# ESSAY

## WHAT THE MARTHA STEWART CASE TELLS US ABOUT WHITE COLLAR CRIMINAL LAW

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## I. INTRODUCTION

Martha Stewart has become an emblematic figure in American life. On one hand, she personifies all that is right about the American Dream. She built a large, profitable company and named it for herself: Martha Stewart Living Omnimedia. She did it through creativity, hard work, and entrepreneurial risk-taking. She reached the pinnacle of success: an invitation to sit on the board of directors of the New York Stock Exchange.[1] Martha Stewart also epitomizes the objective of early feminists who fought for equal opportunity in the workplace. She demonstrated that, given a chance, women can make it in the business world. Her business model, based on domestic art and women's work,[2] demonstrated the purchasing power of women.

Martha Stewart has also come to represent something else. She now represents much that is wrong with American businesses and executives. Her case illustrates the state of white collar crime: the statutes, their enforcement, and the effects of both. Martha Stewart has served her sentence and lost her appeal.[3] Her case is a suitable vehicle for analyzing white collar criminal law: the facts are relatively straightforward, and the case is over. Insights gained here are not, however, confined to the Stewart case; they apply generally, even to the cases that are now being tried in the neighborhood.[4]

I also want to issue a disclaimer. I was never a "Martha Maven." At our house we scramble eggs, we don't serve them poached with hollandaise sauce, and their edges have not been trimmed with manicure scissors. Like many working women, I was aware of Martha Stewart and generally admired her accomplishments, but I was somewhat ambivalent about her emphasis on domestic perfection.[5]

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1. Indictment at 2, United States v. Stewart, 323 F. Supp. 2d 606 (S.D.N.Y. 2004) (03 Cr. 717, (MGC)), *aff'd*, 433 F.3d 273 (2d Cir. 2006) [hereinafter Indictment], *available at* http://fl1.findlaw.com/news.findlaw.com/hdocs/docs/mstewart/usmspb60403ind.pdf.

2. *See* Gloria Borger, *Why Hate Martha?*, U.S. NEWS & WORLD REP., July 8, 2002, at 17 (noting the irony of Stewart's position).

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

4. The trial of Kenneth Lay and Jeffrey Skilling had just begun when this speech was delivered on February 4, 2006. The trial ended in the summer of 2006 with guilty verdicts against both men. *See* Mary Flood, Mark Babineck & John Roper, *Guilty! Guilty!*, HOUS. CHRON., Extra Ed., May 25, 2006, at A1 (discussing guilty verdicts of ex-Enron chiefs).

5. *See* Borger, *supra* note 2, at 17 (suggesting that some women may not like Stewart because her business model celebrates what "baby boom women pledged to escape"). For more on the implications of Stewart's gender on her prosecution, see Joan

A few facts from her story will refresh your memories of Stewart's case.[6] On December 27, 2001, Stewart's friend Sam Waksal sold his holdings in ImClone, a technology company he founded and ran.[7] When Stewart was told about Waksal's sales, she sold all of her shares in ImClone.[8] On the following day, when ImClone announced that the Food and Drug Administration (FDA) had not approved the company's cancer drug, the value of ImClone shares fell by 18%.[9] By selling when she did, Stewart had avoided a loss of approximately $45,000.[10]

Regulators soon suspected that sales of ImClone stock were based on information about the firm's failure to obtain FDA approvals, and they began to investigate whether sellers had violated insider trading law.[11] Eventually, Waksal pleaded guilty to that offense and is now serving a seven year prison term.[12]

During the initial investigation, Stewart was interviewed twice by a set of investigators from three federal agencies: the Federal Bureau of Investigation, the Securities and Exchange Commission (SEC), and the local United States Attorney's Office.[13] On both occasions she offered information about her reasons for selling that a jury later found to be untrue.[14]

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MacLeod Heminway, *Save Martha Stewart? Observations About Equal Justice in U.S. Insider Trading Regulation*, 12 TEX. J. WOMEN & L. 247, 271–74 (2003) (suggesting prosecutors, due to strategic enforcement of securities law, might have targeted Stewart because she is a woman).

6. The facts leading up to Stewart's indictment and trial are found in numerous court filings, decisions, and, of course, in the newspapers, on websites, and in databases. Unless noted, information about Stewart's conduct is taken from the initial indictment. *See* Indictment, *supra* note 1.

A superseding indictment is reprinted as an appendix in a separate opinion regarding a witness in her case, coincidentally also named Stewart. *See* Superseding Indictment, United States v. Stewart, 323 F. Supp. 2d 606, 624–33 (S.D.N.Y. 2004), *aff'd*, 433 F.3d 273 (2d Cir. 2006), *available at* http://fl1.findlaw.com/news.findlaw.com/hdocs/docs/mstewart/usmspb10504sind.pdf. The final appellate decision that rejected her appeals also includes an account of Stewart's conduct. *See Stewart*, 433 F.3d at 281–87.

7. *See* Indictment, *supra* note 1, at 5–6.

8. *Id.* at 7–8.

9. *Id.* at 8.

10. *Id.* at 8–9.

11. *Id.* at 9.

12. *See* Press Release, U.S. Attorney, S. Dist. of N.Y., Samuel Waksal Sentenced in Federal Court to 7 Years 3 Months in Prison, Fined $3 Million (June 10, 2003), *available at* http://www.usdoj.gov/usao/nys/Press%20Releases/June03/WAKSALSENTENCEPR.pdf; *see also* Allan Chernoff, *Sam Waksal Pals Charged*, CNNMONEY, Mar. 9, 2005, http://money.cnn.com/2005/03/09/news/midcaps/scandal_imclone/index.htm (reporting that two friends of Waksal were also arrested on insider trading charges).

13. Indictment, *supra* note 1, at 12, 19.

14. *See* United States v. Stewart, 323 F. Supp. 2d 606, 609–10 (S.D.N.Y. 2004) (describing Stewart's purported reasons for selling and the jury's finding that the statements were false), *aff'd*, 433 F.3d 273 (2d Cir. 2006).

Stewart and her broker, Peter Bacanovic, were eventually indicted for violating several federal criminal laws.[15] A jury found them guilty, and Stewart received a ten month penalty: five months in prison and five months under house arrest.[16] In January 2006, the case officially closed when the Second Circuit rejected her appeals.[17]

What do these events tell us about the federal white collar criminal laws and their enforcement? Quite a lot, as it turns out, and the case serves as an excellent introduction to white collar crime. Stewart's case illustrates nuances of specific federal criminal laws, general issues that are peculiar to white collar criminal law, and concerns about federal white collar criminal law and its enforcement.

To determine what the Stewart case has to say, I begin with the investigation of Stewart's trade. I then proceed to discuss the prosecutor's decision to indict, the specific crimes that were charged, Stewart's trial, and finally, her sentence. Each stage provides insights into white collar criminal law.

## II. THE INVESTIGATION

When a criminal investigation becomes public, several side effects, or collateral consequences, of the investigative process are likely to occur. Most tellingly, financial and business markets react to news of the investigation—and to leaks regarding its progress. Investors sell, shareholders sue, clients withdraw, advertisers bail, and targeted firms soon encounter financial difficulties. The best example of this phenomenon is the case against the Arthur Andersen partnership.[18] By the time the accounting firm was tried, it was only a shadow of its former self.

Stewart's company, Omnimedia, felt similar repercussions, intensified because she was so closely identified with the company's main product lines. Between January 2002, when the investigation began, and March 2004, when the verdict was announced, the company's overall revenues fell 17%, and earnings from publications fell 68.5%.[19] As a result of falling

15. *See* Indictment, *supra* note 1.

16. United States v. Stewart, 433 F.3d 273, 280 (2d Cir. 2006).

17. *Id.* at 319–20 (affirming Stewart's conviction).

18. *See* Arthur Andersen LLP v. United States, 125 S. Ct. 2129 (2005).

19. *See* David Carr & Claudia H. Deutsch, *A Harsh Blow to a Company Based on Image*, N.Y. TIMES, Mar. 6, 2004, at A1. In addition to falling revenue, the strength of her brand, as measured by the customer loyalty index developed by Brand Keys, dropped from a high of 120 (out of a possible 150) in June 2002 to just 83 by June 2003. David Carr, *For the Press, a Case That Is an Irresistible Draw*, N.Y. TIMES, June 5, 2003, at C5.

share prices and general uncertainty about Stewart's future role, corporate shareholders filed thirteen civil suits against Stewart and her company.[20]

Personal and political consequences were also felt by Stewart during the investigation of her trade. As the investigation was beginning in March 2002, she was nominated to the board of the New York Stock Exchange.[21] Seven months later, still during the investigation period, she resigned after her broker's assistant, Douglas Faneuil, pleaded guilty and agreed to testify against her.[22] On the political front, the House Energy and Commerce Committee investigated Stewart's ImClone sale.[23] In September 2002, the Committee referred the matter to the Department of Justice.[24]

Eighteen months into the investigation, Stewart stepped down as CEO and Chairwoman of her company.[25] Now listed on company publications as "founder and editorial director," she has yet to recover those titles.[26] In addition to all of this, the Stewart

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20. *See* Constance L. Hays, *Amended Lawsuit Accuses Some Stewart Executives: Issue Involves When They Knew of Inquiry*, N.Y. TIMES, Feb. 5, 2003, at C2 (reporting one class action lawsuit was filed, and twelve other lawsuits, later consolidated into four, were also filed). For a discussion of the shareholder derivative suit, see Lisa M. Fairfax, *Sarbanes-Oxley, Corporate Federalism, and the Declining Significance of Federal Reforms on State Director Independence Standards*, 31 OHIO N.U. L. REV. 381, 401–03 (2005); *see also* Beam *ex rel.* Martha Stewart Living Omnimedia, Inc. v. Stewart, 833 A.2d 961 (Del. Ch. 2003) (discussing the derivative action against Stewart and the officers and directors of Martha Stewart Living Omnimedia).

21. Indictment, *supra* note 1, at 2.

22. *See* Tracie Rozhon, *Stewart Quits As a Director of Big Board: Her Company's Shares Then Tumble Over 8%*, N.Y. TIMES, Oct. 4, 2002, at C1. To add insult to injury, her company's shares fell 8.7% on the news to $6.21; the high for 2002 was $20.01 in March. *See Besieged Stewart Quits NYSE Board*, HOUS. CHRON., Oct. 4, 2002, at 3C.

23. *See* Letter from W.J. "Billy" Tauzin, Chairman of the House Comm. on Energy and Commerce, to John Ashcroft, U.S. Attorney Gen., (Sept. 10, 2002), *available at* http://energycommerce.house.gov/107/Letters/09102002_714.htm [hereinafter Tauzin Letter] (asking the Department of Justice to investigate whether Stewart violated 18 U.S.C. § 1001); *see also* Constance L. Hays & Patrick McGeehan, *A Closer Look at Martha Stewart's Trades*, N.Y. TIMES, July 15, 2002, at C1 (reporting that Congress was investigating the details of Stewart's trades).

24. Tauzin Letter, *supra* note 23.

25. *See* Brooke A. Masters, *Stewart Pleads Not Guilty to All Charges,* WASH. POST, June 5, 2003, at A1.

26. The SEC brought a civil suit against Stewart on the insider trading charges that was recently settled. *See infra* notes 43–44 and accompanying text. The terms of the settlement forbid Stewart from serving as a company executive or director of any public company for five years. Landon Thomas, Jr., *Stewart Deal Resolves Stock Case*, N.Y. TIMES, Aug. 8, 2006, at C1.

SEC regulations bar any "unfit person" from serving in an executive position in a publicly held company. Congress recently changed the standard from "substantially unfit" to "unfit." *See* Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 305, 116 Stat. 745, 778–79; *see also id.* § 1105 (applying to Section 10(b) enforcement actions). Courts

case, and Stewart herself, were subject to intense public scrutiny throughout the eighteen-month investigation.[27]

What does this account tell us about white collar criminal law? Note first that federal officials were in charge of this criminal matter: administrative agency personnel from the Securities Exchange Commission, agents from the Federal Bureau of Investigation, and lawyers from the United States Attorney's office for the Southern District of New York.[28] White collar crimes are largely a matter of federal criminal law. Although there is significant negative commentary on the tendency of Congress to enact new federal crimes,[29] there is little controversy about treating securities crimes as a federal offense.[30] Congress has constitutional jurisdiction under the Commerce Clause to enact laws that regulate capital markets, and the federal interest in protecting the national securities markets is robust.

Second, as the Stewart case shows, investigations of white collar crimes can take a long time. This is because the conduct and transactions that may constitute a white collar offense occur in private and are often cloaked in secrecy. Hampered by the absence of witnesses, investigators painstakingly follow paper trails. Even though Stewart's transaction was known to

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may prohibit any person from serving as an officer or director of a publicly held company "if the conduct of that person demonstrates unfitness . . . ." *Id.*; *see also* 15 U.S.C. § 78t(e) (2000) (permitting prosecution of persons who aid and abet criminal trade violations); *id.* § 78u(d)(2) (granting authority to the court to prohibit persons who commit civil trading violations from serving as officers and directors).

27. Journalist Jeffrey Toobin interviewed Stewart a year after the investigation began and reported the personal toll that the negative publicity had taken on Stewart. Jeffrey Toobin, *Annals of Law: Lunch at Martha's, Problems with the Perfect Life*, NEW YORKER, Feb. 3, 2003, at 38, 38–44. Stewart exacerbated the media attention when she posted her side of the story on her now defunct web site, http://www.marthatalks.com. *See* Constance L. Hays, *Martha Stewart Uses Web to Tell Her Side of Story*, N.Y. TIMES, June 6, 2003, at C1 (quoting Fordham University School of Law professor Jim Cohen: "The short-term negative is that the U.S. attorney's office will react as if they have been poked in the eye").

28. *See* Indictment, *supra* note 1, at 9 (detailing the investigation federal officials conducted against Stewart).

29. *See* JAMES A. STRAZZELLA, CRIMINAL JUSTICE SECTION, AM. BAR ASS'N, THE FEDERALIZATION OF CRIMINAL LAW 2 (1998) (responding to concerns about the multitude of new federal crimes created by Congress); *see also* Geraldine Szott Moohr, *The Federal Interest in Criminal Law*, 47 SYRACUSE L. REV. 1127, 1130–37 (1997) (recounting critique of the expansion of federal criminal law); Ellen S. Podgor, *Jose Padilla and Martha Stewart: Who Should Be Charged with Criminal Conduct?*, 109 PENN ST. L. REV. 1059, 1060–61 (2005) (stating that the increase in federal crime legislation is due to the fact that crime reform is politically popular, not socially necessary).

30. *See* JUDICIAL CONFERENCE OF THE UNITED STATES, LONG RANGE PLAN FOR THE FEDERAL COURTS 25 (1995) (acceding to criminal laws that involve complex commercial or institutional enterprises).

authorities, an entire year and a half passed between the initial inquiry regarding Stewart's trade and her indictment.[31]

Third, during such a lengthy period, an investigation can set off harmful collateral consequences, such as those experienced by Stewart and her company. These consequences are not, strictly speaking, legal in nature. Rather, most are "extra legal"—they do not result from a legal determination, but from market and social forces that are stimulated by an investigation. In addition to the financial consequences illustrated by Stewart's case, a social stigma attaches to the subject of an investigation and brings suspicion of colleagues and friends as well as of the government, with consequent loss of respect and status. Thus, the stigma of conviction begins long before a finding of guilt. Such serious collateral consequences should, at least in theory, deter criminal behavior—especially among respectable middle-class business people who are presumed to care about what their neighbors think of them, their status in the broader community, and the effect an investigation could have on their careers and businesses. Although the stigma may be justified upon conviction, it is important to realize that the side-effects of a criminal investigation apply to the innocent as well as to the guilty, and it is often impossible to recover from them.

## III. THE INDICTMENT

The pertinent point here is that Stewart was indicted.[32] The decision to indict—or not—rests in the discretion of the federal prosecutor in charge of the case. Nominally, the grand jury investigating the case decides whether a criminal charge is warranted.[33] Because a prosecutor has great influence over the grand jury, in practice the decision to indict rests with the government, not its citizens.

Stewart's celebrity status and the media attention that was given to the investigation posed an initial dilemma that argued

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31. *See* Constance L. Hays, *Martha Stewart Indicted by U.S. on Obstruction*, N.Y. TIMES, June 5, 2003, at A1 (announcing Stewart's indictment in June 2003, and noting testimony given to the SEC beginning in February 2002).

32. For months, pundits had speculated that she would not be charged and reported the possibility of settlement just weeks before she was indicted. *See Martha Stewart Stock Up As Settlement Talks in Air*, HOUS. CHRON., May 14, 2003, at 3B (remarking that share prices of Stewart's company surged amid settlement speculation).

33. *See* U.S. CONST. amend. V ("No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury."). For a discussion of the charging function, see Geraldine Szott Moohr, *Prosecutorial Power in an Adversarial System: Lessons from Current White Collar Cases and the Inquisitorial Model*, 8 BUFF. CRIM. L. REV. 165, 203–04 (2004).

both for and against indictment.[34] Her notoriety made it very difficult for prosecutors not to charge Stewart and, at the same time, provided an incentive to charge her. If the government had not indicted Stewart, prosecutors would be seen as giving the rich and famous a break. Failing to indict would also indicate that the laws at issue were not worth enforcing. On the other hand, if she was charged, prosecutors would be seen as treating all offenders equally and all laws seriously.

Martha Stewart's celebrity status also provided the government with a bonus. When someone rich and famous is charged with a crime, the case attracts greater media attention than cases against ordinary defendants. Simply stated, media attention increases the deterrent effect of a case. As one official put it, when you indict a celebrity "'[t]he deterrent effect is immeasurable.'"[35] Indicting a celebrity sends a message to which more people pay attention because the message attaches to someone who is famous. What is the message that was sent in the Martha Stewart case?

## IV. THE CHARGES

The message sent by a criminal case depends on the offenses that are charged, a decision that is also in the discretion of the prosecutor. Stewart was charged with lying to investigators, obstructing justice, conspiracy, and one count of securities fraud. Thus, the messages here are that law-abiding citizens must be honest with investigators and absolutely truthful with shareholders. Rather stunningly, Stewart was not charged with insider trading. What do the charges—and the noncharge—tell us about white collar criminal law?

### *A. The Absence of an Insider Trading Charge*

Why was Stewart not indicted for the crime of insider trading? Although we can only speculate, we know that the U.S. Attorney in charge of the case characterized a possible insider trading charge as "unprecedented."[36] According to the original indictment, Stewart sold her ImClone stock after she was told

34. Commentators have debated whether Stewart was targeted for reasons unrelated to her conduct. *See, e.g.*, Kathleen F. Brickey, *Enron's Legacy*, 8 BUFF. CRIM. L. REV. 221, 255–60 (2004); Heminway, *supra* note 5, at 249–51; Harry Litman, *Pretextual Prosecution*, 92 GEO. L.J. 1135, 1164–65 & n.115 (2004).

35. Kurt Eichenwald, *Prosecutors Have Reasons for Stalking Celebrities*, N.Y. TIMES, June 5, 2003, at C4 (quoting Christopher Bebel, a former SEC attorney and federal prosecutor).

36. *See* Hays, *supra* note 31 (quoting U.S. Attorney James B. Comey).

that Waksal was trying to sell the ImClone stock in his Merrill Lynch account.[37] Thus, she had traded while in possession of nonpublic information that was arguably material to an ImClone investor. Why would indicting Stewart for insider trading be unprecedented?

The answer to this question rests on insider trading law, formulated by the Supreme Court in three major cases over a period of seventeen years.[38] First, since Stewart was not an insider who owed fiduciary duties to ImClone shareholders, she could not be charged under the classic theory of insider trading. Nor was Stewart a tippee of an insider who gave information to her in breach of a fiduciary duty. As employees of Merrill Lynch, neither the broker nor the assistant owed fiduciary duties to ImClone shareholders. Nor could Stewart be charged for misappropriating information and then trading. She had not betrayed any confidential relationship to the source of the information. It could be argued, however, that Faneuil had misappropriated information that "belonged" to Merrill Lynch, thus betraying a confidential relationship with, and obligations to, the firm.[39] The "unprecedented" issue was whether Stewart had committed insider trading when she traded on information that had been misappropriated by someone else. An insider trading charge on this theory implicates two related but distinct doctrines: tippee liability, a species of classic insider trading, and misappropriation liability.[40]

This noncharge tells us several other things about white collar criminal law. First, the noncharge illustrates the prosecutor's authority to decline to charge a defendant, even

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37. *See* Indictment, *supra* note 1, at 7–8.

38. *See* United States v. O'Hagan, 521 U.S. 642 (1997) (holding that a § 10(b) violation may occur under the misappropriation theory if a corporate outsider fails to disclose to his principal confidential information that is the property of the person to whom confidentiality runs); Dirks v. SEC, 463 U.S. 646, 655–66 (1983) (requiring a breach of insider's fiduciary duty before tippee inherits the duty to disclose or abstain, which requires a benefit to the insider either directly or indirectly); Chiarella v. United States, 445 U.S. 222, 225–29 (1980) (holding there can be no securities violation based on silence where plaintiff had no fiduciary duty to disclose).

39. *See* Carpenter v. United States, 484 U.S. 19, 24–28 (1987) (establishing that confidential workplace information is property of the employer for purposes of mail fraud). The Court later endorsed the theory in the securities context. *See O'Hagan*, 521 U.S. at 649–58.

40. For commentary on the insider trading puzzle presented by the Stewart facts, see Jeanne L. Schroeder, *Envy and Outsider Trading: The Case of Martha Stewart*, 26 CARDOZO L. REV. 2023, 2076–78 (2005) (arguing Bacanovic would not be a misappropriator under *O'Hagan* because he merely breached a contract with Merrill Lynch, since the information of Waksal's stock sale was not the property of Merrill Lynch).

when probable cause exists. A declination was not unusual in the circumstances here, when administrative and civil remedies were available that would achieve societal goals and compensate victims. In addition, the prosecutor had good reasons to avoid an expansive charge in this high-profile case. Significant issues regarding Stewart's culpability, or mens rea, may have led to a finding of not guilty.[41] Incorporating tippee liability into the misappropriation doctrine clearly expands misappropriation theory and, given the constitutional concerns about notice,[42] the prosecutor may have hesitated to establish a new cause of action in a criminal case.

The Stewart facts expose yet another gap in insider trading law that the SEC apparently believes ought to be closed, and the agency pursued the tippee/misappropriation theory in a civil case against Stewart.[43] The SEC's civil enforcement action against Stewart tells us something else about white collar criminal law—that civil regulatory actions often overlap with criminal prosecutions. Almost every regulatory regime has an omnibus criminal provision that states, as do the securities laws: "Any person who willfully violates any provision of this chapter . . . or any rule or regulation thereunder . . . shall upon conviction be fined . . . or imprisoned."[44] Environmental laws have criminal kickers,[45] so do antitrust offenses,[46] so do labor laws,[47] so do food and drug offenses.[48]

This overlap means that the same conduct may give rise to civil or criminal charges, or both. The only distinctions between civil and criminal liability in many statutes are the defendant's felonious intent, the mens rea element that bedevils law students, and the prosecution's burden to prove all elements of the crime beyond a reasonable doubt. In short, if the government

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41. For an interesting application of recent social science research to Stewart's state of mind when she traded, see generally Donald C. Langevoort, *Reflections on Scienter (and the Securities Fraud Case Against Martha Stewart that Never Happened)*, 10 LEWIS & CLARK L. REV. 1 (2006).

42. *See infra* notes 70–79 and accompanying text (discussing the vagueness doctrine).

43. Complaint, SEC v. Stewart, No. 03 CV 4070(NRB) (S.D.N.Y. June 4, 2003), *available at* http://www.sec.gov/litigation/complaints/comp18169.htm. Stewart recently settled the SEC suit, neither admitting nor denying any wrongdoing. *See supra* note 26. In addition to limitations on serving as an officer or director of any public company, she will pay $195,000. *See* Thomas, *supra* note 26.

44. 15 U.S.C. § 78ff (2000).

45. 16 U.S.C. § 1174.

46. 15 U.S.C. § 1.

47. 29 U.S.C. § 463.

48. 21 U.S.C. § 461.

believes it can prove that the defendant acted with criminal intent—as defined in the relevant statute—a civil violation can be treated as a crime.

The convergence of civil and criminal law has two troubling aspects. First, treating the same conduct as the basis for civil liability and for criminal punishment tends to blur the distinction between the standards for each cause of action and inexorably leads courts to expand the scope of the criminal provision.[49] The insider trading laws are a good example of this tendency. There is no definition of the culpability, or mens rea, element of "willful" in the criminal statute. In this vacuum, courts have applied standards that are strikingly similar to the civil scienter standard to criminal cases.[50] The merger of civil and criminal standards means that the only distinction between civil and criminal liability is the standard of proof in a criminal case, beyond a reasonable doubt. Finally, the use of administrative and criminal penalties raises constitutional due process issues and obscures the reasons for and confuses the standards for punishment.[51]

The second troubling aspect of the overlap is the possibility of parallel civil and criminal proceedings against defendants—or the threat of them. Commercial practitioners must be very careful not to implicate clients in the criminal matter when representing clients who may have violated civil provisions. Providing information to administrative authorities or civil parties may result in a forfeiture of attorney-client and work-product privileges in the criminal case. And the threat of criminal charges obviously strengthens the government's position in negotiations over the civil matter.

In the Stewart case, the civil and criminal cases are not strictly "parallel." The SEC took on insider trading and the Department of Justice focused on Stewart's other conduct.

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49. This tendency was first identified in the context of mail fraud. *See, e.g.*, John C. Coffee, Jr., *Does "Unlawful" Mean "Criminal"?: Reflections on the Disappearing Tort/Crime Distinction in American Law*, 71 B.U. L. REV. 193, 202–04 (1991) (explaining how the mail fraud statute has evolved to include breaches of fiduciary duty).

50. For a review of this tendency to treat the same conduct as the basis for civil liability and for criminal punishment, see Langevoort, *supra* note 41, at 5 (stating that the court in the Stewart case did not address the question of how to define the "willfulness" standard applied in criminal versus civil cases). For an explanation as to the source of this tendency, see Lawrence M. Solan, *Statutory Inflation and Institutional Choice*, 44 WM. & MARY L. REV. 2209, 2238–40 (2003) (suggesting that civil courts and the SEC construe securities laws broadly and that this standard influences criminal courts).

51. For the classic discussion of administrative penalties, see generally Kenneth Mann, *Punitive Civil Sanctions: The Middleground Between Criminal and Civil Law*, 101 YALE L.J. 1795 (1992).

Nevertheless, Stewart faced three proceedings that emanated from her infamous trade: civil suits by her shareholders, regulatory action by the SEC, and criminal action by the Justice Department. A three-front defense effort is very challenging. As noted, defending the civil charges can undermine a defense on the criminal charges. Yet the phenomenon of parallel or multiple proceedings is not unusual in white collar crimes.[52]

### *B. The Securities Fraud Charge*

The government passed on a criminal charge of insider trading. But it was not so cautious when it indicted Stewart for another form of securities fraud under the same statute.[53] The reasons for not indicting Stewart for insider trading seem to apply equally to this charge, and the decision to charge securities fraud illustrates the power of the prosecutor to decide what charges to file. This charge also tells us a great deal about white collar criminal law.

Stewart was charged with fraudulently misleading investors in Omnimedia—not ImClone investors, but shareholders of her company.[54] In June 2002, after news reports disclosed Stewart's sale and Waksal's arrest, Stewart made public statements aimed at her company's shareholders.[55] Among other things, she denied any wrongdoing and explained her reason for selling: the price of ImClone had fallen to $60 per share, a price that she and Bacanovic had decided would trigger selling her stock in the company.[56] Prosecutors charged that Stewart's statements had affirmatively misrepresented material facts in order to manipulate the price of her company's stock.[57] The government's implied theory was that she was motivated to do so because as the majority shareholder concerned about the company's share value, she acted to protect her own wealth.[58] According to the government, her deceptive statements fraudulently misled investors and affected their decisions to buy or sell shares of her company.[59]

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52. *See* Brickey, *supra* note 34, at 252 & tbl.3 (presenting summary indicating that 28 individuals or firms involved in Enron criminal actions are also the subject of parallel SEC proceedings).

53. Indictment, *supra* note 1, at 40–41.

54. *Id.* at 41.

55. *Id.* at 38–41.

56. *Id.* at 38–40.

57. *Id.* at 40–41.

58. *Id.* at 36–37.

59. *Id.* at 35, 40.

Commentators almost immediately identified several problems with this unusual—some would say novel—charge. Even former SEC officials registered surprise.[60] The reason for surprise was that her conduct fell outside the heartland of securities fraud and did not obviously constitute securities fraud.[61] Fraud requires more than deception; at a minimum, the deception must be material.[62] Stewart's statements were arguably not material because they referred to a personal transaction that did not concern business at Omnimedia.[63] In addition, the statements were part of a flurry of news reports, and investors could be presumed to know the information contained in the statements. Finally, securities law requires that deception is connected to the purchase or sale of a security. Here, the connection between Stewart's statements and an investor's decision to buy shares of Omnimedia were particularly attenuated.

In addition, the charge is contrary to principles that are basic to our system. It seemed to interfere with her right to defend herself. Because a basic tenet of American law is that a person is innocent until proven guilty, our intuition is that everyone has a right to say "I am innocent."[64] It is perverse to charge someone with a crime for exercising that right because the charge implicitly rejects the basic premise of innocence. The securities fraud charge also raised First Amendment concerns

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60. *See* Brooke A. Masters, *Securities Charge Could Be Biggest Threat to Stewart*, WASH. POST, June 19, 2003, at E2 (quoting David E. Marder, a former SEC enforcement lawyer, who stated he was not aware of any other case where the government alleged a manipulation of stock prices by claiming innocence).

61. *See, e.g.*, David Mills & Robert Weisberg, Op-Ed., *Flunking the Martha Test*, WALL ST. J., Jan. 16, 2004, at A10 (presenting the opinion of two Stanford Law School Professors that a statement of innocence about an offense unrelated to the firm does not defraud shareholders); Was Martha Stewart's Denial Material? The Problem with Count 9, ProfessorBainbridge.com, http://www.professorbainbridge.com (Dec. 4, 2003) (claiming Stewart's statement was not material, and thus the government's case implausible).

62. 17 C.F.R. 240.10b-5 (2006).

63. For a discussion of materiality in the Stewart case, see Joan MacLeod Heminway, *Material Misstatements?*, *in* MARTHA STEWART'S LEGAL TROUBLES (forthcoming 2006) (manuscript on file with the Houston Law Review).

64. *See* William Safire, Op-Ed., *Fight It, Martha*, N.Y. TIMES, June 12, 2003, at A35 (asserting one has a right to defend oneself).

One might argue that Stewart had a right to deny guilt, but no right to add false information. The key information she provided was apparently true, however. The jury found Stewart not guilty for stating that she had a prearranged decision to sell if the shares fell to $60. *See* United States v. Stewart, 323 F. Supp. 2d 606, 610 (S.D.N.Y. 2004), *aff'd*, 433 F.3d 273 (2d Cir. 2006). The statements for which she was found guilty related to details of meetings and communications with Bacanovic and Faneuil. *Id.* at 609.

relating to free speech. Her lawyers argued these and other points in a motion to dismiss,[65] which the trial court rejected.[66]

What does the securities charge tell us about white collar criminal laws? It tells us first that the federal criminal laws use broad, undefined terms that can be applied to a wide range of conduct. The securities fraud charge was based on the same statute that bars insider trading—a person may not willfully make material, untrue statements that would defraud investors.[67] But neither the statute nor the pertinent administrative rule defines key terms, such as "deceptive device," "willfully," and "material," or explains how tight a link is required between a deception and a transaction. Instead, Congress—purposefully or inadvertently—delegated the task of defining these terms to the courts.[68] As those of you who practice in this area know, judicial interpretations of these terms can vary circuit by circuit. Even then, appellate courts revisit precedents and reframe their definitions. Thus, this criminal law is indeterminate—it does not articulate a clear standard.

Over time, interaction between executive branch prosecutors and courts continues to expand the meanings of undefined terms, and the law becomes ever broader. The expansion process typically begins, as here, when the prosecution presses for a new application of the statute.[69] Accepting this theory of the case requires courts to interpret the statute so that it encompasses the new application. Courts, deferring to the authority of the executive branch to enforce the laws, often entertain the charge, giving the term the new meaning advocated by prosecutors. By rejecting Stewart's motion to dismiss, the trial judge accepted the government theory—a defensive statement about a personal

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65. *See* Memorandum of Law in Support of Martha Stewart's Omnibus Pre-Trial Motions, United States v. Stewart, 03-Cr.-717 (MGC) (S.D.N.Y. Oct. 6, 2003).

66. United States v. Stewart, 305 F. Supp. 2d 368 (S.D.N.Y. 2004).

67. 15 U.S.C. § 78j (2000); 15 U.S.C. § 77ff (2000); 17 C.F.R. § 240.10b-5 (2005).

68. Congressional reluctance to define statutory terms is not confined to securities laws. Other examples include mail and wire fraud and the RICO statute. For an analysis of the institutional forces that lead Congress to write ambiguous and broadly written statutes, see Daniel C. Richman, *Federal Criminal Law, Congressional Delegation, and Enforcement Discretion*, 46 UCLA L. REV. 757 (1999).

69. Chuck Ruff identified the role of federal prosecutors in interpreting criminal statutes almost 30 years ago. *See* Charles F.C. Ruff, *Federal Prosecution of Local Corruption: A Case Study in the Making of Law Enforcement Policy*, 65 GEO. L.J. 1171 (1977).

For a more recent treatment of the process of expanding federal criminal laws, see William J. Stuntz, *The Pathological Politics of Criminal Law*, 100 MICH. L. REV. 505, 507 (2001). For an application to mail and wire fraud, see Geraldine Szott Moohr, *Mail Fraud and the Intangible Rights Doctrine: Someone to Watch over Us*, 31 HARV. J. ON LEGIS. 153 (1994).

transaction can operate as a fraud on investors. Thus, a new application of the statute, a new theory of criminality, a new form of fraud, was established.

Laws like this may be so vague that they offend the Constitution. The Constitution requires that statutes provide notice to citizens and guidelines to prosecutors, judges, and juries about the conduct that has been prohibited. The constitutional standard for vagueness is whether citizens "of common intelligence must necessarily guess at its meaning and differ as to its application."[70] The standard is particularly pertinent in white collar crimes because not all unethical or immoral conduct is criminal. As the insider trading allegation against Stewart illustrates, the line between acting lawfully in one's self-interest is not clearly distinct from criminal conduct.

Stewart invoked the vagueness doctrine to argue that she had no notice that general statements regarding her innocence could violate the securities statute.[71] This seems like a reasonable position. An intelligent reading of the statute would not have disclosed that the conduct she was about to undertake was a crime, and even experts disagreed about the eventual charge. In Stewart's case, whether the government's expansive interpretation was indeed encompassed by the statute was not known until the judge refused to dismiss the charge. Had she been indicted for insider trading, she would have made the same arguments.

The Constitution, under the vagueness doctrine, also requires that the written law provide enforcement standards to guide the decisions of prosecutors, judges, and juries.[72] Prosecutors need to know when and what to charge, judges need to advise jurors about the law, and juries need to measure factually proven conduct against a legal standard. Providing such standards prevents arbitrary enforcement and leads to consistent, uniform application, properties now missing from white collar criminal law.

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70. Connally v. Gen. Constr. Co., 269 U.S. 385, 391 (1926). The classic article on the vagueness doctrine is Anthony G. Amsterdam, Note, *The Void-for-Vagueness Doctrine in the Supreme Court*, 109 U. PA. L. REV. 67 (1960).

71. *See* Memorandum of Law in Support of Martha Stewart's Omnibus Pre-Trial Motions, United States v. Stewart, 03 Cr. 717 (MGC) (S.D.N.Y. Oct. 6, 2003).

72. *See* Kolender v. Lawson, 461 U.S. 352, 357–58 (1983) (determining the legislature must provide guidelines for criminal statutes so that the executive and judicial branches cannot pursue their own predilections with regards to enforcement and conviction).

There is also a policy reason to avoid vague criminal laws. Vague laws may not effectively deter criminal conduct.[73] When the law is unclear, persons who are considering some action may not realize that they are in danger of violating criminal laws. In those circumstances, people do not stop to weigh the benefit of the conduct against the risk of being caught and punished. The point is particularly relevant in the white collar context where conduct is often based on ethical lapses, betrayals of trust, and deceptions that are not always crimes.

Finally, vague laws increase the discretion of prosecutors in several ways.[74] First, as the securities fraud charge illustrates, vague laws enhance the authority of prosecutors to choose what charges to bring.[75] Second, vague laws allow prosecutors to apply statutes to conduct that falls outside the harm that the law sought to prevent. Once approved by courts, new applications expand the scope of the substantive law to include more conduct and thus more defendants. Thus, prosecutors, members of the executive branch, with the cooperation of the judiciary, assume a legislative role. In an adversarial system such as ours, based on the rule of law, a democratically elected legislature is responsible for defining criminal conduct.[76] In the criminal realm, the justification for punishment emanates first from statute, rather than from the defendant's conduct or the enforcer's values. Vague laws also expand the authority of prosecutors to negotiate plea bargains and cooperation agreements, an authority—which we take up in a moment—that has disadvantages as well as benefits.

Despite the pernicious effects of vague criminal statutes, courts routinely reject vagueness challenges, even when Supreme Court justices have suggested that a law may be

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73. For further development of this point, see Geraldine Szott Moohr, *An Enron Lesson: The Modest Role of Criminal Law in Preventing Corporate Crime*, 55 FLA. L. REV. 937, 959–61 (2003) (discussing the rational choice model of deterrence).

74. U.S. District Judge Gerard Lynch has written extensively on prosecutorial authority. *See* Gerard E. Lynch, *Our Administrative System of Criminal Justice*, 66 FORDHAM L. REV. 2117, 2136 (1998) (discussing the relationship between vague statutes and prosecutorial discretion); *see also Panel Discussion: The Expanding Prosecutorial Role from Trial Counsel to Investigator and Administrator*, 26 FORDHAM URB. L.J. 679, 682–84 (1999) (describing the broad authority of prosecutors).

75. Indeed, Professors Richman and Stuntz have characterized federal criminal law as providing a "menu" of options to prosecutors. Daniel C. Richman & William J. Stuntz, *Al Capone's Revenge: An Essay on the Political Economy of Pretextual Prosecution*, 105 COLUM. L. REV. 583, 628–30 (2005).

76. For an illuminating discussion of the rule of law and the legality principle, see Paul H. Robinson, *Fair Notice and Fair Adjudication: Two Kinds of Legality*, 154 U. PA. L. REV. 335, 375–78, 395–98 (2005) (explaining the legislative definition of criminal conduct as one of six components of the legality principles).

unconstitutionally vague.[77] The rejections rest on doctrinal rules, established by courts, which limit applicability of the vagueness doctrine.[78] Federal courts should revisit and revise these doctrinal rules so statutes are more rigorously scrutinized.

Ironically, Stewart was ultimately acquitted of securities fraud. Relying on the mens rea element of the offense, the court held that the government had not produced enough evidence for the charge to go to the jury.[79] No reasonable juror could have found her guilty beyond a reasonable doubt without undue speculation that she had acted willfully. Nevertheless, a precedent has been established: protesting one's innocence may operate as a fraud.

### *C. The Cover-up Charges*

As we know, Stewart maintained that she had sold her ImClone stock because its price had fallen to her predetermined $60 limit. Based on these and other statements, Stewart was charged with making false statements to investigators, obstructing justice, and conspiring to commit those offenses.[80] Aptly referred to as "cover-up" crimes, these free-standing, independent offenses are not related to the target offense under investigation. As here, rather than relating directly to insider trading or securities fraud, cover-up crimes originate in the investigation, as defendants seek to avoid charges on the target offense. Cover-up crimes encompass a wide range of actions and include lies and other acts involving evidence of and witnesses to

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77. *See* H.J. Inc. v. Nw. Bell Tel. Co., 492 U.S. 229, 251–56 (1989) (Scalia, J., concurring) (criticizing majority opinion for not improving guidance regarding an element of RICO and suggesting the law is unconstitutionally vague).

78. *See, e.g.*, United States v. Rybicki, 287 F.3d 257, 263–64 (2d Cir. 2002), *aff'd en banc* 354 F.3d 124 (2d Cir. 2003) (detailing various means by which circuit courts have attempted to limit application of honest services fraud); *see also* United States v. Brown, No. 05-20319, 2006 WL 2130525, *6–9 (5th Cir. Aug. 1, 2006) (stating that honest services fraud does not apply when the firm intentionally aligned the interests of its employee with a corporate goal, the employee perceived his pursuit of that goal as mutually benefiting him and the firm, and the employee's conduct was consistent with that perception of mutual interest).

79. *See* United States v. Stewart, 305 F. Supp. 2d 368, 370 (S.D.N.Y. 2004), *aff'd*, 433 F.3d 273 (2d Cir. 2006). For commentary on the district court's opinion, see Joan MacLeod Heminway, *Martha Stewart Saved! Insider Violations of Rule 10b-5 for Misrepresented or Undisclosed Personal Facts*, 65 MD. L. REV. (forthcoming 2006) (analyzing Stewart's acquittal for the securities fraud charge).

80. *See* 18 U.S.C. § 1001 (2000) (prohibiting "knowingly and willfully" making a false statement to a federal official acting within the jurisdiction of the executive, legislative, or judicial branches); 18 U.S.C. § 1505 (prohibiting obstructing "the due and proper administration of the law" before an agency proceeding); 18 U.S.C. § 371 (prohibiting conspiring to commit an offense against the United States).

the crime under investigation.[81] A cover-up offense may be brought even when the target offense, such as insider trading or securities fraud, is not a crime or could not be proven. What do the cover-up charges against Stewart tell us about white collar criminal law?

First, cover-up crimes are another example of the breadth of federal statutes. Section 1001 prohibits making a false statement to virtually any government official.[82] Unlike a perjury charge, § 1001 does not require that the statement be made under oath or in formal circumstances.[83] Similarly, the obstruction statutes are also broadly written to capture a wide range of conduct. The omnibus clauses of §§ 1503 and 1505 authorize criminal punishment when a person "corruptly . . . influences, obstructs, or impedes, or endeavors to influence, obstruct, or impede" justice. [84] The mens rea element of obstruction, which requires the accused to have acted "corruptly," has no uniform meaning and has been interpreted broadly, which expands the scope of the statute.[85] Both Congress and the Court have dealt recently with the obstruction statutes: Congress enacted new obstruction

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81. For a discussion of the moral framework of cover-up offenses, see Stuart P. Green, *Uncovering the Cover-Up Crimes*, 42 AM. CRIM. L. REV. 9, 28–43 (2005). For an explanation of the efficacy of cover-up charges for prosecutors, see Richman & Stuntz, *supra* note 75, at 589–90 (noting that proving cover-ups is often easier than proving the underlying crime).

Some commentators see an increasing tendency to use cover-up charges. *See, e.g.*, Dale A. Oesterle, *Early Observations on the Prosecutions of the Business Scandals of 2002–03: On Sideshow Prosecutions, Spitzer's Clash with Donaldson over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation*, 1 OHIO ST. J. CRIM. L. 443, 449–51 (2004) (noting a new cultural acceptance of using sideshow or pretext charges).

82. 18 U.S.C. § 1001. For a critique of § 1001, see Justice Ginsburg's concurrence in *Brogan v. United States*, 522 U.S. 398, 408 (1998), in which she notes the extraordinary authority the statute gives the government.

83. 18 U.S.C. § 1001.

84. 18 U.S.C. § 1503 (2000) (applying to judicial matters); 18 U.S.C. § 1505 (2000) (applying to agency hearings). Similar language is found in the new obstruction provision. *See* 18 U.S.C. § 1512(c) (2000 & Supp. IV 2004).

85. For commentary on the various definitions of "corruptly," see Eric J. Tamashasky, *The Lewis Carroll Offense: The Ever-Changing Meaning of "Corruptly" Within the Federal Criminal Law*, 31 J. LEGIS. 129, 141–66 (2004). For a comprehensive treatment of federal and state obstruction statutes, see John F. Decker, *The Varying Parameters of Obstruction of Justice in American Criminal Law*, 65 LA. L. REV. 49 (2004).

provisions,[86] and the Supreme Court has issued two opinions that clarify the mens rea element.[87]

Secondly, and the point I want to emphasize here, the cover-up charges against Stewart illustrate the depth of the federal criminal code. The code reportedly contains at least 100 false statement statutes and over 325 fraud statutes.[88] This depth gives prosecutors the ability to pick and choose among various offenses and allows charges of more than one crime for the same conduct. In Stewart's case, she sought to conceal the circumstances of her sale of ImClone shares.[89] Although she made false and misleading statements, she engaged in, as it were, a single scheme to deceive investigators. That single scheme gave rise to three sets of charges: false statement, obstruction, and conspiracy.[90] Overlapping crimes like false statements and perjury—by their nature and almost automatically—also obstruct the due administration of justice. Thus her deceptive statements to federal investigators resulted in charges of separate crimes. These offenses also suggest a conspiracy when another person is involved. On the theory that Stewart and Bacanovic had agreed to violate the false statement and obstruction statutes, they were charged with conspiracy.[91]

The conspiracy statute adds an extra layer of depth. Co-conspirators are liable for the actions of their cohorts when that action furthers the conspiracy, even when a defendant was not present and did not act.[92] Thus, Stewart was also charged with

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86. *See* 18 U.S.C. § 1512(c) (2000 & Supp. IV 2004); 18 U.S.C. § 1519 (2000 & Supp. IV 2004); 18 U.S.C. § 1520 (2000 & Supp. IV 2004). For an evaluation of one new provision, see Daniel A. Shtob, Note, *Corruption of a Term: The Problematic Nature of 18 U.S.C. § 1512(c), the New Federal Obstruction of Justice Provision*, 57 VAND. L. REV. 1429 (2004).

87. *See* Arthur Andersen LLP v. United States, 125 S. Ct. 2129, 2131–32, 2136–37 (2005) (interpreting § 1512(b)(2)(B) to require that defendant was conscious of wrongdoing); United States v. Aguilar, 515 U.S. 593, 599–600 (1995) (interpreting § 1503 to require that a nexus exist between the conduct and the proceeding at issue); *see also* Julie R. O'Sullivan, *The Federal Criminal "Code" Is a Disgrace: Obstruction Statute as Case Study*, 96 Nw. U. L. Rev. 643, 690–708 (2006) (suggesting these cases "mudd[y the] already murky waters").

88. *See* United States v. Wells, 519 U.S. 482, 505–07 & nn. 8–10 (1997) (Stevens, J., dissenting) (noting the number of federal false statement statutes); Jeffrey Standen, *An Economic Perspective On Federal Criminal Law Reform*, 2 BUFF. CRIM. L. REV. 249, 289–90 (1998) (reporting his count of fraud offenses).

89. *See* Indictment, *supra* note 1, at 9.

90. *Id.* at 1, 25, 34.

91. *Id.* at 1, 20–21.

92. This co-conspirator liability rule was formulated in *Pinkerton v. United States*, which held that a co-conspirator may be convicted of offenses committed by a cohort in the conspiracy as long as those acts are in furtherance of the conspiracy and fall within the scope of the agreement and could reasonably be foreseen as a necessary or natural

and found guilty of her broker's independent perjury in testimony before the SEC.[93]

An additional aspect of the depth of federal criminal law is that a single lie can lead to multiple counts of each offense, a practice referred to as "piling-on."[94] Every time a lie is repeated during an investigation, a separate count of the crime may be charged. If a misrepresentation of the truth is repeated in two meetings, prosecutors can charge two counts of false statements and two counts of obstruction. If the statement is made a third time, prosecutors may add another count of each crime.

"Piling-on" does not necessarily aid in truth-finding during trial. Jurors who assume that "where there is smoke, there must be fire" are likely to convict or at best reach compromise verdicts, finding defendants guilty of some but not all of the charges. In addition, multiple counts are used to leverage plea agreements, as prosecutors "give up" some counts in return for the plea. Although the sentencing guidelines have mitigated the effect of multiple counts on prison terms,[95] the practice exposes the limited due process rights of defendants during the plea bargaining and trial stages of a criminal matter.

Despite such harmful effects, there is no obvious remedy. The double jeopardy clause,[96] which protects people from being tried twice for the same crime, only rarely bars multiple counts or charges of overlapping crimes. The Supreme Court has devised a restrictive test for double jeopardy claims that focuses on the elements of the statutes at issue.[97] In Stewart's case, the elements of false statement and obstruction differed from one another. The false statement charge requires that the defendant

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consequence of the agreement. Pinkerton v. United States, 328 U.S. 640, 645–47 (1946).

93. *See* Indictment, *supra* note 1, at 21–22; United States v. Stewart, 433 F.3d 273, 279, 287–89 (2d Cir. 2006).

94. For commentary that questions the use of multiple counts, see Michael L. Seigel & Christopher Slobogin, *Prosecuting Martha: Federal Prosecutorial Power and the Need for a Law of Counts*, 109 PENN ST. L. REV. 1107, 1125–28 (2005). In Stewart's case, prosecutors charged two false statement counts with eight misstatements in one count and three in the other. *Id.* at 1118. She could have faced eleven charges of making false statements. *Id.*

95. *See* U.S. SENTENCING GUIDELINES MANUAL § 3D1.1–.5 (2005) (authorizing grouping of charges according to certain characteristics, such as the amount of the victim's loss).

96. U.S. CONST. amend. V.

97. *See* Blockburger v. United States, 284 U.S. 299, 304 (1932) (finding no double jeopardy where provisions of a criminal statute require proof of a fact that another statute does not); *see also* United States v. Woodward, 469 U.S. 105, 108–10 (1985) (holding that charging defendant with false statements under 18 U.S.C. § 1001 and failing to report transportation of currency under 31 U.S.C. § 1058 did not violate the double jeopardy clause).

made a false statement; obstruction does not. Obstruction under § 1505 requires that the defendant, at a minimum, endeavored to influence, obstruct or impede the proper administration of the law; false statement does not.[98] Thus, Stewart was not being tried twice for the same crime.

Be that as it may, the use of cover-up charges betrays a win-at-any-cost attitude on the part of the government that can devalue the criminal justice system in the eyes of the public.[99] A trial or plea on cover-up charges obscures the substantive crime that is under investigation. Because the defendant is not charged with the substantive charges that gave rise to the investigation, the government need never explain why the underlying conduct was a crime. The public is not well-served by this. We are left, as in Stewart's case, wondering whether willfully trading on a tip of misappropriated information is a crime.

Committing obstruction, false statement, and perjury are serious matters. Without them, investigative efforts necessary to uncover and prosecute white collar crimes would be significantly hampered. Lying, or shredding documents, or withholding information make it more difficult for the government to enforce our laws; cover-up offenses serve a bona fide function, to deter actors from misleading investigators. Such actions harm the criminal justice system and thus society generally.

Having said that, the threats to due process rights of defendants and the long-term harm to the criminal justice system are also serious matters. Over time, using such charges may offend the community's sense of fairness and lessen respect for the entire criminal enforcement system. These long term effects raise the question of whether there is some middle ground—some constraint on using overlapping charges and multiple counts—that would preserve the integrity of government investigations without impugning the rights of defendants and devaluing the criminal justice system.[100]

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98. 18 U.S.C. §§ 1001, 1505 (2000).

99. As an example, consider this statement from the heartland. "In the Martha Stewart case, doesn't it look like the prosecutors are angry because they can't prove insider trading, and are being vindictive in pursuing these other charges?" Howard Chapman, *Both Martha and Justice Have Suffered, and Now It Will Get Even Worse*, FORT WAYNE NEWS-SENTINEL, Mar. 12, 2004, http://www.discovery.org/scripts/viewdb/index.php?command=view&program=misc&id=1926. The passage is cited at length in Green, *supra* note 81, at 12 n.16.

100. Professors Seigel and Slobogin suggest that courts merge all counts that deal with the same conduct or transgression before trial and plea bargaining discussions. *See* Seigel & Slobogin, *supra* note 94, at 1128–30. Professor Ellen Podgor suggests that the obstruction statute should be interpreted to require the government to prove that the statement was material. Ellen S. Podgor, *Arthur Anderson, LLP and Martha Stewart:*

## V. THE TRIAL

In some senses, Stewart's trial was typical of federal criminal trials, and has much to say about the enforcement of white collar crimes. In another sense, Stewart's trial was not at all typical: she went to trial.

### *A. Typical Aspects of Stewart's Trial*

Because of the conspiracy charges, Stewart was tried jointly with her broker, Peter Bacanovic.[101] What does a conspiracy trial tell us about white collar criminal law? First, the strategy of a joint trial shows that the trial strategies applied in federal drug cases have migrated to white collar cases. Following the shocking conduct at some of the nation's most well-known business firms, the executive branch put money and personnel into punishing the "bad apples" who disgraced themselves and American businesses.[102] Stewart's case shows that prosecutors are now as committed to winning white collar cases as they are to winning cases in the war on drugs.[103]

Stewart's trial also reminds us that a joint trial on conspiracy charges offers the government several procedural advantages that disadvantage defendants.[104] Rules regarding joinder, venue, and statutes of limitations give the government an edge before the trial even begins.[105] The advantages continue throughout the trial. For instance, the rules regarding exclusion of hearsay evidence do not apply to the testimony of co-conspirators.[106] Moreover, it is very difficult for a jury to view defendants as individual actors when they are linked together in the courtroom, and testimony as to one defendant can "stick to" a

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*Should Materiality Be an Element of Obstruction of Justice?*, 44 WASHBURN L.J. 583, 598 (2005).

101. United States v. Stewart, 305 F. Supp. 2d 368, 371 (S.D.N.Y. 2004), *aff'd*, 433 F.3d 273 (2d Cir. 2006).

102. *See* Moohr, *supra* note 73, at 966–68 (discussing limitations of the "bad apple" approach).

103. The commitment and subsequent trial tactics may be a consequence of the politically beneficial practice of declaring "war" on certain kinds of crime. For a classic treatment of the habit of the executive branch to target certain kinds of crime during an administration, see Norman Abrams, *Assessing the Federal Government's "War" on White-Collar Crime*, 53 TEMP. L.Q. 984, 984–87 (1980).

104. *See* Krulewitch v. United States, 336 U.S. 440, 445–55 (1949) (Jackson, J., concurring) (identifying and discussing consequences of a conspiracy charge). In Justice Jackson's words, conspiracy is an "elastic, sprawling and pervasive offense" that is "so vague that it almost defies definition." *Id.* at 445–46.

105. Paul Marcus, *The Use of Criminal Statutes to Regulate Financial Markets in the United States*, 46 AM. J. COMP. L. SUPPLEMENT 589, 591 (1998).

106. *See Krulewitch*, 336 U.S. at 443.

codefendant. Conspiracy doctrine also allows defendants to be found guilty of the acts of co-conspirators.[107] In Stewart's case, she was found guilty of the perjury committed by Bacanovic.

In trying Stewart, the government relied on a cooperating witness—Faneuil, her broker's assistant—who testified for the government. A person who "cooperates" has pleaded guilty to a (usually) lesser charge and agreed, in return, to help the government in its investigation and subsequent trials of other individuals.[108] In this case, Faneuil pleaded guilty to a misdemeanor charge of withholding information from authorities.[109] After testifying against Stewart and Bacanovic, he was sentenced to a $2000 fine.[110]

The use of a cooperating witness raises a troubling issue, even though the person provides crucial evidence for the government.[111] Consider that Faneuil is almost as liable as Stewart or Bacanovic on the trading issue and the subsequent cover-up. By his own testimony, he was aware of the insider trading issue at the time of the trade and yet he agreed to and facilitated the sale.[112] He supported Stewart and Bacanovic's story for six months.[113] The cynical trade of small fish for big fish that privileges guilty parties is not lost on the public. For those who believe in the moral basis of criminal law, allowing an offender to escape just punishment is far from satisfying. Those who justify punishment because it deters others may question the efficacy of the tactic if it leads to widespread cynicism about criminal enforcement.[114]

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107. *See id.* at 451 (discussing the *Pinkerton* doctrine); *supra* note 92.

108. For a review of the use of cooperating witnesses in several recent cases, see Kathleen F. Brickey, *From Enron to WorldCom and Beyond: Life and Crime After Sarbanes-Oxley*, 81 WASH. U. L.Q. 357, 370–75 (2003). Perhaps the most extreme use of cooperating witnesses occurred in the trial of Ken Lay and Jeffrey Skilling. *See* Moohr, *supra* note 33, at 183–86.

109. *See* Brooke A. Masters, *Witness in Stewart Trial Is Spared Prison Time*, WASH. POST, July 24, 2004, at E1.

110. *Id.*

111. For commentary on the use of cooperating witnesses, see Ellen S. Podgor, *White-Collar Cooperators: The Government in Employer-Employee Relationships*, 23 CARDOZO L. REV. 795 (2002); Daniel C. Richman, *Cooperating Defendants: The Costs and Benefits of Purchasing Information from Scoundrels*, 8 FED. SENT'G REP. 292 (1996).

112. *See* United States v. Stewart, 323 F. Supp. 2d 606, 611 (S.D.N.Y. 2004), *aff'd*, 433 F.3d 273 (2d Cir. 2006).

113. *Id.* at 611–12.

114. For persuasive arguments on this point, see the work of Paul Robinson and John Darley. *E.g.*, Paul H. Robinson & John M. Darley, *The Utility of Desert*, 91 NW. U. L. REV. 453, 487, 496–97 (1997) (describing public perception of the criminal justice system and arguing for a morally credible system).

### *B. The Atypical Aspect of Stewart's Trial*

By one index Stewart's case is unique: she did not plead guilty, but actually went to trial.[115] In the federal criminal justice system, around 95% of defendants plead guilty.[116] In the white collar cases that have been disposed of between March 2002 and December 2005, 73% of defendants, 140 out of 191, pleaded guilty.[117]

Several factors converge to explain why so many white collar defendants plead. Some defendants are contrite and willing to accept punishment. Others are willing to forego trial in hopes of a lesser or certain sentence. Like Faneuil, some defendants can trade information about others for the probability of a lesser sentence.

A third reason that white collar defendants plead guilty relates to a characteristic of white collar crimes, the presence of a business firm. Most white collar cases involve some kind of organizational entity, usually the defendant's workplace. Under federal case law, firms may be charged with the conduct of employee/agents who act within the scope of their authority and on behalf of the firm.[118] The best example is the case that we here in Houston witnessed, the Arthur Andersen case. The accounting firm, held responsible for David Duncan's crime of obstructing justice, did not survive indictment.[119] The message was loud and clear, and firms are now anxious to avoid indictment and the collateral consequences that flow from an official investigation.

The double threat encourages firms not only to plead guilty but also to cooperate with the government in prosecuting their

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115. *See Stewart*, 323 F. Supp. 2d at 606.

116. GEORGE FISHER, PLEA BARGAINING'S TRIUMPH 223 (2003).

117. *See* Kathleen F. Brickey, *Major Corporate Fraud Prosecutions, March 2002–December 2005* (unpublished manuscript, on file with the Houston Law Review). Forty-four were tried and seven cases were dismissed or received deferred prosecution. *Id.*

Although it appears that white collar defendants are less likely to plead than other defendants, the proportion of pleas to trials in current white collar cases is likely to increase. Many defendants await trial and still have the opportunity to plead guilty. For an interesting argument that only cases that lie outside the norm reach trial, see William J. Stuntz, *Self-Defeating Crimes*, 86 VA. L. REV. 1871 (2000).

118. *See* N.Y. Cent. & Hudson River R.R. Co. v. United States, 212 U.S. 481, 493–94 (1909) (establishing agency theory that attributes criminal conduct to the corporation). For commentary on the propriety of indicting corporations, see Brent Fisse, *Reconstructing Corporate Criminal Law: Deterrence, Retribution, Fault, and Sanctions*, 56 S. CAL. L. REV. 1141 (1983). For a more recent evaluation of the common law basis of the practice, see Elizabeth K. Ainslie, *Indicting Corporations Revisited: Lessons of the Arthur Andersen Prosecution*, 43 AM. CRIM. L. REV. 107, 107–25 (2006).

119. For commentary on the Arthur Andersen case, see Kathleen F. Brickey, *Andersen's Fall From Grace*, 81 WASH. U. L.Q. 917 (2003), and Kurt Eichenwald, *Miscues, Missteps and the Fall of Andersen*, N.Y. TIMES, May 8, 2002 at C1.

employees. Firms may abandon employees who had served the firm by firing them, by refusing to pay their attorney's fees, and by providing the government with suggestive and incriminating evidence.[120] In the Stewart case, Merrill Lynch suspended Bacanovic and Faneuil and eventually dismissed them,[121] just as Arthur Andersen had fired Duncan.[122] Recently KPMG, an accounting firm under threat of indictment for allegedly fraudulently marketing tax shelters, dismissed seventeen of its professional staff and withdrew payment of their legal fees.[123] These actions enhanced the firm's chances of avoiding indictment by securing a deferred prosecution agreement.[124] Current Department of Justice policies, which include forfeiture of privileges,[125] leave firms little choice but to cooperate with the government in convicting their former employees.[126] Former employees are caught between their former firms, who may release incriminating documents and refuse to pay legal fees, and prosecutors, who threaten them with prison terms. Many opt for a plea agreement.

What does plea bargaining tell us about the enforcement of white collar crime? Is it a good thing? It cannot be a good thing if individuals who plead are not guilty of a crime. Yet a rational defendant may accept a plea to a lesser charge—and a certain prison term—rather than risk trial on a more serious charge,

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120. For a critical perspective on government tactics, see JOHN HASNAS, TRAPPED: WHEN ACTING ETHICALLY IS AGAINST THE LAW, 61–64 (2006), and John Hasnas, Op-Ed., *Rule of Law: Department of Coercion*, WALL ST. J., Mar. 11–12, 2006, at A9.

121. Both men were suspended on June 21, 2002. Faneuil was fired when he pleaded guilty on October 2, 2002. Bacanovic was fired the same day because he "refused to cooperate with federal investigators." *See* Constance L. Hays, *Broker's Assistant Pleads Guilty in Stewart Case*, N.Y. TIMES, Oct. 3, 2002 at C1.

122. Brickey, *supra* note 119, at 930 & n.66.

123. *See* Lynnley Browning, *Bond Is Set at $25 Million in KPMG Tax Shelter Case*, N.Y. TIMES, Mar. 9, 2006, at C7. Pressuring firms to withdraw payment of attorney fees has met significant resistance. *See* United States v. Stein, 435 F. Supp. 2d 330, 382 (S.D.N.Y. 2006) (holding that government pressure on firms to withdraw payment of attorney's fees violates defendants' constitutional rights).

124. *See* Browning, *supra* note 123; Kathryn Kennealy & Kenneth M. Breen, *The KPMG Deferred Prosecution: Warning Flags for Defense Rights*, CHAMPION, Nov. 2005, at 44. For commentary on deferred prosecutions of corporations, see Benjamin M. Greenblum, Note, *What Happens to a Prosecution Deferred? Judicial Oversight of Corporate Deferred Prosecution Agreements*, 105 COLUM. L. REV. 1863 (2005); Stephanie Martz, *Trends in Deferred Prosecution Agreements*, CHAMPION, Nov. 2005, at 45; *Crime Without Conviction: The Rise of Deferred and Non Prosecution Agreements*, CORP. CRIME REP., Dec. 28, 2005 (on file with the Houston Law Review).

125. *See* Memorandum from Deputy Attorney Gen. Larry D. Thompson to U.S. Attorneys (Jan. 20, 2003), *available at* http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm (last visited Sept. 21, 2006).

126. *See* Posting of Prof. Larry Ribstein to Ideoblog, http://busmovie.typepad.com/ideoblog (Apr. 21, 2006, 20:27 EST).

even if he or she is innocent.[127] Under current sentencing policy, prosecutors may ask the judge to depart from a guideline sentence when defendants "substantially assist" the government.[128] Neither the judge nor the defense attorney may initiate this departure from the Guideline Sentence. A defendant who declines to plead guilty and cooperate thus risks alienating a person who can influence the length of the prison term.

Plea bargains of those who are in fact guilty may be an expeditious and efficient way of settling the matter, saving taxpayers the expense of trial.[129] But of course there are other considerations. One is that fewer cases go to trial. In giving up public adjudication, we also incur a loss, although it is not immediately obvious. Trials create a public record and educate the public, and I would suggest they are critical to deterrence. At trial, details of the conduct are fully revealed in a convincing way that explains what happened and why that conduct was a crime. Everyone understands after a trial what conduct constituted the crime and that it was wrong, whereas information contained only in an indictment and plea bargain is not generally known and does not have this effect.

Trials also affirm shared social values and reinforce law-abiding behavior of people who do not "skate too close to the wind" in order to benefit themselves. This is the kind of behavior that we want to encourage. We do not want people to go around thinking, "I'm a chump because I obeyed the law." We want business executives to see that people who fail to obey the law are tried and punished. A trial accomplishes this in a visceral way that is more effective than a plea bargain, even one that includes headlines and perp walks. As a result of Stewart's trial and conviction, citizens understand that they are obliged not to lie to federal investigators.

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127. *See* Robert E. Scott & William J. Stuntz, *Plea Bargaining as Contract*, 101 YALE L.J. 1909, 1911 (1992).

128. *See* U.S. SENTENCING GUIDELINES MANUAL § 5K1.1 (2005). For commentary on this practice, see Cynthia K.Y. Lee, *From Gatekeeper to Concierge: Reigning in the Federal Prosecutor's Expanding Power over Substantial Assistance Departures*, 50 RUTGERS L. REV. 199 (1997).

129. For a discussion of plea bargaining that questions whether plea bargains generally reflect the applicable law and a predicted outcome of trial, see Stephanos Bibas, *Plea Bargaining Outside the Shadow of Trial*, 117 HARV. L. REV. 2463 (2004), and William J. Stuntz, *Plea Bargaining and Criminal Law's Disappearing Shadow*, 117 HARV. L. REV. 2548 (2004).

## VI. THE SENTENCE

Federal prison sentences depend on the prison term provided in the statute and on the Federal Sentencing Guidelines. The Guidelines were devised, in part, to constrain judicial discretion in the interests of providing uniform and certain sentences.[130] Overall, punishment of federal white collar offenses became harsher and more certain after 1989, when guideline sentencing was adopted.[131]

Stewart was sentenced as a first offender convicted of a nonviolent crime that did not cause financial harm. She received a five-month prison term, a five-month term of house arrest, two years of probation, and a $30,000 fine.[132] The ten-month term of incarceration was split between prison and home confinement, and Stewart spent five months in a federal prison.[133] Bacanovic received the same term of incarceration, and a $4000 fine.[134] As previously mentioned, Faneuil avoided a prison sentence.[135] What do the sentences in this case tell us about white collar criminal law?

First, federal prison terms for similar conduct are often inconsistent. Faneuil, at a minimum, conspired in the trade and the subsequent cover-up. Yet he was indicted on a lesser charge and, on the prosecutor's recommendation,[136] sentenced to a fine, avoiding both a prison term and probation.[137] A more stark

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130. U.S. SENTENCING GUIDELINES MANUAL ch. 1, pt. A(3) (2002) (explaining that the Guidelines were formulated to provide greater honesty, uniformity, and proportionality in federal sentencing). For an introduction to the rationale that supported their adoption, see Stephen Breyer, *The Federal Sentencing Guidelines and the Key Compromises upon Which They Rest*, 17 HOFSTRA L. REV. 1 (1988).

A recent Supreme Court decision made the Guidelines discretionary, rather than mandatory. *See* United States v. Booker, 125 S. Ct. 738 (2005) (holding that mandatory Guidelines violated the Sixth Amendment right to a jury trial). The effects of this decision are, as yet, unclear. For commentary on the effects of *Booker*, see the symposium articles in *Symposium, The* Booker *Project: The Future of Federal Sentencing*, 43 HOUS. L. REV. 269 (2006).

131. *See* Moohr, *supra* note 73, at 941–43 (explaining the effect of the Guidelines on white collar sentences).

132. United States v. Stewart, 433 F.3d 273, 280 (2d Cir. 2006). For a review of sentencing and other post-trial issues, see Kathleen F. Brickey, *Mostly Martha*, 44 WASHBURN L.J. 517, 542–44 (2005).

133. *Stewart*, 433 F.3d at 280.

134. *Id.*

135. *See supra* text accompanying notes 108–110.

136. Prosecutors requested the judge to give Faneuil "extra leniency" because of the substantial assistance he gave the government before and during Stewart and Bacanovic's trial. *See* U.S. SENTENCING GUIDELINES MANUAL § 5K1.1 (2005); *see also* Masters, *supra* note 109.

137. Masters, *supra* note 109.

example of inconsistent sentencing comes from the Jamie Olis case. After trial and conviction for accounting fraud, Olis was sentenced to 24 years in prison.[138] In contrast, Olis's boss, who had approved the accounting strategy Olis used, received a five-year sentence after testifying for the government.[139] One reason some defendants serve less time in prison than others for the same offense is that prosecutors can evade and influence guideline sentences. They may choose the offenses that are charged, negotiate plea and cooperation agreements, and exercise their authority under the Guidelines.[140]

Inconsistent sentences are not a good thing. First, they are contrary to the purpose of modern sentencing reform, which is to ensure uniform sentences. They also undermine a major reason for subjecting individuals to criminal punishment in the first place. Inconsistent sentences impair the deterrent function of criminal law because people are more likely to desist from crime when sentences are more certain.[141] Finally, inconsistent sentences raise troubling fairness issues and erode citizens' respect for the criminal justice system.

I would like to make an additional point about sentencing that is not suggested by the Stewart sentences. Responding to public outrage over corporate misconduct, Congress recently enacted the Sarbanes-Oxley Act.[142] Among other provisions, the Act increases prison terms for several white collar crimes by as much as 400%; in frauds involving pensions, penalties were increased 1000%, from one to ten years.[143] Congress apparently believed that long prison terms would deter potential offenders.[144] Evidence suggests, however, that long prison terms do not

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138. Laura Goldberg, *Ex-Dynegy Exec Gets 24 Years*, HOUS. CHRON., Mar. 26, 2004, at A1. The sentence was based on financial loss of Dynegy investors, who prosecutors claimed had lost $100 million. The Fifth Circuit, following *Booker*, directed the court to resentence Olis. Upon resentencing, Olis received a six year sentence, based on an intended tax loss to the government of $79 million. *See* United States v. Olis, No. H-03-217-01, 2006 WL 2716048 (S.D. Tex. 2006).

139. *Olis*, 429 F.3d at 542.

140. This list does not exhaust the ways that prosecutors can influence sentences. *See* Nancy J. King, *Judicial Oversight of Negotiated Sentences in a World of Bargained Punishment*, 58 STAN. L. REV. 293, 294–95 (2005) (describing prosecutors' authority to decide whether special sentencing statutes should be used).

141. *See, e.g.*, Gary S. Becker, *Crime and Punishment: An Economic Approach*, 76 J. POL. ECON. 169, 176–79 (1968).

142. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745.

143. For a discussion of the penalty provisions of the Sarbanes-Oxley Act, see Moohr, *supra* note 73, at 954–56.

144. A more realistic reason is that lawmakers apply the "'What do I need to get re-elected?' principle." *See* Joshua Dressler, *The Wisdom and Morality of Present-Day Criminal Sentencing*, 38 AKRON L. REV. 853, 855 (2005).

increase deterrence—even for white collar criminals who presumably plan and consider the risk of criminal behavior.[145] Armed with this knowledge, it would be wise to consider shorter sentences. The money saved by shorter sentences could be used to strengthen another source of deterrence: the likelihood that white collar offenders will be apprehended.

## VII. WHAT THE STEWART CASE HAS TOLD US

Our progression through the Martha Stewart case has revealed quite a bit about the specific white collar crimes at issue in her case. As the review indicates, insider trading law seems to be in a constant state of development. Securities fraud is in a similar flux, with little agreement as to the criminal mens rea element of the offense. The crimes of false statement, obstruction, and conspiracy, although essential to enforcement, are overbroad and duplicative. Reliance on these crimes ignores the merits of charging the target offense, appears overly aggressive, and may offend the community's sense of fairness.

Our progression has also revealed more general issues that apply equally to all federal crimes. Some issues concern enforcement practices: the consequences of the investigatory process, the role of celebrity, parallel and multiple proceedings, use of cooperating witnesses, and plea bargains. The case also illustrates significant issues that pertain to the substance of federal criminal laws: the vagueness of criminal statutes, the breadth and depth of the federal criminal code, merger of civil and criminal standards, and sentencing policies. Throughout the criminal justice process—from lawmaking to sentencing—the enormous discretion given federal prosecutors stands out.

This Essay raises significant issues that threaten the integrity and efficacy of the law and the federal criminal justice system. I leave you with this thought: If Martha Stewart, a well-educated, wealthy person, aided by experienced defense counsel, was caught in the web of statutes and enforcement powers that were outlined here, we should be very concerned about the plight of the more typical offender.

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