

Articles

Skilling's Martyrdom: The Case for Criminalization Without Incarceration

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Introduction

THE FOCUS ON WHITE-COLLAR CRIME has increased following the corporate scandals of the late 1990s, and has been buttressed by the popular perception that white-collar criminals are not punished enough. Despite the long sentences alleged wrongdoers like Jeff Skilling of Enron,¹ Bernie Ebbers of Worldcom,² and Joseph Nacchio of Qwest³ have received, popular opinion remains that the law is too lenient on this class of offenders.⁴ The retributive impulse of the mob's

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1. See Andrew Weissmann & Joshua A. Block, *White-Collar Defendants and White-Collar Crimes*, 116 YALE L.J. POCKET PART 286 (2007), <http://www.yalelawjournal.org/images/pdfs/105.pdf>.

2. Convicted and sentenced to twenty-five years imprisonment. *United States v. Ebbers*, 458 F.3d 110, 129 (2d Cir. 2006) ("Twenty-five years is a long sentence for a white collar crime, longer than the sentences routinely imposed by many states for violent crimes, including murder, or other serious crimes such as serial child molestation.").

3. Convicted on nineteen counts of insider trading, sentenced to six years in prison, and ordered to pay \$19 million in fines. Andy Vuong, *Full Court Upholds Nacchio Insider Trading Conviction*, THE DENVER POST, Feb. 25, 2009, available at http://www.denverpost.com/business/ci_11782036.

4. *Penalties for White Collar Crime: Hearings Before the Subcom. on Crime and Drugs, of the Comm. on the Judiciary*, 107th Cong. 2 (2002) [hereinafter *U.S. Senate Hearings*], available at <http://www.access.gpo.gov/congress/senate/pdf/107hrg/86740.pdf> (statement of Sen. Joseph R. Biden, Jr., U.S. Sen. from Del.) ("[T]he strange thing is when it comes to those who rob us with a pen, rob us with a pencil, rob us with their financial shenanigans, or they steal from us, to be more precise, they tend to go to jail less than someone who would steal the same amount of money from us in a circumstance where they broke into our house.").

baying for blood after Enron's collapse was not sated by the untimely death of Ken Lay shortly after his conviction; they claimed that "justice had been cheated."⁵ This societal turn to vengeance seems to be at the root of the creeping criminalization of conduct that was traditionally dealt with by other areas of the law, as reflected in the fact that of the approximately 3000 crimes in the federal statute books, over 1200 were created since 1970.⁶ Virtually every case of new legislation aimed at behavior modification seems to entail shrill claims about the need for criminalization, upon the pretext that civil sanctions do not pack enough punch.⁷ The Sarbanes-Oxley Act of 2002 is just one example of this phenomenon, enhancing existing penalties and creating new criminal offenses in the wake of Enron's collapse.⁸ Creeping

Three local polls after Skilling's conviction and sentencing showing that forty-six percent thought his sentence was "not tough enough"; thirty-eight percent thought it was "too lenient"; and forty percent thought "he deserves more time." Brief of Defendant-Appellant at 143 n.79, *United States v. Skilling*, 554 F.3d 529 (5th Cir. 2009) (No. 06-20885).

5. See Brief of Defendant-Appellant, *supra* note 4, at 143-44 (quoting trial juror: "I feel bad for the people who really wanted to see [Lay] go to jail, that they needed the closure and they're not going to get it. You would hope [it] would be enough . . . that we came back guilty.").

6. See REPORT OF THE ABA TASK FORCE ON THE FEDERALIZATION OF CRIMINAL LAW 7-9 (1998) (approximately eighty-three percent of all federal criminal statutes have been enacted since 1930, and almost forty percent of all federal criminal statutes have been enacted in since 1970); see also John C. Coffee, Jr., *Does "Unlawful" Mean "Criminal"?: Reflections on the Disappearing Tort/Crime Distinction in American Law*, 71 B.U. L. REV. 193, 198 (1991) (critiquing the ever increasing tendency to authorize criminal sanctions for conduct that is indistinguishable from tort). See generally Sara Sun Beale, *Too Many and Yet Too Few: New Principles to Define the Proper Limits for Federal Criminal Jurisdiction*, 46 HASTINGS L.J. 979 (1995); Kathleen F. Brickey, *Criminal Mischief: The Federalization of American Criminal Law*, 46 HASTINGS L.J. 1135 (1995); Franklin E. Zimring & Gordon Hawkins, *Toward a Principled Basis for Federal Criminal Legislation*, 543 ANNALS AM. ACAD. POL. & SOC. SCI. 15 (1996) (discussing overcriminalization).

7. See Susan L. Pilcher, *Ignorance, Discretion and the Fairness of Notice: Confronting "Apparent Innocence" in the Criminal Law*, 33 AM. CRIM. L. REV. 1, 32 (1995) ("In contemporary America virtually every regulatory scheme, particularly in federal law, includes felony criminal enforcement provisions to add 'teeth' to the costs of noncompliance, covering such diverse areas as environmental safety, securities markets, employment practices, consumer protection, public benefits, and international trade. Estimates suggest that over three hundred thousand federal regulations are punishable by criminal penalties enforceable through the combined efforts of as many as two hundred different federal agencies.").

8. See, e.g., Sarbanes-Oxley Act of 2002 § 807(a), 18 U.S.C. § 1348 (2006) (imposing fines and/or up to twenty-five years imprisonment for any individual who "knowingly executes, or attempts to execute, a scheme or artifice (1) to defraud any person in connection with any security of an issuer . . . ; or (2) to obtain, by means of false or fraudulent pretenses, representations, or promises, any money or property in connection with the purchase or sale of any security of an issuer . . ."); *id.* § 1350 (penalizing CEOs and CFOs for certifying statements they know fail to comport with the requirements of the Act, imposing fines of up to \$1 million and/or imprisonment of up to ten years); *id.* § 1512(c) (imposing a fine and/or a twenty year maximum prison term on any person who "cor-

criminalization has serious ramifications: it undermines the coercive power of the criminal law, dilutes its expressive power,⁹ over-deters otherwise desirable business activities,¹⁰ conflates blameworthiness with imprisonment, creates incentives for prosecutors to abuse their powers, fuels an appetite for enhancing prison terms,¹¹ and increases social costs. Most importantly, it punishes people for actions that are not even civil wrongs,¹² let alone undertaken with the taint of moral wrongfulness.¹³

This Article is restricted to white-collar crimes involving corporate fiduciaries who make bad decisions at the expense of shareholders (corporate governance offenses). It does not address white-collar crimes that have a moral wrongfulness component, such as tax evasion, bribery, perjury, extortion, fraud, and embezzlement.¹⁴ To the extent that white-collar crimes are blameworthy, this Article argues

ruptly—(1) alters, destroys, mutilates, or conceals a record, document, or other object, or attempts to do so, with the intent to impair the object's integrity or availability for use in an official proceeding; or (2) otherwise obstructs, influences, or impedes any official proceeding, or attempts to do so . . .”).

9. See Richard J. Lazarus, *Assimilating Environmental Protection into Legal Rules and the Problem with Environmental Crime*, 27 LOY. L.A. L. REV. 867, 883 (1994) (“The reason why criminal sanctions have greater deterrent value is also the reason why they must be used more selectively. Criminal sanctions should be reserved for the more culpable subset of offenses and not used solely for their ability to deter.”).

10. See Kenneth G. Dau-Schmidt, *An Economic Analysis of the Criminal Law as a Preference-Shaping Policy*, 1990 DUKE L.J. 1, 14 (“High criminal penalties will deter people from desirable, but only marginally lawful, activity because they are uncertain whether they will be convicted of a crime.”); see also Steven Shavell, *Criminal Law and the Optimal Use of Non-monetary Sanctions as a Deterrent*, 85 COLUM. L. REV. 1232 (1985).

11. See John M. Darley, *On the Unlikely Prospect of Reducing Crime Rates by Increasing the Severity of Prison Sentences*, 13 J.L. & POL'Y 189, 199–201, 204 (2005).

12. See Wendy Gerwick Couture, *White Collar Crime's Gray Area: The Anomaly of Criminalizing Conduct Not Civilly Actionable*, 72 ALB. L. REV. 1, 2 (2009) (“[T]he imposition of criminal punishment for conduct not civilly actionable risks disrupting the current scheme of securities regulation, at the expense of considerations deemed important by Congress and the courts. The lower materiality standard and the unavailability of the safe harbor in criminal cases may chill corporate disclosure and may affect what information reasonable investors rely upon when making investment decisions.”).

13. See Mary Flood, *'All-Star Team' of Federal Prosecutors Says Merit of Cases Outweighs Hardship*, HOUS. CHRON., Dec. 19, 2004, at Bus. 1, available at <http://www.chron.com/dispatch/story.mpl/special/enron/2953693.html> (quoting Enron Task Force Prosecutor: “Defendants and suspects understand that if you're selling drugs or if you rob somebody or if you take their car, that that was wrong But the issue we face first in Enron is, was this conduct criminal? When dealing with violent crime cases or even narcotics cases, that's never a question. That's always very, very black and white. Here we have to spend a lot of time figuring out what was done and figuring out whether that was a violation of the criminal law.”).

14. Stuart P. Green, *Why It's a Crime to Tear the Tag Off a Mattress: Overcriminalization and the Moral Content of Regulatory Offenses*, 46 EMORY L.J. 1533, 1537 (1997) (“[M]oral

that the determination of wrongdoing must be disentangled from the determination of punishment—which much of the legal scholarship in this area does not do. Disentanglement of blame from deserts suggests a *via media* between criminalization and decriminalization—criminalization without incarceration. Accordingly, the criminal legal process stops at the determination of guilt.

This Article advances the criminalization debate in a novel way because it does not get bogged down in the irreconcilable quarrel about whether corporate governance misbehavior ought to be criminalized for deterrence, retribution, or rehabilitation reasons, and rather addresses whether criminalization actually achieves any of these purposes. Irrespective of the theoretical justification underpinning the decision to criminalize, imprisonment must not follow conviction. The conviction, despite the lack of incarceration, and the consequential sanctions likely to be imposed on the wrongdoer are sufficient to satisfy the three main justifications for criminalization: incapacitation, retribution, and deterrence.¹⁵ In appropriate cases, disgorgement of the offender's gains will also aid in the achievement of these objectives.¹⁶

This proposed model would yield significant savings by reducing prison costs,¹⁷ while also allowing the state to take advantage of the disproportionate cost/burden of conviction on white-collar offenders.

wrongfulness' . . . is present if the conduct made criminal is viewed by a consensus of society as immoral or in violation of a moral norm.”).

15. To the extent that further action is necessary, there are alternatives to imprisonment. *See, e.g.*, *United States v. Clark*, 195 F.3d 446, 449 (9th Cir. 1999) (imposing probation condition preventing defendant from working in law office or “any institution in the business of providing legal services”); *United States v. Whitlow*, 979 F.2d 1008, 1012 (5th Cir. 1992) (preventing defendant from working in used car industry); *United States v. Burnett*, 952 F.2d 187, 190 (8th Cir. 1991) (preventing defendant from working in business that requires travel or selling vending machines).

16. *SEC v. First Pac. Bancorp*, 142 F.3d 1186, 1191 (9th Cir. 1998) (“The district court has broad equity powers to order the disgorgement of ‘ill-gotten gains’ obtained through the violation of the securities laws. Disgorgement is designed to deprive a wrongdoer of unjust enrichment, and to deter others from violating securities laws by making violations unprofitable.” (internal citations omitted)).

17. Incarceration is extremely costly. As one expert notes,

Between 1982 and 2006, direct expenditures by federal, state, and local governments on corrections jumped from \$9 billion to \$68.7 billion, an increase of over 618%. During the same period, combined criminal justice expenditures (for police, judicial, and corrections activities) by federal, state, county, and municipal governments rose from \$35.7 billion in 1982 to \$214.3 billion in 2006.

Over Criminalization of Conduct and Over-Federalization of Criminal Law: Hearing Before the Subcomm. on Crime, Terrorism, and Homeland Security of the H. Comm. on the Judiciary, 111th Cong. 3 (2009) available at <http://judiciary.house.gov/hearings/pdf/Saltzburg090722.pdf> (testimony of Prof. Stephen A. Saltzburg on behalf of the American Bar Association).

Owing to the offenders' high earning potential,¹⁸ deterrence can be achieved at lower cost by conviction alone because the destruction of the offender's capacity to generate similar (or, indeed, any) income is suffered by the offender even without going to jail.¹⁹ If the cost of incarceration is the same for offenders with different earning capacities, imprisoning those with very high earning capacities is a waste of social capital, especially if the objectives of incarceration can be achieved through other means. Further, the cost of a conviction can be predicted with sufficient certainty in the case of white-collar criminals by looking at their earnings history, and in many cases this can be a significant sum. Unlike the common criminal who may not have a similarly predictable earning capacity and therefore may not suffer the same extent of monetary loss from a conviction, this loss ought to serve the deterrence function without the need for the state to spend money imprisoning the offender. In addition to the loss of earning capacity, clawing back ill-gotten gains would significantly add to the disutility.²⁰

Part I briefly outlines the scope of the wrongs tackled as stemming from the principal-agent relationship in corporate law and the inability of the law to effectively overcome problems resulting from the collectivization of the principal in that relationship. Part II argues that conviction without imprisonment is a second-best alternative to decriminalization in cases where the conduct is blameworthy, and results in non-consensual harm. Part III demonstrates the disutility

18. A 2006 Wall Street Journal compensation survey of CEOs of thirty-five large U.S. corporations showed a median salary and bonus of \$2,598,284, with the median base salary accounting for about \$1 million of that amount. See *The WSJ 350: A Survey of CEO Compensation*, WALL ST. J., Apr. 9, 2007, at R1.

19. For example, an offender's capacity to generate income is hampered by bar orders against serving as an officer and/or director of companies.

20. See *SEC v. Cavanagh*, 445 F.3d 105, 117 (2d Cir. 2006) (The purpose is to "prevent wrongdoers from unjustly enriching themselves through violations, which has the effect of deterring subsequent fraud. . . . The emphasis on public protection, as opposed to simple compensatory relief, illustrates the equitable nature of the remedy."); *Litigation Release No. 20387*, SEC, *Former United Health Group CEO/Chairman Settles Stock Options Backdating Case for \$468 Million* (Dec. 6, 2007), <http://www.sec.gov/litigation/litreleases/2007/lr20387.htm>; see also Sarbanes-Oxley Act of 2002 § 304, 15 U.S.C. § 7243 (2006) ("If an issuer is required to prepare an accounting restatement due to the material noncompliance of the issuer, as a result of misconduct, with any financial reporting requirement under the securities laws, the chief executive officer and chief financial officer of the issuer shall reimburse the issuer for—(1) any bonus or other incentive-based or equity-based compensation received by that person from the issuer during the 12-month period following the first public issuance or filing with the Commission (whichever first occurs) of the financial document embodying such financial reporting requirement; and (2) any profits realized from the sale of securities of the issuer during that 12-month period.").

caused by conviction alone and shows that the objectives of criminalization can be satisfied without the need for imprisonment. Part IV asserts that consequential sanctions like shaming add to the disutility of conviction. And finally, Part V illustrates the problems with conflating blame and punishment by tying the thesis to Skilling's conviction for bad business judgment devoid of moral wrongfulness.

I. Scope of Wrongs Covered

What is white-collar crime and why should it be criminalized? The oft-cited definition proposed by the criminologist Edwin Sutherland—"those crimes committed by persons of respectability and high social status in the course of their occupations"—is now seen to be severely problematic.²¹ There is no normative justification for treating criminal behavior by those of a high social status differently from crimes committed by the *hoi polloi*.²² A murder committed by a person from a higher class is still murder, and to define crimes based on economic status alone makes little sense. It is more useful to define it in terms of the criminal behavior—white-collar crime usually involves the behavior itself having the veneer of respectability and is *mala prohibita*²³ rather than *mala in se*.²⁴ Frequently, the conduct at issue only invites attention because it was seen to be too aggressive by regulators, when the actors themselves only believed they were engaging in legitimately risky enterprise.²⁵

21. EDWIN HARDIN SUTHERLAND & DONALD R. CRESSEY, *CRIMINOLOGY* 40 (Lippincott 1974) (In contrast, the FBI defined white-collar crime as "[t]hose illegal acts which are characterized by deceit, concealment, or violation of trust and which are not dependent upon the application or threat of physical force or violence . . .").

22. See STUART P. GREEN, *LYING, CHEATING, AND STEALING: A MORAL THEORY OF WHITE COLLAR CRIME* 3 (2006) ("[T]he strikingly broad range of moral judgments that surrounds such cases has less to do with the identity of individual defendants than with deeper moral ambiguities, confusions, and uncertainties that pervade our understanding of white-collar crime more generally.").

23. BLACK'S LAW DICTIONARY 960 (6th ed. 1990) (defining a "malum prohibitum" offense as an "act which is not inherently immoral, but becomes so because its commission is expressly forbidden by positive law").

24. *Id.* at 956 (defining "mala in se" offenses as "[w]rongs in themselves; acts morally wrong; offenses against conscience").

25. See Marilyn E. Walsh & Donna D. Schram, *The Victim of White-Collar Crime: Accuser or Accused*, in *WHITE COLLAR CRIME: THEORY AND RESEARCH* 32, 36 (Gilbert Geis & Ezra Stotland eds., 1980) ("Instead of there being a clear consensus about the unacceptability of the conduct in rape and white-collar crimes, there is a tendency to view the conduct as associated with otherwise acceptable behavior. Thus, rape may be identified as behavior distinguished from approved conduct only by its location on the more aggressive end of a continuum of demonstration of sexual prowess. Similarly, many frauds and larcenies by

This Article focuses only on a subset of white-collar offenders: corporate fiduciaries abusing the principal-agent relationship. The core arguments could be extended to other kinds of white-collar crime as well, because, in many cases, conviction without incarceration would satisfy the objectives of criminalization. The principal-agent relationship is especially pregnant with potential for abuse because of its inherently asymmetric nature. Agents are primarily employed in order to make up for the gaps in expertise, skill, and time that prevent principals from accomplishing the delegated tasks on their own. Yet these advantages enjoyed by agents also create problems of adverse selection and moral hazard.

Principals attempt to remain the master of the relationship by implementing such carrot-and-stick structures as keeping a close rein on agents and circumscribing discretion, co-opting the agent into ownership of the enterprise, tying incentives to the principal's returns, and carefully selecting the agent. However, when applied at the corporate level, the collectivization of the principal creates incentives for free riding and rational apathy. Shareholders, even if they care to monitor management, might have very different objectives—ranging from the employee union shareholder's desire to protect jobs to large institutional investors' focus on profits. Furthermore, when management is perceived to be inadequate, most shareholders prefer to exit rather than take corrective action. These factors debilitate the monitoring power of principals to a point where the agent is the de facto master of the relationship. Thus, although in theory the shareholders are the principals, it is the management that exercises the greater power, primarily because of real barriers to removal caused by collective action problems and the deference that corporate law accords to business decisions taken by management.

This Article addresses whether such agency problems should be the subject matter of criminal law with imprisonment as the sanction or whether they are better suited to civil or social sanctions.²⁶ Criminal sanctions have been used, for example, in the Skilling case, despite the prosecution framing the case in terms that invoke the agency

trick or false pretenses can be viewed as excesses in what is normally accepted, aggressive salesmanship or shrewd economic behavior.”).

26. See Larry E. Ribstein, *Perils of Criminalizing Agency Costs 2* (Ill. Law & Econ. Working Papers Series, Paper No. LE06-021, 2006), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=920140 (“We don’t want to spend \$100 to catch \$10 of cheating. This raises questions about when an agent’s unfaithfulness deserves any kind of sanction, and especially about when it crosses the line to criminal.”).

cost problem.²⁷ This resort to criminal law has been justified on the plea that the principals are not the only victims of Skilling's wrongdoing, but that his conduct engendered wider societal harm. It might also be evidence of the vicious nature of the retributive impulse following loss, even when some of the loss is the byproduct of consensual risk taking.²⁸ Shareholders, employees, and the wider public feel the urge to punish those at the top for bad bets despite the absence of moral wrongfulness, and the criminal law serves as an instrument for such punishment.

Crimes with a *mens rea* element are not problematic; therefore, this Article addresses only those offenses where the defendants were most likely acting in the belief that their conduct was legal. This is particularly plausible in cases involving the interpretation of complex accounting rules or risky business decisions. The problem with criminalizing this sort of behavior is that the traditional purposes of criminal punishment—deterrence, incapacitation, retribution, rehabilitation, and restitution—are ill matched with the results that principals seek. Principals' objectives can be achieved at much lower cost either by social or civil sanctions without the need for the expenditure of state resources. The employment of criminal law to combat agency abuses is particularly troubling when the state is content to criminalize based on alleged obstructions of justice rather than proving the underlying allegations. The cases of *Martha Stewart*²⁹ and *Frank Quattrone*³⁰ are illustrative of this trend.

27. See Reply Brief of Defendant-Appellant at 2, *United States v. Skilling*, 554 F.3d 529 (5th Cir. 2009) (No. 06-20885); *id.* at 71 (closing argument by the prosecution: "[M]ake no mistake, they [Skilling and Lay] got wealthy. . . . And in exchange for that money, they owed their employees a duty, a duty of good faith and honest services, a duty to be truthful, and a duty to do their job, ladies and gentlemen, to do their job and do it appropriately." (emphasis added)).

28. Epithets used against Skilling included "pig," "snake," "evil," "crook," "thief," "fraud," "asshole," "criminal," "bastard," "scoundrel," "liar," "weasel," and "economic terrorist." He was described as "dirty," "deceitful," "dishonest," "greedy," "amoral," "devious," "lecherous," "manipulative," "unscrupulous," "despicable," "equivalent [to] an axe murderer" who has "no conscience," "stole from employees," and "swindled a lot of people." He was condemned as "guilty as sin," something for which "he need[ed] . . . to pay the price," go to "jail for 20 years," and "be hanged." Brief of Defendant-Appellant, *supra* note 4, at 134.

29. *United States v. Stewart*, 433 F.3d 273, 280, 319–20 (2d Cir. 2006) (affirming conviction).

30. *United States v. Quattrone*, 441 F.3d 153, 161 (2d Cir. 2006) (obstruction of justice conviction subsequently vacated).

II. Moral Ambiguity of White-Collar Crime

A. Crime Must Be Morally Blameworthy

There must be a fundamental distinction based on the moral blameworthiness of conduct if our distinctions between criminal and civil sanctions are to have any merit.³¹ Misapplication of the criminal label to conduct that is not intrinsically wrong is counterproductive to the objectives sought to be achieved by criminalization.³² As Professor Stuart Green wrote in a recent work, “[w]hat is interesting and distinctive about [white collar crime] is that, in a surprisingly large number of cases, there is genuine doubt as to whether what the defendant was alleged to have done was in fact morally wrong.”³³ This is a major problem, as Green recognizes, because “when there is a gap between what the law regards as morally wrongful and what a significant segment of society views as such, moral conflict and ambiguity are likely to be the result.”³⁴ This sort of ambiguity severely affects what Professor Andrew Ashworth calls the “principle of fair labeling,” because it fails to ensure “that widely felt distinctions between kinds of offences and degrees of wrongdoing are respected and signaled by the law, and that offences should be divided and labeled so as to represent fairly the nature and magnitude of the law-breaking.”³⁵ However, Green ar-

31. See Paul H. Robinson, *The Criminal-Civil Distinction and the Utility of Desert*, 76 B.U. L. REV. 201 (1996); Stephen J. Schulhofer, *Two Systems of Social Protection: Comments on the Civil-Criminal Distinction, with Particular Reference to Sexually Violent Predator Laws*, 7 J. CONTEMP. LEGAL ISSUES 69 (1996); Louis Michael Seidman, *Points of Intersection: Discontinuities at the Junction of Criminal Law and the Regulatory State*, 7 J. CONTEMP. LEGAL ISSUES 97 (1996); Carol S. Steiker, *Foreword—Punishment and Procedure: Punishment Theory and the Criminal-Civil Procedural Divide*, 85 GEO. L.J. 775 (1997).

32. Paul H. Robinson, *Moral Credibility and Crime*, ATL. MONTHLY, Mar. 1995, at 72, 77 (“As the label ‘criminal’ is increasingly applied to minor violations of a merely civil nature, criminal liability will increasingly become indistinct from civil and will lose its particular stigma.”); see also Green, *supra* note 14, at 1536 (“In short, these critics contend, applying criminal sanctions to morally neutral conduct is both unjust and counterproductive. It unfairly brands defendants as criminals, weakens the moral authority of the sanction, and ultimately renders the penalty ineffective. It also squanders scarce enforcement resources and invites selective, and potentially discriminatory, prosecution. We should reserve the criminal law—the ‘heavy artillery’ of our legal system . . . —for conduct that reflects the traditional conception of criminality.”).

33. GREEN, *supra* note 22, at 1 (“It is . . . the manifestation of a widely felt sense—expressed by judges, jurors, scholars, journalists, and the average citizen—that the law in this area involves a kind of moral uncertainty that distinguishes it from that which governs more familiar ‘core’ cases of crime . . .”).

34. *Id.* at 46.

35. *Id.* at 42.

gues that white-collar crimes correspond well to moral norms of a common-sense sort:³⁶

[C]ertain fine-grained distinctions in our criminal law are a reflection of equally fined-grained [sic] distinctions in our moral thinking, and vice versa.³⁷ Thus, white-collar crime doctrine that may at first glance seem puzzling and internally inconsistent can often be explained through reflection on the moral concepts that underlie it. And, by the same token, ostensibly baffling distinctions we make in our everyday moral lives can in some cases be traced to distinctions that first appeared, or are most clearly articulated, in the criminal law.³⁸

Green thus distinguishes lying from deception by arguing that:

[M]erely misleading is less wrongful than lying because what I call the principle of *caveat auditor*, or “listener beware,” applies to cases of merely misleading but does not apply to lying. Like the principle of *caveat emptor*, which says that a buyer is responsible for assessing the quality of a purchase before buying, the principle of *caveat auditor* says that, in certain circumstances, a listener is responsible, or partly responsible, for ascertaining that a statement is true before believing it.³⁹

Green’s thesis posits that people are able to make moral distinctions between these offenses; however, he does not explain how ordinary people are to make such distinctions. Green seems to conflate common morality with critical morality in coming to this conclusion. As the Skilling case demonstrates in the following pages, it is unduly optimistic to suppose that public perceptions of moral wrongfulness are nuanced enough to separate conduct that is merely risky from that which is criminal, and the dangers are exacerbated in the context of corporate criminal conduct due to the infiltration of negative emotions like envy and resentment. The popular perception that CEOs and senior corporate executives are greedy and arrogant is probably at the root of the visceral reactions to news reports about alleged acts of wrongdoing. Given this fact, it is hard to see that common morality

36. These moral norms, according to Green, “are fairly concrete”:

Although there will be significant disagreement over the precise content and application of such norms, almost every civilized person will have some rudimentary understanding that it is morally wrong, at least in certain core cases, to lie, cheat, steal Even people who have never had occasion to read a single page of moral philosophy are capable of making remarkably fine-grained distinctions about, say, what properly constitutes cheating or stealing.

Id. at 45.

37. “[T]he divergent ways in which the offenses of perjury and fraud treat the requirement of deception . . . reflect deep-seated and fine-grained distinctions concerning the concept of deception that we make in our everyday moral lives.” *Id.* at 42.

38. *Id.* at 5.

39. *Id.* at 78–79.

will be able to set aside these negative emotions when evaluating conduct for white-collar criminal sanctions.

There is danger also from the imprecise and ambiguous nature—in terms of moral rightness or wrongness—of the conduct at issue in agency crimes. Given the lack of clarity as to what underlying moral norm has been violated by a particular alleged crime, and because the precise complexities are hard to understand, there is likely to be a great deal of dissonance about moral wrongfulness and culpability.⁴⁰ As Henry Hart writes:

When a criminal enactment proscribes conduct which is *malum in se*, such as murder or manslaughter . . . the moral standards of the community are available always as a guide in the resolution of its indeterminacies, and there is a minimum of unfairness when doubt is resolved against a particular defendant. This guidance is missing when the proscribed conduct is merely *malum prohibitum*.⁴¹

Frequently, the conduct alleged to be wrong involves accounting transactions without any evidence about the offender's expertise in accountancy. The accounting rules often do not have any moral element, and are explained more as coordination devices rather than as moral guidelines. They are also devices for standardization to facilitate comparison and in many situations are substitutable without moral choices being compromised. Aside from the offender's sense as to the moral value of adhering to such rules, it is difficult to imagine that such rules have percolated down into the community to attain the status of moral norms. This might explain the indifference of shareholders to alleged wrongdoing by management in relation to accounting misstatements as long as there is no negative impact on share prices.

Moral wrongfulness is essential to criminalization for corporate agency offenses; otherwise, determinations about culpability rest only on ex post loss rather than from clear guidelines for behavior ex ante. As Green acknowledges, "we need to refer to the idea of [moral] wrongdoing not only in distinguishing among various offenses but also in deciding which conduct to criminalize in the first place, how

40. This is particularly true with cases like Enron where complicated financial transactions were at issue. It is hard to imagine that the average person is able to appreciate the intricacies of the accounting treatment concerning the Enron Special Purpose Entities ("SPEs") and the rules relating to off-balance sheet treatment with regard to the three percent at-risk rule. If the relevant actor believed the SPEs did not have to be consolidated based on expert advice, where is the moral wrongfulness in the conduct? Besides, are accounting rules moral norms?

41. Henry M. Hart, Jr., *The Aims of the Criminal Law*, 23 LAW & CONTEMP. PROBS. 401, 420 (1958).

offense elements should be defined, and what defenses should be available.”⁴² He claims that “without a clearer understanding of the relationship between morality and white-collar criminal law, the retributive principles on which the criminal law is founded are placed in serious jeopardy.”⁴³

With regard to regulatory offenses, Green does not contend it is wrong for the state to criminalize conduct that is not morally wrongful. He argues that “if violating such a regulatory statute constitutes rule-breaking intended to obtain an unfair advantage over another with whom one is in a cooperative, rule-bound relationship,” then the violation constitutes the moral wrong of cheating.⁴⁴ Giving the example of insider trading, he writes it is wrongful because it is essentially cheating, because the trader “(1) violates the [Securities Exchange Commission (SEC)] rule that one must either disclose material non-public information or abstain from trading; and does so (2) with the intent to obtain an advantage over a second party with whom she is in a cooperative, rule-governed relationship.”⁴⁵ The basis of the abstain-or-disclose rule appears to be that investors must have confidence the game is being played fairly, and that it is unfair for some traders, who have privileged access to information, to make money off of that information. This is not as clear as Green would like to believe because there is a body of scholarship contending that insider trading is actually beneficial to the market because it unearths vital information.⁴⁶ Buyers predisposed to purchase shares in a company at the prevailing

42. GREEN, *supra* note 22, at 42.

43. *Id.* at 4. Professor Seigel argues in the same vein:

One of the foundational principles of the American criminal-justice system is that punishment is only appropriate if a person acts voluntarily (*actus reus*) and with some level of intention (*mens rea*) The reasons for this principle stem from the two traditional purposes of punishment: retribution and deterrence. Retribution is the deontological notion that a person who commits a crime deserves to be punished. The converse of this proposition—employing retribution as a limiting principle—is equally true. A person who fails to act voluntarily (such as by way of reflex or subject to duress) simply should not be punished.

Michael L. Seigel, *Bringing Coherence to Mens Rea Analysis for Securities-Related Offenses*, 2006 WIS. L. REV. 1563, 1569 (2006).

44. GREEN, *supra* note 22, at 250. However, he qualifies this by writing that “harmfulness without wrongfulness is not supposed to be enough to satisfy the retributive demands of the criminal law. In the absence of a persuasive argument that lawbreaking per se entails some independent form of moral wrongfulness,” he doubts that “criminalization can be justified.” *Id.* at 254.

45. *Id.* at 240.

46. See, e.g., HENRY G. MANNE, *INSIDER TRADING AND THE STOCK MARKET* (1966) (arguing that insider trading has little or no effect on stockholders, and that insiders are entitled to any gains as a result of their status).

market price might be able to buy at a lower price because of the actions of insiders. Further, it is unlikely that the person who is purchasing the securities from the insider is being taken advantage of in every situation. It is possible that the buyer sold the securities before the information surfaced and caused the stock price to fall. In this case, the buyer is profiting rather than being taken advantage of as Green contends. If it is assumed that the argument is that the entire market is being taken advantage of, even that does not suffice as a strong case for criminalization because in many cases the size of the sale of the securities by the insider might be small in relation to the market for securities of the relevant company, with the result that the consequences are *de minimis*. Further, the chief complaint of non-insiders is that they did not have the opportunity to cash in on the non-public information, not that they were cheated.⁴⁷ If they had been able to cash in, there would have been no complaint. This, again, illustrates the moral ambiguity of the alleged wrong.

Moreover, moral wrongfulness is not an automatic justification for criminalization: several morally wrongful acts might cause no harm in many circumstances involving consent. This is why the state refuses to criminalize such acts in situations involving consensual exchanges. Some scholars like Henry Hart have argued that criminalization should be reserved for conduct that is “intrinsically wrongful.”⁴⁸ Similarly, Sanford Kadish has criticized the tendency to criminalize “aggressive business behavior,” claiming the “stigma of moral reprehensibility does not naturally associate itself with the regulated conduct” in such cases.⁴⁹ This “impair[s] the identity of the criminal sanction and its ultimate effectiveness as a preventive sanction, both in the area of economic crimes and in the areas of its traditional application.”⁵⁰ The fact that our perceptions about morality are capable of temporal change and that conduct regarded as morally wrongful or harmful during a certain timeframe might be regarded as perfectly acceptable in another timeframe must give us further pause for thought when we see the temptation to criminalize.⁵¹

47. See, e.g., Todd A. Bauman, Comment, *Insider Trading at Common Law*, 51 U. CHI. L. REV. 838, 847–55 (1984) (for a thorough outline of what is sometimes referred to as the “equal opportunity” argument against insider trading).

48. Hart, *supra* note 41, at 417.

49. Sanford H. Kadish, *Some Observations on the Use of Criminal Sanctions in Enforcing Economic Regulations*, 30 U. CHI. L. REV. 423, 425–26 (1963).

50. *Id.* at 444.

51. See Harry V. Ball & Lawrence M. Friedman, *The Use of Criminal Sanctions in the Enforcement of Economic Legislation: A Sociological View*, 17 STAN. L. REV. 197, 220–21 (1965).

B. Harm Distinguished

The horror stories of families being deprived of their savings by the actions of corporate executives have shattered the myth that white collar crime is victimless.⁵² In some cases, it has been alleged that entire cities are victims of corporate criminal conduct.⁵³ The purported economic costs imposed by white-collar criminal behavior also have been cited as a reason for adopting a hard line against offenders.⁵⁴ Given the harm caused by white-collar criminals, some believe the privileged treatment accorded to them erodes the deterrent power of the criminal law because it signals that society treats criminals from rich backgrounds differently than those from poorer ones. Some prosecutors complain that judges are more sympathetic to pleas by corporate defendants to reduce or avoid incarceration, and that this affects their decisions to bring such offenses to trial.⁵⁵ It is also claimed that this is particularly lamentable because the deterrent objectives of the criminal law are particularly well suited to effective application against corporate defendants because they are usually educated and commit their crimes after rational thought.⁵⁶ All of these concerns have coa-

52. See *U.S. Senate Hearings*, *supra* note 4, at 10 (statement of Janice Farmer) (“They took more than my money and my dream. They destroyed my pride in my whole career. I am totally ashamed that I worked for Enron.”); *id.* at 22 (statement of Bradley W. Skolnik, Ind. Securities Comm’r, and Chairman, Enforcement Sec., N. Am. Secs. Adm’rs Ass’n, Inc.) (“[W]hite collar crimes aren’t victimless crimes. Just like street crime, securities fraud ruins lives, destroys families, steals hopes, and kills dreams.”).

53. See Brief of Defendant-Appellant, *supra* note 4, at 128 (“I want to talk a little bit about . . . other *victims*, Your Honor. Vendors who sold their goods and services to Enron suffered. Other businesses who relied on Enron suffered. Local economies where Enron did business suffered. *Houston as a community was particularly hit hard by what happened at Enron.*”).

54. One expert stated that the economic value of securities fraud alone is at about \$40 billion, compared with \$10 billion for street crime. See *U.S. Senate Hearings*, *supra* note 4, at 122 (testimony of Glen B. Gainer, III).

55. *Id.* at 19 (statement of Hon. James B. Comey, Jr., U.S. Att’y, S.D.N.Y.) (“[Federal judges] work to eliminate or reduce that jail time because of the defendant’s civic work or charitable work or his great employment record or his big family or his health problems, or a whole host of factors that the Guidelines say are discouraged . . .”).

56. *Id.* (“White collar offenders are . . . more sophisticated than most criminals. They commit their crimes not in a fit of passion or out of addiction or a craving, but with cold and careful calculation. They are, in my experience, the most rational of offenders and are more likely to weigh the risks against the anticipated rewards of committing a crime.”); see also *id.* at 176 (statement of Hon. Jeff Sessions, U.S. Sen. from Ala.) (“I was a United States Attorney during the Savings and Loan fraud cases. I prosecuted Federal land bank fraud cases. My office prosecuted those cases that I supervised, and I am going to tell you there is a lot better behavior in banking today because people went to jail over those cases in the past. They lost everything they had, their families were embarrassed, and a lot of people started checking to make sure they were doing their banking correctly.”).

lesced to create a growing public opinion that corporate wrongdoers must be equated with ordinary criminals and that incarceration is necessary.⁵⁷

To some theorists, the prevention of harm is a sufficient basis for criminalization; it is permissible to criminalize harmful white-collar conduct even if it is not morally wrongful. It is not necessary that the act should have also offended a moral wrong, rather it suffices that the offender violated a legal ban. Joel Feinberg's harm principle, for example, provides that:

[I]t is legitimate for the state to prohibit conduct that causes serious private harm, or the unreasonable risk of such harm, or harm to important public institutions and practices. In short, state interference with a citizen's behavior tends to be morally justified when it is reasonably necessary . . . to prevent harm or the unreasonable risk of harm to parties other than the person interfered with.⁵⁸

It is important to understand what constitutes harm. As is typically used in the criminal law, "criminal harm" can involve bodily harm⁵⁹ as well as social harm involving collective losses.⁶⁰ The first kind is unproblematic, and the validity of the state's criminalization of such conduct is not seriously disputed. The second might also be acceptable in cases where the harm is non-consensual and involves third parties suffering without the ability to avoid the harm. However, no such necessity exists in situations involving agency problems, as the principals have tools at their disposal to control the wrongdoers. There are perfectly adequate civil and social sanctions that can achieve the objectives—incapacitation, retribution, and deterrence—at much lower cost. Principals can act in concert, use regulators like the SEC, or act through intermediaries like stock exchanges and institutional shareholders to do any of these without the state incurring imprisonment expenses.

57. *Id.* at 20 (statement of Glen B. Gainer, III, W. Va. State Auditor, and Chairman, Nat'l White Collar Crime Ctr.) ("Our research section has found through our last nationwide study that most Americans view economic crime, or what we would consider white collar crime, to be every bit as important and deserve equal time and prosecution as traditional street crime . . .").

58. JOEL FEINBERG, *THE MORAL LIMITS OF THE CRIMINAL LAW: HARM TO OTHERS* 11 (1984).

59. See Robert W. Drane & David J. Neal, *On Moral Justifications for the Tort/Crime Distinction*, 68 CAL. L. REV. 398, 409–10 (1980) (considering the individual's relatively greater psychological fear of suffering bodily harm versus harm to her property).

60. See FEINBERG, *supra* note 58, at 221–32 (defining collective harms as harms to the public interest, such as economic disasters, inability to provide public services, and environmental pollution).

Corporate governance crimes involve harm, and some even involve harm on a massive scale such as that caused by the bankruptcy of Enron. However, this harm is the price of capitalism and there are other mechanisms that can tackle it more efficiently than imprisonment. For conduct without the taint of moral wrongfulness, but where non-consensual harm results, criminalization without incarceration is the second-best alternative to decriminalization.

Removing incarceration from the table also separates blameworthiness from punishment. The state possesses advantages in determining blame, but its advantages in terms of punishing white-collar offenders are less clear. If the high cost of incarcerating non-violent offenders outweighs the cost of other kinds of punishment, without corresponding benefits, scaling back the state monopoly on punishment to areas where it enjoys advantages might be advisable. Decoupling blame from punishment also recognizes the reality that conviction alone is sufficient punishment. Assuming further punishment is necessary, state punishment could be restricted to fines and impediments to holding positions of trust.⁶¹

III. Conviction as a Sanction: Theoretical Underpinnings

A. Deterrence

This Part explores the theoretical justifications for the deterrence value of conviction for white-collar wrongs by comparing and contrasting it with the deterrent value of imprisonment. The most frequently advanced justification for criminalization is deterrence—offenders will be deterred from committing criminal acts if the benefits from committing those acts do not exceed the probability of being caught multiplied by the cost of punishment following prosecution.⁶² Thus, a rational actor will trade off the expected value of committing the criminal act against two variables: the probability of being caught and the punishment after conviction. If the probability of being caught is low, the criminal act might still seem attractive even if the punishment is high. The same principle applies if the punishment is low and the probability of being caught is high. These two variables are a function

61. See Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169, 193 (1968) (“[P]robation and institutionalization use up social resources, and fines do not, since the latter are basically just transfer payments, while the former use resources in the form of guards, supervisory personnel, probation officers, and the offenders’ own time.”).

62. See generally *id.*; Dau-Schmidt, *supra* note 10; Richard A. Posner, *An Economic Theory of the Criminal Law*, 85 COLUM. L. REV. 1193 (1985); Shavell, *supra* note 10.

both of the resources that the state possesses and of determinations as to their optimal allocation.

This vein of scholarship draws on work by Gary Becker, whose economics-based approach showed that stringent fines were preferable to imprisonment.⁶³ Subsequent work building on this theory has important implications for this Article's thesis. In an important article calculating the disutility of imprisonment, A. Mitchell Polinsky and Steven Shavell posit there are three kinds of offenders: risk-neutral (offenders for whom the severity and probability of imprisonment has equal deterrent value), risk-averse (offenders for whom severity of imprisonment has greater deterrent value than probability of imprisonment), and risk-preferring (those for whom the severity of imprisonment has less deterrent value than the probability of imprisonment).⁶⁴ Whereas the Polinsky and Shavell study focused on the disutility of imprisonment, this Article builds on that study and focuses on the disutility of conviction rather than the disutility of imprisonment. This allows an understanding of how the removal of imprisonment as punishment might affect a rational offender's calculation. It also facilitates an analysis of the tradeoffs between the relevant variables by slicing the salami even finer than Polinsky and Shavell's study does.

To start this analysis, the probability of conviction is p , the length of imprisonment is l , and the total disutility is u . Total disutility is made up of disutility of conviction c and disutility of imprisonment i . Although other factors like age and social situation can be significant variables in calculating total disutility, for simplicity those factors are excluded, and the calculation is $u = p \times [(l \times i) + c]$. Individuals with a high value for c are reputation conscious and those with a low value for c are reputation indifferent. Consider the following scenario: the probability of conviction is 10%, the disutility of conviction is 200, the disutility of any sentence length is 5, and the sentence is 10 years. Then total disutility is $.1 \times [(5 \times 10) + 200] = 25$. Now, since the disutility of any sentence length is constant, increasing the sentence to 20

63. Becker, *supra* note 61.

64. A. Mitchell Polinsky & Steven Shavell, *On the Disutility and Discounting of Imprisonment and the Theory of Deterrence*, 28 J. LEGAL STUD. 1, 4-7 (1999) ("If the disutility from imprisonment rises in proportion to sentence length, then an increase in the magnitude of sanctions has the same effect as an equal percentage increase in the probability of sanctions. However, if disutility rises more than in proportion to the sentence, raising the magnitude of sanctions has a greater effect than increasing their probability by the same percentage amount. Conversely, if disutility rises less than in proportion to the sentence, raising the magnitude of sanctions has a smaller effect than increasing their probability.").

years will increase the total disutility to $0.1 \times [(5 \times 20) + 200] = 30$. If, however, the disutility of any sentence length is 0, then total disutility is $0.1 \times [(0 \times 10) + 200] = 20$. In this case, increasing the sentence length to 20 does not alter the total disutility at all ($0.1 \times [(0 \times 20) + 200] = 20$). It is unlikely that the disutility of any sentence length is 0 for any rational individual; it is possible that the disutility of year 1 is very low at 1 ($u = 0.1 \times [(1 \times 10) + 200] = 21$), and thereafter declines in some proportion to sentence length to a point where the utility of a life sentence might move into positive territory.⁶⁵ To explain, if an individual is sentenced to imprisonment for 20 years at the age of 55, while the disutility of the first year is likely to be very high, this declines as the person ages because the alternative of being released at an old age without any prospect of an income or caregivers might be more unpalatable than staying in jail. Similarly, if the sentence is life imprisonment, each year after the first might become more bearable, to the point where it might be preferable to die in jail.

Now, consider the case of reputation-indifferent individuals with no disutility for conviction alone. Probability of conviction is 10%, disutility of conviction is 0, disutility of any sentence length is 5, and the sentence is 10 years. Now, total disutility is $0.1 \times [(5 \times 10) + 0] = 5$. Increasing the sentence length to 20 years results in a total disutility of $0.1 \times [(5 \times 20) + 0] = 10$, doubling with the doubling of sentence length. This has startling implications. It shows that for the state to achieve the same disutility for this individual as the offender with the disutility of conviction of 200 and no disutility of imprisonment, the state must imprison him for 40 years. Conversely, the offender with the disutility of 200 on conviction but no disutility on imprisonment can be deterred to the same extent even by saving money on prison costs for 40 years. Thus, sending both individuals to jail for identical amounts is a significant waste of money and fails to capture the savings offered by the disutility experienced by conviction alone.

65. Professors Robinson and Darley quote Kahneman to make a similar point:

[T]he well being of prison inmates is likely to improve in the course of their sentence, as they gain seniority and survival skills. . . . Suppose . . . that prisoners apply a Peak and End rule in retrospective evaluations of their prison experience. The result would be a global evaluation that becomes steadily less aversive with time in prison, implying a negative correlation between sentence length and the deterrence of individual recidivism. This is surely not a socially desirable outcome.

Paul H Robinson & John M. Darley, *The Utility of Desert*, 91 Nw. U. L. REV. 453, 462 n.19 (1997) (quoting Daniel Kahneman, *New Challenges to the Rationality Assumption*, 150 J. INST. & THEORETICAL ECON. 18, 33–34 (1994)).

Similarly, tweaking the probability of conviction has the following consequences. Assume that the probability of conviction is 0.025, disutility of conviction is 200, disutility of any sentence length is 0 and sentence length is 10 years. Total disutility is 0.025 $[(0 \times 10) + 200] = 5$. This means this offender can be deterred to the same extent as the reputation-indifferent individual who is imprisoned for 10 years with a disutility of 5, at one-fourth the cost of enforcement without even incurring the cost of imprisonment, i.e., by conviction alone. Thus, it is a waste of money to spend the same amount on enforcement for both types of offenders.

The above clearly demonstrates the benefits of focusing on the quality of individuals and their disutility of conviction. By taking advantage of this characteristic, a policy can achieve the same deterrence at lower prison cost and lower enforcement cost. White-collar criminals are more likely to be reputation conscious and have a high rate of disutility for conviction alone. This is because their very livelihood is tied to reputation. One study found that “[f]or all the crimes . . . examined, ranging from insider trading to drug offenses to bank larceny, it is not uncommon to find that the highest income criminals suffer reductions in legitimate income of between eighty and ninety-five percent as a result of conviction.”⁶⁶ If earning capacity is destroyed or substantially diminished, the conviction itself would satisfy the punishment function. It serves to convey information to society about the wrongdoer’s unsuitability to hold responsible corporate positions involving trust. To the extent that further deterrence is needed, conviction could be combined with other impediments to ensure that the offender does not have access to opportunities for re-offending.⁶⁷ Conviction also triggers consequential sanctions, such as

66. John R. Lott, Jr., Comment, *Optimal Penalties Versus Minimizing the Level of Crime: Does it Matter Who is Correct?*, 71 B.U. L. REV. 439, 442 (1991) (“Collateral penalties imposed upon criminals, including the loss of licenses and the loss of legitimate income after returning to the work force, are significantly more important for white collar criminals than for poor criminals even assuming they have committed the same crime.”).

67. See SEC v. Posner, 16 F.3d 520 (2d Cir. 1994). The trial court held that the defendants had committed securities fraud, enjoined them from acting as officers and directors of any public company, and ordered them to disgorge money. *Id.* at 520–21. On appeal, the court affirmed stating the court’s conclusion that the officer and director bar was necessary to protect public investors:

The Posners seem to be shocked by what they see as the draconian remedy of eternal boardroom banishment. We intend our affirmance of Judge Pollack’s judgment in this respect as a sharp warning to those who violate the securities laws that they face precisely such banishment. Of course, as the SEC points out, such bar orders are imposed routinely by consent decree.

Id. at 522.

shaming, by emboldening third parties to enforce social norms on offenders.⁶⁸

Given the high profile of the offenders, the information about conviction is likely to be widely disseminated, ensuring that the relevant target group perceives the consequences of offending. Since the number of actual and potential wrongdoers subject to these prosecutions is relatively small (these crimes can only be committed by corporate fiduciaries), saturating the relevant constituency with deterrent information is feasible and ensures that search costs are not significant. Had the pool of corporate fiduciaries been large, corporations would have had to expend significant resources to detect prior offenders and ensure they were not given further opportunities to offend. This is not the case. In addition, executive search firms and other gatekeepers like professional licensing agencies already perform the detection function.

In sum, monetizing the disutility suffered by the white-collar criminal upon conviction offers clarity about the sufficiency of the punishment function served by conviction alone. It also allows for more efficient use of state resources; the cost of imprisonment might be more effectively utilized on those who cannot be deterred by the disutility of conviction alone because they have little to lose. Further, the ability to deter without the cost of imprisonment eliminates the social disutility caused by constantly ratcheting up sentences.⁶⁹ It also frees courts from making fine distinctions about appropriate sentence length, with the risk of a jail term being something of a lottery based on the dispositions of judges.⁷⁰

68. Alon Harel & Alon Klement, *The Economics of Stigma: Why More Detection of Crime May Result in Less Stigmatization*, 36 J. LEGAL STUD. 355, 360 (2007) (“Criminal conviction is clearly relevant for both willing stigmatizers and unwilling stigmatizers. The willing stigmatizers use conviction as a proxy for identifying offenders even if their real intended targets are offenders rather than those who have been convicted and punished. In contrast, unwilling stigmatizers do not use stigmatization merely as a proxy; their primary targets are those who have been publicly identified and labeled as offenders—that is, the stigmatized.”).

69. See Dau-Schmidt, *supra* note 10, at 14 (“[I]ncreasing penalties to prevent crime imposes costs on society in the forms of the mistaken punishment of innocent people, deterrence of beneficial but marginally lawful activity, and destruction of marginal incentives for good behavior.”).

70. Geraldine Szott Moohr, *Prosecutorial Power in an Adversarial System: Lessons from Current White Collar Cases and the Inquisitorial Model*, 8 BUFF. CRIM. L. REV. 165, 211–14 (2004).

B. Retribution

Criminalization of white-collar offenders is often motivated by a retributive impulse. This Article does not undertake an exhaustive review of the literature on retribution or suggest that retribution should not be a factor in determinations about the need for criminal sanctions. The limited claim is that the retributive objective is satisfied by conviction alone given the unique position of white-collar offenders. As discussed previously, these offenders value group membership, which is often tied directly to their earning capacity. Conviction frequently extinguishes such membership and rings the death knell for a professional career.⁷¹ For example, if the offender is a lawyer, he may lose his license.⁷² He may also be suspended from practicing before the SEC.⁷³ If she is a CEO of the company she founded, she must demit that office.⁷⁴ Following the passage of the Sarbanes-Oxley Act, under section 1105, the SEC has the power without going to court to issue officer and director bars as part of a cease-and-desist proceeding.⁷⁵ The standard for a bar is unfitness.⁷⁶ Caution is necessary in exercising the barring power—it must be confined to limited time periods rather than lifetime bars unless there are strong reasons to impose the latter. The inherent limitations of any system of predicting future behavior, even taking account of prior misconduct, will ensure that some CEOs will be falsely predicted to have the potential for re-offending and will receive unnecessarily long bar orders. These individuals will experience undeserved hardship and there will be a net

71. *Id.* at 213.

72. *See, e.g.*, MODEL FEDERAL RULES OF DISCIPLINARY ENFORCEMENT R. I (1991); RULES OF PROCEDURE OF THE STATE BAR OF CALIFORNIA R. 602 (2010).

73. Securities Exchange Act of 1934 § 15(b)(4), 15 U.S.C. § 78o(b)(4) (2006). Section 15(b)(4) authorizes the SEC to “censure, place limitations on the activities, functions, or operations of, suspend for a period not exceeding twelve months, or revoke the registration of any broker or dealer” if, among other things, the broker or dealer has (1) willfully made or caused to be made false material statements in any proceeding before the SEC with respect to registration; (2) willfully violated any provisions of the Securities Act or the Exchange Act, among others; or (3) willfully aided and abetted the same. *Id.* §§ 15(b)(4)(A), (D), (E); *see also* Touche Ross Co. v. SEC, 609 F.2d 570 (2d Cir. 1979) (noting SEC can censure and suspend individuals from practicing before it).

74. One example is Martha Stewart. Under the terms of her settlement with the SEC for insider trading, Stewart was forbidden from serving as a company executive or director of any public company for five years. Landon Thomas, Jr., *Stewart Deal Resolves Stock Case*, N.Y. TIMES, Aug. 8, 2006, at C1. SEC regulations bar any unfit person from serving in an executive position in a publicly held company. Sarbanes-Oxley Act of 2002 § 305, 15 U.S.C. § 78u(d)(2) (2006).

75. Sarbanes-Oxley Act of 2002 § 1105, 15 U.S.C. § 78u-3(f) (2006).

76. *Id.*

loss of social welfare. Yet others will be falsely predicted to be at a low risk of re-offending and will receive short term bars. Such individuals might re-offend and create new victims. Since this category is more likely to be the focus of attention, it might explain the view that white-collar offenders also have a significant rate of recidivism.⁷⁷

To conclude, the principal objectives of criminalization are to prevent white-collar offenders from committing similar offenses and to deter others from committing offenses. The first objective can be achieved by disqualifying the offender from holding responsible office, and the second can be achieved by conviction without imprisonment aided by consequential sanctions.⁷⁸ A third objective is to ensure that the offender does not retain the fruits of his misconduct. This can be achieved by an order to disgorge and by taking back ill-gotten gains. Incarceration does not aid any of these purposes. To the extent that retribution is an objective, and is not satisfied by the above sanctions, consequential sanctions that inevitably follow conviction ought to suffice in any civilized society. This has the added advantage of decentralizing the retributive objective and allowing non-state actors to impose punishment.

IV. Consequential Sanctions

Conviction inevitably results in consequential sanctions ranging from shame to legal impediments and denial of privileges. As has been previously argued, this is a significant burden for white-collar offenders and contributes to their high disutility of conviction alone. If, as can be accepted, one of the objectives of criminalization is to socialize offenders and society at large, the shaming element that inevitably accompanies criminal conviction might meet that objective without the need for incarceration.⁷⁹ The law could stop at conviction without imposing any punishment because the shame might offer sufficient deterrence and retributive advantages.⁸⁰ The shame of conviction might alone serve as a sufficient punishment and incarceration

77. See Paul J. Hofer & Mark H. Allenbaugh, *The Reason Behind the Rules: Finding and Using the Philosophy of the Federal Sentencing Guidelines*, 40 AM. CRIM. L. REV. 19, 61–62 (2003).

78. Robinson & Darley, *supra* note 65, at 471–77 (stating that law can play a role in socialization).

79. See generally Eric Rasmusen, *Stigma and Self-Fulfilling Expectations of Criminality*, 39 J.L. & ECON. 519 (1996).

80. See *id.* at 532 (arguing that the penalty might equal zero in the absence of a trial or when only probation results but, even without a sentence, arrest and conviction alone generate stigma).

would be a waste of resources.⁸¹ Corporate governance offenders are likely to experience significant detriment in terms of loss of employment opportunities and social exclusion and might internalize the values sought to be conveyed by the law even without going to jail.⁸² Consequential sanctions, which can include shaming, withholding of esteem, shunning, and negative voting by investors and other market participants, can also modify behavior in desirable ways.⁸³ Shame-enforcers frequently seek to attach negative labels to an offender,⁸⁴ create the offender's reputation as a bad actor,⁸⁵ label actors as being disloyal to shareholders' interests, exclude those actors from other employment involving trust,⁸⁶ cause economic harm to offenders by seeking disgorgement of ill-gotten gains, and deprive offenders of any opportunity to hold prestigious positions.⁸⁷ These actions are ultimately aimed at norm-internalization by the offender and observers.

81. *Id.* at 534.

82. *Id.* at 537. Some are only satisfied by imprisonment. See 148 CONG. REC. 12,642 (daily ed. July 11, 2002) (statement of Sen. Byrd) (“[S]omebody ought to go to jail, and the doors should be locked and the keys thrown away. Throw away the keys. It really would not be too severe a punishment for some of these four-flushers.”).

83. Studies also show that the ability to express punishment has important implications for cooperative behavior. Astrid Hopfensitz & Ernesto Reuben, *The Importance of Emotions for the Effectiveness of Social Punishment* 19 (Tinbergen Institute, Discussion Paper No. 05-075/1, 2005), available at <http://ssrn.com/abstract=775524> (“[I]ndividuals who are willing to punish are also willing to keep on cooperating. This guaranties that, as long as these individuals have the opportunity to punish, cooperation can be sustained. Furthermore this kind of individuals [sic] might help cooperation emerge, even if it was initially rare. In addition, the same type of people is necessary to support punishment in the presence of retaliation. If retaliation deters individuals from using the punishment mechanism, cooperation can unravel.”).

84. See 148 CONG. REC. 12,642 (daily ed. July 11, 2002) (statement of Sen. Byrd) (“The President apparently is so miffed with these corporate ‘wrongdoers’ that he has elevated them in his rhetoric to a bad-guy level that is almost, but not quite as bad, as al-Qaeda’s ‘evildoers.’ Almost the same level: perhaps not quite.”).

85. SEC v. First Pac. Bancorp, 142 F.3d 1186, 1194 (9th Cir. 1998) (“Sands, a sophisticated businessman and a lawyer, has engaged in numerous activities in violation of the securities laws and basic notions of right and wrong. . . . We need not sort out whether his principles are just plain wrong, or whether he is afflicted with akrasia . . .”).

86. See Troy Wolverton, *AFL-CIO’s Throw-the-Bum-Out Call Gets Cool Reception*, THESTREET.COM, Sept. 26, 2003, <http://www.thestreet.com/stocks/troywolverton/10116076.html> (describing a call by the AFL-CIO for Kenneth Langone, a director of the NYSE board who defended Richard Grasso’s compensation package, to be dropped from the board of GE and four other public companies).

87. In *First Pac. Bancorp*, 142 F.3d at 1194, the defendant argued the bar against him holding office as director was against the public interest because it would prevent him from serving on the boards of charities. The court responded thus:

Perhaps he is right that charities will not want to place him in positions of high visibility and prestige. If so, and if Sands does have a genuine interest in doing charitable works, we are certain that he can continue his charitable involvement

Norm-internalization for white-collar offenders is enabled by the significant detriment in terms of loss of employment opportunities and social exclusion experienced. A variant of this idea is captured by Kenneth Dau-Schmidt, who calls it preference-shaping.⁸⁸ Dau-Schmidt writes:

Preference shaping, on an individual, organizational, and societal level, is an important human endeavor. It has been identified as a primary or secondary goal of childrearing, education, religion, advertising, public service announcements, legislation, and . . . criminal punishment. . . . [It is essential] that the person or group of people who are endeavoring to affect another's preferences have some legitimate claim to authority over the person, or at least have the confidence of the person.⁸⁹

CEOs are particularly suited for desirable behavior modification through the operation of social sanctions because of this very feature—their dependence on approval from diverse constituencies and the value placed on reputation.⁹⁰

Shaming has salience for corporate governance offenders because of their dependence on group membership. The targets of shaming are members of professional associations who possess licenses that allow them to carry on certain kinds of economic activity. Frequently, these professional licenses and certifications are privileges that can be taken away by the relevant authority.⁹¹ Such legal impedi-

in a less prestigious, but just as worthy, capacity. We touch on this argument because it underscores the purblindness of Sands

Id. at 1194.

88. Dau-Schmidt, *supra* note 10, at 14–15 (“If peoples’ preferences are compatible, no one’s preferences will be frustrated, and there will be no need to expend resources on precautionary measures.”).

89. *Id.* at 17. *See also id.* at 18 (“By characterizing a behavior as good or bad rather than just inexpensive or expensive, the authority figure indicates need for a fundamental change in the basis upon which the affected person makes decisions.”).

90. *See* Sandeep Gopalan, *Changing Social Norms and CEO Pay: The Role of Norms Entrepreneurs*, 39 RUTGERS L.J. 1 (2007).

91. The Ninth Circuit explained:

The district court has broad equitable powers to fashion appropriate relief for violations of the federal securities laws, which include the power to order an officer and director bar. In addition to the court’s inherent equitable powers, the Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (Remedies Act) authorizes the court to order an officer and director bar “if the person’s conduct demonstrates substantial unfitness to serve as an officer or director.” In determining whether to order the bar, a court may consider: “(1) the ‘egregiousness’ of the underlying securities law violation; (2) the defendant’s ‘repeat offender’ status; (3) the defendant’s ‘role’ or position when he engaged in the fraud; (4) the defendant’s degree of scienter; (5) the defendant’s economic stake in the violation; and (6) the likelihood that misconduct will recur.”

First Pac. Bancorp, 142 F.3d at 1193 (citations omitted).

ments to the offender holding offices involving trust can be finely calibrated to achieve incapacitation in much the same way that jail does.⁹² Even if impediments are not imposed, it is unlikely the individual will be able to find similar employment following conviction. Prestige goods are also likely to be denied in non-professional contexts because these offenders are also members of social groups which view conviction with distaste.⁹³ Membership conditions and interactions after admittance present ideal conditions for deploying shaming as esteem is vital for profitable interactions.⁹⁴ Even if some offenders are not affected by shaming, other observers might see the disutility of the alleged offense and modify their behavior.⁹⁵ Membership in these groups is intrinsically related to the possession of a good reputation, and the gate-keeping function served by these groups might obviate the need for incarceration by delivering the same behavioral change.⁹⁶

White-collar offenders have a variety of agents who can impose shaming and other social sanctions including investors, other directors, employees, the media, politicians, and potential employers. Their position relative to the offender reduces the risk of retaliation by the offender and facilitates internalization.⁹⁷ Indeed, certain shamers, such as the courts, are completely immune from retalia-

92. See *SEC v. Patel*, 61 F.3d 137, 142 (1995) (discussing the court's discretion to bar service of an officer or director conditionally or unconditionally for a limited amount of time or permanently).

93. See, e.g., Rasmusen, *supra* note 79, at 521 (noting "people [may] feel moral repugnance for criminals and choose to incur personal costs rather than interact with them").

94. Jonathan Macey, *Delaware: Home of the World's Most Expensive Raincoat*, 33 *HOFSTRA L. REV.* 1131, 1134 (2005) ("[Directors] do not like to be made the object of public scorn and ridicule.").

95. Dan M. Kahan, *What Do Alternative Sanctions Mean?*, 63 *U. CHI. L. REV.* 591, 639 (1996). Professor Kahan argues that shaming has the effect of shaping preferences. If individuals are shamed for contravening a particular asserted norm, other observers will modify their own behavior to fit that asserted norm. *Id.*

96. See Donald C. Langevoort, *The Human Nature of Corporate Boards: Law, Norms, and the Unintended Consequences of Independence and Accountability*, 89 *GEO. L.J.* 797, 813 (2001) (noting media coverage makes directors fear liability even more than they ought). Langevoort's "hypothesis is that under certain predictable circumstances, executives will overestimate the risk of liability. There are a number of possible reasons. One is that newspapers and business periodicals highlight dramatic instances of such suits, and hence the threat of liability." *Id.* at 823; see also Alexander Dyck & Luigi Zingales, *The Corporate Governance Role of the Media*, in *THE RIGHT TO TELL: THE ROLE OF MASS MEDIA IN ECONOMIC DEVELOPMENT* (R. Islam ed., 2002) (writing that corporate executives act appropriately because they do not want to be portrayed by the media as "the bad guys").

97. See Hopfensitz & Reuben, *supra* note 83, at 19 ("If retaliation deters individuals from using the punishment mechanism, cooperation can unravel.").

tion.⁹⁸ They also possess significant advantages over other shamers.⁹⁹ First, they have authority conferred by law. Unlike other shamers, the offender is in a decidedly inferior position to the court at every level. Second, a court's findings have certain other positive attributes derived from the legal process. One of these attributes is legitimacy. Another is finality. After the appeals process is exhausted, the verdict of the court is final and any shame that follows cannot be changed.

Shame-targets can respond to shaming with anger and contempt at the shamers.¹⁰⁰ Conviction serves as a focal point for shaming in that it emboldens individuals to impose social sanctions. Collective opinion concretizes around the conviction and holds out the offender as an object of shame. Those who previously were afraid or hesitant to shame draw strength from the conviction. This is because doubt about the guilt of the offender is largely removed by the court's verdict. Indignation and anger-based responses by the offender are less likely to be tolerated following conviction than before. If the focal point created by the conviction yields effective follow-up shaming by other actors, then it serves to reinforce the message and yield sticky norm-internalization.¹⁰¹

Shaming meshes neatly with the white-collar crime debate because it addresses the expressive gap in legal sanctions.¹⁰² Imprison-

98. See, e.g., *In re* Memorandum of Decision of Judicial Conference Comm. on Judicial Conduct and Disability, 517 F.3d 558 (U.S. Jud. Conf. 2008) (holding judges have absolute immunity from civil liability for their decisions).

99. Certain shamers, like politicians, appear to have little effect on those they seek to shame. During the Senate Hearings on the PCAOB, Senator Byrd said:

[O]ne finds disconcerting the acute lack of shame—the acute lack of shame—S-H-A-M-E—on the part of some of these corporate executives. Former Enron CEO Jeffrey Skilling told the House Energy and Commerce Oversight Subcommittee that Enron had tight control on financial risk, but that he could not be expected to oversee everything and “close out the cash drawers . . . every night.” Can you imagine that kind of statement? I think it was Wordsworth who said: No matter how high you are in your department, you are responsible for what the lowliest clerk is doing.

148 CONG. REC. 12,642 (daily ed. July 11, 2002) (statement of Sen. Byrd).

100. Contempt and indignation by the offender are often counterproductive. For example, Senator Byrd had this to say about Skilling's testimony to a House committee: “So here is an individual who tells a House committee he cannot be expected to oversee everything and close out the cash drawers every night—such a stunning, irresponsible, arrogant attitude on the part of a chief executive.” *Id.*

101. See Gopalan, *supra* note 90, at 22 (noting that “[t]he role of influential individuals or groups in socializing or selling the norm is the missing link” to proper internalization).

102. Chad Flanders, *Shame and the Meanings of Punishment*, 55 CLEV. ST. L. REV. 609, 611–12 (2006) (“The law does not exist merely to allocate benefits and burdens; it also *says* things through its actions. . . . It is not as if society punishes by inflicting suffering and then stating in words that it does not approve of the offender's conduct. Rather, the punish-

ment and fine sanctions are crude in their application and do not serve to convey the emotions aroused by the actions of corporate offenders. Frequently, for most indirect, non-dangerous offenses, all that society wants is that these emotions be ventilated, and for the offender to be prevented from re-offending rather than to see the offender go to jail or be made to suffer financial loss.

In the Skilling-type case, what is the point of sending the excessively optimistic CEO to jail or imposing a fine? Civilized society recognizes that the CEO's conduct is not worthy of jail time and that fines are crude matches for their actions. Any sanction, if it is to be meaningful and reflective of a sophisticated system, must match the message that society is trying to convey to the offender and be proportional to the offense. Imprisoning Skilling for 292 months then is an inappropriate tool for what society really wants to do. Conviction ought to suffice because it serves the expressive function of the law insofar as it tells the offender he has acted in a way that meets with society's disapproval and conveys the consequences of such conduct to other observers. It leaves other consequences to individual members to administer.

I have written in previous work about the need for internalization of the underlying norm if shaming is to work.¹⁰³ If offenders charged with violating accounting rules do not believe their conduct was wrongful, then they are likely to be angered by the imposition of a shame sanction rather than feel remorse. Even if they change their actions following the shaming because they realize the disutility created, this reformation is unlikely to be sustainable. Resentment and anger are likely to motivate them to find new ways to break the rules. This problem could be partially addressed by incapacitating them from holding similar positions of trust through the use of legal impediments.

I have also discussed, in previous work,¹⁰⁴ the various objections to shaming and do not restate those arguments here except to address one objection—the lack of process protections.¹⁰⁵ This line of scholar-

ment is the expression of condemnation: Society gives out harsh punishments for serious crimes because it wants to condemn those crimes in no uncertain terms. This is to say that, conventionally, hard treatment is society's way of expressing disapproval of criminal acts. Words alone are not good enough; the walls of a prison are.”).

103. Gopalan, *supra* note 90.

104. Sandeep Gopalan, *Shame Sanctions and Excessive CEO Pay*, 32 DEL. J. CORP. L. 757 (2007).

105. Seth F. Kreimer, *Sunlight, Secrets, and Scarlet Letters: The Tension Between Privacy and Disclosure in Constitutional Law*, 140 U. PA. L. REV. 1, 5–12 (1991).

ship contends that the lack of process might lead to shame sanctions being imposed on the innocent.¹⁰⁶ Further, there is no architecture to make the amount of shame proportional to the wrong committed by the offender resulting in over shaming or under shaming. In some cases, lack of process might inflict too much, irreversible punishment.¹⁰⁷ In addition, those undertaking the shaming are not subject to any accountability mechanisms.¹⁰⁸ While these objections have some merit, they can be overcome to a significant degree here because shaming is consequent upon a determination of blameworthiness by a court. This determination protects against the political deployment of shame sanctions. Trade unions and employee groups might have self-interested reasons to target CEOs. What is criminal conduct to a left-wing trade union might not be so for many other market participants and the deployment of shame sanctions based on political ideologies could be a threat to their efficacy. Similarly, the media could engage in witch hunts without undertaking significant effort to establish guilt. If, however, shaming follows conviction or results from a finding of guilt by a regulatory agency, professional association, or stock exchange, then much of the due process problem can be negated.

V. Skilling's Case

A. The Case

At the peak of its success, Enron was “The World’s Leading Energy Company” and an iconic symbol of American capitalism.¹⁰⁹ In just the span of a decade, it underwent enormous transformation. By 1990, Enron was primarily a pipeline company with 3000 employees, a market capitalization of \$3 billion, and revenues of about \$5 billion.¹¹⁰ By 1999, it had 18,000 employees, offices in 30 countries, a market capitalization of \$22 billion, and revenues over \$40 billion—

106. Toni M. Massaro, *Shame, Culture, and American Criminal Law*, 89 MICH. L. REV. 1880, 1938 (1991).

107. See Tim Eaton, *Prosecutor Kills Himself in Texas Raid Over Child Sex*, N.Y. TIMES, November 7, 2006, available at <http://www.nytimes.com/2006/11/07/us/07pedophile.html?ex=1320555600&en=9a849fc4db0d28ce&ei=5088&partner=rssnyt&emc=rss> (The suicide of a prosecutor who allegedly solicited a person he believed to be thirteen years of age following a Dateline NBC sting is a sobering reminder of the dangerous consequences.).

108. See James Q. Whitman, *What is Wrong with Inflicting Shame Sanctions?*, 107 YALE L.J. 1055, 1088 (1998) (worrying that shaming confers too much “enforcement power to a fickle and uncontrolled general populace”).

109. Brief of Defendant-Appellant, *supra* note 4, at 15.

110. *Id.* at 24.

almost 90% of which came from Jeff Skilling's Wholesale business.¹¹¹ During this period of time, Enron's shareholders received almost 500% return on their investment.¹¹² This transformation was widely acclaimed. Amongst its many awards, Enron was lauded as *Fortune's* "Most Innovative Company in America" for four consecutive years.¹¹³

All this achievement collapsed in an extraordinary sequence of events that was said to epitomize corporate corruption at its worst. Consequences for Enron's employees and the city of Houston were drastic. On "Black Monday," over 4000 Houston Enron employees lost their jobs.¹¹⁴ Over the course of the following months, thousands more lost their jobs until the company, once Houston's largest employer, had only enough employees to administer the bankruptcy. Enron stock plummeted to its nadir, rendering many employees' 401(k) accounts worthless. Savings accumulated over lifetimes were rendered naught. When the trial of Skilling and Enron Chairman and CEO Ken Lay commenced, it became apparent that several jurors knew someone—family, friends, neighbors, co-workers, clients, fellow churchgoers—who was harmed by Enron's collapse.¹¹⁵ Many jurors had suffered financial losses to the tune of thousands of dollars.¹¹⁶ In their responses, several jurors noted "the far reaching impact on the business community," the "extremely negative impact on [Houston's] charitable and arts organizations," and the damage to "Houston[']s real estate market."¹¹⁷

Through 1996, Jeff Skilling headed Enron's Wholesale business, which he founded in 1990 as its first and only employee.¹¹⁸ In 1997, Skilling became Enron's President and Chief Operating Officer, and joined the Board of Directors.¹¹⁹ In February 2001, he was appointed Enron's CEO.¹²⁰ On August 14, 2001, in an end to his meteoric career, he resigned from the company.¹²¹ Skilling was indicted in 2004 along with former Enron Chairman and CEO Ken Lay and former

111. *Id.*

112. *Id.* at 25.

113. *Id.*

114. *Id.* at 125.

115. Defendants' Renewed Motion for Change of Venue and Related Relief at 16–18, *United States v. Skilling*, Crim. No. H-04-25 (S.D. Tex. Jan 1, 2006).

116. *Id.* at 18.

117. *Id.* One juror said: "Was there anyone in Houston not affected in some way?" *Id.*

118. Brief of Defendant-Appellant, *supra* note 4, 15.

119. *Id.*

120. *Id.*

121. *Id.*

Enron Chief Accounting Officer Richard Causey.¹²² On December 28, 2005, just weeks before trial, Causey pled guilty to one count of securities fraud.¹²³ Skilling and Lay's trial began in Houston on January 30, 2006.¹²⁴ On May 25 2006, the jury convicted Skilling on nineteen counts: one count of conspiracy to commit securities or wire fraud; twelve counts of securities fraud; five counts of false statements to auditors; and one count of insider trading.¹²⁵ He was acquitted on nine counts of insider trading.¹²⁶ Thereafter, Skilling was sentenced to 292 months in prison and ordered to pay \$45 million in restitution.¹²⁷ Critical to this Article's argument regarding moral wrongfulness and harm, Skilling was charged not with causing Enron's bankruptcy, but instead misrepresenting Enron's financial condition from 1999 to 2001.¹²⁸

Unlike the other *bete noire*, Enron CFO Andrew Fastow, Skilling was not accused of stealing from Enron. Further, the trial showed that Fastow, by his own admission, had concealed his thefts from Skilling. Given the nature of Skilling's personality and marriage to Enron's success, there was no case that Skilling had sabotaged the company's interests to benefit his own. The Enron Task Force, which had been set up to investigate and bring to justice those who were responsible for Enron's collapse did not deny that Skilling "loved the company," "was very committed" and "dedicated" to it, and "had the best interests of Enron in mind."¹²⁹

Despite these facts, the indictment alleged that, starting in late 1999, Skilling spearheaded a massive conspiracy to deceive investors about Enron's financial health by manipulating the company's financial results and lying about the performance of its businesses.¹³⁰ The indictment alleged this conspiracy included almost 125 people, from

122. Superseding Indictment, *United States v. Causey*, No. H-04-25 (S.D. Tex. Jul. 7, 2004).

123. Associated Press, *Ex-Enron Officer Given 5 1/2 Years in Prison*, N.Y. TIMES, Nov. 16, 2006, at C3. Causey has since been sentenced to five and one-half years in prison. *Id.*

124. Brief of Defendant-Appellant, *supra* note 4, at 15.

125. Judgment in a Criminal Case at 1-3, *United States v. Skilling*, Crim. No. H-04-25 (S.D. Tex. Oct. 25, 2006).

126. *Id.* at 1.

127. *Id.* at 4, 7.

128. Brief of Defendant-Appellant, *supra* note 4, at 16.

129. *Id.* at 17.

130. Brief for the United States as Appellee at 10, *United States v. Skilling*, 554 F.3d 529 (5th Cir. 2009) (No. 06-20885). Fastow testified: "[A]t Enron the culture was and the business practice seemed to consistently be to do transactions that maximized the financial reporting earnings as opposed to . . . maximizing the true economic value of the transaction." *Id.*

Enron's senior management to entry-level employees to professionals at several establishments in the legal, banking, and finance sectors.¹³¹ The Task Force contended the conspiracy's objective had been to pump up Enron's stock price artificially by regularly reporting financial information that met or exceeded Wall Street analysts' expectations, trumpeting Enron's successes, and concealing its failures.¹³²

The indictment alleged that Skilling and his co-conspirators engaged in five areas of fraud. First, by manufacturing earnings and hiding losses through fraudulent transactions involving LJM, a special purpose entity whose general partner was Enron CFO Andrew Fastow.¹³³ Second, by raiding reserves in one quarter and taking extra reserves in another in order to report earnings that exceeded or met with analysts' expectations.¹³⁴ Third, by misrepresenting the nature of the Wholesale business as a "logistics company" that yielded stable, sustainable earnings, when it was really a risky "trading company" whose profits depended on speculative bets on energy prices.¹³⁵ Here, the government alleged that spin-doctoring Wholesale as a "logistics company" made a difference to how the market valued it.¹³⁶ Allegedly, Skilling was aware of this fact and told Enron Broadband Service ("EBS") CEO Ken Rice that the stock would "get whacked" if the fact that it was a risky trading company was apparent to the market.¹³⁷ The government also alleged that Skilling shifted losses from other divisions to Wholesale in order to convey the appearance they were financially sound, when they were not, so as to attract further investment.¹³⁸

Fourth, by concealing the failure of the Retail business (Enron Energy Services ("EES")) by using a "resegmentation" to shift Retail's losses into Wholesale, then stating EES was "firmly on track."¹³⁹ EES was created by Enron to sell natural gas to customers in deregulated markets. It belied its initial expectations of being profitable and was struggling financially. The problems were compounded by the distress

131. Gov't Statement in Compliance with Court's Order Dated November 2, 2004, *United States v. Skilling*, Crim. No. H-04-25 (S.D. Tex. Nov. 19, 2004).

132. Brief for the United States as Appellee, *supra* note 130, at 33–38.

133. Fastow testified that Skilling told him: "I'll make sure you're all right on the project. You won't lose any money." *Id.* at 43. Fastow opined that Enron's failure to disclose these supposed "guarantees" made its financial statements false. *Id.*

134. The Task Force argued that reserves were manipulated to hit earnings targets in three separate quarters: 4Q 1999; 2Q 2000; and 4Q 2000. *Id.* at 33–39.

135. *Id.* at 23.

136. *Id.* at 23–24.

137. *United States v. Skilling*, 554 F.3d 529, 535 (5th Cir. 2009).

138. *Id.* at 535.

139. *Id.* at 537.

faced by Californian utility companies that owed EES substantial amounts that had already been booked as profits under the mark-to-market accounting rules.¹⁴⁰ When the utilities did not pay up in late 2000, the government alleges that instead of booking several hundreds of millions in losses pursuant to the accounting rules, Skilling conspired to hide the losses in Wholesale.¹⁴¹ This ensured EES continued to smell of roses. Similarly, in March 2001, EES's losses were buried in Wholesale following the California energy crisis when the California Public Utilities Commission imposed a surcharge that could not be passed on to customers.¹⁴² This hurt Enron to the tune of hundreds of millions of dollars.¹⁴³ Notwithstanding these machinations, EES's financial condition did not improve and its losses in 2001 alone exceeded \$700 million.¹⁴⁴

And finally, by concealing the failure of EBS by falsely stating it was "healthy" and "growing fast."¹⁴⁵ As is evident at first blush, the statements at issue were remarkably like puffery rather than criminal fraud.¹⁴⁶ In some cases they were bad business decisions based on hindsight, but were they worthy of imprisonment?¹⁴⁷

140. *Id.* at 535.

141. *Id.*

142. *Id.*

143. *Id.*

144. The Task Force alleged Skilling concealed the failure of Enron's relatively new Retail unit, Enron Energy Services, by moving hundreds of millions in alleged losses from Retail to Wholesale. Brief for the United States as Appellee, *supra* note 130, at 12. The Task Force also claimed Skilling had misled analysts by failing to tell them that the real purpose of the reorganization was to hide losses, and instead telling them it was done for efficiency "to get the best . . . hands working risk management." *Id.* at 30. Skilling was also told the accounting and disclosures were appropriate. *Id.* at 61.

145. The Task Force said Skilling misrepresented the outlook of EBS's business and the sources of its revenues. *Id.* at 31-32.

146. Brief of Defendant-Appellant, *supra* note 4, at 98 ("In our Bandwidth Intermediation Business, we are *making excellent progress* in creating a commodity market for bandwidth.").

147. Skilling's testimony is revealing:

I'll make the last one argument for Broadband because people criticize me about Broadband, and I will take the criticism. We—certainly, we made a mistake. But it wasn't big. I mean, it was a billion dollars. We invested a billion dollars in the Broadband business. If it had worked, it could have been worth \$30 billion. It didn't work. We lost a billion dollars, but if you can make those kinds of bets, that's the kind of the risk you [should be taking] as a corporation. And if you do a lot of [deals with a] downside of a billion and upside of 30 [billion], you're doing a good job for your shareholders in the long run, in my opinion. This one didn't work.

Tom Kirkendall, *Reacting to Gladwell's Enron Article*, HOUSTON'S CLEAR THINKERS, Jan. 10, 2007, http://blog.kir.com/archives/2007/01/reacting_to_gla_1.asp.

The government also alleged that Skilling made misrepresentations to investors during several conference calls.¹⁴⁸ The relevant ones are:

January 22, 2001: Skilling told investors “the situation in California had little impact on fourth quarter results. Let me repeat that. For Enron, the situation in California had little impact on fourth quarter results.”¹⁴⁹ Further, “nothing can happen in California that would jeopardize” earnings targets.¹⁵⁰ The government claimed that at the time of these statements, Skilling knew the California utilities were not in a position to pay Enron and that a loss of hundreds of millions of dollars would have to be booked.¹⁵¹ Allegedly, at this call, Skilling was a mute bystander when Mark Koenig, Enron’s Director of Investor Relations, stated that non-core business revenues were a “fairly small” amount of EBS’s earnings.¹⁵² The government contends that this was false.¹⁵³

January 25, 2001: Skilling told Enron’s annual analysts conference that EES and EBS had “sustainable high earnings power.”¹⁵⁴ He also claimed that Enron was “not a trading business. We are a logistics company.”¹⁵⁵

March 23, 2001: Following news on the market that EBS was in dire straits, and Enron’s falling stock price, Skilling convened a special conference call with analysts. He claimed EBS was “having a great quarter,” and Enron was “highly confident” that EES would meet its earning target.¹⁵⁶ The government alleges Skilling knew this was not true.¹⁵⁷

April 17, 2001: Skilling claimed on another conference call that the transfer of EES’s risk-management books to Wholesale was because there was “such capability in our wholesale business that were [sic]—we just weren’t taking advantage of that in managing our portfolio at the retail side. And this retail portfolio has gotten so big so fast that we needed to get the best—the best hands working on risk management there.”¹⁵⁸ The government alleges the motivation was to conceal losses. During the call, Skilling also said that the “first quarter results were great” at EES, despite them being down, and with regard to EBS, claimed there was a “very strong development of the marketplace in the commoditization of

148. Brief for the United States as Appellee, *supra* note 130, at 26–33.

149. *Id.* at 25.

150. *Id.*

151. *Id.*

152. *Id.* at 26.

153. *Id.*

154. *Id.*

155. *Id.*

156. *Id.* at 27–28.

157. *Id.* at 28.

158. *Id.* at 30.

bandwidth. . . . [W]e're feeling very good about the development of this business."¹⁵⁹

July 17, 2001: Skilling stated EES "had an outstanding second quarter" and was "firmly on track to achieve" its earnings targets, despite EES posting a loss of hundreds of millions of dollars.¹⁶⁰ He again claimed EES's reorganization was undertaken for efficiency reasons (not to hide losses as alleged by the government).¹⁶¹

Skilling also allegedly raided Wholesale's reserve accounts flush from its profitable second half of 2000, which allowed Enron to put over \$850 million in its own reserves.¹⁶² The government contended the decision to put the funds into reserves was not based on feared potential liabilities, but rather to use it instrumentally to manipulate earnings.¹⁶³ Skilling allegedly used it to hit a specific earnings target to meet Wall Street expectations.¹⁶⁴ The government also argued Skilling was aware Enron's SEC filings contained false statements, including the recognition of money from a Nigerian barges deal as legitimate income despite the fact that it was not really a sale.¹⁶⁵ In addition, it was alleged that Enron misled Arthur Andersen by giving it management-representation letters knowing them to be false, thus undermining the auditing process.¹⁶⁶ In particular, these representations claimed that all related party transactions were disclosed when they were not.¹⁶⁷

B. Mens Rea

The prosecution based its case largely on self-serving testimony provided by witnesses who had everything to gain by pinning blame on Skilling for what were, at worst, bad business judgments.¹⁶⁸ During the trial, Skilling's defense was that he did not break any laws, and

159. *Id.* at 30–31.

160. *Id.* at 33.

161. *Id.*

162. *United States v. Skilling*, 554 F.3d 529, 538 (5th Cir. 2009).

163. *Id.* at 537–38.

164. *Id.* at 538.

165. *Id.* at 540.

166. *Id.* at 541.

167. *Id.*

168. Press Release, U.S. Dep't of Just., Former Enron Chief Financial Officer Andrew Fastow Pleads Guilty to Conspiracy to Commit Securities and Wire Fraud, Agrees to Cooperate with Enron Investigation (Jan. 14, 2004), available at <http://www.fbi.gov/dojpressrel/pressrel04/enron011404.htm> ("The remaining 96 criminal charges against Fastow from a May 2003 indictment are pending, and will be dismissed if the government determines that Fastow has cooperated fully and truthfully."); see also Kristen Hays, *Enron's Top Accountant Gets 5 Years, Causey's Term Is Third-Harshes, but Less Than Time Sought in Plea Deal*, HOUS. CHRON., Nov. 16, 2006, at A1.

that his actions were undertaken as a loyal employee of Enron.¹⁶⁹ He also claimed he had always relied on competent legal and accounting advice.¹⁷⁰ With regard to the statements made during the calls to analysts, Skilling claimed these were immaterial. Most importantly, Skilling attacked the reliability of the government's key witnesses—Andrew Fastow and Ben Glisan. Fastow's testimony is the most problematic. Fastow claimed that he and Skilling had a shared understanding about Cuiaba¹⁷¹ and the Nigerian barges, which Fastow referred to as “bear hugs.”¹⁷² Skilling contended these were misinterpretations made by Fastow.¹⁷³

“In May 2006, the jury found Skilling guilty of nineteen counts: one count of conspiracy,¹⁷⁴ twelve counts of securities fraud,¹⁷⁵ five counts of making false statements,¹⁷⁶ and one count of insider trad-

169. Brief of Defendant-Appellant, *supra* note 4, at 3.

170. *Id.* at 9.

171. *Skilling*, 554 F.3d at 542.

172. *Id.* at 542.

173. *Id.* He also attacked the “Global Galactic” list kept by Fastow. *Id.*

174. The conspiracy counts required that the defendants:

[K]nowingly and intentionally conspire (1) to willfully and unlawfully use and employ manipulative and deceptive contrivances and directly and indirectly (i) to employ devices, schemes and artifices to defraud; (ii) to make untrue statements of material fact and omit to state facts necessary in order to make the statements made, in the light of the circumstances under which they were made, no misleading; and (iii) to act or engage in acts, practices, and courses of conduct which would and did operate as a fraud and deceit upon members of the investing public

Superseding Indictment at 36, *United States v. Causey*, No. H-04-25 (S.D. Tex. Jul. 7, 2004).

175. The securities fraud count required that the defendants:

[W]illfully and unlawfully use and employ manipulative and deceptive contrivances and directly and indirectly (i) employ devices, schemes and artifices to defraud; (ii) make untrue statements of material fact and omit to state facts necessary in order to make the statements made, in the light of the circumstances under which they were made, no misleading; and (iii) engage in acts, practices, and courses of conduct which would and did operate as a fraud and deceit upon members of the investing public in connection with purchases and sales of Enron securities and by the use of the instruments of communication in the course of interstate commerce and the mails.

Id. at 40.

176. This count required that the defendants:

[K]nowingly and wilfully made and caused to be made materially false and misleading statements, and [had] omitted to state material facts necessary in order to make the statements made . . . no misleading, to accountants retained by Enron . . . in connection with the audit and examination of financial statements of Enron as required by law to be made, and the preparation and filing of documents . . . required to be filed with the SEC

Id. at 50.

ing.”¹⁷⁷ Skilling won a minor victory by being acquitted of nine counts of insider trading.¹⁷⁸ Ken Lay also met a harsh fate and was convicted of every count against him.¹⁷⁹ The district court sentenced Skilling to spend 292 months in imprisonment, three years under supervised release, and to pay \$45 million in restitution.

C. Overzealous Prosecution?

As is apparent, the sheer size of a company like Enron necessitates the creation of large sub-structures comprising several layers of subordinates, governance systems, and internal and outside advisors to ensure the proper structuring and vetting of business transactions and decisions. It is to these substructures that CEOs and senior executives turn for most of the decisions they are required to make. They act upon the basis of the advice provided by these processes, and the success of any company is owed in substantial measure to the efficacy of these decision-making systems. It is indeed rare for CEOs to run companies the size of Enron as personal fiefdoms where every decision is made on their own accord and without consultation with and reliance on advisors, internal and external. It is also not typical that CEOs actively seek out personal accounting or legal advice in addition to those offered by these substructures. It makes sense, then, for them to rely on expert advice, and for such reliance to be useful in showing they did not possess the required knowledge or intent to engage in criminal conduct.

Enron and Skilling were no different in terms of consultation and reliance. Skilling had been advised that the Raptors transactions,¹⁸⁰

177. *United States v. Skilling*, 554 F.3d 529, 542 (5th Cir. 2009). The trafficking count required that Skilling had:

[K]nowingly and wilfully used and employed manipulative and deceptive devices and contrivances, by use of means and instrumentalities of interstate commerce, in violation of Rule 10b-5 of the Rules and Regulations of the SEC . . . in that he engaged in acts, practices and courses of business which would and did operate as a fraud on members of the investing public Specifically, while in possession of material non-public information, [Skilling] sold shares of Enron stock and generated total proceeds of \$62,626,410.90.

Superseding Indictment at 59, *United States v. Causey*, No. H-04-25 (S.D. Tex. Jul. 7, 2004).

178. *Skilling*, 554 F.3d at 542.

179. *United States v. Lay*, 456 F. Supp. 2d 869, 870 (S.D. Tex. 2006).

180. In defense of Skilling, defense counsel notes:

The Raptors were four structured finance transactions used to hedge . . . the risk in [] various Enron investments. Each Raptor was capitalized by \$400 million in Enron stock and a \$30 million investment by LJM. . . . Fastow testified there was a “secret oral side deal”: LJM was to receive its \$30 million investment back, plus

for example, had been reviewed and approved by Arthur Andersen's technical accounting group in Chicago.¹⁸¹ His decision to support the structures was based on presentations made to him and to the full Board, which had voted to approve them.¹⁸² Skilling's testimony showed that he was never told the vehicles were improper.¹⁸³ As one senior prosecuting lawyer wrote:

In a trial involving allegations of earnings manipulation and disputes over the defendants' respective understandings of the application of often arcane accounting rules, proof of criminal intent was of critical importance. Assembling such evidence proved challenging, however, as both Skilling and Lay clearly relied on the advice of inside and outside counsel, as well as their auditors.¹⁸⁴

This was to be of no avail. The Task Force's case against Skilling was predicated primarily on the testimony of cooperating witnesses, who had all agreed to testify in exchange for leniency and favorable sentencing recommendations.¹⁸⁵ In addition, there is some substance to the feeling that witnesses, who could have provided exculpatory testimony for Skilling, were intimidated by the Task Force with threats of indictment.¹⁸⁶ Throughout the trial, there was no other direct evidence that linked Skilling with the alleged crimes.

The duplicity of the prosecution can be seen in one simple instance involving document destruction—the very basis for the government ringing the death knell for Andersen. Skilling had moved for an order requiring the production of the raw interview notes of Fastow's examination by the government in order to determine how much of

\$11 million in profits, before any hedging could begin. . . . Skilling testified that the Raptors were a self-insurance structure that protected the value of the assets hedged by Enron: if Enron's stock in the Raptors went up, the hedging vehicles (or self-insurance policy) would be capitalized with gains on Enron's stock; if Enron's stock went down, Enron's stock contribution to the vehicles would be protected through the proceeds from the put.

Brief of Defendant-Appellant, *supra* note 4, at 29–31.

181. *Id.* at 31.

182. *Id.*

183. Counsel for the United States in the Skilling trial explains:

On June 28, 1999, Skilling and Fastow presented LJM to the Enron Board of Directors for approval. During the discussion, a board member asked if there were risks to Enron from LJM, and he was told that the biggest risk was "Wall Street Journal risk" because it would "look terrible" if the media found out about LJM. At the meeting, the Board granted Fastow a waiver of Enron's conflict-of-interest rules and approved Enron's investment in LJM.

Brief for the United States as Appellee, *supra* note 130, at 40–41.

184. John C. Hueston, *Behind the Scenes of the Enron Trial: Creating the Decisive Moments*, 44 AM. CRIM. L. REV. 197, 197–98 (2007).

185. Brief of Defendant-Appellant, *supra* note 4, at 20.

186. *Id.* at 178–90.

what was produced had been massaged to support their case. In response, the Task Force refused to produce the notes and, in a bizarre move, claimed it had destroyed all the materials including the electronic files from computer hard drives. How was this different from the document destruction engaged in by Andersen? There is a strong implication that the Task Force had destroyed the electronic copies in an attempt to prevent Skilling from attacking the credibility of Fastow and to gain an unfair advantage in the trial. The difference between aggressive prosecution and obstruction of justice is equally thin here.

D. Deliberate Ignorance

A further taint on the prosecution was the employment of the “deliberate ignorance” doctrine to get over the minor problem of Skilling believing his actions were legal.¹⁸⁷ In *United States v. Heredia*,¹⁸⁸ the court justified the use of the doctrine, stating that “‘knowingly’ in criminal statutes is not limited to positive knowledge, but includes the state of mind of one who does not possess positive knowledge only because he consciously avoided it.”¹⁸⁹ In another case, the court concluded that to “[c]onstru[e] knowingly in a criminal statute to include willful blindness to the existence of a fact is no radical concept in the law.”¹⁹⁰ Key to the doctrine is that the conduct of the defendant “denotes a conscious effort to avoid positive knowledge of a fact which is an element of an offense charged . . . choosing to remain ignorant so he can plead lack of positive knowledge in the event he should be caught.”¹⁹¹ In order to apply the doctrine, the conduct

187. The doctrine allows a defendant to be found to have acted knowingly if he knew with high probability that a certain fact existed and acted deliberately to avoid obtaining information that would confirm the fact. The instruction provided to the jury during the trial was:

The word “knowingly,” as that term is used throughout these instructions, means that the act was done voluntarily and intentionally, not because of mistake or accident. You may find that a defendant had knowledge of a fact if you find that the defendant deliberately closed his eyes to what would otherwise have been obvious to him. While knowledge on the part of the defendant cannot be established merely by demonstrating that the defendant was negligent, careless, or foolish, knowledge can be inferred if the defendant deliberately blinded himself to the existence of a fact.

United States v. Skilling, 554 F.3d 529, 548 n.19 (5th Cir. 2009).

188. 483 F.3d 913 (9th Cir. 2007).

189. *Id.* at 918 (quoting *United States v. Jewell*, 532 F.2d 697, 702 (9th Cir. 1976)).

190. *United States v. Evans*, 559 F.2d 244, 246 (5th Cir. 1977).

191. *United States v. Restrepo-Granda*, 575 F.2d 524, 528 (5th Cir. 1978).

must be “Don’t tell me, I don’t want to know.”¹⁹² Given its broad sweep, courts have repeatedly emphasized that it should only be given “in the ‘rare’ instance where there is significant evidence of deliberate ignorance.”¹⁹³ The concern is as follows:

Because the instruction permits a jury to convict a defendant without a finding that the defendant was actually aware of the existence of illegal conduct, the deliberate ignorance instruction poses the risk that a jury might convict the defendant on a lesser negligence standard—the defendant *should* have been aware of the illegal conduct.¹⁹⁴

This is dangerous territory. There is a clear distinction between failing to ascertain information about a fact and knowing the fact. If the former equals the latter, there is little sense in requiring the prosecution to prove knowledge. It dilutes the requirements of knowledge to the breaking point. As the court noted in *United States v. Mendoza-Medina*,¹⁹⁵ “the deliberate ignorance instruction poses the risk that a jury might convict the defendant on a lesser negligence standard—the defendant *should* have been aware of the illegal conduct.”¹⁹⁶ Even setting aside the serious problems with the doctrine, its application in this case does not satisfy the two required conditions: “(1) the defendant was subjectively aware of a high probability of the existence of the illegal conduct; and (2) the defendant purposely contrived to avoid learning of the illegal conduct.”¹⁹⁷ Further, subjective awareness of illegal activity and purposeful contrivance to avoid learning of illegal conduct can be inferred from the defendant’s inactivity in the face of a “routine and repeated pattern of suspicious transactions.”¹⁹⁸ As the Fifth Circuit Court of Appeals stressed,

[W]here there is no such evidence, a district court should not give the instruction because there is no basis for finding deliberate ignorance. In such a case, it is usually harmful, because it is likely to lead the jury to find that the defendant had the requisite knowledge when he in fact did not.¹⁹⁹

Is deliberate ignorance even possible in a corporation the size of Enron with its army of lawyers, accountants, and consultants? Expert

192. *Skilling*, 554 F.3d at 548 (quoting *United States v. de Luna*, 815 F.2d 301, 302 (5th Cir. 1987)).

193. *Id.* at 549.

194. *Id.* at 548 (citing *United States v. Lara-Velasquez*, 919 F.2d 946, 951 (5th Cir. 1990)).

195. 346 F.3d 121 (5th Cir. 2003).

196. *Id.* at 132.

197. *Lara-Velasquez*, 919 F.2d at 951.

198. *United States v. Nguyen*, 493 F.3d 613, 619–22 (5th Cir. 2007).

199. *Skilling*, 554 F.3d at 549.

advice is routinely provided in such large corporations, and there is no evidence that Skilling deliberately sought to avoid getting advice.²⁰⁰ There are few facts that justify the conclusion there was a pattern of suspicious transactions that ought to have caused Skilling to act. Skilling's defense had never been that he did not know the facts, but rather that his actions were not illegal. As the Fifth Circuit put it, "[h]e claims that he 'agreed' at trial with the government's characterization of him as knowing everything that went on at Enron. He maintains that his 'defense was not that he was unaware of fraud, but that there was no fraud.'"²⁰¹ This strikes at the root of deliberate ignorance because if he had full knowledge of the actions but did not believe them to be illegal, there is no case. There is obviously no need to contrive to avoid finding out about legal facts. Having come this far, the Fifth Circuit gets it horribly wrong:

Even if Skilling is correct that there is little evidence to support a deliberate ignorance instruction, however, any error in the district court's decision to give the instruction was harmless. This is because the peril to be avoided in cases reversing convictions based on the deliberate ignorance instruction is not present here. By his own admission, Skilling claims that he knew of the allegedly illegal acts, so there is no risk that a jury would rely on the deliberate ignorance instruction to find that he should have known of the acts. Consequently, even if the district court erred in giving the deliberate ignorance instruction in the sense that the instruction was "not supported by evidence," any such error was necessarily harmless.²⁰²

This is a terrible travesty. The court completely confuses Skilling's case—he did not contend that he knew that the acts were illegal.²⁰³ Rather, the claim was that he knew of the acts, which were all legal!²⁰⁴

Skilling appealed, contending *inter alia*, that the government used an invalid theory of "honest-services fraud" to convict him. The jury had convicted Skilling of one count of conspiracy. The problem was that it did not specify which object of the conspiracy had been used to convict, and given that one of them was honest services, Skill-

200. Brief of Defendant-Appellant, *supra* note 4, at 9.

201. *Skilling*, 554 F.3d at 549.

202. *Id.* at 550 (citation omitted).

203. The court quoted from Skilling's reply brief and said, "[t]here were very few instances where [he] denied that the alleged conduct happened—he agreed statements were made, conversations occurred, transactions were approved. Indeed, most were a matter of written record. [His] position was that the conduct was not criminal or wrongful," but the court still got it wrong! *Id.* at 549 n.20.

204. "His defense was *not* that he was unaware of fraud, but that there was no fraud. As we told the jury in opening statement: 'This is not a case of hear no evil, see no evil. This is a case of there was no evil.'" Brief of Defendant-Appellant, *supra* note 4, at 24.

ing sought to overturn the conviction alleging this was an invalid theory.²⁰⁵

E. Honest Services

The government's case against Skilling was based on a conspiracy to deceive investors about the true performance of Enron's businesses by cooking the books to increase reported earnings, reduce reported losses, maintain an investment-grade credit rating, and improve the price of Enron's stock. In doing so, Skilling allegedly breached his fiduciary duty of "honest services."²⁰⁶ The truth is that Skilling's conviction is founded on no evidence as to when, how, or why the conspiracy was hatched, or anything beyond self-serving testimony from Fastow claiming he committed any crime. The conviction chillingly demonstrates the need to clarify the "honest services" theory if it is to serve any function in distinguishing risky business behavior from criminal behavior.

In *United States v. Brown* ("Brown"),²⁰⁷ the government's honest services theory was rejected by the court in similar circumstances. In *Brown*, Enron and Merrill Lynch employees were alleged to have engaged in a conspiracy to defraud Enron and its shareholders by "parking" the now infamous "Nigerian barges" with Merrill Lynch for six months to artificially boost Enron's earnings.²⁰⁸ It was alleged that Merrill paid \$7 million to acquire equity in the barges to help Enron post \$12 million in earnings to meet its forecasts.²⁰⁹ The state's case was that this was a sham transaction because Enron executives orally promised Merrill a flat fee of \$250,000 and a guaranteed fifteen annual rate of return for the six months it was required to hold the asset.²¹⁰ Further, the government alleged the transaction was in the nature of a lease rather than a sale because Enron executives promised it would buy back Merrill's interest if no third party could be found.²¹¹ The court was unsympathetic to the government's claims be-

205. The prosecution's case contained three objects of the conspiracy: (1) to commit securities fraud, (2) to commit wire fraud to deprive Enron and its shareholders of money and property, and (3) to commit wire fraud to deprive Enron and its shareholders of the honest services owed by its employees. Brief for the United States as Appellee, *supra* note 130, at 84–85.

206. *Id.* at 77–78.

207. 459 F.3d 509 (5th Cir. 2006).

208. *Id.* at 513.

209. *Id.*

210. *Id.*

211. *Id.*

cause the facts did not show that the defendants had acted at the expense of the company or had engaged in bribery and self-dealing.²¹² Rather, their actions were to the benefit of Enron. According to the majority,

We do not presume that it is in a corporation's legitimate interests ever to misstate earnings—it is not. However, where an employer intentionally aligns the interests of the employee with a specified corporate goal, where the employee perceives his pursuit of that goal as mutually benefitting him and his employer, and where the employee's conduct is consistent with that perception of the mutual interest, such conduct is beyond the reach of the honest-services theory of fraud as it has hitherto been applied.²¹³

The test for a deprivation of honest services case, which is laid down in *United States v. Rybicki*,²¹⁴ is that the defendant be secretly acting for his own interest while purporting to act for the employer. This is consistent with the Seventh Circuit's ruling in *United States v. Bloom*.²¹⁵

There is no evidence that Skilling engaged in bribery or self dealing. Nor did he act secretly for his own benefit at the expense of Enron. There was no deprivation of honest services because, if anything, Skilling's interests were too closely aligned with Enron's. Unless the causal link between Enron's ultimate collapse and Skilling's alleged actions are conclusively established, the harm was not directly caused by Skilling's alleged crimes. In fact, the immediate consequences of Skilling's actions were that Enron and its shareholders benefited. The government sought to distinguish Skilling's case from *Brown* by contending:

[Skilling] violated his fiduciary obligations and his duty to provide Enron and its shareholders with honest services by setting an improper corporate goal—improperly maintaining and increasing Enron's share price and maintaining its credit rating—and then scheming to achieve that goal by committing, directing, and causing others to commit a series of fraudulent actions that Skilling could not have perceived as being consistent with any legitimate corporate interest.²¹⁶

They also alleged that in *Brown* the offenders were “low-level” employees who were acting on orders from superiors whereas Skilling

212. *Id.* at 522.

213. *Id.*

214. 354 F.3d 124, 141–42 (2d Cir. 2003) (en banc).

215. 149 F.3d 649, 656–57 (7th Cir. 1998).

216. Brief for the United States as Appellee, *supra* note 130, at 80.

was not acting in pursuance of goals imposed on him by those above him.²¹⁷

The Fifth Circuit analyzed *Brown* as creating the following ingredients for establishing liability:

[W]hen an employer (1) creates a particular goal, (2) aligns the employees' interests with the employer's interest in achieving that goal, and (3) has higher-level management *sanction improper conduct to reach the goal*, then lower-level employees following their boss's direction are not liable for honest-services fraud. Thus, we reversed the convictions of the employees in *Brown* because they were acting both in the corporate interest and at the direction of their employer.²¹⁸

Thereafter, the court manufactured an exception for honest services fraud thus: "In essence, *Brown* created an exception for honest-services fraud where an employer not only aligns its interests with the interests of its employees but also sanctions the fraudulent conduct, i.e., where the corporate decisionmakers, who supervised the employees being prosecuted, specifically authorized the activity."²¹⁹

By their own logic, the employer, Enron, should sanction the fraudulent conduct and the decisionmaker, Skilling, should have specifically authorized the activity. Given the facts of the case, this might be a bridge too far. Nevertheless, the Fifth Circuit would have none of it:

Skilling misconstrues our holding in *Brown* . . . because he fails to recognize the manner in which the court in *Brown* explicitly distinguished [*United States v. Gray*]²²⁰. . . *Gray* and *Brown* present different facts; in *Gray*, the basketball coaches acted on their own volition, without any direction from their supervisors, while in *Brown*, a lower-level Enron employee acted at the direction of Fastow, who as a decisionmaker had the authority to tell his employee that Enron sanctioned the particular fraud in question. The difference is that in *Brown*, the employee undertook the specific fraud in question *at the direction of the employer*, while this did not occur in *Gray*. In essence, because the Enron decisionmaker in *Brown* sanctioned the specific fraudulent conduct of its employee, the employee (and the other conspirators) did not deprive Enron of its honest services. Thus, for example, had the basketball coaches in *Gray* showed that the President of Baylor University or other decisionmakers specifically directed their fraudulent conduct, then they would not have been liable for honest-services fraud.²²¹

217. *Id.* at 80–81.

218. *United States v. Skilling*, 554 F.3d 529, 545 (5th Cir. 2009).

219. *Id.*

220. 96 F.3d 769 (5th Cir. 1996).

221. *Id.* at 546 (footnote omitted).

Having come up with this sword, the court then foisted Skilling on it:

Skilling's convictions must stand. First, Enron created a goal of meeting certain earnings projections. Second, Enron aligned its interests with Skilling's personal interests, e.g., through his compensation structure, leading Skilling to undertake fraudulent means to achieve the goal. Third—and fatally to Skilling's argument—no one at Enron sanctioned Skilling's improper conduct. That is, Skilling does not allege that the Board of Directors or any other decisionmaker specifically directed the improper means that he undertook to achieve his goals. Of course, a senior executive cannot wear his "executive" hat to sanction a fraudulent scheme and then wear his "employee" hat to perpetuate that fraud. Therefore, it is not a matter of Skilling setting the corporation's policy himself. Instead, the question is whether anyone who supervised Skilling specifically directed his actions—such as how Fastow sanctioned the scheme in *Brown*. Skilling never alleged that he engaged in his conduct at the explicit direction of anyone, and therefore he cannot avail himself of the exception from *Brown*.²²²

There is one problem: Where is the "fraudulent" action undertaken by Skilling to achieve the corporate goal of achieving earnings? There is too facile an assumption of fraud and impropriety without the evidence to back it up. The application of the honest services theory in cases where bad business decisions caused financial losses dangerously corrodes the very basis of criminal liability by conflating moral wrongfulness with risk taking. It must be clarified if it has to serve the intended purpose. Further, even upon the court's reasoning, would it not be possible to believe that the board of directors, whose task it was to supervise Skilling, sub silentio, directed and approved his actions?

As the above analysis shows, there is little morally wrongful in Skilling's conduct.²²³ There was no suggestion that Skilling had any-

222. *Id.* The court also stated:

The elements of honest-services wire fraud applicable here are (1) a material breach of a fiduciary duty imposed under state law, including duties defined by the employer-employee relationship, [and] (2) that results in a detriment to the employer. *Brown* sheds light on the employer-employee relationship by creating an exception for when the employer specifically directs the fraudulent conduct. Further, it is a sufficient detriment for an employee, contrary to his duty of honesty, to withhold material information, i.e., information that he had reason to believe would lead a reasonable employer to change its conduct. Accordingly, the jury was entitled to convict Skilling of conspiracy to commit honest-services wire fraud on these elements.

Id. at 547 (footnotes omitted).

223. As Malcolm Gladwell wrote on his website, "Can anyone explain—in plain language—what it is Jeff Skilling and Co. did wrong? . . . The question is strictly a legal one: according to the way the accounting rules were written at the time, what specific transgres-

thing to gain at the expense of Enron by his alleged crimes. In fact, all the evidence pointed to Skilling working for the success of Enron. His alleged misstatements were in the nature of sales talk and puffery, and there is no evidence there was any intention to deceive. The Skilling case demonstrates the perils of letting the notion of harm alone dictate criminalization. The enormous harm suffered by people in Houston appears to have colored the court's perceptions about the moral wrongfulness of Skilling's actions. If Skilling was indeed responsible for the harm, there were other avenues like civil suits to recover for the harm caused. The criminal law ought to require more than mere harm to deprive individuals of their liberty. If Skilling has to suffer the fate of a murderer who has killed five people (based on his sentence), surely there must be the same degree of moral wrongfulness to his actions?

To sum up, Skilling's conduct was, at worst, an aggressive interpretation of existing law. The government did not adduce any evidence that he intentionally committed acts that he knew to be wrong. It is arguable that overly optimistic and egregiously risky actions ought not to be viewed kindly by the law and that CEOs who are guilty of these faults should not be allowed to hold similar positions. If such conduct has to be criminalized upon the justification that non-consenting individuals were harmed, conviction without imprisonment could achieve the purposes of criminalization at lower cost. Skilling would have had his earning capacity destroyed by conviction alone. An order of disgorgement would have reduced him to penury. To the extent it is necessary, other legal impediments could have been imposed on him by regulatory agencies. In addition, if members of society wanted to impose other consequential sanctions, then they could do so upon conviction without sending him to jail.

Conclusion

Criminalizing risky actions undertaken by corporate fiduciaries confuses ex post harm with moral wrongfulness. The scholarly and policy-making communities conflate blameworthiness with imprisonment, explaining the inordinate focus on ratcheting up prison terms. Such a view assumes that physical confinement is essential to achieving the objectives of criminalization when the particular nature of cor-

sions were Skilling guilty of that merited twenty-four years in prison?" Malcolm Gladwell, *Enron*, GLADWELL.COM, Jan. 3, 2007, <http://gladwell.typepad.com/gladwellcom/2007/01/enron.html>.

porate governance offenders facilitates the realization of those objectives without the need for imprisonment. To the extent that criminalization is necessary, the societal goals the law articulates through the criminal law can be realized through conviction alone without the need for imprisonment. Conviction is sufficiently liberty depriving for corporate governance offenders insofar as it destroys their ability to hold fiduciary positions, thereby eliminating the possibility for further social harm. The disutility caused by conviction alone is a sufficient deterrent. If the law stops at conviction, deterrent objectives can be achieved without the need for the state to bear the cost of imprisonment. The possibility of imposing consequential sanctions satisfies the retributive dimension. Lastly, the incapacitation objective is achieved by legal impediments.

The criminal law is a blunt instrument when applied to problems created by agency costs because of the crudeness of its sanctions and their relatively high cost without demonstrable gain. Further, since white-collar wrongs are not always morally wrong, the criminal law's expressive and coercive powers are seriously undermined by the crude application of criminal sanctions. Stopping at conviction without automatic imprisonment minimizes the erosion of expressive power by facilitating the deployment of consequential sanctions like shaming, which allows for the decentralized enforcement of the asserted norms. Thus, conviction without incarceration offers the second-best alternative to decriminalization.