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Corporate Crime Legislation: A Political Economy Analysis

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CORPORATE CRIME LEGISLATION: A POLITICAL ECONOMY ANALYSIS

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ABSTRACT

Corporate crime has once again become an important issue on the U.S. legislative agenda, leading Congress and the various regulatory bodies to tighten the law and enhance honesty and completeness in disclosure. However, the continued and rather explosive growth of corporate crime legislation leaves one with a rather strange puzzle: how can such a state of the world arise? After all, corporations and business interests are considered some of the most, if not *the* most, powerful and effective lobbyists in the country. Yet, we witness the continued expansion of legislation that criminalizes their behavior (one estimate suggests over 300,000 federal regulatory offenses that can be prosecuted criminally). How could this have happened? This paper sets out to explain this puzzle.

Overall, my analysis suggests that most corporate crime legislation arises when there is a large public outcry over a series of corporate scandals during or around a downturn in the economy. In such situations, Congress must respond. Corporate crime legislation may be the preferred response for some corporate interests because it satisfies public outcry while imposing relatively low costs on those interests, thereby avoiding legislative and judicial responses that are more harmful to their interests and sometimes deflecting criminal liability away from managers and executives and onto corporations. This explains not only the impressive growth of corporate crime legislation but also leads to some surprising normative conclusions. In particular, it suggests that if one starts with the view that there is *under-deterrence* of corporate wrongdoing, then one would probably prefer to *reduce* corporate criminal liability and focus more on corporate civil and managerial liability.

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I. INTRODUCTION

Corporate crime is back in the news.[1] The last two years have seen some of the most spectacular revelations of corporate wrongdoing in U.S. history, leading to a significant drain on the economy[2] and to the enactment of various measures, including the Sarbanes-Oxley Act of 2002.[3] This new law adds to the already sprawling area of corporate criminal liability.[4] Indeed, even before Sarbanes-Oxley, the estimated number of federal criminal offenses for which a corporation could be convicted was well over 300,000, covering a wide range of areas such as environmental, securities, banking, and antitrust violations.[5] With such tremendous breadth and so many new measures being debated and enacted—sometimes rather quickly—it seems to be an appropriate time to think more broadly about how we might regulate behavior in the corporate sphere to prevent or deter the kinds of wrongdoing we have witnessed in the recent past.

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1. *See, e.g.*, Daniel Eisenberg, *More Reform and Less Hot Air*, TIME, July 22, 2002, at 24–25; Lee Walczak & Richard S. Dunham, *Corporate Crime: Why It's Not Sticking to Republicans*, BUS. WK., Oct. 7, 2002, at 57 (referring to a "corporate crime wave" starting with the Enron collapse).

2. Between August 2001 and August 2002, the NASDAQ lost 29% of its value, dropping from approximately $2,688,686,785 to $1,921,970,173 (both numbers in thousands). The three markets combined (NASDAQ, NYSE, and Amex) lost 16% of their value between August 2001 and August 2002. *See* Comparing Three Markets: NASDAQ, NYSE & Amex, *available at* http://marketdata.nasdaq.com/asp/Sec1Summary.asp (last visited Apr. 1, 2004).

3. *See generally* Public Accounting Reform and Investor Protection Act of 2002, Pub. L. 107–204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C. and 18 U.S.C.). The Sentencing Guidelines were recently amended to reflect the directives in Sarbanes-Oxley. *See* UNITED STATES SENTENCING COMMISSION REPORT TO THE CONGRESS: INCREASED PENALTIES UNDER THE SARBANES-OXLEY ACT OF 2002, (Jan. 2003), *available at* http://www.ussc.gov/r_congress/S-Oreport.pdf [hereinafter SENTENCING COMMISSION REPORT]. *See generally* U.S. SENTENCING GUIDELINES § 8 (1995) [hereinafter SENTENCING GUIDELINES].

4. *See* John C. Coffee, Jr., *Does "Unlawful" Mean "Criminal"?: Reflections on the Disappearing Tort/Crime Distinction in American Law*, 71 B.U. L. REV. 193, 216–19 (1991) [hereinafter Coffee, *Reflections*]. For a flavor of the breadth of corporate criminal liability, see RICHARD S. GRUNER, CORPORATE CRIME AND SENTENCING § 9.7, at 553–84 (1994) [hereinafter GRUNER] (discussing fines in the antitrust, environmental, and food and drug arenas), § 9.5.5, at 551–52 (discussing fines for money laundering and related offenses).

5. *See* Coffee, *Reflections, supra* note 4, at 216 & n.94 (noting that "there are over 300,000 federal regulations that may be enforced criminally," as estimated by Stanley Arkin, "a well known practitioner in the field of white collar crime, at the George Mason Conference in October 1990" and citing to Leary, *The Commission's New Option That Favors Judicial Discretion in Corporate Sentencing*, 3 FED. SENTENCING REP. 142, 144 n.10 (1990)).

Indeed, legal scholarship has examined many aspects of the imposition of criminal liability on corporate entities;[6] however, there remains a largely unanswered fundamental question: how is there so much corporate crime legislation given that it targets groups (corporate interests) that should be effective at lobbying against criminalization of their behavior?[7] This seems puzzling because we would expect that well-organized and well-funded groups (such as corporations) should obtain a large measure of what they want through legislation. Yet, in the context of corporate crime legislation the corporations seem to be losing the battle.[8] What might explain this outcome?

Overall, my analysis suggests that most of the important players, *including many corporations and management*, have reasons to support

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6. *See, e.g.*, Jennifer Arlen & Reinier Kraakman, *Controlling Corporate Misconduct: An Analysis of Corporate Liability Regimes*, 72 N.Y.U. L. REV. 687 (1997) (discussing corporate liability regimes); John C. Coffee, Jr., *"No Soul to Damn, No Body to Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH. L. REV. 386 (1981); Brent Fisse, *Reconstructing Corporate Criminal Law: Deterrence, Retribution, Fault, and Sanctions*, 56 S. CAL. L. REV. 1141 (1983) (arguing that retribution and deterrence are two primary goals of corporate criminal law); Lawrence Friedman, *In Defense of Corporate Criminal Liability*, 23 HARV. J.L. & PUB. POL'Y 833, 834 (2000) (stating that "even in the corporate context, moral condemnation remains a valid aim of the criminal law"); Vikramaditya S. Khanna, *Should the Behavior of Top Management Matter*, 91 GEO. L.J. 1215 (2003) [hereinafter *Top Management*] (arguing that the current setting of corporate sanctions relying on the involvement of top management in wrongdoing needs refinement); V.S. Khanna, *Corporate Criminal Liability: What Purpose Does it Serve?*, 109 HARV. L. REV. 1477 (1996) [hereinafter Khanna, *Corporate Criminal Liability*] (discussing corporate criminal liability compared to other liability strategies and concluding that corporate criminal liability is rarely desirable); V.S. Khanna, *Is the Notion of Corporate Fault a Faulty Notion?: The Case of Corporate Mens Rea*, 79 B.U. L. REV. 355 (1999) [hereinafter Khanna, *Corporate Fault*] (discussing the incentive effects of corporate fault standards); William S. Laufer, *Corporate Liability, Risk Shifting, and the Paradox of Compliance*, 52 VAND. L. REV. 1343 (1999) [hereinafter Laufer]; Joseph Vining, *Corporate Crime and the Religious Sensibility*, 5 PUNISHMENT & SOC'Y 313 (2003).

7. Few papers address the political dynamics of corporate crime legislation in much depth. *See* Jeffrey S. Parker, *Rules Without . . . : Some Critical Reflections on the Federal Corporate Sentencing Guidelines*, 71 WASH. U. L.Q. 397 (1993) [hereinafter Parker].

8. For a discussion of lobbying and rent-seeking, see generally TOWARDS A THEORY OF A RENT-SEEKING SOCIETY (James M. Buchanan, Robert D. Tollison & Gordon Tullock eds., 1980). There are a number of papers that examine regulation from the perspective of political economy. For a sampling, see Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q. J. ECON. 371 (1983) [hereinafter Becker]; Laura N. Beny, *The Political Economy of Insider Trading Legislation and Enforcement: International Evidence*, Discussion Paper No. 348, John M. Olin Center for Law, Economics & Business, Harvard Law School 2002 [hereinafter Beny], *available at* http://www.law.harvard.edu/programs/olin_center; Sam Peltzman, *Toward a More General Theory of Regulation*, 19 J.L. & ECON. 211 (1976) [hereinafter Peltzman]; Mark J. Roe, *Backlash*, 98 COLUM. L. REV. 217 *passim* (1998) [hereinafter *Backlash*]; Mark J. Roe, *Political Preconditions to Separating Ownership from Corporate Control*, 53 STAN. L. REV. 539 (2000) [hereinafter *Political Preconditions*]. *See also* Keith N. Hylton & Vikramaditya S. Khanna, *Toward an Economic Theory of Criminal Procedure*, B.U. Sch. L. Working Paper No. 01-02, 7 (2002), *available at* http://www.bu.edu/law/faculty/papers/pdf_files/HyltonKhanna033001.pdf [hereinafter Hylton & Khanna].

some corporate crime legislation. This is because it helps to avoid or mitigate legislative and judicial alternatives—such as new forms of corporate civil liability and managerial criminal liability—that would be even more costly to corporate interests. Most corporate crime legislation arises at times when there is a large public outcry over a series of corporate scandals during or around a downturn in the economy. In such a situation, Congress must respond. Corporate crime legislation may be the preferred response for some corporate interests because it satisfies the public outcry while imposing relatively low costs on those interests, thereby avoiding legislative and judicial responses that are more harmful to their interests and sometimes deflecting criminal liability away from managers and executives and onto corporations. In this respect corporate crime legislation is a substitute for these other responses that are less favored by certain corporate interests. I call this the substitution theory of corporate crime legislation. Moreover, my analysis suggests some surprising normative conclusions. In particular, it suggests that if one starts with the view that there is *under-deterrence* of corporate wrongdoing, then one would probably prefer to *reduce* corporate criminal liability and focus more on corporate civil and managerial liability. This raises serious questions about our current regulation in this area.

Part II begins by examining the primary legal doctrine used to hold corporations liable for the acts of their agents and the impressive breadth of corporate crime legislation. I then examine the political dynamics that might explain the vast amount of corporate crime legislation. Parts III and IV focus on the incentives of corporate interests and detail the substitution theses. Part V examines the incentives of the other players (e.g., legislators, prosecutors, judges, victims, and the general public), while Part VI considers the normative implications from my analysis. Part VII explores alternative political explanations for the growth of corporate crime legislation and argues that they do not alter the primary argument in this Article. Part VIII concludes.

II. CORPORATE CRIMINAL LIABILITY: AN INTRODUCTION

At the federal level and in many states the primary method of holding corporations liable (civilly or criminally) for the behavior of their agents is respondeat superior.[9] This requires that the agent be acting "within the

9. *See* RESTATEMENT (THIRD) OF AGENCY § 2.04 (Proposed Official Draft, 2000); Khanna, *Corporate Fault*, *supra* note 6, at 369–70 (citing GRUNER, *supra* note 4, § 3.4.2, at 198–203, § 4.1–.2, at 263–84).

scope of employment" and with some intent to benefit the corporation.[10] Respondeat superior is quite broad and will impose liability on the corporation regardless of whether the involved agent was an executive or a line employee.[11]

The breadth of respondeat superior liability is reflected in the vast amount of corporate behavior that is subject to criminal penalties. Corporations and their agents can be held criminally liable for violations of the environmental laws,[12] securities laws,[13] banking laws,[14] antitrust laws,[15] anti-bribery laws,[16] and a host of other laws.[17] Indeed, some

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In states that follow the Model Penal Code (MPC) instead of respondent superior, corporate responsibility for mens rea offenses usually requires the involvement of a high-level corporate official, not simply any agent. *See* MODEL PENAL CODE § 2.07(1)(c) (1985); Laufer, *supra* note 6, at 1384–85 (discussing "substantial authority" under the Model Penal Code); Anthony Ragozino, *Replacing the Collective Knowledge Doctrine with a Better Theory for Establishing Corporate Mens Rea: The Duty Stratification Approach*, 24 SW. U. L. REV. 423, 449 (1995). The MPC approach is in the minority in the U.S. and is not followed at the federal level and as such I will not discuss it in any greater depth at this time. Similarly, in some overseas jurisdictions corporate criminal liability can only be imposed if the "alter ego" or some group (or person) of considerable importance in the corporate structure was involved in the wrongdoing. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1490–91. It is noteworthy that few countries have corporate criminal liability and those that do have a much more restrained version of it compared to the U.S. *See id.* at 1488–91.

10. *See* Khanna, *Corporate Fault*, *supra* note 6, at 370 (citing *Developments in the Law—Corporate Crime: Regulating Corporate Behavior Through Criminal Sanctions*, 92 HARV. L. REV. 1227, 1247 (1979)); Lewis A. Kornhauser, *An Economic Analysis of the Choice Between Enterprise and Personal Liability for Accidents*, 70 CAL. L. REV. 1345, 1349 (1982).

11. *See Developments in the Law—Corporate Crime: Regulating Corporate Behavior Through Criminal Sanctions*, 92 HARV. L. REV. 1227, 1247 (1979) [hereinafter *Developments*]. Note that respondeat superior liability is in addition to any personal liability that may attach to the agent. *See* RESTATEMENT (SECOND) OF AGENCY Ch. 11 To. 3 Gen. Matls. (1958 App.) Appendix Court Citations (respondeat superior does not defeat agent liability); GRUNER, *supra* note 4, § 3.4.2, at 199–200); Khanna, *Corporate Fault*, *supra* note 6, at 370 (citing KATHLEEN F. BRICKEY, CORPORATE CRIMINAL LIABILITY, § 401, at 130 (2d ed., 1992) [hereinafter BRICKEY].

12. *See, e.g.*, Clean Air Act, 42 U.S.C. §§ 7401–7671 (2000); Federal Water Pollution Control Act, 33 U.S.C. §§ 1251–1387 (2000); Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), 42 U.S.C. §§ 9601–9675 (2000).

13. *See, e.g.*, Securities Act of 1933, 15 U.S.C. § 77a (2000); Securities Act of 1934, 15 U.S.C. §§ 78a–78k (2000); Investment Company Act of 1940, 15 U.S.C. §§ 80a–180a–64 (2000); Public Accounting Reform and Investor Protection (Sarbanes-Oxley) Act of 2002, Pub. L. No. 107–204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C.A and 18 U.S.C.A.).

14. *See* Financial Institutions Reform Recovery and Enforcement Act, 12 U.S.C. § 1818(u) (1988 & Supp. V 1993); Right to Financial Privacy Act of 1978, 12 U.S.C. §§ 3401–3422 (1988 & Supp. V 1993); Federal Deposit Insurance Corporation Improvement Act, 12 U.S.C. § 1831o(k) (1988 & Supp. V 1993).

15. *See* The Sherman Act, 15 U.S.C. § 1 (2000); The Clayton Act, 15 U.S.C. § 17 (2000); The Hart-Scott-Rodino Act, 15 U.S.C. § 18a (2000).

16. *See* Foreign Corrupt Practices Act of 1977, 15 U.S.C. §§ 78m(b), 78m(d)(1), 78m(g)–(h), 78dd–2, 78ff (1994); Bribery of Public Officials, 18 U.S.C.A. § 201 (West 2004).

17. *See, e.g.*, Currency Transaction Reporting Act, 31 U.S.C. § 5313 (1994); 18 U.S.C. § 371 (1994) (conspiracy against the United States); 18 U.S.C. § 4 (1994) (fining whoever knows of the

estimates suggest that even prior to recent events there were over 300,000 federal offenses that could be prosecuted criminally against corporations.[18]

The magnitude of criminal liability for corporate behavior raises many interesting questions, but the one that will occupy this paper is a political one. How is it that there is so much corporate crime legislation given that it targets groups (corporate interests) that should be quite good at lobbying against criminalization of their behavior?

Before delving into this question, a few matters are worth clarifying. First, my discussion is not meant to suggest that corporate interests are a unified interest group. There is a rich and deep public choice literature arguing that regulation is often the result of lobbying battles between different business interests so that some business interests are benefited by regulation and others are harmed (e.g., the creation of regulatory barriers to entry deterring new entry or making it more costly).[19] Such arguments provide strong explanations for regulations more generally, but my interest is in examining corporate crime legislation. Thus, I discuss incentives with respect to corporate crime legislation. I focus on the incentives of groups that would normally oppose regulation (I refer to them as "corporate interests" for expositional ease) and argue that these groups may often *prefer* corporate crime legislation over increases in corporate civil liability for reasons identified in Parts III and IV of this Article.[20] I return to examine some of the issues raised by the battles between corporate interest

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commission of a felony and conceals this information or does not report it to a judge or some other civil or criminal authority in a prompt fashion).

18. *See supra* note 5.

19. This is a vast literature. For a flavor see generally Becker, *supra* note 8; David D. Haddock & Jonathan R. Macey, *Regulation on Demand: A Private Interest Model, With an Application to Insider Trading Regulation*, 30 J.L. & ECON. 311 (1987); Kyle D. Logue, *If Taxpayers Can't Be Fooled, Maybe Congress Can: A Public Choice Perspective on the Tax Transition Debate*, 67 U. CHI. L. REV. 1507 (2000); Michael T. Maloney & Robert E. McCormick, *A Positive Theory of Environmental Quality Regulation*, 25 J. L. & ECON. 99 (1982); Peltzman, *supra* note 8; Richard L. Revesz, *Federalism and Environmental Regulation: A Public Choice Analysis*, 115 HARV. L. REV. 553 (2001) [hereinafter Revesz]; Carlos D. Ramirez & Christian Eigen-Zucchi, *Why Did the Clayton Act Pass? An Analysis of the Interest Group Hypothesis*, Draft 2003 (on file with author); George J. Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3 (1971) [hereinafter Stigler].

20. The corporate interest groups who oppose regulation may vary depending on the regulation at issue, specifically who does it hurt most. My reference to corporate interest groups means those corporate interest groups, in a particular context, that would oppose regulation generally (rather than corporate crime legislation specifically). Correlatively, the groups that normally favor increases in regulation may prefer increases in corporate civil liability, rather than corporate crime legislation. However, these groups may find it difficult to lobby vociferously against criminal liability when they also lobby in favor of increases in civil liability.

groups in Part VII and conclude that they do not alter my primary conclusions.[21]

Second, the focus of this Article is corporate crime legislation. Most of the criminal liability that corporations face in the U.S. stems from acts of Congress. However, the initial development of corporate criminal liability, driven predominantly by case law, was motivated by different factors than the later, largely legislative, growth of corporate criminal liability.[22] The early case law dates from the 1600s in England and involved instances of public harms (e.g., public nuisances) that municipalities had a duty to prevent or clean up.[23] For such harms, private enforcement was unlikely because few people would have the incentive or the information to pursue the case.[24] Thus, public enforcement was needed, and at the time the primary form of it was criminal liability.[25] In addition, one also needed liability against the municipality (i.e., corporations) to maintain deterrence because individuals responsible for the public nuisance were either difficult to identify or judgment-proof.[26] Corporate criminal liability then provided the only available method for combining public enforcement and corporate liability and thus served a useful enforcement function.[27] Indeed, for the first 200–250 years of its existence, corporate criminal liability grew mainly to fill such gaps and was largely contained to only a few areas.[28]

However, by the early 1900s public civil enforcement was a realistic alternative to public criminal enforcement, and by the 1960s public civil

21. I should note that the primary focus of this Article is not whether corporate crime legislation is in the public interest (i.e., normatively desirable). Nonetheless, my analysis does have normative implications, which I discuss in Part VI. My discussion also does not delve into theories behind the administrative process underlying these laws and whether, and when, it may tend towards the public interest. For excellent discussions of this and related matters, see Steven P. Croley, *Theories of Regulation: Incorporating the Administrative Process*, 98 COLUM. L. REV. 1 (1998); Steven P. Croley, *Public Interested Regulation*, 28 FLA. ST. U. L. REV. 7 (2000).

22. *See* L.H. LEIGH, THE CRIMINAL LIABILITY OF CORPORATIONS IN ENGLISH LAW 16–18 (1969) [hereinafter LEIGH]; BRICKEY, *supra* note 11, at 130.

23. *See* LEIGH, *supra* note 22, at 16–18; BRICKEY, supra note 11, at 130.

24. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1486–86 n.45 (referring to BRICKEY, *supra* note 11, at 421–22).

25. *See* Graham Hughes, *Administrative Subpoenas and the Grand Jury: Converging Streams of Criminal and Civil Compulsory Process*, 47 VAND. L. REV. 573, 587 & n.37 (1994) [hereinafter Hughes] (stating that it was only in the late 1800s that agencies developed civil enforcement and information gathering powers).

26. *See* James R. Elkins, *Corporations and the Criminal Law: An Uneasy Alliance*, 65 KY. L.J. 73, 82–84 (1976) [hereinafter Elkins] (noting identifiability concerns); Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1480–86.

27. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1486 nn.53 & 54.

28. *See* BRICKEY, *supra* note 22, § 2.04–2.09, at 70–86; Elkins, *supra* note 26, at 93–96; Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1480–84.

enforcement had the same (and sometimes greater) information gathering powers as public criminal enforcement.[29] Somewhat ironically, most of the growth of corporate crime legislation occurred when public civil enforcement was a realistic alternative and when corporate criminal liability's enforcement rationale was small or non-existent.[30] It is this later more dramatic growth that I examine in this Article as opposed to the initial development of corporate criminal liability.

A third matter is that there is little special legislation singling out corporations for criminal penalties.[31] Rather, criminal legislation is generally enacted to apply to "persons" engaged in certain activities, and then "person" is defined to include natural persons (i.e., humans) and corporate persons.[32] Might this affect the lobbying activities of corporations? It is doubtful that this would make much difference. If corporations find corporate criminal liability costly, then they will lobby against it regardless of how it applies to them.[33] Corporations may then lobby (i) against criminalization of the behavior for any "person," (ii) for provisions that make it harder to attach criminal liability to corporations, or (iii) for some kind of "carve–out" that makes it more difficult to hold corporations criminally liable.[34] Given that the general public is unlikely to pay close attention to the exact wording of the statute (due to collective action concerns) such strategies may be successful.[35] Thus, just because there is little specific legislation imposing criminal penalties on

29. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1520–31.

30. *See id.* at 1487–88.

31. *Cf.* GRUNER, *supra* note 4, at § 3.3, at 179–95.

32. *See* HERBERT L. PACKER, THE LIMITS OF THE CRIMINAL SANCTION 360–61 (1968) [hereinafter PACKER]; John T. Byam, Comment, *The Economic Inefficiency of Corporate Criminal Liability*, 73 J. CRIM. L. & CRIMINOLOGY 582, 584–85 (1982) [hereinafter Byam]. This suggests that corporate criminal liability is something of an "after-thought" or an "add-on". *See* PACKER, *supra*, at 360–61; Byam, *supra*, at 585.

33. Corporations may also lobby against enforcement of corporate crime legislation or attempt to cut off budgetary funding for it (see infra Part III.B & C). *Cf.* WILLIAM N. ESKRIDGE & PHILIP P. FRICKEY, CASES AND MATERIALS ON LEGISLATION: STATUTES AND THE CREATION OF PUBLIC POLICY 37–94 (1998); Daniel C. Richman, *Federal Criminal Law, Congressional Delegation, and Enforcement Discretion*, 46 UCLA LAW REV. 757, 789–810 (1999) [hereinafter *Delegation*]. Indeed, one reason corporations may favor corporate criminal liability (or public enforcement) over civil liability (or private enforcement) is because lobbying may occur with respect to enforcement budgets largely out of sight of the general public. *But see* Jeffrey Toobin, *The Man Chasing Enron: Why America's C.E.O.s Hate Bill Lerach*, THE NEW YORKER, Sept. 9, 2002, at 94 [hereinafter Toobin].

34. Safe harbors that are common in the securities regulation field are an example of achieving a carve-out. Note that I am not necessarily suggesting that the safe harbors in the securities field are examples of corporate lobbying to obtain carve-outs as opposed to simple well-intentioned and thought-out moves by the SEC. Rather, I am suggesting that the use of something like a "safe harbor" could provide a method of achieving a carve-out.

35. *See infra* Part V.A.

corporations does not mean that corporations cannot lobby against corporate criminal liability, find "carve-outs" for themselves, or otherwise mitigate its effects if they so desire. The real questions are why are there not more "carve-outs" and why is there so much potential criminal liability for corporations. As I argue in the parts to follow, corporate criminal liability may not be the worst thing for corporations.[36]

III. THE POLITICAL PUZZLE OF CORPORATE CRIME LEGISLATION AND THE SUBSTITUTION THESIS

To analyze the political dynamics of corporate crime legislation it is important to recognize that the politics of criminal law (street or white collar) are a story of institutional politics—that is, the politics of the institutions and their players—in the criminal context.[37] It is then important to set out the likely incentives of the important players such as Congress, management, corporations, prosecutors, judges, the general public, and victims of crime.[38]

To begin the analysis it is necessary to obtain a sense of how most corporate crime legislation comes to be enacted. The normal pattern of

36. Also one final note about how corporate criminal liability comes to be imposed on corporations at the federal level. Only the U.S. Department of Justice (DOJ) can initiate criminal proceedings against corporations at the federal level. The DOJ can initiate cases on its own motion, but in practice most cases come to the attention of the DOJ through referrals for criminal prosecution from other government agencies engaged in various aspects of law enforcement (e.g., the SEC, EPA) or through private parties (e.g., qui tam suits under the False Claims Act of 1986, victims in antitrust suits). Thus, the pattern of corporate crime enforcement is determined in measure by the activities of the DOJ, various other government bodies, and private entities. One might imagine that this would complicate the analysis of political incentives a great deal because we have so many players. Although clearly the various participants may have different interests and motivations, that does not change the fact that no prosecution can be initiated unless the DOJ initiates it. The other enforcement agencies and private players clearly may influence how and when the DOJ or the state prosecutors become aware of cases, but—given the somewhat overlapping nature of public civil and private civil enforcement—one does not expect that too many cases that have some political support for going criminal will not be brought to the attention of the DOJ. *See generally* JAMES EISENSTEIN, COUNSEL FOR THE UNITED STATES (1978); Robert L. Rabin, *Agency Criminal Referrals in the Federal System: An Empirical Study of Prosecutorial Discretion*, 24 STAN. L. REV. 1036 (1972).

37. *See generally* William J. Stuntz, *The Pathological Politics of Criminal Law*, 100 MICH. L. REV. 505 *passim* (2001) [hereinafter Stuntz].

38. *Cf. id.* I have not listed some other potential players such as federal investigative agencies (FBI, SEC, EPA), the police, defense attorneys and perhaps others. This is largely for analytical simplicity. For a discussion of how some of these players may interact, see generally Daniel Richman, *Prosecutors and Their Agents, Agents and Their Prosecutors*, 103 COLUM. L. REV. 749 (2003) [hereinafter *Agents*]. One suspects that the federal civil agencies would probably not oppose expansion of criminal liability for corporations because it does not impinge on their ability to bring civil suits. Further, the possibility of being able to refer a case for criminal prosecution might be a nice bargaining chip for a federal agency to possess when dealing with corporations and especially managers.

corporate crime legislation is that it comes on the heels of a large public outcry for greater regulation following the revelation of a number of events of corporate wrongdoing usually during or around a weak economy. This was the case for the federal securities laws, the Foreign Corrupt Practices Act, and other legislation surrounding Watergate, insider trading legislation in the mid-1980s, and the recent Sarbanes-Oxley Act.[39] Against this backdrop of increased calls for regulation, Congress must act as a political matter, and the issue is what it will do.[40] However, Congress has many options for regulating corporate behavior: it could enhance corporate civil liability, enhance corporate criminal liability, enhance liability for other parties (e.g., managers, accountants, and so forth), increase direct regulation generally, or rely on some combination of these options. Which option Congress chooses depends to some extent on the lobbying efforts of corporate interests and other interested parties.

I begin with a discussion of the incentives of corporations and executives and then move on to consider the incentives of other parties. For purposes of clarity, I examine two sets of congressional options, although the analysis would be applicable to other options too. First, I compare potential increases in corporate civil liability with corporate crime legislation. Second, in Part IV, I examine the impact of corporate crime legislation on the incidence of managerial criminal liability—specifically, that the presence of corporate criminal liability may lead to deflection of criminal liability away from managers.

In comparing increases in corporate civil liability with corporate crime legislation it is important to define what these phrases mean. Increases in

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39. There are many examples of this. *See* BRICKEY, *supra* note 11, § 1.02, at 5–6 (discussing legislation surrounding Watergate era); JAMES D. COX ET AL., SECURITIES REGULATION: CASES AND MATERIALS 1–31 (3d ed. 2001) (discussing the securities laws) [hereinafter COX]; JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET 1–100 (1982) (providing a detailed account of the history and politics surrounding the federal securities laws); Raymond Paternoster & Sally Simpson, *Sanction Threats and Appeals to Morality: Testing a Rational Choice Model of Corporate Crime*, 30 LAW & SOC'Y REV. 549, 550–51 (1996) (discussing growth of legislation around Watergate era); Revesz, *supra* note 19, at 583–626 (discussing the environmental context); Mark J. Roe, *A Political Theory of American Corporate Finance*, 91 COLUM. L. REV. 10, 17–18 (1991) (discussing the Glass-Stegal Act as a response to the Great Depression); *Backlash*, *supra* note 8, at 234–38 (noting that hostile takeovers and harsh bankruptcy policy increases the probability of severe political reaction). Finally, the Enron-style scandals have led to the passage of Sarbanes-Oxley in 2002 in another economic downturn. *See infra* notes 78–81 and accompanying text.

40. Congress may have to act in the sense that when these series of corporate scandals arise together the collective action problem faced by the general public and dispersed victims may be overcome. If Congress remains silent in the face of this activated group they are likely to face considerable difficulty in the next election and may also, in some countries, endanger longer-run stability. *See Backlash*, *supra* note 8; Larry Reynolds, *Washington Gets Tough on White-Collar Crime*, 79 MGMT. REV., Dec. 1990, at 27 [hereinafter Reynolds].

corporate civil liability refer to instances when Congress expands corporate civil liability by either increasing the kinds of activities that are actionable or by increasing the penalties that corporations may suffer for engaging in certain behavior, or both. For example, Congress could make acts X, Y, and Z all new civil wrongs. Next, corporate crime legislation refers to when Congress expands corporate civil liability somewhat, but not to the extent of the large increases in the first option, and also criminalizes these new wrongs. For example, Congress could make acts X and Y new civil wrongs and also make them new criminal wrongs if undertaken with the required mens rea. For ease of exposition, the first option is referred to as increases or enhancements in corporate civil liability and the second option is referred to as corporate crime legislation (i.e., moderate increases in corporate civil liability accompanied by criminalization of the underlying behavior).

Which of these options might corporate interests prefer? I argue that some corporate interests prefer corporate crime legislation over enhancements in corporate civil liability primarily because corporate criminal liability: (i) has been fairly low cost; (ii) results in more targeted (and hence less frivolous) enforcement; (iii) can have its enforcement more easily influenced by corporate interests; (iv) possesses stronger procedural safeguards (e.g., beyond a reasonable doubt standard of proof); (v) tends not to have high supra-compensatory damages; and (vi) less frequently imposes liability on third parties (e.g., accountants).

A. Low Cost Corporate Crime Legislation—Of Symbolic Measures.

One of the first things to note about corporate crime legislation is that enforcement has traditionally been quite thin—indeed it may appear largely symbolic.[41] This suggests that corporate crime legislation may not

41. The number of prosecutions per year is quite small and has remained nearly constant for the last decade, and most prosecutions occur against smaller firms. *See* UNITED STATES SENTENCING COMMISSION ANNUAL REPORT 2001 [hereinafter SENTENCING COMMISSION ANNUAL REPORT 2001], *available at* http://www.ussc.gov/ANNRPT/2001/ch5-2001.PDF (last visited Apr. 12, 2004); Harry First, *Criminal Antitrust Enforcement*, OCCASIONAL PAPERS FROM THE CENTER FOR RESEARCH IN CRIME AND JUSTICE, NYU SCHOOL OF LAW 3–5 (1991) [hereinafter First] (noting that many antitrust enforcement actions have been against smaller firms); Cindy Alexander et al., *Regulating Corporate Criminal Sanctions: Federal Guidelines and the Sentencing of Public Firms*, 42 J.L. & ECON. 393, 403 (1999) [hereinafter Alexander et al.]; Parker, *supra* note 7, at 399–400; Joe Davidson, *Sentence Rules Mainly Snag Small Firms*, WALL ST. J., Aug. 28, 1995, at B3 [hereinafter Davidson] (stating that "[t]he commission said 97% of the 280 firms sentenced under the guidelines since they took effect have been privately held or controlled by only a small group of shareholders"); Annie Geraghty, *Corporate Criminal Liability*, 39 AM. CRIM. L. REV. 327, 338 (2002) (noting that the majority of defendants sentenced are small, closely held organizations) [hereinafter Geraghty]; Judge Diana E.

generally be perceived as a big threat to management and big business.[42] In contrast, corporate civil liability, which is enforced by both government agencies and private litigants, has greater enforcement. For corporations, the higher likelihood of enforcement in civil liability is an important factor because they face essentially monetary sanctions in both civil and criminal proceedings.[43]

Moreover, the monetary penalties in the civil context are usually greater than those in the criminal context.[44] Thus, if corporations had the

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Murphy, *The Federal Sentencing Guidelines for Organizations: A Decade of Promoting Compliance and Ethics*, 1291 PLI/CORP 97, 113 (2002) [hereinafter Murphy] (finding median number of employees at convicted corporations to be 20); Jed S. Rakoff, *Avoiding Corporate Indictments Under New Sentencing Guidelines*, BUS. CRIMES BULL. COMPLIANCE & LITIG., Feb. 1994, at 2 [hereinafter Rakoff] (stating that Commission data suggests that prosecutors are reluctant to indict public companies unless there are very serious offenses by high-level managers).

One might view the fact that most convictions arise against small firms as indicative that corporate crime legislation benefits incumbent firms and harms smaller firms and that perhaps incumbents push for such legislation. *Cf.* Paul G. Mahoney, *The Political Economy of the Securities Act of 1933*, 30 J. LEGAL STUD. 1 (2001) [hereinafter Mahoney] (arguing that the Securities Act of 1933 reduced competition among investments banks). I suspect this is often a good explanation for regulation generally, but for reasons noted in Part VII, I doubt it provides a strong explanation for corporate crime legislation.

42. *See* NANCY K. FRANK & MICHAEL J. LYNCH, CORPORATE CRIME CORPORATE VIOLENCE: A PRIMER 126 (1992) [hereinafter FRANK & LYNCH] (criminal sanctions viewed by corporations as a "cost of doing business").

43. *See* KIP SCHLEGEL, JUST DESERTS FOR CORPORATE CRIMINALS 22–30 (1990) [hereinafter SCHLEGEL ET AL.]. *See also* CORPORATE AND WHITE COLLAR CRIME: AN ANTHOLOGY 25–26 (Leonard Orland ed., 1995) [hereinafter Orland]; Alexander et al., *supra* note 41, at 395. *See also* CORPORATE MISCONDUCT: THE LEGAL, SOCIETAL, AND MANAGEMENT ISSUES 60–66 (Margaret P. Spencer & Ronald R. Sims eds., 1995) [hereinafter CORPORATE MISCONDUCT] (calculation of fines).

44. *See* Alexander et al., *supra* note 41, at 395. *See also* SCHLEGEL, *supra* note 43, at 11. There is considerable evidence that corporate crime penalties are perceived to be generally lower than corporate civil sanctions. *See, e.g.*, William Glaberson, *S.E.C. Aide Assails Plan on Punishing Companies*, N.Y. TIMES, Oct. 12, 1988, at D6; Stephen Labaton, *Corporate Penalty Plan Stirs Debate*, N.Y. TIMES, Oct. 10, 1988, at D6; Philip Shenon, *Ideas & Trends: Proposals for Punishment; The Case of the Criminal Corporation*, N.Y. TIMES, Jan. 15, 1989, at E28. There are, of course, reputational sanctions imposed on corporations from both corporate civil and criminal liability that are relevant in assessing the costs of each kind of liability. Most studies of reputational effects on corporations (measured by drops in share price associated with revelations of wrongdoing) find that they are (i) sometimes quite large; (ii) about the same regardless of the type of proceedings (civil or criminal), holding the kind of wrongdoing and official sanction size constant; and (iii) that reputational penalties tend to be positively correlated with the size of the official sanction (suggesting that larger official sanctions under corporate civil liability may generate greater reputational losses). *See* Jonathan M. Karpoff & John R. Lott, *On the Determinants and Importance of Punitive Damage Awards*, 42 J.L. & ECON. 527, 570 (1999) [hereinafter Karpoff & Lott] (arguing that "[f]irm values and the use of reputational investments to assure contractual performance, however, will be affected by both the size and predictability of prospective punitive awards"); Jonathan M. Karpoff & John R. Lott, Jr., *The Reputational Penalty Firms Bear for Committing Criminal Fraud*, 36 J.L. & ECON. 757, 758 (1993) (noting that "reputational cost . . . constitutes most of the cost incurred by firms accused or convicted of fraud"); Cindy R. Alexander, *On the Nature of the Reputational Penalty for Corporate Crime: Evidence*, 42 J.L. & ECON. 489, 491 (1999). This suggests that the presence of reputational losses is

choice, they might prefer corporate crime legislation because its enforcement is less frequent and its penalties are often lower than those under corporate civil liability. Simply put, corporate criminal liability has lower expected costs than increases in corporate civil liability.

One caveat is in order. Over the last decade or so the criminal penalties imposed on corporations have increased,[45] as have corporate expenditures on compliance.[46] The increased compliance expenditures suggest that the perceived costs of corporate or executive criminal liability have grown

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important, but that corporate civil liability may tend to have greater or similar reputational losses to corporate criminal liability.

45. Following the Organizational Sentencing Guidelines, the penalties imposed on convicted corporations have increased perhaps by up to 5 to 10 times their pre-Guideline levels. *See* Alexander, et al., *supra* note 41, at 409–13. Indeed, penalties in health care, environmental, securities, and antitrust fields have all increased over the last decade by quite a lot. *See* Mary B. Neumayr, *An Examination of the Criminalization of Commercial Activity* (July 25, 2002) [hereinafter Neumayr], *available at* http://www.fed-soc.org/pdf/CrimFinal.pdf. The recent increases under Sarbanes-Oxley ratchet up penalties even further. *See* SENTENCING COMMISSION REPORT, *supra* note 3.

It is still possible that expected penalties might be small if detection rates are small. However, detection rates for corporate wrongdoing tend to vary with the type of wrongdoing. *See* Neumayr, *supra*, at 8–11 (discussing qui tam enforcement, which is sometimes considered frivolous). *Cf.* Jeffrey S. Parker, *Criminal Sentencing Policy for Organizations*, in U.S. SENTENCING COMMISSION, DISCUSSION MATERIALS ON ORGANIZATIONAL SANCTIONS (1988), *reprinted* in 26 AMER. CRIM. L. REV. 513 (1989) (stating that the likelihood of detection and conviction for antitrust is estimated by the Department of Justice as being about 10%). *But see* Marc D. Goodman, *Why the Police Don't Care About Computer Crime*, 10 HARV. J.L. & TECH. 465, 475 (1997) (noting that for some computer crimes, rates of escape may be about 98%).

46. *See generally* SENTENCING GUIDELINES, *supra* note 3, at § 8C2.5(f); William S. Laufer, *Corporate Prosecution, Cooperation, and the Trading of Favors*, 87 IOWA L. REV. 643 (2002); Murphy, *supra* note 41, at 111, 115, 116; Harvey L. Pitt & Karl A. Groskaufmanis, *Minimizing Corporate Civil and Criminal Liability: A Second Look at Corporate Codes of Conduct*, 78 GEO. L.J. 1559 (1990).

One of the primary corporate responses to the organizational sentencing guidelines has been to invest increased resources and effort in promulgating compliance programs that could earn the corporation a sanction reduction under the guidelines. Under the guidelines a "reasonably effective" compliance program could lead to substantial reductions in corporate penalties. *See* U.S. SENTENCING COMMISSION, HOW THE ORGANIZATIONAL GUIDELINES WORK: AN OVERVIEW, http://www.ussc.gov/SYMPO/WCSYMPO1.HTM. These compliance programs are, however, generally considered expensive to devise and implement and would only be worth the expense if they generated a benefit (e.g., reduced penalties and reduced wrongdoing) that was worth the cost. *See also* Alan Kline et al., *Cost of Compliance*, AMERICAN BANKER, Apr. 19, 2002, *available at* http://www.americanbanker.com (quoting Bob Wilmers, Chairman, M&T Bank Corp. "The cost of regulatory compliance is not insubstantial . . . [w]e estimate that our annual cost . . . is now up to $37 Million and counting"); ERNST & YOUNG, CORPORATE COMPLIANCE PROGRAMS: LEADING PRACTICES SURVEY (2001); Robert J. Ambrogi, *Browse Your Way to Compliance*, Law.com, (Jan. 27, 2003), *at* http://www.law.com/servlet/ContentServer?pagename=OpenMarket/Xcelerate/View&c=LawArticle&cid=1042568695687&live=true&cst=1&pc=0&pa=0 (now defunct) (on file with author) (noting that "Times are good for businesses that provide corporate compliance training online. Los Angeles' Legal Knowledge Co., for example, saw contracts for its Web-based Legal Compliance and Ethics Center (LCEC) double in the past year, to $100 million." This is just one corporation that provides only training services).

enough to justify these expenditures, implying that these costs are not trivial.[47] This may be increasingly true, but it does not change my analysis. My analysis requires that corporate civil liability be more costly to corporations than corporate criminal liability. Evidence suggests that not only has the cost of corporate criminal liability increased recently, but so too has the cost of corporate civil liability (and by at least as much).[48] Thus, we would still expect that corporations prefer corporate crime legislation over increases in corporate civil liability.[49]

47. I do not rely on claims by corporations that they are "truly" scared of corporate criminal liability because such claims may reflect one of at least three things. First, that corporate criminal liability does impose significant costs. Second, corporate criminal liability does not impose large costs, but corporations have self-serving reasons to claim that it does (e.g., to prevent more harmful measures). Third, that managers are scared by corporate criminal liability because the initiation of a prosecution against the corporation might be viewed as a signal that criminal prosecutions against managers are likely. *See* Laufer, *supra* note 6, at 649–52 (noting that cooperation and presumably compliance programs would reduce the likelihood of the corporation being charged, which may help evade liability for higher ups).

There is a question of how compliance programs became so important in the corporate wrongdoing area: who lobbied for them? It appears that both corporate interests and law firms lobbied for them. *See* Daniel Fischel & Alan O. Sykes, *Corporate Crime*, 25 J. LEGAL STUD. 319, 348 (1996) [hereinafter Fischel & Sykes] (noting that compliance programs are a bonanza for law firms because of the business it generates for them); Jonathan R. Macey, *Agency Theory and the Criminal Liability of Organizations*, 71 B.U. L. REV. 315, 316 (1991) [hereinafter Macey]; Reynolds, *supra* note 40, at 27. Why might this be? Corporations and management might be scared of government investigations revealing personal (i.e., managerial) wrongdoing, and the presence of a reasonable compliance program may lead prosecutors not to investigate further and uncover these wrongs or incriminating evidence. *See* Laufer, *supra* note 6, at 657–60. Also, law firms may not be providing management with the best advice about the true risks of liability given that they sell (and hence benefit financially) from the provision of compliance services. *See* Fischel & Sykes, *supra*. *Cf.* John C. Coates IV, *Explaining Variation in Takeover Defenses: "Blame the Lawyers,"* 89 CAL. L. REV. 1301 *passim* (2001) (discussing how variation in takeover defenses at the IPO stage may be explained by the corporations using different law firms).

48. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1514 (noting that "[t]he recent increases in the severity of corporate sanctions in both the civil and criminal spheres may indicate a belief that sanctions are still not stiff enough to deter undesirable behavior."). The analysis thus far does not indicate how or why corporate penalties increased as much as they did in the guidelines. An explanation for this change cannot be explored in the limited space of this Article, but there were suggestions that the pre-guidelines sanctions were considered quite low. *See* Alexander et al., *supra* note 41, at 395. Also, it is possible that, had these increases not gone through, even more costly measures could have been undertaken. After all, the guidelines came about on the heels of the Watergate scandal, insider trading cases, and the savings and loan debacle. This presumably was associated with a large amount of public outcry with corporate wrongdoing. When this is combined with the greater impact corporations have on our everyday lives than in the past, one can imagine how liability increases might become more common now than in the past. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1481–84.

49. *See supra* note 47 and accompanying text. Another noteworthy point is that compliance expenditures are not only useful in reducing criminal sanctions, but they may reduce civil sanctions too. Compliance programs may reduce the total civil sanction suffered by a corporation in two ways. First, sometimes the presence of such programs could lead to a finding of no (or lesser) liability. *See* Burlington Industries v. Ellerth, 524 U.S. 742 (1998); Faragher v. City of Boca Raton, 524 U.S. 775

B. Targeted Enforcement

Enforcement of corporate criminal and civil liability occurs in somewhat different ways. Corporate civil liability is enforced by both government agencies (e.g., the SEC) as well as private litigants,[50] whereas corporate criminal liability is enforced by the Department of Justice (DOJ) *only*.[51] The different sets of enforcers are important to corporate interests. This is because private litigants are more likely than government agents to bring frivolous suits.[52] The core reasons are quite straightforward. First, private litigants may receive direct financial gains by pursuing frivolous or questionable suits against corporations, whereas government agents

(1998); Michael C. Harper, *Employer Liability for Harassment Under Title VII: A Functional Rationale for* Faragher *and* Ellerth, 36 SAN DIEGO L. REV. 41 (1999); Allan Horwich, *Section 11 of the Securities Act: The Cornerstone Needs Some Tuckpointing*, 58 BUS. LAW. 1 (2002). Second, if these programs have a deterrent effect, then the number of wrongs and the number of civil suits premised on these wrongs would decrease. Thus, both the magnitude and frequency of civil sanctions could decrease. This provides yet another benefit to compliance programs (along with reductions in the magnitude and frequency of criminal penalties) that should be weighed against its costs and also suggests that it is not simply increases in criminal sanctions that are triggering compliance expenditures. Indeed, it might be that the reductions in civil liability motivate the increased expenditure in compliance programs. For example, it may be that compliance programs cost $200 million but reduce criminal penalties by $20 million and civil sanctions by $181 million. Nonetheless, the timing of the growth in compliance expenditures seems to coincide with the organizational sentencing guidelines (i.e., criminal sanctions), suggesting that they may well be the critical trigger. *Cf.* Laufer, *supra* note 6, at 650–54 (noting that the issue of corporate compliance got a huge lift following the organizational sentencing guidelines); Murphy, *supra* note 41, at 111, 115, 116 (noting large impact of organizational sentencing guidelines on compliance activity). One explanation for this might be that the criminal penalties were the amount needed at the margin to trigger the growth of compliance programs, although this would assume a fairly accurate sanction-setting policy by the government, which may not necessarily be the case.

50. *See* FRANK & LYNCH, *supra* note 42, at 26–27.

51. I am referring to federal corporate crime legislation. State corporate crime laws are enforced by state prosecutors. *See* CORPORATE MISCONDUCT, *supra* note 43, at 36–38.

52. This is not to suggest that prosecutors always bring socially desirable suits, but only that they tend to bring socially undesirable suits less frequently than private litigants. *See* Toobin, *supra* note 33, at 9. For these concerns in the context of recent securities regulation, see Selective Disclosure and Insider Trading, Exchange Act Release No. 34-43154, 735 SEC Docket 3 (Aug. 15, 2000) and Stephen J. Choi, *Selective Disclosures in the Public Capital Markets*, 35 U.C. DAVIS L. REV. 533, 540–69 (2002) (discussing the efficiency consequences of Regulation F-D). For discussions on how prosecutors' incentives may diverge from the socially optimal, see Edward L. Glaeser, Daniel P. Kessler, & Anne M. Piehl, *What Do Prosecutors Maximize? An Analysis of the Federalization of Drug Crimes*, 2 AM. L. & ECON. REV. 259, 261 (2000) [hereinafter Glaeser et al.] (noting that decisions to prosecute are often influenced by prosecutors' interest in running for higher office); Stuntz, *supra* note 37, at 533 (noting that "local prosecutors are likely to seek to produce the range of outcomes the public desires"); Peter Krug, *Prosecutorial Discretion and Its Limits*, 50 AM. J. COMP. L. 643, 662 (2002) (noting that police misconduct prosecution occurs only in cases of high public visibility) [hereinafter Krug].

generally do not.[53] Second, given that prosecutors want to maximize convictions and are operating within a budget, they will probably use their resources on cases they believe are more likely to result in convictions.[54] Presumably, this pushes them away from the weak and frivolous cases and toward the more meritorious cases, which as a general matter should be easier cases in which to obtain convictions.[55] However, in the private litigation setting—with class actions, contingency fees, and entrepreneurial attorneys—things are likely to be different.[56] This is not to say government agents cannot benefit from frivolous suits but that as a general matter they are less likely to initiate frivolous litigation compared to private litigants.[57] In light of this, corporate interests might be more inclined to prefer less frivolous (read costly) litigation via corporate crime

53. *See* Mark A. Cohen & Paul H. Rubin, *Private Enforcement of Public Policy*, 3 YALE J. ON REG. 167, 169 (1985) [hereinafter Cohen & Rubin] (noting that "[t]hird, and most important, private enforcement agents, unlike government regulators, will possess ongoing economic interests directly related to the costs and benefits of public policy implementation.") (also acknowledging generally that government agencies do not have as much incentive as private litigants). *See generally* Gary S. Becker & George J. Stigler, *Law Enforcement, Malfeasance, and Compensation of Enforcers*, 3 J. LEGAL STUD. 1, 13 (1974) (suggesting that compensation scheme for public enforcers should emulate scheme of private enforcers, given that there is much greater private incentive to enforce).

54. *See* Edward D. Cavanagh, *Detrebling Antitrust Damages: An Idea Whose Time Has Come?*, 61 TUL. L. REV. 777, 807 (1987) [hereinafter Cavanagh] (noting that "[o]n the contrary, given the limited resources available to public enforcement agencies, the government presumably is better able to take into account relevant enforcement costs and prosecute only those matters which are truly in the public interest."); J. Mark Ramseyer & Eric B. Rasmusen, *Why Is the Japanese Conviction Rate So High?*, 30 J. LEGAL STUD. 53, 71–72 (2001) [hereinafter Ramseyer & Rasmusen]. I do not mean to suggest that maximizing convictions is the only thing that prosecutors care about. There may be many other things that matter to prosecutors too, but convictions are important. For discussion of some other factors that may influence prosecutors see Glaeser et al., *supra* note 52, at 261; Krug, *supra* note 52, at 662. *See also infra* notes 142 & 153 and accompanying text.

55. Of course, it is plausible that easier convictions may not be the socially most valuable ones to pursue.

56. *See* Cavanagh, *supra* note 54, at 807; Jill E. Fisch, *Class Action Reform: Lessons from Securities Litigation*, 39 ARIZ. L. REV. 533, 535–36 (1997) (noting that "[t]he costs of defense imposed pressure on defendants to settle even weak cases, pressure that was aggravated by the financial incentives created by the third party payment structure of insurance and indemnification"). *See also* Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 57 (1991).

57. *See* Cohen & Rubin, *supra* note 53, at 169; Richard W. Painter, *Game Theoretic and Contractarian Paradigms in the Uneasy Relationship Between Regulators and Regulatory Lawyers*, 65 FORDHAM L. REV. 149, 169 (1996) (emphasizing that enforcement officials have job-advancement incentives to thoroughly enforce infractions, but not mentioning monetary gain for SEC); A.C. Pritchard, *Markets as Monitors: A Proposal to Replace Class Actions with Exchanges as Securities Fraud Enforcers*, 85 VA. L. REV. 925, 959–62; 1017–18 (2001) (discussing incentives of private litigants and the SEC) [hereinafter Pritchard].

legislation than more frivolous litigation via increases in corporate civil liability.[58]

C. Influencing the Enforcers

Another reason why the identity of the enforcer is important is that government enforcers operate within a budget that is subject to congressional control.[59] In light of this, corporate interests can influence the enforcement of criminal laws—by lobbying over enforcement budgets—in a manner they cannot for civil liability as enforced by private litigants.[60] For example, corporate interests could lobby for a lower enforcement budget and thereby reduce the frequency of enforcement.[61] Furthermore, there is a rich literature discussing how corporate interests may be able to "capture" agencies and their enforcement.[62] Finally, lobbying over enforcement budgets is somewhat less visible than direct lobbying over legislation. Thus, corporate interests would prefer government enforcement of the law, as that still leaves these interests with more influence in the enforcement process.

Of course, government enforcement can occur in two ways: criminal or civil. Corporate interests are more likely to prefer corporate criminal

58. There is considerable evidence from the antitrust and securities laws fields that business interests often prefer government enforcement to private litigation. *See Antitrust Advance*, N.Y. TIMES, Jun 17, 1976, at 34; Susan Antilla, *A Battle Over Securities-Fraud Cases*, N.Y. TIMES, July 4, 1993, at F13; Jeff Gerth, *Overhaul of Securities Laws: A Fast Track to Change or a Hasty Decision?*, N.Y. TIMES, May 26, 1995, at A19; Neil A. Lewis, *House Passes Bill That Would Limit Suits of Investors*, N.Y. TIMES, Mar. 9, 1995, at A1; Bruce Rubenstein, *Cease and Desist*, CORP. LEGAL TIMES, Sept. 1994, at 1.

59. *See* Ronald E. Bornstein & N. Elaine Dugger, *International Regulation of Insider Trading*, 1987 COLUM. BUS. L. REV. 375, 387 (1987) (noting that "[t]he Senate Banking Committee also has held several hearings regarding the problem of insider trading in the context of corporate mergers and takeovers. In the course of those hearings, recommendations were made to clarify the offense of insider trading and to increase the portion of the SEC's budget allocated to related enforcement activities"); William J. Carney, *Signaling and Causation in Insider Trading*, 36 CATH. U. L. REV. 863, 897 (1987) (noting that individuals can lobby Congress to sustain the SEC's enforcement budget).

60. *See Delegation*, *supra* note 33, at 789–810; Christopher Drew, *In the Productivity Push, How Much Is Too Much?*, N.Y. TIMES, Dec. 17, 1995, at C1. *Cf.* William N. Eskridge, Jr., *Politics Without Romance: Implications of Public Choice Theory for Statutory Interpretation*, 74 VA. L. REV. 275, 289 (1988) (indicating that when legislators give power to regulatory agencies, those agencies become the focus of competing interests).

61. *See Delegation*, *supra* note 33, at 776–79; Cynthia A. Williams, *Corporate Compliance with the Law in the Era of Efficiency*, 76 N.C. L. REV. 1265, 1365 n.380 (1998) (indicating that UPS lobbied to decrease the OSHA's budget and that corporations direct some efforts to "lobby to reduce penalties for violations and to reduce funds for enforcement of existing law").

62. *See* S.M. PHILLIPS & J.R. ZECHER, THE SEC AND THE PUBLIC INTEREST 21–24 (1981); Jonathan R. Macey, *Administrative Agency Obsolescence and Interest Group Formation: A Case Study of the SEC at Sixty*, 15 CARDOZO L. REV. 909 (1994).

enforcement because of its infrequency compared to civil enforcement.[63] Further, corporate crime legislation leads to the creation of fewer actionable wrongs than increases in corporate civil liability.[64] This is yet another reason why corporate interests may prefer the criminal route.[65]

D. Procedural Protections

As a general matter, corporate criminal liability requires the moving party to meet more procedural hurdles than corporate civil liability (e.g., the beyond a reasonable doubt standard of proof, and the bar on double jeopardy).[66] In civil cases the moving party (even the government) must prove liability only by preponderance of the evidence and is subject to

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63. *See supra* Part III.A. In theory, corporations could lobby to have exclusively government civil enforcement (i.e., prohibit private litigation) rather than corporate crime legislation. This seems unlikely as a political matter. *See* Adam F. Ingber, Note, *10b-5 or not 10b-5? Are the Current Efforts to Reform Securities Litigation Misguided?*, 61 FORDHAM L. REV. 5351, 5353–55 (1993) (stating that private enforcement of the 1934 Securities laws is "essential for efficient markets"); Pritchard, *supra* note 57, at 1017 n.397; Joel Seligman, *The SEC's Unfinished Soft Information Revolution*, 63 FORDHAM L. REV. 1953, 1988 (1995) (noting that "[g]iven the limited Commission [SEC] resources available for the enforcement of its mandatory disclosure system, private litigation has been recognized as performing a useful augmentative deterrent, as well as compensatory, role"); Jeffrey P. Strickler, Comment, *Inside Information and Outside Traders: Corporate Recovery of the Outsider's Unfair Gain*, 73 CALIF. L. REV. 483, 508 (1985) (advocating use of private enforcement in securities law often because "government enforcement agencies are overburdened and cannot adequately police the market").

Moreover, the U.S. tradition is to extend some private rights of action (even implicitly) when there is an expansion of civil liability. *See, e.g.*, Virginia G. Maurer, *Antitrust and RICO: Standing on the Slippery Slope*, 25 GA. L. REV. 711 (1991) (noting that "[s]ince 1890, federal statutes have provided a private civil damages action to augment public enforcement of antitrust laws"). In addition, the desire for compensation and a distrust of government combine to make excluding private enforcement a fairly infrequent event. *See* Donald C. Langevoort, *Capping Damages for Open-Market Securities Frauds*, 38 ARIZ. L. REV. 639, 652 (1996) (noting that "the conventional view that private litigation is a necessary supplement to SEC enforcement is well-grounded"). However, recent measures in the securities regulation arena, such as Regulation F-D, appear to rely more exclusively on government enforcement. *See* COX, *supra* note 39, at 976–82.

64. Criminalizing civil wrongs does not create new grounds of recovery for private litigants.

65. One might view Sarbanes-Oxley as an example of this. Note also that the analysis in the text suggests that private interests (litigants and their attorneys) favor increases in corporate civil liability over corporate crime legislation. Thus, one expects that private interest support for corporate crime legislation would be weaker than support for increases in corporate civil liability, which increases profits directly for plaintiffs. *See* Toobin, *supra* note 33, at 94 (quoting Joseph Grundfest as saying, "[t]he last thing that Bill Lerach wants is a bigger budget for the SEC and more lawsuits to sue the people that he's suing . . . If the SEC had the resources to go after the problem in a big way, there is a great deal of evidence that suggests they would do a better job with the companies that have really committed fraud, and not pursue cases where the evidence is weaker.").

66. *See generally Developments*, *supra* note 11, at 1341–50. *See also* FRANK & LYNCH, *supra* note 42, at 26–28 (noting the difficulty of proving intent, standard of proof, and procedural rights); Alexander Kovel, *A Case for Civil Penalties: Air Pollution Control*, 46 J. URB. L. 153, 159 (1969).

lesser procedural restrictions than in the criminal process.[67] To the extent that these criminal procedures impede convictions, corporate interests prefer criminal liability over corporate civil liability, for which judgments are easier to obtain.[68]

E. Supra-Compensatory Damages

Corporate civil liability—when enforced by private litigants—involves the real risk of supra-compensatory damages (e.g., treble or punitive damages).[69] The areas in which the government can claim such large sanctions are more limited.[70] Consequently, corporate interests may prefer governmental enforcement because it is likely to lead to lesser sanctions than private litigant enforcement.[71]

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67. On the higher standard of proof, see Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1512–17. On corporate procedural protections, see Vikramaditya S. Khanna, *Should Corporations Receive the Protections of Criminal Procedure?*, Draft Paper 2004 (on file with author). On the importance of budgetary allocation for prosecution, see *Delegation*, *supra* note 33, at 789–810. There is evidence that in some spheres enforcement budgets have increased somewhat. *See* Neumayr, *supra* note 45, at 5–6 (discussing environmental enforcement).

68. The importance of these procedural safeguards is diminished when there is a great deal of criminalization because the increasing amount of potential criminal liability makes it easier for prosecutors to obtain convictions in spite of the procedural safeguards. *See* Stuntz, *supra* note 37, at 537–38. This is due to the greater breadth of the law and greater threat value of trials when criminalization is rampant. *See id.*

69. *See* Orland, *supra* note 43, at 16. *See also* 18 U.S.C. §§ 1961–1968 (1982) (treble damages available under the Racketeer Influenced and Corrupt Organizations Act (RICO)); Charles A. Sullivan, *Breaking Up the Treble Play: Attacks on the Private Treble Damage Antitrust Action*, 14 SETON HALL L. REV. 17, 18–25 (1983) (development of treble damages in antitrust actions).

70. For further anecdotal support, consider the infamous Exxon Valdez case. In that case one suspects that many more people were aware of the civil punitive damages award than the criminal penalties. Although Exxon received a $150 million fine as per a criminal plea agreement, the court forgave $125 million of it in recognition of Exxon's cooperation in cleaning up the spill and paying certain private claims. *See* Consent Decree and Agreement at 18–19, Clerk's Docket No. 46 in United States v. Exxon Corp., No. A91-0082-CV, and Clerk's Docket No. 26 in Alaska v. Exxon Corp., No. A91-0083-CV. In contrast, as part of its civil settlement, Exxon agreed to pay $900 million in addition to the $2.1 billion it had already spent on the clean-up. *Id.* The settlement also contains a "reopener window" between September 1, 2002 and September 1, 2006, during which the states may make a claim for up to an additional $100 million. *Id.* In addition, Exxon remained subject to civil suits by private parties which resulted in a $5 billion punitive jury award (the largest punitive judgment ever suffered by a U.S. corporation). *See Spillionaires*, ANCHORAGE DAILY NEWS, Mar. 17, 1996, at B3, *available at* http://www.adn.com/evos/stories/EV402.html (last visited Apr. 1, 2004). Also, even after the guidelines, the criminal fine is still only a small portion of the total loss the corporation suffers from wrongdoing. *See* Alexander et al., *supra* note 41, at 409–10; Karpoff & Lott, *supra* note 44, at 758 (noting that "[r]eputational cost . . . constitutes most of the cost incurred by firms accused or convicted of fraud.").

71. The preferred form of government enforcement may well be criminal because that reduces the scope for private litigant recovery as argued in Part C, *supra*.

F. Third Party Liability

In civil proceedings the corporation is not the only party who may be pursued. For example, in a standard securities law civil suit the defendants could be the corporation, its officers and directors, its accountants, its attorneys, and its underwriters.[72] Although we can pursue third parties in criminal cases, it is more difficult to impose liability on them (often due in part to mens rea requirements).[73] This may be valuable to corporations because they often bear a large portion of the costs associated with third party liability.[74] For example, if third parties contract with the corporation in some form (e.g., to provide accountancy services), then the increased risk of bearing sanctions for third parties would probably be reflected in higher prices (e.g., higher accounting fees) charged to the corporation.[75] If the expected cost to third parties is less under criminal regimes than under civil liability, then we might expect corporate interests to prefer the lower-cost criminal alternative.

G. Substitution Thesis Examples

For the reasons identified above we might expect corporate interests to prefer corporate crime legislation over enhancements in corporate civil liability when some congressional response is inevitable. If so, do we see instances of this? I would argue that there is evidence which, although not conclusive, is supportive of the substitution thesis.[76]

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72. *See, e.g.*, CORPORATE MISCONDUCT, *supra* note 43, at 89–91 (liability for accountants); George D. Reycraft, *Conflicts and Complications: Conflicts of Interest and Effective Representation: The Dilemma of Corporate Counsel*, 39 HASTINGS L.J. 605, 607 (1988) (noting that "[a] fourth factor that cannot be overlooked is that the lawyer or law firm usually maintains a sizable malpractice insurance policy. Thus lawyers, like accountants and underwriters, are often seen as 'deep pockets' and a ready source of settlement or award money.").

73. *Cf. Developments*, *supra* note 11, at 1259–75. *But see* Neumayr, *supra* note 45, at 10 (arguing that negligence standards are increasing).

74. *See* Reinier H. Kraakman, *Gatekeepers: The Anatomy of a Third-Party Enforcement Strategy*, 2 J.L. ECON. & ORG. 53, 74–78 (1986).

75. *See* A. Mitchell Polinsky & Steven Shavell, *Should Employees Be Subject to Fines and Imprisonment Given the Existence of Corporate Liability?*, 13 INT'L. REV. L. & ECON. 239, 241 (1993) [hereinafter Polinsky & Shavell] (noting that "[w]hen employees face the risk of fines, they naturally will demand higher compensation from firms, everything else being equal. In effect, this will cause firms to pay fines in the form of higher wages"); Richard W. Painter, *Toward a Market for Lawyer Disclosure Services: In Search of Optimal Whistleblowing Rules*, 63 GEO. WASH. L. REV. 221, 239 (1995) (noting that an increase in liability for attorneys for failure to disclose their clients' illegal practices will result in risk premiums charged by whistleblowers).

76. An explanatory note is perhaps in order. I do not expect that there will be direct documentary evidence indicating that corporate interests ignored or supported corporate crime legislation in order to avoid increases in corporate civil liability. Such "smoking gun" memos would be truly useful, but,

Let us begin with the most recent series of corporate scandals involving accounting misrepresentations and securities fraud. One response could have been to repeal the Private Securities Litigation Reform Act of 1995 (PSLRA) and overturn some related U.S. Supreme Court jurisprudence.[77] This is because the PSLRA restricted the scope of private securities fraud liability and, along with some U.S. Supreme Court precedent, made it harder to impose liability on associated parties (e.g., accountants).[78] This in turn insulated accountants and issuers to some extent from securities fraud liability, thereby reducing the costs associated with securities fraud (for them) and, arguably, increasing the incentive to engage in it.[79] Repealing the PSLRA and overturning associated U.S. Supreme Court precedent might combat this and would operate as an increase in corporate civil liability because it would open up corporations and accountants to greater liability.

Indeed, after the Enron scandal some people essentially did lobby for this.[80] However, these initiatives were unsuccessful and instead Congress enacted Sarbanes-Oxley which, amongst other things, ratchets-up criminal penalties.[81] Moreover, we saw little corporate opposition to Sarbanes-

given the likely sophistication of most corporate interests, unlikely to be found. Rather, I provide examples of where, when some kind of congressional response was inevitable, corporate interests appeared to lobby most strongly against increases in corporate civil liability and said little if anything against increases in corporate crime legislation. Although this evidence is not as compelling as a "smoking gun" memo, the pattern created over time does provide an indication as to the lobbying activities and preferences of corporate interests.

77. *See* Pub. L. No. 104–67, 109 Stat. 737 (codified as amended in various sections of 15 U.S.C.); Central Bank of Denver v. First Interstate Bank of Denver, 511 U.S. 164 (1994).

78. *See* John C. Coffee, Jr., *Understanding Enron: "It's About the Gatekeepers, Stupid,"* 57 BUS. LAW. 1403, 1409–12 (2002) [hereinafter Coffee].

79. *See* Coffee, *supra* note 78, at 1409–12. There are other explanations for the recent spate of fraud. *See id.* at 1412–13 (discussing an "irrational market"), 1413–16 (discussing other explanatory matters).

80. *See* Interview with Professor John Coffee, Adolf E. Berle Professor of Law, Columbia Law School (Feb. 28, 2003); ADAM C. PRITCHARD, SHOULD CONGRESS REPEAL SECURITIES CLASS ACTION REFORM?, CATO INSTITUTE POLICY ANALYSIS NO. 471, at 12–14 (Feb. 27, 2003), *at* http://www.cato.org/pubs/pas/pa-471es.html.

81. *See generally* Public Accounting Reform and Investor Protection Act of 2002, Pub.L. 107–204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C.A and 18 U.S.C.A.). *See* SENTENCING COMMISSION REPORT, *supra* note 3. The new law essentially creates fewer private claims (than might repeal of the PSLRA).

Besides corporate crime legislation, there are other areas where corporations may rely on some kind of substitution thesis. For example, it has been argued that Delaware corporate law may develop and respond to threats (tacit and explicit) to federalize corporate law. *See* Mark Roe, *Delaware's Competition* (Draft Paper 2003, on file with author). Thus, certain measures may be undertaken in Delaware not because they are perceived to be the most efficient, but because if they are not adopted, then an even worse outcome may eventuate: federalization of the issue at hand. *See* Roe, *Delaware's Competition*, *supra*. This suggests that changes in state corporate law are acting as substitutes for more costly changes in federal law.

Oxley compared to the opposition to moves to enhance corporate civil liability via repeal of the PSLRA.[82]

This pattern, however, is not unique to Sarbanes-Oxley. If we examine lobbying around the Foreign Corrupt Practices Act we also notice that criminal liability generates little concern.[83] Indeed, there appeared to be more corporate opposition to proposals to require disclosure of payments made to foreign government officials.[84] These disclosure requirements would have imposed a large burden on both corporations (to comply with the requirement) and on the government (to enforce it).[85] In the end, the disclosure requirements did not come to pass and instead we saw an increase in criminal liability.[86] By all accounts the costs of this criminal liability for business interests are quite small.[87] One might interpret these events as suggesting that corporate interests preferred criminalization because it imposed lower costs than disclosure requirements.[88]

There is also some evidence suggesting that the judiciary may rely on substitution too. Some empirical evidence suggests that federal judges have started awarding higher sanctions since the Sentencing Guidelines were adopted even in cases not subject to the Guidelines. *See* Alexander, et al., *supra* note 41, at 416–17. The conjecture is that this may have been a strategic move by the judiciary to head off any more sanction increases or encroachments on sentencing discretion for the time being. *See id.*

82. *See* Pritchard, *supra* note 57, at 2 (noting vigorous opposition exists to the PSLRA but giving no such information on Sarbanes-Oxley).

83. *See* Morton Mintz, *Hill Considers Changing Law on Foreign Bribery*, WASH. POST, Oct. 25, 1987, at H6 [hereinafter Mintz]; S. REP. NO. 95–114, at 10 (1977), *reprinted in* 1977 U.S.C.A.A.N. 4098, 4107–08.

84. *See* S. REP. NO. 95–114, *supra* note 83.

85. *See id.*

86. *See id.*

87. *See* Mintz, *supra* note 83, at H6.

88. Corporate interests have also been known to oppose increased enforcement by private litigants while being less opposed to increased government enforcement. This is consistent with the notion, discussed earlier, that corporate interests may prefer government enforcement because it is more targeted and more subject to their control. For example, in the 1970s there were attempts to permit state attorneys general to bring antitrust suits on behalf of their citizens and then permit follow-on private enforcement. *See Antitrust Advance*, N.Y. TIMES, Jun 17, 1976, at 34; Eileen Shanahan, *Antitrust Bill Stopped By A Business Lobby*, N.Y. TIMES, Nov. 16, 1975, at 1. Corporate interests (led by the Business Roundtable) lobbied heavily against this. *See Antitrust Advance*, *supra*; Shanahan, *supra*. In the end, the version of the law that was enacted was one that did permit state attorneys general to bring suit on behalf of their citizens, but limited the ability of private attorneys to capture treble damages as well as making it more difficult to garner contingency fees. *See Antitrust Advance*, *supra*. Another similar instance is corporate lobbying activities surrounding the availability of treble damages in anti-racketeering cases. Corporations lobbied heavily against the treble damages portions, but not too much against the criminal aspects. *See* Russell Mokhiber, *Triple Damages*, N.Y. TIMES, Sept. 14, 1985, at 23. This is consistent with the notion that corporate interests prefer government enforcement to private litigant enforcement and similarly may prefer corporate crime legislation over increases in corporate civil liability.

This is not to suggest that corporate interests *never* lobby in the criminal sphere but that such lobbying tends to be the exception rather than the rule. Moreover, there is evidence that corporate interests only lobby in the criminal sphere when there are large penalty increases being proposed or when criminal liability for directors and officers is likely to increase significantly.[89] These are instances where the costs of corporate crime legislation are getting larger and closer to the costs of increases in corporate civil liability; thus, the lobbying activity is more understandable.

IV. THE SUBSTITUTION THESIS WHEN THE CONCERN IS MANAGERIAL LIABILITY

Corporate interests may also prefer corporate crime legislation because of its potential effect on the incidence of managerial criminal liability. This is because corporate criminal liability has the potential to deflect criminal liability away from managers and on to the corporation (i.e., shareholders).

For example, having a corporate defendant along with a management defendant in the same case may increase the odds that management escapes conviction or suffers a lesser criminal penalty relative to where management is the only defendant.[90] When there are two sets of

89. For example, when the organizational sentencing guidelines increased corporate criminal penalties, we saw corporate interests lobby heavily for smaller increases in penalties and for sanction reductions based on compliance efforts. These efforts were largely successful. *See* Reynolds, *supra* note 40, at 27; Macey, *supra* note 47, at 316–17. Also, when criminal liability for officers and directors may increase, we see corporate lobbying efforts that often defeat or restrain attempts to expand this liability. Examples would be proposals to increase such liability at the time of the passage of the federal securities laws. *See Attacks Securities Bill; Investment Bankers' Head Calls It Detriment to Industry*, N.Y. TIMES, May 8, 1933, at 29 [hereinafter *Attacks*]; G.R. Davis, *The Securities Bill; Some Features Viewed as In Restraint of Trade*, N.Y. TIMES, May 22, 1933, at 14 [hereinafter Davis]; *Merchants Protest; New Yorkers Ask for Hearing on the Securities Bill*, N.Y. TIMES, May 9, 1933, at 3 [hereinafter *Merchants Protest*]; *Senators Revise Securities Bill*, N.Y. TIMES, Apr. 9, 1933, at N9 [hereinafter *Senators*]; Eustace Seligman, *Securities Bill Held Too Strict*, N.Y. TIMES, Apr. 1, 1933, at 23 [hereinafter Seligman]; *The Securities Bill Made Less Drastic; Conferees Ease Responsibility on Directors, Bar "Censorship" in Advertising;* N.Y. TIMES, May 17, 1933, at 25 [hereinafter *Securities Bill*].

90. *See* BRICKEY, *supra* note 11, § 3.09, at 115–18 (discussing case law upholding corporate convictions when individual agents were not convicted); John C. Coffee, Jr., *"No Soul to Damn, No Body to Kick": An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 MICH. L. REV. 386, 397–402 (1981) [hereinafter Coffee, *Unscandalized Inquiry*]; Jeffrey S. Parker & Raymond A. Atkins, *Did the Corporate Criminal Sentencing Guidelines Matter? Some Preliminary Empirical Observations*, 42 J.L. & ECON. 423, 441–43 (1999) [hereinafter Parker & Atkins]; Jeffrey S. Parker, *Doctrine for Destruction: The Case of Corporate Criminal Liability*, 17 MANAGERIAL & DEC. ECON. 381 (1996); Parker, *supra* note 7, at 399–400. The idea here is that the presence of corporate crime legislation reduces the cost of managerial criminal liability and makes it more acceptable (to managers

defendants (corporation and manager) we provide the decision maker (the judge or jury) with more options of who to hold accountable.[91] The decision maker may then decide to exercise this choice in favor of acquitting managers and convicting corporations.[92] This may be because the decision maker sympathizes with a managerial defendant (a real human being who has a family and can go to jail) more than with a corporate defendant which, of course, cannot go to jail.[93] Simply put, it provides the decision maker with a method of holding someone (the corporation) accountable for the wrongdoing without sending a real human to jail.[94] This option is not present when there is only one defendant. The choice there is to hold the manager accountable or no one at all. It is then plausible that fewer managers are being convicted when corporate criminal liability is available than when it is not. Does such liability deflection happen? If so, why would corporations not lobby against this?

There is anecdotal and empirical evidence suggesting that corporate criminal liability results in corporations bearing some of the blame that would otherwise be visited upon management. For example, there is case law discussing whether a corporate conviction can stand when all potentially liable agents have been acquitted.[95] The answer, perhaps

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and corporations) to enact. Managers are less opposed to this because they expect that there will be some insulation/deflection from liability.

91. *See* Coffee, *Unscandalized Inquiry*, *supra* note 90, at 397–402; Parker & Atkins, *supra* note 90, at 442–43 (providing some evidence that the presence of individual codefendants impacts the penalties imposed).

92. *See* BRICKEY, *supra* note 11, § 3.09, at 115–18.

93. *See id.*

94. Prosecutors and Congress would also like this result as the overall rate of conviction may rise, and convictions are important to prosecutors. *See* Glaeser et al., *supra* note 52, at 262–66 (discussing private career benefits from successful prosecutions); Gordon Van Kessel, *Adversary Excesses in the American Criminal Trial*, 67 NOTRE DAME L. REV. 403, 442 (1992) [hereinafter Van Kessel] (noting that "win-loss records can become an important mark of performance"); Hylton & Khanna, *supra* note 8, at 18–25; Stuntz, *supra* note 37, at 534. One may wonder if prosecutors would prefer to obtain a conviction of a real human being. Might that not be worth more than the conviction of a corporation? This is possible, but it depends on what prosecutors are trying to do. If obtaining convictions against management is more difficult than obtaining convictions against corporations, then prosecutors might not prefer to substitute a high-risk strategy (going after management) at the expense of getting a more certain conviction of a corporation. The fact that prosecutors do bring charges against both the corporation and the individuals (when deflection is a concern) suggests perhaps that prosecutors are willing to take the risk of trading off reduced convictions against individuals for an overall higher rate of conviction.

95. *See* BRICKEY, *supra* note 11, § 3.09, at 115–18 (discussing case law upholding corporate convictions when individual agents were not convicted); GRUNER, *supra* note 4, § 3.7.4, at 254–58 (same); Ann Foerschler, Comment, *Corporate Criminal Intent: Toward a Better Understanding of Corporate Misconduct*, 78 CAL. L. REV. 1287, 1290 (1990) (stating that "In a number of cases in which both were jointly tried for an offense, the jury convicted the corporate defendant and acquitted the individual defendants.").

surprisingly, is that the corporate conviction can stand.[96] Although the legal rationales for this result are interesting,[97] the important point for my analysis is that these cases arise in the first place. This implies that in some instances corporations are being held liable and managers acquitted. One conjectures that this is because juries may empathize more with human defendants than fictional ones. Alternative explanations are plausible too, but the presence of these cases raises the specter that managers were acquitted because, at least in part, the decision maker had an alternative defendant to hold liable—namely, the corporation (i.e., shareholders).[98]

There are also indications that the deflection account is a concern recognized by prosecutors. The Department of Justice's PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS states that "prosecutor[s] should be wary of attempts to shield corporate officers and employees from liability by a willingness of the corporation to plead guilty."[99] This concern may be one factor that has led prosecutors to reduce sanctions on (or not charge) corporations when they turn over information about potentially culpable agents.[100]

Moreover, there is some empirical evidence which is at least not inconsistent with a deflection thesis.[101] The evidence suggests that corporate and individual penalties are at least implicitly coordinated.[102] If such coordination does occur, that suggests that individual penalties

96. *See supra* note 95.

97. *See supra* note 95.

98. *See supra* note 95. *See also Developments*, *supra* note 11, at 1367–68 (highlighting the perception that corporations often are convicted while managers are acquitted). One might also view these outcomes as compromise verdicts.

99. LARRY D. THOMPSON, DEPUTY ATTORNEY GENERAL, MEMORANDUM ON PRINCIPLES OF FEDERAL PROSECUTION OF BUSINESS ORGANIZATIONS, Jan. 20, 2003 [hereinafter PRINCIPLES], Part VI, *available at* http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm. If these guidelines had their desired impact, then the deflection potential would be reduced and may reduce some support for corporate crime legislation by corporations and managers on this front.

100. *See* U.S. SENTENCING GUIDELINES § 8C2.5(g)(1) (2002) (stating that fines and/or sentences may be reduced for cooperation with the government), *available at* http://www.ussc.gov/2002guid/8c2_5.htm. (last visited Apr. 1, 2004); *see also* Win Swenson, Deputy General Counsel/Legislative Counsel, *The Organizational Guidelines' "Carrot and Stick" Philosophy, and Their Focus on Effective Compliance*, *at* http://www.ussc.gov/SYMPO/WCSYMPO1.HTM (the Deputy Director of USSG clarifies § 8C2.5(g)(1): "[v]oluntary disclosure and cooperation by a company mean, for example, that harms caused by the company *will* be rectified and individuals within the company *will* be identified and held accountable.") (emphasis in original); Laufer, *supra* note 6, at 648–52.

101. *See* Parker & Atkins, *supra* note 90, at 441–43.

102. *See id.* at 443. Direct data on the effects of a corporate co-defendant on the other defendants in corporate crime cases appears unavailable due to data constraints at the US Sentencing Commission. *Id.* at 430.

should drop with the presence of corporate co-defendants.[103] Thus, it is plausible that when management is the sole defendant, the likelihood and magnitude of managerial criminal sanctions are higher than the likelihood and magnitude of managerial criminal sanctions when there is another defendant (such as the corporation).[104] In other words, the deflection concern appears real.[105]

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103. *See id.* at 443. The evidence of coordinated penalties is consistent with individual penalties declining with the addition of a corporate co-defendant and also with corporate penalties declining with the addition of an individual co-defendant. This raises an interesting "chicken and egg" problem. Do we assume that the former account (individual defendant later joined by corporate defendant) or latter account (corporate defendant later joined by individual defendant) is the correct picture? If the former, then the deflection account in the text is at issue; if the latter, then a different kind of deflection account is offered—the corporation is avoiding criminal sanctions by shifting some of them to the individual. Both are plausible: the former account because it is the kind of deflection a corporation and management would both support (as it might reduce risk-bearing costs and hence wage bills—see discussion *infra* text accompanying notes 109–24). The latter is consistent with a reverse whistleblowing hypothesis where the corporation turns over employees (regardless of whether the employee "ratted out" was actually culpable or simply a scapegoat). *See infra* text accompanying notes 109–24. My goal is not to choose between these accounts because both are plausible; rather, my aim is to suggest that the deflection account is plausible.

104. *See* Parker & Atkins, *supra* note 90, at 442–43.

105. One may wonder about the significance of the deflection account given that the number of criminal prosecutions in the business sphere is rather small. *See* SENTENCING COMMISSION ANNUAL REPORT 2001, *supra* note 41; Alexander et al., *supra* note 41, at 403; First, *supra* note 41, at 3–5; Geraghty, *supra* note 41, at 338; Murphy, *supra* note 41, at 113; Rakoff, *supra* note 41, at 2; Davidson, *supra* note 41, at B3. To be clear, I am not suggesting that deflection is the *cause* of corporate crime legislation or enforcement—only that it may be another factor that softens the cost of corporate crime legislation for business interests when confronted with a Congress that is going to enact something.

On a separate note, over the last 30 years the rate of *civil* suits brought by government agencies has been increasing while criminal suits have stayed nearly constant. *See* Hughes, *supra* note 25, at 579–80; 587–89; Kenneth Mann, *Punitive Civil Sanctions: The Middleground Between Criminal and Civil Law*, 101 YALE L.J. 1795, 1798 (1992). The reasons for this are fairly simple: corporate civil liability offers the same penalties as and similar or better enforcement tools than corporate criminal liability, but at a lower standard of proof. This raises interesting questions about why prosecutors bring corporate criminal cases at all.

One explanation is that prosecutors consider certain cases particularly egregious and hence decide to pursue them criminally. However, if one casually looks at many corporate criminal prosecutions, it is not at all clear that the underlying behavior is all that egregious—sometimes it is and sometimes not. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1532. The evidence on corporate crime prosecutions at the federal level suggests that most prosecutions are against small distressed corporations which are rarely involved in very harmful wrongdoing and might be considerably easier convictions than targeting larger and more well-funded (and -defended) publicly traded corporations. *See* SENTENCING COMMISSION ANNUAL REPORT 2001, *supra* note 41; First, *supra* note 41, at 4–8; Davidson, *supra* note 41, at B3; Geraghty, *supra* note 41, at 338; Murphy, *supra* note 41, at 113; Rakoff, *supra* note 41, at 2.

Other explanations also abound, such as that prosecutors are actually interested in these cases (e.g., they are interested in acquiring human capital in this field). *See* Glaeser et al., *supra* note 52, at 261; Richard T. Boylan & Cheryl X. Long, *The Sources of Agency: An Empirical Examination of United States Attorneys* 25–27 (Draft paper 1999, on file with author) [hereinafter Boylan & Long]. Although plausible, one expects that there are some constraints on how easily prosecutors can choose cases to simply pad their resumes. *See Delegation*, *supra* note 33, at 789–810 (suggesting some

Of course, I do not expect that deflection will occur all the time. For example, if managers are clearly guilty of wrongdoing and have caused serious harm, deflection is less likely to occur.[106] Juries are likely to place more blame squarely on management's shoulders in such cases.[107] Nonetheless, it is both plausible and likely that deflection occurs in a number of other instances.

If corporations sometimes bear the blame for management behavior because of corporate criminal liability then why might corporations not actively lobby against such liability? There are a couple of potential explanations for this: (1) this "scapegoating" does not hurt the corporation and (2) corporations are hurt but are stymied by agency costs.[108] Let us examine each one in turn.

Corporate criminal liability could arguably benefit corporations by shifting criminal liability from managers, who are poor risk-bearers, to corporations, who are better risk-bearers.[109] Managers are considered poor risk-bearers because they cannot diversify their investment in the corporation (largely human capital, which is allocated to a single firm) as easily as shareholders can diversify their investment in the corporation (largely monetary capital, which can be reallocated to multiple firms).[110] Consequently, managers need to be compensated more than shareholders for bearing risk (i.e., a risk premium reflected in a higher wage), which may lead corporations (i.e., shareholders) to prefer to bear the risk themselves to reduce their wage bills.[111] Corporations could do this in civil

constraints on prosecutors through, for example, budgetary allocation). It is not clear that any of these motivations would correlate with bringing criminal prosecutions against corporations when it is in the public interest (if ever).

106. One presumes juries would be less sympathetic in such a case than when managers are not clearly culpable and where the harm appears to be small. *Cf.* BRICKEY, *supra* note 11, § 3.09, at 115–18.

107. Further, when the corporation is the victim of the wrongdoing (e.g., embezzlement), deflection is less likely to occur because juries may not wish to convict the victim (i.e., the corporation). Corporations may presumably also be more likely to turn over an agent to authorities in such a situation.

108. Of course, if the costs of this "scapegoating" are small, then it may not pay for corporations to spend resources to oppose it. *Cf. generally* Jennifer Arlen & Deborah M. Weiss, *A Political Theory of Corporate Taxation*, 105 YALE L.J. 326 (1995) [hereinafter Arlen & Weiss].

109. *See* Reinier H. Kraakman, *Corporate Liability Strategies and the Costs of Legal Controls*, 93 YALE L.J. 857, 864–67 (1984) [hereinafter Kraakman].

110. *See id.*

111. *See* Polinsky & Shavell, *supra* note 75, at 241. The recent increases in penalties under Sarbanes-Oxley appear to have led to increases in directors' and officers' insurance and to increases in compensation packages for independent directors. *See* Richard A. Epstein, *Sarbanes Overdose Law and Economics*, NAT'L L.J., Jan. 27, 2003, at A17. *See also* John C. Coffee, Jr., *Shareholders Versus Managers: The Strain in the Corporate Web*, 85 MICH. L. REV. 1, 18–19 (1986) (noting that

liability regimes by paying for insurance or indemnification of corporate agents, thereby shifting the risk of liability to themselves.[112]

The risk of criminal sanctions is just another risk that managers bear poorly and a risk for which they need to be, at least implicitly, compensated through something like a higher wage.[113] Thus, corporations may prefer to reduce their wage bills by shifting some criminal liability away from managers, but criminal sanctions on managers (especially jail) are often difficult to indemnify explicitly or insure against.[114] This is where corporate criminal liability might be desirable to corporations: it permits them to shift some liability away from management (and onto themselves), thereby reducing their wage bill.[115]

To elaborate, let us consider the following example. Assume that managers face a criminal fine of $100 for some wrongdoing with a 20% probability when there is no corporate criminal liability.[116] This means they face an expected sanction of $20 and also have risk-bearing costs associated with facing the risk of criminal penalties. Let us say these risk-bearing costs amount to an additional $8 (i.e., for every $5 in expected liability, a $2 risk-bearing cost). This implies that the cost to managers is $28, and this would, in some measure, be reflected in the wages paid to them.[117] This higher wage would be borne by the corporation, and in this sense, the corporation bears the costs of managerial criminal liability.[118]

Now consider the alternative of where both corporations and managers can be held criminally liable. In such a scenario assume that the corporation bears the $100 criminal fine 15% of the time, and managers bear it only 5% of the time (due to liability deflection to corporations). Here the cost to the corporation is the 15% of the time it is held liable and

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corporations end up paying, in the form of higher compensation, for the costs associated with the risk of liability that managers bear).

112. *See* WILLIAM T. ALLEN & REINIER H. KRAAKMAN, COMMENTARIES AND CASES ON THE LAW OF BUSINESS ORGANIZATIONS 242, 243–48, 254–55 (2003) (discussing indemnification and insurance in the context of breaches of fiduciary duty).

113. *See* Polinsky & Shavell, *supra* note 75, at 241. Also, to the extent that some of the loss suffered by management is in the form of stigma it would be difficult to insure against.

114. *See* 2 WILLIAM E. KNEPPER & DAN A. BAILEY, LIABILITY OF CORPORATE OFFICERS & DIRECTORS 446 (6th ed. 1998) [hereinafter KNEPPER & BAILEY].

115. *See* Polinsky & Shavell, *supra* note 75, at 241. This aspect of corporate criminal liability would be even more desirable to corporations if they thought there was over-criminalization of what, in their view, is profit enhancing behavior. For the notion that there is over-criminalization, see, e.g., Coffee, *Reflections*, *supra* note 4, at 210–13; Paul H. Robinson & John M. Darley, *The Utility of Desert*, 91 NW. U. L. REV. 453, 470 (1997) [hereinafter Robinson & Darley].

116. For now I assume this is for some mix of their intentional and unintentional wrongdoing.

117. *See* Polinsky & Shavell, *supra* note 75, at 241.

118. *See id.*

the wage increase to management to reflect the 5% risk of criminal liability.[119] The expected sanctions are then $15 on the corporation and $5 on managers. We are then left with risk-bearing costs. The corporation is normally assumed to be risk-neutral because shareholders can diversify their investment in the corporation, and this suggests they bear little additional cost above the $15 expected sanction.[120] Managers, on the other hand, bear risk poorly and would face some risk-bearing costs.[121] However, managers bear a lesser risk of criminal penalties here than when there is no corporate criminal liability. Thus, their risk-bearing costs should be less and I assume for now that these costs are only $2.[122] This suggests that managers bear costs of $7 ($5 plus $2) and the corporation $15 for a total of $22. This is less than the total costs when there is no corporate criminal liability ($28 in this hypothetical). Because the corporation is paying managerial wages and in effect bearing the cost of these liability regimes, it would prefer the lower total cost option.[123] In other words, here corporations prefer corporate criminal liability.[124]

Finally, even if deflection leads to greater costs for corporations, they may still not lobby against corporate crime legislation because of agency

119. *Cf. id.*

120. *See id.*

121. *See* Kraakman, *supra* note 109, at 864–67.

122. I have assumed that risk-bearing costs decrease linearly. That is, if a $20 expected sanction generated risk bearing costs of $8, then a $5 expected sanction should generate a proportionally smaller amount of risk-bearing costs. Because $5 is 25% of $20, I have assumed risk-bearing costs are 25% of $8 or simply $2. This assumption is for simplicity—all that is required is some decrease in risk-bearing costs.

123. *Cf.* Polinsky & Shavell, *supra* note 75, at 241. The corporation may even find it in its interest to subject itself to an overall greater likelihood of conviction to obtain this risk-shifting. The corporation may bear an overall greater likelihood of liability in two ways. First, when there are two defendants (corporation and managers), the overall conviction rate is higher. This means that it is possible that the corporation could be convicted 20% of the time (instead of 15% as in the text), and management could also be convicted 5% of the time—the corporation and associated parties would then bear a greater overall likelihood of conviction (25% of the time). Another way in which corporate liability could increase is that shifting liability away from managers for intentional wrongdoing creates a moral hazard (*see infra* text accompanying notes 175–78 and accompanying text), which could lead to more managerial wrongdoing and hence more frequent instances of harm, which should lead to increased suits against corporations. It is possible that these costs might be worth the reduction in managerial risk-bearing costs in some instances.

It is also noteworthy that corporate criminal liability's deflection effect *cannot* be replicated by corporate civil liability because a corporation facing only civil liability is not available in the criminal proceedings against the manager as an alternative defendant to convict. Also, one could argue that the liability-shifting feature of corporate criminal liability could be achieved by permitting insurance or indemnification of managerial criminal liability. I doubt this would occur, as insurers (and those who might indemnify or oversee indemnification) are unlikely to offer this for intentional or knowing wrongdoing (the kind most likely at issue here) due to moral hazard concerns. *See infra* notes 175–78 and accompanying text.

124. The reasoning here can be used to support the analysis in Part III.F.

costs.[125] This is because corporations cannot lobby by themselves—it is managers and other agents who lobby on behalf of corporations.[126] However, managers have an incentive not to make the corporation lobby against corporate criminal liability because the presence of corporate criminal liability may benefit managers via deflection of criminal liability, which is difficult to fully shift or insure.[127] Agency costs may then prevent corporations from actively lobbying against corporate criminal liability.[128]

V. INTERESTS OF OTHER PLAYERS

Thus far, I have discussed the likely interests of corporate players, but there are other important players too, such as the general public, victims of crime, Congress, prosecutors, courts, and potential defendants. My analysis suggests that their incentives also push towards broader criminalization.

A. General Public and Victims of Corporate Crime

The general public and victims of corporate crime are important because their desire for punishment, especially of the criminal variety, factors into the decisions of the primary players.[129] However, because the general public and victims often may not be familiar with the details of the corporate criminal law and may suffer from collective action problems, one would not expect them to monitor closely the laws and rules promulgated by legislators.[130] Nonetheless, one can treat the desires of the

125. *Cf.* Arlen & Weiss, *supra* note 108, at 341–43.

126. *Cf. id.*

127. *See id.* For the difficulty in insuring such behavior, see KNEPPER & BAILEY, *supra* note 114, at 446.

128. Further support for this can be gleaned from the PRINCIPLES, *supra* note 99, at 9–10 (suggesting that prosecutors be “wary” of corporate pleas that work to shield individuals within the corporation from criminal liability).

In addition to this, there is evidence that corporate interests have lobbied to reduce managerial liability in certain instances while leaving corporate criminal liability essentially untouched. For example, when the federal securities laws were enacted, the early drafts of the laws had much greater liability for directors of corporations, but that was pared back after extensive criticism and lobbying. *See* Seligman, *supra* note 89, at 23; *Attacks*, *supra* note 89, at 29; Davis, *supra* note 89, at 14; *Merchants Protest*, *supra* note 89, at 3; *Senators*, *supra* note 89, at N9; *Securities Bill*, *supra* note 89, at 25.

129. *See* Stuntz, *supra* note 37, at 523–27.

130. *See id.* at 530. For a classic discussion of collective action, see MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION: PUBLIC GOODS AND THE THEORY OF GROUPS (1965). *See also* RUSSELL HARDIN, COLLECTIVE ACTION (1982). One also would not expect large groups with disaggregated constituents to lobby that effectively. *See* JACK L. WALKER, JR., MOBILIZING INTEREST GROUPS IN AMERICA: PATRONS, PROFESSIONS, AND SOCIAL MOVEMENTS 66 (1991). *See also* David M. Hart,

general public and victims as creating the boundaries within which the primary players engage in their behavior.[131]

B. Congress & Legislators

Next, let us consider the interests of the primary promulgators of the criminal law: Congress and state legislatures. Presumably, legislators would like to remain in power or potentially rise to higher office.[132] For that to happen they need to please their constituents.[133] Most voters appear to care deeply about crime and criminal legislation but suffer from the collective action problems described above.[134] Thus, voters tend to focus more on the *outcomes* of the criminal process (i.e., convictions) rather than specific rules, and they may pay more attention to the information conveyed through intermediaries (e.g., television news shows) than to the entrails of the law.[135] For example, voters may like to see more convictions, which could be achieved by tightening criminal liability rules to make it easier to obtain a conviction or increasing sanctions because that increases the threat value of trial, thereby making it easier to obtain guilty pleas.[136] Voters may also like to know that something is being done about certain behavior that concerns them.[137] The legislature could create

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Business Is Not an Interest Group (And, By the Way, There's No Such Thing as "Business"): On the Study of Companies in American National Politics (Draft Paper 2002, on file with author); David M. Hart, *Political Representation Among Dominant Firms: Revisiting the "Olsonian Hypothesis"* (Oct. 2002), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=357540. On lobbying activities of corporations, see generally John M. de Figueiredo, *Lobbying and Information in Politics*, Discussion Paper No. 369, John M. Olin Center for Law, Economics & Business, Harvard Law School 2002, *available at* http://www.law.harvard.edu/programs/olin_center; John M. de Figueiredo & Rui J.P. de Figueiredo, Jr., *The Allocation of Resources by Interest Groups: Lobbying, Litigation and Administrative Regulation* (Draft Paper 2002, on file with author); John M. de Figueiredo & Emerson H. Tiller, *The Structure and Conduct of Corporate Lobbying: How Firms Lobby the Federal Communications Commission*, (2000), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id =263302; Stephen Ansolabehere, John M. de Figueiredo, & James M. Synder, *Are Campaign Contributions Investment in the Political Marketplace or Individual Consumption? Or "Why Is There So Little Money in Politics"* (Draft Paper 2002, on file with author).

131. *See* Stuntz, *supra* note 37, at 530.

132. *See id.* at 529. I do not mean to suggest that legislators do not (or could not) have altruistic or public interest ideals—only that an important goal of legislators is to remain or move up in office. This is a fairly standard assumption in the public choice literature. *See, e.g.*, J. Mark Ramseyer, *Public Choice*, *in* CHICAGO LECTURES IN LAW & ECONOMICS 101–02 (Eric Posner ed., 2000). Also, staying in office may be an important way of achieving the public interest or altruistic goals that some legislators may possess.

133. *See* Stuntz, *supra* note 37, at 529.

134. *See id.*

135. *See id.* at 530.

136. *See id.* at 537.

137. *See id*. at 529.

new crimes that may not really change underlying behavior but may give voters a sense of security that "something is being done."[138] Professor Stuntz provides an example of such a symbolic measure: when Congress criminalized "carjacking" even though there were several other criminal provisions that already covered it.[139]

C. Prosecutors

The next important institutional player is the prosecutor. In most jurisdictions prosecutors are elected, whereas in others they are appointed.[140] The elected prosecutors are in a similar position to elected legislators—for them to keep their jobs and rise to higher office they need to satisfy voters.[141] This essentially means they need to bring prosecutions in the cases the public wants to see prosecuted.[142] Appointed prosecutors face somewhat similar pressures, depending on what they would like to do. If some would like to run for elected office, then clearly they will need to bring prosecutions in cases that the general public strongly desires. If some would prefer to move to higher appointed office, then they will need to do things that provide the "appointers" with a reason to select them for that office.[143] This may involve a number of things, but it will almost

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138. *See id.* at 530.

139. *See id.* at 560.

140. *See id.* at 533.

141. *See id. See also* Glaeser et al., *supra* note 52, at 262–66. To this point I have spoken only of federal prosecutors, who are not generally elected. I include discussion of elected prosecutors because the effect of their likely interests on corporate crime legislation is similar to that of non-elected prosecutors.

142. *See* Glaeser et al., *supra* note 52, at 261 (noting that decisions to prosecute are often influenced by prosecutors' interest in running for higher office); Peter Krug, *Prosecutorial Discretion and Its Limits*, 50 AM. J. COMP. LAW 643, 662 (2002) (noting that police misconduct prosecution occurs only in high cases of public visibility); Stuntz, *supra* note 37, at 533 (noting that "local prosecutors are likely to seek to produce the range of outcomes the public desires").

143. *See* Glaeser et al., *supra* note 52, at 262–66 (discussing private career benefits from successful prosecutions). *See also* John C. Coates IV, *Private vs. Political Choice of Securities Regulation: A Political Cost/Benefit Analysis*, 41 VA. J. INT'L L. 531, 561 (2001) [hereinafter Coates] (explaining the actions of appointed SEC commissioners); Ramseyer & Rasmusen, *supra* note 54, at 71–72 (discussing incentives for Japanese prosecutors and judges and how these incentives, along with a tight budget constraint on prosecutors, work to ensure high conviction rates); Van Kessel, *supra* note 94, at 442 (noting that "win-loss records can become an important mark of performance").

Prosecutors could be trying to maximize many different things (e.g., sentences, convictions, publicity, human capital). *See* Frank H. Easterbrook, *Criminal Procedure as a Market System*, 12 J. LEGAL STUD. 289, 301 (1983) (noting that career prospects and reputation may impact the exercise of prosecutorial discretion); Glaeser et al., *supra* note 52, at 266–88 (noting that prosecutors are motivated at least in part by career growth prospects and providing empirical evidence to that effect); William M. Landes, *An Economic Analysis of the Courts*, 14 J. L. & ECON. 61, 63–64 (1971) (treating prosecutor's utility as being composed of maximizing expected sentence lengths subject to a budget certainly involve bringing prosecutions in most cases that the general public desires.[144] Further, both kinds of prosecutors would presumably have strong desires to win these cases. This is because the public desires not simply prosecutions but also convictions, and because prosecutors personally benefit from winning suits.[145]

At the same time, line prosecutors (not elected or appointed, but rather "hired" prosecutors) would like rules that do not tremendously increase their own workload yet generate convictions.[146] These last two concerns—to increase convictions for all prosecutors, but not to increase workloads for line prosecutors—might seem to run counter to each other, but they need not. Prosecutors can obtain both goals if the criminal law applies to a wide range of behavior because then prosecutors have great latitude in bringing cases the public desires.[147] They are also more likely to obtain some kind of conviction, as there are so many crimes with which the defendant might be charged.[148] Further, the breadth of the criminal law helps to reduce prosecutorial workloads.[149] With many crimes applying to essentially the same behavior, the prosecutor could charge all the crimes in one trial and thereby increase the expected sanction the defendant faces from going to trial.[150] This makes going to trial less attractive to the defendant and should induce guilty pleas.[151] A guilty plea generates less work for prosecutors than trials, yet still results in convictions of some kind.[152] Moreover, even those prosecutors who are interested in entering private practice after their stints in the prosecutor's office would prefer broader criminal law, because increased breadth would provide them with

constraint); *Agents*, *supra* note 38, at 754; Boylan & Long, *supra* note 105, at 25–27 (finding with empirical support that Assistant U.S. Attorneys are often motivated by human capital concerns). Instead of specifying a prosecutorial utility function, I focus on what might be needed by prosecutors to achieve whatever their ends may be. One expects that bringing cases the public desires and obtaining convictions would be useful to most motivations prosecutors may have. *See* William T. Pizzi, *Understanding Procedural Discretion in the United States: The Limits of Comparative Criminal Procedure as an Instrument of Reform*, 54 OHIO ST. L.J. 1325, 1338 (1993) (stating that "prosecutorial decisions in the United States are 'susceptible to political influences'"); Stuntz, *supra* note 37, at 533 (wishing to keep their jobs, or move up to higher offices, prosecutors' "incentives [are] to generate the level and distribution of prosecutions that the public wants").

144. *See* Coates, *supra* note 143, at 561 (noting that "[t]o pass . . . political muster, appointees are screened to respond to the political preferences of voters"); Stuntz, *supra* note 37, at 533–39.

145. *See* Hylton & Khanna, *supra* note 8, at 18–25; Stuntz, *supra* note 37, at 534.

146. *See* Stuntz, *supra* note 37, at 535.

147. *See id.* at 537–38.

148. *See id.* at 537.

149. *See id.*

150. *See id.*

151. *See id.* at 538.

152. *See id.* at 537.

more opportunities to develop expertise and human capital and become thereby more valuable in their future private practice.[153] Consequently, if prosecutors were to lobby legislators, we would expect them to want broader criminalization because that increases the flexibility of prosecutors' response to public desires, makes it easier to obtain some kind of conviction, helps to build human capital, and makes it easier to obtain guilty pleas (thereby reducing workloads).[154]

Of course, broader criminal law provisions may result in criminalization of innocuous behavior and in a negative reaction by the polity (e.g., Prohibition).[155] However, this concern is muted in the American criminal justice system by prosecutorial discretion. Prosecutors need not prosecute *every* case that presents a potential violation of the criminal law.[156] Further, given the desire of most prosecutors to bring suits that the public desires, we might expect that few prosecutions would deeply offend public sensibilities.[157]

Furthermore, this also suggests that Congress is insulated in some respects from the costs of over-criminalizing behavior because prosecutors will rarely bring unpopular cases.[158] When they do, the general public is more likely to lay blame at the feet of the prosecutor.[159] Consequently, one would expect that Congress would prefer to err on the side of over-criminalizing (which has little cost given prosecutorial discretion) rather

153. On prosecutors' incentives to enter private practice, see generally Glaeser et al., *supra* note 52, at 266–88 (noting that prosecutors are motivated at least in part by career growth prospects, and providing empirical evidence to that effect); Boylan & Long, *supra* note 105, at 25–27 (finding with empirical support that Assistant U.S. Attorneys are often motivated by human capital concerns).

154. *See* Stuntz, *supra* note 37, at 537–38. The investigatory agencies (e.g., the FBI) may have interests that push in the same direction as line prosecutors. More criminalization increases the investigatory agencies' ability to conduct their investigations and may help reduce the work they need to do to gather evidence. *Cf. Agents*, *supra* note 38, at 767–72 (noting that agencies are pressured to devote resources to successful investigations and prosecutors, who are also motivated to obtain convictions, can influence the agencies' decision-making regarding which cases to pursue). Prosecutors prefer fewer cases or easier ones, while legislatures prefer easier ones. *See id.* If they are able to simultaneously keep their conviction rates up, all prosecutors (elected and line prosecutors) are likely to want to reduce their workloads. *See id.*

155. Revulsion towards the passage of Prohibition led to a repeal a mere 14 years later. *See* MARK THORNTON, THE ECONOMICS OF PROHIBITION (1991). *See also* Jonathan Barnett, *The Rational Underenforcement of Vice Laws*, 54 RUTGERS L. REV. 423, 433–35 (2002); Donald J. Boudreaux & A.C. Pritchard, *The Price of Prohibition*, 36 ARIZ. L. REV. 1 (1994) (discussing how revenue generated by the tax system had a pivotal impact on the enactment and repeal of prohibition); Gerald E. Lynch, *The Role of Criminal Law in Policing Corporate Misconduct*, 60 LAW & CONTEMP. PROB. 23, 48 (1997).

156. *See* Stuntz, *supra* note 37, at 548.

157. *See id.*

158. *See id.*

159. *See id.*

than under-criminalizing or in spending resources to define the limits of the criminal law.[160]

Thus, the combination of the incentives of legislators and prosecutors, along with prosecutorial discretion, suggests that corporate criminal law and criminal law generally should be skewed towards expansion over time.[161] That is precisely what we witness.

D. Judges

One might inquire whether judges are able to apply the metaphorical "brakes" on this process as they may presumably be less subject to the winds of public opinion.[162] After all, many judges are not elected and are rarely blamed for a prosecution not leading to a conviction. Instead, the blame tends to fall on the prosecutor.[163] Further, the esteem and culture of the judicial profession may provide judges with some incentive to curtail overly aggressive criminalization.[164] In theory this might be the case, but in reality the structure of the criminal justice system urges against this. First, judges do not often get to determine which cases they will adjudicate.[165] If cases plea out, as most do, then those cases are rarely subjected to serious judicial scrutiny.[166] Further, the expansion of criminal statutes may tend to constrain the role of the courts because it reduces law creation opportunities.[167] Finally, judicial doctrines such as vagueness, double jeopardy, and lenity are less effective when there are many fairly

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160. *See id.* at 548–49. Even where legislatures have sought to limit discretion, prosecutors have been able to increase their bargaining power. *See, e.g.*, Daniel P. Kessler & Anne M. Piehl, *The Role of Discretion in the Criminal Justice System*, 14 J.L. ECON. & ORG. 256 (1998) (noting that replacing indeterminate sentencing laws with determinative sentencing laws has increased prosecutorial bargaining power not only for the specific crime but also factually similar crimes).

161. *See* Stuntz, *supra* note 37, at 546–57. *See also* Phillip Pettit, *Is Political Justice Politically Feasible?*, 5 BUFF. CRIM. L. REV. 427, 430 (2002) [hereinafter Pettit] (noting the powerful role that popular sentiment plays in the expansion of the law in well-publicized types of crime, in our case corporate crime).

162. *See* Stuntz, *supra* note 37, at 541.

163. *See id.* at 540.

164. *See id.* at 541.

165. *See id.*

166. *See id.* at 567. Furthermore, judges might have other reasons for not aggressively patrolling the boundaries of the criminal law. For example, judges would probably not like to be reversed. *See id.* at 541. If so, and if the criminal law is seen as having enough support that it could lead to legislation overturning the judicial outcome, then judges might be cautious in overturning such laws. *See id.* at 542.

167. *See id.* at 565.

precisely written criminal statutes.[168] Thus, even the judges may not halt the trend toward increased criminalization.

Corporate crime legislation then appears to be a method of satisfying public desires along with congressional and prosecutorial incentives at relatively low cost to corporate interests and within the constraints imposed by the lobbying activities of management and corporations. Thus, the growth of corporate criminal liability may be understandable from a political perspective, but what normative consequences follow?[169]

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168. *See id.* at 528.

169. I have not discussed the case of the "street" criminal because the focus of this paper is corporate crime legislation. Nonetheless, there do not appear to be too many private interest groups that pipe up in support of the average street criminal or to constrain the breadth of criminalization. Most interest groups in the street crime context appear to target issues of criminal procedure, death penalty issues, and errors in judicial proceedings (e.g., erroneous convictions) rather than over-criminalization. For example, the American Civil Liberties Union (ACLU) tends to favor changes in criminal procedural rules (*see* ACLU Webpage, *at* http://www.aclu.org/CriminalJustice/CriminalJusticeMain.cfm), which may not be that difficult to work around for prosecutors given the breadth of criminal law. *See* William J. Stuntz, *The Uneasy Relationship Between Criminal Procedure and Criminal Justice*, 107 YALE L.J. 1, 26, 28–29 (1997) (noting that, although these constitutional protections favor the defendant, there is still much discretionary power left with a prosecutor); Kessler & Piehl, *supra* note 160. Families Against Mandatory Minimums (FAMM) is a national, non-profit organization composed of prisoners and their families that challenges mandatory minimum sentencing standards (not over-criminalization per se). FAMM, WHAT IS FAMM?, *at* http://www.famm.org/pdfs/fedbroch2.pdf. There are academics who argue against the trend to over-criminalize, but I am not treating them as a "private interest group" in the sense that the phrase is usually used. *See generally* HERBERT L. PACKER, THE LIMITS OF THE CRIMINAL SANCTION 249–364 (1968); Coffee, *supra* note 4, at 234–38 (noting that the development of federal criminal law blurs the line between civil and criminal law, resulting in injustice); Stanford H. Kadish, *Some Observations on the Use of Criminal Sanctions to Enforce Economic Regulations*, 30 U. CHI. L. REV. 423 (1963); Stuntz, *supra* note 37, at 555.

One might query: why are there so few interest groups that lobby against over-criminalization? This may be due to perceptions that those who lobby against criminalization are likely either to stigmatize themselves or identify themselves as potential wrongdoers. *See Delegation*, *supra* note 33, at 776; Stuntz, *supra* note 37, at 555. Moreover, given prosecutorial discretion, we should not expect too many sympathetic defendants with which to lobby against over-criminalization. *See* Stuntz, *supra* note 37, at 555.

Furthermore, the putative "criminals" themselves are unlikely to have the resources and social capital needed to lobby for less restrictive criminal laws. *See* Dennis E. Curtis & Judith Resnik, *Colloquium: What Does it Mean to Practice Law "In the Interests of Justice" in the Twentieth-Century?: Grieving Criminal Defense Lawyers*, 70 FORDHAM L. REV. 1615, 1618 (2002) (noting that "criminal defendants have no powerful lobby at either the state or federal level"); Donald A. Dripps, *Criminal Procedure, Footnote Four, and the Theory of Public Choice*, 44 SYRACUSE L. REV. 1079, 1081 (1993) (arguing that "public choice theory suggests that an overwhelming preponderance of political incentives favor unrestricted enforcement of the criminal law"). Criminal defendants do, however, benefit from criminal defense attorney lobby groups such as the National Association of Criminal Defense Lawyers. *See* NACDL, WEBPAGE, *at* http://www.criminaljustice.org. The defense attorney lobby concentrates its efforts on increased funding of public defense, defending attorney-client privilege, and abolishing the death penalty, rather than over-criminalization. It should be noted that not all potential defendants are powerless. The National Rifle Association has successfully blocked a number of attempts to federalize various gun crimes. For example, an effort to close the

VI. Normative Concerns Associated with Corporate Crime Legislation

The analysis in this paper raises interesting normative questions and my discussion in this Part sketches my early thoughts on them. I argue that the normative implications of the substitution accounts depend both on the account relied upon and on one's prior beliefs about the state of the world. For example, let us assume that we believe that corporate crime legislation leads to deflection of liability away from management. Is this normatively good or bad for society? To answer this question, let us consider the following example.

Let us assume that to appropriately deter certain corporate wrongdoing we need to impose a penalty of $5 million in total on the various corporate participants. Further, it does not matter how liability is partitioned between managers and the corporation if they can bargain cheaply amongst themselves.[170] This is because when bargaining is easy (i.e., transaction costs are low) the parties bargain for the socially desirable sharing of liability—this is a simple application of the Coase Theorem.[171]

However, in reality, transaction costs are rarely zero and there is much evidence that suggests that bargaining between management and the corporation is rarely conducted in an "arm's length" manner.[172] In light of this, where we impose liability does matter because that is where liability is likely to rest. Consequently, we might prefer to place the lion's share of liability on the corporation rather than the manager. This is because corporations (i.e., shareholders) are generally considered better risk-bearers than managers for the reasons discussed earlier.[173] Further, given that society might like to reduce the costs associated with risk-bearing, placing liability on the better risk-bearer might be the preferred option, and deflection helps to facilitate this.[174]

"gun show loophole" (allowing purchasers to buy guns at gun shows without a background check) was defeated in the House. *See* H.R. Res. 249, 106th Cong. (1999).

170. *See* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 34–35 (1996).

171. This is an application of the Coase Theorem. *See* R.H. Coase, *The Problem of Social Cost*, 3 J.L. ECON. 1 *passim* (1960).

172. *See, e.g.*, Lucian Arye Bebchuk, Jesse M. Fried, & David I. Walker, *Managerial Power and Rent Extraction in the Design of Executive Compensation*, 69 U. CHI. L. REV. 751, 764–74 (2002). I have assumed that the liability is shifted from managers to corporations. If we are dealing with a non-management agent, then the contracting concerns might not be as large as when dealing with a management agent.

173. *See* Kraakman, *supra* note 109, at 864–65.

174. I assume that reducing risk-bearing costs is something that is socially desirable. *See, e.g.*, Polinsky & Shavell, *supra* note 75, at 240–41.

This account appears quite convincing for reducing risk-bearing costs of *unintentional* wrongdoing, but it is not so clear that the same holds for the *intentional* or *knowing* behavior of management.[175] The reason is a familiar one from the insurance literature. Insurance companies do not provide coverage for an insured's knowing or intentional behavior because then the insured would have an incentive to engage in the behavior in order to collect the insurance payout (i.e., a moral hazard).[176] Analogous moral hazard problems might arise if we shifted liability for management's *knowing* wrongdoing away from management and on to corporations when bargaining is difficult.[177] This would in effect make the corporation an insurer for the knowing wrongdoing committed by management, thereby reducing management's incentive not to engage in wrongdoing. Thus, when under-deterrence is a concern, deflection of liability for knowing wrongdoing worsens the situation.[178]

The question is then whether liability is being shifted for unintentional wrongdoing or intentional/knowing wrongdoing by management. In the managerial criminal liability area there are instances of both kinds of wrongdoing,[179] but as a general matter courts tend to require a showing of some mens rea before imposing criminal liability on an individual.[180] Thus, it is plausible that, if criminal liability is being shifted from management to the corporation due to corporate criminal liability, then it may be shifted for intentional or knowing wrongdoing.

Of course, a counter-argument would be to argue that there is too much regulation and criminalization in the business sphere to begin with (i.e.,

175. Where the wrongdoing is unintentional, management will evade liability by means of the business judgment rule. *See* Litwin v. Allen, 25 N.Y.S.2d 667 (Sup. Ct. 1940) (holding that management will be insulated provided that there is no showing of egregious carelessness). *See also* Joseph Sanders et al., *Distributing Responsibility for Wrongdoing Inside Corporate Hierarchies: Public Judgments in Three Societies*, 21 L. & SOC. INQ. 815, 838–39 (1996).

176. *See, e.g.*, KENNETH S. ABRAHAM, DISTRIBUTING RISK: INSURANCE, LEGAL THEORY, AND PUBLIC POLICY 14–16 (1986) [hereinafter ABRAHAM]; ROBERT E. KEETON & ALAN I. WIDISS, INSURANCE LAW 14–15 (1988) [hereinafter KEETON & WIDISS]. Standard issues that might be implicated here are moral hazard and adverse selection. Moral hazard describes an insured individual's potentially decreased incentive to avoid covered costs as well as to mitigate those costs, given that the individual knows that the injury will be covered by insurance. This can potentially lead to higher claim activity and under-deterrence of the group. Adverse selection occurs when higher-risk individuals, aware of their situation, purchase insurance, while at the same time, lower-risk people do not opt for coverage. This occurrence throws off the insurance company's determination of the risk characteristics of a group and leads to more claims than the group, as a whole, would normally produce.

177. *See* ABRAHAM, *supra* note 176, at 14–16; KEETON & WIDISS, *supra* note 176, at 14–15.

178. *Cf.* Khanna, *Top Management*, *supra* note 6, at 1253–55; Coffee, *Unscandalized Inquiry*, *supra* note 90, at 408.

179. *See Developments*, *supra* note 11, at 1259–75.

180. *See id. See* BRICKEY, *supra* note 11, at 15, 81–84 tbl.1.

over-deterrence),[181] and thus liability shifting for intentional "crimes" is desirable because it reduces risk-bearing for things that should not have been "crimes" in the first place. My interest is not in debating which particular state of the world (over- or under-deterrence) is correct—my point is simply that the normative implications depend on one's beliefs about the state of the world. Thus, if we think over-deterrence of managerial behavior is a better description of reality, corporate criminal liability could be desirable if it reduces risk-bearing costs. However, if we think under-deterrence is more likely, then corporate criminal liability may impede deterrence by reducing the risk of liability on management for intentional or knowing wrongdoing.

Let us then consider the other substitution thesis: that corporate crime legislation operates as a substitute for enhancements in corporate civil liability. Here, once again, normative implications depend on one's starting point.

Let us assume that we believe over-deterrence (too much regulation and criminalization) is the problem. In such a case, corporate crime legislation might be treated as the more desirable result because, relative to increases in corporate civil liability, it is easier to constrain (given prosecutors' incentives and resources and budgetary lobbying) and imposes lower social costs. Simply put, corporate crime legislation may satisfy public desires without aggravating the over-deterrence problem as much as increases in corporate civil liability.[182]

On the other hand, under-deterrence leads to a somewhat different analysis. If we believe there is too little enforcement of laws regulating corporate wrongdoing, then an increase in corporate civil liability may be desirable because it may lead to more enforcement than corporate crime legislation. Thus, relying on corporate crime legislation as a substitute for increases in corporate civil liability may not strengthen deterrence as much.

This, however, is not the only effect. Because corporate crime enforcement is less likely to be frivolous than some private civil litigation under corporate civil liability, it is more likely to be used in meritorious cases. However, given that corporate civil liability is composed of both

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181. *Cf.* Fischel & Sykes, *supra* note 47, at 346–48.

182. *See Backlash*, *supra* note 8, at 240. For example, corporate criminal liability might have a lesser impact on deterrence than, say, repeal of the PSLRA. Note that from society's perspective reducing litigation (or targeting it more carefully) through corporate crime legislation would be better than increasing litigation through corporate civil liability when over-deterrence is assumed to be the case.

government enforcement and private litigation, it is likely to be more numerous and frequent. Thus, corporate criminal liability is probably a more precise tool, whereas corporate civil liability is more frequent. Is the more precise tool or the more frequent one better for deterrence? There is no simple answer because the deterrent effect of the law depends not only on the frequency of its enforcement, but also its accuracy.[183] One might think that increases in corporate civil liability are the better option, at present, because there have been measures undertaken that appeared to improve the quality of litigation (i.e., led to more meritorious suits), such as the PSLRA.[184]

The normative implications can be quite complex. What is clear, however, is that those who start from the a priori view that corporate wrongdoing is not sufficiently deterred at present may want to argue for curtailing corporate criminal liability and increasing the focus on corporate civil liability and managerial liability. For example, if we think the deflection account is accurate and that under-deterrence is a concern then we should want to reduce deflection. We might achieve this by making sure that criminal trials for managers and their corporations are separate. We might also exercise prosecutorial discretion carefully in bringing charges.[185] Similarly, those that believe corporate behavior is over-

183. *See* Forrest G. Alogna, *Double Jeopardy, Acquittal Appeals, and the Law-Fact Distinction*, 86 CORNELL L. REV. 1131, 1140 (2001) (arguing that "[g]reater accuracy decreases acquittals of guilty defendants. Public perceptions of inaccuracy and inconsistency in the legal system may lessen the deterrent effect of punishment"); Michal S. Gal, *Harmful Remedies: Optimal Reformation of Anticompetitive Contracts*, 22 CARDOZO L. REV. 91, 124 (2000) (noting that "[o]nce accuracy increases, the expected sanction for innocent acts disappears. This reduces the extent to which individuals are inefficiently induced to choose the act that does not subject them to the risk of sanctions, and thus stiffer sanctions and lower levels of enforcement can be adopted"); Louis Kaplow, *The Value of Accuracy in Adjudication: An Economic Analysis*, 23 J. LEGAL STUD. 307, 344–69 (1994) (discussing how and why accuracy is valuable in the context of liability determinations).

184. *See, e.g.*, Marilyn F. Johnson et al., *Do the Merits Matter More? Class Actions Under the Private Securities Litigation Reform Act*, Working Paper No. 02-011, John M. Olin Center for Law & Economics, University of Michigan Law School (Draft 2003), *available at* http://www.law.umich.edu/CentersAndPrograms/olin/abstracts/discussionpapers/2002/Johnson%20Nelson%20Pritchard%2002011.pdf (arguing that the overall quality of suits post-PSLRA has improved).

185. For example, we might bring charges in ways that the deflection potential is reduced and where obtaining information from corporations about its agents is beneficial. Let us assume that there is some probability that managers/agents can be convicted, and that probability increases and approaches one as we obtain more information from the corporation about its managers/agents (assuming they are not simply scapegoats). Here corporate liability (civil or criminal) might generate information about agents that could be beneficial to prosecutors. Further, if the prosecutor uses the information and initiates a case against the manager and does not charge the corporation (or settles relatively soon), then deflection is not a concern, as the jury/decision-maker would not have the choice of the corporation, the manager, neither nor both. Moreover, if a corporation is not charged, then the costs associated with criminal procedural protections (many of which apply at or near trial) are avoided. This provides one scenario in which prosecuting corporations may not be too undesirable at

deterred should favor increasing corporate criminal liability, in the assumed political climate, to avoid more costly measures. The counter-intuitive nature of many of these conclusions raises intriguing questions about whether it makes sense to regulate the business arena in the method we have.

Indeed, the analysis in this paper raises many further important and interesting questions that could form the bases of separate papers in their own rights. For example, might the analysis here shed some light on aspects of the development of corporate civil liability? Might corporate civil liability deflect civil liability away from management as corporate criminal liability might deflect criminal liability? Finally, what explains the fact that the U.S. is an outlier in terms of corporate crime legislation compared to the rest of the world? Most other developed nations either have no corporate criminal liability or have a more restricted form of it compared to the U.S.[186] The divergence on this issue is impressive and raises very interesting questions about why so much regulation in the U.S. takes a criminal form.[187] Further research into these issues would be very illuminating.

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present (unless we can obtain the information about the agent through the application of corporate civil liability at a similar cost).

Another instance is where managers are clearly criminally liable for something quite harmful. Here there is little fear of deflection and also little to be gained from obtaining information from the corporation. Further, the procedural protections for corporations raise few additional costs over pursuing corporate civil liability because those hurdles would have been cleared in pursuing a manager criminally.

Of course, the other extreme—when no manager/agent can be found liable—is not an instance for corporate criminal prosecution. Although deflection is not a great concern (ex hypothesi it is unlikely that any manager/agent could be held liable), there is little benefit from obtaining information from the corporation because managers are not likely, ex hypothesi, to be convicted. Moreover, the procedural protections would have an additional cost over corporate civil liability as we cannot "piggyback" off of any managerial conviction(s). Thus, when managers are clearly liable or can be made clearly liable by obtaining information from the corporation, then prosecuting a corporation criminally may not be too costly (in the short run). Is this what we witness? This would be an excellent topic for future research.

It is worth noting that no method of exercising prosecutorial discretion can avoid the loss associated with enacting corporate crime legislation instead of something that might be more beneficial to deterrence (e.g., increases in corporate civil liability or managerial liability).

186. *See id.* at 1488–91; Rafael La Porta et al., *What Works in Securities Laws?* 22 (Draft 2002, on file with author) [hereinafter La Porta et al.].

187. The "over-criminalization" in the U.S. is a matter that has been the subject of much scholarly writing. *See* Coffee, *Reflections*, *supra* note 4, at 210–13; Robinson & Darley, *supra* note 115, at 470; Stuntz, *supra* note 37, at 546–47. The divergence in approaches is particularly interesting, as the empirical evidence suggests that at least the criminal laws targeted to securities law violations do not appear to help in the development of well-functioning securities markets. *See* La Porta et al., *supra* note 186, at 28.

There are a few conjectures one might make about what could explain the difference in approaches amongst nations. One is that some countries, as a philosophical matter, reject the idea of vicarious criminal liability and hence would not countenance corporate criminal liability. For example,

VII. ALTERNATIVE EXPLANATIONS

In this last Part, I examine alternative explanations for the growth of corporate crime legislation and argue that they do not alter my analysis. Let us begin with a potential public choice account commonly seen in the regulation area: that corporate crime legislation may benefit some incumbent firms by raising the costs of entering or remaining in business (i.e., raising entry barriers to the market).[188] The incumbent firms that benefit from reduced competition would lobby for such corporate crime legislation.[189] Might this provide an explanation for the growth of corporate crime legislation? I doubt that this is the case.

First, as noted in Part III.A, corporate crime penalties are generally not very large and enforcement is infrequent.[190] This suggests that corporate criminal liability may not be a large cost to businesses.[191]

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in Germany and Italy, there is no corporate crime legislation because criminal "guilt" can not be found through vicarious liability for fictional entities. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1488–91 (discussing historical concerns behind this).

Another is that if corporate crime legislation is a substitute for other liability strategies (e.g., increases in corporate civil liability and managerial liability) then in countries with small amounts of these other strategies one would not expect much corporate crime legislation. Most other countries have less corporate civil liability and managerial liability than the U.S., and hence corporate crime legislation would have less to substitute for in these other countries. These are both plausible explanations for the divergent treatment we observe in different countries, but other factors may also be at play. These include other historical and political constraints, the greater prevalence of corporations in everyday life in the U.S., the degree to which entrepreneurial attorneys influence litigation and legislation, and so forth. Also, the degree to which the general populace is invested in the securities markets may also influence the vigilance of Congress in regulating the securities markets because problems in those markets are likely to influence many voters. *See* Pettit, *supra* note 161, at 430 (indicating that areas of law in the public light tend to experience change because public opinion stirs legal changes). These matters merit greater study and I am in the process of examining these issues in a separate project.

188. *See generally* GORDON TULLOCK, THE ECONOMICS OF SPECIAL PRIVILEGE AND RENT SEEKING (1989); DANIEL A. FARBER & PHILLIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION (1991).

189. *See* SUSAN M. PHILLIPS & J. RICHARD ZECHER, THE SEC AND THE PUBLIC INTEREST 22–25 (1981); Randall S. Kroszner & Thomas Stratmann, *Interest Group Competition and the Organization of Congress: Theory and Evidence from Financial Services Political Action Committees*, 88 AM. ECON. REV. 1163 (1998); Michael E. Levine & Jennifer L. Forrence, *Regulatory Capture, Public Interest, and the Public Agenda: Toward A Synthesis*, 6 J.L. ECON. & ORG. 167 (1990); Michael T. Maloney & Robert E. McCormic, *A Positive Theory of Environmental Quality Regulation*, 25 J.L. ECON. & ORG. 99, 100–06 (1982); Mahoney, *supra* note 41, at 20–21; Sharon Oster, *The Strategic use of Regulatory Investments by Industry Sub-Groups*, 20 ECON. INQUIRY 604, 604 (1982); Peltzman, *supra* note 8, at 21; Stigler, *supra* note 19, at 3.

190. A total of 238 organizations received fines or restitution in the 2001 fiscal year. *See* UNITED STATES SENTENCING COMMISSION, SOURCEBOOK OF FEDERAL SENTENCING STATISTICS tbl. 51, *available at* http://www.ussc.gov/ANNRPT/2001/table51.pdf (last visited Apr. 1, 2004).

191. Moreover, even though the imposition of penalties is more common on smaller businesses than larger ones (supporting the dueling businesses notion) it is still not frequent enough to operate as

In addition, there is evidence that small firms (which newer firms tend to be) are sometimes treated better than larger firms. For example, under the organizational sentencing guidelines, smaller corporations (as determined by number of employees) are likely to receive smaller fines compared with similarly situated larger firms.[192] Further, the primary method of obtaining a sanction reduction under the organizational sentencing guidelines—the presence of a reasonably effective compliance program—seems to favor smaller firms too.[193] For example, the complexity and completeness of a "reasonably effective" compliance program tends to increase with the complexity and size of the corporation.[194] Consequently, smaller firms are expected to have less onerous compliance programs than larger firms to earn a sentence reduction under the guidelines.[195] This is not entirely consistent with an entry barrier account.[196]

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a real entry deterrent. *See* SENTENCING COMMISSION ANNUAL REPORT 2001, *supra* note 41; Alexander, et al., *supra* note 41, at 403; First, *supra* note 41, at 3–5; Geraghty, *supra* note 41, at 338; Murphy, *supra* note 41, at 113; Rakoff, *supra* note 41, at 2; Davidson, *supra* note 41, at B3. Indeed, most prosecutions are against small distressed firms, which are the least likely to pose a serious entry threat (as they are already about to go out of the market as they are distressed) and unlikely to have the resources to put up a very strong defense. *See* SENTENCING COMMISSION ANNUAL REPORT 2001, *supra* note 41; First, *supra* note 41, at 3–5; Geraghty, *supra* note 41, at 338; Davidson, *supra* note 41, at B3; Murphy, *supra* note 41, at 113; Rakoff, *supra* note 41, at 2.

192. *See* SENTENCING GUIDELINES, *supra* note 3, at §§ 8C2.5(b)(1)–(5).

193. *See* PRINCIPLES, *supra* note 99, at § VII (advising prosecutors to examine the compliance programs that corporations establish).

194. *Cf. id.* at 6–7.

195. *See id.*

196. Moreover, some regulations may even benefit smaller firms more directly. For example, in the securities regulation context, smaller issues can avoid a great deal of regulation by relying on a number of exemptions.

This may explain why there appears to be little interest by industry to lobby for regulatory competition. *See* Coates, *supra* note 143, at 543–53. Regulatory competition is the idea that permitting issuers to choose their own securities law (e.g., U.S. law, U.K. law), disclose this choice, and then permit trading anywhere would induce regulatory competition between jurisdictions and may in many instances lead to more responsive and efficient regulation. *See* Stephen Choi, *Regulating Investors Not Issuers: A Market-Based Proposal*, 88 CAL. L. REV. 279 (2000); Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice Is Not Investor Empowerment*, 85 VA. L. REV. 1335 (1999); Howell Jackson, *Centralization, Competition, and Privatization in Financial Regulation*, 2 THEORETICAL INQ. IN L. 649 (2001); Marcel Kahan, *Some Problems with Stock Exchange-Based Securities Regulation*, 83 VA. L. REV. 1509 (1997); Paul G. Mahoney, *The Exchange as Regulator*, 83 VA. L. REV. 1453 (1997); Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359 (1998); Howell Jackson & Eric Pan, *Regulatory Competition in International Securities Markets: Evidence from Europe in 1999* (Sept. 18, 2000) (unpublished manuscript, on file with author).

If so, then we would expect to see firms lobbying for just this kind of regulatory competition, as that would mean the costs of raising money would decrease under more efficient systems. In spite of this, we do not see much lobbying by businesses in favor of regulatory competition. *See* Coates, *supra*

Further, if we wanted to provide a disincentive to enter the market we need not do so by threatening "criminal" liability for corporations. Civil liability would be sufficient, as both "criminal" and "civil" liability offer only monetary penalties against corporations, and civil liability is more frequent and often larger.[197] That leaves us with the substitution theses discussed earlier in this paper.[198]

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note 143, at 565–61. Why might that be? One reason is that regulation already appears quite responsive to industry concerns. *See id.*

197. For example, it has been argued that the prosecution against Drexel Burnham and Michael Milken for various securities law violations was lobbied for by the corporate and investment banking establishment to impede competition from upstarts like Drexel and Milken. *See* Fischel & Sykes, *supra* note 47, at 347; DANIEL R. FISCHEL, PAYBACK: THE CONSPIRACY TO DESTROY MICHAEL MILKEN AND HIS FINANCIAL REVOLUTION (1995).

Regardless of the merits of this explanation, it is somewhat orthogonal to my analysis. Simply put, this account may explain why we have so much regulation and enforcement in the business sphere generally, but not specifically why there is so much *criminal* regulation. For example, even if the Drexel Burnham enforcement took on only a civil flavor, the same critiques still could have been levied against it. *See id.* at 347 (essentially doing just this). Indeed, we do not need corporate criminal liability to impose monetary costs on the Drexel Burnhams of the world—even enhanced civil sanctions would have a similar effect.

One could instead argue that regulation benefits industry by providing it with an imprimatur of trustworthiness if corporations meet these regulations (and correlatively identifies as "bad apples" those corporations that do not meet these regulations). *See* John C. Coffee, Jr., *Racing Towards The Top?: The Impact of Cross-Listings and Stock Market Competition on International Corporate Governance*, 102 COLUM. L. REV. 1757 (2002) [hereinafter *Cross-Listings*] (discussing with supporting evidence how the U.S. securities laws may serve a bonding role for foreign issuers). *Cf.* Michael Jensen & William Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 305–08 (1976) (defining agency costs as including "bonding" costs). Professor Coffee argues that the U.S. securities laws operate as an assurance of transparent accounting and fairly good disclosure to many foreign issuers, and these issuers may cross-list on U.S. markets to convey this assurance to their own or other investors. *See Cross-Listings*, *supra*. There is some support for this bonding hypothesis, and it provides a good explanation of foreign issuers' behavior and also of the bonding role of securities regulation. *See id.* Might this explain the growth in corporate criminal liability? I have some doubts.

First, compliance with U.S. securities regulation is considered fairly well enforced, whereas corporate criminal liability is largely under-enforced. *See id.* (discussing enforcement under U.S. securities laws); SENTENCING COMMISSION ANNUAL REPORT 2001, *supra* note 41; GRUNER, *supra* note 4, § 1.7.1, at 29–36 (noting problems with detection of corporate wrongdoing and enforcement); Alexander et al., *supra* note 41, at 403; First, *infra* note 41, at 3–5; Geraghty, *supra* note 41, at 338; Hughes, *supra* note 25, at 576–80 (noting that a number of new tools in civil enforcement arose in response to problems of enforcement and detection in the corporate crime area); Murphy, *supra* note 41, at 113; Rakoff, *supra* note 41, at 2; Davidson, *supra* note 41, at B3. This suggests that the bonding story of securities regulation is based on some truth, whereas the bonding story of corporate criminal liability is based on illusion in some manner. One expects that the illusory nature of corporate criminal bonding would not go unnoticed by those who invest in such corporations.

Second, if we are relying on the bonding story it is not entirely clear why we need corporate *criminal* liability. We could instead rely on corporate civil liability, as the same assets are being put up as a bond: monetary ones (the only ones the corporation itself possesses). Even if we bring into consideration reputational penalties, there is little evidence that the reputational penalty from corporate criminal liability is any greater than the penalty from corporate civil liability when the underlying wrongdoing is held constant. *See* Khanna, *Corporate Criminal Liability*, *supra* note 6, at 1509.

Another political account could be that corporate crime legislation arises because politicians are using legislation to extract (or extort) rents from various groups.[199] Although a very important political account more generally,[200] in the context of corporate crime legislation it too seems implausible. Again, the infrequency of corporate crime enforcement and the relatively small penalties make one doubt the rent extraction potential. Indeed, rent extraction is more plausible under corporate civil liability where the penalties are larger and enforcement is more frequent. Furthermore, if rent extraction were a large concern, we might expect corporate lobbying against such legislation, but we rarely see such opposition by corporations.

Finally, one might posit that corporate crime legislation could be in the public interest (i.e., socially desirable) and that this may give it some political strength.[201] To the extent this claim relies on the notion that such legislation *deters* corporate wrongdoing, it rests on shaky footing. Earlier studies of the deterrent effect of corporate criminal liability, including my own, find little reason to think that it has much deterrent effect above that associated with corporate civil liability.[202] Even if it did, one might then wonder why we see so little corporate opposition to these laws.

Also, it is not so clear that foreign companies can opt into U.S. corporate crime legislation as easily as opting into U.S. securities laws.

198. On a different note, one could argue that criminal law is better for politically motivated prosecutions because often the prosecutor need not show harm and can pursue criminal enforcement in cases where there is, arguably, little justification for regulation (because there may be no harm), whereas civil cases might be impeded by these considerations. *See* Fischel & Sykes, *supra* note 47, at 347–48. This, at best, provides only a partial explanation for corporate criminal liability. First, it provides little explanation for instances of criminal regulation where harm is required before an offense arises. Second, it is plausible that in some *civil* cases the government need not show harm either. If the legislature provides for civil sanctions even when there is no harm, then the moving party can recover in civil suits even if no harm is caused. Further, it is not clear why corporations and management would not oppose corporate criminal liability because of this feature.

199. *See generally* FRED MCCHESNEY, MONEY FOR NOTHING: POLITICIANS, RENT EXTRACTION, AND POLITICAL EXTORTION (1997).

200. *See id.*; Robert H. Sitkoff, *Corporate Political Speech, Political Extortion, and the Competition for Corporate Charters*, 69 U. CHI. L. REV. 1103 (2002) (discussing how the Tillman Act may have been supported by corporate interests to protect themselves from extortion by politicians).

201. The cost of gaining support, and therefore influence, is reduced when the interest promoted is a popular goal or one that increases efficiency. *See* Becker, *supra* note 8, at 390, 393; Beny, *supra* note 8, at 22–23.

202. Indeed, some of my other papers suggest that certain critical aspects of corporate criminal liability are difficult to justify under a deterrence framework (e.g., the requirement of corporate mens rea, the increasing of corporate penalties because of top management involvement in wrongdoing). *See, e.g.*, Khanna, *Corporate Fault*, *supra* note 6, at 382–84; Khanna, *Top Management*, *supra* note 6, at 1215–19.

VIII. CONCLUSION

Corporate crime is a perennial topic of discussion in the legislature, judiciary, academe, business board rooms, and polity at large. The recent spate of corporate wrongdoing has brought corporate crime to the forefront once again and led to the passage of the Sarbanes-Oxley Act of 2002. This legislation adds to the already sprawling and ever-increasing area of corporate criminal liability.

However, the continued and rather explosive growth of corporate crime legislation leaves a rather strange puzzle: How can such a state of affairs arise? After all, corporations and business interests are considered some of the most powerful and effective, if not *the* most powerful and effective, lobbyists in the country. Yet, we witness the continued expansion of legislation that criminalizes their behavior. What explains the growth of such legislation?

My analysis suggests that corporate crime legislation may grow because it is a *preferred* response for corporate interests when some congressional action is inevitable. Most corporate crime legislation arises during a time of a weak economy and when many instances of corporate wrongdoing are revealed to the public. This generates a strong desire in the polity for enhanced regulation. Corporate criminal liability's growth could then be explained by the following notions: (i) some degree of "punishment" is necessary, as a political matter, to satisfy public desires during recessions and economic downturns when revelations of corporate wrongdoing are numerous; and (ii) corporate crime legislation achieves this while imposing lower costs on business interests relative to other measures that could be undertaken (e.g., increasing corporate civil liability or managerial criminal sanctions). Corporate crime legislation then appears to be a relatively low-cost method of satisfying public desires along with congressional and prosecutorial incentives within the constraints imposed by the lobbying activities of management and corporations. Thus, the growth of corporate criminal liability may be understandable from a political economy perspective.[203]

This then leaves a rather important question for us: if these political accounts provide an explanation for corporate crime legislation, what normative implications follow? My analysis suggests that the normative

203. I hasten to add, however, that these political accounts do not reflect the reasons for the initial development of corporate criminal liability, which came about to fill real enforcement gaps. However, the political accounts do provide some explanations for why corporate criminal liability has grown so much so recently when those enforcement gaps have largely dissipated.

implications are quite complex and depend largely on one's prior beliefs about the world and which political account(s) one finds persuasive. However, one thing appears clear regardless of the preferred political account(s): if we start with the notion that corporate wrongdoing is not sufficiently deterred at present, then we would want to argue for *curtailing* corporate criminal liability and increasing the focus on corporate civil liability and managerial liability. This raises serious questions about how we regulate this area.