

Washington University Law Review

Volume 71
Issue 2 *Corporate Sentencing*

1993

Close Corporations and the Criminal Law: On “Mom and Pop” and a Curious Rule

Kathleen F. Brickey
Washington University School of Law

Follow this and additional works at: https://openscholarship.wustl.edu/law_lawreview



Part of the [Business Organizations Law Commons](#), and the [Criminal Law Commons](#)

Recommended Citation

Kathleen F. Brickey, *Close Corporations and the Criminal Law: On “Mom and Pop” and a Curious Rule*, 71 WASH. U. L. Q. 189 (1993).

Available at: https://openscholarship.wustl.edu/law_lawreview/vol71/iss2/1

This F. Hodge O'Neal Corporate and Securities Law Symposium is brought to you for free and open access by the Law School at Washington University Open Scholarship. It has been accepted for inclusion in Washington University Law Review by an authorized administrator of Washington University Open Scholarship. For more information, please contact digital@wumail.wustl.edu.

Washington University Law Quarterly

VOLUME 71

NUMBER 2

1993

F. HODGE O'NEAL CORPORATE AND SECURITIES LAW SYMPOSIUM: CORPORATE SENTENCING

CLOSE CORPORATIONS AND THE CRIMINAL LAW: ON "MOM AND POP" AND A CURIOUS RULE†

KATHLEEN F. BRICKEY*

I. INTRODUCTION

The federal Sentencing Guidelines for organizations are the product of a long and tortuous process marked by public controversy and internal conflict within the United States Sentencing Commission. Although Congress gave no specific directive to create organizational guidelines, the Commission concluded that it had authority to adopt them and that it was desirable to do so.

The Commission's decision to promulgate organizational sentencing guidelines sparked renewed debate about corporate criminal liability.

† ©Copyright 1993 by Kathleen F. Brickey.

* George Alexander Madill Professor of Law, Washington University. The author twice served briefly as a consultant to the United States Sentencing Commission in connection with its development of guidelines for sentencing organizations.

I am deeply indebted to Bob Thompson, Jim Brickey and the late Hodge O'Neal for their wise counsel on matters corporate and otherwise. I am also grateful to research assistants Rodney Harrison and Dennis Bremer for their complicity in this endeavor.

The root question the Commission set out to address was how (and how much) corporations should be punished.¹ That inevitably brought to the fore the question whether corporations should be punished at all.² Assuming continued recognition of corporate criminal liability, what standard of liability should govern? Is the federal rule, which imposes liability under modified respondeat superior principles, too broad?³ If so, how should it be changed? Should all corporations be treated alike, or should the criminal law recognize distinctions based upon corporate form or size?⁴

Established principles governing corporate criminal liability apply indiscriminately to all corporations, regardless of size or corporate form. Yet to date, little consideration has been given to the question whether the reasons supporting recognition of corporate liability for crime apply with equal force to close corporations.⁵ Nor has the question whether the same sentencing rules should apply to close corporations and their publicly held counterparts been addressed. Hence, this Article journeys off the beaten path to explore these intersecting themes.

1. Compare Richard S. Gruner, *Beyond Fines: Innovative Corporate Sentences Under Federal Sentencing Guidelines*, 71 WASH. U. L.Q. 261 (1993) (supporting innovative sentencing including restitution, notice to victims, remedial orders, probation, and adverse publicity) with Ilene H. Nagel & Winthrop M. Swenson, *The Federal Sentencing Guidelines for Corporations: Their Development, Theoretical Underpinnings, and Some Thoughts About Their Future*, 71 WASH. U. L.Q. 205, 222, 227-28 (1993) (Commission determined that optimal penalty approach based on offense loss is unworkable, and, instead, opted in favor of guideline system favoring incentives and based upon culpability) and Jeffrey S. Parker, *Rules Without . . . : Some Critical Reflections on the Federal Corporate Sentencing Guidelines*, 71 WASH. U. L.Q. 397, 398-99, 408 (1993) (Commission's "carrot and stick" approach is disastrous; guidelines turn profit making into strict liability offense).

The model the Sentencing Commission adopted creates another subset of compliance issues. See Dan K. Webb & Steven F. Molo, *Some Practical Considerations in Developing Effective Compliance Programs: A Framework for Meeting the Requirements of the Organizational Sentencing Guidelines*, 71 WASH. U. L.Q. 375 (1993).

2. Professor Parker concludes they should not. See Parker, *supra* note 1, at 441.

3. Compare Pamela Bucy, *Organizational Sentencing Guidelines: The Cart Before the Horse*, 71 WASH. U. L.Q. 329, 338-39 (1993) (advocating a more narrowly drawn rule of liability based upon indicia of corporate culpability) with Leonard Orland, *Beyond Organizational Guidelines: Toward a Model Federal Corporate Criminal Code*, 71 WASH. U. L.Q. 357, 361, 366 (1993) (supporting a modified version of the present federal rule) and Nagel & Swenson, *supra* note 1, at 238 (indicating some commentators' discomfiture with the present federal rule).

4. Professor Orland believes that they should be treated alike. See Orland, *supra* note 3, at 360-61.

5. *But see id.*

II. "MOM AND POP"

Cases through which courts fashioned the rule that corporations could be liable for crime viewed such liability as a necessary check on corporate power. In a seminal turn of the century case, the Supreme Court observed that in modern times, corporations conduct "the great majority of business transactions"⁶ and that "interstate commerce is almost entirely in their hands."⁷ That being true, to adhere to "the old and exploded" notion that corporations are incapable of committing crimes "would virtually take away the only means of effectually controlling" them and of "correcting the abuses" at which the criminal law is aimed.⁸ The Massachusetts Supreme Judicial Court more recently voiced concern that if corporations were shielded from criminal liability, they could "inflict widespread public harm" and leave the public with no prospect of redressing the wrong.⁹

Both courts undoubtedly had large publicly traded corporations in mind.¹⁰ One can only wonder whether the courts would have been equally receptive to institutional liability if the prosecutions had been

6. *New York Cent. & Hudson River R.R. v. United States*, 212 U.S. 481, 495 (1909).

7. *Id.*

8. *Id.* at 496.

Professor Bucy criticizes the Court for making a simplistic choice between only two options—criminal liability or no liability. Bucy, *supra* note 3, at 341-42. The Court could, of course, have considered individual liability and civil remedies. *Id.* at 340-41.

That courts of this era did not consider civil remedies may be partly attributable to the nature of the pioneering prosecutions that had led to recognition of corporate criminal liability not long before. Most were nuisance prosecutions that arose out of a corporation's pollution of a river, failure to repair deteriorating roads and bridges, or maintenance of a malodorous slaughterhouse. *See Commonwealth v. Hancock Free Bridge Corp.*, 68 Mass. 58 (1854); *State v. Morris Canal & Banking Co.*, 22 N.J.L. 537 (1850); *President of Susquehanna & Bath Turnpike Rd. Co. v. People*, 15 Wend. 267 (N.Y. Sup. Ct. 1836); *People v. Corporation of Albany*, 11 Wend. 539 (N.Y. Sup. Ct. 1834); *State v. Corporation of Shelbyville*, 36 Tenn. (4 Sneed) 112 (1856).

The public at large had no civil cause of action, and individual citizens could sue only if they suffered an injury different from the harm suffered by the public at large. Thus, these early cases were, of necessity, criminal prosecutions. *State v. Ohio Oil Co.*, 49 N.E. 809, 811 (Ind. 1898); *State v. Morris & Essex R.R.*, 23 N.J.L. 360, 370 (1852); *People v. Corporation of Albany*, 11 Wend. 539, 543 (N.Y. Sup. Ct. 1834); *State v. Paggett*, 36 P. 487, 488 (Wash. 1894). An important purpose of the prosecution was to abate the nuisance, and the duty to abate was owed to the public. *People v. Corporation of Albany*, 11 Wend. 539, 543 (N.Y. Sup. Ct. 1834). *See generally* Kathleen F. Brickey, *Corporate Criminal Accountability: A Brief History and an Observation*, 60 WASH. U. L.Q. 393 (1982).

9. *Commonwealth v. Beneficial Fin. Co.*, 275 N.E.2d 33, 84 & n.58 (Mass. 1971), *cert. denied*, 407 U.S. 910, and *cert. denied*, 407 U.S. 914 (1972).

10. In *Beneficial Finance*, for example, three corporations engaged in the business of making small loans were named defendants. The Beneficial Finance Company was a Delaware holding com-

brought against small “mom and pop” corporations. Would the corporate form of doing business have been relevant to the developing liability rule? To address this question, it is necessary to consider these contrasting corporate forms and what “corporateness” really means.

Publicly held corporations are owned by many shareholders. Their ownership and management thus are separate and distinct. Close corporations, in contrast, are privately owned, and their ownership and management usually overlap. The term “close corporation” is variously defined as an organization that has relatively few shareholders, one whose stock is not widely traded in the securities market,¹¹ or one characterized by substantial identity of ownership and management.¹² The term “closely held” corporation invariably refers to a privately owned corporation that has few or relatively few shareholders.¹³ Regardless of which term is used, these corporations will have a relatively small number of shareholders because their stock will not be traded on an exchange or in securities markets.

Although recognition of the distinctive nature of close corporations is largely a twentieth century phenomenon,¹⁴ the importance of this corporate form cannot be overstated. Today, the vast majority of incorporated organizations in this country are closely held,¹⁵ and many are small, family owned businesses.

Do small, closely held corporations “behave more like individuals than organizations?”¹⁶ If so, one might posit that in this context the organiza-

pany that was the sole owner of three business trusts. These trusts had 58 small loans offices throughout Massachusetts. Beneficial Finance also had a wholly owned subsidiary. *Id.* at 93.

The Household Finance Corporation, also a Delaware corporation, had its national headquarters in Chicago. Its operations were divided into geographical divisions as well as into departments and sub-departments. The corporation had 91 loan offices in New England, 40 of them in Massachusetts. *Id.* at 87.

The third corporate defendant was Liberty Loan Corporation, another Delaware company. Liberty owned beneficial shares of several Massachusetts business trusts that engaged in making small loans. *Id.* at 60. It also had an office in St. Louis. *Id.* at 88.

11. Some authorities combine these two concepts and define a close corporation as one that has relatively few shareholders and whose shares are not widely traded.

12. F. HODGE O'NEAL & ROBERT B. THOMPSON, O'NEAL'S CLOSE CORPORATIONS § 1.02 (3d ed. 1992). These close corporation scholars adopt the “not widely traded” definition.

13. *Id.* § 1.04.

14. *Id.* § 1.13.

15. *Id.* § 1.02, at 4-5 & n.11.

16. Orland, *supra* note 3, at 361.

tional behavior model is inapt¹⁷ and that applying institutional rules of criminal liability to them thus makes little sense.

The strongest case against imposing criminal liability on close corporations can be made where complete or substantial overlap exists between management and ownership. Consider, for example, the corporation whose records were subpoenaed in *Braswell v. United States*.¹⁸

After conducting his business as a sole proprietorship for fifteen years, Braswell decided to incorporate. To comply with state corporation law requirements, he appointed three officer/directors. They were, respectively, Braswell, who served as president; Braswell's wife, who was named corporate secretary-treasurer; and Braswell's mother, who was named vice-president. Neither his wife nor his mother had any authority over the business. Thus, in essence, Braswell continued his sole proprietorship, but conducted it in corporate form.

One might argue that in Braswell's setting, imposition of criminal liability on the corporation would be needlessly redundant. One reason that corporate criminal liability is recognized is the difficulty of identifying individual wrongdoers within the organization.¹⁹ Many modern corporations are large, complex, highly decentralized organizations with multiple layers of bureaucracy. These entities depend on a system of delegation that diffuses responsibility throughout the organization. In consequence, lower echelon employees "often exercise more responsibility in the *everyday operations* of the corporation" than does corporate manage-

17. *Id.* at 360-61.

Although Professor Orland's articulated concern is the inappropriateness of prosecuting small closely held corporations, when this Article went to press his proposed Model Federal Corporate Criminal Code made only large publicly held corporations amenable to prosecution. The proposed Code defined the term "corporation" to mean an entity that has at least 500 equity shareholders of record and at least \$5 million in assets. *Id.* at 11 (manuscript, on file with *Washington University Law Quarterly*) (drawing upon § 1.31 of the *American Law Institute Principles of Corporate Governance* (1992)). *But see id.* at 360-61 & n. 20, 365. Thus, his proposal excluded all privately held corporations, including those that are functionally indistinguishable from their publicly held counterparts. *See infra* text accompanying notes 26-37.

18. 487 U.S. 99 (1988). The issue the Court considered was whether Braswell, as custodian of the corporate records, could refuse to produce them on Fifth Amendment grounds. The Court held he could not. To permit corporate custodians to resist subpoenas on the ground that the corporate records would personally incriminate them would, in the Court's view, "have a detrimental impact on the Government's efforts to prosecute 'white-collar crime,' one of the most serious problems confronting law enforcement authorities." *Id.* at 115.

19. *United States v. Hilton Hotels Corp.*, 467 F.2d 1000, 1006-07 (9th Cir. 1972), *cert. denied*, 409 U.S. 1125 (1973).

ment.²⁰ Indeed, under the collective knowledge doctrine, there need not be a single culpable corporate agent.²¹ Hence, fining the corporation becomes an alternative to fining the unidentified or nonexistent wrongdoer.

Even when middle or low-level wrongdoers can be found, there may be other reasons to hold the corporation accountable. Especially in the context of crimes like antitrust violations, the misconduct may be a response to institutional pressures—subtle or overt—to maximize profits.²² Consider, for example, a purchasing agent whose profit maximization efforts result in an unlawful pricing agreement. He agrees to the unlawful arrangement on behalf of the corporation and for its benefit. If the corporate ethos encourages or tolerates such practices, one might reasonably regard the core of the problem as institutional. To single out the lowly employee whose violation occurred in pursuit of the corporate mission could well be regarded as choosing a convenient scapegoat.

Even if high-level managers consciously seek to foster an environment that encourages practices that cross the line and give rise to criminal liability, it is by no means clear that they will bear their share of the blame. The ease with which wrongdoing can be concealed in an organizational setting is another reason corporate criminal liability is recognized. High-level decisions to risk violating the law will not be recorded in corporate minutes. They will, instead, be shrouded in secrecy.²³

20. *Commonwealth v. Beneficial Fin. Co.*, 275 N.E.2d 33, 83 (Mass. 1971), *cert. denied*, 407 U.S. 910, and *cert. denied*, 407 U.S. 914 (1972).

21. Assume that a bank teller with no previous banking experience reports for her first day of work at a branch of Tenth Bank. A customer comes to her window to make two cash deposits in his account. The first deposit is \$8500. The second is \$5000. The teller has never heard of the Currency and Foreign Transactions Reporting Act, which requires that a currency transaction report be filed whenever a deposit or withdrawal of more than \$10,000 in cash occurs. The teller's supervisor knows about the reporting requirement, but does not know that the customer's two deposits must be aggregated for purposes of the reporting requirement. The bank's general counsel, who works across town at the bank's main office, knows that the law requires aggregation, but does not, of course, know that the transaction in question is occurring.

In this scenario, none of the three bank employees has committed a criminal violation of the Act because none has willfully or knowingly failed to file a report. But if we add up what they know—the teller's knowledge that two deposits totalling more than \$10,000 were made, the supervisor's general knowledge of the reporting requirement, and counsel's knowledge that multiple deposits must be aggregated—the requisite knowledge exists. The collective knowledge doctrine permits imputation of the three employees' collective knowledge to the bank for purposes of imposing institutional liability. *See, e.g.*, *United States v. Bank of New England, N.A.*, 821 F.2d 844, 856 (1st Cir.), *cert. denied*, 484 U.S. 943 (1987). Additional cases are collected in 1 KATHLEEN F. BRICKEY, *CORPORATE CRIMINAL LIABILITY* § 4:05 (2d ed. 1992).

22. *Hilton Hotels*, 467 F.2d at 1006.

23. *Beneficial Finance*, 275 N.E.2d at 82.

Thus, we recognize institutional liability for crime partly because group action makes it possible to conceal misconduct even at the highest levels of management.

In the context of Braswell's "one man show," these considerations may seem less than compelling. Although Braswell enjoys the advantages of doing business in corporate form, the cast of characters is small. His business has few employees and no bureaucracy. Thus, miscreant agents will be easier to identify, and opportunities for concealment are considerably reduced. One might posit, moreover, that in a small organization like his, the desire for personal gain is more likely to actuate the wrongdoing.²⁴ Hence, the identified wrongdoer is less likely to be regarded as a scapegoat. The organization may, indeed, be his alter ego.

The premise that close corporations act more like individuals than organizations clearly applies to Braswell's one person corporation. It could apply with equal force to five or ten person corporations, where a small group of people work cooperatively toward a common goal. But as the number of individuals involved in the venture, the complexity of its organization and operations,²⁵ and the volume of business conducted in its name all increase, the characteristics that made its behavior analogous to individual behavior ultimately disappear.

A look at the one thousand largest privately held companies makes the point.²⁶ Cargill Inc., the largest close corporation in the country, boasts sales of \$42 billion and employs nearly 54,000 workers.²⁷ United Parcel Service, the fifth largest, has more than \$13.5 billion in sales and more than 250,000 employees.²⁸

The one hundred largest privately held companies include a litany of household names—corporate providers of goods like Publix Super Markets, Montgomery Ward, Bechtel, Phar-Mor, Hallmark Cards, Levi Strauss, Amway, SC Johnson and Son, Land O'Lakes, Domino's Pizza, Borg-Warner, Ace Hardware, Estee Lauder, and Dow Corning. They

24. Mark A. Cohen, *Corporate Crime and Punishment: An Update on Sentencing Practice in the Federal Courts, 1988-1990*, 71 B.U. L. REV. 247, 278 (1991).

25. E.g., the corporation may have multiple subsidiaries or operating divisions across the country or world wide.

26. Although most of these companies are corporations, the data base includes privately owned businesses that are not incorporated as well. See 4 WARD'S BUSINESS DIRECTORY OF U.S. PRIVATE AND PUBLIC COMPANIES (1993). All of the illustrative examples provided in this article are corporations.

27. *Id.* at 1.

28. *Id.*

include corporate transportation providers like Trans World Airlines and Budget Rent a Car as well. All of the companies in this category have at least \$1.5 billion in sales, and half of them employ tens of thousands of workers.²⁹

The corporate characteristics these organizations display are not limited to the very largest. The top two hundred privately held companies include corporations like Barnes and Noble, Del Monte Foods, Mack Trucks, Maritz, Gulfstream Aerospace, and GAF. Businesses in this second tier post sales ranging from roughly \$900 million to \$1.5 billion and employ up to 45,000 people.³⁰

Levitz Furniture, Seiko of America, Olan Mills, Hartz Mountain, Goodwill Industries, Bell and Howell, and National Car Rental are corporations among the top 300 privately owned companies.³¹ The volume of sales in this tier ranges from \$640 to \$880 million. A majority of these businesses employ more than 3000 people, and employees of about fifteen percent of them number in the tens of thousands.

The top 400 include well known corporate entities like Timex, Alamo Rent A Car, Sverdrup, Franklin Mint, ComputerLand, and Camelot Music.³² The volume of sales for this tier ranges from \$460 to \$540 million. Most of these businesses have more than 2000 employees, and nearly thirty percent employ 5000 or more.

Asplundh Tree Expert, Wickes Lumber Company, and the Bose Corporation are among the top 500.³³ The volume of sales in this tier ranges from \$400 to \$460 million, and most of these companies employ several thousand employees.³⁴

And so it goes down to the thousandth largest privately owned company, Booth Newspapers Inc. Booth has sales of \$450 million and employs 2700 persons.³⁵

The contrast between these corporations and Braswell's business is as stark as that between night and day. Organizations that employ tens of thousands (or perhaps just thousands) of workers are bound to have lay-

29. *Id.*

30. *Id.* at 1-2.

31. *Id.* at 2-3.

32. *Id.* at 3-4.

33. *Id.* at 4-5.

34. West Publishing Company, Rand McNally, Formica, Electrolux, and Russell Stover Candies are among the top 600 close corporations. The volume of sales in this tier ranges from \$400 to \$450 million, and most employ several thousand people. *Id.* at 5-6.

35. *Id.* at 9.

ers of bureaucracy characteristic of large publicly held corporations. Far removed from the one, five, ten, or even thirty person firm, these close corporations function much like their large, publicly held counterparts.

Indeed, some of these entities have had prior incarnations as publicly held corporations. During the corporate takeover mania of the 1980s, the "going private" movement rapidly gained momentum.³⁶ Motivated by the desire to eliminate the trouble and expense of complying with SEC regulations, the need to focus on long-term business strategies rather than quarterly earnings, the determination to avoid hostile takeovers or the like, many publicly traded companies went private—i.e., were acquired by private investment groups or individuals—and thus became close corporations. Instead of being owned by millions or tens of thousands of shareholders, they ordinarily fell into the hands of a single institutional owner—a partnership, management group, corporate subsidiary or the like.

Corporate giants like RJR Nabisco, Beatrice Foods, Safeway, Borg-Warner, Southland Corporation, Macy's, Burlington Industries, and National Gypsum jumped on the going private band wagon.³⁷ But not all of them stayed private for long. Once the threat of a hostile takeover dissipated, for example, so might the sole or principal reason for going private. Thus, within a few years of going private, some firms like RJR Nabisco and Safeway went public again.

These changes in corporate form did not transform the affected entities into smaller, less complex, or less bureaucratic organizations. Just as Braswell's one man corporation continued to function much like a sole proprietorship, large companies that went private in the 1980s continued to behave, for all intents and purposes, like their publicly held counterparts. Their management and capital structures remained the same. All that changed was the shareholder structure—i.e., a change in ownership.

A rule that would subject the RJR Nabiscos and Safeways of the world to criminal liability before they went private and again after they reestablished public personae—but not in between—would be a startling incongruity. The reasons that support recognition of corporate criminal liability are wholly unrelated to the question of who owns the corpora-

36. During the 1980s, 565 publicly traded companies went private. These transactions accounted for a little more than 20% of all public takeovers throughout the decade, but in two peak years equalled 27% of all public takeovers. MERRILL LYNCH, MERGERSTAT REVIEW 1990, 75 (1991).

37. *Id.* at 77.

tion. They are tied, instead, to the bureaucracy that makes personal accountability less likely. That bureaucracy will exist in large corporations whether they are publicly or closely held.

If the rule of institutional liability should treat Braswell and RJR Nabisco differently, then, it is not because Braswell's corporation is closely held. It is because the behavior of his small business is analogous to individual behavior. There are no layers of bureaucracy to penetrate, and he can monitor his few employees with relative ease—not because he is the owner, but because he is the manager. Thus, for purposes of crafting an appropriate institutional liability rule, the corporate form in which he does business has no significance.

Although it is relatively easy to draw gross distinctions between Braswell and RJR Nabisco, to craft a rule that quantifies those distinctions would be a daunting task. A rule that merely selected a minimum number of managers and/or employees, for example, would likely be arbitrary and oversimplified. One that attempted to detail all of the relevant characteristics that distinguish Braswell and RJR Nabisco, on the other hand, would likely be overly complex.

But perhaps an intermediate ground can be found by rethinking why criminal prosecution of Braswell's corporation might be objectionable. Is it because in this setting it is desirable to promote personal accountability? If so, is a corporate fine needed as a proxy for fining the responsible individual? Is the existence of a penetrable "shield of corporate armor"³⁸ apt to make the prosecutor content to prosecute the corporation, thus making it less likely that the individual wrongdoer will be held personally accountable? If so, should we encourage or discourage that result? And if not, what do we gain by giving the government a second bite at the apple? The answers to these questions should guide the wise discretion of the prosecutor.³⁹

III. A CURIOUS RULE

In tandem with the liability issue is the question whether closely held corporations should be subject to the same sentencing rules applicable to their publicly held counterparts. With the exception of a guideline that authorizes offsetting corporate fines against fines paid by owners of

38. *Beneficial Finance*, 275 N.E.2d at 83.

39. *Cf. United States v. Dotterweich*, 320 U.S. 277, 285 (1943) (leaving the task of deciding who has a responsible relationship to a violation of the Food and Drug Act to "the good sense of prosecutors [and] the wise guidance of trial judges").

closely held corporations, the Sentencing Guidelines do not single out close corporations for special treatment.⁴⁰

The offset guideline grants the court discretion to offset a percentage of fines imposed on owners who have at least a five percent ownership interest, provided that the owners were fined for the same offense conduct for which the corporation is to be fined.⁴¹ For purposes of this guideline, a corporation is closely held if it has relatively few owners.⁴² The size of the corporation's work force, sales or assets is of no consequence for sentencing purposes.⁴³

The strongest case for offset presents itself in the context of complete or nearly complete overlap between the fined owner/manager and the corporation. Suppose, for example, that Braswell is convicted of price fixing and fined \$100,000. His corporation is later convicted and fined \$500,000 for the same offense. Although the corporation is an entity separate from Braswell, fining the corporation could be viewed as analogous to fining Braswell himself. As sole owner of the corporation, only he wields any control over it. Thus, payment of a fine with corporate assets is payment with assets he owns. To avoid the appearance of "fining him twice," the corporate fine could be offset by the amount of the fine he personally paid.⁴⁴

40. Cf. Orland, *supra* note 3, at 359 (by ignoring distinctions between large and small corporations, the Guidelines "treat[] unequals equally," thereby "creat[ing] inequality").

The Guidelines do, however, differentiate corporations on the basis of size for purposes of computing the culpability score. See UNITED STATES SENTENCING COMMISSION, GUIDELINES MANUAL, § 8C2.5 (1992) [hereinafter U.S.S.G.].

41. Although an earlier discussion draft of the Guidelines would have required offset, the final version, § 8C3.4, merely authorizes the court to offset the corporate fine.

§ 8C3.4 *Fines Paid by Owners of Closely-Held Organizations*

The court may offset the fine imposed upon a closely-held organization when one or more individuals, each of whom owns at least a 5 percent interest in the organization, has been fined in a federal criminal proceeding for the same offense conduct for which the organization is being sentenced. The amount of such offset shall not exceed the amount resulting from multiplying the total fines imposed on those individuals by those individuals' total percentage interest in the organization.

Id. § 8C3.4.

The offset guideline uses the term "organization" rather than "corporation," presumably for the sake of consistency. But forms of organization other than corporations have no identity separate and apart from their members. Thus, in a noncorporate setting, there is nothing against which an individual owner's fine might be offset. The "organizational" liabilities of partnerships, proprietorships and the like are imposed on any and all of the members, jointly and severally.

42. *Id.* (Application note 1).

43. *Id.*

44. The guideline applies to fines "imposed" on convicted owners. Should it apply when the owner/manager has been indemnified? Cf. DEL CODE ANN. tit. 8, § 145 (1991) (corporation may

The case would be similar if Braswell and his wife were each fifty percent owners and both had been fined. A subsequent corporate fine would likewise be satisfied out of assets that, although held in the corporation's name, they ostensibly own. Hence, the appearance of fining them twice.

It is reasonable to assume that this was the Sentencing Commission's starting point. The offset guideline proceeds from the premise that closely held corporations are usually the alter egos of the owners.⁴⁵ That being true, "appropriate punishment may be achieved by offsetting the fine imposed upon the organization by an amount that reflects the percentage ownership interest of the sentenced individuals and the magnitude of the fines imposed upon those individuals."⁴⁶ Thus, if Mr. Braswell were the sole owner of the corporation, the corporate fine could be offset by the entire amount of his \$100,000 fine. If the Braswells were each fifty percent owners, only fifty percent of his fine could be offset.

Reduction of the corporate fine on the basis of Braswell's personal fine arguably discounts the advantages he derives from doing business in the corporate form. A corporation is a legal entity that is distinct from its incorporators and shareholders. Its rights and obligations are treated as if the corporation were "a separate legal personality."⁴⁷

The separateness of the corporation and its owners usually prevents even a sole shareholder from directly exercising the corporation's rights.⁴⁸ Braswell cannot sue in his own name to redress wrongs against the corporation. Nor can he transfer corporate property in his name.

indemnify agent who acted in good faith, reasonably believed he acted in a manner not inconsistent with the best interests of the corporation, and had no reasonable cause to believe his conduct was unlawful).

If the owner/manager has been indemnified, there is no fairness concern with respect to him if the corporation is later fined. The corporation has made him whole. Nor does the corporation have a fairness argument based on its payment of the fine, because it has voluntarily assumed the liability. The fine was imposed on the individual, not on the corporation.

If fairness to the fined owner is the driving concern behind the offset guideline, should a similar offset be provided for fined officers and directors who have substantial ownership interests in publicly held corporations?

45. U.S.S.G., *supra* note 40, § 8C3.4 (comment. (backg'd.)).

46. *Id.*

47. O'NEAL & THOMPSON, *supra* note 12, § 1.09.

The law recognizes the concept of corporate separateness in the belief that society benefits from allowing the incorporator to separate his personal assets from those invested in the corporation. Separate corporate identity is a privilege designed to promote important objectives like advancing commerce and industrial growth. *Glazer v. Commission on Ethics for Pub. Employees*, 431 So. 2d 752 (La. 1983).

48. Separateness may also prevent a shareholder from exercising personal rights. Thus, for example, an owner/custodian of corporate records like Braswell may not assert the Fifth Amend-

The cause of action belongs to the corporation and must be brought in its name. The corporation likewise owns the property, and Braswell must cause the entity to convey its property in its corporate name.

A principal reason to incorporate (and hence be separate from the organization) is that corporate shareholders enjoy limited liability. All they have at risk is whatever capital they choose to invest. If the corporation breaches a contract with a supplier, the supplier's remedy is against the corporation, and the corporation alone. If the corporation is convicted of a crime but lacks sufficient assets to pay the fine, that is the end of the matter. The government has no claim against the owners in their individual capacities to pay the corporate fine.⁴⁹ Simply put, "[i]nvestors can thus insulate their personal assets from liability arising out of the corporate enterprise."⁵⁰

The concept of corporate separateness does not, of course, insulate the owner/manager from accountability for personal wrongs he commits on behalf of the corporation. Hence, Braswell's amenability to prosecution and conviction for price fixing, notwithstanding that he committed the violation under cloak of his authority as corporate president.⁵¹

Although the offset guideline disregards the separateness of the close corporation owner and the corporation itself, that may well be appropriate in a pure *Braswell* type of setting. Braswell is the sole owner of a small enterprise that he alone manages and operates. In this setting there is *de jure*, but not *de facto*, separateness between Braswell and his corporation. Thus, to fine Braswell *and* his corporation for the same offense is equivalent to fining him twice. The second punishment could be regarded as a penalty for doing business in corporate form. The offset guideline ameliorates the potential harshness of this result by giving Braswell credit for the fine he paid in his own name.

But how does this play outside the context of Braswell's solely owned corporation? Suppose there are five owners—Mr. and Mrs. Braswell, Mr. Braswell's mother, Mr. Braswell's long-time business associate, and the business associate's Aunt Tillie—each of whom owns a twenty per-

ment privilege against self-incrimination to escape producing corporate books and records subpoenaed by grand jury. *Braswell*, 487 U.S. at 115-19.

49. If Braswell is the price fixer, however, the corporate shield will not insulate him from personal liability. *United States v. Wise*, 370 U.S. 405 (1962); O'NEAL & THOMPSON, *supra* note 12, § 1.11. Under some circumstances, however, the corporation is permitted to indemnify him for the fine assessed against him in his individual capacity. *See supra* note 44.

50. O'NEAL & THOMPSON, *supra* note 12, § 1.09, at 38.

51. *See supra* note 49.

cent interest. Braswell and his long-time associate co-manage the business. Braswell's wife, the secretary treasurer, is responsible for corporate financial affairs. His mother, as vice president, is in charge of marketing. Aunt Tillie, who acquired her stock as a gift from her nephew, has never had an active role in the corporation's management. All five owners are compensated in the form of salaries, bonuses, dividends or the like.

Braswell becomes ambitious. Anxious for the corporation to win a lucrative government contract, he arranges a large bank loan to the corporation. To convince the bank that the corporation is creditworthy, he falsifies the corporation's financial statement to report inflated inventories. He also misrepresents the purpose of the loan as "need to expand inventory due to anticipated increased demand." In reality, he will use the loan proceeds to bribe a public official to obtain the government contract.

At the time when this transpires, the remaining officer/managers are experiencing a variety of other distractions. Braswell's wife changes her status from part-time to full-time anesthesiologist at a local hospital, and so attends her corporate financial responsibilities on weekends as time permits. His mother is in a nursing home recuperating from hip surgery. Every day or so she makes goodwill telephone calls to valued corporate customers. The long-time business associate is in the midst of an acrimonious divorce and has assumed a more active role in the care of his children. Aunt Tillie, of course, is blissfully remote from all of this muddle.

The net result is that none of the other owners noticed that Braswell procured a fraudulent corporate loan, whose proceeds were paid as graft to secure the contract. But it is safe to assume that *all* of them noticed the corporation's enhanced profitability under the contract.

Here the case for offset is less than overwhelming, and would be even less so if responsibility for corporate operations were spread among ten, fifteen, or thirty shareholders. In this scenario we lack the kind of identity between owner and organization that exists when Braswell conducts his one man show. Responsibility for corporate operations is more diffused, and one might reasonably conclude that there is both *de jure* and *de facto* separateness between entity and owners.

What is achieved by disregarding that separateness and offsetting Braswell's fine against the corporate fine in this case?⁵² The offset does not

52. Although it is relatively rare for courts to "pierce the corporate veil" and permit an aggrieved third party to hold corporate manager/shareholders personally accountable, the law may

reallocate the corporate fine among the five owners. It does not distinguish between Braswell, who has already paid a fine, and the four “innocent owners” who have not. Thus, granting an offset here merely spreads the credit for Braswell’s fine equally among all five owners.

The focus of the remedy must have changed, then. By reducing the government’s claim against corporate assets that are equally owned by all five owners, the driving concern is not so clearly to minimize unfairness to Braswell. But if that is not it, what else could it be? A desire to give Braswell a little relief because he has already been punished and to share the relief with his co-owners because they have not been convicted? Are his co-owners worthy of relief?⁵³

Assuming *arguendo* that we clear this hurdle and conclude that, at least in principle, offset serves some as yet unarticulated useful goal in

disregard separateness if the corporation is used to promote illegal conduct. *See generally* Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036 (1991).

“[S]ince the franchise is granted by the state for a useful and valid purpose, it may not be employed to further wrong. Where it is so employed the law will disregard the rule, go behind the fiction, and treat the stockholders as if the corporation did not exist.” *Eichelberger v. Arlington Bldg., Inc.*, 280 F. 997, 999 (App. D.C. 1922). *Cf.* *FTC v. Amy Travel Serv., Inc.*, 875 F.2d 564, 574-75 (7th Cir.) (principals of telemarketing firms individually liable for violating FTC Act where they controlled firms, wrote or reviewed misleading telemarketing scripts, and were aware of high volume of consumer complaints and credit card chargebacks), *cert. denied*, 493 U.S. 954 (1989); *Hemphill-Kunstler-Buhler, Auctioneers & Appraisers v. Davis Wholesale Elec. Supply Co.*, 516 So. 2d 402, 403-04 (La. App. 1987) (shareholder, officer or director may not be held liable for corporate obligations except in case of fraud, malfeasance or criminal wrongdoing), *cert. denied*, 520 So. 2d 751 (La. 1988); *J. L. Brock Builders, Inc. v. Dahlbeck*, 391 N.W.2d 110, 114-15 (Neb. 1986) (when corporate entity is used to justify wrong, protect fraud, or defend crime, law will regard corporation as an association of persons); *Nev-Tex Oil & Gas v. Precision Rolled Prods.*, 782 P.2d 1311, 1311 (Nev. 1989) (corporate agent’s fraud on behalf of corporation subjects him to personal liability, whether or not corporate veil could be pierced); *Kaites v. Department of Env’tl. Resources*, 529 A.2d 1148, 1151 (Pa. Commw. 1987) (use of corporate form to perpetrate fraud may justify disregarding corporate form).

Thus, courts may regard the shareholders as an association of individuals whose personal assets are at risk. *J. L. Brock*, 391 N.W.2d at 114-15. The remedy may both make the controlling shareholder liable for corporate obligations and hold the corporation liable for the shareholders’ delicts. *Estudios, Proyectos E Inversiones de Centro America, S.A. v. Swiss Bank Corp.*, 507 So. 2d 1119, 1120-21 (Fla. App. 1987) (corporation may be liable for shareholder’s debts when shareholder fraudulently used corporation to avoid preexisting personal liability).

The offset guideline turns this principle on its head, disregarding the owner’s abuse of the privilege of separateness. The offset amounts to piercing the corporate veil for a wrongdoer’s benefit.

53. Braswell’s crimes put money in the corporate coffers to the benefit of all five owners. The other owners must share some of the blame for his wrongdoing, moreover. Braswell could not have obtained the bank loan on the basis of his personal net worth statement. The corporation was instrumental to his crime. Although none of his co-owners actively participated in his delicts, their lax oversight practices facilitated his misconduct.

this context, the mechanics of applying the guideline to corporations with multiple owners pose another conundrum. Assume that Braswell was fined \$200,000 for his bank fraud and bribery. How much of his personal fine may be offset against that of the corporation? The answer is twenty percent—\$40,000. The guideline achieves “appropriate punishment” by allowing the court to reduce the corporate fine by a percentage of Braswell’s fine that reflects his percentage ownership interest in the corporation.

But what relationship does that percentage bear to minimizing unfairness to Braswell? To minimizing unfairness to the corporation? In what sense does this quantum of relief achieve “appropriate punishment?” In this context the offset guideline is, in truth, a very curious rule.

IV. CONCLUSION

Recognition of corporate criminal liability by the courts was an acknowledgment of the growing power corporations have over commerce. Corporate liability for crime provides a check on corporate power. This core concern applies with equal force to close corporations, which constitute an estimated ninety percent or more of incorporated organizations and include within their ranks some of the largest business entities in the country.

Although many small “mom and pop” operations like Braswell’s conduct business as closely held corporations, their ownership structure is not germane to the question whether their operations should be subject to the rule of institutional criminal liability. What makes the “corporateness” of these operations qualitatively different is not that they are privately held, but that they are small, uncomplicated organizations in which the owners often actively manage the business. In these organizations, wrongdoers can be identified with relative ease because there is little corporate bureaucracy or hierarchy to cloak their identities or motives.

Whether these corporations should be governed by the institutional liability rule is partly a function of the practical relationship between personal and institutional accountability, and partly of what (or whether) we gain from demanding both. If we do demand both, it makes little sense to disregard the institution’s “corporateness” absent strong identity between the convicted owner/manager and the corporation itself.