Hybrid Statutes: A Study in Uncertainty

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My topic tonight is hybrid statutes, that is, statutes that provide both civil and criminal penalties for the same misconduct. I want to suggest that hybrid statutes create more problems than they solve, not least in the area of corporate misconduct.

I have come to this conclusion reluctantly, since hybrid statutes have been part of the American legal framework for a very long time. An early example is the Sherman Antitrust Act enacted in 1890, which criminalizes conspiracies in restraint of trade but also empowers victims of such a conspiracy to sue the conspirators and obtain treble damages and attorneys' fees. In the regulatory context, a good example is the Securities Exchange Act of 1934, which authorizes the SEC to promulgate rules and bring civil enforcement actions for violations of those rules, but also authorizes the Department of Justice to bring criminal prosecutions for willful violations of those same rules, and also implicitly empowers private parties to bring civil suits, including class actions, for violations of certain of those rules. Still another example is RICO – the Racketeer Influenced and Corrupt Organizations Act -- which takes a long list of state and federal criminal statutes that do not themselves provide for civil remedies, defines them as "predicate acts," and provides that anyone who impacts an interstate enterprise in proscribed ways through the use of a pattern of such predicate acts is subject to criminal prosecution, government civil actions awarding substantial injunctive and equitable relief, and private treble-damage civil actions.

What is common to these and various other hybrid statutes found in the federal canon is that they each prescribe for some specified misconduct a host of civil and criminal penalties and remedies. In other words, a typical hybrid statute first defines the underlying misconduct and then provides that perpetrators of that misconduct may be sued in both public and private actions and, depending on the nature of the actions, find themselves facing imprisonment, civil and criminal fines and forfeitures, enhanced damages, and much else besides. The central idea behind these hybrid statutes is to provide maximum deterrence for the misconduct in question by making it subject to every weapon the legal system can bring to bear. Through government-initiated injunctive relief, the misconduct will be halted; through criminal prosecution, the perpetrators will be punished; and through private civil actions not only will the victims be compensated, but also the perpetrators will have to pay damages well in excess of their wrongful profits. In the abstract, it seems to make sense: through a comprehensive attack at every level, maximum deterrence of proscribed antisocial conduct will be halted, punished, remedied, and deterred.

But in practice, I suggest, it leads to material inconsistencies and strange results that both undercut its effectiveness and create major legal headaches. The fundamental reason for these problems is that the legal system has long prescribed totally different rules for the interpretation of civil and criminal statutes that often make it impossible for courts to interpret hybrid civil/criminal statute in a coherent way.

In particular, it is a well-settled principle of United States law that criminal statutes are to be interpreted narrowly, so as to provide fair notice, avoid over-criminalization, and protect the innocent. A corollary of this principle, frequently invoked by the Supreme Court, is the "rule of lenity," by which if a criminal statute can be reasonably interpreted in either of two ways, the narrower interpretation must be adopted, again to help provide fair notice, protect the innocent, avoid governmental overreaching, and the like.

By contrast, it is an equally well-settled principle of United States law that civil statutes serving a remedial or regulatory function should be broadly interpreted so as to effectuate their remedial purposes. "Loopholes" should be avoided and narrow statutory interpretations should be eschewed, for otherwise the remedial or regulatory function of the statute will be undercut.

These principles, which trace back to the common law, reflect the fundamental differences between civil and criminal law that underlie a great deal of our legal system. But in the case of hybrid statutes, they are set at odds. If a statute contains some ambiguity – which, regretfully, is true of most statutes -- a court is directed to resolve the ambiguity by applying equal but opposite canons of construction. What's a poor judge to do? Well, as you might suspect, if the hybrid statutes comes before the judge in a criminal case, the judge interprets the hybrid statute narrowly, and if the same statute comes before the judge in a civil case, the judge interprets the very same statute broadly – leading to inconsistent results. And sometimes the judge gets so befuddled that the results are simply bewildering.

But the Supreme Court has not done much better. Consider, first, the Sherman Act, which may well be the first major hybrid statute passed by Congress. Certainly, it was the first U.S. statute to provide that the same underlying conduct could give rise to criminal prosecution, government civil actions seeking injunctive and other equitable relief, and private civil actions seeking enhanced damages. But what is the underlying conduct that gives rise to this triple threat? It is a conspiracy "in restraint of trade." That, one might argue, is about as vague a phrase as one can imagine – and a criminal defendant named Nash did so argue in the case of Nash v. United States, 229 U.S. 373 (1913), in which he attacked the statute as unconstitutionally vague. Ruling against him, Justice Oliver Wendell Holmes, in an opinion joined by all but one other Justice, rejected this claim in just two sentences, stating, "But, apart from the common law as to the restraint of trade thus taken up by the statute, the law is full of instances where a man's fate depends on his estimating rightly, that is, as the jury subsequently estimates it, some matter of degree. If his judgment is wrong, not only may he incur a fine or a short imprisonment, as here; he may incur the penalty of death."

Holmes or not, the primary point he is making here – that a jury's discretion should include the power to interpret vague statutes on an ad hoc basis -- is clearly wrong. For the Supreme Court has elsewhere consistently held that a statute that is so vague that two reasonable juries, confronted with the same evidence and drawing the same inferences as to credibility, could nonetheless reach opposite conclusions as to guilt or innocence is a classic example of a statute that is void for vagueness.

Of more immediate relevance here is Holmes' alternative point, though literally just an "aside" – that the statute incorporates the common law definition of "restraint of trade." In effect, Holmes says that "restraint of trade" is a term of art, but one defined, not by statute, but by the less precise case law development typical of the common law. At a minimum, this leaves open the question: did Congress, in using the common law term "restraint of trade," mean to prohibit only such conduct as violated the common law definition of "restraint of trade" of the date of the Sherman Act's enactment in 1890, or did it prohibit restraints of trade that subsequent courts might conclude were a reasonable common law extension of the common law of restraint of trade? Classic principles of statutory construction of criminal statutes would favor the former view, not only because criminal statutes should be interpreted narrowly but also because, under separation of powers, only the legislature can define a crime. But classic principles of statutory construction of civil statutes would favor the latter view, since such statutes should be broadly interpreted to effectuate their underlying purposes and since, in any event, a common law definition is never set-in-stone but is constantly developing case-by-case.

This inherent conflict in the interpretation of the Sherman Act has never been definitively resolved, even now, over a century later. For many years, the Department of Justice avoided the issue by only bringing cases of clear-cut antitrust violations that would qualify as restraints of trade under virtually any definition. And ultimately the Supreme Court purported to resolve the issue – but in my view really avoided it – by holding U.S. v. United States Gypsum Co., 438 U.S. 422 (1978), that, whatever the meaning of "restraint of trade," the Government, in order to convict a defendant of a criminal violation of the Sherman Act, had to show that the defendant acted with a higher degree of wrongful intent – specifically knowing involvement – than had to be shown to hold a defendant liable for civil violation of the same act.

This approach – which the Supreme Court has similarly taken in trying to resolve the civil/criminal tension in other hybrid statutes – is, I submit, a partial solution at best. For if a person, with all the wrongful intent in the world, enters into a conspiracy to affect commerce in a manner that does not in fact constitute a restraint of trade - however defined – how can he be found to violate the Sherman Act? Thus, whether "restraint of trade" is to be defined in terms of criminal law principles, that is, narrowly, or in terms of civil law principles, that is, broadly, is still an issue that must be reached, even if silently.

Consider next, the federal securities laws, and, to be *au courant*, the definition of insider trading. Federal law does not prohibit "insider trading" in those words, but treats it as a form of fraud prohibited by SEC Rule 10b-5, promulgated by the SEC in 1942 pursuant to Section 10(b) of the Securities Exchange Act. The rule itself, 10b-5, broadly prohibits any scheme or artifice to defraud in connection with the purchase or sale of securities. But in a series of cases beginning with an SEC administrative decision, In re Cady Roberts, 40 SEC 907 (1961), continuing with a civil case in the Second Circuit, SEC v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968), and concluding with two cases in the Supreme Court, specifically, a civil case, Dirks v. SEC, 483 U.S. 646 (1983) and a criminal case, U.S. v. O'Hagan, 521 U.S. 642 (1997), the courts have determined that trading on inside information can in certain circumstances constitute either an insider's breach of fiduciary duty to his shareholders or an outsider's misappropriation of information in breach of his fiduciary duty to the source of the information. This common law development of the prohibition against insider trading raises all sorts of difficult questions: Should the SEC, which has only civil enforcement authority, play any role whatsoever in defining a criminal prohibition? Should the federal courts, which have both civil and criminal jurisdiction, be defining on a common law, case-by-case basis, the requirements of a criminal violation not specifically defined by the legislature? And, in any event, in undertaking this development, should the SEC, the courts, or both be guided by the broad interpretative principles of the civil law or the narrow interpretive principles of the criminal law?

The courts have largely avoided these questions. For example, the *sine qua non* of any insider trading violation is a breach of either a fiduciary duty or, as the decisions say, some similar duty of trust and confidence. But it is the federal case law that defines what fiduciary duties and duties of trust and confidence are applicable to insider trading, and this raises all the same problems as the common law aspects of the Sherman Act.

Let me digress here to note that over the years, there have been several attempts to enact a federal statute expressly defining insider trading – indeed there are at least two such bills presently pending in Congress – but these attempts have foundered because of criticism by some, notably the SEC, that the proposed statutory definition of insider trading is too narrow, and criticism by others, notably, the business community, that the proposed statutory definition of insider trading is too broad. Their respective arguments, as you might expect, mirror many of the difficulties inherent in interpreting other hybrid statutes.

Would it not make more sense to have two definitions, or even two laws – one on the criminal side narrowly and specifically defining core criminal insider trading and the other on the civil side broadly defining insider trading in a way that leaves room for future development? This would prevent criminal prosecution of those who lacked fair notice of their transgressions, while allowing the SEC to step in and halt new, innovative forms of insider trading at the outset. While, in the short run, this might create a loophole for innovative insider traders to escape criminal prosecution, they would still be subject to substantial civil liabilities, and, over time, amendments could be made to the criminal law to incorporate additional prohibitions that the developing civil law of insider trading had now established should be prohibited.

For my last example, let me turn to the most curious of all hybrid statutes, RICO. RICO should have special interest for this audience, for it was the first hybrid statute that provided for dissolution of a corporation, as in the <u>Princeton-Newport</u> case or for a governmental takeover of an entire enterprise, as in the <u>Teamsters</u> case. While these days, corporate criminal liability and governmental monitoring of companies are usually imposed without reference to RICO, it was originally RICO that set the government on this path.

RICO, moreover, created a special problem for the courts, for its very broad development on the private civil side was, as the Supreme Court has had more than one occasion to note, totally a surprise. But RICO is so broadly and vaguely worded that a statute originally designed to be used against organized crime may, by its terms, be used to seek treble damages and attorneys' fees in ordinary commercial disputes – and the private civil bar eventually came to realize this. The ironic result has been that the courts, from the Supreme Court on down, have consciously sought to interpret RICO broadly on the <u>criminal</u> side (where it is used chiefly against mobsters) and narrowly on the private civil side (where it is used in commercial litigation) - a seeming reversal of ordinary principles of construction. Even there, however, the courts have still been confronted with the classic hybrid dilemma: If the words of a statute are to mean anything, they must have the same meaning whether the statute is used civilly or criminally; so whenever you interpret a term broadly or narrowly in one kind of case, you broaden it or narrow it for all cases.

One of the elements of any RICO violation is a "pattern of racketeering activity," which, as the statute states, requires two predicate acts (i.e., two violations of the various state and federal criminal statutes defined as predicate activity). But in the private civil RICO case of H.J., Inc. v. Northwestern Bell Telephone Co., 492 U.S. 229 (1989), the Supreme Court in an effort to narrow private civil RICO, said that for these two acts to form a "pattern," they must have "continuity and relationship."

These court-imposed terms are vague on their face; indeed, four concurring Justices in H.J., Inc. suggested they were unconstitutionally vague. It is therefore not surprising that in the years since H.J. Inc. was decided, the terms have been defined in materially inconsistent ways by the lowers courts, the only "consistency" being that they are typically defined in private civil actions so as to dismiss the actions, whereas they are typically defined in criminal RICO cases in such a way as to uphold the actions.

For example, whereas most courts have held that the "continuity" requirement of a RICO pattern is not satisfied in private civil RICO actions by anything less than a pattern of acts extending for at least a year – some courts say two years – in the criminal case of U.S. v. Indelicato, 865 F.2d 1370 (2d Cir. 1989), the Second Circuit Court of Appeals, en banc, held that a gangland triple murder lasting at most ten seconds, which was the sole "pattern" alleged in the indictment, was nonetheless sufficient to satisfy the "continuity" requirement.

I will spare you the verbal legerdemain that enabled the court to reach this result. But I respectfully suggest that it is typical of the artificial pressures created by hybrid statutes.

While the problems with hybrid statutes that I have outlined above cut across many different areas of activity, I think they may have special relevance to the subject matter of this conference: corporate crime and financial misdealing. Much of the prohibited conduct that leads to corporations being the subject of governmental actions is regulatory in nature, involving conduct that is not always inherently wrong. Moreover, much corporate liability, whether civil or criminal, is imputed, that is to say, it involves the acts of individuals whose actions are then imputed to the company. In such a context, the notion that corporate criminal liability, as opposed to civil liability, can be premised on the statutory uncertainties and inconsistencies inherent in hybrid statutes strikes me as problematic. When lay people hear that either an individual or a corporation has been charged with a crime, they understand it to mean that what they did was clearly wrong. If, instead, the corporation is criminally charged because an employee, even if knowingly or intentionally, violated an unclear and uncertain standard, the criminal law is seemingly being abused. And it is just such problems that hybrid statutes generate.

In sum, hybrid statues arose from a legitimate attempt to bring to bear all the weapons of the law, civil and criminal, public and private, to root out specified forms of misconduct. But the attempt has created more problems than it has solved. It is time to eliminate hybrid statutes and restore the legitimate distinction between the civil and criminal law.