BUSINESS FIDUCIARY RELATIONSHIPS AND HONEST SERVICES FRAUD: A DEFENSE OF THE STATUTE

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I. INTRODUCTION

"Fraud, like many familiar concepts, is one which seems to have a perfectly obvious meaning until we try to define it."[1] This quote succinctly summarizes the essential problem Congress faced in drafting a law to prohibit fraud through the use of the mails and wire. It also highlights the problem courts have when interpreting the scope of a law meant to deal with this definitional difficulty. While it is clear that criminal law should doubtless tackle the evil that is fraud,

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[1] Milton D. Green, *Fraud, Undue Influence and Mental Incapacity*, 43 COLUM. L. REV. 176, 177 (1943).

and that Congress has the power to prohibit the use of private interstate carriers such as FedEx or UPS for the perpetuation of fraud, this still leaves the problems of 1) how one defines fraud, and 2) how one resolves the legal issues that are created when Congress enacts a statute to address it. The broad construction of the mail fraud statute, combined with prosecutors' attempts to further expand the statute with new theories of prosecution, has led some to call the mail fraud statute the prosecutor's "Stradivarius," "Colt 45," or "Uzi."[2] "Judge Ralph K. Winter noted in referring to 'various federal fraud statutes—in particular, the mail and wire fraud statutes,' that 'with regard to the statutory weapons available to prosecutors, [fraud statutes] rank by analogy with hydrogen bombs on stealth aircraft.'"[3] The discomfort with the provision's breadth reflected in these analogies suggests the fundamental paradox of the statute: one of the principal purposes of anti-fraud provisions, on both the state and federal level, is to protect the integrity of commerce, but if it is applied too expansively, there could be potential chilling effects on a wide range of legitimate business activities. This concern is even more pronounced in the context of intangible rights fraud as defined in 18 U.S.C. § 1346, which states that "for the purpose of this chapter, the term 'scheme or artifice to defraud' includes a scheme or artifice to deprive another of the intangible right of honest services."[4]

This Note examines the nexus between "honest services" mail fraud and the important fiduciary relationships commonly found in commercial enterprise[5] and makes a

[2] Ellen S. Podgor, *Criminal Law Symposium: Mail Fraud: Redefining the Boundaries*, 10 ST. THOMAS L. REV. 557, 558 (1998), (quoting Michael W. Carey et al., *Federal Prosecution of State and Local Public Officials: The Obstacles to Punishing Breaches of the Public Trust and a Proposal for Reform, Part One*, 94 W. VA. L. REV. 301 (1992)).

[3] *Id.* at 558.

[4] 18 U.S.C. § 1346 (2000).

[5] Other articles have addressed the connection between the public right to honest services from state and/or local government employees or officials. *See* Geraldine Szott Moohr, *Mail Fraud and the Intangible*

recommendation on how courts can continue to uphold the validity and strength of § 1346 while addressing its current weaknesses. This Note is principally focused on the exploration of the connection between violations of private fiduciary obligations and "honest services" fraud in the criminal law. It is concerned, on the one hand, with the possible chilling effects of the uncertainty of where criminal liability arises and, on the other, the need for a strong anti-fraud statute. The solution proposed in this Note integrates the two major approaches courts have developed in dealing with § 1346.

One need only engage in a perfunctory examination of any corporations casebook to appreciate the possible ramifications of the connection between honest services mail fraud and fiduciary obligations. The courts have long grappled with violations of fiduciary obligations in regard to the duties of care and loyalty, and the possibility of federal criminal penalties for lapses of such duties presents a number of interesting questions. One of the most important is the following: Will federal law support the felony criminal prosecution of someone who commits mere negligence or an oversight with no intention of exploitation? Such a prosecution would be unlikely, especially when one considers that the mens rea element of honest services mail fraud requires either specific intent to commit the fraud or a deliberate attempt to conceal an unintentional failure to meet one's fiduciary obligation to provide honest services. Either way, the potential defendant must consciously *act*.

Rights Doctrine: Someone to Watch Over Us, 31 HARV. J. ON LEGIS. 153 (1993). It is the way in which the mail fraud statute and its honest services provision in particular can address sophisticated economic misconduct that is central to this Note. *See* Peter J. Henning, *Maybe It Should Just Be Called Federal Fraud: The Changing Nature of the Mail Fraud Statute*, 36 B.C. L. REV. 435, 438 (1995) ("The [mail fraud] statute became a strategic tool in fighting political corruption and increasingly sophisticated economic misconduct that in some way employed the postal service, almost regardless of the mailing's relationship to the underlying scheme.").

Though the threat to the unwary has been exaggerated,[6] there is little doubt that in interpreting the mail fraud statute, courts must balance compelling interests: concerns regarding vagueness and overbreadth on one end of the spectrum and, on the other, the need to maintain the vigor of the statute in confronting new and innovative schemes to defraud.

On a more general level, for the worlds of business and commerce, there is a high premium on avoiding the possibility of criminal offenses; a more clear—yet still strong—honest services mail fraud statute could supply some certainty. There is also a premium on avoiding civil liability, and civil enforcement of honest services fraud laws through RICO provides another example of the importance of this issue for the business world.[7]

This Note will analyze the complexities in balancing the public's interest in using the mail fraud statute to prosecute those engaging in sophisticated economic fraud with the public's equally strong interest in upholding the rule of law and the necessity for reasonable notice. Part II reviews the history and development of the mail fraud statute and the evolution of the intangible rights theory that gave birth to § 1346. Part III addresses circumstances in which prosecutions involving business fiduciary relationships have occurred and may occur. Part IV concludes with the argument that the mail fraud statute can serve as a valuable weapon in the prosecutor's arsenal to protect consumers and

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[6] In addition to the fears of vagueness and lack of notice, the specter of potential unintentional or negligent violations of § 1346 creating criminal liability has concerned commentators calling for the repeal of the statute. In contrast, this Note attempts to address concerns about the viability of the honest services mail fraud statute as a matter of law, rather than as a matter of policy.

[7] 18 U.S.C. §§ 1961, 1964 (2000). These two sections define racketeering activity and provide for civil remedies, respectively. Racketeering activity includes violations of § 1341 which relates to mail fraud and presents the opportunity for plaintiffs to establish civil RICO claims with mail fraud predicates.

those who depend on fiduciaries from those who would intentionally breach their obligations.

II. THE EXPANSION OF THE MAIL FRAUD STATUTE

A. Basic History of the Mail Fraud Statute

One cannot appreciate the importance of § 1346 without an understanding of § 1341, the mail fraud statute.[8] First passed in 1872 as a part of a broader series of provisions that revised laws relating to the post office,[9] its primary concern was to protect the integrity of the postal service from activities by counterfeiters, swindlers, and other scoundrels.[10] The only actus reus required for a violation of the 1872 statute was that the defendant mail or receive a letter; the remainder of the offense rests in the defendant's intent to execute a scheme to defraud by use of the mails.[11] In *Stokes v. United States,* the Court stated that to prove a violation of the 1872 mail fraud statute, the prosecutor must establish

> (1) that the persons charged must have devised a scheme to defraud; (2) that they must have intended to effect this scheme, by opening or intending to open correspondence with some other persons through the post office establishment, or by inciting such other

[8] After all, § 1346 modifies the definition of "scheme or artifice to defraud" as included in § 1341. For a more comprehensive review of the history and development of the mail fraud statute see Jed S. Rakoff, *The Federal Mail Fraud Statute (Part 1)*, 19 DUQ. L. REV. 771 (1980); John C. Coffee, Jr., *Some Reflections on the Criminalization of Fiduciary Breaches and the Problematic Line Between Law and Ethics*, 19 AM. CRIM. L. REV. 117, 126 (1981). *See also* PETER W. LOW & JOSEPH L. HOFFMAN, FEDERAL CRIMINAL LAW 160-261 (1997).

[9] LOW & HOFFMAN, *supra* note 8, at 161.

[10] Gregory D. Jones, Note, *Primum Non Nocere: The Expanding "Honest Services" Mail Fraud Statute and the Physician-Patient Fiduciary Relationship*, 51 VAND. L. REV. 139, 142 (1998).

[11] 18 U.S.C. §§ 1961-1964 (2000).

> person to open communication with them; (3) and that, in carrying out such scheme, such person must have either deposited a letter or packet in the post office, or taken or received one therefrom.[12]

Shortly after the enactment of the 1872 statute, a schism developed among the lower courts between those strictly construing the statute and those reading it more broadly.[13]

The lack of definition of the "scheme to defraud" element is seen as a double-edged sword:

> Proponents hail the statutes as a versatile weapon against fraud—a 'catchall' device that encompasses crimes not yet recognized or well defined in other statutes. Critics argue that this strength is also a weakness because these statutes afford prosecutors too much discretion and fail to give adequate notice of exactly what type of conduct the statutes proscribe.[14]

The real question became whether or not the definition of fraud in the statute was limited by the common law definition. In *Durland v. United States*, the Supreme Court answered the question by holding that the "fraud" in the statute is broader than that of the common law because of the greater scope of the "evil sought to be remedied" by

[12] Stokes v. United States, 157 U.S. 187, 188-89 (1895), *quoted in* LOW & HOFFMAN, *supra* note 8, at 162 cmt. c. The constitutionality of the statute was tested in *Ex Parte Jackson*, where the Court upheld the statute unanimously and spoke broadly of Congress's authority to regulate what could be mailed under the postal power. 96 U.S. 727 (1877).

[13] LOW & HOFFMAN, *supra* note 8, at 164-65 (1997). In *United States v. Owens*, the court dismissed the indictment against the defendant in reliance on the mail-emphasizing language of the statute, interpreting it to be a substantive qualification on the phrase 'any scheme or artifice to defraud'; this understanding reflected the strict construction school, which required the mail to be central to the commission of the fraud. 17 F. 72 (E.D. Mo. 1883). *United States v. Jones* represents the broad construction approach, which maintained that the illegal act was the misuse of the mails to facilitate some criminal fraud possibly unrelated to the postal service itself. 10 F. 469 (C.C.S.D.N.Y. 1882).

[14] Jones, *supra* note 10, at 146 n.26.

Congress.[15] This broad interpretation of mail fraud helps explain why it "continues to be the true love of the federal prosecutor, a self-defining statute that can be used to get crooks whose behavior falls between the cracks of other statutes,"[16] a form of gap filling which "deters criminals from engaging in illicit behavior and enables courts to block new forms of fraud quickly and easily."[17] Today, to prevail on a mail or wire fraud[18] charge, the government must prove: "(1) the defendant's knowing and willing participation in a. scheme or artifice to defraud with the specific intent to defraud and (2) the use of the mails or interstate wire communications in furtherance of the scheme."[19] Though the

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[15] 161 U.S. 306 (1896); *see also* LOW & HOFFMAN, *supra* note 8, at 170-72. In *Durland*, the Court went beyond the traditional common law notion of fraud, which did not include a misrepresentation as to a future promise but required a false statement regarding an existing fact.

[16] LOW & HOFFMAN, *supra* note 8, at 161.

[17] Todd E. Molz, Note, *The Mail Fraud Statute: An Argument for Repeal by Implication*, 64 U. CHI. L. REV. 983, 984 (1997). Molz argues that the mail fraud statute can maintain its strength in its flexibility, while its overbreadth can be addressed by allowing later statutes addressing particular types of fraud to override the mail fraud statute.

[18] The wire fraud statute provides:

> Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio, or television communication in interstate or foreign commerce, any writings, signs, signals, pictures, or sounds for the purpose of executing such scheme or artifice, shall be fined under this title or imprisoned note more than five years or both.

18 U.S.C. § 1343 (2000).

"The mail and wire fraud statutes have been construed identically in relation to the issues discussed here. Therefore, any discussion of mail fraud is applicable to wire fraud claims." Jones, *supra* note 10, at 140 n.13 (citing Carpenter v. United States, 484 U.S. 19, 25 n.6 (1987)).

[19] United States v. Sawyer, 85 F.3d 713, 723 n.6 (1st Cir. 1996) ("The use of the mails or wires to further the fraudulent scheme need only be 'incidental.'"); *see also* United States v. Grandmaison, 77 F.3d 555, 556 (1st Cir. 1996).

"use of the mails" element no longer plays a limiting role in the scope of the mail fraud statute, the "scheme to defraud" element "has been central to the application of the statute"[20] and is increasingly important in determining the reach of honest services fraud under § 1346.

B. Development of the Intangible Right to Honest Services and § 1346

It was not long after the 1889 amendment to the mail fraud statute[21] that lower courts began interpreting a "scheme to defraud" to include the deprivation of intangible rights. In *Hammerschmidt v. United States*, the Supreme Court held that the terms "to defraud" included the intangible right to honest services.[22] This doctrine has since been used by federal prosecutors to combat political corruption at the state and local levels, finding a duty to provide honest services inherent in the official's relationship

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[20] Jones, *supra* note 10, at 144.

[21] The text of the amendment is quite long and can be found in LOW & HOFFMAN, *supra* note 8, at 157-68. The amendment made two clear changes:

> It recited a laundry list of counterfeit schemes—tied to the slang of the day—that were meant to be included in the statute. . . . And it elaborated on the types of mailing that counted, as well as where the mailing could occur . . . it indicated congressional acceptance of the idea that each mailing constituted a separate violation of the statute and that there was no substantive limit on the number of offenses that could be spun out of a single scheme to defraud.

Id. at 168.

[22] 265 U.S. 182, 188 (1924). *Hammerschmidt* interpreted 18 U.S.C. § 371 not § 1341; however, as Justice Stevens notes in his dissent in *United States v. McNally*, there is no basis for interpreting the term "defraud" in § 371 as something different than its use in § 1341. 483 U.S. 350, 369 (1987). *McNally* established that § 1341's use of "defraud" did not include the intangible rights fraud seen under § 371. Congress's enactment of § 1346 has settled this question definitively by statutorily creating the right to honest services.

to the public.[23] For example, with kickbacks, the government usually maintains that a public official who receives undisclosed kickbacks violates citizens' rights to honest and faithful services.[24] "Because the kickback is considered material information, which should be disclosed under fiduciary obligations, the nondisclosure results in the public official's breach of fiduciary duty."[25]

The private sector has also been subject to the strictures of the honest services fraud statute. The duty to provide honest services in the private sector originates in the fiduciary relationship between the defendant and a victim. The relationships subject to this statute include employee-employer, attorney-client and trustee-beneficiary, among others.[26] The trend toward enforcement of fiduciary relationships through the mail fraud statute on the theory of the right to "honest services," however, came to a crashing halt in 1987 in *McNally v. United States.*[27]

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[23] *See* Jones, *supra* note 10, at 146. For examples of cases in which state and local officials were prosecuted for honest services fraud, *see id.* at 146 n.28, citing United States v. Waymer, 55 F.3d 564, 566-67 (11th Cir. 1995) (member of city education board); United States v. Silvano, 812 F.2d 754, 760 (1st Cir. 1987) (acting budget director for the city of Boston); United States v. Brown, 540 F.2d 364, 373-77 (4th Cir. 1976) (governor of Maryland). *See also* Laura Ellers & Harvey Silikovitz, Note, *Ninth Survey of White Collar Crime: Mail and Wire Fraud*, 31 AM. CRIM. L. REV. 703, 708-11 (1994) (reviewing the intangible rights doctrine).

[24] *See* Jones, *supra* note 10, at 147.

[25] *Id.*

[26] *Id.* at 148-49. For examples of cases involving the prosecution of honest services mail fraud for a breach of a private fiduciary duty see Shushan v. United States, 117 F.2d 110 (5th Cir. 1941) (considered the first reported case based on this theory); United States v. Bronston, 658 F.2d 920 (2d Cir. 1981) (finding mail fraud where an attorney gave legal aid to a client who was competing for a franchise with another client represented by the firm); United States v. Weiss, 752 F.2d 777, 785 (2d Cir. 1985) (corporate officer committed mail fraud when he formulated a plan involving phony cash-generating transactions to disguise a cash fund from shareholders at the company which involved payments of non-performed legal services and purchases of speculative stock). *See also* Jones, *supra* note 10, at 148 n.34.

[27] 483 U.S. 350 (1987).

McNally involved the prosecution of a former public official and a private individual for an alleged violation of § 1341. McNally, the private individual, was involved in a scheme in which the state's agent for securing worker's compensation, Wombwell Insurance, agreed to share certain commissions with other insurance companies specified by a Howard Hunt (chairman of the state's Democratic Party) as a condition for renewing Wombell's contract. The scheme then involved the formation of a sham insurance company for the sole purpose of sharing the commissions distributed by Wombwell.[28] The jury convicted petitioners on both mail fraud and conspiracy counts and the court of appeals affirmed the convictions. The Court reversed the convictions and held that "the mail fraud statute clearly protects property rights, but does not refer to the intangible right of the citizenry to good government."[29] The thrust behind the majority's opinion was the conviction that Congress had not departed, in its numerous reenactments and amendments, from the traditional conception of the term "to defraud" stated in *Hammerschmidt*, which did not include the deprivation of "intangible rights."[30] This did not mean that the majority thought that a more expansive interpretation of the mail fraud statute that included protections for the deprivation of intangible rights like the right of honest services was an implausible reading; rather, under the principle of lenity, the Court, when confronted with two rational interpretations of a criminal statute, "one harsher

[28] The mail fraud count alleged that "petitioners had devised a scheme (1) to defraud the citizens and government of Kentucky of their right to have the commonwealth's affairs conducted honestly, and (2) to obtain, directly and indirectly, money and other things of value by means of false pretenses and the concealment of material facts." *Id.* at 353-54.

[29] *Id.* at 356.

[30] 265 U.S. 182 (1924). The definition of the words "to defraud" was "to wrong[] one in his property rights by dishonest methods or schemes," and "usually signif[ies] the deprivation of something of value by trick, deceit, chicane or overreaching."

than the other, [will] choose the harsher only when Congress has spoken in clear and definite language."[31]

The dissent by Justice Stevens phrased the question presented by the case as: "whether that prohibition [in § 1341] is restricted to fraudulent schemes to deprive others of money or property, or whether it also includes fraudulent schemes to deprive individuals of other rights to which they are entitled."[32] Justice Stevens maintained that the Court's holding "shows no fidelity to Congress' words or purpose."[33] Though the legislative history of the mail fraud statute was sparse, Justice Stevens maintained that the conception of fraud at the time it was enacted included crimes beyond those targeting property: "examination of the way the term 'defraud' has long been defined, and was defined at the time of the statute's enactment, makes it clear that Congress' use of the term showed no intent to limit the statute to property loss."[34] He also argued that upon review of the general history of Congress' reactions to the courts' decisions interpreting the mail fraud statute also supported the broader reading of § 1341, and that the statute was enacted

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[31] *McNally*, 483 U.S. at 359-60, (quoting United States v. Bass, 404 U.S. 336, 347 (1971)).

[32] *Id.* at 362.

[33] *Id.* at 366.

[34] *Id.* at 370. Justice Stevens cited three broad 19th-century definitions of the term "defraud": Justice Story defined fraud as "applied to every artifice made use of by one person for the purpose of deceiving another," or as "any cunning, deception, or artifice used to circumvent[,] cheat, or deceive another." *Id.* at 370 (quoting 1 J. STORY, EQUITY JURISPRUDENCE § 186, at 189-90 (1870)). Another contemporary dictionary defined "to defraud" as "to withhold from another that which is justly due to him, or to deprive him of a right by deception or artifice." 1 BOUVIER'S LAW DICTIONARY 530 (1870). Thirdly, Anderson, in his 1893 Dictionary of Law, defined it as "to cheat; to deceive; to deprive of a right by an act of fraud . . . to withhold from another what is justly due him, or to deprive him of a right, by deception or artifice." W. ANDERSON, A DICTIONARY OF LAW 474 (1893). Thus, under Justice Stevens' analysis, the term "defraud" included a broader legal meaning than under the traditional common law when the statute was passed in the late 19th century.

in a time when laws like the Sherman Act, the civil rights legislation, and the mail fraud statute were

> written in broad general language on the understanding that the courts would have wide latitude in construing them to achieve the remedial purposes that Congress had identified.[35] The wide open spaces in statutes such as these are most appropriately interpreted as implicit delegations of authority to the courts to fill in the gaps in the common-law tradition of case-by-case adjudication.[36]

In response to the majority's use of the doctrine of lenity in this case, Justice Stevens posits that

> [w]hen considering how much weight to accord to the doctrine of lenity, it is appropriate to identify the class of litigants that will benefit from the Court's ruling today. They are not uneducated, or even average, citizens. They are the most sophisticated practitioners of the art of government among us. . . . [T]he array of government executives, judges, and legislators who have been accused, and convicted, of mail fraud under the well-settled construction of the statute that the Court renounces today are people

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[35] There are, no doubt, some who may be disturbed by Congress delegating such crime-making authority to the courts and argue that such a delegation violates the separation of powers. However, this article will not focus on this issue because it is simply too broad and has not been a focus of the courts when interpreting § 1346.

[36] *McNally*, 483 U.S. at 372-73. Justice Stevens goes on to quote from Judge Posner's decision in *United States v. Holzer*:

> [t]he argument depends on the view that the meaning of fraud in the mail-fraud statute was frozen by the conception of fraud held by the framers of the statute when it was first passed back in the nineteenth century. This seems to us the opposite and equally untenable extreme from arguing that fraud is whatever strikes a judge as bad, but in any event the 'intangible rights' concept that the argument attacks is too well established in the courts of appeals for us to disturb.

816 F.2d 304, 310 (7th Cir. 1987).

> who unquestionably knew that their conduct was unlawful.[37]

The Court, however, ultimately backpedaled somewhat from its disavowal of intangible rights in *McNally* by later upholding intangible *property* rights in *Carpenter v. United States,* weakening the legal support for the *McNally* decision.[38]

Justice Stevens' contention that the majority in *McNally* was ignoring congressional history with regard to the mail fraud statute proved to be prescient. If the majority were seeking a clear congressional mandate supporting the intangible rights theory of mail fraud, then the passage of § 1346 in 1988 provided it.[39] Thus, *McNally* was overruled and the line of lower court decisions that it set aside was reinstated.[40]

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[37] *McNally*, 483 U.S. at 375 n.9. This position will be used later to maintain that the doctrine of lenity is not adequate to prevent the full force of the "intangible services" doctrine from applying to the private fiduciary context.

[38] 484 U.S. 19, 25-26 (1987).

[39] *See supra* Part I and note 4.

[40] *See* LOW & HOFFMAN, *supra* note 8, at 198; *see also* Jones, *supra* note 10, at 154 ("The sparse legislative history suggests that § 1346 was intended to restore the law to its pre-*McNally* status."). Representative Conyers, the floor sponsor of the amendment, stated "[t]his amendment restores the mail fraud provision to where that provision was before the *McNally* decision. . . . This amendment is intended to overturn the *McNally* decision." *Id.* at 154 n.55 (quoting 134 CONG. REC. H11,251 (daily ed. Oct. 21, 1988) (statement of Rep. Conyers)). The Senate Judiciary Committee also supports such an interpretation for it stated "[t]his section overturns the decision in *McNally v. United States* . . . . The intent is to reinstate all the pre-*McNally* case law pertaining to the mail and wire fraud statutes without change." *Id.* at 154 n.55 (quoting 134 CONG. REC. S17,360-62 (daily ed. Nov. 10, 1988) (statement of Sen. Biden)). *See also* David B. Sweet, Annotation, *Validity, Construction, and Application of the Federal Mail Statute*, 97 L. Ed. 2d 863 (1987); United States v. Frost, 125 F.3d 346 (6th Cir. 1997). Some circuits will refer to pre-*McNally* case law to help them interpret the reach of § 1346; this is an avenue that has been at least facially rejected by the Second Circuit. *See* United States v. Handakas, 286 F.3d 92, 103 (2d Cir. 2002) ("This Circuit has foreclosed the use of pre-*McNally* cases as a tool for construing the revised statute . . . .").

III. BUSINESS FIDUCIARY RELATIONSHIPS AND ENFORCEMENT OF "HONEST SERVICES" FRAUD

A. Business Fiduciary Relationships

Before the benefits and costs of enforcing fiduciary relationships through § 1346 can be weighed and balanced, the fundamentals of those relationships must be examined. Examples of fiduciaries include executors, trustees, attorneys, physicians, corporate directors, and employees, but

> the common law has in fact always defined the term with deliberate imprecision and perhaps surprising expansiveness. In its most frequent formulation, the common law has said that a fiduciary relation arises 'when there is special confidence reposed in one who in equity and good conscience is bound to act in good faith and with due regard to [the] interest of [the] one reposing the confidence.'[41]

Fiduciary obligations do not descend from the heavens unbeknownst to those who owe them. There are four common situations in which a fiduciary relationship can arise:

> (1) when one person places trust in the faithful integrity of another, who as a result gains superiority or influence over the first; (2) when one person assumes control and responsibility over another; (3) when one person has a duty to act for or give advice to another on matters falling within the scope of the relationship; or (4) when there is a specific relationship that has traditionally been recognized as involving fiduciary duties, as with a lawyer and a client, or stockbroker and a customer.[42]

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[41] John C. Coffee, Jr., *From Tort to Crime: Some Reflections on the Criminalization of Fiduciary Breaches and the Problematic Line Between Law and Ethics*, 19 AM. CRIM. L. REV. 117, 150-51 (1981) (quoting BLACK'S LAW DICTIONARY 563-64 (5th ed. 1979)).

[42] BLACK'S LAW DICTIONARY 640 (7th ed. 1999).

On the one hand, concerns that fiduciary obligations are vague, and that in that vagueness resides a threat of overcriminalization, may be overblown since the instances in which a fiduciary relationship arises should not come as a surprise to anyone; this standard is not imposed on third parties negotiating at arm's length. On the other hand, what one is allowed to do in a fiduciary relationship varies from state to state, and ambiguity across jurisdictions is a pronounced problem.[43] In the corporate law context, this problem may be even more troubling because of the "internal affairs" rule which states that the law of the jurisdiction of incorporation will control all intracorporate disputes. The tension with criminal law becomes apparent when one considers that the "internal affairs" doctrine would require the law of the state of incorporation to apply to all breaches of fiduciary obligations, regardless of where the actual violations occurred. If this test were used to govern in criminal "honest services" fraud cases, "the applicable law [would have] no relationship to the community in which the conduct occurred or in which the trial will occur."[44] As Professor Coffee notes, states may engage in a race to the bottom to compete for corporate franchises and thus weaken § 1346.[45]

The problems mentioned above may not be so extreme when one considers that § 1346 criminalizes intentional violations of fiduciary obligations only as far as the duties in that relationship include that of providing "honest services."[46] In fact, even if the states were to race to the

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43 *See* Coffee, *supra* note 41, at 154-56. Professor Coffee provides the example of corporate law as an area where fiduciary duties are developed and analyzed, and "significant disparities exist among state jurisdictions." *Id.* at 154.

44 *Id.* at 156.

45 *Id.* at 157.

46 *See* United States v. Sawyer, 85 F.3d 713 (1st Cir. 1997); United States v. Sancho, 957 F. Supp. 39 (S.D.N.Y. 1997), *aff'd*, 157 F.3d 918 (2d Cir. 1998), *cert. denied*, 525 U.S. 1162 (1999), *overruled by*, United States v. Rybicki, 354 F.3d 124 (2d Cir. 2003); United States v. D'Alessio, 822

bottom as feared, *United States v. Sancho* provides legal support for the position that no such fiduciary relationship is necessary in order for criminal liability to arise under § 1346.[47] The defendant argued that criminal liability under §§ 1341 and 1346 requires a finding of a "genuine fiduciary relationship" to the entity being defrauded.[48] The appeals court found that there "is no such requirement."[49] Although the court did turn to New York law to determine whether the person consulting to the company had a duty to provide honest services and not to conceal the receipt of a bribe, it stated that "[w]e need not ask whether the duty owed is properly considered a 'fiduciary duty.' What matters is whether it comes within the statute's requirement of an 'intangible right of honest services,' and we have no doubt that it does."[50] The real issue is therefore whether the victim of the fraud possessed the right to honest services (and thus the defendant or a co-conspirator owed that duty to the victim), not whether the relationship between the parties is of a fiduciary nature under state law.[51] Federal law governs

F.Supp. 1134 (D.N.J. 1993); United States v. Brumley, 116 F.3d 728 (5th Cir. 1997).

[47] *Sancho,* 157 F.3d at 920. The issue is whether one is entitled to a right of honest services as a matter of federal law, not necessarily whether the relationship is fiduciary under state law.

[48] *Id.* at 920 n.1.

[49] *Id.* at 920.

[50] *Id.* at 921. "We therefore have no need to decide whether the consultant's duties owed to TCC were of fiduciary nature. We need only answer whether Sancho's scheme to bribe a TCC consultant to conceal the very information TCC had engaged the consultant to discover (and to conceal the bribe) constituted a scheme to deprive TCC of a right of honest services." *Id.* at 922.

[51] At least one circuit has held that federal law determines the existence of a fiduciary duty under the mail fraud statute. *See* United States v. Frost, 125 F.3d 346, 366-67 (6th Cir. 1997) (federal law governs the existence of fiduciary duty under the mail fraud statute). There the court turned to federal case law to determine what kind of fiduciary obligations an employee owed an employer, thus rendering the argument over the difference in fiduciary obligations under various state laws somewhat (though not completely) muted.

the context and situations in which honest services are owed, not state law.

B. Fiduciary Relationships and Culpability

It is important to remember that the breach of a fiduciary duty is not a criminal act.[52] If that were the case, then there would be a complete overlap between civil and criminal law. "To justify criminal penalties, the law requires that an actor be blameworthy, or deserving of punishment, and that this 'bad state of mind' and the criminal act concur."[53] "In honest services fraud, the deception lies in failing to disclose a breach of fiduciary duty to the principal."[54] The Supreme Court addressed this issue indirectly in *United States v. O'Hagan,* in which it stated that mail fraud "has long been held to require deception, not merely the breach of a fiduciary duty."[55] Deception is found in the failure to disclose the breach and in the motivation for the concealment; honest services fraud can be classified as a specific intent crime.[56] In *United States v. Paradies*, the court stated that the specific intent required by honest services mail fraud was an "intent to deceive."[57] Professor Moohr criticizes the use of this language, in that it provides very little actual substance and thus no notice to a potential defendant of the criminal mens rea.[58] While it may be true that little legal substance is being added by such a definition, it may provide enough substance for a reasonable person to know whether his or her acts are potentially criminal; in the context of a fiduciary relationship, if one is obligated to provide honest services but withholds those services and fails to make a full disclosure,

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[52] *See* Geraldine Szott Moohr, *Mail Fraud Meets Criminal Theory*, 67 U. CIN. L. REV. 1, 19 (1998).

[53] *Id.* at 20.

[54] *Id.* at 19.

[55] 521 U.S. 642, 654 (1997).

[56] Moohr, *supra* note 52, at 22. *See also* United States v. Paradies, 98 F.3d 1266 (11th Cir. 1996).

[57] *Paradies*, 98 F.3d at 1285; *see also* Moohr, *supra* note 52, at 22.

[58] Moohr, *supra* note 52, at 22.

such acts would raise red flags morally and legally. For example, it seems morally and legally apparent that if a doctor is offered a kickback for each prescription he writes for a certain drug, there would be a fiduciary duty to refuse the offer or, at the very least, to disclose the information to the patient.

In *Paradies*, the defendant was charged with conspiring with city officials, who owe fiduciary duties to the public, to commit honest services mail fraud. Paradies argued that the government, in order to prove specific intent, had to show that he knew his conduct violated the law. The court rejected this argument. One can see this rejection as reflecting the *malum prohibitum* and *malum in se* dichotomy in criminal law.[59] If a crime is merely *malum prohibitum,* then an act must not only be illegal, but the defendant must be on notice that his conduct was morally blameworthy before a conviction can arise. This makes sense when one considers that a *malum prohibitum* crime is only wrong because the state says it is wrong, not because there is anything intrinsically wrong with the act itself. However, the ignorance defense fails in *malum in se* crimes since these crimes are "evil in themselves" and thus by their very nature provide notice that the conduct is wrongful.[60] Honest services mail fraud resembles a *malum in se* crime, since there is an inherent wrongfulness in a fiduciary abusing a

[59] *See also* Cheek v. United States, 498 U.S. 192 (1991) (representing a similar dichotomy).

[60] For example, if a person commits murder, he or she cannot raise the defense that he or she did not know that the act was criminal or immoral. This would be a preposterous contention, since it is universally known that such an act is immoral. Unless the defendant is legally insane, he or she will be held liable even absent personal awareness that the murder was criminal. In the mail fraud context, some may argue that failure to provide honest services does not carry the level of universal moral opprobrium that inheres to murder. While this is undoubtedly true to a certain extent, it is common knowledge that if one is a fiduciary to another, one must not self-servingly take advantage of that relationship to exploit that person or another by purposefully lying, bribing, or committing some other dishonest action and then covering up such misdeeds.

relationship of trust in order to gain personal advantage. Thus, arguing that a particular fiduciary is not culpable because he or she did not know that his or her acts were in violation of § 1346 is off the mark; the nature of a fiduciary relationship should put a potential defendant on sufficient notice to allow the statute to survive constitutional challenge on vagueness or sufficiency of notice grounds.

One may ask whether a person who makes a good faith attempt to comply with his fiduciary duties can be prosecuted for unintentionally failing to provide honest services either through neglect or accident. The answer to that question is a definitive no. Failure to provide honest services is not a crime per se; it is only a crime if that failure is a result of an intentional breach of fiduciary obligation (which would negate any argument that the failure was an accident or unavoidable), or if one fails to provide honest services and then refuses to disclose that breach to the would-be beneficiary. Either way, the defendant must intentionally either breach their fiduciary obligation to provide honest services or, upon discovery of an inadvertent failure, exhibit an intent to conceal that failure.

C. An Application of Honest Services Mail Fraud in the Private Sector

Courts are hesitant to apply the mail fraud statute to activities in the private sector because of the possible chilling effects it could have on important economic transactions and relationships. However, it is often overlooked that honest services fraud itself has chilling effects by undermining the trust and confidence necessary to sustain fiduciary relationships.[61] Proper application of the mail fraud statute must balance these countervailing concerns. The courts have attempted to do this through various limiting techniques while also endeavoring to maintain the vigor of the statute.

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[61] *See* description of the legislative and judicial history of honest services mail fraud *supra* Part II.

1. Tort Requirement

One of the ways courts have addressed the vagueness and notice problems that have been discussed above is by reining in the scope of § 1346. For example, in *Handakas* the Second Circuit imposed a requirement, in cases where the fraud charge is based solely on § 1346, that a "scheme to harm another by the breach of a duty" must be a tort violation and not solely a contractual one.[62] The prosecution in *United States v. Handakas* was based on the defendant's violation of duties imposed upon him by New York State Labor Law and were not enforceable by an action in tort.[63] The court saw no "principled distinction between the duties breached by Handakas and the garden-variety contractual duties usually collected under the rubric of 'representations and warranties.'"[64] The court then found that it would be a violation of the defendant's due process guarantee of fair notice to hold Handakas criminally liable on the grounds that he violated a "state-mandated undertaking to pay 'prevailing rate of wages' or to furnish accurate reports of work performed."[65] However, a broader review of the facts of the case reveals that the defendant violated not only contractual but also state law duties, which means that the defendant should have had even more notice that his

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[62] United States v. Handakas, 286 F.3d 92 (2d Cir. 2002), *overruled by* United States v. Rybicki, 354 F.3d 124 (2d Cir. 2003) (en banc). The *Rybicki* court stated:

> Because we conclude that Handakas's conduct was not within the scope of section 1346, we have no occasion to conclude, as the *Handakas* panel did, that 'the intangible right to honest services' covered by section 1346 can *never* arise in that context. We note only that because of the nature of the services to be rendered in *Handakas*, an intangible right to honest services did not arise out of the contract at issue in that case.

Rybicki, 354 F.3d at 144.

[63] *Handakas*, 286 F.3d at 106.

[64] *Id.* at 106-07.

[65] *Id.* at 107.

behavior violated § 1346 and was criminal.[66] Although *Handakas* was later overruled, the approach used by the Second Circuit represents an example of one way in which courts have wrestled with ways of limiting the potential reach of the statute.

2. *United States v. Rybicki*[67] and the Circuit Split Regarding Restraining Approaches

The Second Circuit revisited the honest services mail fraud statute in *United States v. Rybicki*; the holding in that case is important when formulating either a defense or attack on honest services mail fraud. It stands for a broad reading of the mail fraud statute in affirming convictions where there was no proof that the victims suffered a tangible monetary or property loss, and it responds to many of the same arguments raised by commentators in criticizing the scope of honest services mail fraud. The defendants were personal injury lawyers who obtained favorable results, either as to timing or amount, in settling personal injury suits with the opposing insurance companies by offering a kickback to a middleman or intermediary who would approach the adjuster of the pertinent insurance company and arrange the settlement.[68] As part of the scheme, a percentage of the settlement was kicked back and shared equally by both the adjusters and the middlemen. Each of the insurance companies had policies forbidding adjusters

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[66] *See id.* at 116. Contrary to the majority's reasoning that a mere violation of a non-tort state law requirement failed to provide adequate notice, the dissent maintains that the defendant had more notice, since his behavior was also a state crime rather than simply a tort. This argument should have the same force for contractual obligations, since one would know that the duty of honest services was owed to the victim because it was spelled out in the contract, and the potential defendant had received something in exchange for the promise to provide honest services.

[67] 287 F.3d 257 (2d Cir. 2002), *aff'd en banc*, 354 F.3d 124 (2d Cir. 2003) (upholding the panel's decision, but adopting a materiality standard rather than a reasonably foreseeable standard for the Second Circuit's application of § 1346).

[68] *Id.* at 260.

from receiving any gifts or fees and required them to report any such offer, which the adjusters in this case failed to do. The participants in the scheme also expended considerable effort in disguising and concealing the payments.[69]

The government did not seek to prove that the amount of any of the settlements had exceeded what would have been reasonable for the underlying claims. However, the government did contend that the settlements were necessarily inflated above the amount that the personal injury plaintiffs (clients of the defendants) would have been willing to accept by at least the difference between the amount paid to the middlemen and adjusters.[70] In this case, the defense argued that a conviction for honest services fraud required proof of actual or intended economic or pecuniary harm to the plaintiff, which they asserted was lacking. The court rejected this argument and stated that such a reading would "vitiate § 1346 and would contravene Congress' clear intent to bring within the scope of the mail and wire fraud provisions fraudulent conduct that did not have as its object the deprivation of money or property of another."[71] Instead, the "only intent that need be proven in

[69] One could maintain that this demonstrates a "consciousness of guilt" since there would be no need to conceal legal and ethical transactions.

[70] *Rybicki*, 287 F.3d at 260.

[71] *Id.* at 261. Of course, the argument is a bit circular in this case, since the defendants must have known that, by including the adjusters and the middlemen in the division of the settlement, their piece of the pie was necessarily subtracted from someone else's rightful piece. This is akin to a defendant in a first-degree murder trial arguing that he or she should be cleared because when he or she shot a victim in the heart the accused knew—but did not intend—that death would result. Clearly, in such a case, the defendant would be found guilty, since knowledge of the harm manifests the requisite intent. The same could be said here: the defendants knew that they were engaged in an unlawful activity (or, at the very least, one that was immoral and contrary to the adjusters' obligations to the insurance agency). Vagueness and lack-of-notice are really two sides of the same legal coin. Vagueness challenges stem from the argument that the statute is so poorly written that it fails to provide adequate notice to potential defendants: "As generally stated, the void-for-vagueness doctrine requires that a penal statute define the criminal offense with sufficient

an honest services fraud is the intent to deprive another of the intangible right of honest services."[72]

Another argument raised by the appellants was that even if an intent to cause economic harm is not a required element of § 1346 honest services fraud, some economic harm must result. The court rejected this argument, as well, and held that in proving a scheme or artifice to deprive someone of the intangible right to honest services, the "government need not prove either that the defendant intended to cause the victim economic or pecuniary harm or that such harm actually resulted from the scheme to defraud."[73]

The court was unpersuaded by the argument that "honest services" mail fraud is too vague and fails to provide adequate notice to potential defendants, especially, in this case, given the fact that the appellants were attorneys who "were presumptively aware that their payments to insurance adjusters to expedite claims created improper conflicts of

definiteness that ordinary people can understand what conduct is prohibited and in a manner that does not encourage arbitrary and discriminatory enforcement." United States v. Rybicki, 354 F.3d 124 (2d Cir. 2003) (en banc) (quoting Kolender v. Lawson, 461 U.S. 352, 357 (1983)). The Second Circuit and several others have rejected general vagueness challenges to the statute. *See* United States v. Rybicki, 287 F.3d 257 (2d Cir. 2002) (citing United States v. Frega, 179 F.3d 793, 803 (9th Cir. 1999) (rejecting a vagueness challenge by an attorney convicted under § 1346 for bribing state court judge); United States v. Frost, 125 F.3d 346, 352 (6th Cir. 1997) (discounting a challenge to the statute in the context of a university professor who helped students obtain degrees by fraud in exchange for their influence in obtaining government contracts); United States v. Gray, 96 F.3d 769, 772, 776-77 (5th Cir. 1996) (rejecting a challenge in the context of a basketball coach who helped students receive academic eligibility through fraud); United States v. Castro, 89 F.3d 1443, 1447-48, 1455 (11th Cir. 1996) (rejecting challenge in a case of attorneys who paid kickbacks to state court judges to obtain appointments as public defenders); United States v. O'Hagan, 521 U.S. 642 (1997)).

[72] *Rybicki*, 287 F.3d at 262.

[73] *Id.* at 262-63. However, in *Rybicki*, the court did not "rule out the possibility that the government in this case could have established actual or intended economic or pecuniary harm had it been required to do so." *Id.* at 263 n.1.

interest for the adjusters with respect to their employers."[74] Moreover, the court noted that the defendants' efforts to avoid detection were indicative of a consciousness of guilt, thereby negating appellants' claim that they had no notice that their conduct was illegal. Applying this logic to the overall argument, the crime is not just the failure of providing honest services when one is required to do so, but that the failure was intentional, as evidenced by the subsequent concealment. One may wonder why, if potential defendants were unaware or unsure that their conduct was unlawful, they would not just disclose the breach of the fiduciary obligation and thus potentially escape liability in those gray cases.[75]

The court then placed two restrictions on the application of § 1346 in order to minimize the fears of overcriminalization. First, a de minimis test is employed to make sure that minor infractions of fiduciary obligations do not result in criminal liability.[76] Second, the court adopted a reasonably foreseeable harm standard[77] that requires that it must have been reasonably foreseeable to the defendant that the scheme at issue could have resulted in some economic or pecuniary harm to the victim.[78] The court articulated two justifications for the selection of the reasonably foreseeable harm test. First, the test's focus on "foreseeable risk of economic or pecuniary harm to the victim" is consistent with

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[74] *Id.* at 264.

[75] Of course, in some cases, the fiduciary breaches may be concealed not out of a consciousness of legal guilt but out of a feeling of shame and regret at failing at one's obligations. However, given the de minimis protection discussed *infra* and the fact that there must be a duty to provide honest services, it is unlikely such a scenario could be concocted.

[76] *Rybicki*, 287 F.3d at 266.

[77] Other circuits have adopted this test, as well. *See* United States v. Vinyard, 266 F.3d 320, 328-29 (4th Cir. 2001); United States v. Martin, 228 F.3d 1, 17 (1st Cir. 2000); United States v. deVegter, 198 F.3d 1324, 1329-30 (11th Cir. 1999); United States v. Sun-Diamond Growers, 138 F.3d 963, 973-74 (D.C. Cir. 1998); United States v. Frost, 125 F.3d 346, 368-69 (6th Cir. 1997).

[78] *Rybicki*, 287 F.3d at 265.

"traditional notions of fraud and fraudulent harm."[79] Second, the test "has the virtue of being capable of straightforward and consistent application, while at the same time placing a reasonable boundary around what is otherwise so boundless a concept as to be a suitable candidate for a finding of unconstitutional vagueness."[80] Though the test does provide some boundaries on § 1346, there is still the concern that the test is applying a tort concept of negligence[81] in determining a culpable state of mind.

Other circuits have used different restrictions in this regard. Some courts have placed a requirement that the misrepresentation or omission at issue be "material" so that "an employee has reason to believe the information would lead a reasonable employer to change its business conduct."[82] The *Rybicki* court noted that "[t]he First Circuit has at times adopted a requirement that the deprivation of honest services must either result in some particular harm to the victim or be intended for some gainful, though not necessarily economic, use to the defendant."[83]

On rehearing en banc, the Second Circuit adopted the materiality test rather than the reasonably foreeseable test.[84] Thus, "the misrepresentation or omission at issue for an 'honest services' fraud conviction must be 'material,' such that the misinformation or omission would naturally tend to

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[79] *Id.*; *see also* McNally v. United States, 483 U.S. 350, 358 (1987) ("the words 'to defraud' . . . 'usually signify the deprivation of something of value by trick, deceit, chicane, or overreaching.'" (citation omitted)).

[80] *Rybicki*, 287 F.3d at 265.

[81] The standard can be seen as a mixed subjective/objective mens rea test. However, the reasonably foreseeable element sounds in negligence and would preclude a defense that the defendant did not actually think that the scheme would result in some economic or pecuniary harm to the victim.

[82] United States v. Gray, 96 F.3d 769, 775 (5th Cir. 1996); *see also* United States v. Cochran, 109 F.3d 660, 667 (10th Cir. 1997); United States v. Jain, 93 F.3d 436, 441-42 (8th Cir. 1996).

[83] *Rybicki*, 287 F.3d at 265. *See also* United States v. Jordan, 112 F.3d 14, 19 (1st Cir. 1997); United States v. Czubinski, 106 F.3d 1069, 1077 (1st Cir. 1997).

[84] United States v. Rybicki, 354 F.3d 124 (2d Cir. 2003) (en banc).

lead or is capable of leading a reasonable employer to change its conduct."[85] The materiality standard was preferred over the reasonably foreseeable test in that it had "the virtue of arising out of fundamental principles of the law of fraud: A *material* misrepresentation is an element of the crime."[86] According to the Second Circuit, the "'non-de minimis reasonably foreseeable harm' test, by contrast, seems to be something of an *ispe dixit* designed simply to limit the scope of section 1346."[87] As will be discussed *infra* in Section IV, this Note contends that application of the materiality standard by itself is unconstitutionally overinclusive, because it can reach conduct that may change the conduct of a reasonable employer or other honest services beneficiary, yet be so minimal that to extend criminal liability in such a case would shock the conscience and provide unnecessary ammunition to the statute's detractors.

IV. PROPOSED SOLUTION

Unquestionably, the disagreement over which test to utilize to determine whether a given defendant has violated the mail fraud law perpetuates the vagueness challenge to the statute, and thus it may be only a matter of time before the Supreme Court intervenes and decides on a single standard. In framing a solution to this problem, one must keep in mind the purposes of the statute and the history of judicial attempts to curtail its reach. The solution proposed in this Note is a three-part test combining both approaches of materiality and reasonable foreseeability with an added policy-balancing de minimis test for the gray cases in which the court should consider whether society would benefit from such a prosecution.[88] The tort/contract distinction should be

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[85] *Id.* at 145.

[86] *Id.* at 146 (emphasis in original).

[87] *Id.* at 146.

[88] *See* Coffee, *supra* note 41, at 165. Professor Coffee formulates his affirmative defense as part of the issue of causation in intangible services mail fraud and analogizes it to the tort concept of proximate causation. This test would adopt the same concept though it would drop the tie to

eliminated entirely and the logic of the dissenting opinion in *Handakas* should be adopted. The majority opinion was predicated on the assumption that tort duties somehow provide more notice than contract duties, a proposition that is simply unwarranted. Rather, it appears that the distinction manifests the majority's concern that the reach of § 1346 is too great and that it can reach conduct that is not sufficiently culpable. However, such a concern can be addressed with greater doctrinal consistency through application of a de minimis requirement. Had the court taken this approach, it could have arrived at the same outcome, while avoiding theoretical gymnastics that may have perverse consequences on potential future cases. The simple three-step test proposed in this Note would be faithful to the concepts of notice and due process while maintaining the strength and vigor of the honest services mail fraud statute.

It is a primary contention of this Note that, implemented separately, none of the tests applied by the various circuits sufficiently address the concerns of vagueness and notice while still giving effect to the congressional purpose of protecting individuals from honest services fraud. First, none of those tests explicitly adopt the third part of the proposed solution in this Note, the de minimis review. Without such a balancing inquiry with a de minimis threshold, minor violations of fiduciary obligations could possibly fall within the reach of the criminal law. Second, a reasonable foreseeability test without the related "materiality" prong may suffice as grounds for criminal

actual causation and limit it to the policy-balancing aspect of the proximate causation test. It is tied with the de minimis threshold because it is the author's contention that if the fraud is more than de minimis then it is highly unlikely that policy balancing would work in the defendant's favor. It is also tied to the de minimis standard because the remaining components of the test address other concerns of proximate causation like foreseeability. It appeared that the Second Circuit had implicitly adopted Professor Coffee's suggestions through its reasonable foreseeability test in the panel's *Rybicki* decision, though it was ultimately rejected in the en banc opinion.

conviction for somewhat minor fiduciary breaches that may be more than de minimis but would not lead an employer "to change its business conduct."[89] Though it is unlikely to have much practical impact,[90] such an application makes the statute more vulnerable to a vagueness attack than it need be. Of course, it is accepted that the reasoning in the panel opinion of *Rybicki* is basically sound and that it is a significant step forward in delineating the contours of § 1346 while preserving its deterrent strength. The en banc decision goes too far in abandoning both the reasonable foreseeability and de minimis tests. Without them, minor violations can result in criminal conviction. For example, under the materiality test alone, an employee who violates company policy by making an unauthorized long-distance personal phone call could be held liable if, in the given context, it can be argued that a reasonable employer would change its business conduct by either disconnecting long distance service altogether or by implementing access codes and time limitations on long-distance usage. It might be completely reasonable for an employer to change its conduct on the basis of small violations of its employees' honest

[89] United States v. Frost, 125 F.3d 346 (6th Cir. 1997). In other words, if the person who is owed the fiduciary obligation of honest services would not consider the information so important as to change his or her business conduct in response (a definition of materiality), then it would be harsh to impose criminal penalties, even though it might have been foreseeable that some economic or pecuniary harm may arise that is more than de minimis.

[90] Despite the hypothetical horrors of individuals being charged with felony mail fraud for making an unapproved phone call or other minor fiduciary violation, prosecutors are not likely to bring these cases. *See* Daniel C. Richman, *The Changing Boundaries Between Federal and Local Enforcement*, *in* BOUNDARY CHANGES IN CRIMINAL JUSTICE ORGANIZATIONS, 2 CRIMINAL JUSTICE 2000 (National Institutes of Justice 2000) (arguing that merely looking at the substantive reach of the federal law is misleading because Congress exercises control of federal involvement in traditional areas of state prosecution through funding, and because of the remarkably small size of the federal enforcement bureaucracy in relation to the prospective number of individual violations of federal law).

services obligations, but it would be draconian for those infractions to give rise to federal criminal liability.

Thus, faced with a minor violation, a court applying the materiality test alone will have three options, none of which is appealing. First, the court could apply a de facto de minimis test in determining whether a reasonable employer would change its conduct in light of the violation, and find that in certain cases, the infringement is so small that no reasonable employer would change its conduct. This might involve a bit of strained reasoning, since even if the given "fraudulent" action is very small, reasonable people may change their conduct in order to avoid subsequent violations that, when aggregated, may become a very large problem. Thus, this approach, though more "just," would strain the doctrinal consistency of the materiality test. Second, the court could find that the statute as applied to the defendant is unconstitutional because it does not neatly fit under the given materiality standard. This outcome may be just in a given case, but would create great doctrinal confusion and highlights how the materiality test, by itself, fails to address the problem of minor violations. Third, the court could find the given criminal conviction constitutional, a result that would shock the conscience and further support the argument that § 1346 goes too far.

The materiality standard without the implementation of the reasonable foreseeability test does not adequately concern itself with the intent of the defendant or what he or she would be reasonably expected to know. One of the purposes of criminal law is to deter anti-social behavior. If the defendant could not foresee that his or her allegedly fraudulent behavior could result in some kind of economic harm, the law would have no deterrent value in those contexts and would seriously undercut any argument that § 1346 serves a broader purpose. As Professor Coffee stated, "[i]njuries that are not foreseeable are not easily deterred."[91] Without the reasonable foreseeability test, the statute would have questionable value, since individuals would not be able

[91] Coffee, *supra* note 41, at 165.

to be assess ex ante whether their conduct carried risk of punishment.

Finally, without a de minimis standard attached to the materiality test, criminal liability might ensue for minor violations of a company's internal policies that nonetheless lead the company to change its business conduct.[92] This defense of the statute is qualified and may cause some to wonder why it would be necessary to preserve the prosecutorial option when no economic loss has resulted or can be proved beyond a reasonable doubt. The answer is readily apparent in *Rybicki,* in which the defendants argued that because the claims settled within reasonable timeframes and for amounts appropriate to their clients' losses, that there was no economic loss. If such a defense were given effect, it would vitiate § 1346 by exempting those defendants who defraud others of their right to honest services without causing an economic loss, or those who are knowledgeable enough to structure their fraud in such a way that proving economic harm would be extremely difficult. For example, given the facts of *Rybicki*, if the government had to prove that the insurance company actually suffered economic harm, it would be in a very precarious position, given that the settlements were within a reasonable value for the underlying claim: How could the government prove that, absent the kickbacks to the adjusters, the claims would have been settled on terms more favorable to the insurance company? Indeed, one of § 1346's strengths is that it proscribes the deprivation of honest services iteself, not the economic harm that may result; the resulting flexibility allows the prosecution of those who *intend* to extract an economic gain or cause an economic loss to those whom they owe a duty of honest services, but for whatever reason fail in

[92] As discussed *supra*, the unauthorized telephone call hypothetical demonstrates how a materiality standard by itself is not an optimal legal framework for the honest services mail fraud statute.

actually receiving the economic gain or causing the economic loss.[93]

Though, at first glance, there may not seem to be an definable economic loss, it is relatively easy to develop a theory that by defrauding someone of their right to honest services, the defrauded individuals have been denied the very gain that the defendants have expropriated for themselves. In *Rybicki*, for instance, the defendants' scheme involved kickbacks to insurance adjusters for settlements of claims; even if those settlements were reasonable, both the insurance company and the plaintiff would have benefited from the money that was diverted into the kickback,[94] and thus economic loss to the victims may be inherent in the deprivation of honest services. Though this approach solves the theoretical dilemma of economic damages, it would not suffice for a conviction in a court that required proof of pecuniary harm. Proof of actual pecuniary loss may be harder to establish as fraud grows more complex, and thus this requirement provides solace to those who do not deserve it.

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[93] Consider, for example, a broker-client relationship in which the client is dependent on the advice and guidance of the broker, and the broker intentionally promotes a "pig" stock that will lose the client money, but generate a commission. If the client were to purchase the stock and suffer an economic loss, the case for fraud would be strong. However, what if the client, after receiving all of these "dishonest services," simply decides not to buy that "pig" stock. No economic loss has resulted, but the client's right to honest services has been violated.

[94] For example, assume that in a personal injury action a plaintiff has a claim worth $20,000–$30,000. The plaintiff's attorney bribes the insurance adjuster $1,000 for a settlement of $25,000. At the very least, both the insurance company and the plaintiff have been denied access to a certain percentage of the $1,000 given the adjuster. If the attorney pays the bribe out of the settlement or in attorney's fees, the plaintiff is, in effect, having his or her settlement reduced by $1,000. The insurance company is also being defrauded because it would have been better off settling for an amount less the $1,000 needed to pay the bribe to its own employee. This creates economic inefficiency, as well as morally condemnable behavior.

V. CONCLUSION

The concerns of lack-of-notice and vagueness are pronounced in the abstract, but when faced with particular instances of fraud, the concerns melt away. "The boundaries of 'intangible rights' may be difficult to discern, but that does not mean that it is difficult to determine whether [an individual defendant] in particular violated them."[95] One of the underlying assumptions of this Note is that the right to honest services is important and that the policy goal of protecting honest services beneficiaries is a worthy and commendable one. It is further presumed here that those who would defraud those beneficiaries deserve criminal penalties. This Note is a response to those who would declare the statute facially unconstitutional and contends that some of the arguments marshaled in opposition to § 1346 are exaggerated, while the others can be resolved in a way that preserves the strength of the statute rather than discarding it entirely as congressional overreaching.[96]

A debate about ends may be valuable in another setting; however, in assessing the legal implications at issue here, such a challenge would be off the mark. Debating the value of honest services protections is to attack the wisdom of Congress' decision to pass § 1346 and the presidential decision to sign it into law. That kind of analysis is better left to the political arena. This Note has attempted to demonstrate that, within the legal framework, § 1346 can be interpreted in such a way that preserves its key strengths and resolves the constitutional challenges that it presents. It is the position here that § 1346 serves vital societal interests and that it is a necessary tool in the battle against sophisticated forms of modern fraud. In order to analyze the legal merit of § 1346 and the way in which it is currently being applied in U.S. courts, a good-faith attempt to honor the intent of Congress should be at the very heart of any

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[95] United States v. Brumley, 116 F.3d 728, 733 (5th Cir. 1997).

[96] *See* Moohr, *supra* note 5, at 187-200. Though her article focuses on the application of § 1346 to local government corruption prosecutions, her arguments on facial invalidity of the statute apply in this context, as well.

proposal. There are two strands of legal reasoning that are in conflict here: On the one hand are the traditionally expansive and purposive interpretations courts have given to congressional enactments; on the other are the doctrines of lenity and the constitutional concerns of vagueness embedded in the judiciary's handling of criminal law. Rather than selecting one strand and discarding the other, this Note attempts to integrate both in a way that results in the protection of Congress' powers to enact law (and have its will reflected in law) while respecting the constraints that both the Constitution and the common law have placed on criminal statutes. Legal concerns for vagueness and notice can be resolved given the framework presented here. Policy arguments that the statute is too broad or is harmful to society are pleas to be made to Congress, not to the courts; they certainly do not render the statute unconstitutional as a matter of law.[97]

In an era of Enron and other highly sophisticated schemes to defraud, a strong honest services mail fraud statute is a public good. However, that public good must not come at the cost of the notice and due process considerations that are central to American criminal law. Thus, rather than abandoning the statute by declaring it unconstitutionally vague or simply unwise and dangerous to business, this Note seeks to resolve the tension in a balanced manner.[98]

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[97] As Judge Raggi made clear in his concurring opinion in the en banc opinion of *Rybicki*, "retaining flexibility to recognize that other schemes, not precisely fitting within the models identified by the majority today, could constitute honest services fraud does not establish the vagueness of § 1346. Rather it acknowledges the reality of fraud, a crime of extraordinary variety, limited only by human imagination." United States v. Rybicki, 354 F.3d 124, 155 (2d Cir. 2003) (en banc) (Raggi, J., concurring).

[98] The impact that a strong honest services fraud statute could have on civil RICO cases with mail fraud predicates presents an interesting question. A complete analysis is beyond the purview of this Note. However, the same arguments made in defense of the criminal application of the statute could be made to maintain that civil enforcement of honest services mail fraud in accordance with the test devised in this Note would actually reduce frivolous civil cases. At the very least, more clear honest

As one judge noted, in order to determine the definition of fraud, the law turns to commonly accepted moral principles and "condemns conduct which fails to match the reflection of moral uprightness, of fundamental honesty, fair play and right dealing in the general and business life of members of society."[99] This Note accepts that position and maintains that to separate the concept of "fraud" from all moral underpinnings or to freeze "fraud" in its common law definition would not only compromise the intent of Congress, but also further erode society's confidence in those businesspeople, doctors, lawyers, and others who owe their clients fiduciary obligations.

services mail fraud statutes would provide greater notice to potential defendants in both civil and criminal matters. In fact, the civil RICO problem created by a vague honest services mail fraud interpretation highlights the importance of a clear understanding of the criminal application of the statute.

[99] *See* Jones, *supra* note 10, at 145 n.24 (quoting Blachley v. United States, 380 F.2d 665, 671 (5th Cir. 1967)).