

# HONEST SERVICES FRAUD AND ANTITRUST: WILL THE SUPREME COURT RE-WRITE THE RULES FOR “COMPETITION CRIMES”?

by

J. Brady Dugan and Mark J. Botti

The trio of honest services fraud cases to be decided by the Supreme Court this term – *U.S. v. Black*, *U.S. v. Skilling* and *U.S. v. Weyhrauch* – have the potential to effect a major change in criminal enforcement policy at the Antitrust Division of the Department of Justice (“the Division”). The Division has increasingly used the honest services fraud statute to prosecute competition crimes involving bribes and kickbacks. While the Division has had success using this broadly-worded statute, it has not, to date, provided much guidance to the business community regarding the boundaries to which the statute extends. With these cases, the Supreme Court is poised, at last, to provide guidance to both prosecutors and the business community on what it means to violate the honest services fraud statute.

## *The Antitrust Division Brings a Significant Number of Fraud Prosecutions*

The Antitrust Division is responsible for criminal enforcement of “the Federal antitrust laws and other laws relating to the protection of competition . . . .”<sup>1</sup> Its enforcement of “other laws relating to the protection of competition,” gives it the ability to use a variety of fraud statutes, including the mail and wire fraud, tax fraud, and money-laundering statutes. When the Division uses these statutes, it is careful to do so within its mandate to protect competition. Its press releases typically explain such charges as a “corruption”, “subversion”, or “cheating” of the competitive process.<sup>2</sup> The Division’s expertise with competition fraud has been recognized within DOJ – the Division is routinely represented on Department-wide white collar crime task forces. With the Division’s recent Economic Recovery Initiative designed to uncover collusion

---

<sup>1</sup>28 C.F.R. §0.40.

<sup>2</sup>See, e.g., Press Release, U.S. Department of Justice, New Jersey Electrical Services Company Employee Sentenced to 20 Months in Jail for Kickback and Fraud Scheme (Jul. 13, 2009) at [http://www.usdoj.gov/atr/public/press\\_releases/2009/247919.pdf](http://www.usdoj.gov/atr/public/press_releases/2009/247919.pdf); Press Release, U.S. Department of Justice, Defense Contractor Pleads Guilty to Wire Fraud in Connection With the Procurement of a Bullet-Proof Vest Contract in Iraq, (May 27, 2009) at [http://www.usdoj.gov/atr/public/press\\_releases/2009/246338.pdf](http://www.usdoj.gov/atr/public/press_releases/2009/246338.pdf).

---

**J. Brady Dugan** and **Mark J. Botti** are partners in the Washington DC office of the law firm Akin Gump Strauss Hauer & Feld LLP. Mr. Dugan and Mr. Botti spent 15 and 13 years, respectively, in the U.S. Department of Justice’s Antitrust Division.

and fraud in connection with Stimulus Bill funds, the Division is poised to bring more competition fraud cases, including those relying on the honest services fraud statute.

The honest services fraud statute is a deceptively short amendment to the federal mail and wire fraud statutes. It reads: “the term ‘scheme or artifice to defraud’ includes a scheme or artifice to deprive another of the intangible right of honest services.” 18 U.S.C. § 1346. The statute was a direct response to the Supreme Court’s 1987 decision in *McNally v. United States*.<sup>3</sup> In *McNally*, the Court reversed the mail fraud convictions of a Kentucky state official who had taken part in a kickback scheme. The Court held that the mail fraud statute is limited to schemes to deprive persons of money or property; it does not extend to a scheme to deprive the public of the honest services of a public official. Congress sought to overturn *McNally* in 1988 by passing the honest services fraud statute.

Government has used the honest services fraud statute to prosecute both public and private corruption under the theory that just as politicians owe a duty of honesty to their constituents, so employees owe a duty of honesty to their employers. There are a slew of cases in which misuse of public office for private gain is prosecuted as a fraud under § 1346 including, for example, the cases brought against former Illinois Governor Rod Blagojevich and former Congressman William Jefferson.

But the Antitrust Division typically charges honest services fraud when an employee breaches a duty owed to his employer. For example, in June 2008, an individual pleaded guilty to bribing a manufacturing company to hire the defendant’s freight forwarding business.<sup>4</sup> In December 2008, a processed tomato products broker who bribed purchasing agents to buy from him was charged by the Division and the U.S. Attorney’s office with multiple crimes, including money laundering, using honest services fraud as one of the predicate offenses.<sup>5</sup> And in a Division prosecution earlier this year, Home Depot employees received prison sentences for directing business to vendors who paid them kickbacks.<sup>6</sup> In each of these prosecutions, an employee breached a duty to an employer by participating in a bribery or kickback scheme that deprived the employer of the benefits of competition among its suppliers.<sup>7</sup>

### ***Compliance Counseling Problems Caused by the Lack of Guidance***

The broad wording of the honest services fraud statute makes it difficult to know with certainty what conduct will run afoul of the statute. Consider the Division’s case against Mr. Granizo. Granizo ran a freight forwarding company. He bribed an employee of one of his customers to direct business to Granizo’s company. So Granizo did not breach a duty owed to his own company; instead he deprived his customer of the honest services of the employee Granizo had bribed. But where is the line between honest marketing practices and an honest services violation? If Granizo got the same result by taking the executive on a golf outing rather than bribing him, would that be a crime? Would it depend on the value of the golf outing?

---

<sup>3</sup>483 U.S. 350 (1987).

<sup>4</sup>*United States v. Granizo*, CR 08-377 (E.D. N.Y. 2008).

<sup>5</sup>*United States v. Rahal*, No. 2-08-CR-566 (E.D. CA 2008).

<sup>6</sup>*See, e.g., United States v. Tesvich*, No. 1:08-CR-201 (N.D. GA 2008).

<sup>7</sup>Other examples of the Antitrust Division’s use of the statute, in just the last year, include: *United States v. Hansen*, 1:09-CR-162 (W.D. MI 2009); *United States v. Johnston*, 1:09-CR-14 (N.D. GA 2009); *United States v. Matheny*, 1:09-CR-197 (N.D. GA 2009); *United States v. Brandt*, 09-CR-278 (N.D. IL 2009); *United States v. West, et al.*, 08-CR-669 (N.D. IL 2009); *United States v. Zhu*, 2:08-CR-848 (E.D. NY 2008).

The golf outing hypothetical is not facetious – if the person being bribed by the golf outing had been a foreign government official, the Criminal Division would have to consider charging a violation of the Foreign Corrupt Practices Act (“FCPA”). The honest services fraud statute is, in some ways, a domestic version of the FCPA applied to private companies.<sup>8</sup> The FCPA makes it a crime to bribe foreign government officials; the honest services fraud statute makes it a crime to bribe employees of private firms. Yet DOJ routinely provides guidance regarding the scope of the FCPA, but provides no comparable guidance as to the scope of honest services fraud.<sup>9</sup>

With limited guidance from DOJ, companies are left on their own to assess the risks to themselves and their key employees. What is the range of “dishonest” conduct under the statute? Is the risk limited to individuals, or could companies be charged under the statute? Granizo, but not his company, was charged with conspiring to deprive his customer of the honest services of his customer’s employee. Could Granizo’s company have been charged as a co-conspirator in that scheme? Would the charging decision turn on whether Granizo’s conduct violated his employer’s corporate ethics policy?

The Antitrust Division has at least implied that a duty to provide honest services can arise from a company’s ethics policy. In charging a former Home Depot employee with honest services fraud, the Division charged that Home Depot adopted ethics policies “to ensure that . . . employees acted honestly and faithfully in all of their dealings with Home Depot.”<sup>10</sup> If a duty arises from a corporation’s policies, then does the reach of the statute vary from one company to another?

The compliance challenges with honest services fraud are made more difficult by the lack of clear guidance from the courts. The federal courts of appeal have struggled to find ways to limit the broad language of the statute so that not every breach of an employee’s fiduciary duty gives rise to a federal crime. One limiting principle in private corruption cases is whether the government must show that the scheme could have harmed the employer. Those appellate courts which have addressed this issue have reached a variety of often conflicting conclusions.<sup>11</sup> Recently, the Fifth Circuit reversed a defendant’s honest services convictions arising out of the Enron prosecutions, holding that no statutory violation occurs when the scheme is designed to further rather than harm the interests of the corporation alleged to be the victim.<sup>12</sup> The Fifth Circuit refused to reverse Jeffrey Skilling’s convictions on similar grounds – he now seeks relief in the Supreme Court. The issue of reasonably foreseeable harm to the employer is also at the heart of Conrad Black’s appeal.<sup>13</sup> The issue has additionally arisen in an appeal of an Antitrust Division conviction.<sup>14</sup>

---

<sup>8</sup>Other statutes make self-dealing a crime in other contexts. For example, 18 U.S.C. § 201 prohibits bribing a public official or a witness before a federal proceeding; 18 U.S.C. § 666 prohibits misdealing affecting programs or agencies that receive federal funds. However, these other statutes do not have nearly the broad reach of the honest services fraud statute and unlike the honest services fraud statute, they provide in their texts guidance on what conduct is prohibited.

<sup>9</sup>The FCPA requires DOJ to set up procedures allowing businesses to get opinions as to whether conduct conforms to the Department’s present enforcement policy. *See*, 28 C.F.R. § 80 (2008). For additional guidance, *see*: <http://www.usdoj.gov/criminal/fraud/fcpa/>.

<sup>10</sup>*Tesvich*, Criminal Information at para. 5.

<sup>11</sup>*See, e.g., U.S. v. Welch*, 327 F.3d 1081, 1106-07 (10th Cir. 2003) (honest services violation does not require that defendant intended to achieve personal gain); *U.S. v. Bloom*, 149 F.3d 649, 656 (7th Cir. 1998) (breach of fiduciary duty without misuse of one’s position for personal gain cannot be an intangible rights fraud).

<sup>12</sup>*United States v. Brown*, 459 F.3d 509, 522-23 (5th Cir. 2006).

<sup>13</sup>*United States v. Black*, 530 F.3d 596 (7th Cir. 2008), *cert. granted* No. 08-876 (S. Ct. May 18, 2009).

<sup>14</sup>*United States v. Candelario*, No. 11101-GG (11<sup>th</sup> Cir. 2009).

## *Implications of the Honest Services Cases Before the Supreme Court*

Former Enron CEO Jeffrey Skilling was charged with multiple counts related to his alleged participation in a conspiracy that included overstating Enron's financial situation to keep its stock price artificially high. The government charged that one of the objects of the conspiracy that Skilling joined was to deprive Enron and its shareholders of the honest services of Skilling and other employees. Skilling was convicted on 19 counts, including the conspiracy count. He was sentenced to 292 months in prison.

In his appeal to the Supreme Court, Skilling argues that the government essentially admitted that his actions were taken to benefit Enron. He asks the Court to find that where there was no private gain at the expense of the employer, an employee cannot have violated his duty of honest services.

Conrad Black, the former CEO of media conglomerate Hollinger International, and his co-defendants, caused a Hollinger subsidiary to pay the defendants \$5.5 million, ostensibly as part of an agreement not to compete against certain assets divested by the subsidiary. The government contended that Black essentially stole this money from Hollinger; Black asserted that the money represented management fees owed to him and that the payment was characterized as part of a non-compete agreement in order to receive favorable tax treatment in Canada. Black was convicted on multiple counts, including honest services mail fraud, and was sentenced to 78 months in prison.

Black does not dispute that he received a "private gain," but he maintains that he intended no harm to Hollinger, and that there could not have been any harm to Hollinger, since the money paid to him was owed to him. Without at least some link between the dishonesty and harm to the victim, Black argues that the government is in a position to criminalize almost any violation of corporate policy.<sup>15</sup>

### *Conclusion*

Whatever the Supreme Court decides in the cases before it, the Division will have to rethink its ability to charge honest services fraud. For example, if the Court requires proof of reasonably foreseeable harm to the victim of the honest services scheme, will future Division prosecutions require evidence that but for the bribery or kickback scheme, the victimized company would have paid a lower price for the products involved? The proof needed for such a requirement could be daunting.

Regardless of how the Supreme Court rules, its opinion is bound to offer the business community more certainty on what it means to commit an honest services violation. The Antitrust Division could further aid the business community by providing clear guidance on its enforcement intentions. In the absence of such guidance, businesses must strengthen their own compliance efforts to minimize opportunities to run afoul of the honest services fraud statute when marketing to customers, suppliers and other business partners.

---

<sup>15</sup>In the third honest services fraud case before the Court this term, *Weyhrauch v. United States*, 548 F.3d 1237, *cert. granted*, No. 08-1196 (S. Ct. June 29, 2009), the Court will address whether it is necessary to prove that the conduct at issue violated state law in a public corruption honest services fraud prosecution.