CARLTON FIELDS

“Are You In Control? Does It Matter?”

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The mail fraud statute first appeared in 1872 as part of a revision of federal postal laws. Later, in 1952, Congress enacted the wire fraud statute in order to extend the prohibitions on mail fraud to newer communications technologies. Courts have generally held that wire fraud is identical to mail fraud under federal law, except for the means of communication used.[1] For a long time now, mail and wire fraud prosecutions have served as important weapons in the government’s arsenal to prosecute individuals and businesses alike. A violation occurs when there exists: (i) a scheme to defraud; (ii) money or property [as the object of the scheme], and (iii) use of the mails or wires to further the scheme. *U.S. v. Dinome*, 86 F.3d 277, 283 (2d Cir. 1996). Although, the government must prove these elements beyond a reasonable doubt. *United States v. Binday*, 804, F.3d 558, 569 (2d Cir. 2015), the government is not required to show that the intended victim was actually defrauded. *U.S. v. Mittelstaedt*, 31 F.3d 1208, 1216 (2d Cir. 1994). The government need only show that the defendant contemplated some actual harm or injury. *Id*. This article will predominantly focus on the second fraud element involving money or property (*i.e.*, the intent to defraud) in light of *Kelly v. U.S.*, 140 S. Ct. 1565 (2020) and *U.S. v. Gatto*, 986 F.3d 104 (2d Cir. 2021) and the future of “right to control theory” federal prosecutions post *Kelly*.

The “right to control” theory posits that not all property protected under the fraud statutes is money-based, and is predicated on a showing that some person or entity has been deprived of potentially valuable economic information or position. *Dinome*, 86 F.3d at 283 (quoting *U.S. v. Wallach*, 935 F.2d 445 (2d Cir. 1991). This theory is often seen in cases where the defendant’s scheme affected the victim’s economic calculus or the benefits and burdens of an agreement, or pertained to the quality of services bargained for, or exposed the victim to unexpected economic risk. *U.S. v. Percoco*, 13 F.4th 158, 170 (2d Cir. 2021).

To understand how the “right to control theory” has been utilized, we can look at cases antecedent to *Kelly* and *Gatto*. For instance in *Mittelstaedt*, the defendant, a consulting engineer for two

communities abused his influence with local government on zoning and planning matters by engaging in real estate projects there, making reports and recommendations regarding the construction of the projects, and using partners to conceal his participation and secret interest in those projects. *Mittelstaedt*, 31 F.3d at 1211. He was charged with fraud and convicted. On appeal, the defendant argued that the information he withheld was not material information. *Id.* at 1217. In opposition, the government argued the concealed information created the loss of the right to control the expenditure of public funds, through an inability to make a fully informed decision. *Id.* Ultimately, the Second Circuit reversed the conviction, finding that an individual who is standing in a fiduciary relationship with another and who conceals material information is not subject mail fraud liability. *Id.*

In contrast, in *Dinome*, just one year after *Mittelstaedt*, the same circuit, in an opinion that it acknowledged was at odds with the *Mittelstaedt* formulation, nonetheless upheld a conviction for fraud, where the Defendant was charged in connection with falsely stating his income to a bank to obtain a mortgage. *Dinome*, 86 F.3d at 284. The Defendant argued that the false information had no impact on the ultimate value of the transaction to the bank. *Id.* The Court, focusing on the property element of mail and wire fraud, found that under the "right to control" theory, the information withheld significantly diminished the value of the mortgage transaction to the bank.

Another noteworthy case is *U.S. v. Finazzo*, 850 F.3d 94 (2d Cir. 2017). Defendant, a former merchandising executive, caused the retail apparel company for which he worked to use a supplier for its T-shirts and fleeces that was making secret payments to the defendant on portions of the supplier's profits. *Id.* Defendant argued that the "right to control" does not constitute "property" under the mail and wire fraud statutes, because it is not "obtainable." *Id.* at 105. The Second Circuit rejected his argument, finding that the deprivation of potentially valuable information would create a risk of tangible harm. *Id.* at 111.

Now, less than two years ago, the Supreme Court in *Kelly*, has made clear that to be successful in prosecuting under the federal-program fraud and wire fraud laws, a prosecution must show that the object of the scheme to defraud was money or property. *Kelly*, 140 S. Ct. at 1565. Specifically, a property fraud conviction cannot stand when the loss is only an incidental byproduct of the fraud scheme. *Id.* at 1573. The Supreme Court further noted that the purpose of the mail and wire fraud statutes is not to criminalize acts of undisclosed self-dealing by public officials, acts of dishonesty by state and local officials, nor deprivation of citizens' intangible rights. *Id.* at 1571.

Just last year, the *Gatto* case went up to the Second Circuit. In *Gatto*, defendants were charged with wire fraud for violating the National Collegiate Athletic Association's ("NCAA") rules by paying tens of thousands of dollars to families of high school basketball players to induce them to attend specific universities. *Gatto*, 986 F.3d at 110-11. The Court focused on the second element of mail or wire fraud and found for the government. Notably the court rationalized that defendants need not literally obtain money or property. *Id.* at 113. The Court held that the scheme itself withheld valuable

information that would have caused the universities not to dispense with their property (i.e., athletic-based financial aid).

Many fraud prosecutions involve easily identifiable property takings. The mail and wire fraud statutes are well suited to these types of cases. But Government fraud theories over the years have become expansive. The Bridgegate fiasco is an obvious example. The Supreme Court took on the issue of how far fraud theories can go in *Kelly* by focusing on the object [“property”] of the scheme. Its ruling puts in question future prosecutions where the loss of actual property is less clear, like we saw in 2021, with *Gatto* and the “potential loss of athletic-aid”. These cases reveal that there may be a re-examination of theories of prosecution in cases like Varsity Blues and FIFA. Or cases arising out of alleged unethical conduct affecting organizations like the NCAA and the NFL. The ripple effects may reach prosecutions in money laundering and FCPA cases where the underlying predicate offense is an alleged mail or wire fraud. Given how appellate courts in cases like *Gatto* have not followed *Kelly* in lock step, all that is certain is that prosecutors will continue to be creative in charging decisions and defense lawyers will be ready to push back. Ultimately, these recent cases have demonstrated that not being in control *may* not matter.

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[1] *See United States v. Frey*, 42 F.3d 795 (3d Cir. 1994).

Authored By

Michael S. Pasano

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