

## PREFACE

The Sarbanes-Oxley Act of 2002 is the most major securities regulation to affect companies since the Securities Exchange Act of 1934. Right now there are about 15,000 listed companies, which have a total market value of approximately \$37 trillion and are held by tens of millions of shareholders.

The Enron trial ended after four years of federal investigations and 108 days of sworn evidence. The prosecution based its case on evidence provided by executives below the top level, who themselves took plea deals, and on the Watkins letter, which exposed the fraudulent activities of the corporation in August 2001. Judge Lake invoked a common feature in white-collar prosecutions by giving the “ostrich instruction” to the jurors. This allows the jury to find a defendant guilty if they had sufficient notice of problems (like the Watkins letter), but deliberately refused to recognize or act on that information. Former WorldCom CEO, Bernard Ebbers, was convicted by way of a similar ruling.

Willful blindness satisfies the knowledge for a conspiracy conviction and the intent (*scienter*) element of a fraud conviction. The knowledge element refers to an offending party’s knowledge of the wrongness of an act or event prior to committing it. Black’s Law Dictionary defines fraud under common law as involving three elements: (1) a material false statement made with intent to deceive (also known as the element of *scienter*); (2) a victim’s reliance on those statements; and (3) damages. If the breach of fiduciary duty has no wrongful intent, it is civil fraud, but if it does, it becomes criminal fraud. This treatise does not cover frivolous cases of civil fraud claims, such as the difficulties of Dave Thomas of Wendy’s with an IPO where a footnote disclosure was found inadequate or Ron Howard’s dissolution of his film company whereby investors claimed civil fraud because he walked away from the corporation. These cases cross the line of frivolity.

The ostrich instruction is a common feature in white collar crime prosecutions. *United States v. Jewell*, 532 F.2d 697 (9th Cir. 1976), sets forth the classic instruction in this area: “You may infer knowledge from a combination of suspicion and indifference to the truth. If you find that a person had a strong suspicion that things were not what they seemed or that someone had withheld some important facts, yet shut his eyes for fear that he would learn, you may conclude that he acted knowingly.” Judge Posner explained how the ostrich instruction should be understood, and its limitations, in *United States v. Giovannetti*, 919 F.2d 1223 (7th Cir. 1990):

The most powerful criticism of the ostrich instruction is, precisely, that its tendency is to allow juries to convict upon a finding of negligence for crimes that require intent . . . The criticism can be deflected by thinking carefully about just what it is that real ostriches do (or at least are popularly supposed to do). They do not just fail to follow through on their suspicions of bad things. They are not merely careless birds. They bury their heads in the sand so that they will not see or hear bad things. They deliberately avoid acquiring unpleasant knowledge. The ostrich instruction is designed for cases in which there is evidence that the defendant, knowing or strongly suspecting that he is involved in shady dealings, takes steps to make sure that he does not acquire full or exact knowledge of the nature and extent of those dealings. A deliberate effort to avoid guilty knowledge is all the guilty knowledge the law requires.

Jurors were quoted after the trial as saying that for a man as knowledgeable as Enron Chairman Ken Lay was, he had to know what was going on at his own company. They found the high level of stock

sales unusual, as well, compared to his recommendations at the same time to employees of the company to hold and buy stock.

Why has the last decade seen such an increase in white collar crime? It has been reflected in dozens of cases involving bribery, conflicts of interest, mail and wire fraud, and securities fraud, to name only a few. It is inconceivable that the perpetrators were not aware. It is the purpose of this book to raise the awareness level among educators, practitioners, senior management and their auditors, and researchers of the need for adequate and continued laws and controls on a global basis in order to protect the capital markets and ensure and restore integrity and an ethical standard through the rule of law to world markets.