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Rethinking Vicarious Criminal Liability: Corporate Culpability for White-Collar Crime

by John Hasnas

Much attention has been focused on U.S. Department of Justice (DOJ) policies governing the prosecution of white-collar crime. A federal district court recently ruled that DOJ violated several defendants' constitutional right to counsel when it pressured their employer, accounting powerhouse KPMG, to cut off their attorney fees if they did not cooperate with the government; the court suppressed statements two of the defendants made to the government under this threat. The House of Representatives held a hearing in March, and the Senate plans to hold a hearing in September, on DOJ's policy of requiring corporations to waive their attorney-client and work product privileges in order for DOJ to deem them as having cooperated sufficiently to avoid indictment. Even DOJ's policy of charging individuals with obstruction of justice for lying to or concealing information from corporate counsel during internal investigations has come under scrutiny. These hardball policies, which tilt the balance between corporate defendants and prosecutors, are the result of the federal standard that assigns criminal responsibility to corporations regardless of corporate culpability.

Corporations and Criminal Punishment

Why should corporations be subject to criminal punishment? The response often given is that corporations are legal persons. Once they are invested with the right to utilize the legal system as a unitary entity, the argument goes, corporations should be treated the same as all other legal persons. This includes being subject to criminal punishment.

But this argument is a non sequitur because being considered a person under the law does not necessarily make one subject to criminal responsibility. Infants, the incompetent, and the insane are legal persons but are not subject to criminal responsibility for their actions. Criminal law *punishes* those who engage in wrongdoing. Hence, criminal sanctions apply only to those who can be deserving of punishment. That corporations are legal persons does not answer whether corporations can deserve punishment.

A good argument can be made that it is unjust to subject corporations to criminal punishment. Corporations cannot be imprisoned; hence, they are punished only with fines. Any criminal fine imposed is ultimately paid by a corporation's shareholders. The defining characteristic of the modern publicly traded corporation, however, is the separation of ownership and control. In the publicly traded corporations that are often the targets of federal prosecutors, the shareholders who are the owners of the corporation do not control the actions of corporate employees. Thus, imposing criminal punishment on a corporation for the actions of its employees, rather than exclusively on the employees themselves, is actually punishing shareholders who are innocent of wrongdoing.

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For purposes of discussion, however, assume that punishing corporations criminally does not inappropriately punish the innocent. The question still remains: Under what circumstances should corporations be subject to punishment? The obvious answer is when they deserve it—that is, when they are actually responsible for wrongdoing. But what does it mean to say a corporation is responsible for wrongdoing? Theorists have supplied various answers to this question. One is that a corporation is responsible for any wrongdoing that is corporate policy—i.e., any wrongdoing that has been authorized by the corporation’s internal decision-making procedures.² Another would hold a corporation liable for any wrongdoing committed by its employees when the corporation maintains a corporate culture that encourages such wrongdoing.³ But whatever one’s theory of corporate responsibility, it is clear that a corporation is not responsible for the wrongdoing of its employees when it has done everything in its power to prevent such wrongdoing.

The Current Law’s Loose Standard

Although this idea is obvious and is consistent with reasonable expectations about the proper use and application of the criminal law, it is irrelevant under the current federal standard of corporate criminal responsibility. Under federal law, a corporation is criminally responsible for the actions of any of its employees taken within the scope of their employment for the benefit of the corporation. It makes no difference whether the employees’ conduct violates corporate policy or contravenes explicit instructions not to engage in the conduct.⁴ A corporation is vicariously liable for the conduct of its employees even if it has the most pristine corporate culture and its executives and managers have done everything humanly possible to prevent their employees from violating the law. In other

words, a corporation is strictly liable for the crimes of its employees.

Under this standard of corporate criminal responsibility, there is nothing a corporation can do to ensure that it is not guilty of a criminal offense. Corporate managers know that no matter how good their firm’s internal controls, they cannot guarantee that there will be no intentional or—in today’s highly complex, highly regulated business environment—inadvertent violations of law by its employees. Corporate managers also know that because the corporation’s good behavior is no defense, the corporation can be convicted whenever such violations occur. The financial health and frequently the continued existence of the corporation can therefore rest entirely on whether the corporation is indicted.

Under the present standard of corporate criminal responsibility, whenever one of its employees comes under suspicion of criminal wrongdoing, the corporation faces the stark choice of either betting the company’s future that the employee will be exonerated or doing whatever DOJ demands to avoid corporate indictment. In these circumstances, it is hardly surprising that most corporations waive their attorney–client privilege, cut off payment of their employees’ legal fees, refuse to enter into joint defense agreements with or otherwise help employees prepare their defense, and fire any employee who refuses to cooperate fully with the government.

A Fairer Standard

This demonstrates that reforming DOJ policy is not the best way to prevent prosecutorial abuses. A more effective approach would be to allow corporations that have a good corporate character—corporations that do nothing to facilitate employee wrongdoing and make good-faith efforts to obey the law—to assert this as a defense when charged

1. U.S. v. Stein, ___ F. Supp. 2d ___, No. S1 05 Crim. O888 LAK, 2006 WL 1735260 (S.D.N.Y. June 26, 2006); U.S. v. Stein ___ F. Supp. 2d ___, No. S1 05 Crim. O888 LAK, 2006 WL 2060430 (S.D.N.Y. July 25, 2006).
2. See, e.g., Peter French, *The Corporation as a Moral Person*, 16 AM. PHIL. Q. 207 (1979).
3. See, e.g., Pamela Bucy, *Corporate Ethos: A Standard for Imposing Corporate Criminal Liability*, 75 MINN. L. REV. 1095, 1103-05 (1991).
4. See U.S. v. Hilton Hotels Corp., 467 F.2d 1000, 1007 (9th Cir. 1972).

with a crime. This means abandoning the current standard of corporate criminal liability in favor of one that requires some corporate involvement in employees' wrongdoing.

Precisely what the reformed legal standard should be for imposing criminal liability upon a corporation is open to discussion. A highly restrictive standard might require the prosecution to demonstrate some positive step taken by corporate policymakers to facilitate the employees' criminal conduct. A less restrictive standard might require only that upper management be willfully blind or perhaps merely negligent with regard to employee misconduct. An even less restrictive standard might presume corporate involvement in employee criminal activity but allow corporations to raise their good-faith efforts to discourage employee wrongdoing as an affirmative defense. Even the least restrictive standard could be enough to break DOJ's stranglehold on corporations.

The ability to introduce its good corporate character as a defense would place a corporation's fate back in its own hands. It would no longer have to regard an indictment as equivalent to a conviction and could take affirmative steps to ensure compliance with the law. Under this standard, a corporation's decision to cooperate with a federal criminal investigation could be based on the corporation's best judgment as to whether its employees engaged in criminal activity, rather than on fear of an indict-

ment against which, if its employees turn out to be guilty, there is no defense. This change in the standard of corporate criminal responsibility would not interfere with the government's ability to prosecute individual employees who violate the law. It simply would remove the club that DOJ now uses to beat corporations into "volunteering" as deputy law enforcement agencies.

Conclusion

To be sure, reforms that prevent DOJ from coercing corporations into waiving their attorney-client privilege or firing and refusing to aid employees who are under suspicion would be welcome. But a better approach would be to treat the underlying condition that gives rise to these symptoms. Changing the legal standard for corporate criminal responsibility to require wrongful corporate action for corporate conviction would restore the balance of power between the prosecution and the corporate defendant to one more appropriate to our adversarial system of justice and thus remove the source of DOJ's coercive power. No less important, such a reform would renew business leaders' incentives to ensure legal compliance and good corporate citizenship.

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