Deferred Corporate Prosecution as Corrupt Regime: The Case for Prison

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Abstract: This paper looks at the growing phenomenon of deferred corporate criminal prosecutions from a new perspective. The literature accepts the practice and is largely concerned with the degree to which efficient and effective criminal deterrence is achieved through pretrial diversion. I examine the practice and conclude that it presents, from a structural perspective, a case of a corrupt law enforcement regime centered in the United States Department of Justice. The regime works in effective -- if unintentional-- conspiracy with corporate officials to produce an inefficient enforcement regime that disregards democratic processes and threatens a loss of respect for the rule of law. I conclude that the use of individual prosecution with the possibility of prison for corporate executives is the most effective way to restore the corporate criminal regime to a functioning legal practice.

On January 12, 2015, The New York Times reported that the United States Department of Justice was nearing a settlement with Standard & Poors for more than $1 billion. The case is unusual for two reasons. The first is the amount of the fine. Although there have been far larger settlements in recent years, most of those have amounted to a very small share of the defending corporation’s profits. The billion dollars expected from S&P, in contrast, would wipe out a full year’s operating profits. The second is that S&P vigorously fought the government’s claims. Again, in contrast, virtually every major corporation charged with crime in recent years has caved, either by entering into a deferred prosecution agreement (“DPA”) or a non-prosecution agreement (“NPA”). These negotiated deals almost always call for

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substantial fines and significant internal operational reform to create systems of crime prevention and detection.¹

Corporate criminal liability wasn't much in evidence 30 years ago. In 1996, Fischel and Sykes could observe it as “a relatively new phenomenon in American law.”⁵ Since then, and especially following the corporate scandals at the beginning of this century, the enactment of Sarbanes-Oxley, and the 2008 financial crisis, corporate criminal liability has become an exploding phenomenon. The fines are only part of the story. Some of the most significant corporate criminal investigations have resulted in DPAs or NPAs. Prior to 2003, there were fewer than a couple of dozen corporate DPAs. There have been approximately 250 since then.⁶ Accompanying this dramatic increase in enforcement actions has come a proliferation of literature on the subject.

Reviewing this literature, much of which is focused on DPAs and NPAs (or, more mellifluously, pretrial diversion agreements) is a fascinating exercise. Scholars have criticized the prosecutorial practice of demanding pretrial diversion agreements as too one-sided,⁷ insensitive to corporate governance realities,⁸

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¹ Garrett demonstrates that in fact these fines and institutional reforms are relatively modest, but the general perception of them is as being significant. BRANDON L. GARRETT, TOO BIG TO JAIL: HOW PROSECUTORS COMPROMISE WITH CORPORATIONS (Belknap: 2014). The United States Sentencing Commission’s Organizational Sentencing Guidelines also promise the possibility of leniency for corporations found to have internal deterrence and detection structures. http://www.ussc.gov/guidelines


⁶ BRANDON L. GARRETT, TOO BIG TO JAIL: HOW PROSECUTORS COMPROMISE WITH CORPORATIONS (Belknap: 2014) 7; Lawrence A. Cunningham, Deferred Prosecutions and Corporate Governance: An Integrated Approach to Investigation and Reform, 66 Fla. L. Rev. 1, 19 (2014).

⁷ Margaret Lemos and Max Minzner, For-Profit Law Enforcement, 127 Harv. L. Rev. ___(2014); Peter Reilly, Negotiating Bribery: Toward Increased Transparency, Consistency, and Fairness in Pretrial Bargaining Under the Foreign Corrupt Practices Act, 10 Hastings Bus. L. J. 347. Richard Epstein states that the one-sidedness argument has been ameliorated somewhat by the Department of Justice’s most recent guidance eliminating demands for privilege waivers. Richard A. Epstein, Deferred Prosecution Agreements on Trial, in ANTHONY S. BARKOW AND RACHEL E. BARKOW, PROSECUTORS IN THE BOARDROOM: USING CRIMINAL LAW TO REGULATE CORPORATE CONDUCT (NYU; 2011), 38, 39, although others continue to see the imbalance as significant. Anthony S. Barkow and Rachel E. Barkow, Introduction, id. at 1,2. It also appears that such waivers continue to be requested. Moreover, other significant consequences of corporate non-cooperation remain. So while perhaps the most
inefficient, and desirable but in need of reform. A significant portion of the literature is devoted to calibrating the efficient and effective standard of liability that should be used in determining corporate criminal culpability, and the relationship between corporate criminal liability and civil regulatory and litigation regimes. The assumption that a corporate criminal liability regime should be aimed at deterrence is almost universal, although several commentators focus more on rehabilitation.

As interesting as the literature can be, what is perhaps more interesting is what is missing. Almost nobody talks about the criminal liability of corporate executives, except perhaps in passing. As Fischel and Sykes predicted in 1996, corporate criminal liability – enterprise liability – has become a substitute for individual liability. By itself, this might not be terribly surprising. After all, there are many reasons why prosecutors would prefer to charge corporations rather than

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8 Cunningham, supra note __.
10 Cunningham, supra note __.
13 Uhlmann, for example, grounds his critique specifically in the argument that DPAs fail to deter corporate misconduct. David M. Uhlmann, Deferred Prosecution and Non-Prosecution Agreements and the Erosion of Corporate Criminal Liability, 72 Md. L. Rev. 1295 (2013). Peter J. Henning, Corporate Criminal Liability and the Potential for Rehabilitation, 46 Am. Crim. L. Rev. 1417 (2009). Cunningham’s study seems largely aimed at rehabilitation as much as deterrence. Cunningham, supra note __
14 But see Uhlmann, supra note __ who reaches the conclusion that individuals should be prosecuted after concluding that DPAs fail to deter; Donald C. Langevoort, supra note __ (analyzing equitable remedies in the context of securities fraud).
15 Fischel and Sykes, supra note __.
individuals. What is surprising is that the scholarly literature fails to challenge this preference. I will, in this article, do just that.

This observation is one of more than theoretical interest. I shall argue that the relative absence of individual prosecutions allows the criminal justice system to flourish as a corrupt government enterprise, at least as far as corporate crime is concerned. More, it is, in effect, a conspiracy of corruption between prosecutors and corporate executives, one that may not be ameliorated in the absence of individual prosecutions by the government and prison, when appropriate, for corporate executives.

Let me be clear. I am not accusing anybody of intentional corruption or conspiracy. Rather, I am describing a structure created by the incentives of actors on all sides constrained – or not – by criminal procedure and corporate governance mechanisms. The type of corruption presented by the pre-trial diversion regime is a special case of what Dennis F. Thompson calls “institutional corruption,” one in which political gain replaces individual profit and institutional tendency replaces individual motive. Intentional or not, it creates the same kinds of inefficiencies as purposeful corruption. I will have ample opportunity to explicate below. For the moment, let me establish the theory.

I begin with Robert Klitgaard’s rather sensible “metaphorical” formula for determining the conditions under which corruption gains are established: “Officials will have the opportunity to garner corrupt benefits as a function of their degree of monopoly power over a service or activity, their discretion in deciding who should get how much, and the degree to which their activities are accountable.” Thus:

\[ C = M + D - A \]

Where \( C \) is corruption, \( M \) is monopoly power, \( D \) is discretion, and \( A \) is accountability. On its face, the contemporary corporate criminal regime satisfies the formula. The Justice Department (or state attorneys general) has monopoly power, DPAs are in their sole discretion, and they are not subject to judicial or any other mechanism of accountability. But matters are not quite so simple. I accused


In Part II, I discuss why this is true despite the frequent availability of civil and administrative enforcement of corporate violations.
both prosecutors and corporate executives as being members of a conspiracy of corruption. How do corporate managers come in? After all, they have been portrayed – at some level, appropriately – as victims of the unbridled monopoly power and discretion of prosecutors. But that is too easy a conclusion.

Klitgaard’s formula doesn’t so easily fit corporate managers (although Thompson’s analysis does).\(^\text{20}\) Monopoly power and discretion are contestable, since lower-level managers answer to executives and executives answer to the board in whose ultimate discretion lies the decision to accept a DPA. Such monopoly power and discretion do appear in the relationship of the corporate entity to the board, but I don’t want to, nor do I need to, engage in such reifications in order to sustain my point. For it is not necessary for a conspiracy to exist that each member participate in each element. Rather, the key element on the corporate side is accountability. Accountability does not and, I shall argue, probably cannot exist in a system of prosecution solely dependent upon corporate fines and internal reforms.

Why not? Because levying fines allows the individual wrongdoers to punt to the corporation. Now you might object by noting that boards are subject to shareholder elections, executives to board appointment, and lower-level managers to executive appointment, and this is true. But the evidence thus far suggests that the kinds of fines to which corporations are subjected are insufficient to cause internal corporate upheaval. While some have called for far more significant fines, one wonders how large they would have to be to offset the entropy of corporate culture and the potential benefits (to individuals within the corporation as well as the corporation itself) from criminal violations. It might be empirically demonstrated that such fines could be set sufficiently high (thus possibly creating greater incentives for corporate executives to fight sanctions rather than accede to DPAs). I will argue later that this is unlikely. If I am wrong, the conspiracy dimension of my argument might fall. But the corruption argument stands.

Why does it matter? One reason, prominent in the literature, is that the current regime penalizes shareholders and consumers rather than individual corporate wrongdoers. (I do not here join in the debate as to whether a corporation itself is capable of committing a crime or justly can be punished. I will assume the affirmative as to both questions – it doesn’t matter to my analysis. If the answer were negative, my case would be easy). Related to this is the inefficiency that is inherent in a system of monopoly, discretion, and unaccountability, coupled with the absence of any evidence that the amounts of corporate fines are efficiently set in terms either of deterrence or punishment. As I will argue, the current regime distorts both investment in prosecution and investment in corporate governance. But there is another reason, perhaps a bit more abstract but I think of equal importance. The current system undermines the rule of law, for it sidesteps almost entirely the jurisprudence of crime and punishment.

\(^{20}\) Thompson, *supra* note __ at n.5 (describing the application of his analysis to corporations).
Perhaps as important, the exercise of understanding the current pretrial diversionary regime as a corrupt one provides us with an analytical tool to help determine when developments that might be considered evolutions in legal practice reach a stage where they pose a danger to the integrity of the legal system. The problem of corrupt law enforcement regimes in the United States is quite real but often opaque because of the apparent compliance of law enforcement personal with legal standards permitting broad discretion and little accountability. When we appreciate that a practice that appears to be legal in fact transcends legality we can be vigilant in the need for reform.

Pretrial diversion presents this case. Legislation that would set guidelines for pretrial diversion agreements has been languishing in Congress since 2008. Such legislation would change the corrupt regime into one that is legal precisely by ameliorating the dimensions of opacity and unaccountability that currently render it illegitimate. I suspect that were Congress to understand the corruption – and hence the dangers – the current system embodies, legislation would flow faster.

How would a regime of individual prosecution and prison for wrongdoers correct these problems? I will leave most of the discussion for later, but for now simply want to observe that such a system would limit prosecutorial discretion by the entire infrastructure of criminal procedure built precisely for that purpose (including plea bargains which require judicial oversight). Moreover, by creating far greater transparency through the use of the judicial system, as well as putting prosecutors on the spot for using the sanctioned violence of the state against individuals, it would restore accountability to the entire process. Under such circumstances, corruption (in Klitgaard’s formula) could not exist and its untoward effects would be eradicated.

Would it be sufficient for prosecutors to bring proceedings against corporations rather than individuals? After all, such proceedings invoke the same accountability mechanisms and limits on prosecutorial discretion (once charges are brought) as in the case of actions against individuals. Probably not. For it is here that we encounter the challenges of corporate governance, challenges that have led to a virtual abandonment of individual liability under state corporate law. To

21 Rachel Aviv, *Your Son is Deceased*, The New Yorker, February 2, 2015, p.36, reporting on the corrupt culture of the Albuquerque, New Mexico, police department that has resulted in an apparently extraordinary number of civilian killings by police officers. Recent events in Ferguson, Missouri, and New York City suggest that corruption under the color of law may be a widespread phenomenon. In light of the stakes at issue, especially when it comes to human life, it is critical that we ask these hard questions.

22 I will argue *infra* that such legislation is unlikely to solve the core problems posed by pretrial diversion.

23 But see Langevoort, *supra* note _ at __.
leave individual accountability to the corporate governance process is, at least in the case of more senior managers, to leave it to nothing at all. In the absence of punishing and potentially destructive corporate fines that raise the specter of the kinds of collateral consequences pretrial diversion agreements are said to avoid, \textsuperscript{24} I very much doubt that culpable executives would be likely to suffer significant consequences. \textsuperscript{25}

While judicial review would remove the taint of corruption from the current regime, it likely would leave pretrial diversion as inherently inefficient. With deterrence as the overwhelming rationale for corporate criminal liability, internal corporate governance and management procedures are critical. Yet, as a matter of corporate law, these are matters of business judgment for the corporation's board. Indeed it is hard to imagine more essentially business judgments (at least at the board level) than the governing structure of an enterprise. Precisely for this reason, such decisions are protected from questioning by state law except in the most egregious of cases. What are such cases? Largely where the corporation or its officers or directors are convicted of crime or crippling conflict of interest. \textsuperscript{26} The infrastructure of modern corporate law has developed over the course of a century and works reasonably well. It is hard to imagine the argument for replacing managerial judgment with judicial judgment in the case of a pretrial diversion agreement.

I proceed as follows: Part I is a brief review of the literature on corporate criminal liability. It is followed, in Part II, by an analysis of the current regime as a corrupt enterprise and the problems it creates. Part III concludes.

I. The Scholarly Landscape of Pretrial Diversion

a. Background

Pretrial diversion agreements are a phenomenon of this century. Prior to 2003, little more than a dozen of these agreements existed. More than 250 have been entered into during the ensuing years. \textsuperscript{27} That said, it appears that the practice is not a phenomenon that is spread across the prosecutorial board. The use of DPAs

\textsuperscript{24} But see Uhlmann, supra note __ at 1312-15, 1322, challenging this justification for pretrial diversion.

\textsuperscript{25} My conclusion might be different in the case of a corporation with highly concentrated activist ownership. In such a case, however, the argument against collateral harm ("innocent shareholders") would be weak. See Lawrence E. Mitchell, The Innocent Shareholder: An Essay on Compensation and Deterrence in Securities Class Actions, 2009 Wis. L. Rev. 243 (arguing that shareholders' role in corporate governance can defeat claims of innocence when corporation is punished).

\textsuperscript{26} In re Caremark International Inc. Derivative Litigation, 698 A.2d 959 (Del. Ch. 1996)

\textsuperscript{27} GARRETT, supra note __ at 7.
and NPAs appears concentrated in the Criminal Division of the United States Department of Justice as well as the United States Attorneys Offices in the Southern and Eastern Districts of New York, the Central District of California, and the districts of Massachusetts and New Jersey.\(^{28}\) Even in these offices, the number of pretrial diversion agreements pales in comparison to the number of actual corporate prosecutions.\(^{29}\) But the rapid increase in pretrial diversion agreements, as well as their use against high profile defendants (with high profile fines) by high profile prosecutors, makes them a subject of interest.

The agreements share some general characteristics. In exchange for an admission of wrongdoing and, not infrequently, the waiver of privileges by specified corporate employees, substantial financial penalties, and agreed-upon internal corporate reforms, prosecution will be deferred (or not instituted) for a period of time.\(^{30}\) Upon satisfactory completion of the contractually-agreed term (typically a couple of years), the potential for prosecution will evaporate. The threat of prosecution hangs over the corporation during the term of the agreement, with the often-criticized and rather draconian provision that breach is determined solely by the prosecutor’s office in an unreviewable decision. Variations in these agreements include the appointment of a corporate monitor in substitution for, or connection with, internal reforms. It is further notable, as Jennifer Arlen has observed, that prosecutors seek pretrial diversion agreements not only from corporations that are subject to conviction but also those “that are merely potentially subject to conviction.”\(^{31}\) Regardless of their utility in crime prevention, this observation highlights the extent to which the use of pretrial diversion serves as an end-around the criminal process and should be a matter of real concern.

Pretrial diversion agreements operate much like other contracts, unconstrained except for the interests of the parties. That said, they have been subjected to a fair amount of criticism suggesting that they are, in many ways, not like other contracts at all.\(^{32}\) First is the largely one-sided nature of the negotiation. Commentators have observed that the extraordinary consequences to a corporation of criminal prosecution leave boards and managers little meaningful choice but to

\(^{28}\) Uhlmann, *supra* note __ at 1317-18, reporting and analyzing reasons for this concentration.

\(^{29}\) *Id.* at 1315-16.

\(^{30}\) Krawiec notes that these internal reforms rarely deter. Kimberly Krawiec, *Cosmetic Compliance and the Failure of Negotiated Governance,* 81 Wash. U. L. Q. 487 (2003); Cunningham suggests the use of tailored corporate governance reform to achieve this end. Cunningham, *supra* note __. *See also* Hamdani and Klement, *supra* note __ at 275 (noting that compliance measures cannot be expected to eliminate crime).

\(^{31}\) Arlen, *Removing Prosecutors,* *supra* note __ at 62.

\(^{32}\) Cunningham, *supra* note __ at __.
enter into such arrangements.\textsuperscript{33} In addition to potentially larger penalties following trial and conviction are the often-significant legal fees to be incurred by the defendant as well as the disruption in operations, loss of employee time, and other such negative consequences of extended and highly public corporate litigation. And while some commentators have (correctly, I think) noted that the problem of collateral consequences is overstated,\textsuperscript{34} it is also true that all of these negative dimensions of fully defending a criminal case can have untoward effects on firm value (and therefore shareholders), profitability, leading to increased pricing (and therefore consumers) and, potentially and as a result of these, employees.

While unrestrained, the Justice Department has provided some guidance to prosecutors as to when to offer pretrial diversion agreements and their appropriate general terms. David Uhlmann lays out the history of this guidance, demonstrating rather clearly that policy chased practice almost from the beginning of their use, and that the department’s approach to these agreements was “a policy in search of a rationale.”\textsuperscript{35} A consistent theme throughout this history is the value of corporate cooperation during the course of a criminal investigation, and the weight to be given such cooperation in determining whether to offer pretrial diversion and the terms on which it is to be offered. This desire for cooperation places the corporation in a vulnerable position, and is part of the genesis of the criticisms of pretrial diversion’s one-sidedness.\textsuperscript{36}

\begin{itemize}
  \item \textsuperscript{33} Anthony S. Barkow and Rachel E. Barkow, \textit{Introduction}, in \textsc{Barkow and Barkow}, \textit{supra} note \_ at 1,2.
  \item \textsuperscript{34} Uhlmann, \textit{supra} note \_ at 1321; Gabriel Markoff, \textit{Arthur Andersen and the Myth of the Corporate Death Penalty: Corporate Criminal Convictions in the Twenty-First Century}, 15 J. Bus. L. 797 (2014); Henning, \textit{supra} note \_ at 1419. The exception to this overstatement appears to be in regulated industries where criminal conviction can result in the forfeiture of crucial licenses or government contractor status. [cite]
  \item I find it especially interesting that few of the discussions of collateral consequences discuss the fact the pretrial diversion agreements almost always require the corporation to admit wrongdoing, sometimes in detail. \textsc{Garrett}, \textit{supra} note \_ at 60-1. Although not criminal convictions that can result in license forfeiture or the like, these are admissions of wrongdoing that can evoke the same kind of disapprobation as criminal convictions. That such admissions have not wrought the kinds of collateral damage often discussed in the literature suggests that it is in fact an overblown concern.
  \item \textsuperscript{35} Uhlmann, \textit{supra} note \_ at 1315. Institutional circumstances like this can create conditions under which corruption can develop. Kelly D. Martin, Jean L. Johnson, and John B. Cullen, \textit{Organizational Change, Normative Control Deinstitutionalization, and Corruption}, 19 Bus. Ethics Q. 105, 109 (2009).
\end{itemize}
While it is undoubtedly true that negotiations over pretrial diversionary agreements are largely one-sided, one fact stands out: The criminal investigations leading to these agreements generally are not accompanied by the prosecution of individuals.\textsuperscript{37} This doesn’t necessarily indicate an implicit bargain between prosecutors and corporate officials. Indeed, one commentator makes the sensible observation (upon which I will later elaborate) that criminal convictions of individuals are, for a number of reasons, more difficult to obtain than negotiated corporate settlements. Moreover, the adequacy or inadequacy of individual prosecutions is one factor federal prosecutors consider in determining whether to offer pretrial diversion.\textsuperscript{38} But the simple fact remains that pretrial diversionary agreements pretty much settle matters between the government and the corporation, a fact that cannot have escaped the attention of corporate executives and their lawyers.

\textit{b. Improving Efficiency/ Ensuring Deterrence}

Pretrial diversion agreements appear to be here to stay, and scholars have gamely engaged in the work of making them better. The accepted deterrent calculus is grounded in Gary Becker’s theory that the decision to commit a crime is a product of cost-benefit analysis,\textsuperscript{39} leading to the conclusion that optimal deterrence comprises the net harm caused by the crime divided by the probability of its detection. It is important to note that the theory assumes, undoubtedly correctly, that we cannot deter all crime nor, given the cost, do we want to. Rather, the calculus determines the optimal level of deterrence.\textsuperscript{40}

It seems sensible, for my purposes, to accept Becker’s theory. While many criminal acts are, undoubtedly, committed without such a clear economic calculus,\textsuperscript{41} corporate crime takes place within an economic institution engaged in economic activity, by actors also engaged in economic activity. The corporation’s vicarious liability for its agents’ actions depends upon some benefit of those actions to the corporation, and we presume as well that the agent anticipates some economic benefit from her crime (because it is conducted within an enterprise whose metrics

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\textsuperscript{38} Uhlmann, \textit{supra} note \_.


\textsuperscript{40} For a nice discussion see Cindy R. Alexander and Mark A. Cohen, \textit{The Causes of Corporate Crime}, in Barkow and Barkow, \textit{supra} note \_ at 11.

\textsuperscript{41} I here make the obligatory citation to Fyodor Dostoevsky, \textit{Crime and Punishment}.
and rewards are economic). Given all of this, it would seem perverse to abandon economic theory for something else.

All of that said, criminal liability is hardly the only avenue we have for policing corporate misbehavior. Although corporate criminal liability appears to have grown (although not at the same rate) with the regulatory state, the regulatory and administrative apparatus, at least of the federal government, is much more richly and pointedly honed to establish standards of corporate conduct, police them, and to punish violations of them as well. In fact the most prominent criminal investigations resulting in pretrial diversion involve the pharmaceutical industry (regulated by the Food and Drug Administration) and the financial industry (regulated by a variety of administrative agencies), as well as general financial and securities fraud (regulated by the Securities and Exchange Commission). Indeed, pretrial diversion agreements often demand substantial civil penalties in addition to the fines negotiated by the Justice Department. Substantial and important commentary exists either advocating the complete elimination of corporate crime in favor of regulatory and civil enforcement or the design of corporate monitoring and compliance measures by more expert agencies. Others argue that reform should be based upon principles and practices of corporate law, and one scholar, Miriam Baer, has suggested an ingenious insurance regime as a substitute for mandated internal compliance procedures.

42 The first United States Supreme Court case to establish the ability to hold corporations criminally liable is New York Central & Hudson River Railroad v. United States, 212 U.S. 481 (1909), a case involving the Elkins Act which was a regulatory measure to improve antitrust enforcement against the railroads, diluted from Theodore Roosevelt’s initial ideas. Lawrence E. Mitchell, The Speculation Economy: How Finance Triumphed Over Industry (Berrett-Kohler: 2007). The case took place towards the end of the first significant development of the federal regulatory state, the second taking place during the administration of Franklin D. Roosevelt. See generally, Richard Hofstadter, The Age of Reform: From Bryan to FDR (Vintage: 1955); Herbert Hovenkamp, Enterprise and American Law, 1836-1937 (Harvard: 1991); Morton Keller, Regulating a New Economy: Public Policy and Economic Change in America, 1900-1933 (Harvard: 1990).

43 A complete list is available at Brandon L. Garrett and Jon Ashley, Federal Organizational Prosecution Agreements, University of Virginia School of Law, at http://lib.law.virginia.edu/Garrett/prosecution_agreements/home.suphp.

44 Garrett, supra note ___ at 6.

45 Fischel and Sykes, supra note __; Epstein, supra note __. Langevoort appears to be in this camp. Langevoort, supra note ___.

46 Arlen, Removing Prosecutors, supra note __; Buell, supra note __; Henning, Should the Perception of Corporate Punishment Matter?, 19 J. L. Pol’y 83, 86 (2010);

47 Miriam H. Baer, Organizational Liability and the Tension Between Corporate and Criminal Liability, 19 J.L. Pol’y 1 (2010); Cunningham, supra note __;

c. Individual Liability

To the extent the literature discusses individual liability at all, it is in the context of observing the greater ease and efficiency for prosecutors of going after enterprises rather than individuals. Corporations simply are easier targets. Corporations can pay fines and reform processes, but they cannot go to prison. And, while there is discussion in the literature about the stigmatizing effect of criminal convictions on corporations, the diffuse responsibility for criminal acts absorbed in the corporate conviction does not avail the individual defendant who stands alone, convicted, stigmatized, and, possibly, imprisoned. (I again observe that the admission of corporate wrongdoing contained in pretrial diversion agreements doesn't appear adversely to affect corporations and, indeed, one observer has noted that stock prices go up after such agreements are announced.)

All of this suggests that corporations as defendants have less incentive to fight charges than do individuals. Faced with the decision to indict and prosecute an individual, the prospect of the full panoply of the laws of criminal procedure (along with the required criminal standard of proof as beyond a reasonable doubt), and faced as well with the likely adequate substitute of a corporate defendant that can be expected to be more compliant, the prosecutorial decision to avoid charging individuals seems easy. But the corporation is more than a compliant substitute. In general, a corporation can pay significantly more in fines than can an individual, so headline-grabbing results are more assured. In addition, to the extent that prosecutors believe that internal reform can in fact deter corporate crime, they may believe that corporate prosecution can be more effective as a deterrent than individual prosecution.

Prosecuting corporations appears to be in prosecutors' self-interest. It is generally believed that public servants, like prosecutors, have little or no incentive to self-deal because they are salaried employees on a fixed pay scale working in an organization that is not directed towards maximizing profit. Thus private enforcement, with the promise of damages and large attorneys fees, has been viewed as a necessary supplement to resource-constrained public enforcement in which economic incentives are lacking. But there is reason to think that prosecutors also act in self-interest and have significant incentives to bring actions, and those incentives privilege corporate over individual prosecution. I have already noted the relative ease that prosecutors have by targeting corporations rather than individual defendants. Margaret Lemos and Max Minzner demonstrate that maximizing financial recovery is in fact in the self-interest of prosecutors. This is especially

49 Fishbein, supra note __. It is not clear whether such agreements add real value because Fishbein does not report whether stock prices declined on the announcement of the criminal investigations nor by how much.

50 Margaret Lemos and Max Minzner, For-Profit Law Enforcement, 127 Harv. L. Rev. __-(2014)
obvious where, as is increasingly the case, the enforcement agency gets to keep all or a substantial portion of the agreed-upon fines. Moreover, large fines are a clear metric of success, especially in light of the less-clear measurements provided by internal corporate reform.

Pretrial diversion in corporate criminal proceedings appears to be here to stay. Scholars, sometimes crankily, accept this reality, and have produced some excellent work in the service of improving the efficiency of these agreements. The trend toward corporate prosecution, in contrast to that of individuals, as well as the incentives prosecutors have to continue this practice, leads to the conclusion that an increase in individual criminal proceedings is unlikely. This would largely be unremarkable, except as a matter of interest, if corporate prosecutions could efficiently deter corporate crime at an optimal level. As a matter of theory, at least, there appears to be no reason why this is not the case.

And there matters might end if the efficient deterrence of crime were our only concern. But embedded in this entire discussion is a concern with the criminal justice system itself or, more broadly, the role of our government in using the sanctioned violence of the law in service to our society. Scholars have observed the extent to which the pretrial diversionary regime allows prosecutors to shortcut the rather elaborate infrastructure of rules and processes we maintain to achieve some balance between the state’s monopoly on legal violence and the rights of individuals. This is a problem that cannot be addressed by concerns with efficiency alone, although I will have occasion to return to efficiency concerns later. Rather, the observation requires us to ask whether the current corporate criminal regime is serving the ends of both law and justice. It requires us to step back from the important but more targeted question of efficient corporate behavior and look at the bigger picture.

II. Corruption

a. An Overview of the Problem

The view from above reveals a system that operates independently of our laws but uses those laws to its own end. There is nothing necessarily troubling about this on its face. After all, we have long understood that a system of social norms runs parallel to our laws. While social norms have multiple sources, we have long accepted that many of our relationships are legal in nature but not precisely congruent with our laws. Instead they are negotiated and formed in the shadow of the law, with law providing a default failsafe in the event that negotiations don’t succeed. The corporate criminal regime of pretrial diversion is such a normative

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51 Id. at 864.
52 Infra Part II d.
53 Robert H. Mnookin and Lewis Kornhauser, Bargaining in the Shadow of the Law: The Case of Divorce, 88 Yale L. J. 950 (1979); ROBERT ELLICKSON, ORDER WITHOUT LAW:
system, one that operates in, as Epstein puts it, “the shadow of the grand inversion” of civil liability and criminal law. But the problem is more than one of inversion. When a normative system – especially one so dependent upon the law as divorce, commercial contracting, property disputes, and other “legal” relationships – develops in the shadow of the law, the law itself is the substantive backstop upon which negotiations take place. Parties understand the way the law is likely to arrange their affairs if negotiations fail, and so bargaining power itself is ordered by the default legal rules.

The corporate pretrial diversion regime is quite different. It is essentially lawless. True, there are predicate crimes that can and do create the opportunity for enforcement although, as Arlen has observed, pretrial diversion tactics are sometimes used against corporations that are only “potentially” liable. But the imbalance of bargaining power created by the government’s threat advantage, as well as the black box of negotiations over terms and the lack of ultimate accountability by prosecutors, create real questions as to whether these negotiations take place in the shadow of the law at all.

I recognize that this last statement is controversial, but bear with me. It is certainly true that many crimes indicate the appropriate penalties or range of penalties, refined and supplemented in the case of corporate crime by the Organizational Sentencing Guidelines developed by the United States Sentencing Commission. But these are not the principal penalties that lead to pretrial diversion agreements. In fact it appears that in practice, both in convictions following trial and in pretrial diversion agreements, penalties tend to be assessed at the very low end of the sentencing guideline ranges. Rather, the driving incentive for corporations to enter into these agreements appears to be the fear of collateral consequences. These collateral consequences can range from the termination of necessary licenses and permits to prohibitions on government contracting, damage to corporate value, and, in the very extreme (yet unlikely) case, the destruction of


54 Epstein, supra note __ at 41.

55 Peter Reilly agrees but for different reasons, noting that the absence of transparency in DPAs in Foreign Corrupt Practices Act cases leaves defendants without precedent on which to rely. Peter Reilly, Negotiating Bribery: Toward Increased Transparency, Consistency, and Fairness in Pretrial Bargaining Under the Foreign Corrupt Practices Act, 10 Hastings Bus. L. J. 347, 379; see also A Mammoth Guilt Trip, The Economist, Aug. 30, 2014, for a discussion of the consequences of lack of transparency; Baer, supra note __ at 1062 (opacity of process).

56 Arlen, supra note __ at __.


58 GARRETT, supra note __ at __.

59 Barkow and Barkow, supra note __.
the firm itself. There are also the costs, the continuation of adverse publicity, and the time demands on corporate employees that a criminal trial would entail. In addition, and largely absent from the literature, is the very distinct possibility that if law enforcement officials have to go to the trouble of prosecuting the corporation, they might well include individual executives and employees as defendants. I suggest that it is these extra-legal concerns that form more of the context of the bargain than the legal elements of the alleged crime and sentencing guidelines.

Contrast the case of plea bargains. There, the requirement of judicial approval provides some, if sometimes weak, assurance of disciplined negotiations and, indeed, the very real shadow of the law. And where the defendant is an individual, the incentives to fight I mentioned above help to balance out the negotiating power. None of this exists in the corporate criminal regime as currently practiced. Add to this mix the incentives prosecutors have to score big and quickly against corporate defendants, and a different picture emerges.

What emerges is a corrupt system. We have on one side a party possessing monopoly power, practically complete discretion, and little or no accountability, such power exercisable over a party with very strong incentives to defray the use of that power. Please notice that the preceding sentences are descriptive. While “corrupt” is often a normatively-loaded term, even the scholarship of corruption accepts that it need not always be venal. Nor am I accusing anybody of bad faith. Rather, I am identifying a situation that has developed that has the potential to do significant harm, even if that harm is caused by actors behaving in good faith. In fact it is precisely because I assume federal prosecutors to be acting in good faith that it is all the more important to call the phenomenon what it is, because we are unlikely fully to appreciate its harms and thus unlikely to correct it if we fail to see it starkly.

b. The Contours of Corruption

When we think about corruption, I suspect that typically we think about an individual taking bribes in exchange for a public service (or public forebearance).  

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60 The shadow of Arthur Andersen looms large in the literature. Nothing like its demise has happened since, and it is generally seen as an unlikely consequence in the literature. There are enough other potential consequences of criminal litigation to provide executives with incentives to bargain out. But in one sense, it doesn’t matter if corporate destruction is unlikely – it may be enough that executives fear that possibility to provide additional incentives for quick resolution of criminal matters.


62 The literature on corruption has grown on a parallel track (although for different reasons) to the literature on corporate crime. For an excellent survey see Jain, supra note __. It is important to note that most of the corruption literature is focused in the area of economic development, because it is in the context of economic
Even a superficial glance at the literature reveals the predominant image of the fin d’siecle Tammany politician, George Washington Plunkitt who famously is quoted: “There’s an honest graft, and I’m an example of how it works. I might sum up the whole thing by sayin’: “I seen my opportunities and I took ‘em.”” (Mr. Plunkitt might soon be replaced by the contemporary New York politico, Sheldon Silver.) More formally, Susan Rose-Ackerman uses the “umbrella definition” of corruption as “the abuse of public power for private gain.” Our tendency to think in terms of corruption this way makes it perhaps more difficult to understand a system as corrupt in which officials appear to be performing their duties honestly. It is precisely because institutional corruption is so easy to miss that it is important to identify it when it exists.

To explain. Institutional corruption occurs in circumstances where in fact public officials may be performing their tasks honestly, at least as far as individual motives are concerned. Yet the incentives and patterns that develop wind up distorting legitimate legal processes for political or institutional gain, whether in terms of agency reputation, career advancement, political success or, as Lemos and Minzner have pointed out in the case of pretrial diversion agreements, agency profit.

One might simply conclude that all of these goals are endemic to any institution, cannot be eradicated, and indeed create incentives for superior individual performance. That would be true. But these same incentives create the possibility that individuals pursuing these goals in the institutional context could pervert legal processes in order to achieve them, much in the same way that private-sector compensation schemes can create incentives for perverse behavior.

devlopment that corruption might be most damaging. That said, the structure of the arguments and concerns about corruption transfer reasonably well to other contexts, and I have so adapted them here.

63 http://historymatters.gmu.edu/d/5030/
66 Thompson, supra note __. Lemos and Minzner, supra note __.
67 For a general discussion of the ways that executive compensation structures can create perverse incentives see LAWRENCE E. MITCHELL, CORPORATE IRRESPONSIBILITY: AMERICA’S NEWEST EXPORT (Yale 2002).
It is not necessary to institutional corruption that individuals act from bad motives. What is significant is the “cumulative impact” of many individual decisions on the institution’s behavior and practices. That cumulative impact causes the institution to pursue goals that may not be democratically sanctioned. In the case of pretrial diversion, it causes the more subtle situation in which the institution pursues its goals in a manner that is not democratically sanctioned. It also causes the misallocation of resources.

Another way of looking at this type of corruption is what Arvind Jain calls “grand corruption.” He defines grand corruption as “the acts of the political elite by which they exploit their power to make economic policies.” In the context of pretrial diversion, this would be the Justice Department using its power to restructure the internal workings of corporations and perhaps entire industries. Like institutional corruption, grand corruption arises from agency problems, here the case of politically unaccountable prosecutors wielding power on behalf of the electorate. Like institutional corruption, it results in the distortion of public behavior, in this case corporate managers agreeing to conform internal corporate operations to prosecutor’s demands. The benefit of looking at the pretrial diversion regime through the additional lens of grand corruption is that it focuses us on one possible harm arising from corruption in the corporate criminal context, the possible distortion in the Justice Department’s choice of targets, a topic to which I shall later return.

It is important to emphasize again that my description of the pretrial diversion regime as corrupt is not an assertion of evil intent or criminal activity. It

68 Thompson, supra note __ at 16. See also Kelly D. Martin, Jean L. Johnson, and John B. Cullen, Organizational Change, Normative Control Deinstitutionalization, and Corruption, 19 Bus. Ethics Q. 105 (2009) (showing how corrupt behavior can infiltrate organizations in the absence of bad motives).
70 Jain, supra note __ at 73.
71 Anthony S. Barkow and Rachel E. Barkow, Introduction, in BARKOW AND BARKOW, supra note __ at 1,2. Barkow and Barkow describe the regime of compliance through pretrial diversion as analogous to the kinds of structural injunctions courts have used to supervise school districts and prisons.
72 Except in the broadest sense, prosecutors are not politically accountable under any circumstances, but their power is restrained by rules of criminal procedure, the defense bar, and the courts, in ways that are absent in the pretrial diversionary regime.
73 Prosecutors have no particular expertise in corporate governance or business management. Jennifer Arlen, Removing Prosecutors from the Boardroom, in BARKOW AND BARKOW, supra note __ at 63.
74 An interesting study of the non-conscious abuse of power is John A. Bargh and Jeanette Alvarez, The Road to Hell: Good Intentions in the Face of Nonconscious
is, rather, a structural argument, one that shows the characteristics of that regime to be those of an organization in which corruption exists. On one hand, this may appear to be no more than a simple claim about the way that individual behaviors within organizations become normative. Thus seen, one can perhaps understand the argument as one about the “banality of corruption.” Blake Ashford and Vikas Anand present a fascinating explication of just this process. The “three pillars” of institutionalization, socialization, and rationalization describe a process that is typical of the way values and behaviors develop within organizations, but for the somewhat more challenging fact that the values and behaviors they are interested in are criminal. Now, admittedly, the fact that they are interested in the way that criminal (or at the very least unethical) behavior is normalized does suggest that the mechanisms at work have to be somewhat more powerful than in the case of socially-accepted norms. But the basic process is the same. If criminal norms can become accepted and even celebrated in organizations, we can certainly expect to see the same for illegitimate behavior that appears to be within the bounds of ethics and legality.

None of this would matter in the case of pretrial diversions in the absence of harm. So, one might ask, what harm is done? I haven’t seen anybody writing about pretrial diversion accusing the Justice Department of targeting corporations in which there is no evidence of criminal wrongdoing. Why worry if prosecutors are in fact prosecuting, or at least investigating, likely criminals? Leaving aside questions of overall economic efficiency, to which I will later return, the more systemic and fundamental concern is a disregard of the democratic process. Our criminal laws are passed by Congress, fleshed out by administrative agencies, and prosecuted in courts. Democratic accountability, no matter how attenuated, exists at every level. This system has produced all of the burdens that law enforcement officials face in prosecuting crimes. But it disregards that process to the extent that self-interest (broadly understood) leads prosecutors to use their offices to evade these burdens.

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77 Thompson, supra note __ at 4, 5.
It is important to understand the damage created by the systemic nature of this perversion. As Thompson notes, “[r]ecognizing institutional corruption is not always easy because it is so closely related to conduct that is a perfectly acceptable part of . . . [institutional] life.” And its context of occurrence in continuing relationships makes it difficult not only to stop but “even to see the practice as corrupt.” Thus one of the dangers of institutional corruption is its ability to mask itself, to normalize, to appear as legitimate as other forms of institutional activity. We cannot see the very activity with which we should be concerned because it makes itself invisible.

We might not care about this dimension of institutional corruption in the absence of other harms. But there are other harms. There is, as I noted earlier, the possibility that the largely opaque and unaccountable system of pretrial diversion creates significant economic inefficiency. There is also the possibility that corruption of this nature can influence the Justice Department’s choice of targets in ways that may be suboptimal. But there is also the more fundamental harm that occurs when institutional corruption causes us to doubt the legitimacy of the system itself, doubt that seems imminent in the literature on pretrial diversion.

Let’s put all of this in the context of pretrial diversion. Despite interesting arguments that the corporate side of the equation is far more powerful than the government side, the general thrust of the literature treats the government as the more powerful party, certainly in the threat advantage that it possesses and the – justified or not – corporate fear of collateral consequences. That threat advantage is amplified significantly by the threat - -often inchoate in these negotiations but quite real -- of the prosecution of individual defendants. The government uses that threat advantage to persuade corporate defendants to forebear challenging the government’s use of its power to extract penalties, including internal corporate restructuring. No judge rules on the matter. No court reporter records negotiations. Admissions of wrongdoing may or may not relate to actual criminal matters with which the Justice Department is concerned. Fines are paid, the calculation of

78 Thompson, supra note __ at 7, 12.
79 Ashforth and Anand, supra note __ at 6, describe the process by which corruption internally becomes invisible.
80 Infra notes __-__ and accompanying text.
81 See Jain, supra note __ at 95 (discussing misallocation of public investment due to corruption).
82 GARRETT, supra note __ at__.
83 Barkow and Barkow, supra note __ at 1.
84 It might well be that the Justice Department would lose that threat advantage if it actually were to prioritize the pursuit of individual defendants. In that case, all of the reasons that individuals are more likely to fight than are corporations would emerge.
85 GARRETT, supra note __ at 60-2.
which is a mystery. More often than not, nobody goes to jail and the corporation gets on with its business. No determination beyond a reasonable doubt is made. The machinery of criminal procedure is never engaged. The Justice Department announces a victory. And sometimes it gets to keep the change.

The preceding description (admittedly done without nuance) does not describe anything like our normal legal process. Moreover, there is no law sanctioning this exception, and precious little policy guidance even within the Justice Department as to how, when, and why to employ it. It is a description of a process that should trouble us.

c. The Corruption Calculus

The notion of institutional corruption is a powerful tool for identifying and understanding the manner in which apparently legitimate (and even useful) activity can harm our political and legal processes. Another way of looking at the issue is to understand the conditions under which gains from corruption are possible.

Robert Klitgaard provides a straightforward, albeit “metaphorical,” formula for determining the conditions under which corruption gains are established: “Officials will have the opportunity to garner corrupt benefits as a function of their degree of monopoly power over a service or activity, their discretion in deciding who should get how much, and the degree to which their activities are accountable.” Thus:

\[ C = M + D - A \]

Where C is corruption, M is monopoly power, D is discretion, and A is accountability. It should be clear that the pretrial diversion regime satisfies this formula and thus creates the conditions under which corrupt gains are possible. The Justice Department has monopoly power; As it now stands, the opportunity to enter into a pretrial diversion agreement is within the sole power of the department. While the terms of that agreement are the result of bargaining between prosecutors and corporate officials, the literature raises significant concerns that bargaining conditions individually and systematically favor the

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86 The Organizational Sentencing Guidelines, supra note __, here provide some background but, as commentators have observed, the basis for calculating actual fines is opaque.
87 Lemos and Minzner, supra note __.
88 Uhlmann, supra note __.
90 In Part __ I discuss why this is true despite the frequent availability of civil and administrative enforcement of corporate violations.
government. And I add to that the observation that the inchoate threat of individual prosecution makes the government’s position that much more powerful. In addition to the monopoly power and largely unfettered discretion of prosecutors is the absence of accountability. There is no meaningful judicial (or other external) review of deferred prosecution agreements, and no judicial (or other external) review whatsoever of non-prosecution agreements. Thus it would appear that the pretrial diversion regime satisfies Klitgaard’s conditions for corruption gains.

One might object that the Justice Department doesn’t really have monopoly power. After all, as I previously noted, administrative and regulatory agencies typically overlap with criminal enforcement. Thus one might see the landscape more in the light that Shleifer and Vishny described in examining the relative efficiency of governmental regimes in the bribe-taking context; bureaucrats competing to provide public goods is the arrangement most likely to reduce bribes. Put in the context of this discussion, multiple agencies seeking to prosecute the same wrongdoing diminish the ability of any to exercise monopoly power.

But the parallel isn’t quite right. In the first place, as many scholars have observed, administrative and regulatory agencies often work together, so the situation is more akin to a cartel than to independent monopolists seeking rents. Moreover, the Justice Department does have one very significant monopoly, the monopoly to designate behavior as criminal, which of course includes the monopoly to seek imprisonment as well as other criminal remedies. This distinction strikes me as quite important, especially if, as I hypothesize, the inchoate threat of imprisonment is an important dimension of the department’s threat advantage. It also has a monopoly on the threat of causing the kinds of collateral consequences to which the literature attributes the department’s bargaining power. And while I take no position here on corporate stigmatization that accompanies a corporate criminal conviction, some commentators have argued that such stigmatization is damaging and real.

It is for these reasons, too, that the parallel regime of private enforcement through civil litigation fails to mitigate the Justice Department’s monopoly power. While it appears that civil fines (as well as regulatory and administrative fines) dwarf monetary amounts assessed by the Justice Department in pretrial diversion

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91 Discussed infra at notes ___-__ and accompanying text.
92 Andrei Shleifer and Robert W. Vishny, Corruption, 108 Q. J. Econ. 599 (1993). I should add that the bribery regime for which this works is what they call bribery without theft. Although the situation I describe is not one of actual bribery, this description largely fits.
93 Garrett, Collaborative Prosecution, supra note __.
94 Henning, supra note __ at 1419; Dan-Cohen, supra note __.
agreements,\textsuperscript{95} it too lacks the very significant force of criminal sanction and can easily be seen simply as a cost of doing business.

d. The Use of Pretrial Diversion Can Misallocate Resources

Corruption can have the effect of misallocating resources.\textsuperscript{96} The current pretrial diversion regime can misallocate resources in two respects: (i) it can misallocate prosecutorial resources, and (ii) it can misallocate corporate resources.

i. Enforcement Resources and Penalties

I take as a given that the basic goal of corporate criminal liability is to enhance social welfare.\textsuperscript{97} Leaving aside the contested question of whether a regime of corporate criminal liability does this at all, there is significant reason to question whether the pretrial diversion regime is welfare-enhancing. There is reason to believe that the growing use of deferred and non-prosecution agreements distorts both the investment of enforcement resources and the determination of corporate fines.

Pretrial diversion agreements tend to be concentrated in the types of crimes and industries they cover. Various types of fraud, Foreign Corrupt Practices Act prosecutions, and FDA violations seem to dominate. Financial firms and pharmaceutical companies are among the biggest and most predominant counterparties to pretrial diversion agreements.\textsuperscript{98}

While I am quite sure that no corporation’s management would be happy with a criminal investigation or prosecution, these types of actions do seem to have some commonalities. Financial institutional integrity is essential to attract and keep business and thus to firm value. And pharmaceutical companies are also quite sensitive to reputational harm, as Johnson & Johnson’s 1982 Tylenol crisis illustrates.\textsuperscript{99} Moreover, the financial and pharmaceutical industries both are heavily regulated, depend upon federal licensing and, in the case of the latter, also significant government contracting, and thus are especially susceptible to the threat of collateral harm following criminal convictions. It hardly strains the imagination to think that these types of companies would be particularly happy to avoid the possibility of conviction, along with the negative publicity a trial would entail, and

\textsuperscript{95} Garrett, supra note \textunderscore at \textunderscore.
\textsuperscript{96} Otahal, supra note \textunderscore at 401.
\textsuperscript{97} Arlen and Kraakman, supra note \textunderscore.
\textsuperscript{98} Garrett and Ashley, supra note \textunderscore.
\textsuperscript{99} For an account of this crisis see http://www.ou.edu/deptcomm/dodjcc/groups/02C2/Johnson%20&%20Johnson.htm
would be content to resolve its problems in one or a handful of news cycles with a pretrial diversion agreement.

For these reasons, one can infer that the Justice Department would be inclined to pursue these types of companies with these types of claims. They are easy targets which prosecutors can have reason to believe will negotiate quickly and in the government’s favor. Managerial incentives of these types of corporations match prosecutorial incentives to resolve matters quickly. Although incentives diverge when it comes to the terms of the agreements, prosecutorial leverage constrains managerial options.

These types of cases – particularly those involving financial fraud and other forms of wrongdoing by financial institutions – have a tendency to be complex. Complexity obviously would demand the dedication of greater prosecutorial resources were the matter pursued at trial, and discount the chances of government success. Here, again, the incentives to pursue pretrial diversion are significant from the government side.

The question of whether prosecutorial resources should be focused on these crimes is an empirical one that I am not prepared to answer. But, as a theoretical matter, it appears that the pretrial diversion regime distorts the pricing of corporate crime. The optimum penalty for corporate crime (as for any crime) is the social harm increased by a premium reflecting the probability of detection. Pretrial diversion distorts this calculus. Given the dominance of prosecutorial power and the incentives for corporate capitulation, it is as likely that enforcement resources are underallocated to corporate crime as it is that they are overallocated. The relatively low cost of achieving a deferred or non-prosecution agreement compared with a trial may in part be causative of the relatively low financial penalties observed by Garrett. That is to say, a cost-benefit analysis by prosecutors may lead to their acceptance of a penalty that, in relationship to the investment of enforcement resources, represents a fair return, but in light of the social harm the penalty is meant to redress is artificially low.

The probability of detection also becomes an ambiguous question. As Arlen has noted, prosecutors often pursue corporations that may have committed a crime. Given the incentives I’ve already discussed, a corporation’s entry into a deferred or non-prosecution agreement is not conclusive of the commission of a crime. It is, rather, evidence of probable cause coupled with the corporation’s desire to avoid prosecution. The kind of pricing mechanism that arguably exists in a

\[\text{Baer, supra note __ at 1048 (noting prosecutors’ claims of complexity of corporate violations generally).}\]
\[\text{Gary S. Becker, Crime and Punishment: An Economic Approach, 76 J. Pol. Econ.}\]
\[\text{169 (1968); Fischel and Sykes, supra note __ at 324.}\]
\[\text{Arlen, supra note __.}\]
market of crime and punishment doesn’t operate. Consequently, the likelihood that prosecutors got it right is diminished.

The relative absence of individual prosecution also causes distortions. In the classic cost-benefit analysis concept of criminal behavior, the potential criminal must factor in the possibility of punishment in his calculus. It is, in other words, part of the way the crime is priced. As we have seen, individual prosecution in the case of deferred and non-prosecution agreements is relatively rare. Moreover, as I have also noted, the desire to avoid individual prosecution may be one of the factors that encourages management to enter into these arrangements. If we remove the likelihood of individual punishment from the calculus – that is to say, if we remove one of the significant inputs, the cost-benefit analysis is distorted. For this reason, it may well be that the pretrial diversion regime not only causes inefficiencies in prosecution but diminishes efficient deterrence as well.\(^\text{103}\)

One might, as a theoretical matter, argue that both prosecutors and executives are aware of the relative rareness of individual prosecution and so discount it as part of their calculations. That is to say, if prosecutors never charged individuals, the calculus would work as well as if they always charged individuals. But in fact prosecutors sometimes charge individuals, and there is no pattern evident to me, at least, of when this is likely to occur. Consequently, both prosecutors and corporate actors calculate crime and punishment in an aura of uncertainty. It is almost certainly the case that pricing then is wrong.

These observations demonstrate the manner in which the corrupt regime of pretrial diversion has the potential to misallocate enforcement resources and misprice crime. By itself, this is enough to raise serious concerns about the pretrial diversion regime. I would also suggest that if individual indictment were a regular part of the process, prosecutorial leverage would considerably diminish, putting these types of corporations and crimes perhaps on a par with other types.

\textit{ii. Corporate Resources}

As many commentators have observed, the pretrial diversion regime has the potential to misallocate corporate resources.\(^\text{104}\) Understanding the regime as corrupt also highlights this problem, just as any corrupt system has the potential to misallocate investment.\(^\text{105}\) These inefficiencies add to those created by the potential

\(^{103}\) Arlen has made the compelling argument that corporate prosecutions may lead corporations to underinvest in deterrence to avoid detection in the absence of countervailing benefits. Arlen, \textit{supra} note __.

\(^{104}\) Baer, \textit{supra} note __; Krawiec, \textit{supra} note __.

\(^{105}\) It is largely this effect on investment decisions that has led the corruption literature to be grounded primarily in the field of economic development.
for corporate criminal liability to create inefficient deterrence. Given the amount of commentary on this dimension of the problem, I will be relatively brief.

I start with Jennifer Arlen’s general critique of corporate criminal liability. Corporate criminal liability is, of necessity, vicarious liability. Leaving aside metaphysical questions or arguments for attribution, it is obvious that only individual actors can commit crimes. The crimes of corporations are derivative of these individual crimes. Criminal law cannot, therefore, deter corporations from committing crimes. It can only deter individuals from committing crimes.

Now the problem is that corporations are complex organizations, often comprised of hundreds or thousands of agents. Detection of criminal activity is quite challenging. Yet the vicarious liability of the corporation for its agents’ acts is strict. One might think that this would lead corporations to construct elaborate internal prevention and detection mechanisms. But, as Arlen points out, this is not necessarily the case. Strict corporate liability might lead managers to underinvest in deterrence and detection (or at least detection) because detection exposes a crime for which the corporation is strictly liable. Managers would be better off if the crime were undetected. So corporate criminal liability as it now stands is inherently inefficient.

Only if a corporation is given an incentive to detect crime (by offers of leniency and the like) is it possible to rectify this. Typically leniency includes some form of internal corporate reforms that make deterrence and detection more likely. While Garrett observes that some percentage of pretrial diversion agreements lack the requirement of internal reforms, the large majority require something. (I include the appointment of a corporate monitor as one of these).

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107 Arlen, Perverse, supra note __.
108 I am not sure I agree with Arlen’s point that individuals act to maximize their own utility, not that of the corporation, Arlen, supra note __ at 834, unless individual utility is taken so broadly as to be useless, but the point is not important to my argument nor to my acceptance of Arlen’s.
109 As many have noted, the requirement that the agent benefit the corporation in some way is a minimal condition.
110 Arlen, Perverse, supra note __ at 841 (noting that strict corporate liability probably cannot be made to be efficient).
111 Arlen, Removing Prosecutors, supra note __.
112 These are built into the Organizational Sentencing Guidelines promulgated by the United States Sentencing Commission as well as Justice Department policy. Uhlmann, supra note __ at __.
113 On the practice (and pitfalls) of appointing corporate monitors see Vikramaditya Khanna, Reforming the Corporate Monitor?, in Barkow and Barkow, supra note __ at 226.
Moreover, their consideration as a mitigating factor in the Organizational Sentencing Guidelines practically mandates that corporations adopt some form of deterrence and detection system.\(^{114}\)

Leaving aside the observation that these reforms shut the barn door a bit too late (and conceding that a going concern that has committed a crime might well do so again),\(^{115}\) the problem is that prosecutors have no particular expertise in corporate governance or management, and thus are unlikely counterparts (with the lion’s share of bargaining power) to construct efficient mechanisms. This observation has been made many times before.\(^{116}\) Commentators have called for reforms ranging from the more integral use of regulatory agencies in designing compliance systems, sensitivity to corporate governance and contracting realities, and even a rather ingenious system of insurance that internalizes both cost of compliance and project design within the corporation.\(^{117}\)

While all of these undoubtedly are improvements over the current prosecutor-driven system, I suspect that all of them (except the insurance scheme) would likely be suboptimal. The reason can be found in the structure of corporate law itself.\(^{118}\)

Courts have long recognized their own incompetence to evaluate the wisdom of business decisions. This recognition has taken the form of the business judgment rule. The business judgment rule casts courts in a hands off posture when confronted with the question of whether a board’s decision was proper.\(^{119}\) Limiting cases include situations in which the board (or members thereof) are conflicted in the decision at hand\(^{120}\) or, perhaps, when it has been derelict in its duty to monitor.\(^{121}\) But those limiting cases are few and far between. As a general matter,

\(^{114}\) As does state corporate law, Caremark, supra note __, although state law leaves its design to the discretion of the corporate board.

\(^{115}\) Garrett notes the corporate recidivism rate. Garrett, supra note __ at __.

\(^{116}\) Cunningham, supra note __.

\(^{117}\) Buell, supra note __; Lisa Kern Griffin, Inside Out Enforcement, in Barkow and Barkow, supra note __ at 110; Brandon L. Garrett, Collaborative Organizational Prosecution, id. at 110; Cunningham, supra note __; Krawiec, supra note __; Baer, supra note __.


\(^{120}\) Smith v. Van Gorkom 488 A.2d 858 (Del. 1985).

\(^{121}\) Caremark, supra note __. The failure to monitor might be implicated in pretrial diversion agreements where corporate mechanisms are so badly structured as to lead to infestation, but I suspect these situations are rare and there is no evidence that they dominate in the actual cases in which deferred and non-prosecution agreements have been executed.
courts leave boards to structure the internal workings of their corporations, and boards leave managers to execute and operate those structures.

While I might quibble (indeed, have quibbled) with the extent of judicial deference,\textsuperscript{122} time has shown the wisdom of the business judgment rule. Business is best (and most efficiently) left to business experts. There is nothing about deterrence and detection regimes that would suggest they be treated differently from other business decisions (except in the possible case of a pervasive corporate criminal culture). There is nothing about prosecutors that suggests they have more expertise in designing such systems than boards, let alone courts like Delaware’s that adjudicate business cases all the time but nonetheless refrain from making business judgments. It would seem on the face of it that prosecutors are more likely to get it wrong than to get it right. Getting it wrong not only affects compliance and deterrence; it also imposes costs in cash and in human capital on the corporation, costs that divert investment from productive activities.\textsuperscript{123}

Enter now the regulatory agencies. Most commentators see their role as a needed corrective to the absence of prosecutorial expertise. But I admit to being puzzled why one would think that a regulatory agency would get it right any more than a prosecutor. Regulatory agencies monitor corporate compliance with specific regulatory regimes, whether the offer and sale of securities, the manufacture and marketing of drugs, or the taking of deposits and making of loans. Certainly this gives the agency expertise in the specific regulations themselves, and presumably some knowledge of the business line being regulated. The SEC is expert on disclosure, accounting, and the mechanisms of securities trading.\textsuperscript{124} The FDA understands science and marketing. The Federal Reserve Board knows reserve requirements and interest rates. But these agencies are not business experts any more than are prosecutors. They have the advantage of knowing the regulatory landscape better. But matters of corporate finance, personnel, reporting structures, record-keeping, sales, marketing, real estate, and the like are beyond their expertise yet are integral to whatever business is run by the corporation at issue.\textsuperscript{125} True, the criminal liability asserted often concerns actions centered in the regulated area of the business. But it is hardly coterminous with the business itself. The imposition

\textsuperscript{122} I confess here that I was stimulated to look into this topic by a friend in the financial industry who one day complained to me that he had just returned from “yet another” pointless ethics seminar that stated the obvious and wasted everybody’s time.

\textsuperscript{123} Baker, supra note \_ at 333(noting that while securities laws are the most comprehensive federal laws regulating business, there is a “conceptual line” keeping the SEC out of corporate governance.

\textsuperscript{124} See also Baker, supra note \_ at 33-32 (noting that federal law forms a “fragmented overlay with particular legislation passed under one or more of Congress’s enumerated powers).
of a new infrastructure with a going concern may well have significant effects of which even regulators would be unaware, or at the very least, inexpert.

I’ve overstated my case a bit, and deliberately so. I don’t have to show that regulators are completely incompetent, only that they, too, are limited in overall business expertise. The logic of the business judgment rule would suggest that they, too, ought to refrain from making business decisions on behalf of the corporations they regulate and for the very same reason – to do so is to risk distortion and inefficiency. A pretrial diversion regime that imposes internal structures designed or strongly influenced by prosecutors and regulators is likely to be inefficient.

e. A Corrupt Conspiracy? Herein of Club Fed

I have thus far made the case that the current pretrial diversion regime is a corrupt enterprise causing the characteristic problems of corrupt organizations, namely diminished respect for the rule of law, distortion of democratic processes, and inefficiency in the use of public and private resources. This would be enough, I think, to call for reformation of the system, and indeed reform has been suggested. In addition to the reforms I have previously described, the possibility of judicial oversight or some other accountability mechanism exists to correct for at least one of the factors in the corruption calculus. But it would be unfortunate if reform were to focus solely on the prosecution side of the equation. It is possible to see the pretrial diversion regime as a conspiracy of corruption between prosecutors and corporate executives. The best way to dissolve the conspiracy is by the use of individual prosecution and prison sentences.

As with my theory of corruption more generally, it is unnecessary to think of this conspiracy as evilly motivated. Like my argument from corruption, it is a structural argument, showing that the behavior of the parties fulfills our understanding of conspiracy. As I describe it, the conspiracy simply is a consequence of both sides of the bargain following the incentives the system provides to achieve a result that is socially suboptimal but mutually beneficial. I have already discussed prosecutor’s incentives. How do corporate managers come in? After all, they have been portrayed – at some level, appropriately – as victims of the unbridled monopoly power and discretion of prosecutors. But that is too easy a conclusion.

Recall Klitgaard’s formula: C= M+D-A. This formula doesn’t so easily fit corporate managers (although Thompson’s analysis does). Monopoly power and discretion are contestable, since lower-level managers answer to executives and executives answer to the board in whose ultimate discretion lies the decision to

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126 The Accountability in Deferred Prosecution Act has been languishing in Congress for years.
127 Thompson, supra note _ at n.5 (describing the application of his analysis to corporations).
accept a DPA. Such monopoly power and discretion do appear in the relationship of the corporate entity to the board, but reification is not needed to sustain my point. For it is not necessary for a conspiracy to exist that each member participate in each element. Rather, the key element on the corporate side is accountability. Accountability does not and probably cannot exist in a system of prosecution solely dependent upon corporate fines and internal reforms.

Why not? Because levying fines allows the individual wrongdoers to punt to the corporation. Now you might object by noting that boards are subject to shareholder elections, executives to board appointment, and lower-level managers to executive appointment, and this is all true. But the evidence thus far suggests that the kinds of fines to which corporations are subjected are insufficient to cause internal corporate upheaval. While some have called for far more significant fines, one wonders how large they would have to be to offset the entropy of corporate culture and the potential benefits (to individuals within the corporation as well as the corporation itself) from criminal violations. It might be empirically demonstrated that such fines could be set sufficiently high (thus possibly creating greater incentives for corporate executives to fight sanctions rather than accede to pretrial diversion, eliminating one of the attractions of pretrial diversion to prosecutors). I suspect – although again the question is empirical – that fines set high enough to make corporate heads roll through the processes of corporate governance would have to be so high as to cause precisely the kinds of collateral damage that have been avoided through the pretrial diversion regime. For this reason, it is unlikely that fines could achieve the same results (in as fair and efficient a manner) as individual prosecution and imprisonment. If in fact they could, then fines would be sufficient to eliminate the incentives on the corporate side that lead to structural conspiracy. They might even ameliorate corruption by holding prosecutors accountable to the employees, shareholders, and customers of corporations paying such outsized fines. But for these same reasons, I very much doubt that a system of meaningful fines will – or should – be forthcoming.  

We are left with prison which, by the way, is where we put criminals – even those committing economic crimes – before the development of corporate criminal liability. But my argument is not one from nostalgia, nor even one of punishment and retribution. It is practical. In order to break a cycle of corruption that causes social harm, we need to change the incentives of those who participate in the corrupt enterprise. We could change prosecutors’ incentives. We could prohibit pretrial diversion for corporations and other organizations. To the extent that pretrial diversion is beneficial in some cases, though, outright prohibition would be undesirable. Congress could pass strict guidelines (or I suppose the Justice Department could create and publicize them). But it is almost certainly the case that any meaningful guidelines – that is to say, guidelines embracing the kinds of metrics that would ease the determination of compliance – would be too inflexible to be useful and pose the threat of the same kinds of inefficiencies that exist at present.

128 Garret calls for a meaningful increase in fines. GARRETT, supra note __ at __.

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We could insist upon meaningful judicial oversight. While this would ensure some
degree of prosecutorial accountability and thus diminish if not eliminate the corrupt
dimensions of pretrial diversion, it does not address the inefficiencies created by
externally-imposed infrastructures on the corporation (at least to the extent that
deterrence and detection mechanisms are desirable).

It is much easier to change the incentives of corporate managers. Individual
prosecutions with threatened prison time would rather quickly change their
incentives to settle out on terms that may be beneficial neither to the corporation
nor to society. Moreover, individual prosecution for crimes committed by
individuals with appropriate individual punishments imposed has the virtue of
engaging the procedural mechanisms and protections of criminal law, and landing
appropriate punishment on the only actors within the corporate setting that are
capable of bad acts – human beings.

One might reasonably object that I have just created circumstances in which
the practice of pretrial diversion would dissipate. I’m tempted simply to dismiss the
objection by arguing that if pretrial diversion does not serve the ends of criminal
justice, it ought to be eliminated. But that moves too fast. It is obvious that pretrial
diversion has the potential to (and may in some cases) save scarce public resources,
result in appropriate penalties, and improve corporate compliance. Using individual
prosecution can only enhance this. Prosecutors will not lose their incentives to save
resources and resolve a case quickly. But the balance of the bargain will change. For
once the possibility of individual prosecution looms, corporate managers will be
more likely to bargain aggressively on behalf of their corporations. If prosecutors
have been overly aggressive in singling out a particular corporation, managers
potentially threatened with prosecution will resist, and that resistance might be
informative.

III. Conclusion

The abuse of corporate criminals is probably not the most pressing item on
our national law enforcement agenda. From Staten Island to Ferguson, Missouri, we
have seen the abuse of individuals at the hands of law enforcement officers highlight
a problem that tears at our national fabric. The bad behavior of law enforcement
officers is allowed to persist because it typically takes place under the color of law
and legal processes, even when those colors start to fade. Law enforcement
organizations, like any other organization, are susceptible to cultural and behavioral
distortions that arise from the incentives of organizational actors and organizational
realities.

It is therefore crucial that we continually examine the behavior of these
organizations stripped of normative priors to determine their consistency with the
rule of law. Organizational corruption – departure from the rule of law, with all of

129 Rachel Aviv’s description of the Albuquerque police department is illustrative.
the consequences I’ve described – is especially pernicious precisely because it is so
difficult to detect. I have tried to construct a tool that can be used, at least in the
first instance, to determine whether we have our own probable cause to question
the legality of the behavior of those who are charged with enforcing our laws. It is
critical to our democracy that we continue to ask these questions.