# NOTES & COMMENTS

## A NEW USE FOR THE RESPONSIBLE CORPORATE OFFICER DOCTRINE: PROSECUTING INDUSTRY INSIDERS FOR MORTGAGE FRAUD

*by*
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*Mortgage fraud is widely perceived as the driving force behind the meteoric rise and fall of the housing market. Although the United States government expends substantial resources attempting to combat mortgage fraud, the legal doctrines currently used to prosecute those responsible are insufficient. Directly prosecuting the corporations responsible could exacerbate the fragile status of American banks, while directly prosecuting mortgage professionals is not feasible unless the executive directly and affirmatively encouraged false statements. This Note posits that the rarely-used, but far-reaching, Responsible Corporate Officer ("RCO") doctrine could be used to prosecute mortgage fraud. Unlike charges of aiding or abetting, the RCO doctrine only requires that the officer be aware of the wrongdoing and have authority to end the wrongdoing. As such, the RCO doctrine would be an effective tool for prosecuting executives of corporations most culpable for mortgage fraud.*



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## I. INTRODUCTION

Many believe that mortgage fraud played a starring role in the dramatic rise and fall of the housing market. In the time period leading up to the mortgage meltdown, lending institutions relaxed standards and rewarded mortgage professionals with commissions based upon the quantity—not quality—of loans closed. The combination of the lowered lending standards, skyrocketing home prices, and the securitization of loans masked the exponential rise in mortgage fraud.[1] Now, amidst a worldwide financial crisis, law enforcement faces increased pressure to prosecute those responsible for the billions of dollars in losses.[2] In response, the Federal Bureau of Investigation (FBI) now employs 65 Task Forces and as of April 2009 has 2,440 pending mortgage fraud investigations.[3] Additionally, Congress passed legislation to provide more funding for FBI agents and United States Attorneys to devote to the investigation and prosecution of crimes related to the financial crisis.[4]

But who should these resources target? Notwithstanding their glaring culpability, it is unlikely lending institutions will be prosecuted. High-profile prosecutions of corporations can lead to disastrous consequences, only exacerbating the economic turmoil.[5] The FBI acknowledges that because there are so many mortgage fraud cases to

[1] 155 CONG. REC. S4408-09 (daily ed. Apr. 20, 2009) (statement of Sen. Leahy) (stating that reports of mortgage fraud are up 682% over the past 5 years and up more than 2,800% in the past decade).

[2] Fbi.gov, Just the Facts: The Latest Mortgage Fraud Statistics, http://www.fbi.gov/hq/mortgage_fraud.htm (last visited Jan. 16, 2010) (citing estimation of the loss annually attributable to mortgage fraud at four to six billion dollars) [hereinafter Just the Facts].

[3] *Id.*

[4] Fraud Enforcement and Recovery Act of 2009 (FERA), Pub. L. No. 111-21, 123 Stat. 1617 (2009). To combat the growth in mortgage fraud, the legislation appropriates $165 million dollars for the Department of Justice to combat mortgage fraud.

[5] For example, the accounting firm Arthur Andersen, LLP was convicted of obstruction of justice relating to the shredding of tons of documents associated with its work for Enron Corp. After the firm was indicted, it went out of business, costing 28,000 people their jobs. *See, e.g.*, Carrie Johnson, *U.S. Ends Prosecution of Arthur Andersen*, WASH. POST, Nov. 23, 2005, at D1.

investigate, it can no longer simply pursue individual borrowers. Instead, the government vows to target "industry insiders," the mortgage professionals who not only failed to prevent mortgage fraud from occurring, but profited from it.[6] In fact, Neil Barofsky, a former federal prosecutor in New York and the inspector general of the financial bailout funds, suggested the prosecution of licensed mortgage professionals as the best way to address mortgage fraud.[7] However, traditional standards of criminal liability handicap efforts to prosecute the professionals who did not directly perpetrate the fraud.

Yet prosecutors do possess a powerful, although not widely used, tool to employ in the prosecution of industry insiders: the Responsible Corporate Officer ("RCO") doctrine. Under this doctrine, individuals can be held criminally liable if they fail to prevent fraud from occurring despite having the authority and capacity to do so.

The RCO doctrine originated in *United States v. Dotterweich*, when the Supreme Court upheld the conviction of a corporate executive for misdemeanor violations of the Food, Drug and Cosmetic Act without requiring proof that the executive participated or even knew of the violation.[8] Since then, the RCO doctrine has been successfully expanded outside strict liability food and safety violations to other areas of public well-being.[9] Building upon both the foundation and the expansion of the RCO doctrine, this Note argues that the courts, or alternatively, Congress, should extend the doctrine to the mortgage fraud context. Part II describes mortgage fraud and how it is currently prosecuted. Part III explains the difficulty in prosecuting corporations and corporate officers. Part IV discusses the origins and development of the RCO doctrine. Finally, Part V proposes two means of expanding the RCO doctrine to the mortgage fraud context.

## II. MORTGAGE FRAUD

### A. *The Definition of Mortgage Fraud*

The FBI defines mortgage fraud as: "the intentional misstatement, misrepresentation, or omission by an applicant or other interested parties, relied on by a lender or underwriter to provide funding for, to purchase, or to insure a mortgage loan."[10] Unlike other frauds such as

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6 *See* discussion *infra* Part II.A.

7 155 CONG. REC. S2315-16 (daily ed. Feb. 13, 2009) (statement of Sen. Kaufman) (declaring that Barofsky "suggested the best way to clean up mortgage fraud is to pursue licensed professionals in the industry, and make examples of them. 'They have the most to lose, they're the most likely to flip, and they make the best examples'").

8 320 U.S. 277, 284–285 (1943).

9 *See* discussion *infra* Part IV.B.

10 FED. BUREAU OF INVESTIGATION, 2007 MORTGAGE FRAUD REPORT (2008), http://www.fbi.gov/publications/fraud/mortgage_fraud07.htm [hereinafter 2007 MORTGAGE FRAUD REPORT]; *see also* Douglas McNabb, *Federal Mortgage Fraud Charges*,

health care fraud, there is no specific federal statute associated with mortgage fraud.[11] Instead, it is prosecuted under a number of general criminal statutes such as mail, wire, and bank fraud.[12] Additionally, no single regulatory agency controls the monitoring of this crime. The FBI, the Department of Housing and Urban Development-Office of Inspector General ("HUD-OIG"), the Internal Revenue Service, the Postal Inspection Service, and state and local agencies all investigate mortgage fraud.[13] These agencies rely upon the filing of Suspicious Activity Reports,[14] reports created by HUD-OIG, and complaints from the mortgage industry at large to track mortgage fraud.[15]

The FBI divides its investigation of mortgage fraud into two basic categories: fraud for profit and fraud for housing.[16] Fraud for housing, typically perpetrated by individual borrowers, occurs when a borrower commits fraud to obtain a mortgage for which he or she normally would not have qualified.[17] Fraud for profit schemes differ in purpose and complexity from fraud for housing. These schemes often include multiple parties seeking to profit from revolving equity, falsely inflated home values, or loans issued upon fictitious properties.[18] Fraud for profit

HG.ORG, http://www.hg.org/article.asp?id=4996 (explaining that mortgage fraud is making a knowing misrepresentation of the truth, concealing a material fact, and inducing someone to act to his or her detriment, in conjunction with the mortgage process).

[11] McNabb, *supra* note 10.

[12] Holly A. Pierson, *Mortgage Fraud Boot Camp: Basic Training on Defending a Criminal Mortgage Fraud Case*, THE CHAMPION, Sept./Oct. 2007, at 22 n.13 (listing common federal statutes used to prosecute mortgage fraud, including 18 U.S.C. § 1005 (2006) (false entries to federal insured institutions); 18 U.S.C. § 1010 (2006) (false statements in HUD transactions); 18 U.S.C. § 1014 (2006) (false statements on a loan or credit application); 18 U.S.C. § 1341 (2006) (mail fraud); 18 U.S.C. § 1343 (2006) (wire fraud); 18 U.S.C. § 1349 (2006) (conspiracy); and 18 U.S.C. § 1344 (2006) (bank fraud)); *see also* McNabb, *supra* note 10 (listing additional statutes used for prosecution, including 18 U.S.C. § 1001 (2006) (false statements); 18 U.S.C. § 1006 (2006) (credit institution fraud); 18 U.S.C. § 225 (2006) (Continuing Financial Crimes Enterprise Act); 18 U.S.C. § 1503 (2006) (obstruction of justice); 18 U.S.C. §§ 1956–1957 (2006) (money laundering); 18 U.S.C. § 2314 (2006) (interstate transfer of funds); and 42 U.S.C. § 408 (2006) (use of another's Social Security Number)).

[13] 2007 MORTGAGE FRAUD REPORT, *supra* note 10.

[14] 12 C.F.R. § 21.11(a) (2006) ("This section ensures that national banks file a Suspicious Activity Report when they detect a known or suspected violation of Federal law . . . .").

[15] 2007 MORTGAGE FRAUD REPORT, *supra* note 10.

[16] Pierson, *supra* note 12, at 15.

[17] *Id.* Fraud for housing or property typically includes a misrepresentation of income or debt by one borrower to obtain a single loan. Often the borrower intends to pay it back. However, the misrepresentation allows the borrower to obtain a loan he or she may not have qualified for, subjecting the financial institution to a risk it did not bargain for. 2007 MORTGAGE FRAUD REPORT, *supra* note 10.

[18] FED. BUREAU OF INVESTIGATION, FINANCIAL CRIMES REPORT TO THE PUBLIC FISCAL YEAR 2007, http://www.fbi.gov/publications/financial/fcs_report2007/financial_crime_2007.htm.

is often referred to as "Industry Insider Fraud," because typically the perpetrators work within the real estate or mortgage industry and use their insider knowledge to override lender controls.[19] The FBI defines industry insiders to include appraisers, loan officers, underwriters, attorneys, real estate agents, loan processors, mortgage brokers, and other mortgage professionals.[20]

### B. *The Loan Application Process*

With the current high numbers of investigations of mortgage fraud and the vast amount of losses attributed to it, it is fair to ask how lending institutions failed to prevent the fraud in the first place. Examining the mortgage application process helps explain how many incidences of mortgage fraud occurred unchecked.

Generally, borrowers obtain financing to purchase a home using one of two methods. Some borrowers originate mortgage loans with a mortgage broker. Others obtain financing directly from a financial institution such as a thrift institution, commercial bank, or credit union.[21] A broker acts as a conduit between the borrower and the lending institution, often providing the borrower with information on mortgage guidelines and incentives from multiple lending institutions.[22] The broker originates the loan by gathering information on the borrower's assets, liabilities, income, credit score, and occupancy intent, ultimately passing the application along to the lending institution. Consequently, lenders often rely solely upon the broker's screening of the applicant in determining creditworthiness.[23]

Instead of using a mortgage broker, many mortgage applicants apply directly to a lending institution. In this situation, the process starts with a loan officer or loan processor gathering the information necessary from the borrower to verify that the lender's basic requirements have been

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[19] *Id.*

[20] John S. Pistole, Deputy Director, Federal Bureau of Investigation, Statement Before the Senate Judiciary Committee (Feb. 11, 2009), http://www.fbi.gov/congress/congress09/pistole021109.htm.

[21] FED. RESERVE BOARD, LOOKING FOR THE BEST MORTGAGE (2007), http://www.federalreserve.gov/pubs/mortgage/mortb_1.htm.

[22] *Id.*; Cassandra Jones Havard, *"Goin' Round in Circles" . . . and Letting the Bad Loans Win: When Subprime Lending Fails Borrowers: The Need for Uniform Broker Regulation*, 86 NEB. L. REV. 737, 750 (2008).

[23] Many lenders place total reliance on the broker's assessment of borrower risk and do not impose any conditions upon the broker. Thus, many of the loans the broker brings to the lending institution "are designed to fail, unbeknownst to the lender." Havard, *supra* note 22, at 752. Information on borrowers' assets, liabilities and income help determine the four key characteristics that are used to predict loan defaults: loan-to-value ratio; debt service-to-income ratio; credit score; and extent of verification of borrower assets, liabilities, and income. ANDREW HAUGHWOUT ET AL., FED. RESERVE BANK OF N.Y., STAFF REPORTS, JUVENILE DELINQUENT MORTGAGES: BAD CREDIT OR BAD ECONOMY? 1 (2008), http://www.newyorkfed.org/research/staff_reports/sr341.pdf.

met.[24] Then, the loan officer sends the documentation to the underwriting department. Many lending institutions now use computerized underwriting systems, which analyze a borrower's information and recommend a lending decision.[25] After an automated approval, the financial institution's underwriter simply verifies the supporting documentation.[26] Traditionally, the lending institutions approving the loan funded and serviced it, keeping it within their own portfolios.[27] Now, most institutions securitize the mortgages, selling them on the secondary market.[28]

Each of these methods contains exploitable weaknesses that allowed mortgage fraud to flourish. The first weakness relates to the overall process and lending standards. Specifically, since the 1990s, lending institutions have dramatically lowered underwriting standards, allowing banks to accept more types of loans.[29] The most notorious loans offered during this period were stated income loans, which became popular starting in 2002.[30] These loans gained popularity because they did not require verified documentation of borrower income.[31] Instead, borrowers simply stated their income on loan applications and loan officers and underwriters merely confirmed the stated amount as reasonable. Not surprisingly, many within the mortgage industry openly referred to stated

[24] Mortgageunderwriters.com, Mortgage Loan Process, http://www.mortgageunderwriters.com/loan.html [hereinafter Mortgage Loan Process] (last visited Jan. 16, 2010).

[25] *Id.*; *see also* Vicki Been et al., *The High Cost of Segregation: Exploring Racial Disparities in High-Cost Lending*, 36 FORDHAM URB. L.J. 361, 365, 365 n.8 (2009) (explaining that because Fannie Mae and Freddie Mac make their proprietary automated underwriting systems available to originating lenders, much of the underwriting is largely standardized). The underwriting calculations typically rely upon credit history, ratio of loan principal to home value, ratio of proposed mortgage payments including property tax to the applicant's income, liquid assets, and type of documentation used to substantiate reported income and assets. *Id.*

[26] Mortgage Loan Process, *supra* note 24.

[27] Havard, *supra* note 22, at 761.

[28] Loan securitization involves selling the loan to an investment company which adds the loan to a pool of other loans that is then sold on the secondary market. Following this, secondary market bonds are sold to individuals or corporate investors. *Id.* at 745.

[29] Stan J. Liebowitz, *Anatomy of a Train Wreck: Causes of the Mortgage Meltdown*, *in* HOUSING AMERICA, BUILDING OUT OF A CRISIS 287, 288 (Randall G. Holcombe & Benjamin Powell eds., 2009).

[30] Steven Krystofiak, President, Mortgage Brokers Ass'n for Responsible Lending, Statement to the Federal Reserve (Aug. 1, 2006), *available at* http://www.federalreserve.gov/secrs/2006/august/20060801/op-1253/op-1253_3_1.pdf [hereinafter Krystofiak Statement]; Mark Gimein, *Inside the Liar's Loan*, SLATE, Apr. 24, 2008, http://www.slate.com/id/2189576 (explaining that stated income loans originally benefitted salespeople, those working on commission, and business owners who could not simply predict their future income by looking at their previous year's income).

[31] These loans also became popular in parts of the country with especially high home prices. *See* Gimein, *supra* note 30.

income loans as "liar's loan[s]."[32] In a statement to the Federal Reserve in 2006, the President of the Mortgage Brokers Association for Responsible Lending presented a report comparing 100 stated income loan applications to the applicants' IRS records. It found 90% of borrowers overstated their incomes by at least 5%. More strikingly, nearly 60% of the applicants overstated their income by more than 50%.[33] Overstating income on a loan application constitutes fraud.[34]

Even with the openly dishonest reputation of the stated income loans and prescient warnings from law enforcement officials, mortgage professionals routinely approved loan applications with overstated incomes.[35] One reason mortgage fraud was not prevented at loan origination is because industry practices essentially encouraged mortgage professionals to ignore misrepresentations. Specifically, lending institutions paid those in the best place to spot fraud at the beginning of the application process on a commission basis, where individuals earned money per loan application.[36] In fact, in most lending institutions, all mortgage professionals, from loan officers up to managers, earned commissions based upon loan production.[37] Compounding this, banks often insulated themselves from the increased risks associated with these loans, by packaging and selling them on the secondary market.[38] Thus, mortgage industry practices in effect discouraged professionals from monitoring loan applications for intentional misstatements, misrepresentations, or omissions by applicants.

## III. CURRENT METHODS OF PROSECUTION

Under current practices, targeting industry insiders involves prosecuting corporations or corporate officers. However, traditional theories of criminal liability afford little opportunity to hold the industry insiders responsible for participating in, encouraging, and failing to prevent mortgage fraud.

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[32] *Id.*

[33] Krystofiak Statement, *supra* note 30.

[34] 2007 MORTGAGE FRAUD REPORT, *supra* note 10 (defining mortgage fraud as an intentional misstatement or misrepresentation by an applicant that is relied upon by a lender or underwriter to obtain a mortgage).

[35] Sanjay Bhatt, *Mortgage-Fraud Defendant Sentenced to Seven Years in Prison*, SEATTLE TIMES, Feb. 27, 2009, http://seattletimes.nwsource.com/html/localnews/2008793819_webbrooks27m.html (reporting that Washington State's Assistant Attorney General warned real estate industry professionals that "no-documentation loans were extremely vulnerable to fraud").

[36] Krystofiak Statement, *supra* note 30.

[37] *Id.*

[38] *Id.*; Havard, *supra* note 22, at 745.

*A. Prosecuting Lending Institutions*

The most obvious targets of mortgage fraud prosecutions are the lending institutions themselves. In fact, corporations can be held liable not only for crimes committed or authorized by those in the policy-making levels of the corporation, but also for crimes committed by employees at the lowest levels of the corporation.[39] As an artificial being, a corporation can act only through its employees.[40] Therefore, the employees' and officers' "purposes, motives, and intent are just as much those of the corporation as are the things done."[41] The Supreme Court has stated that it sees "no good reason why corporations may not be held responsible for and charged with the knowledge and purposes of their agents, acting within the authority conferred upon them."[42]

A corporation is criminally liable for the actions of its employees, so long as the employees are acting within the scope of their authority and intended, at least in part, to benefit the corporation.[43] Both of these tests are easily met. First, acting within the "scope of authority" encompasses not only duties authorized by the corporation, but also the acts of employees that are contrary to explicit corporate policy.[44] Second, an employee can be considered as acting to benefit the corporation even when not predominantly intending to benefit the company.[45] Further, the corporation need not even realize the intended benefit.[46]

Despite the apparent ease of successfully prosecuting a corporation, there have been no high-profile prosecutions of lending institutions in response to the mortgage crisis.[47] Since the 2002 verdict against the

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[39] United States v. Hilton Hotels Corp., 467 F.2d 1000, 1004 (9th Cir. 1972); Kathleen F. Brickey, *Corporate Criminal Liability: A Primer for Corporate Counsel*, 40 BUS. LAW. 129, 131 (1984).

[40] N.Y. Cent. & Hudson River R.R. Co. v. United States, 212 U.S. 481, 492–93 (1909); Harvey L. Pitt & Karl A. Groskaufmanis, *Minimizing Corporate Civil and Criminal Liability: A Second Look at Corporate Codes of Conduct*, 78 GEO. L.J. 1559, 1562 (1990).

[41] *N.Y. Cent. & Hudson River R.R. Co.*, 212 U.S. at 492–93 (quoting 2 JOEL PRENTISS BISHOP, NEW COMMENTARIES ON THE CRIMINAL LAW 255, at § 417 (8th ed. 1892)).

[42] *Id. at* 494–95.

[43] Brickey, *supra* note 39, at 131–35.

[44] *Hilton Hotels Corp.*, 467 F.2d at 1004 (describing how the sales agent agreed to give preferential treatment to suppliers despite confirming receipt of instructions from the corporation to the contrary).

[45] United States v. Sun-Diamond Growers of Cal., 138 F.3d 961, 970 (D.C. Cir. 1998), *aff'd*, 526 U.S. 398 (1999) (holding that although actions were undertaken to hide illegal contributions from others in the company, "the jury was entitled to conclude that he was acting instead, or also, with an intent (however befuddled) to further the interests of his employer").

[46] *Id.*

[47] In fact, a search for mortgage fraud prosecutions of corporations yields only one result: Countrywide. *See* Raymond Hernandez, *Countrywide Said to Be Subject of Federal Criminal Inquiry*, N.Y. TIMES, Mar. 9, 2008, at 20 (stating that "federal

Arthur Andersen accounting firm for obstruction of justice,[48] nearly every major "case of corporate misconduct has been resolved without" an indictment.[49] Instead, United States Attorneys increasingly rely upon deferred prosecution or non-prosecution agreements.[50] This seems to be a reasonable approach, considering the potential devastating consequences a criminal indictment could have upon a lending institution. For example, in the mortgage fraud context, a prosecution of a depository institution could wreak havoc not only upon the institution, but also upon the depositors, shareholders, and ultimately the taxpayers.[51] Thus, despite the possibility and relative ease of holding a corporation criminally liable for mortgage fraud, it is simply not a viable solution.

### B. *Prosecuting Mortgage Professionals*

Because a corporation only acts through the individuals who act on its behalf, it makes sense to prosecute those individuals directly. Typically, individuals working for a corporation can be held criminally liable under three theories: (1) direct participation in the commission of the crime, (2) aiding or abetting the commission of the crime, and (3) failing to prevent the crime by not properly controlling or supervising subordinates.[52]

First, an agent of a corporation can be held liable for engaging in a criminal act, even though acting in his or her official capacity.[53] Therefore, criminal liability would attach to a loan officer who knowingly misrepresented a borrower's income. However, under this theory, the superior who examined the loan file, noted the misrepresentation, yet did nothing, would escape criminal responsibility.

authorities have opened a criminal inquiry" on Countrywide for suspected securities fraud).

[48] Johnson, *supra* note 5, at D1.

[49] Leonard Orland, *The Transformation of Corporate Criminal Law*, 1 BROOK. J. CORP., FIN. & COM. L. 45, 45 (2006).

[50] JULIE R. O'SULLIVAN, FEDERAL WHITE COLLAR CRIME CASES AND MATERIALS 41–42 (3rd ed. 2007) (explaining that "Deferred Prosecution" and "Non-Prosecution Agreements" generally offer corporations an opportunity to trade the corporation's full cooperation in the government's investigation and prosecution of individual wrongdoers for dismissal or a forgoing of criminal charges).

[51] Arguably if Countrywide or Bank of America was indicted, the taxpayers could have been doubly affected. First, by putting the TARP "bailout" funds at risk and second by having to insure depositors through the FDIC.

[52] O'SULLIVAN, *supra* note 50, at 230–31.

[53] *See, e.g.* United States v. Gold, 743 F.2d 800, 823–24 (11th Cir. 1984) (holding that "following orders" is not an excuse when agent knew the act was criminal and therefore did not lack the specific knowledge and intent "necessary to be convicted under the applicable statutes").

A corporate officer can also be held criminally liable as an aider and abettor.[54] The aiding and abetting theory holds corporate agents and officers liable for crimes they did not commit personally, but when he or she "aids, abets, counsels, commands . . . or procures" in the commission of a crime.[55] Therefore the government recognizes no difference between a principal—one who personally commits the crime—and one who aids and abets a criminal violation. Instead, both are deemed equally culpable.

To be found guilty as an aider or abettor, an individual must engage in some act of encouragement or assistance, with the intent and desire (meeting the culpable state of mind requirement) that the criminal act succeed.[56] Consequently, unless a loan officer affirmatively encouraged the borrower to make false statements on a loan application, he or she could not be held criminally liable as an aider and abettor.[57]

Alternatively, an officer can be held accountable by failing to control the misconduct of others. Under this theory, the harm derives not from actively committing a crime or aiding and abetting in the commission of a crime, but in the supervisor's or corporate officer's "failure to discover or correct a problem" lying within his or her authority or capacity to control.[58] This theory of liability is known as the RCO doctrine.

## IV. THE ORIGINS AND EXPANSION OF THE RCO DOCTRINE

### A. *The Origins of the RCO Doctrine*

In 1943, the Supreme Court altered corporate officer responsibility when it decided *United States v. Dotterweich*, upholding the conviction of the president of a pharmaceutical company for violations of the Food, Drug and Cosmetic Act (FDCA).[59] Dotterweich's company purchased drugs from manufacturers, repackaged them under the company's own

[54] 18 U.S.C. § 2(a) (2006) ("Whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal.").

[55] *Id.*

[56] *See, e.g.*, Nye & Nissen v. United States, 336 U.S. 613, 619 (1949) (holding that aiding and abetting requires the defendant to associate with the act, participating in such a manner that it is something "he wishes to bring about" and seeks to make the act succeed (quoting United States v. Peoni, 100 F.2d 401, 402 (2d Cir 1938) (Learned Hand, J.))). *See also* United States v. Searan, 259 F.3d 434, 444 (6th Cir. 2001) (requiring an "act on the part of a defendant which contributes to the execution of a crime"); United States v. Belt, 574 F.2d 1234, 1240 (5th Cir. 1978) (stating that aiding and abetting requires an overt act); United States v. Aarons, 718 F.2d 188, 190–93 (6th Cir. 1983) (rejecting aiding and abetting criminal liability because the officer did not affirmatively encourage making false statements to a government agency).

[57] *See, e.g.*, *Searan*, 259 F.3d at 444.

[58] O'SULLIVAN, *supra* note 50, at 231.

[59] United States v. Dotterweich, 320 U.S. 277, 285 (1943).

label and distributed them.[60] Despite no evidence of Dotterweich's knowledge of the mislabeling of the shipments, he was convicted of misbranding and shipping adulterated drugs.[61] The Court stated that legislation of such importance to the larger good of society "dispenses with the conventional requirement for criminal conduct—awareness of some wrongdoing."[62] Consequently, "[i]n the interest of the larger good it puts the burden of acting at hazard upon a person otherwise innocent but standing in responsible relation to a public danger."[63] Thus, the Court determined that violation of the FDCA, a misdemeanor, is a crime of strict liability and that the statute imposes a duty upon the officer who was in a position to prevent or rectify violations.[64]

The Court acknowledged the potential hardship the RCO doctrine places upon corporate officers, but concluded that in the context of public health and danger, Congress had decided the hardship should not be borne by the "innocent public who are wholly helpless."[65] Conversely, the hardship should be placed upon those "who have at least the opportunity of informing themselves of the existence of conditions imposed for the protection of consumers . . . ."[66] The Court also refused to define the class of employees standing in responsible relation, leaving it instead to the discretion of prosecutors and trial judges and "the ultimate judgment of juries . . . ."[67]

Decades later, the Court in *United States v. Park* upheld the RCO doctrine, applying it once again to a violation of the FDCA.[68] This time the defendant was the CEO of a large national food company convicted for violating the FDCA by allowing the food held for sale in its warehouse to be exposed to rodents.[69] Evidence revealed that Park was informed of the conditions of the warehouses.[70] Additionally, Park testified that his responsibilities included directing the operations of the company, although he had delegated the responsibility of overseeing sanitary conditions to others.[71] The Court upheld Park's conviction and the jury instructions stating that to be found guilty, Park "need not have personally participated in the situation," but "must have had a responsible relationship to the issue."[72] Thus, he, like Dotterweich, as a corporate officer, could be held liable for an "act, default, or omission"

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60 *Id.* at 278.
61 *Id.* at 285–86.
62 *Id.* at 281.
63 *Id.* (citing United States v. Balint, 258 U.S. 250, 252 (1922)).
64 *Id.*; *see also* Susan F. Mandiberg, *Moral Issues in Environmental Crime*, 7 FORDHAM ENVTL. L.J. 881, 898 (1996).
65 *Dotterweich*, 320 U.S. at 285.
66 *Id.*
67 *Id.*
68 421 U.S. 658, 671–73 (1975).
69 *Id.* at 660.
70 *Id.* at 661.
71 *Id.* at 663.
72 *Id.* at 665 n.9.

because the FDCA imposed a duty not only to seek out and remedy violations, but to prevent them from occurring.[73] In fact, the Court stated that the highest standards of foresight and vigilance are rightly expected by the public and required of the corporate agents who "voluntarily assume positions of authority in business enterprises whose services and products affect the health and well-being of the public that supports them."[74]

*Park* also added an important limit to the RCO doctrine: the defense of impossibility. The Court acknowledged that even the highest standard of vigilance does not require "that which is objectively impossible" and contemplated a defense allowing the defendant to claim he or she was powerless to prevent or correct the violation.[75] The Court also determined that the guilt of a responsible corporate officer could not solely be based upon the defendant's position in the corporation.[76] Instead, the jury must find that the defendant had a "responsible relation to the situation."[77]

Since *Dotterweich* and *Park*, both Congress and the courts have expanded the RCO doctrine from food safety to the environmental law context. First, Congress added the phrase to both the Clean Water Act ("CWA") and the Clean Air Act ("CAA").[78] Second, some courts have expanded the RCO doctrine's application to the Resource Conservation and Recovery Act ("RCRA").[79] Both means of expansion are important, because these statutes, unlike the FDCA, contain a mens rea element, and do not impose strict liability.

### *B. The RCO Doctrine in the CAA and CWA*

Statutory language in both the CWA and CAA function as a vehicle of expansion for the RCO doctrine.[80] Both statutes impose criminal liability upon "responsible corporate officers."[81] The CWA does not define the term, nor does the legislative history speak to Congress's

[73] *Id.* at 672.

[74] *Id.* at 672 ("[T]he Act imposes not only a positive duty to seek out and remedy violations when they occur but also, and primarily, a duty to implement measures that will insure that violations will not occur.").

[75] *Id.* at 673.

[76] *Id.* at 674.

[77] *Id.* (internal quotation marks omitted).

[78] Clean Water Act, 33 U.S.C. § 1319(c)(6) (2006) (responsible corporate officer language added in the 1977 amendments, stating that "person" for the purposes of this subsection also means a "responsible corporate officer"); Clean Air Act, 42 U.S.C. § 7413(c)(6) (2006) (where the definition of "person" includes "any responsible corporate officer"); 42 U.S.C. § 7413(h) (2006) ("operator[s]" defined to include senior management personnel or corporate officers).

[79] *See, e.g.*, United States v. Dee, 912 F.2d 741, 748–49 (4th Cir. 1990); United States v. Self, 2 F.3d 1071, 1087–88 (10th Cir. 1993).

[80] *See* 33 U.S.C. § 1319(c)(6); 42 U.S.C. § 7413(c)(6).

[81] *See* 33 U.S.C. § 1319(c)(6); 42 U.S.C. § 7413(c)(6).

intention in adding the language.[82] However, Congress commented that the Environment and Public Works Committee intended that criminal penalties be sought not only against employees directly involved in a violation, but also against those corporate officers under whose responsibility a violation has taken place.[83]

The courts take two approaches to the RCO language within the CAA and CWA. Under one approach, courts apply the canon of construction that the legislature means for each word it used to be given effect.[84] Another approach presumes that when a legislature borrows an already judicially interpreted phrase, it intends to adopt both the old phrase and the judicial construction of that phrase.[85] Courts utilizing this approach interpret the phrase "responsible corporate officer" as it was previously defined in *Dotterweich* and *Park*.

Using the language in the CAA and CWA, courts have successfully applied the RCO doctrine to violations outside of the strict liability context. For example, in *United States v. Brittain*, a city public utilities director was convicted for discharging pollutants in violation of a permit.[86] Brittain's conviction was based upon considerable evidence linking him to the unlawful discharge.[87] However, the court also addressed the application of the RCO doctrine, determining that the addition of the language "responsible corporate officers" to the definition of person in the CWA expanded criminal liability and intended to invoke the RCO doctrine.[88]

Later, the cases *United States v. Iverson*[89] and *United States v. Ming Hong*[90] both upheld prosecutions of responsible corporate officers under the CWA. Each case also expanded the doctrine. In the late 1990s, the Ninth Circuit in *Iverson* applied the RCO doctrine to the president and chairman of the board of a chemical company.[91] Iverson argued he could only be held liable if he actually exercised control of the activity causing the violation. The court disagreed, ruling that the question for the jury

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[82] 33 U.S.C. § 1319(c)(6); United States. v. Brittain, 931 F.2d 1413, 1419 (10th Cir. 1991).

[83] S. REP. NO. 95-127, at 51 (1977), *reprinted in* 3 A LEGISLATIVE HISTORY OF THE CLEAN AIR ACT AMENDMENTS OF 1977, at 1425 (1978) [hereinafter Environment and Public Works Report].

[84] *See, e.g.*, United States v. George, 266 F.3d 52, 62–63 (2d Cir. 2001).

[85] *See, e.g.*, United States v. Iverson, 162 F.3d 1015, 1023 (9th Cir. 1998) (quoting Long v. Dir., Office of Workers' Comp. Programs, 767 F.2d 1578, 1581 (9th Cir. 1985)).

[86] 931 F.2d at 1414.

[87] *Id.* at 1420 (describing how employees informed Brittain of the discharges and that he personally witnessed the discharges and instructed the supervisors not to report the discharges).

[88] *Id.* at 1419.

[89] 162 F.3d at 1018.

[90] 242 F.3d 528, 531–32 (4th Cir. 2001).

[91] 162 F.3d at 1018, 1022.

was if the officer had the authority to control the activity, not if the officer actually exercised control.[92]

Similarly, in *Ming Hong*, the Fourth Circuit determined that the government was not required to prove a defendant was a formally designated corporate officer.[93] Although Hong challenged his conviction based upon the fact he was not a designated corporate officer, the court instead concentrated on his role in the company.[94] Specifically, Hong controlled the company's finances and played a substantial role in its operations.[95] Although his employees informed him that the wastewater treatment system was clogged and he inspected the system himself, he still refused to authorize an upgrade to the system.[96] The court determined his official title did not matter, declaring that: "[t]he gravamen of liability as a responsible corporate officer is not one's corporate title or lack thereof; [but] rather, . . . whether the defendant bore such a relationship to the corporation that it is appropriate to hold him criminally liable for failing to prevent the charged violations of the CWA."[97]

Application of the RCO doctrine under the CAA and CWA is also important to the expansion of the doctrine because unlike the FDCA, both the CAA and CWA contain the mens rea requirement of "knowingly."[98] Many feared that because the RCO doctrine originated in public welfare offenses that imposed strict liability, any extension to other contexts would circumvent knowledge requirements and enforce strict liability upon corporate officers.[99] Additionally, during the 1990s, as criminal prosecution of environmental crimes increased,[100] some scholars warned that the RCO doctrine would be used to infer the requisite intent based solely upon a corporate officer's position.[101]

Contrary to this fear, courts did not use the RCO doctrine to infer the requisite intent based solely upon a corporate officer's position. For example, in *Iverson*, the Ninth Circuit clearly explained that application

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[92] *Id.* at 1024.
[93] 242 F.3d at 531.
[94] *Id.* at 531.
[95] *Id.* at 532.
[96] *Id.* at 530.
[97] *Id.* at 531.
[98] *See generally*, 33 U.S.C. § 1319(c)(2)(A) (2006) (stating that any person who "knowingly violates section 1311, 1312, 1316, 1317, 1318, 1321(b)(3), 1328, or 1345 of this title, or any permit condition or limitation implementing any of such sections in a permit issued under section 1342 of this title by the Administrator or by a State . . ." shall be subject to criminal prosecution).
[99] Peter C. White, *Environmental Justice Since Hammurbai: From Assigning Risk "Eye for an Eye" to Modern-Day Application of the Responsible Corporate Officer Doctrine*, 29 WM. & MARY ENVTL. L. & POL'Y REV. 633, 649–50 (2005).
[100] *See* David Aufhauser et al., *Environmental Crimes, 1990 Annual Report*, 1990 A.B.A. SEC. NAT. RESOURCES ENERGY & ENVTL. L. 211, 211 (1990).
[101] *See, e.g.*, Steven M. Morgan & Allison K. Obermann, *Perils of the Profession: Responsible Corporate Officer Doctrine May Facilitate a Dramatic Increase in Criminal Prosecutions of Environmental Offenders*, 45 SW. L.J. 1199, 1200 (1991).

of the RCO doctrine did not alter the mens rea requirement of the CWA, but "relieved the government only of having to prove that the defendant personally discharged or caused the discharge of a pollutant."[102] The government still must prove that the discharges violated the law and that the defendant knew that the discharges were pollutants.[103]

### *C. Judicial Expansion of the RCO Doctrine*

#### *1. Public Welfare Rationale*

Since *Dotterweich* and *Park*, courts have also applied the RCO doctrine to other statutes concerning public health and welfare. In 1986, the Tenth Circuit applied the doctrine and upheld the conviction of a corporate officer for violation of the Federal Meat Inspection Act.[104] In *Cattle King*, instead of reading *Park* as narrowly applying only to misdemeanor violations of the FDCA, the court decided that the RCO doctrine also applies when the crime concerns the safety of the food sold to the American public.[105] Therefore, anyone managing a company engaging in the food business is obligated to insure the food sold to the public is safe.[106]

Relying upon the public interest rationale, courts have also utilized the RCO doctrine in the environmental context. Namely, the courts have applied the doctrine to violations of Resource Conservation and Recovery Act of 1976 (RCRA),[107] a statute designed to provide "nationwide protection against the dangers of improper hazardous waste disposal."[108] The Third Circuit in *United States v. Johnson & Towers, Inc.*, while not directly applying the RCO doctrine, did identify similar legislative objectives underlying RCRA and the FDCA.[109] In so doing, the court laid a framework for judicial expansion of the RCO doctrine based upon legislative intent. First, the court directly compared the legislative intent of the FDCA and RCRA, finding that in both statutes, "Congress endeavored to control hazards that, 'in the circumstances of modern industrialism, are largely beyond self-protection.'"[110] Second, in its

[102] United States v. Iverson, 162 F.3d 1015, 1026 (9th Cir. 1998) (emphasis omitted).

[103] *Id.*

[104] United States v. Cattle King Packing Co., 793 F.2d 232, 240 (10th Cir. 1986).

[105] *Id.*

[106] *Id.*

[107] Resource Conservation and Recovery Act of 1976, 42 U.S.C. §§ 6901–6992k (2006).

[108] H.R. REP. NO. 94-1491 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6238, 6243–44, 6249. The statute requires a permit for the treatment, storage, and disposal of such waste, requires detailed record keeping for the generation and transportation of the waste, and authorizes the EPA to promulgate further regulations relating to the handling of the waste to protect the health of humans and the environment. *Id.* at 6244.

[109] 741 F.2d 662, 667 (3d Cir. 1984).

[110] *Id.* (quoting United States v. Dotterweich, 320 U.S. 277, 280 (1943)).

comparison to the FDCA, the court stressed that RCRA was also enacted to address a "serious national problem."[111]

The expansion to RCRA adds to the RCO doctrine in two important respects. First, without statutory authority, the courts imposed an affirmative duty on corporate officers based upon the potential impact of violations on the public's health and safety.[112] Second, the courts applied the doctrine to a statute expressly requiring proof that the officer "knowingly" committed the offense.[113]

*2. The RCO Doctrine and Mens Rea*

Many feared that judicial expansion of the RCO doctrine would effectively eviscerate mens rea requirements and simply impose strict liability. Commentators warned that a corporate officer could be convicted based solely upon the officer's position within the corporation.[114] However, as the case law illustrates, this fear did not come to fruition. Instead, when applying the doctrine, courts analyzed whether an individual stood in responsible relation to the danger separately from the statute's mens rea requirement.

In fact, courts have refused to allow the position of a defendant to substitute for the knowledge requirement of a statute. Two cases clearly illustrate this point. First, the district court in *United States v. White* refused to convict a corporate officer for violations under RCRA without proving the requisite intent.[115] The government argued that the defendant, who was responsible for handling all environmental and safety matters for the company, was liable for the acts of all other employees regardless if he actually knew of the activities, "so long as he *should* have known of those activities."[116] However, the court determined unlike the FDCA at issue in *Dotterweich* and *Park*, RCRA is not a strict liability offense.[117] Consequently, the government must prove the requisite intent because no support exists for a conviction under a state of mind requirement other than that specified by Congress.[118]

[111] *Id.* at 666–67 (stating that the committee reports contain numerous statements indicating that Congress viewed the improper disposal of toxic waste to be a "serious national problem"). Additionally, the court considered the fact that RCRA had been amended twice to broaden its scope and enhance the penalties associated with a violation as an additional indication that toxic waste disposal is a serious national problem. *Id.* at 667.

[112] Mandiberg, *supra* note 64, at 903–04; Barbara DiTata, *Proof of Knowledge Under RCRA and Use of the Responsible Corporate Officer Doctrine*, 7 FORDHAM ENVTL. L.J. 795, 807 (1996).

[113] *See* DiTata, *supra* note 112, at 807; *see also* 42 U.S.C. § 6928(d) (2006) (providing in pertinent part that "[a]ny person who—(1) knowingly transports or causes to be transported . . . (2) knowingly treats, stores, or disposes of any hazardous waste . . ." is subject to criminal penalties).

[114] Morgan & Obermann, *supra* note 101, at 1200.

[115] 766 F. Supp. 873, 895 (E.D. Wash. 1991).

[116] *Id.* at 894.

[117] *Id.* at 895.

[118] *Id.*

The second case illustrating that the RCO doctrine cannot be substituted as a knowledge requirement is *United States v. MacDonald & Watson Waste Oil Co.*[119] In this case, the First Circuit held that a president of a small company, even with a hands-on manager role, could not be convicted under RCRA simply based upon his status as a corporate officer.[120] However, the court indicated that the jury could infer knowledge from relevant circumstantial evidence, including the defendant's position, his responsibilities, and his activities as a corporate officer.[121]

In fact, both *United States v. Dee*[122] and *United States v. Self*[123] used circumstantial evidence to meet the knowledge requirement of RCRA. In *Dee*, the Fourth Circuit upheld convictions of a chemical engineer and two of his superiors based upon evidence that the defendants ignored warnings that employees were improperly storing chemicals.[124] Similarly, the Tenth Circuit in *Self* cited evidence that the defendant had knowledge of previous illegal storage, directed an employee to store hazardous waste in a warehouse, and supervised the billing in regard to the hazardous waste as sufficient to meet the knowledge requirement of RCRA.[125]

*United States v. Jorgensen* plainly illustrates how courts analyze mens rea separately from the question of responsible relation. In that case, three defendants were convicted for misbranding meat under a statute requiring the government prove intent to defraud.[126] The jury found that the Jorgensens distributed misbranded meat by blending outside ordinary commercial beef trim with their own meat product and marketing it as meat from "genetically selected" cattle raised on native prairie grass.[127] The Eighth Circuit upheld the conviction and specifically spelled out that in order to convict the defendants, the jury must find not only that the defendants were in a responsible relationship to an activity violating the statute, but must also find that the defendants intended to defraud.[128] Therefore, the court clearly established that the RCO doctrine could not be used to impose strict liability upon defendants standing in responsible relation to a danger. Instead, the government needs to separately prove the requisite intent.

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[119] 933 F.2d 35, 55 (1st Cir. 1991).
[120] *Id.* at 55.
[121] *Id.* at 52.
[122] 912 F.2d 741, 747–48 (4th Cir. 1990).
[123] 2 F.3d 1071, 1088 (10th Cir. 1993).
[124] *Dee*, 912 F.2d at 747–49.
[125] *Self*, 2 F.3d at 1088.
[126] 144 F.3d 550, 557, 560 (8th Cir. 1998); Federal Meat Inspection Act, 21 U.S.C. §§ 601–695 (2006) (providing, in pertinent part, that it is a felony under 21 U.S.C. § 676(a) or any person, firm, or corporation to violate any provisions of the act with an "intent to defraud").
[127] *Jorgensen*, 144 F.3d at 556–57.
[128] *Id.* at 560.

## V. THE RCO DOCTRINE AND MORTGAGE FRAUD

Based upon the origin and expansion of the RCO doctrine, two possibilities exist to expand the doctrine to mortgage fraud. First, courts can expand the doctrine by applying it to mortgage fraud prosecutions. Alternatively, Congress can amend a statute already used to prosecute mortgage fraud to include "responsible corporate officers."

### A. *Judicial Expansion of the RCO Doctrine*

When imposing the RCO doctrine upon a corporate officer in *Park*, the Supreme Court acknowledged that the imposition may be onerous.[129] Nevertheless, the Court determined the obligation was "no more stringent than the public has a right to expect of those who voluntarily assume positions of authority in business enterprises whose services and products affect the health and well-being of the public that supports them."[130] Although mortgage fraud does not affect the health of the public, it certainly affects the public's well-being.[131] To promote the application of the RCO doctrine to the mortgage fraud context, courts need to expand the focus outside of the public welfare context.[132] This can be accomplished by interpreting the phrase "well-being" as signaling a wider scope.

[129] United States v. Park, 421 U.S. 658, 672 (1975).

[130] *Id.*

[131] *See infra* Part IV.C.1; Just the Facts, *supra* note 2 (attributing four to six billion dollars in loss to mortgage fraud); *see also*, Liebowitz, *supra* note 29, at 1–2 (describing the financial difficulties the United States suffers based upon the mortgage meltdown and detailing the extraordinary measures taken by the government to combat the problems).

[132] The Supreme Court, in *Liparota v. United States*, 471 U.S. 419, 432–433 (1985), ruled that legislation regulating food stamps was not a public welfare statute. The Court held that in order to qualify as a public welfare offense, a statute must first render criminal conduct that a reasonable person would know is subject to stringent regulation and second, seriously threaten the community's health and safety. *Id.* Thus, in that case, the Court determined that a law regulating food stamps, although pertaining to a public interest, was not a public welfare statute. *Id.* Additionally, relying upon a strict "public welfare" rationale proves problematic because of the perceived inconsistencies in its applications. *See* Amiad Kushner, Comment, *Applying the Responsible Corporate Officer Doctrine Outside the Public Welfare Context*, 93 J. CRIM. L. & CRIMINOLOGY 681, 703–04 (2003) (describing how clinging to a public welfare rationale for application of the RCO doctrine provides a "ready excuse to preclude application of the RCO doctrine" and is problematic because of the inconsistency in various courts' definitions of public welfare). Further, it is not clear if the statutes that the RCO doctrine has already been applied to are all definitively "public welfare offenses." *See, e.g.*, Mandiberg, *supra* note 64, at 889 ("The CWA's felony provision is *probably* a 'public welfare offense,' at least when the Act regulates the discharge of toxic pollutants." (emphasis added)); *see also* DiTata, *supra* note 112, at 796 (stating that RCRA "has been recognized" as a public welfare statute).

Utilizing this rationale, 18 U.S.C. § 1014, which prohibits making false statements on a loan application,[133] provides an opportunity for the courts to apply the RCO doctrine to the mortgage fraud context. Like that of the FDCA and RCRA, § 1014's legislative history indicates Congress's concern with the public's well-being. For example, in *Dotterweich*, the Court discussed how the history and purpose of the FDCA was aimed to protect the public from hazards "largely beyond self-protection."[134] The court in *Johnson & Towers* determined that Congress passed RCRA for similar reasons.[135] In the same way, Congress initially enacted § 1014 with the explicit purpose of protecting investors while the government was trying to revitalize the economy and recover from the Great Depression.[136] Thus, Congress declared that the underlying interest of all three statutes was to protect the public from hazards largely beyond individual control.

Another similarity between the FDCA, RCRA, and § 1014 is that Congress amended all three statutes to broaden their scope. For instance, the court in *Johnson & Towers, Inc.* cited amendments to the RCRA which expand its scope and enhance penalties as evidence of Congress's increasing concern about the prohibited conduct.[137] Moreover, such actions by legislators indicated that they deemed the issue a "serious national problem."[138] Similarly, Congress's actions regarding mortgage fraud indicate that Congress considers it a "serious national problem." First, Congress has continually enlarged the scope of statutes used to prosecute mortgage fraud. For example, amendments to § 1014 have not only dramatically enhanced the penalties for violations, but also have expanded the number of institutions covered by the

[133] 18 U.S.C. § 1014 (2006) (stating in part that "[w]hoever knowingly makes any false statement or report, or willfully overvalues any land . . . for the purpose of influencing in any way the action of . . . any institution the accounts of which are insured by the Federal Deposit Insurance Corporation, . . . upon any application . . . commitment, or loan . . . shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both").

[134] United States v. Dotterweich, 320 U.S. 277, 280 (1943).

[135] 741 F.2d 662, 667 (3d Cir. 1984) (quoting *Dotterweich*, 320 U.S. at 280).

[136] *See* United States v. Johnson, 585 F.2d 119, 123 n.3 (5th Cir. 1978) (explaining the legislative history of § 1014 and how many of the statutes it was originally combined with were enacted in the 1930s to protect investors while revitalizing the economy).

[137] *Johnson & Towers, Inc.*, 741 F.2d at 667.

[138] *Id.* at 667 (citing the fact that Congress amended the RCRA twice to broaden the scope and enhanced penalties as evidence of Congress's increasing concern about the disposal and storage of hazardous wastes); *Dotterweich*, 320 U.S. at 280–281 (describing the development of the FDCA, noting that by the 1938 Act, Congress had extended its control and increased the penalties associated with violations). The same is also true for the CAA where the 1990 Amendments added extra provisions providing significant protections and upgraded nearly all "knowing" violations to felonies. Clean Air Act of 1990, Pub. L. No. 101-549, §§ 103–109, 701, 104 Stat. 2399, 2423–2465, 2675 (1990).

statute.[139] Second, Congress has devoted increased resources to mortgage fraud investigations and prosecutions. As of April 2009, the FBI employed sixty-five task forces to investigate mortgage fraud, and legislation was recently enacted to hire additional agents and prosecutors to help combat it.[140] Third, lawmakers have made strong public statements regarding the problems associated with mortgage fraud. Specifically, Patrick Leahy, Chair of the Senate Judiciary Committee, defined his purpose in introducing the 2009 Fraud Enforcement and Recovery Act (FERA),[141] by stating that those in the mortgage industry who are dishonest, "are creating economic havoc and I want to make sure that we're able to go after them. I want to see people prosecuted . . . Frankly, I want to see them go to jail."[142] This statement not only indicates the seriousness of the problem, but also Congress's recognition of the threat mortgage fraud poses to the well-being of the economy and to the American public.

Further, as the Court stated in *Dotterweich* and as the financial crisis has illustrated, it is essential that legislation protect the well-being of citizens in situations where they cannot protect themselves. Mortgage fraud sends ripple effects throughout society, creating "economic havoc" because the negative effects are not limited to the banks and lending institutions funding the loans. Rampant foreclosures send shock waves throughout communities and the economy at large, especially when coupled with a stalled housing market and rapidly decreasing home

[139] The 1970 Amendments to § 1014 extended the criminal penalty for fraud or false statements to influence any institution insured by the Federal Savings and Loan Insurance Corporation, and any bank insured by the Federal Deposit Insurance Corporation. Housing and Urban Development Act of 1970, Pub. L. No. 91-609, § 915, 84 Stat. 1770, 1815 (1970) (codified at 18 U.S.C. § 1014 (2006)). The 1989 Amendments increased the fine from $5,000 to $1,000,000 and the maximum term of imprisonment from 2 to 20 years. Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, § 961(h), 103 Stat. 183, 500 (1989). Similarly, other statutes used to prosecute mortgage fraud have been amended to increase their reach and penalties. For example, the amendments to 18 U.S.C. § 1341 (mail fraud) in 1989 added a provision where if the fraud affects a financial institution, the maximum fine increases to $1,000,000 and raises the statutory maximum sentence to 20 years. Financial Institutions Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, § 961(i), 103 Stat. 183, 500 (1989). Then in 1990, amendments increased the statutory maximum sentence from 20 to 30 years. Crime Control Act of 1990, Pub. L. No. 101-647, § 2504(h), 104 Stat. 4789, 4861 (1990).

[140] Fraud Enforcement and Recovery Act of 2009 (FERA), Pub. L. No. 111-21, 123 Stat. 1617 (2009).

[141] *Id.* Some of the provisions in FERA include: authorizing hiring fraud prosecutors and investigators and improving the fraud and money laundering statutes to strengthen prosecutors' ability to combat the growing wave of fraud. FERA also amends the definition of "financial institution" to extend Federal fraud laws to mortgage lending businesses that are not directly regulated or insured by the Federal Government (for example, Countrywide Home Loans and GMAC Mortgage). §§ 2(a)–3(a), 123 Stat. at 1617–19.

[142] 155 CONG. REC. S2316 (daily ed. Feb. 13, 2009) (statement of Patrick Leahy).

values.[143] If a home is foreclosed, it may have lost up to twenty percent of its value, which means even if it is possible for the bank to sell the house, it will be at a loss.[144] Further, if the mortgage was securitized, investors are also negatively impacted. Finally, if multiple foreclosures occur within a community, it depresses the surrounding housing market. Thus, individuals living down the street from foreclosed homes purchased through fraudulent means are, as the Court described in *Dotterweich*, victims of circumstances of the modern economy and part of the "innocent public who are wholly helpless."[145] Although *Dotterweich* and *Park* specifically addressed public health and safety, the underlying concept of protecting ordinary citizens from the devastating effects of something they cannot self-protect against remains the same.

Additionally, judicially imposing a duty based upon a statute such as § 1014 is appropriate because it does not offend notions of criminal liability. Application of the RCO doctrine has not meant that courts modify or eliminate the mens rea requirements of the underlying statutes.[146] Therefore, expanding the doctrine to mortgage fraud, where the statutes used to prosecute it include knowledge requirements, carries no danger of the courts simply imposing strict liability. In fact, in *Jorgensen*, the court specifically applied the RCO doctrine to a conviction under the Federal Meat Inspection Act, which requires proof of intent to defraud.[147] In that case, the court held that in order to convict the corporate officers, the jury must find that they were in a responsible relationship, but also that each defendant had intent to defraud.[148]

Also significant is the Court's establishment in *Park* of a powerlessness defense to limit the scope of the doctrine. This defense compels the government to prove that the defendant had both the

[143] *See, e.g.*, Liebowitz, *supra* note 29, at 1–2.

[144] By the Numbers: Median Home Price Declines Even as Existing-Home Sales Rise, http://blogs.consumerreports.org/home/2009/03/national-association-of-realtors-median-home-price-home-sales-lawrence-yun-foreclosure-vultures.html (Mar. 25, 2009), (reporting that distressed homes are selling for 20% less than the normal market price and that the median home price has fallen 15.5% from a year earlier). The percentage of decline, of course, will vary regionally.

[145] United States v. Dotterweich, 320 U.S. 277, 280, 285 (1943); *see also* Kai-yan Lee, *Foreclosure's Price Depressing Spillover Effects on Local Properties: A Literature Review* 2008-1 PUB. & COMMUNITY AFF. PAPER (Fed. Reserve Bank of Boston), Sept. 2008, at 1–2, http://www.bos.frb.org/commdev/pcadp/2008/pcadp0801.pdf (describing the spillover effects of foreclosures as lowering nearby property values, reducing the property tax base, increasing blight and crime, and reducing commercial activity).

[146] *See, e.g.*, United States v. White, 766 F. Supp. 873, 895 (E.D. Wash. 1991) (rejecting a theory of respondeat superior and refusing to hold the corporate officer vicariously liable through the actions of his employees); United States v. MacDonald & Watson Waste Oil Co., 933 F.2d 35, 51–52 (1st Cir. 1991) (holding that the mental state of "knowing" in the RCRA cannot be satisfied solely through showing that defendant was a corporate officer).

[147] United States v. Jorgensen, 144 F.3d 550, 556–57 (8th Cir. 1998).

[148] *Id.* at 560.

authority and capacity to prevent the violation.[149] The powerlessness defense illustrates that although the RCO doctrine requires "the highest standard of foresight and vigilance" it does not hold the person in responsible relation criminally liable for something that was impossible to prevent.[150]

### B. *Congressional Expansion of the RCO Doctrine*

As an alternative to judicial expansion, Congress could expand the RCO doctrine by amending a statute already used to prosecute mortgage fraud. In fact, Congress established the groundwork for such an expansion in the CWA by including the phrase "responsible corporate officer" in the definition of person. Although Congress did not explicitly explain its intent, the legislative history indicates that the objective was to enforce criminal penalties not just against employees directly involved in the violation, but also the corporate officers who exerted responsibility over the actions of these employees.[151] Several advantages exist to choosing a statute already in existence and used to prosecute mortgage fraud. First, the RCO doctrine does not create any new crimes, but instead assigns responsibility for conduct already criminalized.[152] Second, addressing mortgage fraud through applying the RCO doctrine to a statute already in existence prevents a redundant statute from being added to the federal code based upon a knee-jerk reaction to current events.[153] Third, applying the RCO doctrine to a specific statute relating to mortgage fraud allows it to be tailored to specific behavior.

Section 1014 provides an ideal opportunity for Congress to apply the RCO doctrine to a statute already used to prosecute mortgage fraud. Section 1014 is appropriate because it is narrowly tailored to the specific behavior at issue—prohibiting false statements on a loan application.[154] To accomplish this expansion in § 1014, Congress should amend the statute to read "any person who knowingly makes any false statement or report," and then further define "person" to include a "responsible

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[149] United States v. Iverson, 162 F.3d 1015, 1025 (9th Cir. 1998).

[150] United States v. Park, 421 U.S. 658, 673 (1975).

[151] Environment and Public Works Report, *supra* note 83, at 1425.

[152] Kushner, *supra* note 132, at 710.

[153] Given the heated rhetoric in Washington regarding mortgage fraud, this is a distinct danger. *See* Julie R. O'Sullivan, *The Federal Criminal "Code" Is a Disgrace: Obstruction Statutes as Case Study*, 96 J. CRIM. L. & CRIMINOLOGY 643, 654 (2006) (describing the redundancy and overlapping of statutes in the federal code and tracing it to the political desire to react to a given scandal).

[154] Section 1014 has been chosen as a model statute because it is specific to loan applications and directly on point to the specific incidence of making false statements on loan applications. This Note does not contemplate applying the RCO doctrine to general statutes such as mail or wire fraud, used to prosecute a wide variety of fraudulent schemes. Further discussion of the perils of doing so is beyond the scope of this Note.

corporate officer."[155] The Ninth Circuit in *Iverson* interpreted the addition of this language in the CWA to mean Congress intended to incorporate the RCO doctrine into the statute.[156] Additionally, this approach is bolstered by the canon of construction that presumes when a legislature uses a term that has been judicially interpreted, it intends to adopt not only the old phrase, but the judicial interpretation of that phrase.[157] Notwithstanding this precedent, to successfully apply the doctrine to the mortgage fraud context and avoid any confusion, the phrase "responsible corporate officer" should not only be added to the statute, but defined and discussed on the record.

In defining an RCO, Congress must remember that the Supreme Court in *Dotterweich* refused to explicitly define a class of defendants. In fact, the Court stated it is "too treacherous" to define or even illustrate the class of employees who could be found to stand in a responsible relation.[158] Since *Dotterweich,* while not defining the class of defendants explicitly, courts have created some boundaries and general guidelines. For example, courts have held the actual title of the individual is not dispositive. In *Ming Hong*, the Fourth Circuit declared that the "gravamen of liability" is not a corporate title or lack thereof, but is instead based upon the defendant's relationship to the violation and the appropriateness of criminal liability for the failure to prevent the charged violations.[159] Consequently, the class of defendants in the mortgage fraud context should not be strictly limited by title or corporate position. Instead, Congress should determine that if a person has the power to prevent or correct violations of § 1014, then that individual is in a responsible relationship and liable as an RCO.[160] Thus, in the mortgage fraud context, loan officers up to credit compliance officers can be criminally liable, based upon the nature of the individual's position and his or her authority and control to prevent the fraud from occurring.

Not limiting the class of employees liable as RCOs carries both advantages and disadvantages. In *Dotterweich*, the Court thought it best to rely upon "the good sense of prosecutors, the wise guidance of trial judges, and the ultimate judgment of juries" to define the class of possible defendants under the RCO doctrine.[161] The danger of such reliance lies in the fact that prosecutorial discretion is not only broad,

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[155] The original text of § 1014 reads: "*Whoever* knowingly makes any false statement . . . ." 18 U.S.C. § 1014 (2006) (emphasis added).

[156] United States v. Iverson, 162 F.3d 1015, 1023 (9th Cir. 1998).

[157] *Id.* (quoting Long v. Dir., Office of Workers' Comp. Programs, 767 F.2d 1578, 1581 (9th Cir. 1985)).

[158] United States v. Dotterweich, 320 U.S. 277, 285 (1943).

[159] United States v. Ming Hong, 242 F.3d 528, 531 (4th Cir. 2001).

[160] *See* Paul F. Schaaff, Jr., Note, *Indirect Criminal Conduct of Corporate Officers—Law in Search of a Fair and Effective Standard of Liability*, 13 DEL. J. CORP. L. 137, 141 (1988) (explaining how in *Dotterweich*, "the Court established a parallel between the concepts of responsibility and power" and how if a person has the power to prevent or correct violations of the statute, he is in a responsible relation).

[161] *Dotterweich*, 320 U.S. at 285.

but for the most part, unreviewable. Consequently, such wide discretion risks the arbitrary imposition of criminal liability.[162] In fact, the dissent in *Dotterweich* argued that relying upon this discretion is "precisely what our constitutional system sought to avoid."[163] Although these dangers exist, the congressional addition of RCO liability to a mortgage fraud statute alleviates these concerns. First, in this case, the RCO doctrine would be applied to specific conduct within § 1014, thus limiting the class of defendants. Second, many of the concerns with relying upon judicial and prosecutorial discretion stem from the absence of congressional authorization. Certainly if Congress deliberately chooses to impose criminal liability upon RCOs in a specific context, there is less danger of prosecutors arbitrarily employing the doctrine for political reasons.[164]

Additionally, not limiting the class of defendants contains the added benefit of assisting prosecutors in holding those higher up on the corporate ladder responsible. For example, exposing an underwriter to criminal liability as an RCO could encourage lower level employees to expose the corporate officers who created the policies inviting the fraud to occur and continue unchecked.[165] Moreover, widening the prosecutorial net may prove a better alternative to merely enhancing penalties. Notwithstanding congressional amendments exponentially increasing prison times and fines for committing fraud, the incidence of mortgage fraud has continued to rise.[166] Therefore, enlarging the class of possible defendants as opposed to punishing more harshly a smaller class of defendants may prove a better deterrent to mortgage fraud in the future.

## VI. CONCLUSION

The recent increase in mortgage fraud has wreaked havoc on America's housing and credit markets. As lawmakers and law enforcement search for effective and just ways to prosecute mortgage fraud, they should consider employing the powerful tool already in their arsenal: the RCO doctrine. Expansion of the RCO doctrine affords law

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[162] O'Sullivan, *supra* note 153, at 670–71. *See also* Morgan & Obermann, *supra*, note 101, at 1210–11 (discussing the agendas of prosecutors and the appeal of prosecuting high-profile white-collar criminal cases).

[163] *Dotterweich*, 320 U.S. at 292 (Murphy, J., dissenting).

[164] *Id.* at 292–93.

[165] This technique, referred to as "working up the ladder" or the "domino game" is often employed by prosecutors in complex white-collar cases, whereby a lower level employee is implicated and offered a favorable deal to implicate someone higher up on the chain of command. *See* Dale A. Oesterle, *Early Observations on the Prosecutions of the Business Scandals of 2002-03: On Sideshow Prosecutions, Spitzer's Clash With Donaldson Over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation*, 1 OHIO ST. J. CRIM. L. 443, 447–48 (2004).

[166] *See* 155 CONG. REC. S4409 (daily ed. Apr. 20, 2009) (statement of Sen. Leahy) (stating that reports of mortgage fraud are "up 682 percent over the past 5 years and more than 2,800 percent in the past decade").

enforcement, prosecutors, and legislators a means to pursue those who at least failed to prevent, and at worst, encouraged and profited from, mortgage fraud. The RCO doctrine builds upon the framework of statutes already in existence and focuses upon the prosecution of industry insiders without adding new laws to an already tangled, complicated federal code. Applying the RCO doctrine does not apply blanket criminal liability to corporations at the risk of devastating effects, but instead isolates those in a position to prevent mortgage fraud from occurring in the first place and from becoming a systemic, serious national problem. Thus, its successful application would also fulfill its original purpose as identified in *Dotterweich*, whereby "in the interest of the larger good," the burden is placed upon a person "standing in responsible relation to a public danger."[167]

[167] 320 U.S. at 281.