

Criminal Law—Fifth Circuit Misinterprets the Federal Honest Services Fraud Statute—*United States v. Brown*, 459 F.3d 509 (5th Cir. 2006)

The federal honest services fraud statute proscribes the use of mail or wires to execute a scheme depriving another of the right of honest services.¹ In the private sector, federal courts generally recognize honest services fraud where an employee or agent, using the mail or wires, breaches a fiduciary duty owed to an employer or principal through bribes, kickbacks, or self-dealing.² In *United States v. Brown*,³ the Fifth Circuit Court of Appeals considered whether four executives at Merrill Lynch (Merrill) conspired to defraud the right of its executives' honest services from Enron's executives by facilitating the sale of Enron power barges to Merrill, conditioned upon a secret buy-back agreement which made Merrill's purchase a loan.⁴ The appeals court held that the wrongful conduct of the Enron executives was not sufficiently divorced from Enron's corporate goal of increasing profits to "constitute a *criminal* breach of duty."⁵

In late 1999, executives at Enron's APACHI energy division sought a buyer for a set of Nigerian power barges to meet earning forecasts for the final quarter of 1999.⁶ Numerous attempts to sell the barges proved unsuccessful.⁷ In December 1999, Enron contacted executives at Merrill's Houston office to

1. See 18 U.S.C. § 1341 (2000) (codifying federal mail fraud statute); 18 U.S.C. § 1343 (2000) (codifying federal wire fraud statute); 18 U.S.C. § 1346 (2000) (including deprivation of "intangible right of honest services" as fraudulent scheme under §§ 1341 and 1343); see also *Neder v. United States*, 527 U.S. 1, 20-23 (1999) (outlining elements of federal wire and mail fraud statute); Skye Lynn Perryman, *Mail and Wire Fraud*, 43 AM. CRIM. L. REV. 715, 717-34 (2006) (providing detailed analysis of §§ 1341, 1343, and 1346).

2. See *United States v. Rybicki*, 354 F.3d 124, 139-44 (2d Cir. 2003) (dividing private sector honest services fraud into bribery and self-dealing categories). Despite *Rybicki's* attempt to make sense of § 1346, the circuits are split on the precise meaning of honest services fraud and have proffered a myriad of distinct definitions. See *infra* notes 29-31 (discussing federal courts disagreement over meaning of § 1346); *infra* note 37 (listing different standards for determining honest services fraud in private sector amongst federal circuit courts).

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

4. *Id.* at 513-14. The sham sale enabled Enron executives to artificially inflate 1999 year-end profits and receive increased personal bonuses, while generating \$775,000 in fees and interest payable to Merrill. *Id.* at 513-18. Despite the financial losses Merrill executives' caused Enron and its shareholders, the appeals court decided that the executives did not commit honest services wire fraud. *Id.* at 522-23.

5. *Id.* at 522-23 (holding executives' conduct consistent with Enron's established goals of generating profits, despite company's financial loss). Therefore, the government relied on a different theory of fraud "to punish this character of wrongdoing." *Id.* at 523. But see *id.* at 532-33 (Reavley, J., dissenting) (arguing government's theory of honest services fraud valid). Specifically, Judge Reavley rejected the majority's assertion that Enron and its employees had a mutual interest in the Nigerian barge deal, notwithstanding the employee's fiduciary breach. *Id.* at 533 (Reavley, J., dissenting).

6. *Id.* at 514 (discussing APACHI executives' decision to sell Nigerian barges to boost Enron profits). APACHI stands for "Asia/Pacific/Africa/China." *Id.* at 513.

7. 459 F.3d at 514 (noting Enron executives' inability to find buyer for Nigerian barges).

propose a deal, whereby Merrill would make a \$7 million equity investment in a “special purpose vehicle” to allow Enron to report \$10 million in earnings.⁸ Enron executives stressed that the deal must close by December thirty-first, but noted that Merrill would only hold the assets for six months and make a 22.5% return.⁹

At Merrill, the proposed deal’s year-end timing and rushed character created concern and doubt among some employees.¹⁰ Merrill executives, however, maintained interest in the deal after Enron executives verbally assured that it or an affiliate would repurchase the barges at a predetermined price by June 30, 2000.¹¹ When Merrill executives requested written assurance of the buy-back agreement, an Enron executive responded that such an assurance would preclude Enron from reporting the barge deal as an earnings-generating sale.¹² Later that day, a Merrill attorney warned company executives, at two separate meetings, that “Merrill would have to own the barges outright without any buyback agreement,” if Enron wanted to “show the sale as a profit on its books.”¹³ The following day, during a second conference call between Merrill and Enron executives, Andy Fastow, Enron’s Chief Financial Officer, again promised that Enron or an affiliate would repurchase the barges from Merrill within six months.¹⁴

By the end of 1999, Enron and Merrill executed the barge deal.¹⁵ At trial, the government contended that Enron’s oral buy-back agreement with Merrill made the deal a loan, not a sale, because Merrill’s interest in the barges was risk-free, and therefore “Enron’s accounting of the deal as a sale . . . was false.”¹⁶ In facilitating the sham deal, the government asserted that high-level Merrill executives defrauded and conspired to defraud Enron and its shareholders the right of their employees’ honest services.¹⁷ Without relying

8. *Id.* at 514 (plotting early stages of barge deal). Daniel Boyle, Enron Vice President of Global Finance, first discussed the deal with Robert Furst, a Merrill executive working under Daniel Bayly, the head of Merrill’s Global Investment Banking division. *Id.* at 513-514. Furst communicated the deal to Bayly and Jim Brown, the head of Merrill’s Strategic Asset and Lease Finance Group in New York City. *Id.* at 514.

9. *Id.* at 514 (discussing details of Nigerian Barges deal).

10. *Id.* (summarizing concerns of Katherine Zrike, chief counsel for Merrill Investment Banking, and Tina Trinkle, Merrill analyst).

11. 459 F.3d at 514-15 (noting communication commonly referred to as “Trinkle call”). Bayly, Brown, and Furst participated in this conference call. *Id.*

12. *Id.* at 515 (explaining written assurance would make sale equivalent to loan and prohibit Enron from showing profit).

13. *Id.* (discussing warning to Merrill executives). Zrike personally cautioned Furst and Bayly. *Id.* Neither Furst nor Bayly disclosed any knowledge of the proposed buy-back deal to Zrike. *Id.*

14. *Id.* (discussing Fastow’s oral promise to buy back barges). The government alleged that Bayly, Furst, and Brown—although himself not on the conference call—were each aware of Fastow’s promise. *Id.*

15. 459 F.3d at 515-16 (explaining transaction yielded \$12,563,000 in profit to Enron and \$775,000 in profit to Merrill). The profits included Merrill’s advisory fee and funds obtained after selling the barges to Enron affiliate LJM2. *Id.* at 516.

16. *Id.* at 513 (discussing government’s argument at trial equating barge sale to a loan).

17. *Id.* at 520 (discussing Brown, Bayly, Furst, and Fuhs’ alleged misconduct, including failure to disclose oral buy-back provision). Additionally, the government contended that the defendants’ conduct

on a specific theory of criminal fraud, a jury convicted the Merrill executives and Enron's Daniel Boyle of two counts of wire fraud and one count of conspiracy to commit wire fraud.¹⁸ On appeal, the Fifth Circuit vacated the Merrill executives' convictions, holding that the government's theory of honest services fraud could not include circumstances where "dishonest conduct is disassociated from bribery or self-dealing and indeed associated with and concomitant to the employer's own immediate interest."¹⁹

Federal courts historically construed the mail and wire fraud statutes to penalize a variety of interstate schemes that defraud persons of money and property.²⁰ During the 1970s and 1980s, federal courts further interpreted the statutes to protect intangible rights, and thereby created the doctrine of honest services fraud.²¹ This doctrine significantly increased the statutes' scope because the government did not need to show deprivation of money or property

resulted in concrete harms "in the form of fees paid to Merrill . . . and compensation bonuses paid to Enron . . ." *Id.*

18. *Id.* at 516 (noting wire fraud charges based on two interstate transmissions between Houston, Texas, and New York, New York).

19. 459 F.3d at 522 (describing case as "exceptional" due to relationship between Enron's corporate goal and executives' personal enrichment). *But see id.* at 532-33 (Reavley, J., dissenting) (arguing executives' conduct fits mold of honest services wire fraud).

20. *See* 18 U.S.C. § 1341 (2000) (codifying mail fraud statute); 18 U.S.C. § 1343 (2000) (codifying wire fraud statute); Brian C. Behrens, Note, *18 U.S.C. § 1341 and § 1346: Deciphering the Confusing Letters of the Mail Fraud Statute*, 13 ST. LOUIS U. PUB. L. REV. 489, 491-92 (1993) (explaining post offices' authorization to prohibit use of mails to commit fraud). The Supreme Court later interpreted § 1341 to criminalize "everything designed to defraud by representations as to the past or present, or suggestions and promises as to the future." *Durland v. United States*, 161 U.S. 306, 313 (1896); *see also* Jed S. Rakoff, *The Federal Mail Fraud Statute (Part I)*, 18 DUQ. L. REV. 771, 772 (1980) (providing in-depth history of mail fraud statute). In 1952, Congress enacted the wire fraud statute, the mail fraud statute's "direct descendent," to combat schemes using wire communication to defraud. Andrew B. Matheson, *A Critique of United States v. Rybicki: Why Foreseeable Harm Should be an Aspect of the Mens Rea of Honest Services Fraud*, 28 AM. J. TRIAL ADVOC. 355, 358 (2004). The wire fraud and mail fraud statutes are identical in their relevant parts. *Id.* at 386 n.10. For this reason, federal courts have generally interpreted both the mail and wire fraud statutes in the same way. *See* John C. Coffee, Jr., *Modern Mail Fraud: The Restoration of the Public/Private Distinction*, 35 AM. CRIM. L. REV. 427, 465 n.1 (1998).

21. *See* Coffee, *supra* note 20, at 427 (noting "flowering" of intangible rights doctrine in the 1970s and 1980s); Joshua A. Kobrin, Note, *Betraying Honest Services: Theories of Trust and Betrayal Applied to the Mail Fraud Statute and § 1346*, 61 N.Y.U. ANN. SURV. AM. L. 779, 792-93 (2006) (discussing federal case law contributing to intangible rights doctrine's evolution during the 1970s). In the early 20th century, the United States Supreme Court hinted that the mail fraud statute may not be limited to only deprivations of money or property. *See, e.g., Hammerschmidt v. United States*, 265 U.S. 182, 188 (1924) (explaining conspiracy to defraud United States only requires government officials to defeat government's "legitimate" interest in fraudulent manner); *United States v. Barnow*, 239 U.S. 74, 79-80 (1915) (upholding conviction for fraudulent impersonation of federal official supported without tangible loss to victim); *United States v. Plyler*, 222 U.S. 15, 17 (1911) (explaining pecuniary or property loss not required to convict defendant for fraudulently forging vouchers). Some contend that *Shushan v. United States* marked the true formation of the mail (and later wire) fraud statute's "twin theories" of intangible rights and honest services. *See* *Shushan v. United States*, 117 F.2d 110, 118-21 (5th Cir. 1941) (holding bribery of public official also constitutes scheme to defraud public), *overruled by* *United States v. Cruz*, 478 F.2d 408 (5th Cir. 1973). *But see* W. Robert Gray, Comment, *The Intangible-Rights Doctrine and Political-Corruption Prosecutions Under the Federal Mail Fraud Statute*, 47 U. CHI. L. REV. 562, 585-86 (1980) (criticizing inaccurate interpretations of *Shushan* as foundation for honest services fraud).

in order to prove fraud.²² Consequently, honest services fraud prosecutions soared during the 1970s and 1980s, and federal courts struggled to isolate the doctrine's seemingly boundless contours.²³ In response, in *McNally v. United States*,²⁴ the United States Supreme Court limited the statutes' protections to tangible money and property rights only.²⁵ The Court, nevertheless, invited congressional response, and in 1988 Congress enacted 18 U.S.C. § 1346, codifying protection of the "intangible right of honest services" under the mail and wire fraud statutes.²⁶

22. See Carrie A. Tendler, Note, *An Indictment of Bright Line Tests for Honest Services Mail Fraud*, 72 FORDHAM L. REV. 2729, 2730 (2004) (noting prosecutors not obliged to prove principal economically harmed under honest services fraud); Daniel Richman & Alan Vinegrad, "Rybicki": *The Intangible Rights Theory of Criminal Fraud*, N.Y.L.J., Jan 12, 2004, at 4 (discussing lack of money or property deprivation requirement under intangible rights doctrine).

23. See Coffee, *supra* note 20, at 427 ("few ethical or fiduciary breaches seemed beyond [intangible rights doctrine's] potential reach"). Federal courts initially applied the intangible rights doctrine to cases of political corruption, particularly bribery and failure to disclose conflicts of interests. See Tendler, *supra* note 22, at 2733-34; see also *McNally v. United States*, 483 U.S. 350, 362 n.1, 363 n.2 (1987) (Stevens, J., dissenting) (listing intangible rights doctrine cases involving public sector bribery and self-dealing). Federal courts later expanded the doctrine to include "an employer's or other principal's right to the honest services of its employees or agents." Tendler, *supra* note 22, at 2734; see also *McNally v. United States*, 483 U.S. 350, 362 n.1, 363 n.2 (1987) (Stevens, J., dissenting) (listing intangible rights doctrine cases involving private sector actors). For many commentators, *United States v. Margiotta* and *United States v. Bronston* represented the intangible rights doctrine's "high water mark" in the public and private sectors. *United States v. Margiotta*, 688 F.2d 108, 138 (2d Cir. 1982) (holding political party chairman's patronage system deprived public of "honest and faithful participation" in government); *United States v. Bronston*, 658 F.2d 920, 927 (2d Cir. 1981) (holding attorney committed honest services fraud by concealing conflict of interest between clients); Coffee, *supra* note 20, at 432 (describing *Margiotta* and *Bronston*'s reading of intangible rights doctrine as a "flood tide at its crest"). The Second Circuit upheld this expansive reading of the mail and wire fraud statutes in a string of subsequent cases. See, e.g., *United States v. Wallach*, 935 F.2d 445, 461-64 (2d Cir. 1991) (holding scheme concealing and misrepresenting corporate information to shareholders punishable under mail fraud statute); *United States v. Weiss*, 752 F.2d 777, 784 (2d Cir. 1985) (quoting *United States v. Siegel* in stating government's burden of proof); *United States v. Siegel*, 717 F.2d 9, 14 (2d Cir. 1983) (noting mail fiduciary violates mail fraud statute when breaching duty to reveal material information). But see Coffee, *supra* note 20, at 435 (asserting, under Second Circuits interpretation, "mail fraud became a crime without a clear victim"); Matheson, *supra* note 20, at 356 (noting pre-*McNally* mail and wire fraud created limitless offense); Roger J. Miner, *Federal Courts, Federal Crimes, and Federalism*, 10 HARV. J.L. & PUB. POL'Y 117, 121 (1987) (calling mail fraud statute "vehicle for the prosecution of an almost unlimited number of offenses"); Paul Mogin, *Reigning in the Mail Fraud Statute*, 26 CHAMPION 12, 13 (2002) (observing intangible rights doctrine "limited only by prosecutors' imagination"); Geraldine Szott Moohr, *Mail Fraud and the Intangible Rights Doctrine: Someone to Watch Over Us*, 31 HARV. J. ON LEGIS. 153, 166 n.51 (1994) (providing examples of scholars' criticism of mail fraud's broad, pre-*McNally* construction).

24. 483 U.S. 350 (1987).

25. See *McNally v. United States*, 483 U.S. 350, 356 (1987) (limiting mail and wire fraud statutes' protections to tangible property rights only); see also Moohr, *supra* note 23, at 166 (discussing Supreme Court's response to mail and wire fraud statutes' broad application by prosecutors).

26. See 18 U.S.C. § 1346 (codifying "intangible right of honest services" under §§ 1341 and 1343); *McNally v. United States*, 483 U.S. 350, 376 (1987) (Stevens, J., dissenting) (acknowledging Congress's ability to negate Court's *McNally* decision by amending mail and wire fraud statutes).

Though Congress intended to overrule *McNally* with § 1346, they failed to define “honest services” under the new statute, instead obliging the courts to interpret the term’s meaning.²⁷ Given the absence of a clear legislative directive, the courts construed § 1346 and its impact on mail and wire fraud in a variety of ways.²⁸ The First, Sixth, and Eleventh Circuits held that § 1346 “reinstate[s]” the entire intangible rights doctrine as it existed before *McNally*.²⁹ The Fifth Circuit, noting the inconsistency of pre-*McNally* doctrine, interpreted § 1346 only in light of pre-*McNally* case law comporting with the spirit of the statute.³⁰ Conversely, the Second Circuit held that § 1346 creates a new federal crime; therefore, courts must interpret the statute only by reference to its statutory language and history.³¹ All courts, nonetheless, agreed

27. See *United States v. Frost*, 125 F.3d 346, 364 (6th Cir. 1997) (noting every circuit addressing § 1346 has held it overruled *McNally*); *Coffee*, *supra* note 20, at 428 (asserting Congress intended § 1346 to reverse *McNally*); Edward J. Loya, Jr., Comment, *Upholding “Honest Services” While Abandoning Interpretive Principles: United States v. Rybicki*, 10 STAN. J.L. BUS. & FIN. 138, 138 (2004) (stating “far from clarifying matters, [§ 1346] left courts with unenviable task of defining ‘honest services’”); Tendler, *supra* note 22, at 2740 (noting judiciary responsible for defining scope of § 1346); see also *United States v. Brumley*, 116 F.3d 728, 742 (5th Cir. 1997) (Jolly, J., DeMoss, J., dissenting) (explaining § 1346’s legislative origins and reasons for its limited history). Judges Jolly and DeMoss stated that “[t]he phrase ‘the intangible right of honest services’ is . . . inherently undefined and ambiguous. There is no listing in the United States Code of all ‘intangible rights’; therefore, there is nothing which could be identified as ‘the intangible right of honest services.’” *United States v. Brumley*, 116 F.3d 728, 742 (5th Cir. 1997) (Jolly, J., DeMoss, J., dissenting).

28. See Loya, *supra* note 27, at 139 (observing lack of uniformity in cases despite passage of § 1346); *infra* notes 29–31 (discussing federal circuit courts of appeals’ varying approaches to defining “honest services” under § 1346).

29. See *United States v. Frost*, 125 F.3d 346, 364 (6th Cir. 1997) (interpreting § 1346 to “reinstate” doctrine of intangible rights to honest services); *United States v. Czubinski*, 106 F.3d 1069, 1076 (1st Cir. 1997) (reiterating § 1346 restores mail and wire fraud statutes to pre-*McNally* scope); *United States v. Lopez-Lukis*, 102 F.3d 1164, 1168-69 (11th Cir. 1997) (recognizing § 1346 enacted in order to overrule *McNally* and reinstate prior intangible rights law).

30. See *United States v. Brumley*, 116 F.3d 728, 733 (5th Cir. 1997) (interpreting § 1346 and listing cases demonstrating honest services’ “uneven” interpretation before *McNally*). Judge Higginbotham wrote that “Congress could not have intended to bless each and every pre-*McNally* lower court ‘honest services’ opinion. Many of these opinions have expressions far broader than their holdings. Congress, then, has set us back on a course of defining ‘honest services,’ and we turn to that task.” *Id.* (internal citation omitted).

31. See *United States v. Sancho*, 157 F.3d 918, 921-22 (2d Cir. 1998) (per curiam) (foreclosing use of pre-*McNally* cases to define § 1346). In *Sancho*, the court held that “Congress passed a new law, § 1346 What the government must prove to satisfy this element of the offense is defined by Section 1346—not by judicial decisions that sought to interpret the mail and wire fraud statutes prior to the passage of § 1346.” *Id.* at 922; see also *United States v. Handakas*, 286 F.3d 92, 103 (2d Cir. 2002) (criticizing First, Sixth, and Fifth Circuits’ methods of interpreting § 1346). Judge Jacobs wrote:

Some circuits have implemented § 1346 by resurrecting pre-*McNally* law. Thus the Sixth Circuit has held that “§ 1346 has restored the mail fraud statute to its pre-*McNally* scope.” And the Fifth Circuit . . . observed that “Congress . . . has set us back on a course of defining ‘honest services’”; and that Court has “turn[ed] to that task.” However, one of these approaches simply reinstates the entire, dissonant body of prior circuit precedent, while the other invites the creation out of whole cloth of new judicial interpretations of “honest services”—interpretations that will undoubtedly vary from circuit to circuit.

that § 1346's "intangible right of honest services," like its common law predecessor, applies to both the public and private sectors.³²

Despite § 1346's broad application across the public and private sectors, the courts' application of the honest services doctrine in the private sector developed incongruously.³³ Since the inception of the intangible rights doctrine, jurists and scholars recognized crucial differences between fiduciary duties, including honest services, among the public and private sectors.³⁴ To the courts, these differences revealed the impracticability of applying a broad construction of § 1346, historically used in the public sector, to the private sector, where economic relationships, not abstract concepts of integrity, govern the fiduciary duties and honest services one must provide another.³⁵ In response, courts carefully tailored § 1346's private sector application to address a general concern of over-criminalization, especially within the commercial sector.³⁶ Nevertheless, the circuits are fractured as to what precise factors

United States v. Handakas, 286 F.3d 92, 103 (2d Cir. 2002). *But see* United States v. Rybicki, 354 F.3d 124, 139-44 (2d Cir. 2003) (using pre-*McNally* case law to create kickback/self-dealing bifurcation of honest services fraud).

32. *See, e.g.*, United States v. Devegter, 198 F.3d 1324, 1328 (11th Cir. 1999) (affirming § 1346 applies to defrauding duties of loyalty in private sector); United States v. Frost, 125 F.3d 346, 366 (6th Cir. 1997) (noting private person violates § 1341 by defrauding private parties of right to honest services); United States v. Jain, 93 F.3d 436, 441 (8th Cir. 1996) (agreeing § 1346 extends to private sector schemes to defraud another).

33. *See infra* note 37 (detailing circuit court disagreement over prima facie requirements for private sector honest services fraud).

34. *See* United States v. Jain, 93 F.3d 436, 441 (8th Cir. 1996) (discussing "troublesome issues" concerning § 1346's "transition from public to private sector"). Judge Loken wrote:

In a democracy, citizens elect public officials to act for the common good. When official action is corrupted by secret bribes or kickbacks, the essence of the political contract is violated. But in the private sector, most relationships are limited to more concrete matters. When there is no tangible harm to the victim of a private scheme, it is hard to discern what intangible "rights" have been violated.

Id. at 442; *see also* United States v. Devegter, 198 F.3d 1324, 1328 (11th Cir. 1999) (contrasting public duty of honest services from less stringent duties involved in private sector relationships).

35. *See* United States v. Devegter, 198 F.3d 1324, 1328-29 (11th Cir. 1999) (contrasting conflicts of interest of private and public sectors in § 1346 cases). Conflicts of interest in the private sector, unlike those in the public sector, may not necessarily undermine the economic realities of a business relationship. *Id.* at 1328. Therefore, a defendant's "breach of loyalty alone" in the private sector may not always be sufficient to subject the private defendant to criminal liability under § 1346. *Id.* In response, the appellate courts have been a source of balance by limiting § 1346's application in the private sector. *See* United States v. Jain, 93 F.3d 436, 441-42 (8th Cir. 1996) (reversing doctor's conviction because nondisclosure of referral fees immaterial when quality service provided to patient); Coffee, *supra* note 20, at 430 (noting appeals courts regularly overturn private fiduciary cases because government "overextend[s]" mail and wire fraud statutes); *cf.* United States v. Lopez-Lukis, 102 F.3d 1164, 1169 (11th Cir. 1997) (holding public official's failure to disclose conflict always defrauds "the public of [official's] honest services").

36. *See* United States v. Sun-Diamond Growers of Cal., 138 F.3d 961, 973 (D.C. Cir. 1998) (noting not all private sector fiduciary breaches represent mail or wire fraud); United States v. Frost, 125 F.3d 346, 368 (6th Cir. 1997) (discussing necessity of avoiding over-criminalization of private relationships); United States v. Cochran, 109 F.3d 660, 667 (10th Cir. 1997) (cautioning against strict § 1346 interpretation in commercial setting); United States v. Czubinski, 106 F.3d 1069, 1077 (1st Cir. 1997) (observing § 1346 not intended "to

contribute to a *criminal* deprivation of the right of honest services; consequently, § 1346 has become “a truly extraordinary statute” whose “substantive force . . . varie[s] in each judicial circuit.”³⁷

In *United States v. Brown*, the Fifth Circuit held that Merrill executives did not defraud Enron of the right of its employees’ honest services when Merrill executives facilitated Merrill’s fictitious purchase of Enron assets.³⁸ Despite both the Merrill and Enron executives’ breach of a duty to disclose the buy-back agreement to their respective employers, the executives’ dishonest conduct did not defraud Enron of honest services because it was “disassociated from bribery or self-dealing and indeed associated with . . . [Enron’s] own immediate interest.”³⁹ Because Enron provided increased personal bonuses hinging on the corporation’s “legitimate interest” in increasing annual profits, the “employee services” used to obtain such bonuses were not sufficiently abused to represent a “*criminal* breach of duty to Enron.”⁴⁰ As a result, the appeals court held that where an employee and employer’s interests are sufficiently aligned and the employee perceives and acts consistently upon this mutual benefit, the employee’s conduct is “beyond the reach of the honest services theory of fraud,” regardless of whether the employee defrauds the employer of honest services.⁴¹

The majority incorrectly held that the Merrill executives’ dishonest conduct did not constitute honest services wire fraud.⁴² In looking to Enron’s personal bonus policy, the majority gave too much significance to the perceived “mutual interest” between Enron and its executives.⁴³ As a result, the majority improperly determined that the executives could not foresee that their dishonest

create . . . draconian personal regulation” in private sector); *United States v. Jain*, 93 F.3d 436, 441 (8th Cir. 1996) (holding undisclosed employee conflict absent economic harm does not justify criminal culpability); *see also* John C. Coffee, *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, 167 (1981) (cautioning expansive reading of honest services leads to possible indictment for any “civil wrong”); Tendler, *supra* note 22, at 2741 (noting concern for over-criminalizing commercial relationships “persuasive reason” for limiting § 1346’s application).

37. *See United States v. Brumley*, 116 F.3d 728, 743 n.6 (5th Cir. 1997) (Jolly, J., DeMoss, J., dissenting) (noting possible fracture among circuits regarding interpretations and impact of § 1346); *see also United States v. Rybicki*, 354 F.3d 124, 163 (2d Cir. 2003) (Jacobs, C.J., dissenting) (quoting *United States v. Brumley*, 116 F.3d 728, 743 n.7 (5th Cir. 1997) (Jolly, J., DeMoss, J., dissenting)) (providing overview of differing factors circuits require for showing of honest services fraud). In his dissent in *Rybicki*, Chief Judge Jacobs wrote that the circuits disagree as to “(1) the requisite *mens rea* to commit the crime, (2) whether the defendant must cause actual tangible harm, (3) the duty that must be breached, (4) the source of that duty, and (5) which body of law informs us of the statute’s meaning.” *See United States v. Rybicki*, 354 F.3d 124, 163 (2d Cir. 2003) (Jacobs, C.J., dissenting).

38. *See* 459 F.3d at 513-18 (5th Cir. 2006) (discussing facts of case).

39. *See id.* at 522 (detailing insufficiency of defendants’ conduct to warrant criminal culpability).

40. *Id.* (describing relationship between executives’ personal interests and Enron’s corporate interests) (internal quotation omitted).

41. *Id.* (reciting holding of case).

42. *See* 459 F.3d at 522-23 (noting majority holding).

43. *Id.* at 522 (discussing relationship between Enron and its employees).

conduct represented a “*criminal* breach of duty to Enron.”⁴⁴ In addition, the majority interpreted *Rybicki*’s categorization of honest services fraud into “bribery and kickback or self-dealing” too rigidly when asserting that the executives’ conduct could not violate § 1346 because it did not clearly fit into either category.⁴⁵ Although properly noting that “not every breach of fiduciary duty works a criminal fraud,” the Fifth Circuit erroneously created a broad and unnecessary limitation to the theory of honest services fraud, thereby protecting corporate executives from zealous, though legitimate, mail and wire fraud prosecution.⁴⁶

The majority holding also departed significantly from the honest service doctrine’s basic purpose of criminalizing egregious acts of dishonesty and deception.⁴⁷ The majority focused too narrowly upon the supposed “mutual” relationship between Enron and its executives.⁴⁸ In doing so, the majority trivialized the fundamentally deceptive and dishonest conduct of the Merrill executives and failed to recognize the significant economic harm the executives’ conduct caused Enron and its shareholders.⁴⁹ Because the executives’ conduct did result in significant economic “ramifications outside of the relationship at hand,” including fees paid to Merrill and artificially inflated stock prices, it represented precisely the kind of fraud that Congress intended to criminalize with § 1346.⁵⁰ For this reason, the majority broadly and

44. See *id.* at 522 (holding alleged scheme not within scope of § 1346). But see *id.* at 533 (Reavley, J., dissenting) (discussing factual and legal reasoning for convicting defendants of honest services wire fraud). Judge Reavley rejected the majority’s assertion that Enron and its employees had a mutual interest in the Nigerian barge deal, notwithstanding the employees’ fiduciary breach. *Id.* (Reavley, J., dissenting).

45. See *id.* at 521-22 (discussing *Rybicki*’s bifurcation of honest services fraud cases and application to majority’s decision).

46. See 459 F.3d at 522 (announcing Merrill executives’ conduct not the sort of private infidelity criminally punishable under § 1346); *supra* note 31 (quoting Judge Jacobs’ criticism of Fifth Circuit’s construction of § 1346 in *Handakas*). But see 459 F.3d at 533 (Reavley, J., dissenting) (concluding defendants’ behavior “falls squarely within the meaning” of Fifth Circuit § 1346 precedent). Unlike the Fifth Circuit’s holding in *Brumley*, limiting § 1346 violations to breaches of duty under state law, or the Second Circuit’s holding in *Rybicki*, limiting § 1346 prosecutions to breaches implicating foreseeable harm, the majority’s justification is weak given the defendants’ conduct was no mere fiduciary breach. See *id.* at 533 (Reavley, J., dissenting) (describing significant financial harm defendants’ conduct caused Enron and its shareholders).

47. See Tendler, *supra* note 22, at 2759-60 (discussing Sen. Biden’s statements regarding § 1346’s proposed private sector predecessor). Senator Biden’s statements concerning § 1346’s predecessor—a proposal to provide separate statutes for private and public sector fraud—revealed Congress’s underlying interest in regulating honesty and loyalty in private relationships that rely on trust for success. See *id.* at 2759-60. Senator Biden further stated that § 1346’s private sector predecessor is “not intended to criminalize mere breaches of fiduciary duty, or private confidence, or violations [of] ordinary rules of the workplace.” *Id.* at 2760.

48. See 459 F.3d at 533 (Reavley, J., dissenting) (rejecting assertion that mutual interest between Enron executives and corporation preclude finding honest services fraud). Judge Reavley’s dissent recognized the outside ramifications of the defendants’ conduct, notwithstanding the Enron executives’ awareness of the defendants’ deceptive actions. *Id.* (Reavley, J., dissenting); see also *supra* note 4 and accompanying text (discussing Enron and shareholders’ losses resulting from executives’ bonuses and fees paid to Merrill).

49. 459 F.3d at 532-33 (Reavley, J., dissenting) (explaining why Brown, Bayley, and Furst’s behavior rises to level of honest services fraud).

50. See *id.* at 533 (discussing harm Enron shareholders experienced and rejecting contentions that

unnecessarily excluded sufficient fraudulent “schemes and artifices” from legitimate criminal prosecution.⁵¹

Furthermore, the majority’s “mutual benefit” rule represents an unprecedented departure from the federal courts of appeals’ past and present construction of the honest services fraud doctrine.⁵² The majority’s new interpretation creates the possibility of a significant loophole by broadly protecting employee misconduct from criminal prosecution, regardless of economic harm, when the employee believes engaging in such misconduct mutually benefits the employee and employer.⁵³ This holding unduly limits future federal prosecution of employees where the employer-employee relationship, whether intentionally or incidentally, fits within the majority’s new “mutual interest” exception.⁵⁴ Ultimately, the majority holding severely diminishes the mail and wire fraud statutes’ capacity to punish and deter egregious acts of corporate deception and dishonesty under the honest services doctrine, and consequently, the court failed to protect the interests of those with the most to lose—the corporation’s shareholders, non-executive employees, and investors.⁵⁵

In *United States v. Brown*, the Fifth Circuit considered whether four Merrill executives conspired to defraud Enron of the right to its executives’ honest services by facilitating the sale of Enron power barges to Merrill, conditioned upon a secret buy-back agreement that made Merrill’s purchase a loan, thereby enabling Enron executives to artificially inflate year-end profits and receive increased personal bonuses. The majority reasoned that because the personal benefits Enron executives received originated from Enron and did not resemble a kickback or self-dealing, the Merrill defendants could not foresee that their conduct represented a “*criminal* breach of duty to Enron.” Rather, the defendants acted under the belief that their conduct, although fraudulent, represented a valid mutual interest between their own personal interest and Enron. As a result, the majority announced an unprecedented and sweeping limitation that precludes prosecution honest services fraud where an employee believes he is acting in accordance with the employer’s particular corporate goal. The majority holding unduly limits the prosecution of egregious acts of corporate deception and dishonesty, the exact reasons Congress enacted the

defendants’ conduct served a “legitimate corporate purpose”); *see also* Kobrin, *supra* note 21, at 801 (noting private scams resulting in public repercussions represent special breaches of trust).

51. *See id.* at 533 (arguing defendants’ behavior prosecutable under § 1346).

52. *See* 459 F.3d at 522 (overturning defendants’ conviction and creating new limitations for honest services fraud convictions); *supra* note 37 (discussing current circuit requirements for finding honest services mail or wire fraud).

53. 459 F.3d at 522 (presenting new limitation). The majority’s caveat—“we do not presume that it is in a corporation’s legitimate interests ever to misstate earnings—it is not”—does little to ease concern that such a loophole could arise in future cases. *Id.*

54. *Id.* (presenting majority’s new “mutual interest” limitation).

55. *See supra* notes 47, 51 and accompanying text (discussing majority’s failure to recognize impact of defendants’ deceptive conduct on Enron shareholders).

mail and wire fraud statutes. Consequently, the decision diminished deterrence of corporate misconduct while compromising the faith of the investing public who rely significantly on the honest services of corporate employees.

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