No. 11-882

IN THE

# Supreme Court of the United States

CHARLES W. MCCALL,

*Petitioner,*

v.

UNITED STATES,

*Respondent.*

**On Petition For A Writ Of Certiorari To The United States Court of Appeals for the Ninth Circuit**

## REPLY BRIEF FOR PETITIONER


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## REPLY BRIEF FOR PETITIONER

Petitioner's second jury was told that it could convict him if it found that he had acted with "reckless disregard," even if not with actual knowledge. In a double-whammy, the second jury was also instructed that "reckless disregard" means nothing more than making a statement "without regard to its truth or falsity." So instructed, petitioner's second jury did what his first jury could not—it convicted him on all but one of the charged counts.

Understandably, the government does not defend the "without regard" instruction. Nor does it dispute that, in the wake of this Court's decision in *United States* v. *O'Hagan*, 521 U.S. 642 (1997), two Circuits have flatly stated that recklessness—even if properly defined—*never* suffices to prove scienter in a criminal securities case. And the government has no response to our fundamental point: these two questions cut to the heart of what separates *criminal* scienter from ordinary *civil* securities-fraud liability.

In the government's view, however, this case is the wrong vehicle for resolving the questions presented. That is just not so. As we explained in the petition, the court of appeals explicitly *presupposed* the validity of the "without regard" instruction; indeed, only by doing so was the panel able to avoid applying Circuit precedent requiring *per se* reversal for failure to give a defense-theory instruction. Accordingly, a favorable disposition by this Court of the questions presented would result in a new trial for petitioner. The petition should be granted.

## I. The Petition Presents Important And Recurring Questions About Criminal Scienter That Divide The Circuits

The Second and Eighth Circuits have held that mere recklessness does not constitute "willfulness" under the criminal securities laws. The government disputes whether they really meant it. They did.

The Eighth Circuit applied this Court's decision in *O'Hagan*, on remand, to a challenged scienter instruction. *United States* v. *O'Hagan*, 139 F.3d 641 (8th Cir. 1998). The defendant contended that, to act willfully, he had to know and intend to violate the precise contours of Rule 10b-5. See *id.* at 646. The defendant relied on the following language in this Court's *O'Hagan* decision:

> Vital to our decision that criminal liability may be sustained under the misappropriation theory, we emphasize, are two sturdy safeguards Congress has provided regarding scienter. To establish a criminal violation of Rule 10b-5, the Government must prove that a person 'willfully' violated the provision. *See* 15 U.S.C. § 77ff(a). Furthermore, a defendant may not be imprisoned for violating Rule 10b-5 if he proves that he had no knowledge of the rule. *See ibid.*

*Id.* at 646–47 (quoting 521 U.S. at 665).

The Eighth Circuit concluded that the defendant's reading of *O'Hagan* was a bridge too far. Instead, the court of appeals held (not the least bit in *dicta*):

> *Contrary to [defendant's] present claim*, we think it is clear that the Supreme Court was simply explaining that the statute provides that a negligent or reckless violation of the securities

> law cannot result in criminal liability; instead, the defendant must act willfully.

*Id.* at 647 (emphasis added).[1]

The Second Circuit has spoken just as emphatically. The "principal question" in *United States* v. *Gansman* was whether the district court had erred when it refused to instruct the jury that, by reposing trust and confidence in a colleague, defendant did not "willfully" engage in insider trading. 657 F.3d 85, 91 (2d Cir. 2011). In resolving that issue, the Second Circuit explained what scienter means in a criminal Section 10(b) case:

> To impose criminal sanctions, the government must prove the offense beyond a reasonable doubt, *including that the defendant's conduct was willful*. Civil liability, on the other hand, may attach if the government proves the offense by a preponderance of the evidence, *including that the defendant's conduct was merely reckless, rather than willful*.

*Id.* at 91 n.7 (emphasis added and citations omitted). The Second Circuit's disagreement with the Ninth Circuit's contrary position could not be clearer.

The government's reliance (Opp. 18) on four-decade-old Second and Eighth Circuit decisions does

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[1] In recent briefing to the Eighth Circuit in another case, the government recognized the quoted text to have been that court's "conclu[sion]" in *O'Hagan*. See U.S. Br. 50–51, *United States* v. *Behrens*, No. 11-3482, 2012 WL 948100 (filed Mar. 5, 2012). Other courts likewise have understood the Eighth Circuit's pronouncement in *O'Hagan*. See *United States* v. *Moldofsky*, No. 00-cr-388-RPP, 2002 WL 31385819, at *5 (S.D.N.Y. Oct. 21, 2002).

not explain away those courts' divergent rulings *since* this Court's 1997 *O'Hagan* decision (and its relevant pronouncements in *Bryan* v. *United States*, 524 U.S. 184 (1998), and *Ratzlaf* v. *United States*, 510 U.S. 135 (1994)).[2] And its citation (Opp. 19) of the Ninth and Sixth Circuits' contrary decisions only underscores the circuit split.

In short, the "'scienter mess'" in federal criminal securities law (Pet. 12 (quoting Samuel W. Buell, *What Is Securities Fraud?*, 61 Duke L.J. 511, 548 (2011)) is reflected in a deepening split among the circuits on recklessness. This Court's resolution of the questions presented is of surpassing importance.[3]

## II. This Case Is A Good Vehicle To Address The Questions Presented Because A Favorable Answer To Either Question Would Require Reversal

The government's primary contention in opposition is that petitioner's case is a poor vehicle for addressing the important legal questions presented.[4] The government makes two points: first,

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[2] The government (Opp. 22–23) attacks a strawman in lieu of confronting petitioner's fundamental point based on *Bryan* and *Ratzlaf*: Where, as here, "willfulness" is all that distinguishes civil from criminal liability for the same act, it cannot be mere surplusage. See Pet. 13–15.

[3] The government is mistaken when it says (Opp. 19) that this Court did not grant review of a question presenting the merits of a civil recklessness standard in *Central Bank of Denver, N.A.* v. *First Interstate Bank of Denver, N.A.*, 511 U.S. 164 (1994). See *id.* at 194–95 (Stevens, J., dissenting).

[4] The government also quarrels with whether the questions presented are broad enough to result in reversal. They are. The questions presented are "[w]hether petitioner's convictions *must*

that the court of appeals would adhere to its judgment regardless of how this Court answers the questions presented; and second, that this was in any event an "actual knowledge" case only, not a recklessness case. Both premises are false.

1. It is simply not true that the court below would adhere to its disposition if this Court were to resolve the questions presented in petitioner's favor. To the contrary, the Ninth Circuit's analysis explicitly *presupposed* that the district court's "reckless disregard" instruction—including its "without regard" definition—*was correct*. If this Court held differently, the court of appeals surely would follow suit.

Indeed, it would have to do so. It is well settled in the Ninth Circuit that the failure to give a defense-theory instruction is reversible *per se*. See, *e.g.*, *United States* v. *Marguet-Pillado*, 648 F.3d 1001, 1006 (9th Cir. 2011). In rejecting petitioner's contention to that effect, the court of appeals therefore could not—and did not—rely on harmless error. See 441 Fed. App'x 515. Instead, it held that in light of the "reckless disregard" instruction (and the plain vanilla good-faith instruction), there was no need to give petitioner's defense-theory instruction. In short, the panel relied on the very instruction we have challenged to avoid the application of the Ninth

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*be reversed*" either because "reckless" misstatements aren't "willful," or because a criminal-recklessness standard in securities cases cannot be *less* robust than the civil-recklessness standard. Pet. i (emphasis added). As described in the Petition (at 21–25) and herein (pp. 5–6, 9 n.6), the Ninth Circuit's harmless-error speculation does not prevent this Court from reversing in the event that it reaches an affirmative answer to either question presented.

Circuit's rule of *per se* reversal. It is inconceivable that the Ninth Circuit would adhere to that result if this Court were to hold that that the "reckless disregard" instruction is in fact *erroneous*.

2. Nor is it the case that the government's only "theory at trial was that petitioner 'knew—not merely must have known—about the company's fraudulent practices.'" Opp. 14 (quoting Gov't C.A. Opp'n to Reh'g 4, 10); see also Opp. 16. Indeed, that is flat out wrong. Prosecutors told petitioner's jury, point blank, that reckless disregard was an alternative path to conviction:

> [I]n the instructions you will find [an] alternative theory for guilt, *and this is a theory based on reckless disregard*.

Tr. 2849–50 (emphasis added). The government emphasized that if the jury found that petitioner had "turned a blind eye to what was going on," it should find that he had acted "with reckless disregard, *which would be an alternative theory supporting the guilt here*." Tr. 2850 (emphasis added).

The government milked that "alternative theory" for all it was worth. It asked the company's outside investigator to describe various "yellow flags" that he had discussed with petitioner, and elicited petitioner's statements that those yellow flags "should have prompted him to do more," that he had "dropped the ball," and that "in hindsight he had been an idiot" for trusting assurances from his subordinates. Tr. 1680, 1683–85, 1687, 1716–17, 1719. It also asked witnesses whether it would "be fair" to have expected more diligence from petitioner in response to yellow flags. Tr. 1667.

The government's summation drove home that "reckless disregard" theory. The prosecutors argued, for example, that "yellow flag[s] * * * about possible fraud within the finance department" had stared petitioner in the face. Tr. 2799–2800. And they told the jury—time and again—that to be a "truly innocent person" petitioner needed to have reacted more boldly in response to those yellow flags. Tr. 2806, 2821. In particular, the government proposed to the jury that petitioner should have issued clearer directives to his finance team (Tr. 2807), prohibited the clarification of sales policies by voicemail (Tr. 2807), referred yellow flags to auditors (Tr. 2820), authorized a "forensic audit" of the company's revenue recognition (Tr. 2822), and hired outside counsel to probe whether the company had unreported side letters (Tr. 2822).

And there is more. No less an observer of the government's evidence than the judge at petitioner's first trial remarked, after hearing the case against petitioner, that prosecutors "in large measure" were "*rely[ing] on the recklessness standard*," and accordingly that "the definition of what is reckless disregard *is an important instruction in this case*." 2006 Tr. 2689, 2709 (emphasis added); see also Pet. 21. Things were no different the second time around, where the record demonstrates *to a certainty* that petitioner's second jury was deeply concerned with how it should apply the district court's revised (and watered down) "reckless disregard" instruction to the evidence. See Pet. 16 n.4.

The government responds to those inconvenient facts with radio silence. Moreover, it misstates and overstates the record to make evidence of petitioner's

actual knowledge loom larger than it really did at trial:

- Petitioner was not among the "managers" (Opp. 2–3) in attendance on June 17, 1998, when Bergonzi instructed his sales team to close business with side-letter contingencies. Tr. 487.
- Petitioner's only part in a June 1998 transaction with Holy Cross Hospital was attending a short lunch meeting on June 25. Tr. 567–73. The evidence was equivocal, at best, that "HBOC personnel proposed" a side letter "during the same meeting," when petitioner was "present." Opp. 3; cf. Tr. 599–601. In fact, HBOC and Holy Cross Hospital finalized a contract and side letter at a *different* meeting, on a *different* day, in a *different* city—all without petitioner's attendance or involvement. See Tr. 588; Trial Exs. 103, 329, 330 (contracts dated June 30, 1998); cf. Opp. 3, 14.
- Petitioner *did* "look into the matter[s]" that Petras raised. Cf. Opp. 4. The company's investigator, Daniel Dooley, and its co-president, Bergonzi, testified that petitioner confronted Bergonzi with Petras's accusations, and that Bergonzi misled him with assurances that Petras had his facts wrong. Tr. 1718–21, 2161.
- Petitioner's involvement in the April 1999 Data General transaction was limited to a five-minute telephone call, during which petitioner told the counter-party that he had heard nothing about any supposed right of return. Tr. 1194–96; cf. Opp. 5, 14–15. Moreover, it is not true (cf. Opp. 5, 14) that the Data General transaction closed the "same day" as petitioner's telephone call. Rather,

it closed a few days later, after negotiations in which petitioner did not take part. Tr. 1197–1200.

The evidence that petitioner *actually knew* about the fraud was nowhere close to overwhelming, and that is doubtless why the government relied so heavily on its "alternative theory for guilt" premised on petitioner's "reckless disregard" of "yellow flags."[5]

## III. The "Reckless Disregard" Instruction, And Its "Without Regard" Definition, Diluted The *Mens Rea* Element

The government finds solace in petitioner's inability to cite a case "rejecting the district court's instructions in this case." Opp. 24. *But those instructions were unprecedented*; there is no case to cite. To our knowledge, no court has ever instructed a jury that it could convict a defendant merely for making a statement "without regard" to its truth or falsity. Naturally enough, the government is unable

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[5] The government bolsters its argument (Opp. 15–16) by pointing to petitioner's conviction on the circumvention count, which it claims could be based only on a finding of actual knowledge, not reckless disregard. Like the court below, the government slices the onion too thin. Petitioner's jury was told that "reckless disregard"—defined as nothing more than acting "without regard" to the truth—constituted a "purpose to defraud." At the same time, the jury was told that "willfulness" meant having "the purpose of undertaking an act that one knows to be wrongful." Tr. 3131–32; see also Pet. 23. Any jury—especially a jury that is presumed to follow the instructions *as a whole* (Opp. 15)—would naturally infer that a defendant who had a "purpose to defraud" therefore acted "willfully" as well. There is therefore every reason to believe that the erroneous recklessness instruction tainted every count that required a "willfulness" finding—including the circumvention count.

to locate a single case *approving* such a prejudicially low scienter standard.

In fact, the government never contends that the "without regard" instruction was *correct*; instead it claims that the deeply flawed instruction can be chalked up to "latitude in wording." Opp. 23. But the district court did not enjoy poetic license to misstate the law on such a critical issue. Nor did the instructions cover the "essential points" of the *civil* recklessness instruction on which petitioner based his defense. Petitioner's second jury was not instructed—as his first jury had been—that only an "'*intentional and extreme departure* from standards of ordinary care that presents a danger of misleading buyers and sellers that is either *known* to the defendant or *so obvious* that the defendant *must have been aware of it*'" is criminal. Pet. 5–6. In particular, the second jury did not learn that "gross" and even "inexcusable" negligence are not enough to support a conviction. *Ibid.* Instructions that "'careless[ness],'" "'ignorance,'" and "'mistake'" were insufficient could not possibly substitute for petitioner's requested charge. Cf. Opp. 23–24.[6] An ocean of potentially culpable mental states divides "mistakes" from "intentional and extreme departure[s] from standards of ordinary care," and petitioner's second jury was left to navigate those murky waters on its own.

And so it is remarkable that the government claims "no harm, no foul" by suggesting that

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[6] The government does not address this Court's explanation, in another context, that "reckless disregard" and "good faith" are *not* two sides of the same coin, because the latter is "'far less stringent'" a standard than the former. Pet. 20 (quoting *Monitor Patriot Co.* v. *Roy*, 401 U.S. 265, 272 (1971)).

petitioner wasn't "prevented" "from presenting his defense that his gross or inexcusable negligence could not establish the requisite fraudulent intent." Opp. 24. The government's hypothesis is that (1) petitioner should have argued a legal standard to the jury that the district court had just *rejected* at his charge conference, and (2) if counsel managed to make that argument before being shouted down, the jury would have credited it, despite its being untethered from the instructions that jurors are commanded to follow. The suggestion is baseless, and petitioner in fact diluted his summation to the second jury to track the diluted jury instructions. See Pet. 7. There is every reason to believe that made all the difference.

* * * * *

Petitioner is serving ten years in prison almost surely because his second jury, unlike his first, was told that reckless disregard means nothing more than making a statement "without regard" to its truth or falsity. At no stage of this case—not in the district court, not in the Ninth Circuit, and not in its brief in opposition—has the government defended that unprecedented instruction. And although the court below presupposed the correctness of that instruction in its decision, it steered clear of actually saying a kind word about it on the merits. Instead, the court of appeals served up an utterly speculative reason to affirm—the only conceivable way it could have avoided addressing squarely the very split with its sister circuits presented here. Petitioner is due his day in court.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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