

WHO IS RESPONSIBLE FOR HOW EXECUTIVES BEHAVE?

Executive officers of companies work to maximize profits. For public companies, the stock price is often connected to the direct actions taken by the executive officers and dictates the health of the company. Executives who allow a stock price to fall are often ousted in the hopes that a new leader can reverse the company's negative course. Yet some executives take this profit drive to the extreme, utilizing illegal means to increase the profitability of their company, and in turn, increasing their own wealth.¹

The idea of corporate governance is broad—encompassing various actions that officers and directors should take, documents that should be produced for investors and shareholders, and outlines of company goals and initiatives undertaken to increase future profitability. However, underlying all of the corporate governance initiatives is the fundamental incentive to increase the profitability of the company.

Does corporate governance also require that companies must monitor the means their executives use to create profit? In industries where companies are already breaking the rules, due to lackluster regulatory bodies, disproportionately low enforcement, or insufficient incentivizing via fines, it is acceptable to allow for socially responsible rule breaking?

If socially responsible rule breaking were allowable, who would decide the limits? One might suggest that shareholders hold executives accountable. However, this could give rise to potential abuse by shareholders to constantly launch attacks against companies, with attorneys' reaping significant amounts of money in a process that seems to only benefit them, as is often the argument with shareholder derivative suits.²

If we choose not to allow rule breaking, which is the likely path for most members of society, should corporations have a duty to scrutinize the behaviors of their executives, particularly if illegal means are utilized? One solution explored below, and seen in food and drug law, is where criminal liability may be an implication to prevent egregious social harm.³

¹ Ethan Rome, *Big Pharma CEOs Rake in \$1.57 Billion in Pay*, HUFFPOST BUS. (May 8, 2013, 8:19 AM), http://www.huffingtonpost.com/ethan-rome/big-pharma-ceo-pay_b_3236641.html.

² David G. Epstein et al., *BUS. STRUCTURES 279* (West Academic Publishing, 4th ed. 2015).

³ *United States v. Park*, 421 U.S. 658, 669 (1975).

I. ALLOWING RULE BREAKING

Some illegal actions are socially acceptable.⁴ Most drivers have surpassed the speed limit and many pedestrians have jaywalked across a street. But how far would society go in allowing corporate executives to break the law? Currently laws are passed by the elected legislative branch and interpreted by the judicial branch.⁵ If we permitted certain violations of the law, one suggestion might be that companies within the industry regulate themselves with a plan put in place after discussions with government overseers. An example of this method might be compared to the Corporate Integrity Agreements (“CIA”), which are self-policing mechanisms that pharmaceutical companies sign to comply with the U.S. Department of Health and Human Services’ policies after they have negotiated civil settlement agreements.⁶ The CIAs are tailored to the company to try to address the specific facts of the case where the pharmaceutical companies have violated a law.⁷ But one problem with this solution would be enforcement, as the government would be overburdened with the added regulatory responsibility of making sure that companies are self-policing.⁸

Another suggestion might be to have auditors measure the impact of the rule breaking to determine the impact of the violation and if it is acceptable. This suggestion, however, is quite subjective as different parties have different ways of measuring “acceptability” because one has to take in the impact on human capital, the environment, industry, and money, among other things.⁹

II. SCRUTINIZING EXECUTIVES’ BEHAVIOR

Before the Food, Drug and Cosmetic Act of 1938, courts rationalized dispensing the *mens rea* requirement and imposing a strict liability standard, by stating that the statutory prohibition of the sale of liquor did not require

⁴ Christina Sterbenz, *The 13 Most Commonly Broken Laws*, BUS. INSIDER (Oct. 10, 2013, 6:15 PM), <http://www.businessinsider.com/most-commonly-broken-laws-in-america-2013-10>.

⁵ *The Judicial Branch*, THE WHITE HOUSE, <https://www.whitehouse.gov/1600/judicial-branch>; *The Legislative Branch*, THE WHITE HOUSE, <https://www.whitehouse.gov/1600/legislative-branch>.

⁶ OFFICE OF INSPECTOR GEN., *Corporate Integrity Agreement FAQ*, U.S. DEP’T OF HEALTH & HUMAN SERVS., <http://oig.hhs.gov/faqs/corporate-integrity-agreements-faq.asp> (last visited Apr. 10, 2016).

⁷ OFFICE OF INSPECTOR GEN., *supra* note 6.

⁸ Breanna Holt, *An Examination of Strict Criminal Liability Under the Food, Drug and Cosmetic Act of 1938: Is It Time For Change?*, DIG. ACCESS TO SCHOLARSHIP AT HARV., 1999, at 27, https://dash.harvard.edu/bitstream/handle/1/8889485/Holt,_Breanna_-_Paper.pdf?sequence=1.

⁹ Daron Acemoglu & Matthew O. Jackson, *Social Norms and Enforcement Laws*, VOX (Sept. 19, 2014), <http://www.voxeu.org/article/social-norms-and-enforcement-laws>.

evidence that the seller/defendant knew or did not know the illegality of his act.¹⁰ Throughout the 1860's, this public welfare doctrine prevailed in many states in cases involving food adulteration.¹¹ In *United States v. Dotterweich*, the Court reasoned that because corporations are intangible entities and must act through people, those who are engaged in distributing adulterated or misbranded drugs are strictly liable if they are in a "position of responsibility."¹² Building off of that, in *United States v. Park*, the Court stated that "[t]he Act imposes upon persons exercising supervisory responsibility reposed in them by a business organization not only a positive duty to seek out and remedy violations but also, and primarily a duty to implement measures that will insure that violations do not occur."¹³

Since *Dotterweich* and *Park*, researchers have questioned whether the threat of criminal liability serves as an adequate deterrent.¹⁴ This is the most often cited rationale for imposing criminal liability on corporate executives that fall within the scope of the definition.¹⁵ However, there is no evidence that personal criminal liability is an effective deterrent.¹⁶ Arguments opposing the use of strict personal liability include: (1) that is is unjust; (2) that other mechanisms could be used to protect the public welfare; (3) that is it unfair to subject people to possible criminal punishment where the requirements of the Act are not clear; (4) that the deterrent purpose is not a satisfactory rationale if the defendant exercised reasonable care and was unaware of the violation; and (5) that the government might require companies to conform to a higher standard not required by the law with simply the threat of criminal prosecution.¹⁷

Criminal prosecution of corporate executives is more likely if the alleged offender "was previously notified of suspected violations and thereafter refused to correct the offending conduct . . . [or] if the violation was intentional, easily detectable, preventable, fraudulent, or life threatening."¹⁸

¹⁰ Holt, *supra* note 8, at 3.

¹¹ *Id.*

¹² *United States v. Dotterweich*, 320 U.S. 277, 284 (1943).

¹³ *United States v. Park*, 421 U.S. 658, 658–59 (1975) (syllabus).

¹⁴ Holt, *supra* note 8; Vandya Swaminathan & Matthew Avery, *FDA Enforcement of Criminal Liability for Clinical Investigator Fraud*, 4:2 HASTINGS SCI. AND TECH. L. J. 325 (2012).

¹⁵ Holt, *supra* note 8, at 27.

¹⁶ *Id.* at 28.

¹⁷ *Id.* at 28–29.

¹⁸ Holt, *supra* note 8, at 30.

However, there is no concrete definition of who qualifies as a “reasonable person,” which makes criminal liability a real threat for corporate executives.¹⁹

Another method to curb corporate executives’ urge to use illegal means is to bar executives from participating within the industry. Debarment is used by the Food and Drug Administration (FDA) when executives have been convicted of crimes “relating to health care fraud.”²⁰ The debarment consequence applies if an executive has been convicted of a violation of the Food, Drug and Cosmetic Act that relates to the approval or regulation of a drug product.²¹ Debarment can occur in addition to imprisonment or a fine.²² Disallowing an executive to continue to practice within that industry would seemingly limit one’s job prospects, which could also serve as a deterrent. Ultimately, the issue with both criminal prosecution and debarment is that the use of these tools hinge on the enforcement power of the FDA and the Department of Justice.

The last option is ever present: to accept a reduction in profits in order to ensure that the company is in complete compliance with the law and is not too far into the gray zone. This, however, can be detrimental for a company because this risk-adverse approach is antithetical to the traditional business ideology of taking risks to increase the potential for profit windfalls. This then becomes a strategic decision. How long should corporations accept profit losses in order to comply with laws and regulations, without adversely impacting the company?

CONCLUSION

Ultimately, executive behavior is difficult to control. Executives are constantly driven to raise company profits in order to maintain their positions, and deterrent methods are limited. While the strict liability standard is present in the food and drug industries, it would be a slippery slope to extend the public welfare argument to all corporations. Additionally, there is little justification for debarment because a conviction has to be present before that action is taken. This ultimately leads back to the issue of enforcement and the difficulty in proving inappropriate or illegal executive behavior. It is likely that many companies will allow executives to explore in the gray area so long as

¹⁹ *Id.* at 30–31.

²⁰ 42 U.S.C. § 1320(a) (2010).

²¹ *Id.*

²² *Id.*

they continue to increase company profits without increasing company liability.

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