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# SUPREME COURT REVIEW

## FOREWORD: MAIL FRAUD AFTER *McNALLY* AND *CARPENTER*: THE ESSENCE OF FRAUD

CRAIG M. BRADLEY\*

### I. INTRODUCTION

In two recent decisions<sup>1</sup> the Supreme Court has attempted to discern the essence of the crime of fraud under the federal mail and wire fraud statutes.<sup>2</sup> In *McNally v. United States*,<sup>3</sup> decided in June of 1987, the Court struck down a conviction premised on the defrauding of the citizens of a state of their "intangible right to good government."<sup>4</sup> The Court held that the mail fraud statute is limited to schemes "aimed at causing deprivations of money or property."<sup>5</sup> The Court tempered *McNally* considerably in *Carpenter v. United States*<sup>6</sup> by unanimously concluding that "intangible" interests, such as an employer's confidential business information, were "property" within the mail fraud statute when misappropriated by an employee.<sup>7</sup>

The reaction to *McNally* could not have been stronger. A

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<sup>1</sup> *McNally v. United States*, 107 S. Ct. 2875 (1987) was termed "blockbusting" by Judge Aldisert, dissenting in *United States v. Piccolo*, 835 F.2d 517 (3d Cir. 1987)(Aldisert, J., dissenting).

<sup>2</sup> 18 U.S.C. §§ 1341 and 1343 (1982).

<sup>3</sup> 107 S. Ct. at 2875.

<sup>4</sup> *Id.* at 2878.

<sup>5</sup> *Id.* at 2881.

<sup>6</sup> 108 S. Ct. 316 (1987).

<sup>7</sup> *Id.* at 320-21.

Washington attorney deemed it "one of the most devastating blows to the Justice Department in years."<sup>8</sup> Similarly, Congressman Conyers of Michigan, Chairman of the House Judiciary Subcommittee on Criminal Justice, called it "a crippling blow" and introduced legislation to change the statute to include intangible rights.<sup>9</sup> The Harvard Law Review accused the Court of "fail[ing] to fulfill its role" in statutory interpretation and "insulating schemes of unquestionably criminal character from federal prosecution".<sup>10</sup> This reaction culminated in an amendment to the mail fraud statute which is discussed in the last section of this Article.

To the extent that the critics were referring to past or pending cases that would have to be reconsidered in light of *McNally*, their prediction that the decision would have a major impact was surely correct. In just over a year since *McNally* was decided, the federal courts of appeal have decided twenty-three reported cases involving *McNally* issues and twelve convictions have been wholly or partially reversed on that ground. Given the unanimity of opinion in the lower courts prior to *McNally* that intangible rights to "good government," "honest and faithful services" of an employee, etc., could be the basis of a fraud conviction, this outcome is not surprising. A conflict in the circuits is already developing as to the retroactivity of *McNally* and the problem of convictions which are based on some combination of "property" and "non-property" interests will continue to be a knotty one for cases that were tried or indicted before *McNally*. These issues will be discussed later in this Article.

The impact of *McNally* for the future is less clear. Of course the government will have to abandon the popular "intangible interests" language in future indictments.<sup>11</sup> But most cases which the government seeks to prosecute under the mail fraud statute involve either the acquisition or the deprivation of money or property. In *McNally* itself, for example, the defendants obtained over \$200,000 to which they were not entitled.<sup>12</sup> While the government was never able to pin down exactly *who* the victim was, when \$200,000 is missing, there is usually somebody who is out the money. In the political corruption cases, the federal government will frequently be able to get around *McNally* by finding a victim who is deprived of money or

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<sup>8</sup> *U.S. Prosecutors Reel in Wake of Mail Fraud Ruling*, Nat'l L. J., July 20, 1987, at 1, col. 1. See also Kaplan, *The Convictions that Weren't*, 2 CRIM. JUST. 4 (1988).

<sup>9</sup> New York Law Journal, September 1, 1987, at 1, col. 1. The legislation ultimately enacted by Congress is discussed in the last section of this Article.

<sup>10</sup> *The Supreme Court, 1986 Term*, 101 HARV. L. REV. 119, 330 (1987).

<sup>11</sup> But see the new statutory provisions discussed *infra* notes 277-94 and accompanying text.

<sup>12</sup> *McNally v. United States*, 107 S. Ct. 2875, 2878 (1987).

property. Similarly, given *Carpenter*, in many cases in which money is not directly involved, some sort of intangible "property" interest may be found, depending on where the courts draw the line between property and non-property rights. These issues will be discussed in greater detail later in this Article.<sup>13</sup>

The more important question, however, underlying all the others, including those dealt with in *McNally* and *Carpenter* is, "What is the essence of fraud?" In *McNally* the Court partially answered this question by holding that money or property must be involved.<sup>14</sup> But there are further questions that must be answered before the concept of fraud, and hence the meaning of the mail fraud statute, is fully understood. Specifically, the questions are: Does "fraud" require a victim? and, Does a fraud imply either a loss to the victim, an unjust gain to the perpetrator, both, or neither?

These questions are not merely of general, theoretical interest. They are of immediate and vital concern to attorneys and judges concerned with litigating cases under the mail fraud statute. Consider the statute:

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 . . . for the purpose of executing such scheme or artifice or attempting to do so [uses the mails or causes them to be used] shall be fined . . .<sup>15</sup>

Note that the statute refers to two types of "scheme(s) or artifice(s)." Those "to defraud" and those "for obtaining money or property by means of false pretenses, representations or promises."<sup>16</sup> In *McNally* the Court held that the term "to defraud" in the first clause was implicitly limited to money or property, just as the prohibition against "false pretenses, representations or promises" was explicitly so limited in the second clause.<sup>17</sup> The Court *did not* thereby necessarily conclude that the two clauses were identical<sup>18</sup> but only that the *object* of the scheme, money or property, must be the same. *McNally* further held that "defraud" in Clause 1,

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<sup>13</sup> See *infra* notes 151-52 and accompanying text.

<sup>14</sup> *McNally*, 107 S. Ct. at 2881.

<sup>15</sup> 18 U.S.C. § 1341 (1982). Section 1343 is identical except that it refers to use of "wire, radio or television transmission in interstate commerce" instead of the mails. 18 U.S.C. § 1343 (1982).

<sup>16</sup> Actually, the statute also prohibits a third type of scheme as well: "or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security or other article or anything represented to be [such a counterfeit article] . . ." 18 U.S.C. § 1341 (1982).

<sup>17</sup> *McNally*, 107 S. Ct. at 2880 (1987).

<sup>18</sup> As Justice Stevens observed, dissenting in *McNally*: "The Court recognizes that the 'money or property' limitation of the second clause does not actually apply to prose-

“usually signif[ies] the *deprivation* of something of value.”<sup>19</sup> It did *not* decide whether the “obtaining” language of Clause 2 similarly was limited to such deprivations or whether an unjust gain alone might suffice to convict under that clause.<sup>20</sup> Consider the following two cases:

Case I: A and B are polygraph operators who share office space. Because of a personal grudge, A takes B’s letter renewing his license from the “Out” box and destroys it. Then he writes B’s customers, under an assumed name, telling them that B is unlicensed. A has no expectation of any gain from this activity.<sup>21</sup>

Case II: A is employed by Megacorp as a purchasing officer. He is required by the company to “accept no outside remuneration in any form from any source with which the company does business and to disclose offers of any such remuneration to the company.” Megacorp sets the price at which it will purchase veeblefizers. A’s job is to find a supply at that price that meets Megacorp’s quality guidelines. A arranges with North American Veeblefizer Corp. to supply Megacorp’s needs at the fixed price and conforming to Megacorp’s specifications. North American pays A \$10,000 for giving it the business. A does not disclose it. The comptroller of Megacorp will testify that the company has “no procedure” for somehow taking the \$10,000 as a discount. A should simply have given it back.<sup>22</sup>

In Case I there is a loss to the victim but no gain to the defendant. In Case II there is a gain but no loss.<sup>23</sup> Neither *McNally* nor *Carpenter* decided explicitly whether either of these cases, if charged

cutions under the first clause.” *McNally v. United States*, 107 S. Ct. 2875, 2887 (1987)(Stevens, J., dissenting).

<sup>19</sup> *Id.* at 2881.

<sup>20</sup> “Although the Government now relies in part on the assertion that the petitioners obtained property by means of false representations . . . there was nothing in the jury charge that required such a finding.” *Id.* at 2882.

<sup>21</sup> These are the facts of *United States v. Baldinger*, 838 F.2d 178 (6th Cir. 1988). The Court of Appeals reversed the defendant’s conviction on the ground that there was no motive to “*gain*” and that such a motive is essential to a fraud case.

<sup>22</sup> The facts of this case are similar to *United States v. Covino*, 837 F.2d 35 (2d Cir. 1988) *See also* *United States v. Lemire*, 720 F.2d 1327 (D.C. Cir. 1983)(defendant employee provided information to a shipper that allowed it to underbid competitors for his firm’s shipping business. He was held to have defrauded his firm of its intangible right to the loyal and faithful services of its employee, though his firm lost no money); *McNally*, 107 S. Ct. at 2879; *United States v. Murphy*, 836 F.2d 248 (6th Cir. 1988); *United States v. Mandel*, 591 F.2d 1347 (4th Cir. 1979).

<sup>23</sup> Arguably, however, the class of competitors for the veeblefizer contract were victims who suffered a “loss”—for example, the opportunity to compete for the contract. *See infra* notes 220-22 and accompanying text. For the purposes of analyzing this case it is sufficient to assume that, as in *Covino*, the government failed to charge any such loss.

under a "money or property," rather than an "intangible rights" theory, is a violation of the mail fraud statute despite the fact that both, obviously, involve "property." Yet the answer to the question of whether mail fraud requires either a gain, a loss, neither or both is at the heart of many of the cases that have troubled the courts in recent years<sup>24</sup> and that will trouble them even more now that *McNally* has eliminated the "intangible interests" approach which had allowed the government to proceed to trial without ever clearly defining who was defrauded of what.

## II. THE *MCNALLY* AND *CARPENTER* HOLDINGS

The *McNally* case presented a good fact situation to the Court because it typified the government's cavalier approach to defining both the victim and the object of the fraud, an approach that the courts of appeals had been enthusiastically endorsing for years. At first blush, *McNally* seems to present a clear case of criminality: Kentucky Democratic Party officials getting rich at the taxpayer's expense. But like cotton candy, though this case appears substantial, when it is bitten into, there is no substance. The defendants in *McNally* were not charged with defrauding the state of money<sup>25</sup> but only with defrauding the citizens of their intangible right to good government. A complete understanding of the case requires a trip into the darkest reaches of Kentucky politics.

In 1974, after the election of Democratic Governor Carroll, defendant Hunt<sup>26</sup> became Democratic Party Chairman. As such he had de facto control over the selection of insurance agencies with which the state would do business.<sup>27</sup> He arranged with Wombwell Insurance Company to obtain workmen's compensation insurance for the state. Wombwell's job was to arrange coverage with a big national insurer, in this case Hartford Insurance Company.<sup>28</sup> Pursuant to established practice and consistent with Kentucky law, Hartford paid Wombwell a "commission" of 5% of the premiums tendered. This totaled \$1,051,000 over four years.<sup>29</sup> However, this money was never destined for Wombwell alone. Rather Wombwell

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<sup>24</sup> *E.g.*, *Baldinger*, 838 F.2d at 178; *Covino*, 837 F.2d at 35; *Lemire*, 720 F.2d at 1327.

<sup>25</sup> "[T]here is no charge . . . that the Commonwealth itself was defrauded of any money or property." *McNally*, 107 S. Ct. at 2881.

<sup>26</sup> Hunt pled guilty to one count of intangible rights mail fraud and one count of tax fraud. Consequently he was not before the Supreme Court. *Id.* at 2879.

<sup>27</sup> *Id.*

<sup>28</sup> Brief for the United States at 3, *McNally v. United States*, 107 S. Ct. 2875 (1987)(No. 86-422). United States Fire Insurance also supplied coverage during part of the period covered in the indictment. *Id.*

<sup>29</sup> *McNally*, 107 S. Ct. at 2878.

agreed with Hunt that it would receive \$50,000 per year (a total of \$200,000 over four years) and it distributed the rest (\$851,000) to various other insurance agencies designated by Hunt. Over four years 21 agencies were so designated and they received the \$851,000. *It was undisputed that this practice of sharing commissions among insurance agents was an accepted and lawful matter of political patronage in Kentucky.*<sup>30</sup>

So far then, even in the government's view, there was no fraud. The fraud occurred when Hunt, Gray (a high state government official)<sup>31</sup> and McNally, a private businessman, set up a fake "insurance agency," Seton Investments, to receive a share of these commissions. Pursuant to Hunt's instructions, Wombwell paid \$200,000 to Seton Investments over four years.<sup>32</sup> McNally was the nominal owner of Seton; Hunt's and Gray's interest was secret, but they got the money.<sup>33</sup>

Hunt pled guilty to one count of mail and one of tax fraud.<sup>34</sup> Gray and McNally<sup>35</sup> were indicted for one count of conspiracy to commit mail fraud and seven counts of mail fraud, six of which were dismissed before trial.<sup>36</sup> The single remaining mail fraud count involved a check mailed by Hartford to Wombwell and alleged both that the defendants had devised a scheme (1) to "defraud the citizens of Kentucky . . . of their right to have the Commonwealth business and its affairs conducted honestly, impartially, free from corruption, bias, dishonesty, deceit, official misconduct and fraud"<sup>37</sup> and (2) "to obtain money (and property) by means of false and fraudulent pretenses. . . ."<sup>38</sup> Though the government argued that

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<sup>30</sup> "[I]t was not charged that requiring the Wombwell agency to share commissions violated state law. We should assume that it did not." *Id.* at 2881 n.9.

<sup>31</sup> Brief for the United States at 4.

<sup>32</sup> *Id.*

<sup>33</sup> *Id.* McNally's cut came from another agency, Snodgrass, which, at Hunt's direction, got \$77,500 from Wombwell and passed it on to McNally. *Id.* at 5.

<sup>34</sup> *McNally*, 107 S. Ct. at 2881.

<sup>35</sup> Since Mr. McNally was not a government official, nor a person who, like Hunt, exercised de facto control over governmental affairs, he clearly owed no such duty to the citizens of Kentucky. He was convicted on the theory that he aided and abetted the scheme. Brief for the United States at 10-11.

<sup>36</sup> The six counts dismissed alleged Seton's tax returns as mailings in furtherance of the scheme. They were dismissed on the ground that "mailings required by law to be made can only be viewed as in furtherance of a scheme prohibited by 18 U.S.C. § 1341 where the mailed documents are themselves false or fraudulent," which was not alleged. Brief for the United States at 5 n.5.

<sup>37</sup> Brief for the United States at 9 (quoting indictment).

<sup>38</sup> *Id.* The mail fraud count also alleged that the scheme had the purpose of defrauding the citizens of their right to be made aware of all relevant facts when selecting an insurance agent. The District Court did not instruct on this purpose, holding that it

the second allegation was clearly proved and was sufficient by itself to sustain the conviction,<sup>39</sup> the Court brushed off this point, discussing the case as if only the first allegation were contained in the indictment.<sup>40</sup> The defendants were convicted of the single substantive count and the conspiracy count.<sup>41</sup>

Having now been apprised of the facts, the reader may still be rather uncertain about just where the fraud occurred. Who was defrauded of what? If the money did not belong to the State of Kentucky (the government conceded that it did not),<sup>42</sup> why were the citizens of Kentucky defrauded of their right to good government? What exactly did the defendants do to commit the fraud?<sup>43</sup> The government's brief is vague on this point. It points out that Hunt and Gray used the \$200,000 for personal purposes,<sup>44</sup> but this alone is not fraud. It points out that they "concealed their ownership of Seton and the fact that it was not a bona fide insurance agency" from Wombwell,<sup>45</sup> but why is this a fraud against the citizens of Kentucky? It was not charged that Wombwell was defrauded. While it is clear that Hunt and Gray were *not* entitled to the money, it is not clear who *was* entitled to it. Had it been clear, the government could have charged this as a straightforward fraud against that victim.<sup>46</sup>

In fact, the government's theory (though it never appears explicitly in its brief), is that Hunt and Gray breached a *fiduciary* duty to

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was subsumed in the purpose to deny the right to honest government. *McNally v. United States*, 107 S. Ct. 2875, 2879 (1987).

<sup>39</sup> The government, evidently feeling uneasy about defending the vague "intangible rights" theory in this case, advanced, as its primary argument, that the Court need not reach that point because the defendants had also been convicted in the same count, for obtaining property by false pretenses. Brief for the United States at 16-22.

<sup>40</sup> "There was no charge . . . that the Commonwealth itself was defrauded of any money or property. . . . Although the government now relies in part on the assertion that the petitioners obtained property by means of false representations to Wombwell. . . . There was nothing in the jury charge that required such a finding." *McNally*, 107 S. Ct. at 2882.

<sup>41</sup> *Id.* at 2879.

<sup>42</sup> "[T]hose commissions were not the Commonwealth's money. *McNally*, 107 S. Ct. at 2881. "[T]here is no charge . . . that the Commonwealth itself was defrauded of any money or property [or] what in the absence of the scheme the Commonwealth would have paid a lower premium or secured better insurance." *Id.*

<sup>43</sup> "[T]he government has never claimed that [Hunt's] directing Wombwell to split excess commissions with valid insurance agencies not controlled by Hunt and Gray violated any law." Brief for the United States at 34 n.126.

<sup>44</sup> *Id.* at 4.

<sup>45</sup> *Id.*

<sup>46</sup> See *infra* notes 220-22 and accompanying text arguing that the government could have designated the class of legitimate insurance agencies as the victim since, had Seton not gotten the money, it would have been divided in some way among that class.



disclose their interest in Seton to some, unspecified, person or entity in Kentucky government and, by their silence, defrauded the citizens of good government, despite the fact that Kentucky law required no such disclosure.<sup>47</sup> Yet it would seem that their behavior would be no less “fraudulent” if they *had* told somebody about it, if only they had known who they were supposed to tell.

The Supreme Court, treating this strictly as a conviction based on the intangible right to good government,<sup>48</sup> recognized that the statute set forth two different offenses. Schemes “to defraud” (Clause 1) and schemes “for obtaining money or property by false pretenses, representations or promises.” (Clause 2)<sup>49</sup> Only Clause 1, the Court assumed, was charged in this case. The courts of appeals had all reasoned that since Clause 1, “to defraud,” did not mention money or property, it was not necessary that these be the object of such a scheme. Thus deprivation of intangible rights to good government, loyal services, etc., had been recognized as objects of fraud.<sup>50</sup>

However, the Supreme Court observed, quite correctly<sup>51</sup> that the term “fraud” itself, both in its original understanding and, apparently, in Congress’ understanding at the time of the enactment of the mail fraud statute in 1872 and its amendment in 1909,<sup>52</sup> contemplated “‘wronging one in his property rights by dishonest methods or schemes.’”<sup>53</sup> Clause 2 had been added in 1909,<sup>54</sup> not to create a new crime of deprivation of money or property, but to

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<sup>47</sup> This theory of the government’s case is helpfully supplied by the Supreme Court in footnote 9 of its opinion. *McNally v. United States*, 107 S. Ct. 2875, 2881 n.9 (1987). It does not appear in the government’s brief. The indictment simply charged that the citizens of Kentucky were defrauded of their “right to be made aware of all relevant and pertinent facts and circumstances when selecting an insurance agent” without specifying which misrepresentations (or failures to disclose) by the defendants had constituted the fraud. *Id.* at 2879 n.4.

<sup>48</sup> “Although the Government now relies in part on the assertion that the petitioners obtained property by means of false representations to Wombwell, . . . there was nothing in the jury charge that required such a finding.” *Id.* at 2882.

<sup>49</sup> *Id.* at 2881.

<sup>50</sup> *Id.* at 2881. See also cases listed in footnotes 2-4 of Justice Steven’s dissent. *Id.* at 2887 nn.2-4 (Stevens, J., dissenting).

<sup>51</sup> See *infra* notes 126-29 and accompanying text. See also Goldstein, *Conspiracy to Defraud the United States*, 68 *YALE L.J.* 405, 420 (1959) (noting the common law understanding that fraud was limited to “money or property”).

<sup>52</sup> 17 Stat. 302 and 323 (1872). The original statute referred only to schemes to defraud, not mentioning “obtaining money or property by means of false pretenses, etc.”

<sup>53</sup> *McNally*, 107 S. Ct. at 2881 (quoting *Hammerschmidt v. United States*, 265 U.S. 182, 188 (1929)).

<sup>54</sup> 35 Stat. 1130 (1909).

“codify” the holding of *Durland v. United States* in 1896<sup>55</sup> that the schemes to defraud prohibited by the mail fraud statute were not limited to “false pretenses” as that term was then understood<sup>56</sup> such as representations as to past or present facts but included representations as to the future.<sup>57</sup>

This Article will argue later<sup>58</sup> that to write off the language “or for obtaining money or property by means of false pretenses, representations, or promises” as *merely* a codification of *Durland*, is to ignore the clear meaning of the words. Nevertheless, there is certainly nothing on the face of the statute or anywhere in the legislative history of either the original 1872 enactment or the 1909 amendment to suggest that Congress contemplated the criminalization of schemes that were not aimed at either money or property.<sup>59</sup> The 1909 addition of the phrase referring to money or property simply reflected Congress’ understanding that money or property were necessarily a part of schemes to defraud. There is no basis for the assumption that the specific reference to money or property in Clause 2 was meant to expand the concept of “defraud” in Clause 1 to include non-property interests.

Having thus discerned the purpose of the statute, the Court applied the rule of lenity to choose the narrower reading limiting it to schemes aimed at money or property, which reading comported with Congress’ apparent purpose and was consistent with the traditional understanding of “scheme to defraud.”<sup>60</sup>

In reversing the courts of appeals reliance on the intangible rights theory, the Court seemed to be holding that only *tangible*

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<sup>55</sup> 161 U.S. 306 (1896).

<sup>56</sup> Wrongly, as it turns out, see *infra* note 122 and accompanying text.

<sup>57</sup> *McNally*, 107 S. Ct. at 2881 n.7. This information about the meager legislative history of the 1909 revision, which was limited to a note in the margin of a 1901 Senate report, is found in Pearce, *Theft by False Promises*, 101 U. PA. L. REV. 967, 980 n.56 (1953).

<sup>58</sup> See *infra* notes 226-30 and accompanying text.

<sup>59</sup> For example, the sponsor of the legislation, Representative Farnsworth, suggested that it was “to prevent the frauds, which are mostly gotten up in the large cities . . . by thieves, forgers and rascallions generally, for the purpose of deceiving and fleecing the innocent people of this country.” CONG. GLOBE, 41st Cong., 3d Sess. 35 (1870) (statement of Rep. Farnsworth). He then went on to describe such schemes, all of which involved cheating people out of money. *Id.* See Rakoff, *The Federal Mail Fraud Statute (Part I)*, 18 DUQ. L. REV. 771, 816-817 (1980), and Note, *The Intangible Rights Doctrine and Political Corruption Prosecutions Under the Federal Mail Fraud Statute*, 47 U. CHI. L. REV. 562, 569-572 (1980), for a full discussion of the 1909 amendment.

It is, however, true, as Justice Stevens argued, dissenting in *McNally*, that the reading that the courts of appeals had given the statute, is a *permissible* one, given the statutory language. *McNally*, 107 S. Ct. at 2882 (Stevens, J., dissenting).

<sup>60</sup> *McNally*, 107 S. Ct. at 2881 (citing *United States v. Bass*, 404 U.S. 336, 347 (1971); *United States v. Universal CIT Corp.*, 344 U.S. 218, 221-222 (1952)).

property could be the object of a fraud. Indeed, the lower court in *McNally* had expressly distinguished between the “intangible right, such as honest service [and] a scheme to obtain tangible property through fraud.”<sup>61</sup> Certainly, it was such tangible property that Congress was concerned with when the statute was enacted.<sup>62</sup> The Supreme Court even observed that *Haas v. Henkel*,<sup>63</sup> in which the Court had upheld a conviction for conspiracy to defraud the government for the bribing of a government official to make advance disclosure of a cotton crop report, was inapplicable.<sup>64</sup> That statute, which prohibited conspiracy to defraud the United States,<sup>65</sup> protected different interests (“the protection and welfare of the government”<sup>66</sup>) than the mail fraud statute (protection of “individual property rights”).<sup>67</sup> Thus, *McNally* definitely indicated that disclosure of the confidential information of a private business, as opposed to the government, would not involve deprivation of a “property right” punishable under section 1341.<sup>68</sup> However, whatever the *McNally* dictum may have suggested, *Carpenter* made it clear that “property” included intangible interests such as a business’ right to confidential information and that the relevant question is not, “was the object of the fraud tangible or intangible?” but “was it property, including intangible property, or not?”<sup>69</sup> The meaning of this enigmatic distinction is far from clear and will be the subject of discussion later in this Article.

Justice Stevens, in a forceful dissent in *McNally*, pointed out the unanimity of the courts of appeals in supporting the intangible rights theory, disagreed with the majority’s reading of the original purpose of Congress<sup>70</sup> and argued that, whatever the original pur-

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<sup>61</sup> *United States v. Gray*, 790 F.2d 1290, 1295 (6th Cir. 1986) (quoting *United States v. Alexander*, 741 F.2d 962, 964 (7th Cir. 1984)).

<sup>62</sup> See *supra* note 59.

<sup>63</sup> 216 U.S. 462 (1910).

<sup>64</sup> *McNally v. United States*, 107 S. Ct. 2875, 2881 n.8 (1987).

<sup>65</sup> 18 U.S.C. § 371 (1982).

<sup>66</sup> *McNally*, 107 S. Ct. at 2881 n.8.

<sup>67</sup> *Id.* While *Henkel* was a “strained extension”, Goldstein, *supra* note 41, at 426, of the concept of fraud, the Court does seem to have accurately stated the rationale of the case. *Id.*

<sup>68</sup> Thus “fraud” in the Conspiracy to Defraud the Government statute means something different than “fraud” in the mail fraud statute.

<sup>69</sup> See *infra* note 93.

<sup>70</sup> Justice Steven’s argument from history is not convincing. See *infra* notes 220-23 and accompanying text. In particular, Justice Stevens gives the following example from an 1809 British case. “A, a commissary—general of stores in the West Indies makes contracts with B to supply the stores on the condition that B should divide the profits with A.” *McNally*, 107 S. Ct. at 2887 (Stevens, J., dissenting).

Contrary to Justice Stevens’ assertion, A has here defrauded his employer, not only

pose of Congress in 1872, the Court should not be bound by it today, given that the terms of the statute supported the intangible rights approach.<sup>71</sup>

Why did the Court, which has so often taken a very expansive view of federal powers under the Constitution and federal criminal statutes,<sup>72</sup> adopt this "crabbed construction"<sup>73</sup> of the mail fraud statute? Because, in the Court's view, to uphold the conviction in this case would have been to "construe the statute in a manner that leaves its outer boundaries ambiguous and involves the Federal Government in setting standards of disclosure and good government for state and local officials."<sup>74</sup> As will be discussed, by requiring that a "property" interest, albeit, as clarified in *Carpenter*, not necessarily a tangible property interest, be involved, the Court, while not choosing the best line of reasoning available, has nevertheless gone far toward eliminating many of the problems of overbreadth that had led to strong criticism of the mail fraud statute as it had been applied.<sup>75</sup>

Another point must be made about *McNally*. The Court accepted, at least arguendo, the theory advanced successfully by the Government in the Second Circuit in *United States v. Margiotta*.<sup>76</sup> In *Margiotta*, a case with facts remarkably similar to *McNally*, the Second Circuit Court of Appeals held that if a person exercises the powers of a government official, he owes the same duties to the pub-

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of his loyal services, but also of money. Since B was willing to supply the stores for half the profit ostensibly received (the other half having gone to A), A could have negotiated the contract at a lower price that reflected that reduced profit. Thus, A has defrauded his employer of the price increase that was necessary to pay kickbacks to himself.

<sup>71</sup> *Id.* at 2882-86 (Stevens, J. dissenting).

<sup>72</sup> See, e.g., Bradley, *Racketeering and the Federalization of Crime*, 22 AM. CRIM. L. REV. 213 (1985)(discussing the Court's broad interpretation of federal powers under the commerce clause and under various federal criminal statutes).

<sup>73</sup> *McNally*, 107 S. Ct. at 2889 (Stevens, J., dissenting).

<sup>74</sup> *Id.* at 2881.

<sup>75</sup> See Coffee, *The Metastasis of Mail Fraud: The Continuing Story of the Evolution of a White Collar Crime*, 21 AM. CRIM. L. REV. 1 (1983)[hereinafter Coffee, *Metastasis*]; Hurson, *Limiting the Mail Fraud Statute — A Legislative Approach*, 20 AM. CRIM. L. REV. 423 (1982); 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 (1981)[hereinafter Coffee, *Tort to Crime*]; *United States v. Weiss*, 752 F.2d 777, 791 (2d Cir. 1984)(Newman, J., dissenting), *cert. denied*, 474 U.S. 944 (1985); *United States v. Margiotta*, 688 F.2d 108, 140 (2d Cir. 1982)(Winter, J., dissenting), *cert. denied*, 461 U.S. 913 (1983).

<sup>76</sup> 688 F.2d 108 (2d Cir. 1982). Like Mr. Hunt, Mr. Margiotta was a political boss who received a secret share of insurance commissions kicked back from the government's insurers for political patronage purposes. *Id.* at 114. The only difference is that Margiotta, unlike Hunt, was a licensed insurance broker and consequently had at least a colorable claim of legality in the receipt of a share of the commissions.

lic that an actual officeholder does.<sup>77</sup> In *McNally* the Supreme Court “assume[d] that Hunt, as well as Gray was a state officer.”<sup>78</sup> *Margiotta* has been strongly criticized by both Professor Coffee<sup>79</sup> and Mr. Hurson<sup>80</sup> in leading articles condemning the expansion of the mail fraud statute. However, that criticism was in the context of the intangible rights theory of prosecution. It seemed particularly unfair, when the only alleged wrong was breach of a fiduciary duty to “the citizens,” to prosecute a person for such a wrong who didn’t even occupy the formal position of a fiduciary. After *McNally*, however, when a person, such as Margiotta or Hunt, is in a position to defraud some victim, be it the government or an individual, of money or property, the fact that he does not formally hold office should not be an impediment to prosecution. Once the essence of the crime becomes deprivation of property rather than breach of fiduciary duty, the arguable absence of a fiduciary relationship to the victim becomes irrelevant.

In *Carpenter*,<sup>81</sup> a case that the Court agreed to hear well before the *McNally* decision was rendered,<sup>82</sup> the Court, as noted, unanimously made it clear that “property” for the purposes of mail fraud, was not limited to tangible property. In that case, petitioner Winans was a reporter for the *Wall Street Journal* who wrote the “Heard on the Street” column.<sup>83</sup> He had recognized that, when that column

<sup>77</sup> *Id.* at 122.

<sup>78</sup> *McNally*, 107 S. Ct. at 2881.

<sup>79</sup> Coffee, *Metastasis*, *supra* note 75, at 15 (“*Margiotta* expanded the scope of the covered behavior to include not only excessive zeal in helping one’s friends and business associates but also one’s political party or presumably any other interest group one serves. . . . *Margiotta* . . . can be read to include *ideological* conflicts of interest as opposed to simple economic ones.”).

Margiotta also personally profitted from this scheme, but that was not, apparently, essential to the “intangible rights” theory of the government’s case. *Margiotta*, 688 F.2d at 114.

<sup>80</sup> Hurson, *supra* note 75, at 439.

If a jury finds that a defendant has a substantial influence in government, a conviction for mail fraud will follow from the mere establishment of a failure to disclose some piece of material information and the mailing of a letter. . . . [T]he Second Circuit in *Margiotta* opened the door for criminal prosecution of almost anyone playing a role in the political process who merits the prosecution’s disfavor.

*Id.* See also Jeffries, *Legality, Vagueness and the Construction of Penal Statutes*, 71 VA. L. REV. 189, 234-242 (1985).

<sup>81</sup> *Carpenter v. United States*, 108 S. Ct. 316 (1987).

<sup>82</sup> Certiorari was granted in *McNally* on December 6, 1986, 479 U.S. 1005 (1986), and in *Carpenter* on December 15, 1986, 479 U.S. 1016 (1986). Perhaps it was the Court’s original intent to strengthen *McNally* by applying it to insider trading cases, rather than to decide *Carpenter* in a way that directly contradicted the *McNally* footnote as to the meaning of “property,” see *infra* note 92-93, and thereby substantially undercut the *McNally* holding.

<sup>83</sup> *Carpenter*, 108 S. Ct. at 318-19.

reported favorably on a company, that company's stock tended to increase in price. Consequently, he entered into an agreement with petitioner Felis and one Peter Brand, stockbrokers, to trade on this knowledge.<sup>84</sup> This was in violation of specific *Wall Street Journal* employment guidelines. In all, the scheme netted the participants about \$690,000.<sup>85</sup> Winans and Felis were convicted of securities, mail and wire fraud and conspiracy. Carpenter was convicted of aiding and abetting.<sup>86</sup>

The government, not anticipating the *McNally* holding, did not argue that the *Wall Street Journal* was deprived of "property" in its original brief.<sup>87</sup> Rather the government's brief focused on whether Winan's abuse of his position of trust with the *Journal* was sufficient to constitute "fraud," and whether the publication of the *Journal*, which required use of the mails and interstate wires, was enough to satisfy the mailing requirements.

The Court had "little trouble"<sup>88</sup> deciding these issues. As to the first, it quoted the New York Court of Appeals to the effect that exploitation of confidential information acquired "by virtue of a confidential or fiduciary relationship with another" is a breach of fiduciary duty and that such a breach is an aspect of fraud.<sup>89</sup> As to the second point, the Court observed that "circulation of the 'Heard' column was not only anticipated but an essential part of the scheme."<sup>90</sup> Consequently the mailings and wirings associated with that circulation could be charged to the defendants.

The third issue decided in *Carpenter* was raised by the *McNally* decision: Assuming that the misuse of the confidential publication schedule and contents of the "Heard" column may be "trick, deceit, chicane or overreaching" as *McNally* required,<sup>91</sup> was there a deprivation of "property" under *McNally*? As previously discussed,<sup>92</sup> *McNally* seemed to suggest that the crucial distinction was between tangible property and intangible interests which were not "prop-

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<sup>84</sup> Petitioner Carpenter was Winans' roommate. He was aware of the scheme and received some of the profits from it. Brief for the United States at 6, *Carpenter v. United States*, 108 S. Ct. 316 (1987)(No. 86-422).

<sup>85</sup> *Carpenter*, 108 S. Ct. at 319.

<sup>86</sup> *Id.* at 318

<sup>87</sup> This issue was addressed in a Supplemental Brief. Supplemental Brief for the United States, *Carpenter*, 108 S. Ct. at 316 (No. 86-422).

<sup>88</sup> *Carpenter*, 108 S. Ct. at 321.

<sup>89</sup> *Id.* at 321-22 (quoting *Diamond v. Oremuno*, 24 N.Y.2d 494, 497, 248 N.E.2d 910, 912, 301 N.Y.S.2d 78, 80 (1969)).

<sup>90</sup> *Id.* at 322. That is, if the stock was to rise in price, potential buyers had to read about the company in the *Journal*.

<sup>91</sup> *McNally v. United States*, 107 S. Ct. 2875, 2881 (1987).

<sup>92</sup> See *supra* notes 68-69 and accompanying text.

erty," the latter not being subject to the mail fraud statute. In *Carpenter*, the Court made it clear that certain intangible interests, including "confidential business information" are "property" under the terms of the statute.<sup>93</sup> It reaffirmed *McNally*, however, by holding that the *Journal's* "contractual right to [Winan's] honest and faithful service" was "too ethereal in itself to fall within the mail fraud statute."<sup>94</sup> The issue thus posed, where to draw the line between those intangible rights that are and are not "property," will be discussed later in the Article.<sup>95</sup>

The scheme prosecuted in *Carpenter* does not seem quite as much a cotton candy crime as that in *McNally*. Here, at least, there is an identifiable victim who was, in a sense, tricked or misled by the scheme. Still, there are problems when this case is compared to a classic fraud in which the victim is tricked into giving his or her money or property to the defrauder.

First, there was arguably no "trick, chicane, deceit or overreaching" which, as the Court recognized in *McNally*,<sup>96</sup> is an element of fraud. Winans neither lied nor gave a false impression by his conduct. He did, however, breach a fiduciary duty not to disclose confidential information and a further duty to disclose such breaches to his employer and, in doing so, caused potential harm to the employer. This has long been recognized as satisfying the "deceit" element of a fraud.<sup>97</sup>

Second, it is not clear how the *Journal* was deprived of "property" here. As the case was originally tried by the government, the fraudulent behavior was the failure to disclose the breach and the harm to the victim was the loss of the *Journal's* intangible right to the honest and faithful services of its employee. After *McNally*, the government filed a supplemental brief urging that the fraudulent behavior was the embezzlement of confidential information and the harm was the loss of the exclusive use of that information.<sup>98</sup> The Court

<sup>93</sup> *Carpenter*, 108 S. Ct. at 320.

<sup>94</sup> *Id.*

<sup>95</sup> See *infra* notes 151-52 and accompanying text.

<sup>96</sup> *McNally*, 107 S. Ct. at 2881.

<sup>97</sup> E.g., *Haas v. Henkel*, 216 U.S. 462 (1910); Goldstein, *supra* note 51, at 425-27. It has long been recognized that conduct alone may constitute fraud. For example, the wearing of the dress of an Oxford student in order to obtain credit at local stores was held to be a false pretense. *Rex v. Barnard*, 173 Eng. Rep. 342 (1837). Mere silence, even when it does not constitute an affirmation, as in *Barnard*, will suffice if the defendant stands in a fiduciary relationship to the victim. 2 W. LAFAVE & A. SCOTT, SUBSTANTIVE CRIMINAL LAW § 8.7(b)(3) (1986).

<sup>98</sup> Petitioners used this misimpression [that Winans was a faithful employee] and Winans' position of trust to gain access to a continuing flow of confidential information. That flow started because Winans made at least implicit representations of

adopted this latter theory,<sup>99</sup> endeavoring to conform to the “property” limitation of *McNally*.

By holding that “the concept of fraud includes the act of embezzlement”<sup>100</sup> the Court ignored the very history of fraud that it had relied on in *McNally*. On the contrary, the crime of fraud had always been understood by both Congress<sup>101</sup> and the Supreme Court<sup>102</sup> as proscribing only the fraud of false pretenses,<sup>103</sup> rather than any crime that involved “fraudulent” behavior, which crimes included larceny, embezzlement, forgery, and larceny by trick as well as false pretenses.<sup>104</sup> According to the Court’s holding in *Carpenter*, any employee who helps himself to money or property which his or her employer has entrusted to him or her is now guilty of the federal offense of wire or mail fraud if only the mails or wires are used or caused to be used in some way. The Congress that enacted this statute would surely have been surprised at this declaration.<sup>105</sup>

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loyalty at the outset of his employment, and continued because Winans failed to disabuse the Journal of its mistaken belief [that he was still loyal] and to comply with his specific duty to disclose leaks of the Heard column.

Brief for the United States at 10, *Carpenter*, 108 S. Ct. 316.

By contrast to this “failure to disclose” theory, the government urged in its Supplemental Brief that the crime was misappropriation of confidential information. Supplemental Brief for the United States at 1-2. Obviously failure to disclose has nothing to do with this crime—it occurs as soon as the information is misappropriated, whether or not the defendant reports that dereliction. *Id.*

<sup>99</sup> *Carpenter*, 108 S. Ct. at 321. The indictment, which was 21 pages long, included both of these theories. Joint Appendix at 1-21.

<sup>100</sup> *Carpenter*, 108 S. Ct. at 321.

<sup>101</sup> See *supra* note 59 for a discussion of section 1341’s legislative history. “The typical false pretenses statute is almost identical to section 1341 as amended in 1909.” Note, *supra* note 59, at 573-74.

<sup>102</sup> Note, *supra* note 59, at 573-74 (citing *Durland v. United States*, 161 U.S. 306 (1896)).

<sup>103</sup> *Id.* (“The mail fraud statute should properly be interpreted as prohibiting [only] the fraud of false pretenses.”).

<sup>104</sup> E.g., 2 F. WHARTON, CRIMINAL LAW § 1154 (“[T]aking . . . need not be secret but must be fraudulent.”). See Note, *supra* note 49, at 573 (“Crimes of fraud have generally been regarded as crimes against property involving some form of trickery or deception [including] embezzlement, false pretenses, forgery and larceny by trick.” (citing 1 J. BISHOP, COMMENTARIES ON THE CRIMINAL LAW §§ 565-590 (7th ed. 1882))).

<sup>105</sup> The Court’s holding that Winans’ misappropriation of the information was an “embezzlement” reflects the difficulty of the government’s position. The government changed its mind about whether the fraud occurred when Winans *first took* information (the embezzlement theory) or when he failed to disclose his use of the information (the false pretenses theory). Compare Brief for the United States at 13 (“he foster[ed] and maintain[ed] a misimpression that afford(ed) him access to his employer’s confidential information”) with Supplemental Brief for the United States at 1 (“petitioners’ convictions were based squarely on their fraudulent misappropriation of proprietary information”). Presumably the Court adopted the latter “embezzlement” approach because the false pretenses approach suggested that if Winans had taken information once and then told the *Journal* about it, he wouldn’t have violated the statute. This “every criminal gets



But while it was an overstatement by the Court to suggest that any embezzlement is a "fraud," it is fair to say that Winans' acts constituted "fraud," whether they are characterized as "embezzlement" or "false pretenses." The difficulty arises because neither of these traditional crimes were defined in terms of intangible property. On the one hand, this looks like an embezzlement because Winans was entrusted with the *Journal's* information and he took it for his own use.<sup>106</sup> However, embezzlement requires a *conversion*, that is, "a serious act of interference with the owner's rights."<sup>107</sup> Though Winans used the information himself, he did not substantially interfere with the *Journal's* use of it. It is also not strictly false pretenses. While Winans' conduct in holding himself out as a loyal employee may be sufficient to satisfy the "false representation" element<sup>108</sup> he certainly didn't acquire title to the information and thus, one of the traditional elements of false pretenses<sup>109</sup> is missing. Once intangibles are recognized as being the proper subjects of a fraud, however, as *Carpenter* held, it would make no sense to find no fraud simply because the object of the offense did not have the traditional characteristics of tangible property. Intangibles, such as information, can be used by the defendant without being converted and without title passing. The Court should have recognized Winans' behavior as involving the kind of deceitful behavior traditionally encompassed by the concept of "false pretenses," not "embezzlement," and consequently as falling within the fraud stat-

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one bite" result was, obviously, a distasteful one. The Court would have been better off to have simply held that Winans' misappropriation was the kind of deceitful behavior that fraud has always been concerned with, rather than characterizing Winans' acts as an "embezzlement."

<sup>106</sup> 2 W. LAFAVE & A. SCOTT, *supra* note 97, § 8.6. Embezzlement is "(1) the fraudulent (2) conversion of (3) the property (4) of another (5) by one who is already in possession of it." *Id.*

<sup>107</sup> *Id.* However:

some modern embezzlement statutes go so far as to penalize breach of faith without regard to whether anything is misappropriated. Thus, the fiduciary who makes forbidden investments [and] the official who deposits public funds in an unauthorized depository . . . may be designated an embezzler. Although this kind of coverage is relatively new for Anglo-American penal law, certain foreign codes have long recognized criminal "breach of trust" as a distrust entity.

MODEL PENAL CODE § 223.1, commentary at 129 (1980).

<sup>108</sup> "There may . . . be a duty to speak to correct a misapprehension . . . as where [the defendant] stands in a fiduciary relationship to the [victim]." 2 W. LAFAVE & A. SCOTT, *supra* note 97, § 8.7(b)(3).

<sup>109</sup> False pretenses is "(1) a false representation of a material past or present fact (2) which causes the victim (3) to pass title [of] (4) his property to the wrongdoer (5) who (a) knows his representation to be false and (b) intends thereby to defraud the victim." *Id.* at § 8.7.

ute. The remaining question then, is whether the Court was correct in holding that "property" in that statute includes intangibles.

The Court simply held, without any pertinent authority, that deprivation of the right to exclusive use of confidential information impinges on a "property" interest.<sup>110</sup> Certainly this too was inconsistent with the historic understanding of fraud that had informed the *McNally* decision. Contrary to *Carpenter*, the legislative history as well as the general understanding of "fraud" at the time of the enactment of the mail fraud statute suggests that "fraud" was limited to money or *tangible* property, as discussed below.

While courts use the term "common law" to refer to the early law of fraud,<sup>111</sup> in fact, that law is largely statutory. The common law punished only those cheats that were "effected by deceitful tokens or symbols which may affect the public at large and against which common prudence could not have guarded."<sup>112</sup>

The American law of false pretenses or fraud is based on the 1757 statute of 30 Geo II, ch. 24<sup>113</sup> which forbade: "Knowingly and designedly, by false pretense or pretenses, obtain(ing) from any person or persons money, goods, wares or merchandise with intent to cheat or defraud any person or persons of the same. . . ."<sup>114</sup>

The original mail fraud statute, enacted in 1872, provided

That if any person having devised or intending to devise any scheme or artifice to defraud, to be effected by either opening or intending to open correspondence or communication with any other person (whether resident within or outside the United States), by means of the post-office establishment of the United States, or by inciting such other person to open communication with the person so devising or intending, shall, in and for executing such scheme or artifice (or attempting so to do), place any letter or packet in any post-office of the United States, or take or receive any therefrom, such person, so misus-

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<sup>110</sup> *Carpenter v. United States*, 108 S. Ct. 316, 320 (1987).

<sup>111</sup> In *McNally*, the Court rejected "the argument that the statute reaches only such cases as, at common law, would come within the reach of 'false pretenses.'" *McNally v. United States*, 108 S. Ct. 2875, 2879 (1987)(quoting *United States v. Durland*, 161 U.S. 306, 312 (1896)).

<sup>112</sup> F. WHARTON, *CRIMINAL LAW* § 1380 (12th ed. 1932). Thus it was a common law crime to sell by false weight or measure or to sell clothing with a forged label. *Id.* at § 1382. "The cases in which fraud is indictable at common law, seem confined to the use of false weights and measures—the selling of goods with counterfeit marks, playing with false dice—and frauds affecting the course of justice and immediately injuring the interests of the public or crown." J. CHITTY, *A PRACTICAL TREATISE ON THE COMMON LAW* 995 (1816).

<sup>113</sup> F. WHARTON, *supra* note 112, § 1395 n.11 (referring to this as "the original from which most of our [American] statutes are drawn"). *Accord* Pearce, *supra* note 57, at 968 n.6.

<sup>114</sup> F. WHARTON, *supra* note 112, § 1395 n.11 (quoting 30 Geo. II, ch. 24 (1757)).

ing the post-office establishment shall be guilty of a misdemeanor.<sup>115</sup>

In 1896 in the *Durland* case,<sup>116</sup> the Supreme Court held that the phrase "scheme or artifice to defraud" was not limited to schemes punishable at "common law" such as those involving representations as to past or present fact<sup>117</sup> but included "representations and promises as to the future."<sup>118</sup> In 1909, Congress, in an apparent effort to codify *Durland*,<sup>119</sup> added the language of Clause 2, "or for obtaining money or property by means of false or fraudulent pretenses, representations or promises" to the statute.<sup>120</sup>

It is clear that, while *Durland* may have charted a prudential course in divorcing the term "defraud" in the mail fraud statute from the common (albeit incorrect)<sup>121</sup> American understanding of "false pretenses," the terms did not in fact have any different meaning in this context. Thus, the *Durland* Court was wrong in giving a criminal statute a meaning clearly not contemplated by Congress.<sup>122</sup> As discussed, "fraud" was a broader term applied to other crimes of deception, such as embezzlement, as well as to false pretenses,<sup>123</sup> but in the mail fraud statute the term "fraud" meant, essentially, "false pretenses" and the *Durland* Court did not change that, except

<sup>115</sup> Act of June 8, 1872, ch. 335, § 301, 17 Stat. 323. See Rakoff, *supra* note 59, at 779-86 for an excellent discussion of the history of this statute.

Note the presence of an additional element compared to the current statute. That is that the scheme "be effected by opening . . . correspondence . . . by means of the post office establishment of the United States." This "mail emphasizing" language explains the concept, still extant today, that the misuse of the mails is the "gist" or essence of the mail fraud statute—a concept that is no larger justified by the statutory language. Rakoff, *supra* note 59, at 821-22.

<sup>116</sup> 161 U.S. 306 (1896).

<sup>117</sup> In fact, this was a widespread, but erroneous view of the 18th century British law of fraud.

<sup>118</sup> *Durland*, 161 U.S. at 313.

<sup>119</sup> Pearce, *supra* note 57, at 980. The addition of Clause 2 "was in the Code submitted by the Commission appointed to prepare a draft. There was no comment on this change other than the citation of *Durland v. United States* in the margin of the Commission's report." *Id.* at 981 n.56.

<sup>120</sup> 35 Stat. 1130 (1909). Congress also eliminated the mail-emphasizing language, as well as other language, added in 1889, Act of March 2, 1889 Ch. 393 § 1, 25 Stat. 873, that had listed specific types of frauds such as "sawdust swindle" and "counterfeit money fraud."

<sup>121</sup> As Professor Pearce has demonstrated, the British understanding of false pretenses in the 1757 statute was *not* limited to representations as to past or present facts but included false promises as to the future as to which the promisor had no intention of fulfilling his promises. Pearce, *supra* note 57, at 979. Wharton is responsible for the contrary American understanding, apparently based on his reading of the British cases in the first edition of his *Criminal Law* which appeared in 1846. *Id.* at 968.

<sup>122</sup> See *infra* note 272.

<sup>123</sup> Note, *supra* note 59, at 573 and sources cited therein.

in one particular.<sup>124</sup> As the *Durland* Court admitted, it was going “beyond the letter of the statute” to reach “the evil sought to be remedied.”<sup>125</sup>

As Professor Pearce observed, “The Court interpreted the statute as essentially a false pretense statute but simply refused to accept the restriction [as to representations of past or present fact.]”<sup>126</sup>

Having determined that “fraud” and “false pretenses” described the same crime, the question now becomes whether that crime was limited to tangible property. The answer, at the time the mail fraud statute was enacted was certainly yes: “A false pretense . . . induces a party to whom it is made to part with his property. . . . A mere pecuniary advantage, devoid of any physical attribute possessed by money, chattels, or valuable securities is not within a statute as to false pretenses.”<sup>127</sup>

Thus, in terms of the common understanding of the crime of fraud or false pretenses at the time of the original 1872 statute and the 1909 amendment, it is clear, that the concept of “defraud” was limited to tangible property.

It is thus apparent that while history supported the Court’s holding in *McNally*, limiting “fraud” to money or property, it did not support *Carpenter*’s extension of “property” to include such intangibles as confidential information.

Indeed, prior to *McNally*, the lower courts had all assumed that “property” meant “tangible property” but that, because Clause 1’s “scheme to defraud” did not mention “money or property,” Clause 1 also embraced schemes to deprive victims of such intangibles as the right to honest services, reputation, information, and the like.<sup>128</sup>

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<sup>124</sup> “[T]he mail fraud statute should be properly interpreted as proscribing the fraud of false pretenses.” *Id.*

<sup>125</sup> *Durland v. United States*, 161 U.S. 306, 313 (1896).

<sup>126</sup> Pearce, *supra* note 57, at 979.

<sup>127</sup> F. WHARTON, *supra* note 112, § 1399 n.18. *Accord* J. CHITTY, *supra* note 112, at 998. Obtaining an extension of time in which to pay a loan is not considered “property.” F. WHARTON, *supra*.

<sup>128</sup> See, e.g., *United States v. Gray*, 790 F.2d 1290 (6th Cir. 1986), *rev’d sub nom.* *United States v. McNally*, 107 S. Ct. 2875 (1987). In *Gray*, the Court quoted the Seventh Circuit:

A scheme to defraud the citizenry and government of an intangible right, such as honest service, can be contrasted with a scheme to obtain tangible property through fraud. A scheme to obtain tangible property is cognizable under the mail fraud statute regardless of the relationship between the defendant and his victim. In contrast, an intangible rights scheme is only cognizable when at least one of the schemes has a fiduciary relationship with the defrauded person or entity.

*Id.* at 1294-95 (quoting *United States v. Alexander*, 741 F.2d 962, 964 (7th Cir. 1984)).

Once the Court limited mail fraud to money or property, it was reasonable to assume that intangibles were not included.

Furthermore, once it is recognized that the term "defraud" implied a deprivation of tangible property, the fact, as the Court observed in *Carpenter*, that "confidential business information has long been recognized as property"<sup>129</sup> in other contexts is irrelevant. Whether or not confidential information had long been regarded as "property," it and other intangibles, such as a business' reputation, had not long been recognized, and certainly were not recognized in 1872 and 1909, as covered by a statute prohibiting "fraud."

The Court put itself in a box in *McNally* from which it could only escape, in *Carpenter*, by a gross distortion of the historical evidence on which *McNally* had been based. A far better approach would have been to have recognized the problem in *McNally* as being the lack of an identifiable victim who suffered economic harm,<sup>130</sup> rather than holding that a traditional view of "property" was an essential element of fraud. Then, in *Carpenter*, it could have noted the presence of a specific victim and a potential economic loss to that victim as satisfying the *McNally* requirement. In response to the argument that "fraud" traditionally required a deprivation of tangible property, the Court in *Carpenter*, not constrained by a contrary reliance on history in *McNally*, could simply have agreed with this point but held, forthrightly, that, in this information age much that is intangible is just as valuable as tangible property.<sup>131</sup> The key question

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<sup>129</sup> *Carpenter v. United States*, 108 S. Ct. 316, 320 (1987). For example, the Court cited *Board of Trade of Chicago v. Christie Grain Co.*, 198 U.S. 236, 250-51 (1905), which held that confidential information compiled by plaintiff Board of Trade is property, and it is entitled to keep that information secret. Nothing in any of the cases cited by the Court deals with the coverage of the crime of fraud. The best case would have been *Haas v. Henkel*, 216 U.S. 462, 479-80 (1910), in which the Court had held that conspiracy to defraud the government embraced a theft of information and did not require an "actual financial or property loss." However, as discussed *supra* notes 14-26, the Court had already closed this door in *McNally* by holding that the statute interpreted in *Henkel*, protecting, as it did, the operations of government, should be read more broadly than the mail fraud statute which only protected the "individual property rights of the members of the civic body." *McNally*, 107 S. Ct. at 2880 n.8. Historically speaking, given the language of the *Henkel* decision, the Court was surely correct not to extend this "strained extension of the word defraud," Goldstein, *supra* note 51, at 462, to private frauds in *McNally*. However, in *Carpenter* it did precisely what it had refused to do in *McNally*.

<sup>130</sup> *Accord* *United States v. Feldman*, 711 F.2d 758 (7th Cir. 1983) and cases cited therein.

<sup>131</sup> This is a description of how the Court could have reached the result it desired in *Carpenter*. It is not how *I* would have interpreted the statute, believing that criminal statutes should be construed according to their ordinary meaning at the time of drafting (as best as can be determined). See *infra* notes 272-74 and accompanying text. However, as Professor Jeffries has recognized, one of the most important tasks of courts in inter-

is not what kind of property was involved but whether there was an economic loss to an identifiable victim as well as an unjust gain to the defendant.<sup>132</sup> As will be argued, while this is not precisely what the Court *said*, this line of reasoning is the only way to explain what it *did*, in *McNally* and *Carpenter*.

Prior to *McNally*, the lower courts, while not focusing carefully on this issue, had offered divergent views as to whether an unjust gain and/or a loss to the victim is required. Under the "intangible rights" approach, the courts sometimes seemed to require neither, as Professor Coffee explained:

Under the "intangible rights" doctrine, a public or private fiduciary can be prosecuted on the theory that this conduct has deprived his beneficiaries of their right to his "honest and faithful services" [by non-disclosure of a conflict of interest]. [T]he operative effect of this disclosure requirement is to simplify the prosecutor's case by substituting proof of non-disclosure for proof of loss or illicit gain.<sup>133</sup>

However, sometimes courts have required at least proof of one or the other, as illustrated by the district court's opinion in *Carpenter*. The court quoted Devitt and Blackmar's *Federal Jury Practice and Instructions* to the effect that "intent to defraud" means to act with the purpose of " 'either causing some financial loss to another, or bringing about some financial gain to oneself.' "<sup>134</sup>

Yet another approach was taken by the Second Circuit in *United States v. Dixon*.<sup>135</sup> In *Dixon* the Court distinguished between corrup-

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preting statutes is to "make the law more . . . certain." Jeffries, *supra* note 80, at 220. If the Court had forthrightly declared that it was departing from the common law in including intangible property, at least it would have taken an honest approach. By claiming to adhere to traditional understanding while at the same time departing from it, the Court has sacrificed future certainty for present results. See also Bradley, *The Uncertainty Principle in the Supreme Court*, 1986 DUKE L.J. 1 (1986)(discussing the Court's repeated tendency to do this).

<sup>132</sup> This latter point is generally assumed by the courts since, in the cases prosecuted, it is almost invariably present. *But see* *United States v. Baldinger*, 838 F.2d 176 (6th Cir. 1988).

<sup>133</sup> Coffee, *Metastasis*, *supra* note 75, at 1-2. In *United States v. Mandel*, 591 F.2d 1347, *aff'd in part*, 602 F.2d 653 (4th Cir. 1979), *cert. denied*, 445 U.S. 961 (1980), the court noted that the case could have been submitted to the jury simply on the theory that Governor Mandel had been bribed or that "false information was presented to, or this information concealed from the Maryland General Assembly . . . in order to induce . . . favorable action toward those interested in [the racetrack involved in the scheme]." *Id.* at 1364. No proof was advanced that the Governor "had a direct interest in the racetrack business." *Id.* See also *Feldman*, 711 F.2d at 763 and cases cited therein (economic harm to a victim was required).

<sup>134</sup> *United States v. Winans*, 612 F. Supp 827, 847 (S.D.N.Y. 1985)(quoting 2 E. DEVITT & C. BLACKMAR, FEDERAL JURY PRACTICE AND INSTRUCTIONS § 47.08 (3d ed. 1977)(emphasis added)). This alternative approach is reflected in Hurson's proposed statute. Hurson, *supra* note 75, at 457.

<sup>135</sup> 536 F.2d 1388 (2d Cir. 1976).

tion of public official cases, in which there need only be an unjust gain, and private delicts, in which there must be both a gain to the defendant and harm to the victim.<sup>136</sup> In the former case, even if the public fisc is enriched, it is a fraud “since the public official has been paid [i.e., bribed] to act in breach of his duties.”<sup>137</sup>

If history is to be the guide, then it is quite clear that, for a fraud to occur, there must be both a gain and a loss. As one commentator has observed, “[d]uring the period of enactment and critical amendment of the mail fraud statute, it was impossible to obtain a conviction for false pretenses unless the defendant had directly received something of economic value from the victim.”<sup>138</sup>

That is, as previously discussed, Congress almost surely contemplated a classic fraud in which the victim is induced by false representations to hand over money or tangible property to the defendant and the victim’s loss is the defendant’s gain. Under this approach, even assuming that confidential information counts as “property,” *Carpenter* would not be a fraud case because Winans’ gain—insider trading profits—was not the *Journal*’s loss—the confidentiality of its information.<sup>139</sup>

<sup>136</sup> *Id.* at 1400.

<sup>137</sup> *Id.* The court does not explain why this reasoning would not apply equally to a private employee who is paid to act in breach of his or her duties.

*Accord* United States v. Isaacs, 493 F.2d 1124, 1151-52 (7th Cir. 1974), *cert. denied sub nom.*, Kerner v. United States, 417 U.S. 976 (1974) (holding that the defendant could be prosecuted for breach of the public trust, even though the public had *profited* from the scheme). *Isaacs*, in turn, relied on *Shushan v. United States*, 117 F.2d 110 (5th Cir. 1941), *cert. denied*, 313 U.S. 574 (1941). “No trustee has more sacred duties than a public official and any scheme to obtain an advantage by corrupting such an [sic.] one must in the federal law be considered a scheme to defraud.” *Isaacs*, 493 F.2d 1150 (quoting *Shushan*, 117 F.2d at 115 (5th Cir.), *cert. denied*, 313 U.S. 574 (1941)).

In *Isaacs*, the Court discussed United States v. George, 477 F.2d 508 (7th Cir.), *cert. denied*, 414 U.S. 827 (1973) with approval. That case involved kickbacks to a private employee, suggesting that the Seventh Circuit did not draw the same distinction between private and public employees as did the Second Circuit.

There is support for the notion that a victim need not be specified if the fraud is against the public because, as Wharton points out, “it is the essence of the common law cheat that it should be addressed to the public generally.” F. WHARTON, *supra* note 112, § 1393 (“Indictment for public cheats need not name party cheated”). This was the distinction drawn between private and public frauds in *McNally v. United States*, 107 S. Ct. 2875, 2880 n.8 (1987).

<sup>138</sup> Note, *supra* note 59, at 574. The Note discusses at length the American and English cases from the 19th and early 20th centuries. *Accord* United States v. Runnels, 833 F.2d 1183, 1185 (6th Cir. 1987) (“Criminal liability for false pretenses, which the mail fraud statute was intended to reach, was consistently predicated upon the defendant’s taking of some economic benefit from the scheme’s victim” at the time the statute was enacted.); F. WHARTON, *supra* note 112, § 1465 (“[t]hing obtained must be of same value”).

<sup>139</sup> The government could not have argued in *Carpenter* that Winans’ gain was simply the confidential information. He already *had* that information as part of his job. It was

*McNally* and *Carpenter* thus are inconsistent with each other, one relying on, and the other ignoring, history. The only way to come close to reconciling the two decisions is to recognize this as the Court's purpose: *to force the prosecution to clearly identify the victim, and to define, in economic terms, what he or she stood to lose and what the defendant stood to gain.* In *McNally*, the Court focused on the need to prove loss, requiring the "deprivation of something of value by trick, deceit, chicane, or overreaching."<sup>140</sup> In *Carpenter*, while first making it clear that deprivation of the exclusive use of information was sufficient to satisfy the "property loss" requirement<sup>141</sup> (as opposed to actual monetary loss), the Court went on to focus on Winans' "scheme to share profits from trading in anticipation of the "Heard" column's impact on the stock market"<sup>142</sup> and to recognize that Winans was "not free to exploit [confidential] information for his own personal benefit."<sup>143</sup> That is, the Court found the anticipated *gain* a crucial aspect of the scheme. Thus, *McNally* and *Carpenter*, read together, require an *economic* gain to the defendant and loss to the victim (or the prospect of same) but do not require that this gain and loss be of "property" as that term had been understood by Congress.

In its brief in *Carpenter*, the government agreed that both gain and loss are necessary: "[A] scheme to use a private fiduciary position to obtain direct pecuniary gain is within the mail fraud statute, at least where that scheme contemplates some sort of harm to the victim."<sup>144</sup>

In the recent, post-*McNally* case, *United States v. Baldinger*,<sup>145</sup> the Sixth Circuit also read *McNally* in this way, holding that the Supreme Court had limited the mail fraud statute to schemes "that have as their goal the transfer of something of economic value to the defendant."<sup>146</sup>

In *Baldinger*, the court was presented with the factual situation described in Case 1 at the beginning of this Article. The defendant, with no expectation of gain, set out to ruin another person in his

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the *trading* on the information that was the fraud. Had he traded on this information without disclosing it to anybody he would have been equally guilty.

<sup>140</sup> *McNally*, 107 S. Ct. at 2880.

<sup>141</sup> *Carpenter v. United States*, 108 S. Ct. 316, 321 (1987).

<sup>142</sup> *Id.*

<sup>143</sup> *Id.*

<sup>144</sup> Brief for the United States at 19, *Carpenter*, 108 S. Ct. 316 (quoting *United States v. Dixon*, 536 F.2d 1388, 1399-1400 (2d Cir. 1976)).

<sup>145</sup> 838 F.2d 176 (6th Cir. 1988).

<sup>146</sup> *Id.* at 180.



business.<sup>147</sup> Despite the fact that the victim clearly stood to suffer tangible property loss, the court reversed the conviction based on *McNally*. While this reversal was based in part on the “intangible rights” language of the indictment, the court went on to hold that a “proprietary gain ingredient” was necessary to a mail fraud conviction (in addition to the loss).<sup>148</sup>

Had Winans knowingly breached his duty not to disclose confidential information (in which case harm to the *Journal's* reputation was surely reasonably foreseeable) but had no intent that he, or anyone else, would profit from the disclosure, surely there would be no “fraud.” As the government recognized, the essence of fraud is that the defendant seeks “pecuniary gain.” This point will be discussed further when the appropriate mens rea is considered.

While the Supreme Court in *Carpenter* correctly assumed that the potential for gain and loss was inherent in a “scheme to defraud,” it incorrectly identified the potential harm in *Carpenter*. Why this is so can be illustrated by some examples.

Suppose Winans, home for Sunday dinner, tells his family about a forthcoming “Heard” column. The *Journal* has lost the exclusivity of its information but surely no “fraud” has occurred. Why not? Because there is no real harm to the *Journal* and no unjust gain to Winans. Suppose, by contrast, that Winans tells no one about forthcoming “Heard” columns but trades on his knowledge himself. Surely this is a fraud after *Carpenter*, despite the fact that the information has gone no further than Winans himself. Why? Because Winans has experienced an unjust gain and he has subjected the *Journal* to possible reputational damage if his trading is publicly disclosed. Thus, the real harm to the *Journal* is not the loss of the exclusivity of its information, but the threat to its reputation.

The loss of confidential information is only a deprivation of a “property” interest if the loss threatens the victim with economic harm, such as selling news information to a competing newspaper.<sup>149</sup> Here, it was not the loss of the information, as such, but the risk that Winans’ insider trading would be disclosed that threatened the *Journal's* economic interests. Nevertheless, the Court recognized the main point—that fraud requires an identifiable victim who stands to suffer economic harm<sup>150</sup> and a defendant who stands to

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<sup>147</sup> *Id.* at 179-80.

<sup>148</sup> *Id.*

<sup>149</sup> This was the holding of *International News Service v. Associated Press*, 248 U.S. 215, 236 (1918), quoted by the Court in *Carpenter*, 108 S. Ct. at 321.

<sup>150</sup> As the government argues in its Supplemental Brief, “*McNally* is not at all concerned with the *means* by which the defendant effects his scheme; it addresses only the

make an unjust profit.

Once this is recognized, the question of what is "property," after the Court's seemingly inconsistent signals in *McNally* and *Carpenter*, answers itself: Property is anything that can satisfy this requirement. That is, anything that can provide economic loss to the victim and gain to the defendant including information, reputation and anything else on which a dollar value can be placed.<sup>151</sup>

The Seventh Circuit has used essentially this standard for several years to distinguish those fiduciary breach cases which are, and those which are not, fraud:

[N]ot every breach of duty by an employee works as a criminal fraud . . . and receipt of secret profits, standing alone, cannot support a mail fraud conviction. . . . When an employee breaches a fiduciary duty to disclose information to his employer, that breach of duty can support a mail or wire fraud conviction only if the nondisclosed information was material to the conduct of the employer's business and the nondisclosure could or does result in harm to the employer.<sup>152</sup>

Thus, in order to have a fraud, there must be, in addition to an unjust gain, an identifiable victim, as the government conceded in *Carpenter*.<sup>153</sup> This victim, which can be a corporation, a governmental entity, or a class of individuals, must have *standing to sue* for the *economic harm* which the defendant caused, or could have caused,

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requisite *injury to the victim.*" Supplemental Brief for the United States at 3, *Carpenter*, 108 S. Ct. 316 (No. 86-422)(emphasis added).

<sup>151</sup> The United States argued:

The term [property] surely includes many kinds of valuable proprietary information such as trade secrets, customer lists, business plans, financial analysis and advice, and the like. The misappropriation of such information has long been understood to deprive the owner of something of value [citations omitted]. . . . An individual or firm's reputation is also an intangible asset with a monetary value.

Supplemental Brief for the United States at 4, *Carpenter*, 108 S. Ct. 309.

<sup>152</sup> *United States v. Feldman*, 711 F.2d 758, 765 (7th Cir. 1983), *cert. denied*, 464 U.S. 949 (1983). Similarly, in *United States v. Wellman*, 830 F.2d 1453 (7th Cir. 1987), the Court, per Judge Eschbach, who also authored *Feldman*, held that "property" rights under the mail fraud statute are "rights whose violation would ordinarily result in . . . concrete economic [or to use Justice Stevens' term 'monetary'] harm." *Wellman*, 830 F.2d at 1462. *Accord* *United States v. Newman*, 664 F.2d 12, 19 (2d Cir. 1981), *aff'd*, 722 F.2d 729 (2d Cir.), *cert. denied*, 464 U.S. 863 (1983)("the concealment by a fiduciary of material information which he is under a duty to disclose to another under circumstances where the non-disclosure could or does result in harm to another is a violation of the [mail fraud] statute").

<sup>153</sup> The United States argued the:

right of the citizenry to good government at issue in *McNally* cannot be valued in monetary terms, and no individual has an enforceable possessory interest in it. But many intangibles have monetary value and belong to identifiable persons who are entitled to exclude other persons; such intangibles are universally thought of as "property."

Supplemental Brief for the United States at 4, *Carpenter*, 108 S. Ct. 316.

it.<sup>154</sup> In this respect the *McNally* indictment was insufficient. The "citizens of the State of Kentucky," as opposed to the government, which was not alleged to have lost anything in *McNally*, were not an identifiable victim. They had no standing to sue and they could point to no concrete economic harm that they suffered or could have suffered from the scheme.<sup>155</sup> By contrast, in *Carpenter*, the *Wall Street Journal* was an identifiable victim, it had standing to sue and the misappropriation of its business information had the potential to cause it economic harm.<sup>156</sup>

In the recent case of *United States v. Covino*,<sup>157</sup> the Second Circuit reversed a conviction on *McNally* grounds based on similar reasoning. In *Covino*, similarly to the second hypothetical case at the beginning of this Article, the defendant extorted payments from a contractor in return for giving the contractor his firm's (NYNEX) business.<sup>158</sup> There was no evidence that NYNEX was in any way deprived of money or property or that the contract was administered poorly. In fact, the jury was instructed to the contrary.<sup>159</sup> The basis for the charge was that the defendant took, and failed to disclose, the payments, contrary to company policy.<sup>160</sup> Here, there was an unjust gain and an identifiable victim with standing to sue, but the victim suffered no loss beyond its intangible, non-property interest in its employee's honest and faithful services. The Second Circuit reversed the conviction based on *McNally*, holding that, despite his unjust gain, the defendant was charged with "depriving NYNEX of material information concerning breaches of his fiduciary duty, not with depriving it of property"<sup>161</sup> Thus, the victim had not suffered any loss of property.

The "materiality" requirement of the *Feldman* test also solves the problem posed by Justice Scalia to the Solicitor General at the oral argument in *Carpenter*. In the Fred M. Smith Company

One of his employees asks [Mr. Smith] "What does 'M' stand for?" And Smith says, "Well I will tell you this just in confidence. . . . It is Marmaduke. I am really very ashamed of it." The employee writes to

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<sup>154</sup> *Id.*

<sup>155</sup> *Id.*

<sup>156</sup> The government conceded at oral argument in *Carpenter* that "there has to be some kind of harm which is contemplated or risked. [It does not have] to actually eventuate." Transcript of Proceedings at 30, *Carpenter*, 108 S. Ct. 316.

<sup>157</sup> 837 F.2d 65 (2d Cir. 1988).

<sup>158</sup> *Id.* at 66-67.

<sup>159</sup> *Id.* at 70.

<sup>160</sup> *Id.*

<sup>161</sup> *Id.* at 72. *Accord* *United States v. Ballard*, 663 F.2d 534, 541 (5th Cir. 1981), *modified on reh'g*, 680 F.2d 352 (5th Cir. 1982)(no fraud when price was fixed by law and consequently kickback did not cost employer any money).

a newspaper and says, "You know, Fred M. Smith's middle name is Marmaduke." And he gets . . . five bucks from the newspaper for that. Is that mail fraud?<sup>162</sup>

The Solicitor General replied that it was not but had difficulty explaining why.<sup>163</sup> His vague allusion to "weight and seriousness" was, however, essentially correct.<sup>164</sup> The employee's misdeed must relate to a *material* aspect of the employer's *business* and must cause (or threaten to cause) the *business* material<sup>165</sup> economic harm (unless, of course, the employee also owes a fiduciary duty to the employer personally, as a lawyer would to a client). The breach of trust in the hypothetical was arguably of a personal, non-fiduciary nature,<sup>166</sup> was not material, and did not, apparently, cause or threaten to cause the business economic harm. However, it is clear from *Carpenter* that the *disclosure* of confidential information by one who has a duty not to disclose<sup>167</sup> as opposed to the nondisclosure of a breach of trust contemplated in *Feldman*, certainly can be the basis of a mail fraud charge; even though such a disclosure could be considered an "embezzlement" rather than a "fraud."<sup>168</sup> Thus, if the employee learned, in the course of business, that the Fred M. Smith Company had once sold pornographic literature and had sold this information to a newspaper, causing the company to lose business, all of the ele-

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<sup>162</sup> Transcript of Proceedings at 35-36, *supra* note 156.

<sup>163</sup> "I am confident in saying it is not. And now let me try and figure out why not." *Id.*

<sup>164</sup> *Id.*

<sup>165</sup> The *Feldman* test should be amended to make it clear that not only must the information be material to the business but that the harm to the employer must be material. Thus, minor employee pilfering of office supplies, in violation of company policy, and the failure to disclose such pilfering, would not qualify as "fraud" under the federal statute. There is general agreement on the materiality requirement in the lower courts. *E.g.*, *Ballard*, 663 F.2d at 541; *United States v. Lemire*, 720 F.2d 1327, 1337 (D.C. Cir. 1983), *cert. denied*, 467 U.S. 1226 (1984), and cases cited therein.

<sup>166</sup> Despite the Supreme Court's use of the term "confidential or fiduciary relationship," *Carpenter v. United States*, 108 S. Ct. 316, 321 (1987), it seems unlikely that it intended to extend the concept of "fraud" to *any* breach of confidence. Thus, if A's personal friend discloses A's secrets to the newspapers, even for money, there is not a fraud. Rather, there must be a *fiduciary* (i.e., legally recognized relationship of trust) breach before disclosure or nondisclosure of information can be a fraud. In the hypothetical in the text, it is unclear whether the breach would be of a personnel or fiduciary relationship.

<sup>167</sup> It is also clear from *Carpenter* that Winans' fiduciary relationship was necessary to make this a fraud. "[A] person who acquires special knowledge or information by virtue of a confidential or fiduciary relationship with another is not free to exploit that knowledge or information for his own personal benefit. . . ." *Id.* at 321. Thus, if Winans were visiting at the *Journal*, saw confidential information on someone's desk, and traded on that information, there might be a theft, but there would be no fraud.

<sup>168</sup> *E.g.*, *United States v. Gray*, 790 F.2d 1290 (6th Cir. 1986) (the lower court decision in *McNally*); *United States v. Alexander*, 741 F.2d. 962, 964 (7th Cir. 1984).

ments of fraud would have been met.<sup>169</sup>

Having posited that mail fraud requires at least the potential for both loss and gain, the question arises as to what the defendant's mens rea must be as to these two elements.

Suppose that Winans had met Felis at a cocktail party and that Felis but not Winans had recognized the potential for gain in advance information about the "Heard" column. Consequently he pumped Winans for this information and Winans, unthinkingly, gave it to him. Winans is thus, at most, reckless as to both the *Journal's* loss and anybody's gain. Most would agree that this is not a "scheme to defraud." Why not? Because there was neither an intent to gain nor any knowingly fraudulent behavior.

While, as noted, there has begun to be some recognition in the lower courts of the need to prove both a gain and a loss,<sup>170</sup> no court has yet focused on what the appropriate mens rea should be as to both of these elements. There has, however, been considerable agreement that, as to the victim's loss (or employer's loss when the defendant is an employee), the appropriate mens rea is "reasonably foreseeable."<sup>171</sup> That is, as the D.C. Circuit held, the jury must find that "the non-disclosure furthers a scheme to abuse the trust of an employer in a manner that makes an identifiable harm to him, apart from the breach itself, reasonably foreseeable."<sup>172</sup>

This view is borne out by the holding in *Carpenter* in which liability, as discussed, was based on unjust gain as well as potential deprivation of something of value.<sup>173</sup> Winans intended an unjust gain but he did *not* intend to harm the *Journal*. The only way the *Journal* could be harmed was if he manipulated the column to advance his interests, which the evidence showed he did not do,<sup>174</sup> or

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<sup>169</sup> Of course, certain employee disclosures might be subject to protection under the first amendment or "whistle-blower" statutes, but the discussion of such disclosures is beyond the scope of this Article.

<sup>170</sup> *United States v. Baldinger*, 838 F.2d 176 (6th Cir. 1988).

<sup>171</sup> *United States v. Lemire*, 720 F.2d 1327, 1337 (D.C. Cir. 1983). See also *United States v. Vor Barta*, 635 F.2d 999, 1005 (2d Cir. 1980), cert. denied, 450 U.S. 998 (1981) (requires that scheme was devised with specific intent to defraud); Brief for the United States at 20, *Carpenter*, 108 S. Ct. at 316.

<sup>172</sup> Brief for the United States at 20.

<sup>173</sup> *Carpenter*, 108 S. Ct. at 321. This mens rea element of intent to gain is in contradistinction to that which the Supreme Court has already established for the mailing element. In *Periera v. United States*, 347 U.S. 1 (1954), the Court held that the defendant need not intend the mailing, rather, the mailing need only "reasonably be foreseen." *Id.* at 9. However, the establishment of a lesser, or even no, mens rea for the jurisdictional element has long been approved by the Court. *E.g.*, *United States v. Feola*, 420 U.S. 671, 684 (1975) (no mens rea required as to the jurisdictional element "federal officer" in the crime of assault on federal officer, 18 U.S.C. § 1111 (1982)).

<sup>174</sup> *Carpenter*, 108 S. Ct. at 319.

if the scheme became public knowledge, which Winans assiduously sought to avoid.<sup>175</sup> Rather, he disregarded a reasonably foreseeable risk that the *Journal* would be harmed—negligence in *Model Penal Code* terms.<sup>176</sup>

As for the gain, inherent in every fraud scheme prosecuted by the government, with the exception of *Baldinger* which was reversed by the court of appeals,<sup>177</sup> is an intent to gain. So it was at common law: "Every one commits the misdemeanor called cheating who fraudulently obtains the property of another by any deceitful practice."<sup>178</sup>

To the same effect was the original false pretense statute which required that the defendant "knowingly and designedly by false pretense or pretenses obtain [property]."<sup>179</sup> Thus, in the cocktail party hypothetical, Winans, though he should, perhaps, have reasonably foreseen that disclosure of the information might harm the *Journal*, had no purpose to gain. Consequently, there is no fraud. Even if Winans had *knowingly* violated the *Journal's* non-disclosure rules, there would be no "scheme to defraud" because there was no purpose to gain.<sup>180</sup>

Finally, as the false pretense statute just quoted indicated, in fraud the defendant must proceed "knowingly and designedly by false pretense." That is, if an individual makes a representation, he or she must know it to be false and if he acts misleadingly, he or she must know it.<sup>181</sup> When the defendant is charged with breaching a fiduciary duty to disclose certain facts or with acting in breach of that duty, the same standard should apply. That is, he or she must know of the duty and knowingly breach it.<sup>182</sup>

A final point must be made about the elements of mail fraud after *McNally* and *Carpenter*. As discussed, in the classic fraud, the

<sup>175</sup> Appellant's Brief at 7-8, *Carpenter*, 108 S. Ct. 316.

<sup>176</sup> MODEL PENAL CODE § 2.01(2)(d) (1980) ("A person acts negligently with respect to a material element of an offense when he should be aware of a substantial and unjustifiable risk that the material element . . . will result from his conduct.")

<sup>177</sup> See *supra* notes 145-48 and accompanying text. Even in *Baldinger* there was evidence of an intent to gain, though this was not proved. *United States v. Baldinger*, 838 F.2d 176, 179-80 (6th Cir. 1988).

<sup>178</sup> J. STEPHEN, DIGEST OF THE CRIMINAL LAW 406 (8th ed. 1947) (Stephen goes on to discuss the common law limitation of "affecting the public at large" which was eliminated by the 1757 statute.)

<sup>179</sup> 30 Geo. 2, ch. 24 (1757).

<sup>180</sup> Thus, I disagree with Professor Coffee who would find criminal liability if the fiduciary duty is knowingly breached and there was a reasonably foreseeable risk of harm to the victim. Coffee, *Tort to Crime*, *supra* note 75, at 124.

<sup>181</sup> See, e.g., 2 W. LAFAVE & A. SCOTT, *supra* note 80, § 8.7 (f)(1) ("the defendant to be guilty [of false pretenses] must know that his representation is false").

<sup>182</sup> See Coffee, *Tort to Crime*, *supra* note 75, at 124, 164.

victim hands over something of value to the defendant. When the victim is defrauded of tangible property, such as money or a cow, his or her loss necessarily is the defendant's gain, and this was, therefore, an inevitable aspect of traditional fraud. When intangibles are involved, by contrast, it is possible that the loss and the gain may not be the same. Thus, in *Carpenter*, as discussed, the *Journal's* potential loss was to its reputation; Winans' gain was confidential information and insider trading profits. However, the Court claimed that the loss was the exclusive use of confidential information, the same as the gain. Since the Court strained in *Carpenter* to claim that the gain was the same as the loss, it might be thought that it intended to adopt the traditional view of this. On the other hand, since it abandoned the traditional view in allowing a prosecution based on intangible property rights in the first place, it is reasonable to suppose that it would not insist on a loss/gain identity. Given that this problem will frequently arise in intangible property cases, and that the defendant is no less culpable because the loss threatened to the victim is not the same as the gain, it would be unreasonable for the courts to insist on this limitation.

In summary, the best way to reconcile *McNally*, *Carpenter* and the history of fraud (to the somewhat limited extent that they are reconcilable) is to conclude that mail fraud includes, in addition to the requisite mailings, a scheme in which the defendant, through knowingly deceitful behavior, intends an economic gain and is at least negligent as to economic harm to the victim.<sup>183</sup> The "deceitful behavior" can include a breach of fiduciary duty. Thus, Winans committed fraud the first time he disclosed confidential information, with the requisite intent as to gain and loss.

Consider how this formulation applies to a particular, controversial case, *United States v. Bronston*.<sup>184</sup> In *Bronston* the defendant, a partner in a law firm, secretly worked for Client B, while his firm was representing Client A, both of which clients were competing for a city contract. However, Bronston did not use his fiduciary position

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<sup>183</sup> Contrary to the scheme of Professor Coffee, an element of causation, or use of it as an affirmative defense is not included. A "scheme to defraud" clearly requires no actual loss and hence no "causation" of such a loss. The important point is that the defendant have the appropriate mens rea as to loss, not that he or she actually cause it. While it could be argued that Bronston's breach did potentially harm the client, in my view, such causation is not required as long as the defendant was negligent as to harm.

<sup>184</sup> 658 F.2d 920 (2d Cir. 1981), cert. denied, 456 U.S. 915 (1982). *Bronston* has been heavily criticized by both Hurson, *supra* note 75, at 431, and Coffee, *Tort to Crime*, *supra* note 75, at 130.

to harm Client A.<sup>185</sup> Bronston was convicted of defrauding Client A.<sup>186</sup>

Contrary to Professor Coffee,<sup>187</sup> I have no difficulty with the *Bronston* case. Bronston knowingly breached his fiduciary duty to Client A, intended to gain from that breach and could reasonably foresee that the breach would cause harm to Client A. That is, he intended that, through his efforts, Client B should get the contract rather than Client A. The fact that he did not *use* his position to gain extra advantage, as Winans did, does not deny that the breach caused, or could have caused the harm. Accordingly, under the reading of *Carpenter* and *McNally* advanced in this Article, Bronston committed fraud.<sup>188</sup>

### III. ISSUES INVOLVED IN PENDING CASES

Two questions are raised by *McNally* which affect pending cases. They will be dealt with briefly. They are whether *McNally* is retroactive and whether a conviction must be reversed when based upon both property and intangible (non-property) rights theories of mail fraud.

#### A. RETROACTIVITY

As to cases pending on direct review, there is no question but that the *McNally* holding applies.<sup>189</sup> The more difficult issue is whether *McNally* should be applied to convictions that were final

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<sup>185</sup> Or so it was assumed for the purposes of this case. *Bronston*, 658 F.2d at 926; see also *id.* at 931 (Van Graafeiland, J., dissenting).

<sup>186</sup> *Id.* at 930. Since Bronston took \$12,500.00 from Client B, which he did not turn over to his firm, *id.*, he could certainly have been charged with defrauding the firm of this money. This was *not* the charge, however.

<sup>187</sup> Coffee, *Tort to Crime*, *supra* note 75, at 130-33.

<sup>188</sup> Professor Coffee would only have found a fraud in *Bronston* if the defendant had used his fiduciary position to harm the firm's client, as, for example, by giving confidential information about Client A from the firm's files, to Client B. However, under the test he proposed, it could be argued that there was liability: "[I]t is insufficient that there be a fiduciary breach and a pecuniary gain to the defendant or loss to the victim; rather the former must in some way cause the latter." *Id.* at 132. I agree with this standard. It is inherent in the notion that the victim's loss must be reasonably foreseeable. However, as long as the defendant engages in conduct that is a breach of duty and will reasonably foreseeably cause harm to the victim, I do not agree that the harm must be "directly" caused by the breach.

<sup>189</sup> As the First Circuit recently held in *United States v. Ochs*, 842 F.2d 515, 520 (1st Cir. 1988)(quoting *Hamling v. United States*, 418 U.S. 87, 102 (1974)), "[o]ur prior decisions establish a general rule that a change in the law occurring after a relevant event in a case will be given effect while the case is pending on direct review." *Accord Griffith v. Kentucky*, 479 S. Ct. 314, 328 (1987)(new criminal procedure rules apply to cases pending on direct review).



before that decision was rendered. The federal courts are split on this issue with the Second Circuit, joined by District Courts in Florida and Maryland finding *McNally* retroactively applicable to final convictions<sup>190</sup> and District Courts in Pennsylvania and Michigan holding to the contrary.<sup>191</sup>

In *Ingber v. Enzor* the Second Circuit held that *McNally* was fully retroactive because it was a "ruling that a trial court lacked authority to convict or punish a criminal defendant in the first place,"<sup>192</sup> relying on the Supreme Court's decision in *United States v. Johnson*.<sup>193</sup> The Second Circuit dismissed the recent decision of *Griffith v. Kentucky*,<sup>194</sup> which held that new decisions are not normally given such full retroactivity, as inapplicable because it was a case involving "rules of criminal procedure" rather than "a new rule of substantive law."<sup>195</sup>

The problem of retroactivity is similar to that of the defendants' challenges to guilty pleas. In both cases, it is necessary to balance the virtues of finality against the concern that a particular defendant has been unjustly imprisoned. Professor Westen has advanced a test to distinguish between those issues that may and those that may not be raised after a guilty plea that seems useful in the retroactivity context:

[A] defendant who has been convicted on a plea of guilty may challenge his conviction on any constitutional ground that, if asserted before trial, would *forever preclude* the state from obtaining a valid conviction against him, regardless of how much the state might endeavor to correct the defect. In other words, a plea of guilty may operate as a forfeiture of all defenses except those that, once raised, cannot be "cured."<sup>196</sup>

When this test is applied in the retroactivity context, the result depends on the facts of the particular case. In a case like *McNally*, as this Article will discuss,<sup>197</sup> even if the conviction is reversed, there is a factual basis for a new mail fraud conviction, under a "money or property" theory, without resort to the now discredited "intangible

<sup>190</sup> *Ingber v. Enzor*, 841 F.2d 450 (2d Cir. 1988); *Belt v. United States*, 679 F. Supp. 1088, 1091 (M.D. Fla. 1988); *United States v. Mandel*, 672 F. Supp. 864, 875 (D. Md. 1987).

<sup>191</sup> *United States v. Smith*, 675 F. Supp. 978 (M.D. Pa. 1987); *United States v. Callanan*, 671 F. Supp. 487, 488-94 (E.D. Mich. 1987).

<sup>192</sup> *Ingber*, 841 F.2d at 453-54.

<sup>193</sup> 457 U.S. 537 (1982).

<sup>194</sup> 479 U.S. 314 (1987).

<sup>195</sup> *Ingber*, 841 F.2d. at 454 n.l.

<sup>196</sup> Westen, *Away from Waiver: A Rationale for the Forfeiture of Constitutional Rights in Criminal Procedure*, 75 MICH. L. REV. 1214, 1226 (1977)(emphasis added).

<sup>197</sup> See *infra* notes 220-23 and accompanying text.

right to good government" approach. Consequently, since the government is not "forever precluded from obtaining a valid conviction,"<sup>198</sup> *McNally* should not be applied retroactively to such a case. If, on the other hand, the *only* factual basis for the defendants' conviction is an "intangible rights" theory, then *McNally* should be applied retroactively and his or her conviction reversed because a valid conviction can never be had. Thus, there should be *no* retrials due to *McNally*. Only those cases which could not be retried receive retroactive application. In the others, since the facts on the record appear to support a valid conviction, retroactive application of *McNally* is not warranted.<sup>199</sup>

#### B. CONVICTIONS BASED IN PART ON IMPROPER THEORIES

The second issue concerns convictions, subject to possible reversal after *McNally*, which were also based on a still valid money or property theory. A conflict in the circuits has developed on this issue.<sup>200</sup> The First Circuit confronted the issue in *United States v. Ochs*.<sup>201</sup> There the defendants, including the city's Building Inspector, had grossly understated a construction estimate so as to defraud the city of \$12,000 that would have been paid for a building permit had the estimate been accurate (only about \$12,000 of the \$24,000 owed was paid). The indictment charged a conspiracy both to defraud the city of money and of the loyal and faithful services of its employee.<sup>202</sup> The Court quoted *Zant v. Stephens*,<sup>203</sup> stating that "a general verdict must be set aside if the jury was instructed that it could rely on any of two or more independent grounds, and one of those grounds is insufficient, because the verdict may have rested exclusively on the insufficient ground."<sup>204</sup>

<sup>198</sup> Westen, *supra* note 175, at 1226.

<sup>199</sup> The "full retroactivity" position taken by the Second Circuit leads to ironic results as Professor Lynch pointed out in a letter to the author:

If the Second Circuit and I are right that convictions invalid under *McNally* must be vacated, but you are right (as I think you are) that many of the cases previously tried on the "honest and faithful services" theory could easily be recharged with a showing of pecuniary harm, then *McNally* becomes a fairly perverse exercise: minimal effect on the kinds of cases the government can bring, combined with maximum disruption of settled convictions in cases in which the prosecutors would almost always have gotten convictions, if they'd had advance notice of the requirements.

Letter from Professor Gerard Lynch to Craig Bradley (August 16, 1988).

<sup>200</sup> Compare *United States v. Ochs*, 842 F.2d 515 (1st Cir. 1988) and *United States v. Italiano*, 837 F.2d 1480 (11th Cir. 1988) with *United States v. Richerson*, 833 F.2d 1147 (5th Cir. 1987) and *United States v. Runnels*, 833 F.2d 1183 (6th Cir. 1987).

<sup>201</sup> 842 F.2d 515 (1st Cir. 1988).

<sup>202</sup> *Id.* at 517-18.

<sup>203</sup> 462 U.S. 862, 881 (1983).

<sup>204</sup> *Ochs*, 842 F.2d at 520 (quoting *Zant*, 462 U.S. at 881).

However, the First Circuit further recognized that an exception exists “if the uncertainty as to the ground upon which the jury relied can be eliminated.”<sup>205</sup> This can be done either “where a verdict based on any ground would mean that the jury found every element necessary to support the conviction on the sufficient ground”<sup>206</sup> or “where extrinsic factors in the record make it clear that, although the jury could have relied on insufficient ground, it did not, in fact, do so.”<sup>207</sup> In *Ochs*, the Court pointed to repeated instructions to the jury that the “scheme need not financially harm the city of Boston.”<sup>208</sup> Accordingly, since the jury may have based its verdict on the improper theory, the conviction had to be reversed.<sup>209</sup>

By contrast, in *United States v. Piccolo*<sup>210</sup> the trial judge had instructed the jury that, in order to find the defendant guilty in a “kickback” case<sup>211</sup> it had to find that he had participated in a scheme to defraud the employer of “its right to the honest and faithful services of its employee and “to defraud (the employer) of money.”<sup>212</sup> The court of appeals, recognizing that the “honest and faithful services” theory had been disapproved by *McNally*, nevertheless affirmed the conviction on the basis of the “money” theory.<sup>213</sup> Assuming that the indictment similarly alleged both theories,<sup>214</sup> then this is surely correct. Given the clear proof that the defendant did, in fact, defraud the employer of money there has been no variance as to “affect the substantial rights of the accused.”<sup>215</sup>

In *United States v. Richerson*<sup>216</sup> and *United States v. Runnels*,<sup>217</sup> the

<sup>205</sup> *Id.*

<sup>206</sup> *Id.*

<sup>207</sup> *Id.*

<sup>208</sup> *Id.* at 524. See also *United States v. Italiano*, 837 F.2d 1480, 1482 (11th Cir. 1988) (indictment alleged only the “intangible right to good government” theory). The government argued that nevertheless, a deprivation of money had been shown by the coincidence. *Id.* at 1485. The Court properly rejected this argument out of hand.

<sup>209</sup> This result was consistent with *McNally* itself where the Court reversed the conviction, despite the “money” language in the indictment because “there was nothing in the jury charge that required such a finding.” *McNally v. United States*, 107 S. Ct. 2875, 2882 (1987).

<sup>210</sup> 835 F.2d 517 (3d Cir.), *cert. denied*, 108 S. Ct. 2014 (1987).

<sup>211</sup> The defendant was charged with participating in a kickback scheme whereby one McCuen informed a subcontractor to his company that it could increase its bid by \$303,000 and still be the low bidder. McCuen and the other participants, including Piccolo, then split the \$303,000 with the subcontractor. *Id.* at 518.

<sup>212</sup> *Id.* at 520. The judge also required the jury to find that the employee’s nondisclosure was capable of causing “business harm” to the employer. *Id.* at 522 (Aldisert, J., dissenting).

<sup>213</sup> *Id.* at 520.

<sup>214</sup> The court does not discuss what the indictment alleged.

<sup>215</sup> *Berger v. United States*, 295 U.S. 78, 82 (1935).

<sup>216</sup> 833 F.2d 1147 (5th Cir. 1987).

courts upheld convictions of defendants despite the fact that they had been convicted on an intangible rights theory, which did not require, as in *Piccolo*, that the jury also find a deprivation of money or property. The courts reasoned that since the evidence in fact showed a deprivation of property,<sup>218</sup> a conviction was proper, despite the indictment which required no such finding. This goes against the fundamental rule that a defendant may not be convicted of a crime for which he has not been indicted.<sup>219</sup>

#### IV. AVOIDING THE IMPACT OF *MCNALLY*

It follows from the discussion of *McNally* and *Carpenter* that mere unjust gain cases, in which no loss or potential loss to a victim is shown, cannot be fraud. This type of arrangement has typified many of the important political corruption cases tried by the government, including *McNally* itself.<sup>220</sup> However, while it is theoretically possible to reap a benefit at the expense of no one,<sup>221</sup> in most cases where the prospective defendant has obtained an unjust gain, a victim who has suffered a concrete economic loss may be found. In *McNally* finding such a victim would not have been difficult. The prosecutor should have asked someone from Wombwell the following question at the trial: "If you had not paid this \$200,000 to Seton Investments what would you have done with it?" Answer: "Distributed it to other qualifying insurance agencies at Hunt's direction."<sup>222</sup> Thus there is a victim—a victim that could sue via a class action and that suffered concrete, material (\$200,000) economic harm—the *class* of legitimate Kentucky insurance agents. Similarly, in *Isaacs*, one should not conclude too quickly that, since all that Governor Kerner did was grant extra racing days to the parties that bribed him, nobody lost. Arguably, if new racing days were available, then the *class* of other racetrack owners, who didn't have an

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<sup>217</sup> 833 F.2d 1183 (6th Cir. 1987), *aff'd*, 842 F.2d 909 (1988).

<sup>218</sup> Moreover, that "constructive trust" theory was, in my view, wrong. See *infra* note 235 and accompanying text.

<sup>219</sup> *Russell v. United States*, 367 U.S. 749, 770 (1962). See *United States v. Ochs*, 842 F.2d 515, 523 (1st Cir. 1988).

<sup>220</sup> See also *United States v. Margiotta*, 688 F.2d 108 (2d Cir. 1982), *cert. denied*, 461 U.S.913 (1983); *United States v. Mandel*, 591 F.2d 1347, *aff'd*, 602 F.2d 653 (4th Cir. 1979), *cert. denied*, 445 U.S. 961 (1980); *United States v. Isaacs*, 493 F.2d 1124 (7th Cir.), *cert. denied*, 417 U.S. 976 (1974).

<sup>221</sup> Hypothetical Case 2 is such a situation. See *supra* notes 22-23 and accompanying text.

<sup>222</sup> A Kentucky law required that the Commissions only be distributed among bona fide insurance agencies. KY. REV. STAT. ANN. §§ 304.9-100, 304.9-420 (Michie/Bobbs-Merrill 1981).

opportunity to use, or to bid on, those new dates, lost a lot of money because of the bribery scheme.

The finding of economic loss to an identifiable victim is even easier in the employee kickback cases.<sup>223</sup> If the employee receives kickbacks from a supplier to buy the supplier's product for the employer, then the employer has suffered economic harm in the amount of the kickback. The kickback demonstrates that, even if the supplier was supplying the product at a fair market price, he or she was, in fact, willing to supply it at a lesser price—the charged price minus the kickback. Unlike the political corruption cases, it is not even necessary to use a class of victims or to speculate about their losses; both the victim and its loss are clearcut.<sup>224</sup>

The only time that this technique will not work is when, as in hypothetical Case 2, the employee's actions have nothing to do with the price. If the government can't prove that the company lost money through the corrupt actions of its employee, then it has not shown fraud.<sup>225</sup> Similarly, in the political corruption cases it may sometimes be impossible to track down even a class of victims who lost by the corrupt officials' actions. However, even these cases may sometimes be subject to prosecution after *McNally*.

Reconsider the mail fraud statute: It prohibits both use of the mails in a scheme to defraud (Clause 1) *or* in a scheme "for obtaining money or property by means of false pretenses, representations or promises."<sup>226</sup> As previously noted, the government urged in *McNally* that the scheme charged there should be considered such an "obtaining" scheme, but the Court ignored that argument holding that "there was nothing in the jury charge that required such a finding."<sup>227</sup> But what if the government, in *McNally*, had simply indicted the defendants for "obtaining money by false representations: to wit the claim to Wombwell that Seton Investments was a bona fide insurance agency."<sup>228</sup> Such a charge surely fits the language of the statute. While Congress may not have "intended" to expand the scope of the statute to cover such "unjust gain but no

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<sup>223</sup> *E.g.*, *United States v. George*, 477 F.2d 508 (7th Cir.), *cert. denied*, 414 U.S. 827 (1973).

<sup>224</sup> The Fifth Circuit has recognized that such cases cause economic loss to the employer. *See United States v. Fagan*, 821 F.2d 1002 (5th Cir. 1987), *cert. denied*, 108 S. Ct. 697 (1988) and cases cited therein.

<sup>225</sup> *Accord United States v. Ballard*, 663 F.2d 541 (5th Cir. 1981), *modified on reh'g*, 680 F.2d 352 (1982).

<sup>226</sup> 18 U.S.C. § 1341 (1982).

<sup>227</sup> *McNally v. United States*, 107 S. Ct. 2875, 2882 (1987). This is a true statement but somewhat misleading since the indictment did charge this as one theory of the case.

<sup>228</sup> *McNally*, 107 S. Ct. at 2882.

loss" cases, by using the phrase "obtaining money or property by false pretenses, representations or promises" it not only focused on the "gain" type of crime, it explicitly went beyond the common understanding of the crime of false pretenses. As discussed, historically, "false pretenses" was thought to be limited to inducing a loss as well as to representations as to past or present facts. The 1909 amendment expanded the coverage of the statute to include other "representations or promises" which may not amount to false pretenses. It is a fundamental of statutory construction that, if the language of the statute is clear, a contrary intent of the legislature will not ordinarily be considered.<sup>229</sup> Here, the mere marginal note citing *Durland* in a Senate Report is hardly sufficient to override such clear statutory language. Thus Clause 2 requires an unjust gain, but no loss.<sup>230</sup>

It might be argued that, by reading the statute as embodying the historic understanding of fraud to include money or property, the Court was also, at least implicitly, suggesting that the historic notion that a fraud required loss to a victim must similarly be incorporated into the entire statute. This argument misconceives the *McNally* holding. The Court did *not* hold that Clause 1 and Clause 2 mean the same thing.<sup>231</sup> It explicitly declined to address itself to the applicability of Clause 2 to the *McNally* indictment.<sup>232</sup> While it is certainly true that "false pretenses" meant the same thing as fraud in 1909, and therefore required a deprivation of money or property, the 1909 amendment went beyond the common law understanding of "false pretenses" to forbid "obtaining money or property by false

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<sup>229</sup> *E.g.*, *Rubin v. United States*, 449 U.S. 424, 430 (1980). "When we find the terms of a statute unambiguous, judicial inquiry is complete, except in 'rare and exceptional circumstances.'" *TVA v. Hill*, 437 U.S. 153, 187 n.33 (1978) (quoting *Crooks v. Harrelson*, 282 U.S. 55, 60 (1930)).

<sup>230</sup> In drawing this conclusion, I am not unmindful of Judge Easterbrook's observation that "the invocation of 'plain meaning' just sweeps under the rug the process by which meaning is devined." Easterbrook, *Statutes' Domains*, 50 U. CHI. L. REV. 533, 536 (1983). Still, in the conduct of everyday life, people constantly assume, and act on the assumption, that words really do have a meaning that is frequently "plain." The phrase in question comprises such words. *See, e.g.*, *Estep v. United States*, 327 U.S. 114, 136 (1946) (Frankfurter, J., concurring) ("Ordinary words [in statutes] should be read with their common, everyday meaning when they serve as directions for ordinary people."). Note, however, that Justice Frankfurter made this observation shortly after he had observed that "[t]he notion that because the words of a statute are plain, its meaning is also plain, is merely pernicious oversimplification." *United States v. Monia*, 317 U.S. 424, 431 (1943) (Frankfurter, J., dissenting).

<sup>231</sup> "The Court recognizes that the 'money or property' limitation of the second clause does not actually apply to prosecutions under the first clause." *McNally*, 107 S. Ct. at 2885 (Stevens, J., dissenting).

<sup>232</sup> *Id.* at 2881.

. . . representations or promises.” Given this clear statutory language (unlike the “to defraud” language interpreted in *McNally*) an “unjust gain” scheme should be prosecutable under Clause 2 without reference to any loss.

The “unjust gain” approach is a preferable theory for the government because, unlike the fraud theory, it does not require proof of loss. Defendants could, however, argue with some force that it requires an affirmative misrepresentation.<sup>233</sup> This would provide a certain symmetry to the statute, requiring the government to prove loss (but no affirmative misrepresentation) in a fraud case and an affirmative misrepresentation but no loss in an “unjust gain” case. However, as previously discussed, the crime of false pretenses traditionally could be satisfied by actions or by a failure to disclose that which the defendant had a duty to disclose.<sup>234</sup> There is no reason to suppose that Congress, by adding Clause 2 to the statute intended to change the meaning of “false pretenses.”<sup>235</sup> While the statute, by its very terms, must be read as *expanding* on traditional false pretenses by adding “representations or promises,” there is absolutely no reason to read it as, at the same time, *narrowing* false pretenses to require an affirmative representation. Misleading actions, or a failure to speak when there is a duty to do so, while they may not be “representations or promises,” continue to be “false pretenses” after the 1909 amendment. Thus, the lawyer who fails to disclose a conflict of interest to his or her client and is then paid by that client has obtained money by false pretenses, whether or not the client stood to be harmed. *However, the false pretenses must be directed toward the payor, otherwise the property has not been obtained “by means of false pretenses” as required by the statute.* Thus, as will be discussed,<sup>236</sup> the highway commissioner who accepts money to grant a highway contract to a contractor has not violated the statute, for he or she has

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<sup>233</sup> As it seemed to in American federal law prior to 1907. Goldstein, *supra* note 51, at 425.

In the 1907 case of *United States v. Robbins*, 157 F. 999, 1001 (D. Utah 1907), the court held that an affirmative misstatement was not required in conspiracy to defraud the government cases, reflecting the trend in civil law. Goldstein, *supra* note 51, at 425. In 1910 the Supreme Court upheld the conviction of a government employee for conspiracy to defraud the United States when he sold confidential government information about grain prices, despite the fact that he had made no representations or promises to any official. *Haas v. Henkel*, 216 U.S. 462 (1910). See generally Goldstein, *supra* note 51, at 425-26 (discussing the abandonment, in the early twentieth century federal law of fraud, of the requirement that there be an affirmative misstatement). What impact these decisions had on Congress reenactment of the mail fraud statute in 1909 is a difficult question.

<sup>234</sup> See *supra* note 97.

<sup>235</sup> See *Carpenter v. United States*, 108 S. Ct. 316, 321 (1987).

<sup>236</sup> See *infra* notes 253-54 and accompanying text.

not obtained money by means of any false pretense (unless the government can establish a case using unsuccessful bidders, rather than the bribe-payor as the victim).

Consider the recent case of *United States v. Murphy*.<sup>237</sup> Murphy was a Tennessee judge who used an inactive Masonic lodge to apply for a state bingo license under the state's "charitable organization" exception to the gambling laws. He used a false name and falsely asserted that he was a member of a charitable organization and that no member of the organization would profit personally from the game.<sup>238</sup> He then split the profits with one Smith who operated the game. He was convicted of eleven counts of mail fraud.<sup>239</sup> The court of appeals reversed the conviction. The indictment charged that the defendant had "defraud[ed] the State of Tennessee of the right to issue certificates of registration . . . based on complete true and accurate information."<sup>240</sup> The court concluded that this right was an intangible, not a property right: "[T]he certificate of registration . . . may well be 'property' once issued, insofar as the charitable organization is concerned, but certainly an unissued certificate of registration is not property of the State of Tennessee and once issued it is not the property of the State of Tennessee."<sup>241</sup>

The State suffered no economic loss here and therefore was not deprived of property. However, the defendant clearly *did* acquire an economic gain by means of false representations. Accordingly, he should have been prosecuted under Clause 2. By the same token, in election fraud cases, while it may be argued that a defendant who has won an election by fraudulent means has not defrauded the state or city of money or property because it would have paid out the elected official's salary anyway,<sup>242</sup> it is certainly true that the defendant has obtained money (the salary of the office) by means of false pretenses or representations (e.g., the representation that the bought or forged votes are valid).<sup>243</sup> Thus the election fraud cases cited by Justice Stevens in his *McNally* dissent<sup>244</sup> could still be prosecuted under the mail fraud statute.

To summarize this approach, then, the government would have to prove that the defendant engaged in a (1) scheme to intentionally

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<sup>237</sup> 836 F.2d 248 (6th Cir.), *cert. denied*, 109 S. Ct. 307 (1988).

<sup>238</sup> *Id.* at 249.

<sup>239</sup> *Id.*

<sup>240</sup> *Id.* at 251.

<sup>241</sup> *Id.* at 253-54.

<sup>242</sup> Though the successful opponent *has* been defrauded.

<sup>243</sup> The candidate may make no such false representation but, normally, one of his or her confederates will have done so.

<sup>244</sup> *McNally v. United States*, 107 S. Ct. 2875, 2883 n.2 (1987)(Stevens, J., dissenting).



obtain money or property (2) by means of (3) knowing false pretenses, representations or promises, and (4) used the mails or wires or caused their use. As in the fraud cases, it would not be necessary to show that the scheme was successful. As long as the scheme involved money or tangible property, as in *McNally*, the government's burden would certainly be less than in a fraud case under Clause 1 because it would not be necessary to prove economic harm to a particular victim. However, recall that Clause 2 of the statute requires that a defendant obtain "money or property" and that Congress understood that to mean money or *tangible* property. As discussed, in *Carpenter* the Court stretched the meaning of "property" to include certain intangibles but made it fairly clear that the concept of "property" itself required economic harm (or potential harm) to an identifiable victim.<sup>245</sup> Obviously, the concept of "property" means nothing different in Clause 2 than its implicit meaning in Clause 1. Thus, to prove an unjust gain case under Clause 2, *where the gain is an intangible*, the government, to be consistent with *Carpenter*, must prove concrete economic harm to an identifiable victim. Otherwise the defendant cannot be said to have obtained "property." *Carpenter* aside, it would make no sense to prosecute an employee for obtaining the employer's darkest secrets unless the employee sought to use them for his or her own profit (in which case he or she would have sought to obtain tangible property—the profit). Mere curiosity, even when satisfied by means of false representations, should not be criminalized. The concept of "misappropriating" an intangible simply makes no sense unless it is accompanied by harm to an identifiable victim. By contrast, if one takes money or tangible property that doesn't belong to him or her, a culpable act has occurred, without the victim being identified.

There is another limit on this theory of prosecution that does not apply to Clause 1 prosecutions. Recall that, in *Carpenter*, the Court held that "the concept of fraud" includes the act of embezzlement.<sup>246</sup> As discussed, this was a misunderstanding of the "concept of fraud" and an expansion of the statute. However, whatever may be said of the "concept of fraud," it is unavoidably true that the "concept of false pretenses" (representations or promises) does not include embezzlement, for the two have always been separate crimes.<sup>247</sup> Consequently, if the fraudulent behavior is embezzlement, larceny by trick, or other similar activity, the government

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<sup>245</sup> See *Carpenter v. United States*, 108 S. Ct. 316, 321 (1987).

<sup>246</sup> *Id.*

<sup>247</sup> See 2 W. LAFAYE & A. SCOTT, *supra* note 97, § 8.6 (Embezzlement), § 8.7 (False Pretenses).

must prove that a loss to the victim was reasonably foreseeable. However, it is hard to imagine an embezzlement or larceny by trick in which this would not be true anyway.

The above two means of avoiding the thrust of *McNally*—either finding a victim or class of victims who lost property or charging an unjust gain under the second clause of the statute—will be very effective. They allow the federal government to prosecute, with no amendment of the mail fraud statute, many of the approximately thirty-five cases that were cited in Justice Stevens' *McNally* dissent that had been previously charged under the "intangible rights" theory.<sup>248</sup> However, one case, *United States v. Condolon*,<sup>249</sup> involved a defendant who falsely held himself out as a talent agent to obtain sexual favors from women. Assuming that the courts would find no "economic gain" for the defendant or economic harm to the victim here, this would not count as "property" under *McNally*. However, one could reasonably wonder why the federal government felt it necessary to prosecute this case in the first place.

Another common case involves politicians and judges who accept money in order to make decisions favorable to the payor. In addition to being guilty of bribery under state law, the Hobbs Act<sup>250</sup> and possibly RICO,<sup>251</sup> would they still be liable under the mail fraud statute? In some cases, as in *McNally*, they would have received money as a result of a misrepresentation ("Seton is a legitimate insurance agency") and could certainly be prosecuted on that ground. In other cases they will have defrauded their employer, the state or local government, of money. Finally, in many cases, the unsuccessful bidder or litigant may be identified as a victim who lost money as a result of the defendant's misrepresentation or breach of fiduciary duty owed to him or her. However, in many bribery cases there is

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<sup>248</sup> *McNally*, 107 S. Ct. at 2883 n.1 (Stevens, J., dissenting).

<sup>249</sup> 600 F.2d 7 (4th Cir. 1979).

<sup>250</sup> 18 U.S.C. § 1951(a) (1982). The Act provides that "whoever in any way or degree obstructs, delays or affects commerce . . . by robbery or extortion" is guilty. 18 U.S.C. § 1951(b)(2) "Extortion" includes acting "under color of official right." The Hobbs Act has frequently been used to prosecute corrupt politicians who receive bribes. See, e.g., *United States v. Kenney*, 462 F.2d 1205 (3d Cir. 1972); *United States v. Staszczuk*, 502 F.2d 875 (7th Cir. 1974), *modified*, 517 F.2d 53 (7th Cir.) (en banc), *cert. denied*, 423 U.S. 837 (1975). Some minimal effect on interstate commerce must be shown, however. *Staszczuk*, 502 F.2d at 879.

<sup>251</sup> 18 U.S.C. § 1962(c) (1982). RICO forbids operating an enterprise (the office in question) through a pattern (2 or more) of racketeering activity. 18 U.S.C. § 1961(1) (1982) lists "bribery" and "extortion which are cognizable under state law as crimes that constitute "racketeering activity." The commission of two or more acts of racketeering activities constitutes "a pattern of racketeering activity." 18 U.S.C. § 1961(5) (1982). Thus, if two counts of state law bribery may be proved in the federal trial, the RICO prosecution will likely succeed.

no victim and no false representation. Consequently, there is no mail fraud. It would not be enough to argue that the official has made an implicit promise or explicit oath to conduct his or her office honestly and that, in receiving bribes, has violated that oath and thus obtained money by false pretenses. This is nothing more than the intangible right to honest and faithful services rejected in *McNally*, although under a different clause of the statute. Clearly the crime of obtaining money by false pretenses assumes that the false representation is made, directly or indirectly, explicitly or implicitly, *to the party delivering the money or property* and that it *caused* that delivery.<sup>252</sup> The corrupt judge, bribed by a criminal defendant, has offered no false pretense, representation or promise, either to the city or the payor nor, most likely, was his or her oath of office false at the time it was made. The judge has also not induced the city to part with property by misleading actions or by silence (unlike in *Carpenter*). Unless it can be shown that the city lost money in the transaction (as it frequently can be)<sup>253</sup> the government will have to be satisfied with prosecuting under RICO, the Hobbs Act, and state bribery law, for this is neither a fraud nor the obtainment of money by means of false pretenses, representations or promises. It is, rather, a bribery.<sup>254</sup>

In order to get around the problems posed by *McNally*, the government has advanced a more complex argument. This is based on a footnote to Justice Stevens' dissent in *McNally*:

When a person is being paid a salary for his loyal services, any breach

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<sup>252</sup> *E.g.*, F. WHARTON, *supra* note 112, § 1398. The victim must swear that the "false representation . . . induced him to part with his property." *Accord* Coffee, *Tort to Crime*, *supra* note 75, at 169. The Second Circuit recognized this in *United States v. Covino*, 837 F.2d 65, 71 (2d Cir. 1988) (mail fraud requires a finding that the *victim* be defrauded of money or property). *Accord* *United States v. Evans*, 844 F.2d 36, 39 (2d Cir. 1988).

<sup>253</sup> *See supra* note 236. If the principal has lost money, then the defendant is guilty of fraud under Clause 1.

<sup>254</sup> *Fasulo v. United States*, 272 U.S. 620, 628 (1926) (use of the mails to carry out a scheme of extortion, while "reprehensible" was not a scheme to "defraud").

MODEL PENAL CODE § 223.3 (1980). The Code states:

A person is guilty of theft if he purposely obtains property of another by deception.

A person deceives if he purposely:

- 1) creates or reinforces a false impression . . . or
- 2) prevents another from acquiring information which would affect his judgment of a transaction; or,
- 3) fails to correct a false impression which the deceiver previously created or reinforced, or which the deceiver knows to be influencing another to whom he stands in a fiduciary or confidential relationship; or,
- 4) fails to disclose a known lien (etc.)

This statute embodies the traditional offense of false pretenses. MODEL PENAL CODE § 223.3 commentary at 180 (1980). None of these categories apply to the corrupt judge in the hypothetical.

of that loyalty would appear to carry with it some loss of money to the employer—he is not getting what he paid for. Additionally, “if an agent receives anything as a result of his violation of a duty of loyalty to the principal, he is subject to a liability to deliver it, its value, or its proceeds to the principal.” This duty may fulfill the Court’s “money or property” requirement in most kickback schemes.<sup>255</sup>

This “constructive trust” theory, adopted by a number of courts of appeal in post-*McNally* opinions,<sup>256</sup> was rightly rejected by the Seventh Circuit in *United States v. Holzer*,<sup>257</sup> which held that it is “only in an attenuated and artificial sense that the bribe is the principal’s property.”<sup>258</sup> It makes little sense to argue, for example, that bribe money paid to a state judge is really the state’s, for, as the *Holzer* court observed, “the State of Illinois does not sell justice.”<sup>259</sup> Clearly, there is no “loss” to the employer in any meaningful sense here, and consequently there is no fraud (in contradistinction to cases in which the government can show that a kickback to the employee had the effect of raising the price that the employer paid for the product).<sup>260</sup> Also, as discussed,<sup>261</sup> there has been no false representation to the employer, so an “unjust gain” theory would not work either. Only if the government could prove that payments to the defendant judge had caused him to breach a duty to parties before him, causing *their* loss of money or property would this be a fraud.<sup>262</sup> The Hobbs Act and RICO (predicated on state bribery or federal Hobbs Act violations) would, however be available as the

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<sup>255</sup> *McNally v. United States*, 107 S. Ct. 2875, 2890 n.10 (1987)(Stevens, J. dissenting)(quoting Restatement (Second) of Agency § 403 (1958)).

<sup>256</sup> *E.g.*, *United States v. Rannels*, 833 F.2d 1183, 1188 (6th Cir. 1987), *aff’d on reh’g*, 842 F.2d 909 (6th Cir. 1988); *United States v. Richerson*, 833 F.2d 1147, 1157 (5th Cir. 1987).

<sup>257</sup> 840 F.2d 1343 (7th Cir. 1988).

<sup>258</sup> *Id.* at 1348.

<sup>259</sup> *Id.* Having made these observations the court went on to suggest that a viable prosecution could be made out if the “corrupt public official, having received bribes, takes steps to conceal them in order to defeat the public employer’s right to obtain them by a suit based on constructive fraud principles.” *Id.* The idea seems to be that the employer’s interest in the bribe was too “attenuated” to constitute a loss, in part because it is not clear when the employee is obliged to turn over the proceeds. Nevertheless the employer could sue for the proceeds of the bribe, and the employee’s attempts at a coverup would be a fraud. *Id.* How the government would prove that “the efforts [at concealment] were designed to prevent the state from obtaining the bribe money, as distinguished from preventing the state from discovering the bribery” in the first place, as the court required, *id.*, is not clear.

<sup>260</sup> *See supra* notes 223-24 and accompanying text.

<sup>261</sup> *See supra* notes 235-36 and accompanying text.

<sup>262</sup> Or, of course, if the people who paid money to the judge had in some way been defrauded. *See United States v. Holzer*, 840 F.2d 1343, 1345 (7th Cir. 1988).

*Holzer* court held.<sup>263</sup>

A similar approach was adopted by the Fifth Circuit in *United States v. Richerson*.<sup>264</sup> After *McNally*, the government simply argued that the charge in the indictments, alleging the right of the employer to his employee's honest and faithful services, was a "property right." That is, that the defendant defrauded the employer out of money (his salary) by failing to deliver the honest services for which he was being paid. But this is nothing more than another way of stating that the employer has an interest in the honest and faithful services of its employee, an interest that the *Carpenter* Court deemed, "too ethereal to fall within the protection of the mail fraud statute."<sup>265</sup> The employer would have paid the employee's salary in any event. Unless an independent economic loss from the fraud can be shown, the "loss" element has not been satisfied. The First Circuit properly rejected this approach in *United States v. Ochs*.<sup>266</sup>

Another argument was advanced by the government in *United States v. Evans*.<sup>267</sup> There, the defendant conspired to sell arms of American manufacture to an "Iranian buyer"<sup>268</sup> who was actually an American undercover agent. The arms were admittedly not owned by the United States but by foreign countries. Thus it would appear, that whatever violation of statutes prohibiting arms sales may have occurred, the United States was in no way defrauded of money or property. However, the government argued that it maintained an interest in the resale of American arms to Iran, which resale was prohibited by law, and that that interest was a "property" interest under *McNally*.<sup>269</sup> The Second Circuit rejected this argument, holding, after an analysis of property law, that this was not a "property" interest at common law.<sup>270</sup> Whatever the resolution of that issue, it seems clear that, under the test advanced in this Article, the government was harmed in its *political* rather than its *economic* interests and consequently, there was no deprivation of "property" as that term is used in the criminal law of fraud.

The above conclusions about the meaning of the term "fraud" are based on my reading of the statute, as illuminated by history,

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<sup>263</sup> *Id.* at 1350-51. However, *Holzer's* RICO conviction was vacated because it may have been predicated on the invalidated mail fraud counts.

<sup>264</sup> 833 F.2d 1147, 1157 (5th Cir. 1987).

<sup>265</sup> *Carpenter v. United States*, 108 S. Ct. 316, 320 (1987).

<sup>266</sup> 842 F.2d 515, 523-24 (1st Cir. 1988). *Accord* *United States v. Lytle*, 677 F. Supp. 1370, 1381 (N.D. Ill. 1988).

<sup>267</sup> 844 F.2d 36 (2d Cir. 1988).

<sup>268</sup> *Id.* at 37.

<sup>269</sup> *Id.*

<sup>270</sup> *Id.* at 41-42.

and of the *Carpenter* and *McNally* decisions. The Court squares with the historic understanding of fraud when it requires a victim, a gain and a loss. It deviates from history when it allows the gain and loss to be intangible in nature and, as a concomitant of that holding, apparently allows the gain to differ from the loss. While the Court has allowed the concept of "fraud" to expand somewhat, to include at least some kinds of embezzlement as well as to allow intangible property as the object of the scheme, still, the basic principle of these cases, is that the term "fraud," when it appears in a federal statute, has content. It does not mean "any wrongful behavior." It does not mean extortion, bribery, or robbery.<sup>271</sup> It means, as it had always meant, until the recent federal court decisions reversed by *McNally*, *depriving a victim of property by means of deceit*. If the principle of legality is to have any vitality in American law,<sup>272</sup> as the Supreme Court asserts that it has,<sup>273</sup> then criminal statutes must be construed according to their ordinary meaning.<sup>274</sup> It is enough to satisfy the

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<sup>271</sup> As the Court has held in *Hammerschmidt v. United States*, 265 U.S. 182, 188 (1924), and *Fasulo v. United States*, 272 U.S. 620, 627-28 (1926).

<sup>272</sup> The principle of legality, *nulla poena sine lege* (no punishment except in accordance with law), is the basis of the rule, applied in *McNally v. United States*, 107 S. Ct. 2875, 2881 (1987), that criminal statutes be strictly construed. See generally G. WILLIAMS, CRIMINAL LAW, THE GENERAL PART §§ 184-86 (2d ed. 1961).

As Chief Justice Marshall observed long ago:

The rule that penal laws are to be construed strictly, is perhaps not much less old than construction itself. It is founded on the tenderness of the law for the rights of individuals; and on the plain principle that the power of punishment is vested in the legislature, not in the judicial department. It is the legislature, not the Court, which is to define a crime, and *ordain* its punishment.

*United States v. Wiltberger*, 18 U.S. (5 Wheat) 76, 95 (1820). See Jeffries, *supra* note 80, at 190 (insightful discussion of the application of the various aspects of the principle in contemporary American law).

<sup>273</sup> "There are no constructive offenses, and before one can be punished it must be shown that his case is plainly within the statute." *Fasulo*, 272 U.S. at 629. "Engrained in our concept of due process is the requirement of notice." *Lambert v. California*, 355 U.S. 225, 228 (1957).

<sup>274</sup> Sometimes statutes or constitutional provisions must be read more broadly than their ordinary meaning at the time of drafting in order to deal with changes that have occurred since that drafting. Thus, the Supreme Court was surely correct to consider electronic eavesdropping to be a "search" in *Katz v. United States*, 389 U.S. 367 (1967), despite the fact that "search" did not include such activity in the late 18th century. When the government is using a statutory provision as a sword to prosecute criminal activity, rather than an individual using it as a shield against governmental overacting, however, the language of the writing in question must be more strictly construed. Thus, if an 18th century criminal statute forbade people from engaging in certain "searches," I would have difficulty agreeing that that term applied to electronic surveillance, despite my agreement with *Katz*. The principle of legality applies to the interpretation of criminal prohibitions, not constitutional limitations.

Finally, the breaches of trust punished in the pre-*McNally* mail fraud prosecutions did not even present the problem discussed above. Dishonest employees and corrupt government officials were obviously within the ken of Congress in 1872 and 1909. The

interests of the federal government that Congress has virtually unlimited power to declare any wrongful behavior a federal violation, notwithstanding traditional limitations on federal power.<sup>275</sup> It is neither necessary nor proper for the federal courts to take it upon themselves, in the absence of congressional enactment, to expand the clear meaning of statutes, in order to reach behavior that the courts and the Justice Department feel should be punished.<sup>276</sup> While the people singled out for prosecution under the mail fraud statute may have richly deserved criminal sanction, the fleeting satisfaction derived from bringing such malefactors to the bar of justice must be sacrificed for deference to constitutional principles.

## V. THE GOVERNMENT STRIKES BACK

As discussed, on August 4, 1987, shortly after *McNally* was decided, Representative Conyers introduced a bill, H.R. 3089,<sup>277</sup> to counter that holding. The bill simply amended chapter 1, title 1 of the United States Code to add a definition of "fraud" throughout the Code as: "1) defrauding another of intangible rights of any kind whatsoever in any manner or for any purpose whatsoever; or 2) by using material private information wrongfully stolen or misap-

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mail fraud statute *could* have been written to cover bribery and breaches of duty that did not result in economic harm. There is simply no reason to believe that it *was*. Since deficiencies in statutes are more easily remedied than those in constitutions, it is sensible to read the former more narrowly than the latter.

<sup>275</sup> *E.g.*, *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528 (1985); *Perez v. United States*, 402 U.S. 146 (1971).

<sup>276</sup> The approach of the federal courts, simply declaring a variety of wrongful behavior to be "fraud" and therefore punishable, while certainly well intentioned and not leading to the punishment of innocents, nevertheless is reminiscent of the approach of the Nazis in Germany. According to the German Act of June 28, 1935:

Whoever commits an act which the law declares to be punishable or which is deserving of punishment according to the fundamental idea of a penal law and sound popular feeling shall be punished. If there is no penal law applying directly to the act it shall be punished under the law whose basic idea best fits it.

G. WILLIAMS, *supra* note 272, § 184. As Williams points out, violation of the principle of legality can also occur in a cause that most would consider "just." The Nuremberg war crimes trials are an example of this. *Id.* One could argue that the Nazis, by enacting this statute, complied with the principle of legality and that their scheme suffered from some other problem, such as overbreadth.

<sup>277</sup> H.R. 3089, 100th Cong., 1st Sess., 133 CONG. REC. (August 4, 1987). Another bill, H.R. 3050, 100th Cong., 1st Sess., 133 CONG. REC. (July 29, 1987) was introduced by Representative Mfume. This bill simply added a new § 1346 to title 18 which provided that:

[a]s used in sections 1341 and 1343, the term 'defraud' includes the defrauding of the citizens of a body politic—

- 1) of their right to the conscientious loyal, faithful, disinterested, and unbiased performance of official duties by a public official thereof; or
- 2) of their right to have the public business conducted honestly, impartially, free from bribery, corruption, bias, dishonesty, deceit, official misconduct, and fraud.

propriated in breach of any statutory, common law, contractual, employment, personal or other fiduciary relationship."<sup>278</sup>

Despite the fact that Congress can define the terms in its Code any way it likes, with no jurisdictional justification,<sup>279</sup> the bill went on to state the jurisdictional basis of the bill as including article IV, section 4 of the Constitution (the United States shall "guarantee to every State . . . a Republican Form of Government").<sup>280</sup> Congressman Conyers then presented a lengthy and learned discussion as to why this clause was an appropriate basis for federal criminal jurisdiction as to state and local government corruption.<sup>281</sup>

The Justice Department, evidently awaiting the outcome of the *Carpenter* case, introduced its version on May 12, 1988. The Department did not support HR 3089 because it was "too broad" and an "overreaction" to the *McNally* decision."<sup>282</sup> More specifically, by changing the definition of "fraud" in the entire code, it would affect over 500 sections with possible unforeseen consequences.<sup>283</sup> Second, it would "greatly expand federal authority into a wide range of commercial and personal matters."<sup>284</sup> This was an odd objection for the Department to make since it had just argued in *McNally* and *Carpenter* that it already *had* this authority under the mail fraud statute.

Instead the Justice Department proposed a new statute prohibiting "public corruption" and providing that anyone who "attempts to deprive or to defraud by any scheme or artifice, the inhabitants of a State or political subdivision of a State of the honest services of [its] official or employee." violates the section.<sup>285</sup> This statute thus avoided twisting the term "fraud" to mean something that it had never meant before, and created a new statute to deal with corruption of public officials, but not private employees.

While Congress saw the wisdom in avoiding a change in the meaning of fraud throughout the entire Code, it otherwise rejected the Department's proposal. Instead, it adopted a new definition of

<sup>278</sup> H.R. 3089, 100th Cong., 1st Sess. (August 4, 1987).

<sup>279</sup> The jurisdictional basis for prosecution under the mail fraud statute would still be the use of the mails, as is presently the case.

<sup>280</sup> H.R. 3089, 100th Cong., 1st Sess., 133 CONG. REC. § 3 (3) (August 4, 1987).

<sup>281</sup> 133 CONG. REC. H10,657 (daily ed. November 19, 1987)(statement of Rep. Conyers)(citing NATIONAL COMMISSION ON REFORM OF FEDERAL CRIMINAL LAW, STUDY DRAFT OF A NEW CRIMINAL CODE 133 (1970)).

<sup>282</sup> Hearings on H.R. 3089 *Before the House Subcomm. on Criminal Justice, Committee on the Judiciary*, 100th Cong., 2d Sess. 5-6 (May 12, 1988)(statement of Acting Assistant Attorney General Keeney)[Hereinafter *Hearings*.]

<sup>283</sup> *Id.* at 6.

<sup>284</sup> *Id.*

<sup>285</sup> The Anti-Corruption Act of 1988, S. 2793, 100th Cong., 2d Sess. (Sept. 15, 1988).



fraud, applicable only to the Mail Fraud statute "that defines the term 'scheme or artifice to defraud' to include a 'scheme or artifice to defraud another of the intangible right of honest services.'"<sup>286</sup>

This statutory change was accompanied by a statement by Representative Conyers indicating that it was intended to "restore the mail fraud provision to where [it] was before the *McNally* decision."<sup>287</sup> He continued that it "is no longer necessary to determine whether or not the scheme or artifice to defraud involved money or property."<sup>288</sup>

Since this statute does not change the meaning of "fraud" in the other 500 odd times it appears in the Code, everything said about the meaning of fraud in this Article would still be applicable to those sections. Indeed, Congress' decision, contrary to Representative Conyers' original proposal, *not* to change the definition of fraud throughout the Code, may be taken as an accession to *McNally's* narrow reading of the term.<sup>289</sup>

If this change in the mail fraud statute is read narrowly by the courts, it will have little impact on the law as it now stands after *Carpenter*. While Congress expanded the mail fraud statute beyond "money or property," the Court had already done this, in effect, in *Carpenter*. Congress did *not* eliminate the requirement, implicit in *McNally* and *Carpenter*, that the concept of fraud includes an identifiable victim. Indeed, the new requirement that the government show that the defendant deprived *another* of the intangible right of honest services surely requires that this "other" be identified and, for his or her "right" to be established, the defendant should owe this individual a fiduciary duty.

It is clear, on the other hand, that the requirement of economic gain to the defendant and loss to the victim has been eliminated. However, the government would be well advised not to rely too heavily on this innovation and, instead, to try to define the defendant's gain and the victim's loss in economic terms. In *Carpenter*, the Court held that the employer's right to its employee's "honest and faithful service" was "an interest too ethereal in itself to fall within the mail fraud statute."<sup>290</sup> It is at best unseemly and at worst sub-

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<sup>286</sup> 134 CONG. REC. H11,251 (daily ed. Oct. 21, 1988).

<sup>287</sup> *Id.* (statement of Rep. Conyers).

<sup>288</sup> *Id.* (statement of Rep. Conyers).

<sup>289</sup> *But see* Haas v. Henkel, 216 U.S. 462, 480 (1910), discussed in *McNally v. United States*, 107 S. Ct. 2875, 2881 n.8 (1987) (Court had already read the "money or property" requirement out of the term "defraud" for purposes of 18 U.S.C. § 371 (conspiracy to defraud the United States)).

<sup>290</sup> *Carpenter v. United States*, 108 S. Ct. 316, 320 (1987).

ject to reversal on vagueness grounds, for the government to prosecute people on a theory deemed "ethereal" by the Supreme Court, whatever Congress says. This is particularly true where the statute can be read as prohibiting mere dishonest statements which may be protected by the first amendment,<sup>291</sup> and where it is apparently intended to apply to people like Mr. McNally and/or Mr. Hunt, who had no fiduciary relationship with the "people of the State of Kentucky." "Men of common intelligence must necessarily guess at [the] meaning" of such a statute.<sup>292</sup> Since, in the normal case, economic loss and gain can be readily identified, the government should strive to do so.

If, on the other hand, the courts read this statute broadly, as they are wont to do,<sup>293</sup> it may create difficulties unanticipated by Congress. While the concept of "money and property" is not entirely clear after *Carpenter*, it at least has a concrete grounding in economic gain and loss. But what is the "intangible right of honest service," to the extent that it goes beyond such economically motivated behavior? Did the citizens of Kentucky have such a right as to McNally, a private citizen, or Hunt, the Democratic Party chairman? Certainly a court could conclude that they did, given Congress' intent to overrule *McNally*.<sup>294</sup> Does a Governor who, for purely political purposes, dissembles about his intent to raise taxes, or his knowledge of a judicial nominee's background, deprive the citizens of his "honest services?" What of a lobbyist who invites a member of Congress to spend a weekend at a resort or a corporation which pays him to give a speech? Such lobbying efforts are obviously aimed at gaining an advantage for the party offering them, an advantage that an enthusiastic prosecutor and willing jury could well deem to be an attempt to deprive the citizens of the "honest services" of their representative. If history is to be the guide, the Justice Department and the courts will find cases to prosecute that were never contemplated by the drafters of the bill. Instead of the debate focusing on whether or not "fraud" includes certain, obviously corrupt, but not necessarily loss-producing behavior, such as in *Mandel* and *McNally*, the focus will now become whether mere dishonesty by public and private employees, unaccompanied by any corrupt eco-

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<sup>291</sup> The vagueness problem is particularly acute where, as here, "a statute's literal scope . . . is capable of reaching expression sheltered by the first amendment." *Smith v. Goguen*, 415 U.S. 566, 573 (1974).

<sup>292</sup> *Connally v. Gen. Constr. Co.*, 269 U.S. 385, 391 (1926).

<sup>293</sup> See, e.g., Bradley, *Racketeering and the Federalization of Crime*, 22 AM. CRIM. L. REV. 213, 245 (1984).

<sup>294</sup> Though, as noted, the words of the statute could be read as requiring a fiduciary relationship.

conomic motive, violates the new statute. The words of the statute suggest that it does. Congress may find, to the discomfort of its own members, that it has let a genie out of a bottle that was best left corked.

## VI. CONCLUSION

The Court in *McNally* and *Carpenter* went back, but not all the way back, to basics with the mail fraud statute. The holdings require that, as traditionally was the case, a "fraud" requires the government to prove that a victim suffered, or stood to suffer, economic harm and that the defendant stood to obtain an unjust economic gain. The holding of *McNally* that the victim's loss must be of "money or property" was rendered nugatory by *Carpenter*. Any deprivation of an intangible interest that could give rise to economic harm may be the basis of the fraud prosecution. And, while it is necessary that the victim stand to lose and the defendant to gain, it is not necessary that the victim's loss be the defendant's gain, for such was not the case in *Carpenter*. The mens rea as to these elements is intent or purpose to gain, negligence as to loss and knowledge as to the fraudulent behavior. In many of the cases previously tried under "intangible rights" theories, the government could have identified a victim who suffered an economic loss and successfully prosecuted the case according to the *McNally* strictures. While a "scheme to defraud" requires a gain and a loss, the crime described in Clause 2 of the statute, "obtaining money or property by false pretenses, representations or promises," clearly does *not* require any proof of loss. Defendants who, by knowingly false representations or breaches of fiduciary duty, obtain property to which they are not entitled have violated this statute. However, even in these cases the government must prove the false pretense or breach of a duty to disclose. In the normal bribery case the defendant makes no false representation. He is guilty of bribery, not fraud, and there is no justification for reading a statute that prohibits fraud as operating against all forms of dishonest behavior.