goes forward on this type of activity.

While I urge the Committee to defer this legislation pending further study and consideration, I thank it for the opportunity to appear. I have more specific observations in my prepared statement, which Senator Leahy has said would be accepted for the record. I have just two comments on the testimony that the Committee has heard thus far.

First, I appreciate very much and agree I think with about 90 percent with what we heard from Assistant Attorney General Breuer. The one question that I think lingers after his formulation of principles for a testimony is when he talks about a specific intent to defraud. I think one has to ask the question: Defraud whom and for what? And if that gets us back to defrauding the citizens or the people from their honest services that they have a right to or some other intangible, I think it continues to beg the question.

In terms of Professor Buell's testimony, I would only observe that Coke was talking about common law fraud, and one of the elements of common law fraud has always been the occasion of economic injury to someone. When we went beyond economic injury into the concept of the deprivation of intangible rights, I think this became a very difficult endeavor.

Senator Sessions mentioned the importance of clarity. I think it was Judge Learned Hand who once wrote, or words to the effect, that the true dimensions of fraud are only limited by the human imagination. Fraud is in and of itself a very expansive concept. Adding onto it concepts of intangible rights as deprivations that can support an allegation of fraud I think is very difficult.

The bottom-line problem with all of that has come down to—and I think the Court will never accept going back to this, and that is that it puts prosecutors in the position of setting the standards instead of the legislature writing what they may be, or at least writing what they may be by reference to some other disclosure obligation that already exists.

Thank you very much, Senator Whitehouse, Senator Sessions.

[The prepared statement of Mr. Terwilliger appears as a submission for the record.]

Senator WHITEHOUSE. Thank you, Mr. Terwilliger. We appreciate your testimony.

I will defer to the Ranking Member, Senator Sessions.

Senator SESSIONS. Well, thank you, Senator Whitehouse, and I know as a former United States Attorney you are familiar with these issues.

I do think the Supreme Court has raised an important issue. This is not something we can just respond to in a knee-jerk fashion. Apparently, the new version of the mail fraud statute as a result of the *McNally* decision, we just promptly came in and passed 1346 that said, well, you struck that down, so we now make it a crime to deprive a person of an intangible right of honest services.

Now, that is a bit of a stretch, I got to tell you. That is all it takes to do that consistent with the traditional mail fraud statute. Now that is not holding up, so we say we want to redo it to respond

to the Supreme Court in *Skilling* and make it a crime to undisclosed self-dealing, which is a bit nervous to me.

And then, Professor Buell, I do not think you were suggesting this, but some might think it appropriate that a judge develop the law as it goes forward and just case by case decide what a statute means. But I do think it is incumbent on Congress to pass a law that means what it says and is clear so a person can adjust their conduct to it. If they do not have internal moral standards that would otherwise cause them to behave better, they at least know what the law is and where the line is. And when you leave it vague for a judge to decide, obviously the defendant did not have a very good chance to know what it was either before he or she committed the crime.

Professor Seigel, with regard to the *McNally* standard that the Supreme Court struck down, I am not sure when that developed. That was not really in the original understanding of mail fraud when I was prosecuting cases, I do not think.

Mr. SEIGEL. That is correct.

Senator SESSIONS. Somewhere along the line, prosecutors figured out how to stretch this to include honest services, and eventually the Supreme Court said, "Uh-uh." Do you know when it first started in——

Mr. SEIGEL. I believe it started somewhere in the 1920s or 1930s, maybe a little later than that. Congress had amended the statute adding money or property for a completely different reason, trying to make it clear that fraud was not the common law concept of fraud but was a more modern version of fraud. And as I understand it, Congress left a comma in there which later on prosecutors used to argue separated out the money and property from the notion of fraud, and that is how they developed this intangible rights theory, which the courts let them go along with.

But really I agree with you, Senator Sessions, I think that not only has the law been unclear—I mean, one of the main pieces of evidence of the lack of clarity for the law is that most of the circuits that have—everybody has recognized that this is way too broad, and so each circuit has tried to narrow the concept to what they felt comfortable with in terms of making it a Federal prosecution, and they have come up with four, five, or six different methods of narrowing it. And I think that is really where the Supreme Court was coming from, saying it needs to be narrowed and it needs to be narrowed very precisely and carefully by the legislative body, because if the courts are doing it all over the place, there is no notice to the citizens.

Senator SESSIONS. Well, Mr. Terwilliger, you were a long-time Federal prosecutor, very familiar with these cases, and as a Federal prosecutor, you know that certain crimes or wrongs that you would like to vindicate did not fall within Federal law. They just do not. And I have been there. This is horrible and you dig into it, and it just did not violate the Federal law. Maybe it violated State law, but maybe we do not think they are good enough or got enough money or time or effort to prosecute this case. And so an injustice will be done.

But perfect justice is not possible in this world. I think it was a judge on the Supreme Court of California who said perfect justice

is a mirage, that in the pursuit of perfect justice, we destroy what justice we can achieve.

And so where do you feel this line ought to be drawn? You were the Deputy Attorney General, and you were a line prosecutor, and you were a U.S. Attorney. Are we leaving too much out, in other words, as a matter of policy, or are we leaving too many wrongs outside of Federal prosecution, or are we, in an attempt to eliminate all wrongs, reaching beyond the historical role of the Federal Government and trying to criminalize things that are too vague to criminalize?

Mr. TERWILLIGER. Well, Senator Sessions, I think you have really put your finger on what the challenge here is. It certainly is not a partisan issue. I think, to coin a phrase, this is a post-partisan issue given the level of corruption that exists at various levels of Government. But I think you can parse the challenge into two parts.

One part is writing a law that is clear enough, that is going to pass muster with the Supreme Court along the standard that Justice Ginsburg's admonition sets; and, second, that really does give people fair notice of what they can do and not do.

The second, which really applies more to the issue of dealing with State and local corruption and perhaps corruption in the business and private world, is how far should the Federal Government go. And the problem that we have—and I think everybody here is a former Federal prosecutor, recognizes that the more space that there is in a statute, the more prosecutors will find a way to fill that space and expand perhaps even what the Congress originally intended.

Really, I am not—I do not think anybody has all the answers, and I know that I do not at this point. But I do think that sort of framing the issue as let us deal with what is appropriate to deal with Federal officials, let us deal with what is appropriate to deal with State and local officials, and then let us deal separately with what is appropriate in terms of conflicts of interest and undisclosed financial interests in the private world makes sense, because each one of those is a different kind of wrong that offends a different notion of justice and what the Federal Government should be doing.

For me, frankly, one thing that occurs to me on the State and local issue, which I think is really where this is perhaps difficult to focus, Congress passed a statute which is now 18 U.S.C. 666, bribery in Federal programs. The courts, including the Supreme Court, have really expanded the coverage of that statute to cover any bribery in a State or jurisdiction in a State that gets Federal assistance, which is literally everybody.

It seems to me that rather than grapple with this issue that Mr. Breuer's suggestion to put this in the wire and mail fraud statute brings up—and, that is, a scheme to defraud whom of what—it might be easier to put this in 666 and to criminalize conflicts of interest arising from undisclosed financial obligations by any official in a jurisdiction that receives Federal funds—constitutionally, then it goes right to the spending power—and to have that dependent, as Mr. Breuer I think rightfully suggests, on some pre-existing State or local obligation to make that disclosure.

If you will permit me just one more minute here, when I saw Senator Leahy, I was actually reminded we both were in Vermont for a long period of time. We have very localized governments. A road commissioner in Vermont is in charge of plowing the snow and keeping the roads clean, which can be a real challenge in Vermont. If a town were to allow a circumstance where, instead of investing in all the heavy equipment necessary to do that, the road commissioner was allowed to contract that service out and he contracted that service out to a contractor who made the capital investment in that equipment, thus saving the town those capital costs, who happened to be his brother-in-law, or his brother for that matter, and everybody in town knew it, one would expect that nobody would have a problem with that, including on the Federal level. And I think what we need to do is make sure that when we write the standards that would govern what can be a Federal crime under State and local law, we take into account those very localized sets of circumstances and keep those off limits.

Senator SESSIONS. Well, I think 666 is a suggestion that I had thought might be a way to proceed also.

Well, thank you, Mr. Chairman. These are not little-bitty matters, and I do not think that Congressmen or Senators should be condemned if they say we do not need to Federalize every wrong. You know, we would rather have a clear line, make sure this line is clear on what it is that amounts to a Federal crime. And if people can maneuver out of it on occasion and you miss a few cases that have to be prosecuted in State court, I do not know that the Republic will decline. Certainly we did not have this language previously in our statutes.

Mr. SEIGEL. Senator Sessions, may I address that? Again, we all are former members of the Department of Justice, and I do think that it is important also to balance the countervailing notion that it seems to me it has always been a special province of the United States Department of Justice to root out local corruption, because as we know for a wide variety of reasons, that is a particularly difficult area for local law enforcement to do on their own. There are lots of local political pressures and other reasons, budget reasons, but there are lots of reasons why it is often not done at the local level. And it always made me proud as a Federal prosecutor that that was one of the areas that we spent time on. And if it was local law enforcement or local political environment or whatever it was, it seemed to me that that was a very legitimate area of Federal interest because, in effect, it is the central government assuring the citizens that they are being fairly treated by all of their governments.

So although I agree with you, you know, we do not need to Federalize everything and maybe there are things that already are Federal that probably ought not be, I do think we want to make sure, as we are looking at a fix for this, that we not leave out any significant area of corruption that will not otherwise be addressed. And at the same time, I remind the Congress that, as I pointed out, right now if you did nothing, you have an honest services fraud statute that can apply to a $20 bribery on the State level. And I am not saying a Federal prosecutor would take that case, but there is nothing in the law at the moment that even after *Skilling* would

stop a Federal prosecutor from taking that case. So I think it is both overbroad and underinclusive.

Senator SESSIONS. Thank you. We need to work on it, and to me it is a bit of a sad thing that the Federal Government has had the burden of prosecuting more of these cases. In truth, it would be better that they could be prosecuted locally. I think the police departments, State investigators, State prosecutors are more skilled than they used to be, but still they are overworked, stressed, and often the objectivity that occurs in a Federal courtroom as opposed to a judge and his friend who is the mayor and he is trying the case, it just becomes very difficult, in my personal view, and we do not want to eliminate the Federal ability to—its historic role. But these phrases I do not believe when I was prosecuting in the early 1980s, particularly I tried a number of cases, I do not believe the honest services was available, or maybe there was a case or two that were just touching on it, and I successfully prosecuted mayors and county commissioners and water and sewer board people. In Georgia, I think, Mr. Terwilliger, they prosecuted 40 sheriffs over a period of years out of the 170 that I think they have. But the result—the tools existed for pretty effective Federal prosecution, even without these newer powers.

Senator WHITEHOUSE. I would tend to agree with Senator Sessions on this, and I think a lot of it has to do with resources. I can remember as United States Attorney in Rhode Island running a very lengthy and very complex undercover investigation into municipal corruption in our capital city. It involved confidential informants. It involved undercover agents who had to be backstopped and brought in and the cover created and all of them, you know, run as agents. It involved wiretaps and surveillance. It involved a very complex array of techniques and strategies, and in doing all of that, it was a quite well established Federal process to go through all that. If anything, the Department of Justice's role was to push back a little bit on the U.S. Attorneys and say, Wait a minute, let us double-check, let us take a second look, what are you doing And, you know, you had to push for your case against that pressure.

I then was elected Attorney General for the State of Rhode Island, and we did the first public corruption wiretap in the State's history. As Professor Buell knows from his time growing up there and from his time at Brown University, Rhode Island is not a State that has been immune to political corruption. And yet it was tradition of the State that wiretaps were used for narcotics investigations, not for public corruption investigations. The State police knew how to do it. It just had never been sort of—that skill set had never been picked up from the narcotics unit, moved over to the public corruption unit, and deployed against public officials. And we were able to deploy it effectively against a local public official and get him on tape in a bribery scheme.

And so I agree that there is an important Federal role. I think it has a lot to do with resources. I think that the idea that the Federal Government can sometimes be the only place that comes in to clean up a local corruption problem is one that we have to bear keenly in mind. But I think Senator Sessions is dead right that that goes to the definition of what local is, and that should not be

the bar. The definition of what corruption is needs to be clear and bright, and I think that is what we are talking about.

It strikes me that—I would like to ask you to comment on Lanny Breuer's testimony in one respect, and here is how I read it. The vast bulk of these public corruption cases can be pursued under a bribery, extortion, racketeering, RICO even, existing rubric. And in those cases, you need a payment of some kind made, some thing of value being delivered to the principal or to a party in interest with him or her. And then you kind of have the law in place to go ahead and do that.

Then you have the problem of these conflicts of interest, and what he has brought together is a notion that if two things occur in tandem—one is somebody concealing a financial interest, and the second is them taking official action to benefit themselves or a party in interest with them—in relation to or as, you know, bound together in a common scheme with the failure to disclose, then you have a sound basis for a Federal prosecution. You are not going to go after a public official who has missed a contribution in a filing schedule and 4 years later voted for a bill that helps the insurance industry, and it turns out that that contribution 4 years ago was from an insurance executive and, boom, if you are targeting that public official, now you have a case. It requires more than that. It requires this common scheme that the failure to disclose relates to the misconduct or the advancement of that financial interest.

I think that seems like a sensible place to begin, and we are buttressed a little bit in this, as I understand it, by—with respect to many of the reporting statutes, particularly those that govern public official, a willful failure to file, a knowing failure to file has its own set of adverse consequences. So you can pick up the filing problem on its own. You can pick up the bribery payment extortion problem on its own. And this seems to me like a good foundation for looking at the remainder without getting into terms as abstruse as denial of honest services.

I would like to have each of you just react to that observation, you know, if you think I am off base on that, if Assistant Attorney General Breuer is off base.

Mr. BUELL. Thank you, Senator. I addressed my comments primarily to the problem of private sector cases, but I think part of what I said, and particularly in my written testimony——

Senator WHITEHOUSE. For purposes of this question, let us focus on public——

Mr. BUELL. Yes, and what I was going to say is I think an important part of what I had to say about that translates over here to what I would want to stress in the public sector context as well, which is that I do not think enough attention has been given in this entire discussion to the importance of mental state, mens rea in criminal statutes, and particularly in fraud statutes. And the Assistant Attorney General kept emphasizing you would have to have the specific intent to defraud, that that is how we know it is more than just a non-disclosure or even a—you knew you did not fill the form out right. And I think Mr. Terwilliger is right to ask, well, what do we mean by that? And maybe more thought needs to go into what we mean by that——

Senator WHITEHOUSE. Doesn't connecting the concealment with the official act act as a very, very good proxy for the adequate mental state?

Mr. BUELL. I would say in general, yes, but what we really need to be talking about—and, I mean, this really draws from my experience as a prosecutor and will probably resonate with others here—is the kinds of evidence that you normally look for in a case to say what we have here is a specific intent to defraud, isn't just the conduct itself, but it's what traditionally we refer to as the badges of fraud. You know, it is some kind of creation of fictitious entities, destruction of evidence, covering up, the kind of conduct that can allow you to say, look, this person was not just hiding something, they knew they were doing it in a wrongful manner.

And I believe that that kind of an inquiry and how you embody that in a statute, whether it is with a willfulness requirement or something else, I believe that kind of an inquiry goes a long way to guarding against the worries about overapplication of an overly vague law. The Supreme Court has said over and over again——

Senator WHITEHOUSE. Professor, if you could wrap up really quickly, I just got passed a note that says we have 10 minutes left on the vote on the floor——

Mr. BUELL. OK. Well, I was just going to say——

Senator WHITEHOUSE [continuing]. And I would like to give time to the other two——

Mr. BUELL [continuing]. That the Supreme Court itself has emphasized again and again that demanding mental state requirements can go a long way to dealing with vagueness problems in criminal statutes.

Senator WHITEHOUSE. Very good.

Professor Seigel.

Mr. SEIGEL. My reaction very briefly would be I think you are right, and I just want to point out, the reason why you need this additional tweak after *Skilling* is that in these kinds of arrangements, let us say that the decisionmaker in Government is on the payroll secretly of the company that he has voted to give the work to. The reason why that is not traditional money or property fraud is the prosecutor may not be able to prove that the taxpayers did not get their money's worth. They may very well have gotten good services. The point is they did not know that he was getting a cut of the pie. So it is not traditional, you know, mail and wire fraud, and now it is not covered because——

Senator WHITEHOUSE. Because there is no loss.

Mr. SEIGEL. There is no monetary loss.

Senator WHITEHOUSE. To the injured party.

Mr. SEIGEL. That is right.

Senator WHITEHOUSE. At least not provable loss.

Mr. SEIGEL. Correct. Correct. And yet there is this deception resulting in this personal gain which I think we all agree is corruption. So I do think that is a very important area to address, and I do think with the various safeguards requiring some—you know, it has to be more than a trivial amount of money and so forth that we can—and adding in the other requirements, we can make sure that it is specific and puts sufficient notice to the public.

Senator WHITEHOUSE. Mr. Terwilliger.

Mr. TERWILLIGER. Thank you, Senator Whitehouse. I really must say I compliment the Committee on the substantive nature of this hearing. I do not want to say it does not happen that often, but in my experience, this one is sort of above the line considerably. I think it does provide a good foundation, but I think you have just put your finger on exactly where the problem lies and where this can go awry.

If we assume we have a local official who does his job to the nth degree, takes care of the citizens and does everything, and in the process finds a way to enrich himself or herself in a way that is undisclosed, that is the problem we are talking about. The question then becomes: Is that purely a Federal crime And I think the answer to that is it is probably not purely a Federal crime, unless the State or locality has set some kind of a standard of disclosure of that very interest that would, in fact, make it an actionable wrong under Federal law.

The federalism issue, I could not agree with you more, and your experience, Senator Whitehouse, in Rhode Island is probably one of the quintessential great examples of what the Federal role really is and needs to be. And I compliment you on the success of that.

But I think we have to be very, very careful that we do not have anything as amorphous, again, as honest services that lets Federal prosecutors set the standards for what may be disclosed or even what self-dealing is allowed. Those lines ought to be drawn by the State and local jurisdictions, and then Federal prosecutors are the safety net under whatever kind of enforcement mechanism they have to make sure, if that job does not get done on the State or local level, that it does get done on the Federal level.

Senator WHITEHOUSE. We are winding down toward the end of the vote, so why don't I give Senator Sessions closing words, and then we will adjourn, and the hearing will remain open for an additional week if anybody wishes to add further testimony.

Senator SESSIONS. I think it is a good discussion. What we do not want to get into is something like you have in Russia with a bunch of oligarchs and one of them here takes the President and it is easy to find he did something wrong. Most American business and public officials try to stay within the law, and you do not want to be in one of these situations where the perception is among the private sector and the public sector that anybody that wants to "get me" can go out and find something and prosecute me for it. That is an overreach, too, and we do need to think through that. Otherwise, it can become—the prosecution can become a tool of political power and punishment of opponents. Usually that is raised when you prosecute somebody, as I found, but I always felt I could defend clearly what I charged and what the law was, and that this person violated it. The vaguer you get, the harder it is to defend against accusations of political and abusive prosecution.

Thank you, Mr. Chairman.

Senator WHITEHOUSE. The hearing is adjourned. I thank very much the witnesses for their testimony. One of the reasons that the hearing was substantive was because you were all so expert and helpful. Thank you.

Mr. BUELL. Thank you.

Mr. SEIGEL. Thank you.

Mr. TERWILLIGER. Thank you.

[Whereupon, at 11:42 a.m., the Committee was adjourned.]

[Questions and answers and submissions for the record follow.]

QUESTIONS AND ANSWERS

U.S. Department of Justice

Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

November 9, 2010

The Honorable Patrick Leahy
Chairman
Committee on Judiciary
United States Senate
Washington, D.C. 20515

Dear Mr. Chairman:

Enclosed please find responses to questions for the record arising from the appearance of Lanny Breuer, Assistant Attorney General of the Criminal Division, before the Committee on September 28, 2010, at a hearing entitled "Restoring Key Tools to Combat Fraud and Corruption After the Supreme Court's Skilling Decision."

The Office of Management and Budget has advised us that from the perspective of the Administration's program, there is no objection to submission of this letter. We hope this information is helpful. Please do not hesitate to contact this office if we may provide additional assistance regarding this, or any other matter.

Sincerely,

Ronald Weich
Assistant Attorney General

Enclosures

cc: The Honorable Jeff Sessions
Ranking Member

Written Question for Assistant Attorney General Lanny Breuer
Senator Patrick Leahy, Chairman, Senate Judiciary Committee,
Hearing on "Restoring Key Tools to Combat Fraud and Corruption
After the Supreme Court's Skilling Decision"
September 28, 2010

In your hearing testimony, you focused primarily on the impact of the Skilling decision on prosecutions of state and local public officials. You asserted that a legislative fix, particularly one that addresses the issue of undisclosed self-dealing, is necessary and that, absent such a fix, federal prosecutors might be unable to prosecute significant corrupt conduct by state and local officials.

A. Have there also been cases in which federal officials have been charged with honest services fraud for undisclosed self-dealing?

As an initial matter, the Department of Justice believes that any effort to fill the gap created by the Supreme Court's decision in Skilling v. United States, 130 S.Ct. 2896 (2010), should apply to public officials at all levels of government – state, local, and federal. The public has a right to know that government officials are acting in the public's best interests, rather than attempting to further their own undisclosed financial interests. That right applies with regard to officials from the three branches of the federal government, as well as to officials from state and local governments.

The Department has charged federal officials with honest services fraud not only for cases involving bribery, but also those related to undisclosed self-dealing. Indeed, the honest services fraud statute, 18 U.S.C. § 1346, has been used against federal officials, as well as state and local officials, for many years. For example, Congressman William Jefferson was convicted of honest services fraud, and former Congressman Richard Renzi has been indicted on multiple charges of honest services fraud, and both cases involve undisclosed self-dealing in addition to bribery.

B. Is the Department of Justice concerned that, without a legislative fix clarifying that honest services fraud includes undisclosed self-dealing, there will be cases involving significant corrupt conduct by federal officials, as well as state and local officials, that will be more difficult or impossible to prosecute?

Yes, the Department is concerned that, without a legislative fix, it will be more difficult and, in some instances, impossible to prosecute federal officials, as well as state and local officials, for significant corrupt conduct. Corrupt public officials are creative and consistently devise new kinds of schemes to benefit themselves at the expense of the citizens who trust them. Before the Skilling decision, the honest services fraud statute provided an important and flexible tool to address the wide variety of criminal schemes devised by corrupt officials.

64789.002

When a federal public official engages in undisclosed self-dealing, it is likely that the conduct will fall outside the reach of currently existing statutes. If the federal official is within the executive branch, we may be able to use the conflict of interest statute, 18 U.S.C. § 208, to address the conduct if all of the elements of that statute have been met. Section 208, however, has limitations. For example, § 208 does not apply to the judicial or legislative branches, and thus undisclosed self-dealing by employees in Congress or the federal courts is not covered. Moreover, § 208 is not a predicate offense for Title III wiretaps or for racketeering charges under the RICO statute, while the mail and wire fraud statues are predicates for both.

In sum, the Department believes that a legislative fix that fills the gap created by the Skilling decision should apply to undisclosed self dealing in the federal government, as well as state and local governments.

64789.003

SUBMISSIONS FOR THE RECORD

STATEMENT OF

LANNY A. BREUER
ASSISTANT ATTORNEY GENERAL
CRIMINAL DIVISION
UNITED STATES DEPARTMENT OF JUSTICE

BEFORE THE

UNITED STATES SENATE
COMMITTEE ON THE JUDICIARY

HEARING ENTITLED

"HONEST SERVICES FRAUD"

PRESENTED

SEPTEMBER 28, 2010

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00035 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.004

Mr. Chairman, Senator Sessions, and distinguished Members of the Committee – thank you for your invitation to address the Committee and for giving me the opportunity to discuss the Department of Justice's views on the important topic of honest services fraud.

Introduction

I am privileged to represent the Department of Justice at this hearing and to lead the Criminal Division's many exceptional lawyers, including those involved in the investigation and prosecution of fraud and public corruption. Protecting the integrity of our government institutions and our market place is among the highest priorities for the Department of Justice. Our citizens are entitled to know that their public servants are making decisions based upon the best interests of the citizens who elect them rather than for personal gain. Likewise, investors and shareholders are entitled to know that corporate officers and fiduciaries are acting in the investors' and shareholders' best interests and not attempting to secretly benefit themselves.

The Department of Justice is committed to using all available tools in our effort to combat fraud and corruption in the public and private sectors. Our enforcement efforts, which employ a number of different federal statutes, remain active and successful. However, one of the tools that we have relied upon for more than two decades was significantly eroded as a result of the Supreme Court's recent decision in *Skilling v. United States*. In *Skilling*, the Supreme Court held that the honest services fraud statute, 18 U.S.C. § 1346, applies only to bribery and kickback schemes, and not in situations involving undisclosed self-dealing by a public official or private employee. In short, the *Skilling* decision removed a category of deceptive, fraudulent, and corrupt conduct from the scope of the honest services fraud statute and placed that conduct beyond the reach of federal criminal law. The Department believes that the Court's decision has

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00036 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.005

created a gap in our ability to address the full range of fraudulent and corrupt conduct by public officials and corporate executives, and we urge Congress to pass legislation to fill the void.

In my testimony today, I would like to describe for the Committee the importance of honest services fraud prosecutions, the impact of the *Skilling* decision on our ability to combat fraud and corruption, and the need for legislation to fill the gap created by the Supreme Court's decision.

BACKGROUND

For decades, federal prosecutors used the mail fraud and wire fraud statutes – 18 U.S.C. §§ 1341 and 1343 – to reach not only crimes aimed at depriving victims of money or property, but also schemes designed to deprive citizens of the honest services of public and private officials who owe them a fiduciary duty of loyalty. The two core examples of honest services fraud had always been public officials and corporate officers (1) accepting bribes or kickbacks, or (2) engaging in undisclosed self-dealing. Such schemes did not always cause a tangible loss of money or property to the victims. Instead, the harm was to the integrity of the decision-making process itself.

While other criminal statutes, such as those prohibiting bribery and extortion, have long been the primary tools used by federal prosecutors to attack corruption by public and corporate officials, the honest services theory of mail and wire fraud was used widely because corrupt individuals could be very creative, and the schemes that they devised included a wide range of dishonest conduct that was not always susceptible to definition as a bribe or extortion. For example, if a local health official were to refer citizens with disabilities to a housing facility owned by a third party in exchange for payments from that third party, the corrupt conduct is easily characterized as bribery. But imagine instead a situation where the local health official

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00037 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.006

profits by referring disabled citizens to a housing facility in which the official himself has a concealed ownership interest. This undisclosed self-dealing or concealed conflict of interest is not bribery, but is just as violative of the public trust. The honest services fraud offense provided prosecutors with a tool that could be used to attack corrupt conduct in all its diverse and creative forms.

In 1987, however, in *McNally v. United States*, the Supreme Court held that the mail and wire fraud statutes did not cover honest services fraud schemes and instead applied only to schemes to deprive victims of money or property. Congress immediately recognized that the *McNally* decision created a gap in the Department's ability to address serious fraud and corruption, and acted quickly to bring honest services fraud within the scope of the mail and wire fraud statutes. In 1988, Congress enacted Section 1346, expressly providing that the mail and wire fraud statutes cover schemes "to deprive another of the intangible right to honest services."

In the twenty-two years since the enactment of Section 1346, the Department of Justice has used the statute extensively to prosecute fraud and corruption in the public and private sectors. Hundreds of prominent defendants and public officials have been convicted using this statute, under both core theories of honest services fraud. To name just a few from recent years:

- Former Congressman William Jefferson was convicted in 2009 of honest services fraud for accepting bribes related to his efforts to influence foreign officials in obtaining contracts for a technology company.
- Former Congressman Robert Ney pleaded guilty in 2006 to honest services fraud conspiracy for taking official action on behalf of clients of Jack Abramoff in exchange for bribes, as well as for taking official action on behalf of a foreign businessman in exchange for over $50,000 in gambling trips.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00038 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.007

- Former Lobbyist Jack Abramoff also pleaded guilty in 2006 to honest services fraud conspiracy for his role in orchestrating the bribery of Members of Congress, Congressional staffers, and Executive Branch officials.
- And former Illinois Governor George Ryan was convicted of honest services fraud for his actions while Secretary of State and Governor, when he steered contracts and leases to entities controlled or represented by his co-defendant and others in exchange for thousands of dollars in personal benefits to him and his family.

THE *SKILLING* DECISION

For many decades, both before the *McNally* decision and under Section 1346, the two core forms of honest services fraud recognized by the courts remained the same: first, schemes involving bribery and kickbacks, and, second, schemes involving undisclosed self-dealing. In *Skilling*, the Supreme Court eliminated this entire second category of schemes from the reach of Section 1346, holding that the statute covers only bribery and kickback schemes, and not schemes involving undisclosed self-dealing.

The impact of *Skilling* on pending investigations and our ability to bring criminal charges for certain types of corrupt conduct is significant. The Department's efforts in this area are robust. But by eliminating undisclosed self-dealing from the scope of the honest services fraud statute, the *Skilling* decision takes away one of the tools that the Department has heavily relied on to address corruption. Again, while I cannot comment on any investigations that have not led to criminal charges, I can assure you that the impact of *Skilling* is real, and that there is conduct that would have been prosecuted under the honest services fraud statute before *Skilling* that can no longer be prosecuted under the federal criminal law.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00039 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.008

As any prosecutor can attest, corrupt officials and those who corrupt them can be very ingenious, and, as we all know, not all corruption takes the form of bribery. For example, if a mayor were to solicit tens of thousands of dollars in bribes in return for giving out city contracts to unqualified bidders, that mayor could be charged with bribery. But if the same Mayor decides that he wants to make even more money through the abuse of his official position, he might secretly create his own company, and use the authority and power of his office to funnel City contracts to that company. Although this second kind of scheme is corrupt, and undermines public confidence in the integrity of their government, it is not bribery. Accordingly, after *Skilling*, it is no longer covered by the honest services fraud statute or any other federal statute.

NEED FOR LEGISLATION

A public official who conceals his financial interests and then takes official action to advance those interests engages in behavior every bit as corrupt as if he accepts a clear bribe from a third party. The Department urges Congress to act quickly to restore our ability to prosecute individuals for this kind of undisclosed self-dealing. We recognize that Congress cannot remedy the problems caused by *Skilling* in regard to past conduct because of the *Ex Post Facto* Clause of the Constitution, but it can act to provide our prosecutors with an additional important tool to fight fraud and corruption in the future. We look forward to working with the Committee to insure that any legislative solution to fill the gap created by *Skilling* will not only cover the necessary ground, but also stand the test of time.

The need for a statute focusing on the public sector is urgent because undisclosed self-dealing by public officials is the type of corrupt conduct that is most likely to fall outside the reach of any other statute. The Department therefore supports legislation that would restore our ability to use the mail and wire fraud statutes to prosecute state, local, and federal officials who

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00040 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.009

engage in schemes that involve undisclosed self-dealing. Let me provide a few suggestions regarding such legislation:

First, in order to follow the Supreme Court's direction in *Skilling* that any legislation in this area provide notice to citizens as to what conduct is prohibited, the statute should be clear and specific.

Second, like Section 1346, the new statute should rely upon the mail and wire fraud statutes, which provide a reliable and well-established jurisdictional basis for prosecution, and would enable prosecutors to capture the full scope of an expansive criminal scheme in an appropriate criminal charge.

Third, in order to define the scope of the financial interests that underlie improper self-dealing, the statute should draw content from the well-established federal conflict of interest statute, 18 U.S.C. § 208, which currently applies to the federal Executive Branch.

Finally, the statute should provide that no public official can be prosecuted unless he or she knowingly conceals, covers up, or fails to disclose material information that he or she is already required by law or regulation to disclose. By requiring the government to prove both knowing concealment <u>and</u> a specific intent to defraud, there is no risk that a person could be convicted for a mistake or unwitting conflict of interest.

We believe that legislation along these lines would restore our ability to address the full range of criminal conduct by state, local, and federal public officials, whether the corrupting influence comes from an outside third-party, or from the public official's concealment of his financial interests.

The Department is also interested in working with the Committee on legislation to address corrupt private sector actors as well. For a number of reasons, crafting appropriate

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00041 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.010

language concerning undisclosed self-dealing in the private sector is more difficult than with respect to the public sector. In addition, because undisclosed self-dealing in the private sector usually involves a loss of money or property, the existing mail and wire fraud statutes can often be used effectively to reach the improper conduct. That said, there are certain types of self-dealing by corporate officers that existing statutes do not allow us to reach and where a new prosecutorial tool would be welcomed. The Department is happy to work with the Committee in crafting an appropriate solution.

CONCLUSION

Corrupt individuals can be very creative in their efforts to benefit themselves at the expense of those to whom they owe a duty of loyalty. While the Department of Justice's work in this area remains active and successful, the Department needs a full range of tools to address fraud and corruption in all forms. the Supreme Court's decision in *Skilling* removed undisclosed self-dealing from the scope of the federal criminal law, and we urge Congress to act quickly to restore our ability to address this significant category of fraudulent and corrupt conduct.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00042 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.011

Written Testimony

United States Senate Committee on the Judiciary Hearing: "Restoring Key Tools to Combat Fraud and Corruption After the Supreme Court's *Skilling* Decision"

September 28, 2010

Professor Samuel W. Buell, Duke University School of Law

Chairman Leahy, Ranking Member Sessions, Members of the Committee, and staff:

Thank you for the opportunity to testify today about the fate of fraud prosecutions in the wake of the Supreme Court's decision in *United States v. Skilling*. I am a professor of law at Duke University and have served on the faculties of the University of Texas School of Law and Washington University School of Law in St. Louis.

For nine years prior to teaching, I served as an Assistant United States Attorney, prosecuting complex federal criminal cases in New York, Boston, Washington, DC and Houston. I spent my last years in the Department of Justice as a member of the Enron Task Force, leading the two-year investigation that produced the initial indictment in the *Skilling* case. While with the Department, I twice received the Attorney General's Award for Exceptional Service.

I will stress two points in my testimony today. First, the problem of defining criminal fraud is both difficult and important. This is not a new problem. It is not limited to the particular linguistic formulation that Congress chose when it enacted the federal "honest services" statute. And Congress must not shy away from continuing to address the challenge of legislatively prohibiting fraud.

Second, the worries raised by the Court's narrowing of the mail and wire fraud statutes in the *Skilling* decision include—but may not be limited to—the possible loss of serious cases of fraud involving breaches of fiduciary duty, both within and outside the corporate context.

Allow me to begin with a quote: "[B]ecause fraud and deceit abound in these days more than in former times ... all statutes made against fraud should be liberally and beneficially expounded to suppress ... fraud."

The date of this quote? 1601. Its author? The famous English jurist Sir Edward Coke, reporting a decision interpreting an Elizabethan statute.

Fraud is, by definition, a form of wrongdoing that evolves rapidly and is committed by actors who design their behaviors with one eye on the constraints of the law. This was true in the 1600s—at the dawn of the Anglo-American legal system and the beginnings of modern markets. It has never been more true than today, after we have witnessed a

64789.028

decade marked by a number of massive and elaborate financial deceptions, some dizzying in complexity.

It is neither possible nor wise to attempt to define fraud in overly specific terms. Our legal system has long recognized this. As the Maryland Supreme Court observed in 1872,

> The common law not only gives no definition of fraud, but perhaps wisely asserts as a principle that there shall be no definition of it, for, as it is the very nature and essence of fraud to elude all laws in fact, without appearing to break them in form, a technical definition of fraud, making everything come within the scope of its words before the law could deal with it as such, would be in effect telling to the crafty precisely how to avoid the grasp of the law.

Current U.S. law is, without serious controversy, full of highly general prohibitions against fraud, nowhere more prominently than in our law of securities regulation—a pillar of which is Rule 10b-5's edict against any and all schemes to defraud in connection with the purchase or sale of a security.

There is thus, in my view, a somewhat unrealistic quality to what the Supreme Court said in the *Skilling* case. There is nothing novel, or unworkable, or imprudent about the idea of Congress passing general prohibitions on fraud and the courts working out how to apply those general concepts to new forms of harmful deception as they arise. This process alone presents no special problem of vagueness and due process. If it did, large swaths of American law would have to fall, and fraud would become largely immune to prosecution.

What, then, explains the particular controversy over the "honest services" statute? This brings me to the second point I would like to make today. What has distinguished this statute is its effort to target frauds that involve less tangible harm than simple and direct deprivations of money or property.

This legislative effort alone should not be especially controversial. As our society and economy have become more sophisticated and complex, it has become more and more apparent that information is critical and valuable, and that fiduciary and other trust relationships are both essential to the functioning of a highly specialized economy and subject to harmful abuse. The legal concept of fraud must be permitted to adapt, as it always has, with such changes in society.

The Court's somewhat arbitrary decision in *Skilling* that frauds inflicting less tangible or less measurable harms can only be prosecuted when they involve a bribe or kickback payment risks leaving important forms of abusive deception outside the scope of federal criminal law.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00044 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.029

Suppose that a senior officer of a company uses a loan program, approved in general terms by the board of directors, to spend lavishly and abusively on real estate, art, and luxury goods for him and his family. I am thinking here of the former Tyco chief Dennis Kozlowski.

Or suppose an executive uses a revolving line of credit, extended as a convenience by his company's board of directors, repeatedly and abusively as a means of unloading his holdings in the company's stock. I am thinking here of how former Enron Chairman Kenneth Lay disposed of nearly $100 million in stock as Enron's fortunes were declining, without his shareholders or board of directors knowing what he was doing.

Or suppose that the Chief Financial Officer of a large public company obtains general approval to head up a private investment partnership in order to engage in hedging transactions with the company—and then arranges those transactions to line his own pockets immensely, often with undisclosed and mischaracterized payments. I am thinking, of course, of former Enron CFO Andrew Fastow.

How are such serious cases to be prosecuted? One might say these are securities frauds because they involve public companies. But these are not traditional accounting fraud cases. They are cases of self-dealing, hidden conflicts of interest, and looting of corporations.

Some of the requirements of the law of securities fraud, such as its particular doctrine of materiality, could pose problems for prosecutors in such cases. The government's theories of harm in these cases are not always based on direct impact to the public company's share price. Rather the theories of prosecution are based on the deceptive deprivation from shareholders, directors, and other gatekeepers and stakeholders of the ability to police this kind of conduct and, if warranted, to exit from the relevant fiduciary relationship by firing the actor involved.

Perhaps more significantly, the law of securities fraud is limited to fraud in connection with the purchase or sale of a security. There is no reason why these forms of harmful and deceptive self-dealing and looting cannot arise, with equal seriousness, in institutions and relationships ranging from law firms to hospitals to accounting firms to major non-profit organizations.

I can see no good argument why the federal criminal law of fraud ought to be limited in its application to just that sophisticated and harmful self-dealing that happens to take place in the securities markets.

One might also argue that these kinds of cases can be reached through property theories under the mail and wire fraud statutes and are thus unaffected by the *Skilling* decision. But a prosecutor can often be confronted in such cases with defenses asserting that the general form of the conduct had been approved and that any property obtained by the defendant was within the bounds of such approval.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00045 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.030

The value of the intangible-rights theory of fraud has been that it gets at the essence of these frauds: the deceptive deprivation of important information that could allow a person to exit a trust relationship in which he or she is unknowingly suffering abuse.

In addition and as importantly, abusive self-dealing is not always engaged in directly for profit. A defendant's objective may be to enhance his own power and prestige, or his control over an institution or relationship in which others are depending importantly on him not to engage in abuse—and are counting on transparency to allow them to prevent and control such abuse if it occurs.

There is at least substantial doubt, in the wake of the *Skilling* decision, about whether prosecutors will be able to reach serious cases of this type using deprivation of property theories under the mail and wire fraud statutes. As in the wake of the *McNally* decision over two decades ago, prosecutors have new incentive to argue theories based on intangible forms of property. But such theories were subject to differing treatment in the courts during the period between the *McNally* decision and Congress's codification of "honest services" fraud.

I do not believe that the concept of fraud suddenly becomes unconstitutionally vague simply because it is applied to forms of deception that work less tangible forms of harm. The "honest services" statute became controversial not because of its conceptual structure but because of the occasional but worrisome exercise of prosecutorial discretion to apply the statute to marginal cases that most people would readily identify as not belonging in federal court.

The "vagueness" problem, if there was one, was not so much because the statute was not specific enough about what fraud means as because the law could be used, and was used, against people who could genuinely claim surprise that their minor wrongdoing subjected them to federal prosecution.

The natural outgrowth of such prosecutions was the kind of criticism the statute received at oral argument in the Supreme Court—with some justices, for example, speculating that an ordinary employee could land in federal prison for playing hooky from work. The concern about unconstitutional vagueness, I submit, was really a concern about overbreadth.

I thus want to conclude by suggesting some alternatives that Congress might examine as means of retaining a fraud prohibition flexible enough to deal with serious, novel forms of intangible harm but confined enough to allay fears about overbroad application in the hands of imprudent prosecutors.

First, it has long been a hallmark of criminal fraud prohibitions that they have demanding requirements with regard to mental state. Not only do such laws generally require proof beyond a reasonable doubt of the defendant's specific intent to defraud, but they have often been interpreted—especially in novel contexts—as requiring that the defendant act with consciousness of wrongdoing, that is, with awareness that his conduct is wrongful.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00046 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.031

One might draft a statute that applies only to "willful" violations and, contrary to Congress's usual practice, include within the statute an explicit definition of willfulness that embodies the requirement that violators must know that what they are doing is wrongful (though not necessarily illegal under any specific law). The Supreme Court itself has often observed that actors who are aware of the wrongfulness of their own conduct are not in a position to complain that they have been the victims of surprising application of allegedly vague laws.

Second, Congress might look more extensively at the question of what kinds of relationships tend to involve the serious instances of intangible harm that a federal criminal statute ought to reach. A new statute might be limited to important fiduciary and trust relationships and made inapplicable, for example, to ordinary employment and contractual relationships.

Third, Congress might consider possible thresholds for sorting serious cases of harm from less serious ones. There is no reason not to use statutes to draw clear lines when such lines can readily be drawn. One might choose, for example, to require that the relationship in which the intangible harm occurs be one involving a single transaction or a course of conduct in which the victim had at risk something of a value of at least $50,000.

I do not think this is a magic number, of course, and there are bound to be complications with calculating value. But size thresholds seem like one potential avenue for eliminating some of the trivial and ill-advised prosecutions that had begun to give the "honest services" statute a bad name.

Regardless of whether new legislation is pursued, or of what shape it might take, I urge this Committee and Congress to uphold the centuries-long commitment of our legislatures, courts, and other legal institutions to deal with the ever-challenging and evolving problem of fraud.

Thank you for the opportunity to address you this morning. I am happy to assist the Committee in any further way.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00047 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.032

Senate Judiciary Committee
Hearing on "Restoring Key Tools to Combat Fraud and Corruption After the Supreme Court's *Skilling* Decision"
Tuesday, September 28, 2010

Statement of U.S. Senator Russell D. Feingold

Tackling corruption by public officials and large corporations remains one of Congress's most important and most difficult tasks. Bribery, embezzlement, and kickbacks are all illegal and relatively easy to identify, but there are many other types of corruption that we all know are wrong that are more elusive. I am talking about deals where it is clear that government officials are using their power and influence to benefit themselves, or a spouse or a business partner, but there is no money that changes hands. This type of undisclosed self-dealing, particularly when it is done by public officials, undermines people's faith in their government and destroys the integrity of our democracy. When corporate executives engage in this sort of deceptive behavior, it can have a destabilizing effect on the market, which can ultimately lead to financial ruin for the employees and shareholders who are dependent on companies like Enron, Tyco, or Worldcom for their livelihoods and their retirement funds.

Congress has been struggling to get this area of the law right for decades, and in 1988 it created a new category of fraud called honest services fraud. This past June, the Supreme Court struck a devastating blow to this area of the law when it handed down a decision that involved the former CEO of Enron, Jeffrey Skilling. Skilling was accused of participating in a scheme to deceive investors about Enron's financial position, but the Court said the law was not specific enough for Skilling to have notice that this was criminal conduct. The Court said that honest services fraud can only apply to bribes and kickbacks, not self-dealing.

As a result of this case, it is now no longer enough to show that a mayor accepted lavish gifts, tickets to sporting events, and expensive meals from someone bidding on a development contract with the city. A prosecutor now must show a direct quid pro quo relationship between these meals and gifts and a decision to award a contract to that individual in order to prove bribery. This is often a very difficult element to prove, and as expected, this decision has had a chilling effect on the number of corruption prosecutions that have been filed in the last year. Over the last several months, we have also seen a wave of challenges to existing convictions and requests for reconsideration of sentences. We need to act quickly to close the large loophole that the Court created. This type of fraudulent behavior should not go unpunished merely because it is more devious, more sophisticated, or more complex than a simple bribe or kickback.

I have been working closely with Chairman Leahy and other members of the Committee on this issue, and I am pleased that we seem to be getting closer to reaching an agreement on an appropriate fix that addresses the concerns raised by the Court. I look forward to continuing this collaboration in the coming months so that we can restore the Department of Justice's ability to prosecute this type of fraudulent conduct.

64789.033

Statement of

The Honorable Patrick Leahy

United States Senator
Vermont
September 28, 2010

Statement Of Senator Patrick Leahy,
Chairman, Senate Judiciary Committee,
Hearing On "Restoring Key Tools To Combat Fraud And Corruption
After The Supreme Court's Skilling Decision"
September 28, 2010

Today, the Judiciary Committee considers another in a series of recent cases in which the Supreme Court appears to have undermined congressional efforts to protect hardworking Americans from powerful interests. In Skilling v. United States, the Court sided with an Enron executive who had been convicted of fraud, and gutted a statute vital to combating public corruption, corporate fraud and self-dealing.

We will explore today the kinds of problematic conduct that may now go unchecked in the wake of the Skilling decision and consider what Congress can and should do to fill those gaps and restore strong enforcement against corrupt and fraudulent conduct. I thank Assistant Attorney General Lanny Breuer for coming in to share the Justice Department's focus on this important issue, and I look forward to hearing from our panel of distinguished experts.

In recent years, the stain of corruption has spread to all levels of government. It is an issue that both parties must address. This is a problem that victimizes every American by chipping away at the foundations of our democracy and the faith that Americans have in their government.

Too often, loopholes in existing laws have meant that corrupt conduct can go unchecked. Senator Cornyn and I introduced the Public Corruption Prosecution Improvements Act last year to try to address some of these gaps. It was passed by this Committee, and the Senate should pass that important bill. The honest services fraud statute has in the past served to fill in some of the gaps in corruption laws, but now it too has been greatly limited. We must act aggressively but carefully to strengthen our laws to root out the kinds of public corruption that have resulted in convictions of high state officials, members of Congress, and many others.

Recent years have also seen a plague of financial and corporate frauds that have severely undermined our economy and hurt too many hardworking people in this country. These frauds have robbed people of their savings, their retirement accounts, college funds for their children, and have cost too many people their homes. Congress has acted, by passing the Fraud Enforcement and Recovery Act and other key provisions, to give prosecutors and investigators

64789.034

more tools to combat fraud. We must remain vigilant, as the methods and techniques used by those who would defraud hardworking Americans continue to change. The honest services fraud statute has allowed prosecutors the flexibility to keep up with corporate criminals.

For decades, courts and prosecutors agreed that the Federal mail and wire fraud laws could be used to prosecute individuals for "deprivation of honest services." That included cases in which public officials acted to benefit their own hidden financial interests, rather than the interests of the people they were supposed to be serving, and cases in which corporate executives secretly enriched themselves at the expense of their companies.

In 1987, the Supreme Court, over Justice Stevens' dissent, overturned those decades of case law, holding that the mail and wire fraud statutes only outlawed fraud aimed at stealing money or property. Congress responded quickly, explicitly adding in 1989 a provision for prosecuting deprivations of honest services under the mail and wire fraud statute. In the 21 years following that congressional action, every circuit court upheld the honest services fraud statute, and no court had limited it in the sweeping way the Supreme Court chose to in the Skilling decision.

The honest services statute was used to prosecute lobbyist Jack Abramoff, Congressman Bob Ney, many corrupt state and local officials, and corporate wrongdoers like Enron executive Jeff Skilling and multi-millionaire Canadian publisher Conrad Black, whose conviction for blatant self-dealing was called into question by the Supreme Court's ruling in the Skilling case.

The Court in Skilling ruled that the honest services fraud statute may be used to prosecute only bribery and kickbacks, but no other conduct. Of course, a number of statutory tools are already available to go after bribery and kickbacks, so the honest services fraud statute was always more important in other contexts.

Honest services fraud allowed prosecutors to go after public officials who hid their own financial interests and then acted to benefit those interests or who took a string of gifts intending to act in the interest of a benefactor in the future and then did so when the time was right. It allowed prosecutors to go after corporate executives who acted to benefit themselves financially at the expense of the shareholders and employees of their company. Now these cases are at risk. I look forward to hearing from Assistant Attorney General Breuer about the impact on prosecutions has been, but I am confident that important cases have been undermined.

I understand the concerns in many circles about vague or undefined Federal laws which could leave some public officials or executives uncertain about what kind of conduct could leave them susceptible to criminal charges. But that is no reason for us to let corrupt or fraudulent conduct go unchecked. Rather, we need to identify the gaps in current law after the Skilling case and act promptly with precise, careful legislation that fills those gaps in clear terms.

We should be clear about what conduct is unacceptable, but surely we can agree that undisclosed self-dealing by public officials and corporate executives is clearly unacceptable. I look forward to learning more today about exactly what the gaps are that need to be filled and how best to fill them, and I plan to introduce legislation shortly to take on this important issue.

64789.035

I thank the Senators of both parties who have been working with me to find the best way to appropriately restore our fraud and corruption laws, and I will continue working with them to make sure we get it right. Today's hearing will help us get there.

# # # # #

64789.036

ABBE DAVID LOWELL
11315 S. GLEN ROAD
POTOMAC, MD 20854

October 5, 2010

VIA EMAIL

The Honorable Patrick J. Leahy
Chairman
Committee on the Judiciary
SD-224 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Jefferson Beauregard Sessions III
Ranking Minority Member
Committee on the Judiciary
SD-224 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Chairman Leahy and Ranking Member Sessions:

I appreciate the opportunity to address the issue of honest services fraud and the legislation you are contemplating.

As I think you know, my perspective on this subject is based on my 30 years of practice (5 in the Department of Justice and 25 as a defense attorney). Included in that experience are trials in which honest services counts were included[1], appeals in which honest services charged were involved, my writing the *amicus curiae* brief for the National Association of Criminal Defense Lawyers in one of the honest service cases just decided by the Supreme Court, my teaching honest services law as part of my law courses at Columbia Law School and Georgetown Law Schools, and my chairing various continuing legal education programs for practicing attorneys in which honest services law was a topic. I also have spent a considerable amount of time practicing and teaching in the area of public corruption and similar offenses – serving as Special Counsel to the House Committee on Standards of Official Conduct, serving as Chief Minority Counsel to the House during the Impeachment of President Clinton, and representing numerous public officials accused on wrongdoing.

---

[1] For example, I am counsel in *United States* v. *Bruno*, Case No. 09-cr-29 (N.D.N.Y.) a case in which honest services counts are being challenged as inconsistent with the Supreme Court's decision in *Skilling*.

64789.037

To begin with, let me state my view that public corruption and private conflicts of interest are serious offenses that should be addressed as a priority of federal, state and local law enforcement agencies. One aspect of such offenses is that they erode the foundation of so many other government and non-government functions and therefore have a ripple effect beyond the offense itself. When a public official is found guilty of corruption it also adds to the public's already strong view that government is aimed at personal, rather than public, good. Such offenses add immeasurably to the cynicism we see when Americans talk about their government.

Despite the need to address all areas of public corruption seriously, I am writing to suggest that Congress go slowly in addressing the Supreme Court's decision because the problem may not be as great as some claim.

At the end of June 2010, the Supreme Court decided *Skilling v. United States* and two related honest service cases. Right away, many claimed that "Congress needed to do something to fix the problem or reverse the Court." In his testimony before the Committee, Assistant Attorney General Lanny Breuer echoed this line and said the Supreme Court had "created a gap" in the ability to prosecute these offenses and asked Congress to "fill the void."

A. There Is No "Void"

I want to start off by questioning whether there is any void to be filled and certainly whether there is enough data or experience for Congress to act. In this letter, I will address the use of honest services charges against federal officials and then state and local officials and finally private business people. Let me address each separately.

1. Federal Officials

On the federal level, there are currently powerful and effective laws—all of which have been tested for constitutionality—that already address: bribery (18 U.S.C. § 201), gratuities (18 U.S.C. § 201), extortion (18 U.S.C. §§ 872 & 1951), kickbacks (18 U.S.C. §§ 201, 41 U.S.C. §51-58), and conflicts of interest[2] (18 U.S.C. §§ 203-09). Equally important, almost all federal officials file some type of ethics/financial disclosure forms so that an official's purposeful failure to disclose or his or her lying about his or her interests can also be prosecuted as a false statement (18 U.S.C. §1001). This is not to mention that when a public official gets involved with people for the purposes of committing some financial wrongdoing, the general mail and wire fraud statutes addressing economic crimes (18 U.S.C. §§ 1341, 1343) also can be employed.

[2] Indeed, in his testimony, Assistant Attorney General Breuer mentioned that a new honest services statute could be based on the current conflict of interest provisions, which underscores that there already exists an effective tool for law enforcement.

64789.038

2. State/Local Officials

On the state and local levels, first and foremost, our society needs to rely on the law enforcement activities of state and local investigators and prosecutors. Every state has those same types of laws making serious crimes of bribery, extortion, kickbacks, etc. Each state has also decided what types of conflicts of interest should be treated criminally and what penalties ought to be applied to such conduct. It is a potential serious issue of states' rights and excessive federalism (and even a potential touch of paternalism) for the federal government to impose its decisions on how certain state and local public official conduct should be addressed when a state or locality has addressed that issue and has the tools to enforce it laws.

If a state or locality does not have such laws or rules or shirks its responsibility or otherwise is ill-equipped to address public corruption on the state or local level, then it is, of course, completely appropriate for the federal government to use its resources to "fill that gap." However, here too, there are sufficient tools in the box already. When a state or local official involves him or herself with illegal financial or economic gain, the ordinary federal mail or wire fraud statutes apply with no problem. If there is fraud or bribery or similar wrongdoing in a state or local program in which there is a federal interest of more than $10,000, the federal law enforcement agencies have a powerful and effective weapon in 18 U.S.C. § 666. Indeed, where there is not such a federal interest, then the federal government ought to be careful in not using its already-stretched resources to reach down to conduct without the impact on federal interests to justify that effort. A state public official can be prosecuted for his or her role in a scheme with private individuals as a co-conspirator (18 U.S.C. § 371) or as aiding and abetting the conduct of these others (18 U.S.C. § 2). If an official's acts are repeated, he or she is subject to the RICO laws (18 U.S.C. §§ 1961-68). Federal prosecutors have been charging state and local officials under the Travel Act (18 U.S.C. § 1952) as well when there is an interstate aspect to the alleged scheme. All of the existing statutes have serious penalties, including many years of incarceration and the possibility of forfeiture of ill-gotten gains. And, we should not forget that the Supreme Court in its recent honest services decisions actually endorsed the current honest service laws' application to state and local officials who commit bribery or kickbacks (very broad categories given the elements of those offenses and how an official's conduct often can be described as one or the other).

So, to make this very clear, then, the honest service statute reach beyond bribery and kickback cases was needed, if at all, only in a very limited circumstance: some form of conflict of interest that is not disclosed properly and that is then not addressed by another count addressing other conduct in a scheme and/or not addressed by state and local authorities under state or local law. This is not a large "gap" or "void" that requires immediate action or concern.

3. Private Business People

With respect to the application of the honest services statute to private individuals in the business setting, there is even less need for any new law. It is almost always the case that, when

a private individual is creating a conflict of interest in a business setting, there will be economic gain or loss involved. Then, the normal wire and mail fraud statutes (as well as other economic-based crimes) apply. In addition, if there is a more subtle non-disclosure, odds are that it will implicate the securities laws (18 U.S.C. § 1348), the banking disclosure laws (18 U.S.C. § 1014), or the tax laws (e.g., 26 U.S.C. § 7206).

In fact, given the heightened state of mind requirement in all fraud cases, prosecutors are apt not to want to use honest services if another of the non-disclosure-based laws can be used. Again, there are few times when there are not economic impacts of a businessperson's wrongdoing that will not give rise to a non-honest services theory of prosecution.

B. So, Why Was Honest Services Used So Frequently?

My review of the lack of any real void above gives rise to a simple question: why was the honest services fraud statute used with such frequency? The answer has been stated by many others—judges, academics, commentators and the Supreme Court. The way the application of the honest services law crept and oozed, it just became an easy catch-all for prosecutors to use instead of relying on more traditional prosecutorial theories. And, because its terms were so obviously vague—what is an honest service? to whom is it owed? where does the obligation for it arise—it was easier for prosecutors to get convictions based on applying such an elastic phrase. But, "easier" is not better, and it certainly is not fairer or more constitutional. Indeed, it was the law's ever-increasing elasticity that caused even staunch conservatives and a conservative Supreme Court to criticize it and rule it unconstitutional.

My father used to say he did not like marzipan, the sweet paste used in food decorations. When asked why, he would say that he was very suspicious of something that could be made to look like a colorful bowl of fruit one day and a gray battleship on a cake the next. That is the problem with the old use of the honest services law and something that must be avoided in the future. One day it was a substitute for a straight-forward bribery scheme; the next day it was used to address a businessman's failure to properly disclose to shareholders; the next it was used against a clergyman for his improper relationships with his parishioners. Any criminal law that can be bent and twisted in so many shapes has obvious attraction to prosecutors, but is something that can cause all the harms to due process that the Supreme Court identified.

The serious offenses of public and private wrongdoing that have been addressed through the vague parts of the honest services statutes can be addressed with the better defined laws now available.

C. Proposals To "Fix" The Problem And "Fill The Gap"

Given that phrases like "honest services" are so vague and cause the harms detailed by the Supreme Court, the issue is whether there can be any better substitute, any words that are

better. Again, there is no proven need to fix a problem that does not yet exist, but if there, was what could be done?

Mr. Chairman, you have started the process with a first draft that does not try to do too much. It seeks to address only the narrowest area of undisclosed conflicts of interest that the Supreme Court said could not be included in the current statute. However, because this area is very much like trying to squeeze jello in your hands, that is a goal more easily stated than able to be done.

For example, the core of the proposal you have put forward is to prohibit "undisclosed self-dealing." "Undisclosed self-dealing" is then defined to be when a "public official performs an official act for the purpose, "in whole or part, of benefitting . . . a financial interest." Mr. Chairman, one can only imagine the litigation that will ensue over the phrase "in whole or part." The issues of how to divine a person's intent is always difficult in criminal case. This will be even harder. And, even then, what is the scale—what if a person is motivated by having a minimal desire (1%) to seek a personal benefit and 99% for a more general good. Is that enough to bring a case? Is it enough to get a conviction? Should it be? Prosecutors will have no incentive to limit the statutes application and—as with the original section 1346—this new honest services statute will push and likely surpass constitutional boundaries.

As to disclosure, the draft bill prohibits a public official who "knowingly falsifies, conceals or covers up material information that is required to be disclosed regarding that financial interest by any Federal, State, or local statute, rule, regulation or charter . . . " Again, there will be a great debate and a lot of litigation over the phrase "covers up" as to what it adds to the other terms in your proposal. And, as to the notion that information is concealed if it is "required" to be disclosed by other rules, that does not solve the problem. In the case concerning former New York State Senator Joseph Bruno, for example, the charge was that he did not disclose the names of the clients who hired his consulting firm (he listed the name of the consulting firm and the amount he made from that entity). State ethics rules required him to file a disclosure form and list the "source" of his income, which was interpreted by all public officials as their employer—whether it be a law firm, a consulting firm, or a small business—not their clients. Indeed, the state disclosure form that Mr. Bruno and others in New York had to fill out specifically stated that legislators should *not* list clients. For more than a dozen years, New York State never once sanctioned a state legislator for interpreting the form in this manner. Yet, the federal prosecutors built their entire case under the notion that Mr. Bruno should have listed the names of his clients. The anomaly that a state official's conduct could be perfectly correct under state law, and in accordance with the conduct of all other state officials, and yet be made into a federal felony by a law that empowered prosecutors with the discretion to create federal common law that trumped state law and practice was extremely troubling in Mr. Bruno's case. This anomaly could persist under the draft you have proposed.

In the *Skilling* decision, Justice Ginsburg wrote an important footnote concerning the possibility of a new law that might be proposed for the honest services area. This is what she said:

> If Congress were to take up the enterprise of criminalizing "undisclosed self-dealing by a public official or private employee," Brief for United States 43, it would have to employ standards of sufficient definiteness and specificity to overcome due process concerns. The Government proposes a standard that prohibits the "taking of official action by the employee that furthers his own undisclosed financial interests while purporting to act in the interests of those to whom he owes a fiduciary duty," so long as the employee acts with a specific intent to deceive and the undisclosed conduct could influence the victim to change its behavior. *Id.*, at 43–44. See also *id.*, at 40–41. That formulation, however, leaves many questions unanswered. How direct or significant does the conflicting financial interest have to be? To what extent does the official action have to further that interest in order to amount to fraud? To whom should the disclosure be made and what information should it convey? These questions and others call for particular care in attempting to formulate an adequate criminal prohibition in this context.

Skilling, Slip. Op. at 47, n.44. I know Congress will not want to take any action that only re-creates the very problem the Supreme Court found existed in the current law.

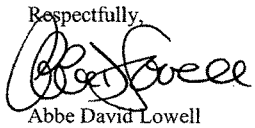
It is very difficult to craft something that fills the alleged "gap" when the substance used for filler is so elusive to define and malleable in the hands of those applying the law. This is why Congress should wait to be absolutely sure there is a "void" or a "gap" before creating another constitutional problem equal to the one the Court finally resolved. In addition, only by seeing what cases are being brought with the other tools and what, if any, conduct is not being charged can Congress see what is needed and how to tailor such a proposal to the real problem.

There have been many occasions where a Supreme Court decision results in an immediate cry for a legislative solution. The 2005 sentencing decisions in *United States v. Booker* and *United States v. Fanfan* come to mind. But only when Congress waits and is more deliberate can it truly determine whether a problem exists and whether a solution is needed. For now, however, honest services remains a solution in search of a problem.

The Honorable Patrick J. Leahy
The Honorable Jefferson Beauregard Sessions III
Page 7
October 5, 2010

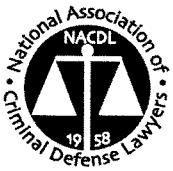
I appreciate the opportunity to add my views to the preliminary discussions you and the others on the Committee and in the legal community are having. I stand by to add to these views whenever and however may be useful to you.

Respectfully,



Abbe David Lowell

64789.043



Written Statement of
Timothy P. O'Toole

on behalf of the
National Association of Criminal Defense Lawyers

Before the
Senate Committee on the Judiciary
Subcommittee on Crime, Terrorism, and Homeland Security

Re: "Restoring Key Tools To Combat Fraud and Corruption After the Supreme Court's Skilling Decision"

September 28, 2010

64789.044

TIMOTHY P. O'TOOLE, ESQ. defends individuals and companies in white collar criminal prosecutions, conducts internal investigations, and handles complex litigation arising under the Employee Retirement Income Security Act (ERISA) as a partner at Miller & Chevalier in Washington, D.C. In the fall of 2009, Mr. O'Toole served as co-counsel in the only trial to date of a lobbyist arising out of the Abramoff scandal, litigating a number of cutting-edge issues related to the honest services fraud and gratuities laws. In addition, Mr. O'Toole has a wealth of experience handling criminal and civil appeals, having presented more than 25 appellate arguments in the state and federal courts, and represented multiple parties and amici curiae before the United States Supreme Court. Mr. O'Toole has published and lectured nationwide on a variety of topics. Prior to joining Miller & Chevalier, Mr. O'Toole served as the Chief of the Special Litigation Division of the Public Defender Service for the District of Columbia, where he supervised and handled complex cases in the local and federal courts. He is also a former Assistant Federal Public Defender in Las Vegas, Nevada, where he represented people under sentence of death in federal proceedings.

* * * * *

The National Association of Criminal Defense Lawyers (NACDL) is the preeminent organization in the United States advancing the mission of the nation's criminal defense lawyers to ensure justice and due process for persons accused of crime or other misconduct. A professional bar association founded in 1958, NACDL's more than 10,000 direct members — and 80 state and local affiliate organizations with another 28,000 members — include private criminal defense lawyers, public defenders, active-duty U.S. military defense counsel, law professors and judges committed to preserving fairness within America's criminal justice system.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00060 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.045

My name is Timothy P. O'Toole, and I am writing on behalf of the National Association of Criminal Defense Lawyers (NACDL), an organization of over 10,000 members. NACDL is the preeminent organization in the United States advancing the goal of the criminal defense bar to ensure justice and due process for persons charged with a crime or wrongdoing. I am a practicing criminal defense attorney in Washington, DC, specializing in white collar crime. I sit on NACDL's Board of Directors and am a member of NACDL's White Collar Crime Committee.

Since its adoption in 1988, the honest services fraud statute (18 U.S.C. § 1346) has been widely criticized as vague and overbroad. The statute's failure to define the phrase "intangible right of honest services" allowed it to be stretched to cover conduct that no reasonable legislator would have deemed criminal. This vagueness, in turn, permitted the government to treat the "honest services fraud" law as the ultimate in flexible prosecutorial weapons—a statute whose application, especially in high-profile cases, seemed limited only by the prosecutor's imagination.

The Supreme Court's recent decision in *Skilling v. United States*[1] validated these criticisms, with all nine members of the Court expressing concern about the expansive nature in which this facially vague statute had been applied. While three members of the Court would have addressed these concerns by striking the statute in its entirety on vagueness grounds,[2] the Court's majority chose instead to construe the statute as criminalizing "*only* the bribe-and-kickback core of the pre-*McNally* case law."[3] A narrowed version of the offense thus survives, but Congress should not lose sight of the fact that the statute's vagueness was uniformly condemned by a unanimous Supreme Court, representing views across the ideological spectrum.

The Supreme Court did not simply narrow the current statute, however. It also expressly warned Congress about the difficulty in amending the statute to revive the sorts of amorphous "undisclosed conflict of interest" theories that were pursued prior to *Skilling*. As the Court held, the very flexibility of the honest-services statute—touted by some as its primary virtue—was in fact its fatal flaw. In particular, the Supreme Court expressly recognized in footnote 45 of its decision that attempts to revive a federal criminal prohibition on "undisclosed conflicts of interest" would face a host of practical and constitutional problems. Given the Supreme Court's teachings on this subject, Congress should be extremely cautious of any legislative "fix" and *especially* wary of any *quick* legislative "fix" that attempts to retain the "flexibility" that prosecutors enjoyed when they had an unlimited honest services statute in their toolbox.

The difficulty of the endeavor is one sound reason for treading lightly in this area; the lack of any exigency is another. Simply put, there are already many overlapping federal criminal laws that reach "corrupt" conduct by public officials and no one has identified any legitimate gap in this area. Indeed, even without mentioning the honest services fraud law, the Supreme Court

[1] *Skilling v. United States*, ___ U.S. ___; 2010 U.S. LEXIS 5259; 2010 WL 2518587 (June 24, 2010).
[2] *Id.*, 2010 U.S. LEXIS 5259 at *108-128.
[3] *Id. at* *97-98 (emphasis in original).

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00061 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.046

has already observed that potentially corrupt behavior of public officials is governed by an "intricate web of regulations, both administrative and criminal."[4] These federal criminal laws include not only the anti-bribery statutes, but also the mail fraud and racketeering statutes, the Hobbs Act, the Travel Act, and the Anti-Kickback laws. Congress has also passed laws specifically prohibiting public officials' acceptance of gifts.[5] In addition, Congress passed the Honest Leadership and Open Government Act of 2007 ("HLOGA"), which contains a criminal prohibition expressly prohibiting private citizen lobbyists from making gifts or providing travel to government officials if the person has knowledge that the gift or travel may not be accepted by the official under the Rules of the House of Representatives or the Standing Rules of the Senate.[6] Any new honest services statute would be duplicative of these already-existing prohibitions, which already carry extensive penalties.

A new honest services statute is likewise unnecessary in the state and local context. Many have argued that the primary purpose of the honest services law is to allow federal prosecutors to prosecute corruption that would otherwise be ignored by conflicted and politically weak state and local officials.[7] But there is simply no merit to this idea. First, state and local jurisdictions often have their own extensive anti-corruption laws.[8] Second, using the federal honest services law to essentially displace this extensive state and local regulatory framework creates potential federalism concerns, as courts have noted, since it essentially allows the federal government to override the laws that state and local governments adopted to address the misconduct of their own officials.[9]

Third, and most importantly, even if one were to accept the need for federal officials to police state and local corruption, federal prosecutors have plenty of other tools at their disposal. For example, *Skilling* makes clear that the honest services fraud statute may still be applied to state and local officials who participate in fraudulent schemes that were clearly illegal prior to the adoption of the statute and meet the elements of the federal bribery and kickback statutes.[10] Likewise, many other federal criminal laws—most importantly, the Hobbs Act and the Travel Act—apply to corruption offenses involving state and local officials. And Congress passed at

---

[4] *United States v. Sun-Diamond Growers*, 526 U.S. 398, 409 (1999).
[5] 5 U.S.C. § 7353, discussed *infra*.
[6] 2 U.S.C. § 1613 (2009). That provision expressly prohibits private citizen lobbyists from "mak[ing] a gift or provid[ing] travel to a covered legislative branch official if the person has knowledge that the gift or travel may not by accepted by that covered legislative branch official under the Rules of the House of Representatives or the Standing Rules of the Senate (as the case may be)." *Id.* The HLOGA also added a provision requiring lobbyists to certify on a semi-annual basis that they are familiar with the House and Senate Rules on gifts and travel, and have not provided or offered such gifts or travel in violation of those rules. HLOGA, § 203(a), 2 U.S.C. § 1604(d)(1)(G) (2009).
[7] *See, e.g.*, Brief for Respondent at 50-51, *Weyhrauch v. United States*, No. 08-1196 (U.S. Oct. 2009); Joshua A. Kobrin, *Betraying Honest Services: Theories of Trust and Betrayal Applied to the Mail Fraud Statute and § 1346*, 61 N.Y.U. ANN. SURV. AM. L. 779, 809-811 (2006).
[8] *See, e.g.*, N.Y. Penal Law (McKinney) § 200 et seq. (1999); Title 13A: Alabama Criminal Code § 13A-10-60 et seq.; CAL. PENAL CODE § 67 et seq. (2009); § 85 et seq. (2009); 720 ILL. COMP. STAT. 5/33-1 et seq. (2010); TEX. PENAL CODE § 36.01 et seq. (2010).
[9] *See, e.g.*, *Brumley v. United States*, 116 F.3d 728, 735 (5th Cir. 1997) (en banc).
[10] *Skilling*, __ U.S. at __, 2010 U.S. 5259 at *104 n.46.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00062 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.047

least one other law governing state and local corruption—18 U.S.C. § 666—that prohibits bribery involving state and local officials employed by agencies receiving more than $10,000 in federal program grants. That law has also been broadly applied by the Supreme Court.[11]

As this non-exhaustive list shows, a host of criminal statutes already address the conduct the honest services law attempted to prohibit.

List of Relevant Charging Statutes and Maximum Sentences

- **Title 18, Chapter 11 - Bribery Offenses**
  - 18 U.S.C. § 201 - Bribery of public officials and witnesses (15 years)
  - 18 U.S.C. § 201(c) - Anti-gratuities statute (2 years)
  - 18 U.S.C. § 205 - Activities of officers and employees in claims against and other matters affecting the Government (1 year or 5 years for willful violation)
  - 18 U.S.C. § 207 - Restrictions on former officers, employees, and elected officials of the executive and legislative branches (1 year or 5 years for willful violation)
  - 18 U.S.C. § 208 - Acts affecting a personal financial interest (1 year or 5 years for willful violation)
  - 18 U.S.C. § 209 - Salary of Government officials and employees payable only by United States (1 year or 5 years for willful violation)
  - 18 U.S.C. § 217 - Acceptance of consideration for adjustment of farm indebtedness (1 year)

- **Title 18, Chapter 31 - Embezzlement and Theft Offenses**
  - 18 U.S.C § 666 - Theft or bribery concerning programs receiving Federal funds (10 years)

- **Title 18, Chapter 63 - Mail Fraud Offenses**
  - 18 U.S.C. § 1341 - Mail Fraud (20 years)
  - 18 U.S.C. § 1343 - Wire Fraud (20 years)
  - 18 U.S.C. § 1347 - Health Care Fraud (20 years)
  - 18 U.S.C. § 1348 - Securities Fraud (25 years)
  - 18 U.S.C. § 1351 - Fraud in foreign labor contracting (5 years)

- **Title 18, Chapter 95 - Racketeering Offenses**
  - 18 U.S.C § 1951 - Interference with commerce by threats or violence ("The Hobbs Act") (20 years)
  - 18 U.S.C § 1952 - Interstate and foreign travel or transportation in aid of racketeering enterprises ("The Travel Act") (5 years, 20 years or life, depending on applicable subsection)

[11] *Sabri v. United States*, 541 U.S. 600, 606 (2004).

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00063 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.048

- **Title 41 - "The Anti-Kickback Act of 1986"**
  - 41 U.S.C. § 53
  - 41 U.S.C. § 54 (10 years)

- **Title 26, Chapter 75 - Crimes, Other Offenses and Forfeitures (Internal Revenue Code)**
  - 26 U.S.C. § 7214(a)(9) - Offenses by officers and employees of the United States (5 years)

- **Title 2, Chapter 26 - Disclosure of Lobbying Activities**
  - 2 U.S.C. § 1606(b) - Penalties (5 years)
  - 2 U.S.C. § 1613 - Prohibition on provision of gifts or travel by registered lobbyists to Members of Congress and to congressional employees

- **Title 15, Chapter 2B - Securities Exchanges**
  - 15 U.S.C. §§ 78dd-1, *et seq.* - "The Foreign Corrupt Practices Act"

- **Relevant Administrative Provisions**
  - **Title 5, Chapter 73 - Suitability, Security and Conduct**
    - 5 U.S.C. § 7353 - Gifts to federal employees (prohibiting federal employees from soliciting anything of value from individuals whose interests may be substantially affected by the performance or non-performance of the individual's official duties)
  - **Rule XXXV** of the Standing Rules of the Senate[12]
  - **Rule XXVI** of the Rules of the House of Representatives[13]

As this list illustrates, there are currently more than enough federal statutes on the books to deal with corruption by federal and state officials. The Supreme Court's limitation on one of these tools—the honest services fraud law—cannot justify fashioning a replacement statute, particularly without a methodical attempt to both address all of the concerns identified by the Supreme Court in *Skilling*, as well as a reasoned effort to see if any replacement statute is needed in the first place. Attempting to revive any aspect of the invalidated portion of the statute is complicated and a hasty attempt to "fix" a perceived gap will almost certainly revive the vagueness concerns that caused the Supreme Court to invalidate the statute. It is difficult to believe that existing federal, state and local criminal laws do not already reach all conduct that is properly criminal. If conduct is still beyond reach, that is likely because the conduct itself is properly beyond the reach of the criminal laws.

[12] This Rule prohibits senators or their employees—except under defined circumstances—from knowingly accepting a gift from a registered lobbyist or a private entity that retains or employs a registered lobbyist.
[13] This Rule covers financial disclosure requirements for Members of Congress.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00064 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.049

Thank you for this opportunity to express NACDL's views. We urge the Committee to thoughtfully consider the wide array of existing federal and state criminal and civil laws that already proscribe misconduct in this arena before it acts further.

Respectfully,

Timothy P. O'Toole
Miller & Chevalier
655 Fifteenth Street N.W.
Suite 900
Washington, DC 20005
Phone: 202-626-5552
Fax: 202-626-5801
Email: totoole@milchev.com

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00065 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.050

UF | UNIVERSITY of FLORIDA

Fredric G. Levin College of Law
Office of the Faculty

College of Law
PO Box 117625
Gainesville, FL 32611-7625
352-273-0914
352-392-3005 Fax

ORAL STATEMENT before the United States Senate
Committee on the Judiciary
Michael L. Seigel, University of Florida Research Foundation Professor of Law
Fredric G. Levin College of Law
September 28, 2010

"Restoring Key Tools to Combat Fraud and Corruption
After the Supreme Court's *Skilling* Decision"

Mr. Chairman and Distinguished Members of the Committee:

Thank you for providing me with the opportunity to testify here today. I am going to limit my remarks to issues surrounding the impact of *Skilling v. United States*[1] on the prosecution of public-sector honest services fraud.

Few experts would take issue with the Supreme Court's conclusion in *Skilling* that the concept of honest services found in 18 U.S.C. § 1346 was unconstitutionally vague. As the Court held, the term was so general that (1) it did not provide citizens with fair notice of potential criminal conduct; (2) it allowed for abuse of prosecutorial discretion, both through vindictive prosecution and the waste of precious law enforcement resources on trivial cases; and (3) it risked intrusion on the right of States to regulate their own political affairs.

However, the solution that the Court devised -- limiting the application of the statute to cases involving bribery and kickbacks -- is far from ideal. In fact, the newly-narrowed statute suffers from the very same ills as before. One example will suffice to prove this point. Even after *Skilling*, federal prosecutors could charge a State Department of Motor Vehicles employee with honest services fraud for taking a $20 bribe to allow a driver's license applicant to cut in line. I think we'd all agree that making a federal case out of such minor conduct would be an improvident use of DOJ resources in an area in which state officials are surely equipped to handle the infraction themselves.

At the same time, the *Skilling* limitation has made the scope of honest services fraud considerably too narrow, causing serious malfeasance meriting the attention of federal law enforcement to be beyond its reach. The case's most glaring flaw is its failure to define bribery and kickbacks. Lacking direct guidance, lower courts are likely to import the definition of these terms from the federal bribery statute, 18 U.S.C. § 201. According to the Supreme Court's

[1] 130 S. Ct. 2896 (2010).

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00066 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.017

decision in *Sun Diamond Growers*,[2] conviction under § 201 for an illegal bribe or gratuity (which is included within the definition of a kickback pursuant to 41 U.S.C. § 52(2)) requires proof of a *quid pro quo* -- in other words, proof that the bribe or gratuity was paid in connection with a specific official act.[3] Sometimes, despite obviously corrupt behavior, this element is impossible to prove beyond a reasonable doubt. For example, a state legislator might secretly be on the payroll of a corporation that has an interest in a wide variety of matters that are the constant subject of legislation. The employer and employee use all kinds of deception to conceal the illicit income, which adds up to more than a half million dollars over the course of several years. Although the legislator is a routine champion of causes that benefit the company, there is no evidence of a direct link between any particular official act and his undisclosed conflict of interest. Under the post-*Skilling* status quo, this arrangement, so obviously antithetical to a healthy political environment, lacks a federal criminal remedy.

Unless Congress acts, two other categories of public sector honest services fraud will likewise go unaddressed. The first is composed of cases involving a public employee or official who receives a non-monetary benefit as a result of an undisclosed conflict of interest. Cases falling into this category would include a prosecutor whose purposeful failure to reveal his ties to the victim in a murder investigation led to an overturned conviction requiring retrial at taxpayer's expense; or a legislator who secretly directed an appropriation to his alma mater by disguising the recipient's identity through deceptive language buried deep within the legislation; or a judge who failed to disclose that he was negotiating for a future job (that perhaps never came to fruition) with a party to a major case before the court. Unfortunately, these scenarios are derived from real life.

The last type of undesirable conduct that is now beyond the reach of the mail and wire fraud statutes is a public employee's use of outright deception to obtain something other than money or property. Consider, for example, a disturbed employee of the Department of Homeland Security who exaggerates a threat for the sheer evil pleasure of causing a public panic. Or a civil servant who has repeatedly falsified test scores to secure the promotion of one racial or ethnic group over another. Perhaps these actions violate other federal laws, but honest services fraud -- properly construed -- would be a useful and straightforward means of punishing and deterring such antisocial conduct.

Congress should address these shortcomings of the holding in the *Skilling* case. In should rewrite the honest services statute to make clear that, at the very least, cases relying on illegal gratuities do not require proof of a *quid pro quo*, and situations involving undisclosed conflicts of interest or outright deception by public officials that result in a non-monetary benefit are within its scope.

At the same time, to avoid future vagueness problems and respect the sovereignty of the States, Congress should use this opportunity to limit honest services fraud to carefully

---

[2] United States v. Sun Diamond Growers of Cal., 526 U.S. 398 (1999).

[3] 18 U.S.C. § 201 and 41 U.S.C. § 52 were both used by the Court in Skilling as points of reference. 130 S. Ct. at 2933-34.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00067 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.018

circumscribed and well-defined conduct that is of true federal significance. The new legislation should (1) define each of its terms with precision; (2) require that, to be cognizable, the conduct of the public official must violate a state or federal law, rule, or regulation; (3) impose a minimum, though flexibly measured, level of intended or caused benefit or harm; and (4) spell out in clear terms high levels of specific intent -- for example, intent to defraud and knowing conduct -- that the prosecution must prove before the statute is breached.

Properly redrafted, the mail and wire fraud statutes can continue to serve a very important role in the constant battle against serious and corrosive public corruption.

Thank you.

64789.019

STATEMENT OF

GEORGE J. TERWILLIGER III

Before

COMMITTEE ON THE JUDICIARY

UNITED STATES SENATE

WASHINGTON, D.C.
September 28, 2010

64789.020

Mr. Chairman and Ranking Member Sessions:

Public corruption investigations and prosecutions continue to deserve to be among the highest priorities of federal prosecutors. Public corruption is an insidious wrong that engenders in our citizens disrespect for the rule of law and cynicism about the rectitude of public institutions. When the legislative process is corrupted by personal financial gain or the deliberative process is warped by corrupt practices, fundamental guarantees made to the people by law are thwarted and the democratic process itself is undermined.

To briefly relate aspects of my experience that inform my testimony today, during the time that I was privileged to serve as Deputy Attorney General of the United States, I was called upon to make final judgments concerning recommended prosecutions of several members of this body and other public officials. In private practice, I have been counsel to members of this body and of the other house, as well as for appointed officials in the executive branch and high ranking state officials. I have seen first-hand the horrible toll that investigations and accusations can exact on an individual. I am thus especially grateful to have the opportunity you have afforded me today to participate in the committee's consideration of anti-corruption legislation.

I agree with the committee's apparent goal of providing federal prosecutors with the tools they need to address corruption not just in the federal government, but at the state and local level as well. In terms of the specifics of the proposal, and as elaborated further below, I think great care needs to be taken, as is always the case, in defining federal crimes, especially when it comes to defining crimes by state and local officials

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00070 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.021

where there are federalism and jurisdictional concerns. In addition, undisclosed self-dealing by federal officials may better be addressed by amendments to chapter 11 of the criminal code which deals with bribery and conflicts of interest involving federal officials. Because of the complex jurisdictional and other issues dealing with state and local officials, and the added complexity of incorporating vastly differing state and local disclosure obligations into a broad federal prohibition, as the current proposal envisions, I would urge further analysis and consideration of the appropriate scope of that aspect of the proposal and due consideration of how the substantive offense could best be defined, including whether amending the mail and wire fraud statute is the best way to achieve it.

Part of the potential legislation under discussion addresses undisclosed financial interests outside the government setting, suggesting a new federal offense for certain undisclosed private self-dealing. That appears to me to present a daunting challenge to define the enforcement objective and to draft clear terms to achieve it. There has been considerable new legislation recently in this area, suggesting also the need to determine how any new prohibitions would interact with those already on the books. For these reasons and because the legislation would necessarily be a broad new criminal prohibition reaching private conflicts of interest, I would respectfully recommend further analysis and consideration before proceeding with it.

As to these provisions affecting private conflicts of interest and all aspects of the matters under discussion, I urge the utmost care in defining clearly that conduct which is to be proscribed under federal law. As Justice Ginsburg observed in the *Skilling* decision, a new statute

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00071 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.022

"would have to employ standards of sufficient definiteness and specificity to overcome due process concerns," (*Skilling v. United States*, 561 U.S. ---, 130 S.Ct. 2896, 2934 n.45 (2010)). Ambiguous statutory terms and requirements present interpretive problems that may require substantial judicial and other resources to resolve, and are unfair to public officials and others who deserve to be able to refer to and abide by clear lines between lawful and unlawful behavior.

The need for clarity is especially important in connection with the financial affairs involving alleged conflicts of interest and undisclosed self-dealing. One only needs to lightly survey the range of public corruption prosecutions in the last twenty or thirty years to see that many arise from the financial dealings of public officials. While bribery and kickback schemes often present great challenges to investigate and successfully prosecute, the line between lawful and unlawful conduct is fairly clear in those cases once the facts are developed. More difficult, however, are the cases that involve circumstances where legislation or official action may be of keen interest to companies and individuals who also provide substantial financial support to political candidates, parties and other political organizations. These present yet another level of difficulty in drawing lines between lawful and unlawful conduct.

Lastly, and most relevant to the legislation on the table for discussion today, are issues that arise where public or corporate officials have private or personal financial interests which may affect, or be affected by, their execution of duties. These circumstances present an even greater challenge in trying to write clear laws that both recognize the complex financial and regulatory world we live in today and nonetheless

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00072 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.023

provide the clarity necessary to delineate conduct which could subject individuals to criminal conviction. Given the complexity of determining corporate and other disclosure obligations, heeding Justice Ginsburg's admonition may well suggest further study and consideration before taking legislative action on this type of activity.

To date in drawing the lines between lawful and unlawful conduct, Congress has in some instances written with a broad and rather generalized brush and in others has been quite specific. An example of general proscriptions are those of the wire and mail fraud statute, including the 1987 so-called *McNally* fix that established honest services fraud as a federal crime under the wire and mail fraud statute after the Supreme Court had nullified that basis for prosecution. In the interest of full disclosure, I was a United States Attorney at the time the Justice Department considered its position after the *McNally* decision and I supported adding the loss of honest services to the wire and mail fraud statute.

Another example is 18 U.S.C. § 666, which on its face rather specifically criminalizes bribery in federal programs where a requisite amount of federal funds go to a state or local agency. However, as interpreted and applied by the courts, most notably the Supreme Court in *Sabri v. United States* (541 U.S. 600 (2004)), this statute renders any bribery at the state and local level subject to federal prosecution by virtue of its jurisdiction being not limited to specific programs receiving federal assistance, but entire states and subdivisions which do so. One may question whether Congress intended to occasion the wholesale importation of state and local corruption to the federal enforcement docket. Regardless of what was intended, one could consider what has resulted from the action of the courts and see the value of

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00073 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.024

legislative restraint and the careful consideration of consequences when sending the federal law enforcement establishment forth with new crimes directed at state and local jurisdictions. I also mention this statute because it seems to me that it might be prudent to separate the proscription of undisclosed self-dealing by federal officials from that applying to state and/or local officials and to amend Section 666 to cover the latter. There are two reasons that doing so may commend itself to a reasoned approach in the effort to restore some of what the Supreme Court's decision in *Skilling* took from the federal prosecutor's tool box.

First, part of the fundamental difficulty with adding deprivation of intangible rights to the fraud statute, as 18 U.S.C. § 1346 does, is that it is somewhat inconsistent with the established element of fraud as grounded in an economic loss by a victim. Rendering a fraud statute to include loss of something intangible, such as a right to honest services, results in expanding exponentially an already broad statute by adding the elasticity of what "honest services" means. In contrast, amending Section 666 to cover not just bribery, but undisclosed self dealing by state and local public officials is a relatively simple amendment that has the added benefit of streamlining the new offense by eliminating the need to prove a scheme or artifice to defraud.

Second, because two very different interests and enforcement objectives are at stake as to self-dealing by federal as opposed to state and local officials, separating them in the criminal code may be well-advised. Currently, Chapter 11 of the code (sections 201 to 227) addresses bribery, graft and conflicts of interest by federal public officials. The proscriptions and requirements therein attest to the plenary federal role in policing the conduct of its own officials; it may not be so with regard

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00074 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.025

to state and local officials. It is perhaps worth considering adding any proscription on undisclosed self-dealing by federal officials to that chapter and in so doing ensuring its harmony with existing law.

In addition, if disclosure is the enforcement objective, it may be more effective and more consistent with the traditional application of criminal law to regulate the disclosure conduct through sanctions for the required disclosure as provided by the entity that requires it, rather than painting with a broad brush in the federal criminal law. This may be especially important as Congress considers creating a new federal crime that reaches employees of private organizations engaging in undisclosed or improper self-dealing.

Failure to meet disclosure obligations may not even be a criminal violation under the "statute, rule, regulation or charter" that serves as a predicate for an offense in the draft bill, but could nonetheless become a federal violation. By pointing this out, I am not at all condoning self-dealing designed to harm an employer, but simply observing that doing so may not, in the broad scope of instances potentially to be covered, rise to the level of a federal felony. Combating corruption involving purely private financial interests raises even more difficult questions deserving in my judgment careful study and consideration before providing new statutory tools to federal prosecutors. I offer a few considerations worthy of additional study.

First, as suggested, deciding and defining precisely what corporate corruption in the form of self-dealing ought to be a felony under federal law deserves careful consideration on its own merits, even apart from self-dealing by government officials. While the lack of a required disclosure

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00075 Fmt 6633 Sfmt 6633 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.026

may be a predicate for both kinds of conduct, the protected interests - the public versus the private interests - are quite different, as is the harm that results from each - namely, loss of the public's confidence in the government, versus private economic gain or loss.

Second, undefined terms in the draft legislation, including "financial interest," "harm" (to the employer), and "acts" (having an actual or intended value), may engender considerable legal controversy as to their meaning and the scope of what they encompass. Such controversy and uncertainty surrounding an unclear standard in any final piece of legislation will inevitably create and compound difficulties enforcing these provisions.

Third, given recent federal enactments covering a wide range of financial affairs, further consideration of criminalizing private self-dealing may benefit from ensuring that doing so would be in harmony with these enactments and the criminal and other provisions therein. These may be especially so in regard to disclosure requirements under existing federal securities laws.

While I urge the Committee to defer this legislation pending further study and consideration, I thank it for the opportunity to appear and comment on the matters of great importance raised by the need to protect our government and private systems from the highly corrosive effects of corruption.

Thank you, Mr. Chairman.

VerDate Nov 24 2008 14:27 Mar 28, 2011 Jkt 064789 PO 00000 Frm 00076 Fmt 6633 Sfmt 6011 S:\GPO\HEARINGS\64789.TXT SJUD1 PsN: CMORC

64789.027