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Honors Legal Studies

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Corporate Criminal Liability: Arthur Andersen v. United States

The Case

Before its fatal implosion, Enron Corporation was an American energy, commodities, and services company that was based in Houston, Texas. In just 15 years, Enron grew from nowhere to be America's seventh largest company, employing 21,000 staff in more than 40 countries[1]. Large companies like Enron also need well equipped auditors for its accounting purposes and most of those auditors tend to work within the company. As time went on, it turned out that most of Enron's profits were falsified and they were actually in more debt than they could comprehend. The scam could have only been possibly hidden from the public eye because their auditing firm, Arthur Andersen, one of the "big five" accounting companies, worked so close with them they were able to hide the rising debt and false profits. With the decline and bankruptcy of Enron, and in efforts to avoid impending doom, Enron's chief auditor at Andersen ordered his employees to shred all documents kept that involved them with Enron. The massive destruction of Enron related documents after the scandal caused suspicion and resulted in an indictment by the SEC for obstruction of justice.

The case was taken to the federal court and Andersen was charged for the violation of federal law, which made it a crime to "knowingly...corruptly persuade another person" and to "withhold" or "alter" documents in an "official proceeding". [2] Under the United States Code Service, clause 1512 (b)(2), it is explicitly stated that it is illegal to tamper with documents that are pertinent to legal processes. Because Arthur Andersen shredded all Enron accounting documents at the time of the scandal, the federal court found the company in direct violation of the clause and the U.S. Court of Appeals for the Fifth Circuit also affirmed the conviction

After the fifth circuit conviction, Andersen then appealed the case to the U.S. Supreme Court. The Supreme Court was unanimous in reversing the fifth circuit decision because the jury instructions of the federal court did not satisfy the requirements of expatiating on their decision. The government court was only relying on the shredded documents and nothing else to fully litigate Arthur Andersen. The decision was reversed and remanded.

Legal Issues

[1] http://news.bbc.co.uk/2/hi/business/1780075.stm

[2] http://www.oyez.org/cases/2000-2009/2004/2004_04_368

As Albert Spalding and Mary Ashby Morrison state, "documents are shredded every day. E-mails are deleted. And voice-mail messages are seldom retained... [with] growing threats, such as corporate espionage and identity theft, business organizations, professionals, and individuals are shredding paper at record rate."[3] Most firms delete and destroy their documents for multitudes of reasons, it is seen as normal. This also part of Arthur Anderson's retention policy in which final memoranda and documents are retained but notes and correspondence are destroyed. Enron was a big company and Arthur Andersen was one of the big five working with one of the largest energy companies. When the scandal surfaced and actions came into federal question, every document was important. Ordering so many employees to destroy what was seen as evidence was taken as corrupt persuasion to the trial court. Andersen argued that he district court erroneously charged the jury by not instructing that "a conviction under section 1512(b)(2) is permissible only if the defendant is shown to have known that its conduct was wrongful." Whereas the circuit court countered "at the jury was properly instructed because knowledge of one's violation is not an element of 1512(b)(2). The general rule, of course, is that ignorance of the law is no defense."[4] Thus holding Andersen extremely liable for their "corrupt" actions.

However, the United State Supreme Court unanimously reversed the circuit court conviction because the jury failed to correctly convey the elements of "corrupt persuasion" under 1512 (b)(2)., which states, "Whoever knowingly uses intimidation, threatens or corruptly persuades another person, or attempts to do so, or engages in misleading conduct toward another person, with intent to-- (2) cause or induce any person to--(A) withhold testimony, or withhold a record, document, or other object, from an official proceeding; (B) alter, destroy, mutilate, or conceal an object with intent to impair the object's integrity or availability for use in an official proceeding; (C) evade legal process summoning that person to appear as a witness, or to produce a record, document, or other object, in an official proceeding"[5] The general opinion was that the jury instructions simply failed to requisite consciousness of wrongdoing and how there was little culpability required by the jury. Words like "knowingly" and "corrupt persuasion" were too vague especially if there was already a retention policy in place.[6] Andersen could not really be

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[3] "Criminal Liability for Document Shredding After Arthur Andersen LLP"

[4] UNITED STATES OF AMERICA, Plaintiff-Appellee, versus ARTHUR ANDERSEN, LLP, Defendant-Appellant. No. 02-21200
UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT
374 F.3d 281; 2004 U.S. App. LEXIS 11814

[5] UNITED STATES CODE SERVICE

[6] ARTHUR ANDERSEN LLP, PETITIONER v. UNITED STATES
No. 04-368
SUPREME COURT OF THE UNITED STATES
544 U.S. 696; 125 S. Ct. 2129; 161 L. Ed. 2d 1008; 2005 U.S. LEXIS 4348; 73 U.S.L.W. 4393; Fed. Sec. L. Rep. (CCH) P93,266; 18 Fla. L. Weekly Fed. S 324

held under "knowledgeable corruption" if they had a retention policy in place already and the government court had no further evidence despite the massive shredding. The basis of the case was too vague and the evidence not powerful enough for the Supreme Court to rule in favor of the circuit court.

Analysis

This is a very simple corporate criminal liability case turned complex. Enron was partnered with Arthur Andersen which aided the former in concealing one of the biggest accounting scams in American history. Upon realizing Enron's demise, the chief accountant at Andersen ordered for all Enron related documents to be shredded. The company already had a retention policy in which they deleted documents that could possibly incriminate their clients but as the article, *Risk and Retention Policies* states, "one person's careful protection of privacy rights, client confidences, trade secrets, or national security secrets can be characterized as another person's obstruction of justice."[7] The higher corporate level at Andersen knew what was happening and the crimes they were committing but chose to conceal it. The SEC/Federal government was right to step in during the massive shredding and charge the company for violation of Federal law. Their reasons being: First, David Duncan, its partner in charge of the Enron account, pleaded guilty to a criminal charge of obstruction, confessing intent to impede the SEC investigation by shredding documents. Second, it could hardly deny that Andersen engaged in massive shredding and deletion of files as a part of senior management's investigation of its handling of Enron, including difficulties with the accuracy of Enron's financial statement. Third, it must have known that a restatement of earnings of any appreciable size by a Fortune 500 company would prompt a formal SEC investigation and subpoena for its documents.[8] However, there should have been more evidence to follow up on the suit to strengthen the conviction in the case. The Supreme Court held that the jury instructions were flawed in some important respects. The circuit court had no fleshed out definitions of corrupt intent and really could not prove besides the massive shredding the culpability of Enron. The Supreme Court decision, in light of the entire scandal, seems entirely legalistic; they strictly stuck to the law and left no room for interpretation. Their unanimity is entirely surprising because it would have been expected that at least a minority would vote in favor of the circuit court. This illustrates how in regards to the Supreme Court, everything must be dealt with a straightforward and solid instruction and application to the law. Despite the reversal, it was a pyrrhic win for Andersen and they ended up being dissolved after the case settled. They committed years of accounting

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[7] Risk And Document Retention Policies
By Robert J. Hennessey, J.D. and Mark H. Zitzewitz, J.D.
Lindquist & Vennum P.L.L.P.

[8] UNITED STATES OF AMERICA, Plaintiff-Appellee, versus ARTHUR ANDERSEN, LLP, Defendant-Appellant. No. 02-21200
UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT
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fraud and scam and tried to conceal them at the end. Justice brought them to court, justice reversed their decision, but at the end they received their due justice.