Nos. 08-10436, 08-10486

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

UNITED STATES,
Plaintiff-Appellee/Cross-Appellant,
v.
PRABHAT K. GOYAL,
Defendant-Appellant/Cross-Appellee.

BRIEF OF *AMICUS CURIAE* NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS SUPPORTING REVERSAL

On Appeal from the United States District Court
for the Northern District of California
No. CR 04-0201

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Fed. R. App. P. 26.1 and Fed. R. App. P. 29(c), *Amicus Curiae* National Association of Criminal Defense Lawyers states that it is a nonprofit corporation organized under the laws of the District of Columbia. It has no parent corporation, and no publicly-held corporation owns 10 percent or more of its stock.

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INTEREST OF THE *AMICUS CURIAE*

The National Association of Criminal Defense Lawyers ("NACDL") is a nonprofit organization with more than 12,000 direct members, including private criminal defense lawyers, public defenders, active U.S. military defense counsel, law professors, and judges committed to preserving fairness within America's criminal justice system. Founded in 1958 to ensure justice and due process for persons accused of crimes, the NACDL is the only professional association that represents public defenders and private criminal defense lawyers at the national level. NACDL members serve in positions bringing them into daily contact with the criminal justice system in the state and federal courts.

NACDL thus has a broad view of our adversarial system of justice, including its ramifications in the corporate world. Those ramifications weigh against imposing felony liability on a corporate officer for complicated judgments and activities that occur within the officer's general area of responsibility, without implementation of common sense safeguards. Because so few securities fraud cases are criminally prosecuted, this case will stand as an unusually influential precedent, making it particularly important that the Court give full consideration to the policy repercussions and broader jurisprudential impact of the issues presented here.

All parties have consented to the filing of this brief. *See* Fed. R. App. P. 29(a).

INTRODUCTION

In the face of headline-driven public suspicion of the motives of corporate officers, this Court should not acquiesce to prosecutorial efforts to erode the burden of proving guilt beyond a reasonable doubt. The responsibilities and tarnished prestige of a high corporate position should not become practical substitutes for proof of misconduct and bad intent.

In this case, Prabhat Goyal, former Chief Financial Officer ("CFO") of Network Associates, Inc. ("NAI"), was convicted of securities fraud, false SEC filings, and false statements to auditors. To convict Goyal for securities fraud and false SEC filings, the government had to prove, among other things, that NAI's practices violated Generally Accepted Accounting Principles ("GAAP"), the complex and sometimes contradictory practice guidelines of the accounting profession.[1] Goyal Br. at 34-35 & n.9. At trial, however, no expert testified that a GAAP violation had occurred. To convict Goyal for false statements to auditors, the government had to prove, among

[1] NACDL has not independently reviewed the record. For the factual setting, NACDL relies on the opinion of the district court denying Goyal's motion for judgment of acquittal. NACDL also relies on the accuracy and substantial completeness of Goyal's account in his opening brief of the case and the evidence against him.

other things, that Goyal acted willfully. 15 U.S.C. § 78ff(a). In its post-trial order, the district court suggested that this element was satisfied because there were omissions in the records provided, and "Goyal had an affirmative responsibility . . . to disclose the unusual terms of the quarter-end purchase orders and invoices to the auditors." ER9.

This brief addresses two questions:

(1) Whether, where a criminal charge is premised on a violation of GAAP, and the application of the relevant GAAP provisions requires substantial accounting judgment, the government must offer expert testimony that a GAAP violation in fact occurred;

and

(2) Whether the "affirmative responsibility" of a corporate officer to disclose deal terms to auditors can supplant the government's burden to prove that the officer made false statements to auditors willfully.

First, a corporate officer should not be sent to prison when the government rests its theory of guilt on a GAAP violation yet offers no expert testimony that a GAAP violation occurred. Put differently, a jury should not be treated as a team of accountants and asked to interpret and apply GAAP without expert guidance. That is because, as courts and commentators have recognized, GAAP "can create a labyrinth of complex rules that only an experienced auditor could hope to understand." David F. Birke, *The Toothless Watchdog: Corporate Fraud and the Independent Audit—How*

Can the Public's Confidence Be Restored?, 58 U. MIAMI L. REV. 891, 904 (2004).

Moreover, GAAP's application requires accounting judgment, acquired through "technical, and specialized knowledge," *SEC v. Guenthner*, 395 F. Supp. 2d 835, 847 (D. Neb. 2005), and "extensive and continuous training," Steven L. Schwarcz, *Financial Information Failure and Lawyer Responsibility*, 31 J. CORP. L. 1097, 1105 (Summer 2006). In short, whether a violation of GAAP has occurred is precisely the kind of issue that, under fundamental principles of evidence and jury competency, "is beyond the ken of the jury"; accordingly, the government "*must* present [it through] expert testimony." DAVID H. KAYE ET AL., THE NEW WIGMORE: EXPERT EVIDENCE § 1.6, at 38 (2004) (emphasis in original).

Second, in the current economic climate, it is critical to ensure that the criminal justice system distinguishes between actions taken with criminal intent and actions that result from misjudgment or lack of comprehensive punctiliousness. That is particularly so when considering crimes based on the provision of a large corporation's business records to its auditors. Courts should resist "the temptation . . . [to impose] a 'zero-tolerance' policy and stricter standards of liability" without legislative authorization. U.S. Chamber of Commerce, *Report on the Current Enforcement Program of the*

Securities and Exchange Commission 22 (March 2006) ("U.S. Chamber Report"). It goes too far to seize on the supposed omission of a few documents from the mass provided for a particular audit, and then substitute evidence of a corporate officer's "affirmative responsibility" to provide complete information to auditors for proof of willfulness. That approach would accomplish the very "over criminalization of securities law violations" that "can stifle creativity and legitimate risk-taking and create a liability-imbued and uncertain environment in which to do business." *Id.* at 15. That is bad law and bad policy.

ARGUMENT

GAAP is a loosely organized collection of written and unwritten principles that can only be applied using accounting experience, training, and judgment. Given the complexities of GAAP—and of its application in detailed factual settings such as the software sales transactions here—no criminal conviction that rests on the premise that GAAP has been violated should stand without expert testimony establishing the violation.

In addition, the *mens rea* element of the false-statements charges requires proof of willfulness. That element cannot be satisfied simply by pointing to a corporate officer's duty to provide an auditor with complete financial information coupled with the fact that, due to an omission of

unknown cause, complete information was not provided. Vicarious criminal liability should not stretch so far.

I. EXPERT TESTIMONY IS NECESSARY TO PROVE BEYOND A REASONABLE DOUBT THAT A GAAP VIOLATION OCCURRED.

Accounting fraud significantly threatens the transparency of investment markets, and criminal frauds undoubtedly should result in criminal punishment. But criminal punishment must be reserved for actual crimes actually proven beyond a reasonable doubt, not for every accounting misstep in a public company. Some accounting frauds may be simple: forging invoices, say, or reporting revenue that never existed. But when the issues are more complicated—when proof of an alleged crime rests on the application of gauzy accounting principles to complex transactions in dynamic industries—courts must remain mindful of the complexities of GAAP, a criminal defendant's right to a fair trial, and the reasons why expert testimony is required in similar contexts.

Because GAAP is "often indeterminate," *Shalala v. Guernsey Mem. Hosp.*, 514 U.S. 87, 101 (1995), a trained eye and accounting judgment are necessary to apply it. It is not enough to send a copy of GAAP into the jury room and accept a jury's determination that a GAAP violation occurred based on mere "inferences." ER5.

A. GAAP Is Complex And Drawn From Multiple Sources.

To understand why an expert should be required in criminal cases premised on a violation of GAAP, it is important to understand what GAAP is and what its application requires.

Former SEC Chairman Cox recognized the "inescapable fact that the complexity of modern financial transactions often calls for a commensurately detailed set of regulatory requirements. But the sheer accretion of detail has, in time, led to one of the system's weaknesses—its extreme complexity." Christopher Cox, *Speech by SEC Chairman: Remarks Before the 2005 AICPA National Conference on Current SEC and PCAOB Developments* (Dec. 5, 2005). Even a single GAAP rule in isolation can be "extremely complex." Gideon Mark, *Accounting Fraud: Pleading Scienter of Auditors Under the PSLRA*, 39 CONN. L. REV. 1097, 1114 (Feb. 2007). This complexity is inevitable because GAAP is drawn from diverse and conflicting sources. There are almost two dozen GAAP sources.[2] "Because

[2] These include Financial Accounting Standards Board ("FASB") Statements of Financial Accounting Standards, FASB Interpretations, American Institute of Certified Public Accountants ("AICPA") APB Opinions not superseded, AICPA Accounting Research Bulletins not superseded, FASB Staff positions, FASB Statement 133 Implementation Issues, FASB Technical Bulletins, AICPA Industry Audit and Accounting Guides cleared by FASB, AICPA Statements of Position cleared by FASB, Consensus Positions of the Emerging Issues Task Force ("EITF"), AICPA Accounting Standards Executive Committee Practice Bulletins cleared by

these sources of accounting principles arose over many years and were promulgated by different groups, some conflicts exist among them." JAN R. WILLIAMS *ET AL.*, MILLER GAAP GUIDE LEVEL A xiii (2009). "When such conflicts arise, the accountant is directed to consult an elaborate hierarchy of GAAP sources to determine which treatment to follow."[3] *Guernsey Mem. Hosp.*, 514 U.S. at 101.

Ultimately, "'GAAP' may be defined as those conventions, rules, and practices which represent accepted financial accounting practice at a particular point in time." Wade R. Sjogren, *The World According to "GAAP": Tax Accounting for Accrued Expenses*, 20 RUTGERS L.J. 227, 227

FASB, EITF D-Topics, AICPA Accounting Interpretations, FASB Implementation Guides, AICPA Industry Audit and Accounting Guides and Statement of Positions not cleared by FASB, practices widely recognized and prevalent either generally or in the industry, FASB Concepts Statements, AICPA Issues Papers, International Financial Reporting Standards, pronouncements of other professional associations or regulatory agencies, Technical Information Services Inquiries and Replies included in AICPA Technical Practice Aids, accounting textbooks, accounting handbooks, and accounting articles. *See* JAN R. WILLIAMS *ET AL.*, MILLER GAAP GUIDE LEVEL A xiv-xv (2009).

[3] The Financial Accounting Standards Board ("FASB") "is trying to codify all of the existing literature, in order to establish a single source for all GAAP material," expected to go into effect on July 1, 2009. Cox, *supra*; *see also* FASB, *FASB Accounting Standards Codification Expected to Officially Launch on July 1, 2009* (News Release Dec. 4, 2008), *available at* http://www.fasb.org/news/nr120408.shtml. But both GAAP and the critical prerequisite for application of GAAP—accounting judgment—will remain unchanged by codification. *See* Cox, *supra* ("[Codification will] let [accountants] focus [their] efforts on what really matters[—] . . . *questions of accounting judgment and materiality* . . . ." (emphasis added)).

n. 1 (Fall 1988). Thus, where the written pronouncements in GAAP leave off—where they do not resolve a sub-issue—a more nuanced professional understanding is necessary to divine GAAP's meaning. As this Court has recognized, "[i]n the event there is no official pronouncement, the consensus of the accounting profession, as manifested in textbooks, for example, determines GAAP." *Providence Hosp. of Toppenish v. Shalala*, 52 F.3d 213, 218 n.7 (9th Cir. 1995). The task of identifying and articulating that professional consensus as of a particular time is not one that jurors should perform unaided.

As an initial matter, then, an accountant must navigate the possible sources of GAAP, identify the applicable sources of GAAP, and understand the relationships between those sources.

B. An Expert Should Guide The Jury Through The Specific Facts And Documents Supporting The Government's Theory Of An Alleged GAAP Violation.

Identifying the applicable GAAP is only the beginning of the matter. Applying GAAP is a highly fact-specific process, and an accountant must distill the relevant facts from often voluminous and technical corporate records and knowledge. Thus, a case regarding an auditor's compliance with GAAP "normally presents a complex factual situation that requires interpretation of technical accounting principles which the average jury

member is unable to understand." Anne T. Prillaman, *Countering Unrealistic Expectations: Limiting Auditors' Liability to Investors*, 32 DUQ. L. REV. 849, 861-62 (1994) (internal footnote omitted).

The GAAP guidelines at issue here—Financial Accounting Standard No. 48 ("FAS 48") and Statement of Position 97–2 ("SOP 97–2")—are no exception. FAS 48 lists six conditions that must be met in order to recognize revenue at the time of sale where a right of return exists. *See* Revenue Recognition When Right of Return Exists, Statement of Financial Accounting Standards No. 48, para. 6 (Fin. Accounting Standards Bd. 1981). Those conditions require fact-specific (and judgment-laden) analysis. For example, "[t]he ability to make a reasonable estimate of the amount of future returns depends on many factors and circumstances that will vary from one case to the next." *Id.* para. 8. SOP 97–2 similarly requires detailed inquiry into the specifics of the transaction. For example, SOP 97–2 imposes the condition that "the arrangement does not require significant production, modification, or customization of software" and requires, among many prerequisites for revenue recognition, that the sales price is "determinable" and its collectibility "probable." Software Revenue Recognition, Statement of Position No. 97–2, para. .08 (Am. Inst. of Certified Pub. Accountants 1998).

C. Applying GAAP Requires Substantial Accounting Judgment, Borne Of Experience And Training.

If all that was required to determine whether a violation of GAAP occurred was mechanical application of the relevant GAAP to the relevant facts, expert testimony might not be necessary. Indeed, jurors every day apply *legal* principles to facts. But GAAP and the law differ in at least one fundamental respect: To determine whether a violation of GAAP occurred—or to apply GAAP at all—one must use accounting judgment, a product of extensive accounting experience and training.

1. *The interpretation and application of GAAP requires substantial accounting judgment*.

As the Supreme Court of the United States has recognized, financial accounting "is not a science." *Guernsey Mem. Hosp.*, 514 U.S. at 100. Instead, it "is a 'process [that] involves continuous judgments and estimates.'" *Id.* (quoting R. KAY & D. SEARFOSS, HANDBOOK OF ACCOUNTING AND AUDITING, ch. 5, pp. 7-8 (2d ed. 1989)). Repeated "judgments about the proper characterizations of the data" are thus intrinsic to the task. John A. Siciliano, *Negligent Accounting and the Limits of Instrumental Tort Reform*, 86 MICH. L. REV. 1929, 1962 n. 158 (1988); Roger J. Buffington, *A Proposed Standard of Common Law Liability for the*

Public Accounting Profession, 5 S. CAL. INTERDISC. L.J. 485, 544 (1997) (recognizing the "judgmental nature[] of GAAP").

And judgment sufficient to interpret and apply GAAP requires experience and "extensive and continuous training." Schwarcz, *supra*, at 1105. That is why the few courts to address GAAP compliance in the context of securities litigation have held that "[w]hether defendants' actions . . . complied with GAAP is a question that requires technical, and specialized knowledge." *Guenthner*, 395 F. Supp. 2d at 847; *see also* authorities collected in Goyal Br. at 37-39 & nn. 11-12.

The GAAP guidelines at issue here are no exception. Professionals with the SEC acknowledge that SOP 97–2 "require[s] significant judgment." Sandie E. Kim, *Remarks Before the 2007 AICPA National Conference on Current SEC and PCAOB Developments* (Dec. 10, 2007). Indeed, the factors and subfactors of SOP 97–2 all require professional experience and reasoned judgment. *See* SOP 97–2, para. .30. And significant judgment is likewise required to properly apply the four factors listed in FAS 48 as potentially "impair[ing] the ability to make a reasonable estimate": The only guidance in how to use those factors to reach a conclusion is that "[t]he existence of one or more of the [] factors, in light of the significance of other factors, may not be sufficient to prevent making a reasonable estimate; likewise, other

factors may preclude a reasonable estimate." FAS 48, para. 8. This is not the type of determination that can be made beyond a reasonable doubt when it is based on little or nothing more than a lay appreciation of the common meaning of the English words.

In the few weeks of a criminal trial, a lay jury cannot gain either the experience or depth of knowledge necessary to wade through both the "hundreds of pages of dense financial records," Goyal Br. at 40, and dissect the pertinent GAAP provisions layer by layer, much less to apply the proper judgment in determining whether a GAAP violation occurred. Because "[GAAP] issues can be positively mystifying to the lay jury," a jury is unusually susceptible to be influenced by general suspicion of corporate officers and to make "unwarranted inferences on the basis of evidence taken out of the proper auditing context." Scott B. Schreiber & Robert Alexander Schwartz, *Five Common Evidentiary Issues in Securities Fraud Actions Against Auditors and Accounting Firms*, 18 PRAC. LITIGATOR 45, 46 (2007). Thus "it is even more important for criminal authorities to be cautious in their approach to prosecution of complex securities disclosure and accounting matters" considering that "'[c]orporations and their executives are easily demonized.'" U.S. Chamber Report at 24 (quoting John S. Baker,

Reforming Corporations Through Threats of Federal Prosecution, 89 CORNELL L. REV. 310, 351 (2004)).

Under established standards designed to ensure that a jury acts on evidence and understanding rather than bias, an expert is needed to supply the necessary judgment, experience, and training to guide the jury through the government's theory and evidence of a GAAP violation.

2. *Expert testimony is particularly important where the principles that the jury must apply are both complex and counterintuitive.*

Step-by-step expert testimony regarding the applicable GAAP principles and how those principles might apply to the facts in evidence is particularly important because, as the Supreme Court has recognized, GAAP "tolerate[s] a range of 'reasonable' treatments, leaving the choice among alternatives to management." *Thor Power Tool Co. v. Comm'r of Internal Revenue*, 439 U.S. 522, 544 (1979).

Moreover, "[e]ven basic principles of [GAAP] . . . are usually quite foreign and, in many cases, . . . counterintuitive" to jurors. Schreiber & Schwartz, *supra*, at 45. Indeed, the Supreme Court has observed, "GAAP 'do[es] not necessarily parallel economic reality,'" *Guernsey Mem. Hosp.*, 514 U.S. at 100 (quoting KAY & SEARFOSS, *supra*, ch. 5, at 7), and experience shows that even what constitutes "economic reality" may be a

point of contention among accountants and economists, not to mention lay jurors.

The risk of confusion is particularly acute because jurors may be more familiar with other financial frameworks, such as the tax code, that are "designed to ensure as far as possible that similarly situated [individuals] pay the same [amount]." *Thor Power Tool*, 439 U.S. at 544. By contrast, "[a]ccountants long have recognized that 'generally accepted accounting principles' are far from being a canonical set of rules that will ensure identical accounting treatment of identical transactions." *Id.* As former SEC Commissioner Atkins explained:

> Accounting issues are often not black and white. We can recognize this and act accordingly without undermining GAAP . . . . One accountant's approach can differ from another's without either approach violating our rules. It is inappropriate for regulators to take enforcement action over reasonable differences of opinion about the application of GAAP.

Paul S. Atkins, *Speech by the SEC Commissioner: Remarks before the American Institute of Certified Public Accountants* (Dec. 5, 2005).

That observation lays bare the difficulty in a case like this one, where a criminal charge rests on the notion not only that a certain accounting treatment violated GAAP, but that beyond a reasonable doubt it departed so far as to reflect criminality rather than mistaken judgment. Indeed, the

government here had to prove not only the GAAP violation, but that the violation was so blatant as to contribute to an inference, beyond a reasonable doubt, that Goyal knew it was fraudulent. (That alone may not be sufficient to prove criminal intent, but as we understand the evidence, there is no more direct foundation for the *mens rea* element.)

Without the clarity and precision an expert can provide, the government may "use [GAAP's] complexity to [its] [] advantage, capitalizing on the jury's preconceptions . . . , inviting the factfinder to jump to easy conclusions on technical questions, and arguing for unwarranted inferences on the basis of evidence taken out of the proper auditing context." Schreiber & Schwartz, *supra*, at 45-46. Under these circumstances, it is not too much to ask the government to find a competent professional to endorse its theory of the case before imprisoning an individual for failing to conduct himself in accord with the government's view of accounting propriety.

As Goyal has explained, many courts have require expert testimony in order to base civil liability for securities fraud on a GAAP violation. *See* Goyal Br. 37-38 & nn. 11-12. And many more courts require expert testimony to prove departures from the standard of care for accountants.[4] *See*

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[4] *See, e.g.*, *Brown-Wilbert, Inc. v. Copeland Buhl & Co., P.L.L.P.*, 732 N.W.2d 209, 218 (Minn. 2007); *Kemmerlin v. Wingate*, 261 S.E.2d 50, 51

GEORGE SPELLMIRE *ET AL.*, ACCOUNTANTS' LEGAL LIABILITY GUIDE § 12.12 (1990). That issue is closely related (and sometimes identical) to the question whether a practice complies with GAAP. *See, e.g.*, *In the Matter of Hawaii Corp.*, 567 F. Supp. 609, 617 (D. Hawaii 1983) (noting that an accountant or auditor generally "discharges his professional obligations by complying with industry standards," including GAAP). Deciding compliance with GAAP requires at least as much technical and professional judgment as assessing compliance with a professional standard of care. And the latter issue requires proof through expert testimony as a matter of hornbook law. *See* THE NEW WIGMORE: EXPERT EVIDENCE, *supra*, § 1.6, at 38 ("[E]xpert testimony is required to prove that a professional failed to meet his profession's standard of care.").

To the extent courts have recognized the need for an expert in *civil* accounting cases, the need is even more pressing in *criminal* cases, where the burden of proof of each element is higher—beyond a reasonable doubt, rather than merely by a preponderance of the evidence. *See United States v. Curtin*, 489 F.3d 935, 939 (9th Cir. 2007) (en banc) (burden of proof "beyond a reasonable doubt" is "demanding"); *United States v. Rutledge*, 28 F.3d 998, 1005 (9th Cir. 1994) ("the highest standard"). Indeed, the Supreme

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(S.C. 1979); *Greenstein, Logan & Co. v. Burgess Mktg., Inc.*, 744 S.W.2d 170, 185 (Tex. Ct. App. 1987).

Court has strongly suggested that evidence that would be insufficient to support civil liability cannot suffice to support a criminal conviction. *In re Winship*, 397 U.S. 358, 363 (1970). Certainly a criminal conviction cannot rest on evidence that would not support civil liability.

And expert testimony is particularly important to avoid the situation here: *no* accounting expert was willing to conclude that GAAP was violated or explain why. A lay jury should not be permitted to make a professional, technical judgment that GAAP was violated beyond a reasonable doubt when no actual trained accountant, qualified to offer an expert opinion under oath, was willing to do so. In such cases, even if *someone* could conclude that GAAP was violated, any violation must have fallen sufficiently close to, if not within, the gray area of professional judgment as to preclude criminal liability. Any confusion that might result from adding government expert testimony to defense expert testimony is more than outweighed by the benefit of properly channeling the jury's analysis. More fundamentally, however, regardless of any risk of confusion, without expert testimony, the government simply cannot prove its case.

In sum, whether an accounting judgment or omission violated GAAP should be recognized as among those "areas of the law [where] courts have held that relevant expert testimony regarding matters beyond the

comprehension of laypersons is . . . essential." *Centricut, LLC v. The ESAB Group, Inc.*, 390 F.3d 1361, 1369 (Fed. Cir. 2004). Indeed, the Federal Rules advisory committee recognized that expert testimony is designed for issues just like this, where "[a]n intelligent evaluation of facts is . . . impossible without the application of some scientific, technical, or other specialized knowledge." FED. R. EVID. 702 advisory committee's note (1972). Put differently, application of the GAAP at issue here requires accounting judgment and is not "so clear and obvious that it will be within the understanding of the ordinary layman without the need for expert testimony." *Olivier v. Robert L. Yeager Mental Health Center*, 398 F.3d 183, 190 (2d Cir. 2005) (quoting *Sitts v. United States*, 811 F.2d 736, 740 (2d Cir. 1987)).

The government therefore should have been required to submit expert testimony explaining how and why the conduct it challenged resulted in a GAAP violation, and on what theory the defendant here should be held criminally accountable for it. The government's failure to present even one qualified expert willing to stake her reputation on the notion that a GAAP violation occurred should invalidate the securities-fraud and false-filings convictions.

II. THE *MENS REA* ELEMENT OF THE LYING-TO-AUDITORS COUNTS REQUIRES MORE THAN PROOF OF A HIGH CORPORATE OFFICER'S DUTY TO PROVIDE COMPLETE INFORMATION COMBINED WITH PROOF THAT INCOMPLETE INFORMATION WAS PROVIDED.

Goyal was convicted of making false statements to NAI's auditor in several management representation letters that asserted NAI had "fully disclosed" all sales terms to its auditor. Goyal Br. at 15. To prove the false-statement counts, the government had to show that Goyal acted willfully. 15 U.S.C. § 78ff(a). That conclusion cannot rest beyond a reasonable doubt solely on the notion that Goyal had an "affirmative responsibility" to ensure that deal terms were disclosed to an auditor, plus the asserted fact that not all terms were disclosed. Both the plain language of the statute and sound public policy require more.

A. This Court Should Not Dilute The *Mens Rea* Element Of The False-Statement Counts.

The government, by relying on Goyal's "affirmative responsibility," apparently seeks to eliminate its burden to prove criminal intent. Put differently, proof that an officer fell short in guaranteeing the underlying completeness of a routine management representation letter does not substitute for proof of criminal intent. If any breach of that "affirmative responsibility" is enough, whenever a CFO signs off on a management representation letter, even if she did not turn the materials over to the auditor

directly herself—a common practice in the industry and the practice here (Goyal Br. at 60, 78-79), she would expose herself to criminal liability *regardless of what she knew or did not know* about the precise contents of what the auditor received. If the subordinate who collected and delivered the documents to the auditor willfully hid material documents but the CFO believed reasonably and in good faith that the documents provided to the auditor were complete, she nonetheless could be criminally liable. Even if *no one* acted willfully, and documents had simply been misplaced or inadvertently omitted from the boxes delivered for the audit, criminal intent would be ascribed to the CFO.

This theory replaces concepts of criminal intent with inferences more appropriate in the context of contractual breach. Even if no one acted willfully, criminal liability is charged to the corporate officer who takes responsibility for corporate acts, which in reality are the collective conduct of herself and her subordinates. In that respect, the "affirmative responsibility" theory effectively turns 15 U.S.C. § 78ff(a) into a strict liability offense. This strict-liability approach accords with an observed trend in financial crimes prosecutions to "shift[] and shape[] malleable standards such as . . . 'scienter[]' and 'willfulness[,]' . . . influenced by the public view that almost all corporate conduct and motivations of corporate

officials are suspect." U.S. Chamber Report at 22. Indeed, by diluting the mental element of the criminal intent, the government can neutralize or even "eliminate the presumption of innocence." Baker, *supra*, at 344.

But the *mens rea* element of 15 U.S.C. § 78ff(a) is not mere surplusage. This Court has held that "'willfully' as it is used in § 78ff(a) means intentionally undertaking an act that one knows to be wrongful." *United States v. Tarallo*, 380 F.3d 1174, 1188 (9th Cir. 2004). Thus, "a[] defendant may vitiate a government securities fraud allegation by arguing that she did not 'willfully' violate the securities laws and, therefore, lacked the requisite fraudulent intent." Nic Heuer *et al.*, *Securities Fraud*, 44 AM. CRIM. L. REV. 955, 996 (2007).

The preservation and judicial enforcement of the *mens rea* element is particularly important to ensure that "the stigma of crime attaches only to individuals proven to have been 'morally culpable' by virtue of having acted with a guilty state of mind." Baker, *supra*, at 345. Indeed, vigilance of that kind is necessary to ensure sound and coherent jurisprudence in which the mental state for criminal liability logically should be more culpable than the mental state supporting civil liability for the same acts. *Cf.* Michael L. Seigel, *Bringing Coherence to Mens Rea Analysis For Securities-Related Offenses*, 2006 WIS. L. REV. 1563, 1613 (2006). The heavy penalties

provided in 15 U.S.C. § 78ff(a)—now up to 20 years' imprisonment and a $5 million fine—have led this Court to "disfavor[]" any interpretation of the underlying substantive securities-law provisions "that de facto eliminates the mens rea requirement." *United States v. Smith*, 155 F.3d 1051, 1068 n.25 (9th Cir. 1998) (insider trading). That disfavor should extend to the interpretation advanced by the government here.

B. Imposing Strict Liability On A Corporate Officer For A Felony Offense Is Not An Appropriate, Proportionate, Or Effective Method Of Raising Standards For Corporate Conduct.

Nor does sound policy weigh on the side of expanding criminal liability here. The "affirmative responsibility" theory may be intended to increase incentives to ensure the completeness and accuracy of statements made to auditors, but strict felony liability for individual officers is too draconian and blunt a tool. Civil liability and corporate sanctions offer a more measured response for violations not accompanied by proof of individual moral culpability. Thus, "[i]t is incumbent on regulators and prosecutors alike strongly to resist lowering the standards for liability for fraud and blurring the line between civil and criminal responsibility in the name of raising standards for corporate conduct." U.S. Chamber Report at 22.

If the courts dilute the *mens rea* standard so that a jury may infer criminal liability from the absence of the secondary documents at issue here, the consequences would be felt throughout the corporate world. Corporate officers are required to certify financial statements similar to the ones at issue here—indeed, much broader and more comprehensive statements—as a matter of routine. Thus, under the Sarbanes-Oxley Act, both the CEO and the CFO of each issuer must certify that the information in Forms 10-K and 10-Q "fairly presents, in all material respects, the financial conditions and results of operations of the issuer." 18 U.S.C. § 1350. But no one could reasonably expect those officers to be criminally punished each time they fail to notice that not every piece of paper connected with a transaction was provided to the auditors. Indeed, no one reasonably could expect those officers to comb through every transaction document. In any event, failure to do so certainly should not carry *criminal* risks.

For that reason, the Sarbanes-Oxley Act, which criminalizes failure of corporate officers to properly certify financial reports, requires *mens rea* much like that required in the false-statement counts at issue here. *See* 18 U.S.C. § 1350(c); Larry Catá Backer, *The Sarbanes-Oxley Act: Federalizing Norms for Officer, Lawyer, and Accountant Behavior*, 76 ST. JOHN'S L. REV. 897, 944 (Fall 2002) ("Each of the [criminal penalty] provisions requires

knowledge or intentional violation."). The Court should carefully consider whether its holding here logically will extend to make every erroneous Form 10-K or 10-Q a basis for imprisoning the certifying CEO and CFO.

The associated policy concerns are significant. "In cases involving accounting and disclosure issues, often the line between improper conduct and mistakes, and between misfeasance and a failure to appreciate the complexities or the legal ramifications of difficult, complex situations, can easily be blurred, resulting in allegations of fraud to justify large penalties and career-ending sanctions." U.S. Chamber Report at 26. "[T]he threat of harsh, punitive sanctions for violations based on complex and unclear legal and accounting principles" will hinder the performance of a corporate officer's duties. *Id.* at 15. A threat of that magnitude may "stifle creativity and legitimate risk-taking and create a liability-imbued and uncertain environment in which to do business," *id.*, and generally "make[] people reluctant to use their professional judgment," Atkins, *supra*.

And it is not merely risk-taking that would be impeded. If the personal criminal liability of CEOs and CFOs extends to strict liability for the acts of subordinates in failing to provide documents—or even to non-negligent omissions by persons—the most skilled and savvy executives may shy away from the leading positions at public companies rather than wager their

freedom on the punctiliousness of their back office. That is not good for shareholders or the economy at large.

Indeed, even those who believe that the *mens rea* requirement in criminal securities cases is too strict would not support its effective elimination here. Enron prosecutor John Kroger, for example, has expressed frustration that intent is difficult to prove where "CEOs, CFOs and other corporate executives . . . provide false information to the market." John R. Kroger, *Enron, Fraud, and Securities Reform: An Enron Prosecutor's Perspective*, 76 U. COLO. L. REV. 57, 115, 129-30 (Winter 2005). But rather than redefine the current formulation of felonious criminal intent to encompass negligence or strict liability in this context, Kroger proposed that "Congress pass a new federal criminal statute making it a *misdemeanor* . . . for any person to *negligently* make any untrue statement of material fact about a publicly traded company's operations, performance, or financial condition, or to negligently omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading." *Id.* at 131-32 (emphasis added).

But Congress has not made negligence, much less strict liability, the standard for the current felony. Accordingly, the *mens rea* requirement of 15 U.S.C. § 78ff should be strictly enforced as written. Put differently, proof of

criminal intent sufficient to imprison a CFO should not rest on an omission and signature on a management representation letter without more meaningful evidence that the omission resulted from the CFO's willful misconduct, as 15 U.S.C. §§ 78ff(a) requires.

CONCLUSION

The judgment should be reversed to the extent inconsistent with the principles expressed here.

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Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

1. Pursuant to Fed. R. App. P. 29(d) and 9th Cir. R. 32-1, the undersigned hereby certifies that the attached amicus brief is proportionally spaced, has a typeface of 14 points or more, and contains 5,742 words, exclusive of the exempted portions of the brief, as provided in Fed. R. App. P. 32(a)(7)(B).

2. The brief has been prepared in proportionally-spaced typeface using Microsoft Word 2002 in 14-point Times New Roman font. As permitted by Fed. R. App. P. 32(a)(7)(C), the undersigned has relied upon the word-count feature of this word-processing system in preparing this certificate.

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