

# OFFICIAL TRANSCRIPT PROCEEDINGS BEFORE

THE SUPREME COURT OF THE UNITED STATES

DKT/CASE NO. 86-234 & 86-286

TITLE CHARLES J. McNALLY, Petitioner V. UNITED STATES; and  
JAMES E. GRAY, Petitioner V. UNITED STATES

PLACE Washington, D. C.

DATE April 22, 1987

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IN THE SUPREME COURT OF THE UNITED STATES

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CHARLES J. MCNALLY, :  
Petitioner :  
v. : No. 86-234  
UNITED STATES; :  
and :  
JAMES E. GRAY, :  
Petitioner : No. 86-286  
v. :  
UNITED STATES :  
-----x

Washington, D.C.  
April 21, 1987

The above-entitled matter came on for oral  
argument before the Supreme Court of the United States  
at 1:56 o'clock p.m.

APPEARANCES:

CARTER J. PHILLIPS, Washington, D.C.;  
on behalf of Petitioner  
DONALD B. AYER, Washington, D.C.;  
Dep. Sol. Gen.  
Dept. of Justice  
on behalf of Respondent

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1 P R O C E E D I N G S

2 CHIEF JUSTICE REHNQUIST: Mr. Phillips, you may  
3 proceed whenever you're ready.

4 ORAL ARGUMENT OF

5 CARTER J. PHILLIPS

6 ON BEHALF OF PETITIONER

7 MR. PHILLIPS: Mr. Chief Justice, and may it  
8 please the Court:

9 MR. PHILLIPS: This case involves the proper  
10 interpretation of 18 U.S.C. Section 1341, the Federal Mail  
11 Fraud Statute. The primary issue presented is whether it  
12 is fraud within the meaning of that statute for a  
13 political party leader to fail to disclose to state  
14 officials a potential conflict of interest in his handling  
15 of the state's patronage system.

16 The Court of Appeals held that a conviction  
17 under this so-called intangible rights theory is proper  
18 and we urge this court to reverse. The basic facts were  
19 as follows: The petitioners and the third individual,  
20 Howard Hunt, were politically active in the Democratic  
21 Party, in the state of Kentucky, during the 1970s. In  
22 part because of their hard work on behalf of Governor  
23 Carroll, who was elected in 1974, petitioner Gray was  
24 appointed to a cabinet position in 1976 and Mr. Hunt was  
25 named head of the Democratic Party.



1           Hunt as the head of the Democratic Party was  
2   invested with substantial patronage powers by the  
3   governor, which is not an uncommon practice, I think, in  
4   any state. What may be somewhat less common is the  
5   decades long tradition in Kentucky that certain state  
6   insurance commissions are treated as part of the patronage  
7   system.

8           Thus, the agent for the state in procuring  
9   insurance was asked to share commissions with other  
10   individuals holding insurance licenses.

11           QUESTION: Why is that worse than ordinary party  
12   patronage? I don't understand.

13           MR. PHILLIPS: I don't know that it is worse  
14   than ordinary party patronage. I think it's just somewhat  
15   less common than any other party patronage.

16           QUESTION: All of it is fraud as far as you're  
17   concerned?

18           MR. PHILLIPS: As far as the government's  
19   concerned.

20           QUESTION: Right.

21           MR. PHILLIPS: Yes, I think that's correct.

22           QUESTION: Does it include box seats to the  
23   Derby? (Laughter).

24           MR. PHILLIPS: I suspect the government would  
25   say so. Yes, Your Honor. Those receiving shared

1 commissions were not required to perform any services or  
2 to be engaged in the insurance business at the time that  
3 they received those commissions. All that was required  
4 was that a licensed agent be available. And it was not  
5 uncommon frankly for relatives of public officials to  
6 receive some of those commissions. For instance, the  
7 State Insurance Commission --

8 QUESTION: Was there no violation of state law  
9 for these people to get commissions for having done no  
10 work?

11 MR. PHILLIPS: No, absolutely not a violation of  
12 state law to receive commissions for doing no work. There  
13 is no obligation that you do any work.

14 QUESTION: How about if you're not a licensed  
15 agent?

16 MR. PHILLIPS: That would be a violation of the  
17 state law.

18 QUESTION: And that was involved here as well,  
19 wasn't it?

20 MR. PHILLIPS: No, at the time that all the  
21 commissions were received, the individuals receiving them  
22 were licensed agents, or had a licensed agent affiliated  
23 with the company involved, or the recipient of the  
24 commission.

25 QUESTION: So, it's your position that at no

1 time was any Kentucky state law violated here by either of  
2 your clients?

3 MR. PHILLIPS: I would say two things about  
4 that, Justice O'Connor. First, that's correct. No state  
5 law was violated. Two, even if state law had been  
6 violated there was no instruction to the jury asking the  
7 jury to find that state law had been violated. So that  
8 it's not, you know, whether there was a violation of state  
9 law in this case is simply not relevant to what the jury  
10 decided.

11 As I was suggesting. It was not uncommon for  
12 public officials, or the relatives of public officials  
13 themselves to receive shared commissions under the  
14 patronage scheme. The Insurance Commissioner himself  
15 testified that his son was receiving insurance commissions  
16 as a part of this practice. He knew about it and never  
17 doubted that it was a lawful practice.

18 In this case the government has however,  
19 challenged Mr. Hunt's recommendation to the Insurance  
20 Commissioner to appoint the Wombwell Insurance Agency as  
21 the agent of the state for Worker's Compensation and his  
22 directions as to how to share those commissions.

23 Because the government in its brief, in this  
24 Court on the merits, has for the first time suggested that  
25 this case is not really an intangible rights case, I think

1 that it is terribly important that the court understand  
2 clearly, precisely how the case was submitted to the jury.

3 The government has reproduced the relevant  
4 instructions in its brief at pages nine to ten and  
5 footnote eight. In reading them as a whole, I submit,  
6 reveals quite clearly that the District Court told the  
7 jury, at the government's request that it could conclude  
8 that petitioners "devised such a scheme," describing the  
9 scheme in the indictment as read in relevant portion to  
10 the jury, if the jury found five facts basically.

11 One, that there was control over the naming of  
12 an insurance agency by Mr. Hunt. Two, that Mr. Hunt had  
13 something to do with the selection of Wombwell. Three,  
14 that he directed Wombwell to share those commissions in a  
15 particular way, or that he held an ownership interest in  
16 Seton Investments. And five, that he failed to disclose  
17 that interest to the state government.

18 With respect to the petitioners then, they are  
19 charged solely with aiding and abetting that basic claim.  
20 Our position is that however you analyze those facts as  
21 required to be found by the jury, there is no fraud in  
22 this case. And that the jury was clearly instructed that  
23 it could find on that theory as an alternative basis for  
24 holding that the Mail Fraud Statute has been violated and  
25 that the jury, and therefore the government must justify



1 its extension of the Mail Fraud Statute to the situation  
2 involving Hunt.

3 QUESTION: Well, Mr. Phillips, I thought the  
4 government is now telling us that the jury was instructed  
5 that for mail fraud, the government had to prove a scheme  
6 to defraud the citizens of their right to honest  
7 performance of public business and to obtain money or  
8 property by false pretenses. And that the jury clearly  
9 had to find both present.

10 MR. PHILLIPS: Well, the first part, the  
11 government is clearly, I mean, the government is clearly  
12 making that argument and there is a statement in re-  
13 reading --

14 QUESTION: And there is such an instruction?

15 MR. PHILLIPS: Well, the indictment was read to  
16 the jury and that is in the indictment. But if you read  
17 the paragraphs before the indictment and the paragraphs  
18 after the indictment, the reliance on obtaining money or  
19 property by false pretenses is irrelevant. It is a scheme  
20 to defraud as described at the beginning.

21 QUESTION: So you think, the position you take  
22 is that the instructions as a whole do not bear out that  
23 argument.

24 MR. PHILLIPS: Absolutely. Absolutely.  
25 Couldn't say it better myself. Because the government in

1 it's brief on the merits in this Court has taken, excuse  
2 me, to the place the government's theory then into  
3 perspective, the Court must realize, one, the jury was not  
4 asked to find that the state of Kentucky or any of its  
5 citizens lost any money as a consequence of this scheme.

6 And two, the jury was not asked to find that  
7 Hunt, Gray, or McNally frankly received one cent from the  
8 patronage arrangement. The theory is merely one of non-  
9 disclosure.

10 QUESTION: The theory being these commissions  
11 would have been paid to somebody anyway.

12 MR. PHILLIPS: That's absolutely correct.

13 QUESTION: So --

14 MR. PHILLIPS: The commissions, the size of the  
15 commissions were outside of the state's control. That  
16 money went to Wombwell. So that the government's repeated  
17 reference to this as a matter of public funds, simply  
18 inaccurate. They were not public funds. They were  
19 Wombwell's funds and Wombwell willingly parted with them.

20 QUESTION: The theory is that so much commission  
21 was going to be paid to Wombwell, what by the company or  
22 by the Kentucky government?

23 MR. PHILLIPS: It is paid by the underwriter.

24 QUESTION: By the under --

25 MR. PHILLIPS: It's a commission paid back by

1 the underwriter. But the amount of money that Kentucky  
2 had to pay to --

3 QUESTION: When you say (inaudible).

4 MR. PHILLIPS: --have insurance was set. It  
5 couldn't be modified in any way.

6 QUESTION: When you say it's a commission paid  
7 back by the underwriter, who is the underwriter in this  
8 case?

9 MR. PHILLIPS: Well, there were two underwriters  
10 and they're just large insurance companies.

11 QUESTION: And they're --

12 MR. PHILLIPS: (Inaudible).

13 QUESTION: It's basically a discount?

14 MR. PHILLIPS: No, it's just the method of  
15 recompense for the activities of the agent and so --

16 QUESTION: So they're paying the agent for  
17 having gotten the business?

18 MR. PHILLIPS: Right.

19 QUESTION: The way other insurance commissioners  
20 would.

21 MR. PHILLIPS: Absolutely.

22 QUESTION: And they were going to pay a  
23 specified amount to Wombwell and these people's theory is  
24 if Wombwell wanted to split it up with other people that  
25 was a private arrangement.

1 MR. PHILLIPS: That is precisely our position,  
2 Mr. Chief Justice. As far as we're concerned the term --

3 QUESTION: Although I suppose you can say if  
4 Wombwell's willing to split it with other people, Wombwell  
5 would also be willing to charge less.

6 MR. PHILLIPS: Might of been willing to charge  
7 less.

8 QUESTION: Which would mean that the state would  
9 probably be able to buy its insurance for less.

10 MR. PHILLIPS: Well, except that there's --

11 QUESTION: (Inaudible).

12 MR. PHILLIPS: -- no evidence to that effect in  
13 the record in this case. And no effort by the government  
14 to try to prove that --

15 QUESTION: Well, but that's common sense isn't  
16 it? I mean, what does Wombwell care. Wombwell's not  
17 getting the money. They would as soon give it back to the  
18 state as give it to some third party.

19 MR. PHILLIPS: Well, I mean, my guess is that  
20 Wombwell would prefer to share it with other insurance  
21 agents if for no other reason than to develop good will.

22 QUESTION: That the whole reason for the scheme?  
23 It was a patronage device wasn't it?

24 MR. PHILLIPS: Yes, it was a patronage device.  
25 It was to generate good will both with the state of



1 Kentucky and with other insurance agencies.

2 QUESTION: They weren't handing anything back to  
3 the state.

4 MR. PHILLIPS: No, no one ever suggested that  
5 anything could be granted back to the state.

6 QUESTION: That wasn't patronage to hand it back  
7 to the state.

8 MR. PHILLIPS: No, that would be sort of anti-  
9 patronage, I suppose.

10 QUESTION: Yeah. (Laughter).

11 MR. PHILLIPS: In light of the jury instructions  
12 in this case, it seems to us quite remarkable that the  
13 government has all, I think, but conceded that the Mail  
14 Fraud Statute as applied to a political party leader is  
15 wholly inapplicable. It's sole defense on this issue in  
16 the brief appears in a single paragraph on page 32.

17 And the government tells the court, quote, it is  
18 at least clear that those individuals, referring to party  
19 leaders given the power to carry on the state's business,  
20 have a duty not to use that governmental party to  
21 criminally profit themselves or their friends.

22 The problem with that statement and it's the  
23 sole defense of the government's case here, is that it  
24 again ignores the jury instructions. There was no  
25 criminal profit. There was no profit at all, in terms of

1 what the jury was asked to find.

2 The sole theory in this case involves a matter  
3 of non-disclosure. That's what the jury was instructed on  
4 and that's what the jury found. The fact the jury found  
5 that however is unfortunate for the government because  
6 this is not mail fraud. It's not fraud of any sort.

7 Because as this Court said in Schiarella, in  
8 order for there to be fraud, there must be a duty to  
9 disclose and what is utterly missing in anything, in  
10 either the government's brief or anything at the trial in  
11 this case is any indication of where a duty to disclose  
12 exists and extends to a political party leader. And  
13 because of that, the government's case necessarily fails  
14 as a matter of law.

15 Mr. Gray was a political official, but as the  
16 jury --

17 QUESTION: You mean a state official, you mean?

18 MR. PHILLIPS: Yes, he was a state official.  
19 But as the jury instruction quite clearly specifies --

20 QUESTION: He was part of the scheme?

21 MR. PHILLIPS: He was found guilty under the  
22 government's theory of aiding and abetting Hunt. But, not  
23 as a government official. There's nothing in the  
24 instruction with respect to aiding and abetting that  
25 required Mr. Gray to be a government official. And in the

1 closing arguments --

2 QUESTION: Did he have any duty to disclose?

3 MR. PHILLIPS: I don't believe he would of had a  
4 duty to disclose, although the jury wasn't required to  
5 find that he would.

6 QUESTION: But, he was a state official.

7 MR. PHILLIPS: He was a state official.

8 QUESTION: He certainly is in a different  
9 position than Hunt.

10 MR. PHILLIPS: He would be in a different  
11 position and this case would be somewhat different if the  
12 jury had been instructed only that it had to find the Mr.  
13 Gray had violated his duties. But that was not the way  
14 the jury was instructed. The jury was instructed --

15 QUESTION: Did Mr. Gray get any money?

16 MR. PHILLIPS: I'm sorry?

17 QUESTION: Did Mr. Gray get any money?

18 MR. PHILLIPS: No, Mr. Gray did not receive any  
19 money.

20 QUESTION: He didn't get any benefit?

21 MR. PHILLIPS: The government attempted to prove  
22 that he may of gained some benefit, but the jury was not  
23 asked to make any findings as to whether he had gained any  
24 benefit. And there is clearly no evidence as to receipt  
25 of any money. Whether he gained a benefit is unclear but

1       --

2               QUESTION: You answered while ago that this  
3 scheme didn't involve any violation of state law. I take  
4 it means that Mr. Gray didn't violate state law either?

5               MR. PHILLIPS: I don't believe that Mr. Gray  
6 violated any state law as a consequence of his conduct.

7               QUESTION: Even if he did in fact receive  
8 benefits in the form of condominium usage and vehicle  
9 usage and so forth and so on in Florida and elsewhere?

10              MR. PHILLIPS: Well, I'm not frankly completely  
11 familiar with bribery laws in the state of Kentucky, but  
12 my sense is that those benefits are so far removed from  
13 any public actions that Mr. Gray would have undertaken  
14 that I doubt seriously there would have been a violation  
15 of state law.

16              QUESTION: Well, he was the insurance  
17 commissioner, wasn't he?

18              MR. PHILLIPS: No, no. He wasn't the insurance  
19 commissioner.

20              QUESTION: (Inaudible).

21              MR. PHILLIPS: He was the Secretary of the  
22 Cabinet.

23              QUESTION: Yeah, that's right. And why did Mr.  
24 Hunt want him in the scheme?

25              MR. PHILLIPS: Well, I hesitate to speak on it,



1 for Mr. Hunt, but I think the answer is they were friends  
2 and I don't think it is a scheme, frankly. They were  
3 friends and they happened to have an inter-relationship.

4 But I don't know that from our perspective and  
5 given that the jury wasn't required to make any findings,  
6 I hesitate to say that he was involved in that particular  
7 scheme.

8 But I think the important point to remember,  
9 Justice White, is that the jury was instructed on that  
10 point in the alternative and therefore, whether or not,  
11 and I don't think the Gray theory would hold water either,  
12 but whether or not it would is irrelevant to this case.

13 The government still has to demonstrate that Mr.  
14 Hunt violated the law in the ways that he did and that the  
15 petitioners aided and abetted that violation.

16 QUESTION: Who again was Mr. Hunt?

17 MR. PHILLIPS: Mr. Hunt was the head of the  
18 Democratic Party. He was the Executive Chairman of the  
19 Democratic Party of the state of Kentucky. Never held  
20 public office within the state of Kentucky.

21 QUESTION: But, he was empowered by the governor  
22 to direct the receipt of these insurance commissions?

23 MR. PHILLIPS: He was placed in charge of basic  
24 patronage recommendations.

25 QUESTION: He was given some kind of defacto

1 duty to perform on behalf of the state.

2 MR. PHILLIPS: Well, the jury instruction didn't  
3 ask for that. All the jury was asked to find was that he  
4 had control over those decisions and so, and the evidence  
5 was that he made recommendations and those recommendations  
6 were followed.

7 To say that he had defacto control in that sense  
8 strikes me as not any different than any other party  
9 leader making recommendations to his own party leaders who  
10 happened to hold public offices. So, in a sense sure, he  
11 had defacto control, but our position is that jury  
12 instruction is so far removed from anything that would  
13 make him a public official, that there is simply no basis  
14 for creating a duty, certainly if the government has cited  
15 nothing --

16 QUESTION: Mr. --

17 MR. PHILLIPS: -- on the basis for creating that  
18 duty. And that is a federally created duty. It does not  
19 exist in state law. And, --

20 QUESTION: Mr. Phillips, may I just be sure I  
21 understand something? Is it your position on this the  
22 fact there are no pecuniary benefit and nothing but a  
23 violation of an alleged duty to disclose, which you deny  
24 existed? Would you say the case would be different if he  
25 were a state official? If Mr. Hunt were a state official?

1 MR. PHILLIPS: Well, on that issue, just on that  
2 one issue as to whether they're might be a state law duty  
3 to disclose the issue would be different. On the issue of  
4 whether or not there's any pecuniary gain, and whether  
5 pecuniary gain is a necessary requirement of the Mail  
6 Fraud Statute, I'd say that's a separate and open issue.

7 I think we would also have made some additional  
8 arguments if this case turned on Mr. Gray's status in  
9 terms of when does a duty trigger. It is one thing to say  
10 that public officials have some duties to disclose, but it  
11 doesn't seem to me that every, that you know, in this case  
12 the government says, Mr. Gray had a duty to disclose  
13 basically because he saw some wrong doing  
14 going on. Not that he necessarily benefitted from it.

15 So, it's not at all clear to me that he would of  
16 had a duty to disclose in this case. But again, we run  
17 far afield from anything the jury was asked to decide in  
18 this particular case.

19 QUESTION: Mr. Phillips, I don't think our cases  
20 are at common law that it was ever an element of fraud  
21 that you had to prove pecuniary gain to the defendant.

22 MR. PHILLIPS: This Court's decisions in both  
23 Fasulo and Hammerschmidt state that what is involved with  
24 respect to fraud is injury and injury defined in terms of  
25 property.

1 QUESTION: Maybe economic injury to the victim,  
2 but never a requirement of gain to the perpetrator.

3 MR. PHILLIPS: Okay. Oh no, that's correct.  
4 That's correct.

5 QUESTION: And that's what you keep arguing --

6 MR. PHILLIPS: Well, --

7 QUESTION: -- is missing. And I just don't see  
8 that as an element at all.

9 MR. PHILLIPS: No, Justice O'Connor, I don't  
10 mean to imply that. Throughout our brief we argue that  
11 what's missing here is any injury, any economic injury to  
12 the victim of a fraud, which is the state of Kentucky, and  
13 what is also missing is any pecuniary gain to the  
14 defendants. But that was only in response to Justice  
15 Stevens' question.

16 QUESTION: That just isn't an element. Yeah.

17 MR. PHILLIPS: You know, our position remains  
18 that injury to money or property is a condition required  
19 for mail fraud.

20 QUESTION: Well, there's been a lot of cases  
21 haven't there in which that has not been required under  
22 this Mail Fraud Statute. You're looking at a number of  
23 public officials in other states who have been convicted  
24 by the use of this statute.

25 MR. PHILLIPS: Well, no decisions --



1 QUESTION: Without proof of some kind of, much  
2 more than an intangible right kind of an argument.

3 MR. PHILLIPS: Well, none of those decisions  
4 were by this Court and the government freely concedes that  
5 this Court has never decided the validity of the  
6 intangible rights theory. And as we indicate --

7 QUESTION: But your position is squarely  
8 inconsistent with the Kerner case, or Isaacs case rather,  
9 isn't it?

10 MR. PHILLIPS: I'm sorry? Justice Stevens, I'm

11 --

12 QUESTION: I know it's not been decided by this  
13 Court, but the decision Governor Kerner's case, you would  
14 require that one, your position is inconsistent with the  
15 holding in that case.

16 MR. PHILLIPS: Well, I think the evidence is  
17 slightly different in that case because there really was  
18 bribery and --

19 QUESTION: But no injury to the --

20 MR. PHILLIPS: -- and closeness, the nexus in  
21 terms of the duty and the creation of duty --

22 QUESTION: I don't think there was any injury,  
23 any pecuniary injury to the state of Illinois.

24 MR. PHILLIPS: No, on that issue it's the same.

25 QUESTION: It's the same.

1 MR. PHILLIPS: But, --

2 QUESTION: But, then where did the duty to  
3 disclose come from there? Cause the status of a public  
4 official, wasn't it?

5 MR. PHILLIPS: Well, there was more to Kerner  
6 actually than simply a duty to disclose. There were  
7 intangible rights underlying it and that's certainly a  
8 part of that case. There was also, you know, a certain  
9 amount of --

10 QUESTION: In other accounts, but just on the  
11 mail fraud is all I'm talking --

12 MR. PHILLIPS: Just on the mail fraud. But, you  
13 know, as we suggested in our reply brief, that wasn't all  
14 he was convicted of. So that even if the Court had taken  
15 up the mail fraud issue, would not have required reversal  
16 of all the convictions against him.

17 QUESTION: I understand.

18 MR. PHILLIPS: Which I think --

19 QUESTION: Well, you say that case is the same  
20 as this only insofar as your broader argument is  
21 concerned. That is your attack on the intangible rights  
22 theory.

23 MR. PHILLIPS: Right. Yes, I understood that to  
24 be Justice Stevens point.

25 QUESTION: But, even we reject that argument,

1 you would still say that Kerner was a public official --

2 MR. PHILLIPS: Sure, he was clearly a public  
3 official. Nobody disputes that. And, none of the  
4 petitioners are, I mean, Hunt does not.

5 In sum, the government today asks this Court to  
6 sign what is basically a prosecutorial blank check to rid  
7 the mails of any political act that a United States  
8 attorney finds unacceptable. What makes this request most  
9 dangerous we think, is the fact that even an indictment in  
10 the context of political officials or public, or it's  
11 going to be party leaders, can be devastating to their  
12 public careers.

13 And thus, the government is asking this Court  
14 not only to sign a blank check, but a check that is of  
15 enormous consequence. This Court cannot sign that check.  
16 Only Congress can because only Congress can declare  
17 conduct to be illegal. And Congress has not declared  
18 anything that the petitioners have done in this case, as  
19 presented to the jury, to be against the law. Now, what  
20 the government --

21 QUESTION: (Inaudible) the two parties here are  
22 McNally and Gray?

23 MR. PHILLIPS: The petitioners are McNally and  
24 Gray, yes, Justice White.

25 QUESTION: And what was Gray's offense?

1 MR. PHILLIPS: Gray's offense, under the  
2 instructions to the jury was aiding and abetting Hunt.

3 QUESTION: And he wasn't charged as a principal?

4 MR. PHILLIPS: He was charged in the alternative  
5 as a principal. The instruction is quite clear at  
6 footnote A, the District Court's instruction to the jury  
7 says, in order to find this scheme, you must find one of  
8 the following: Either that Hunt engaged in certain  
9 activities and was aided and abetted by the two  
10 petitioners, or that Mr. Gray engaged in certain  
11 activities and was aided and abetted by petitioner  
12 McNally. It is clearly in the alternative and therefore,  
13 the government is obliged to justify both of those  
14 theories.

15 With respect, unless there are further questions  
16 on the mail fraud count, with respect to the conspiracy  
17 issue and the failure of the Court of Appeals to consider  
18 petitioner's contention that the government failed to  
19 prove the tax object of the conspiracy, we explained in  
20 both our opening brief and our reply brief, why the  
21 government's request for a rule of per se harmless error  
22 seems to us unwarranted.

23 In light of the government's concession;  
24 however, that if it loses on the mail fraud issue that the  
25 conspiracy count must necessarily be reversed. I would



1 rest on the briefs unless the Court has questions and  
2 reserve the balance of my time.

3 QUESTION: Thank you, Mr. Phillips. We'll hear  
4 now from you Mr. Ayer.

5 ORAL ARGUMENT OF

6 DONALD B. AYER

7 ON BEHALF OF RESPONDENT

8 MR. AYER: Mr. Chief Justice, and may it please  
9 the Court:

10 The government agrees, I think, with one general  
11 proposition that is made by the petitioners in this case.  
12 And that's the point that there is a substantial amount of  
13 confusion concerning this intangible rights mail fraud  
14 theory.

15 And we would further agree that there is in some  
16 opinions of various courts of appeals, what I would  
17 describe as extravagant language, talking in terms of  
18 standards of moral uprightness, fundamental honesty, fair  
19 play and right dealing. But that's, I think, where our  
20 agreement ends because first of all, in terms of this  
21 case, which is before this Court, that language I think is  
22 completely irrelevant.

23 Also, as to the very cases in which that  
24 language appears, I think one is hard-pressed to find even  
25 one where the language itself is necessary to the holding

1 of the case and indeed where the outcome, the decision and  
2 indeed the reasoning, if you read the opinion further,  
3 isn't well supported on a much sounder and narrower theory  
4 of the Mail Fraud Statute.

5 But before we get to that question of intangible  
6 rights, I want to address the first proposition made in  
7 our brief, which is the point that this intangible rights  
8 theory need not and indeed I think, should not be  
9 addressed in order to resolve this case.

10 QUESTION: Why didn't you tell us that when we  
11 were entertaining petition for cert?

12 QUESTION: Yeah.

13 MR. AYER: If we had known it, we would have  
14 told you.

15 QUESTION: (Laughter). You mean have thought  
16 of? it?

17 MR. AYER: Well, yes. (Laughter). If we had  
18 focused on the jury instructions at the time that we filed  
19 our opposition, which we filed I think, 700 or so up for a  
20 year.

21 Indeed it would have been much better had we  
22 done that for all of us, I guess, but we didn't and thus  
23 we didn't make the point. But having discovered it when  
24 we discovered it we felt like it was only right to bring  
25 it up as soon as we figured it out.

1 QUESTION: Surely would have been better for us  
2 and maybe better for you.

3 MR. AYER: Well, we'll find out I guess.  
4 (Laughter). The reason why, I think that the issue was  
5 not presented comes from a simple reading of the  
6 instructions. I wouldn't represent that the instructions  
7 themselves are simple --

8 QUESTION: What page and what document?

9 MR. AYER: The government's brief at page 11  
10 indicates in footnote eight. What must be proved beyond a  
11 reasonable doubt is that the defendant's knowingly and  
12 willfully devised, or intended to devise a scheme to  
13 defraud as described in instruction 11. I don't know why  
14 the reference to instruction 11 because the precise  
15 language of instruction 11 appears in this instruction 15.

16 But, in any event, repeated twice is the  
17 description of the scheme. Repeated in instruction 11 and  
18 in instruction 15. If you look at page nine at the  
19 beginning of footnote eight back where it first indents,  
20 is the reference to the scheme to defraud the citizens of  
21 their right to have the business and it's affairs  
22 conducted honestly, etc.

23 And then immediately following, the same scheme  
24 to obtain directly and indirectly money and other things  
25 of value by means of false and fraudulent pretenses,

1 representations and promises and the concealment of facts.  
2 There is no instruction as is typical in situations where  
3 you have multiple ways of violating a particular statute.

4 There is no instruction that says the jury must  
5 agree unanimously. I have at least one of these ways of  
6 violating the statute.

7 QUESTION: But, Mr., that instruction does  
8 charge that, devised a scheme or artifice to and then it's  
9 a conjunctive not a disjunctive that links one or two  
10 which suggests that the scheme or artifice embodied both  
11 (a)(1) and (2).

12 MR. AYER: That's exactly right, Your Honor.  
13 That's exactly our point is that the jury was told that  
14 they had to find a scheme to do both, or they couldn't  
15 convict and indeed they did find a scheme to do both.

16 They found a scheme to obtain property by false  
17 pretenses and having done that, and we knowing that they  
18 have done that there is no occasion to go further and ask  
19 whether the theory and the evidence would support the  
20 other theory as well.

21 QUESTION: (Inaudible).

22 MR. AYER: I think, if both --

23 QUESTION: I mean, the Court shouldn't have said  
24 you had to find both. Under your theory it would be a  
25 scheme to defraud if they just found number two.



1 MR. AYER: That's correct. And I must say when  
2 I first --

3 QUESTION: So, the and is really not right.  
4 Take advantage of it, so it's exactly right.

5 MR. AYER: Exactly right. Yeah.

6 MR. AYER: We will take advantage of it and I  
7 think it is in fact, clearly what the jury was told to do  
8 and it's got to be what the jury (inaudible).

9 QUESTION: It certainly isn't clearly because  
10 the court then goes on to say to find that the defendants,  
11 or either of them, devise such a scheme, referring back to  
12 the beginning of the preceding paragraph. A scheme or  
13 artifice too. One and two, which you just quoted. To  
14 find that either of them devise such a scheme you must  
15 find beyond a reasonable doubt one of the following, and  
16 then it has one or two.

17 MR. AYER: Right. And the one or two, those are  
18 references to the roles played by Hunt and Gray. In each  
19 of those paragraphs, you find discussion of the channeling  
20 of commissions. That is the appropriation, the obtaining  
21 of property.

22 QUESTION: (Inaudible) one of those, you proved  
23 the scheme described above.

24 MR. AYER: That's correct and that language plus  
25 the additional language that says you must find beyond a

1 reasonable doubt that they knowingly devised the scheme  
2 above. (Inaudible).

3 QUESTION: Well, now, wait a minute. How do  
4 you find any obtaining of property in Number two? Where  
5 is the, or, you know --

6 MR. AYER: Yeah, I do. It was a matter under  
7 the supervisory authority of the Defendant Gray, a  
8 secretary of public protection of regulation or secretary  
9 of the governor's cabinet at the time that Seton  
10 Investment Inc. received commissions from that insurance  
11 policy. And then they talk about the ownership interest  
12 that Gray had. So, there must have been a receiving of  
13 commissions by Seton.

14 QUESTION: Yes, but you're still left with  
15 whatever defect in hears in that number two. And that, --

16 MR. AYER: Well, I will address that now, Your  
17 Honor, as you brought it up. That the first, that is  
18 paragraph one requires in order to convict Mr. Gray that  
19 he had aided and abetted Mr. Hunt. Mr. Gray was at all  
20 times relevant either or both the Secretary to the  
21 Cabinet, or the Secretary of Public Protection in  
22 Regulation.

23 And in both of those positions, in the second  
24 position of protection and regulation, he directly oversaw  
25 the entire state insurance program. And as Secretary to

1 the Cabinet, he was one step and oversaw among others the  
2 Secretary of Regulation.

3 Our theory is that in order to have found one,  
4 in order to have convicted under one, and who to have  
5 convicted Gray as the jury did, they must have found that  
6 Gray aided and abetted Hunt.

7 And for Gray in his public position to have been  
8 essentially turn, at least turning his head to the  
9 diversion of this money in ways which in a minute I will  
10 show to have been quite improper. That in itself  
11 constitutes the breach of a public duty. That is his duty  
12 as a public official.

13 QUESTION: Oh yes, but not under one. Because  
14 under one he's charged as an aider and abetter and for  
15 that to be wrong, the principal, namely Hunt, has to be  
16 doing something wrong. I don't think you can rely on  
17 Gray's capacity as a public official to satisfy the  
18 paragraph one.

19 MR. AYER: Well, we think we can, Your Honor.  
20 And the reason we do is that there is no dispute as to his  
21 occupying a public position at all times relevant. And  
22 the public position --

23 QUESTION: But that's not because an  
24 aider/abetter is it? I mean, as an aider and abetter, he  
25 has to be aiding Hunt to do what is charged in that

1 paragraph.

2 MR. AYER: Well, the fact that most have been  
3 found is that Gray aided and abetted the scheme that Hunt  
4 was carrying out.

5 QUESTION: Right. If it said aided or abetted,  
6 in his official capacity, yes. But it doesn't, it just  
7 says aided or abetted. He could have aided and abetted  
8 him as a private citizen.

9 MR. AYER: I think what might be helpful in  
10 answering this question in a slightly, maybe circuitous  
11 way, but nonetheless it may be useful to refer to the  
12 facts in the case and in order to that in a brief way, I  
13 have submitted through the clerk, copies of exhibits that  
14 were used at trial. And what they do, I'm not going to go  
15 through them line by line, but they were indeed used in  
16 trial to demonstrate the evidence in the case in a fairly  
17 brief and concise way.

18 Exhibits one and two are essentially flow charts  
19 of the way the money flowed from the Commonwealth of  
20 Kentucky to, in premium payments, to two different  
21 insurance companies and then the Commission's coming back  
22 from the carriers to the Wombwell Agency.

23 The Wombwell agency being the broker who got the  
24 business and agreed to handle this Workman's Compensation  
25 business for \$50,000 a year and then at Hunt's request



1 agreed, take that \$50,000 and I, Hunt, as head of the  
2 Democratic Party will tell you where to send the rest of  
3 the commissions that you get back.

4 The key part of these diagrams. Number one  
5 covers the period of 1976, I guess '76 through the middle  
6 of '77 and then other one covers the period '77 through  
7 '79. Is what happens with the money, the premium, I'm  
8 sorry the commission payments once hey come back to the  
9 Wombwell Agency and what these, the little boxes over on  
10 the right hand side show, are the channeling of the checks  
11 to different places. One is to Seton Investments.

12 Now Seton Investments as we've indicated in our  
13 brief is an entity which was created by Hunt and Gray. It  
14 was set up as a real estate investment company, but in  
15 fact, transacted no real estate business except the  
16 purchase of two condominiums, which the evidence showed  
17 was for the personal use of Gray and Hunt.

18 It purported to be for purposes of this scheme  
19 because it had to be under state law an insurance  
20 brokerage entity. In fact, it transacted and the evidence  
21 showed it transacted no insurance business whatsoever. It  
22 did not have an insurance license. It put on forms which  
23 were submitted to the Wombwell agency as proof.

24 QUESTION: (Inaudible) receiving commissions.

25 MR. AYER: That was the business it was in,

1 Justice White. And that is illegal under state law. It  
2 is illegal under the provision of state law, under  
3 Kentucky revised statute 34.9-100, which we've cited in  
4 our brief, says that it is not a proper purpose of an  
5 insurance license to have it for the purpose and solely  
6 for the purpose of enabling the licensee to receive  
7 rebates or premiums.

8 QUESTION: Do you think they foresaw this  
9 situation? (Laughter).

10 MR. AYER: Well, they probably foresaw  
11 situations like it, given the existence of this kind of a  
12 patronage system in Kentucky, and given the acceptability  
13 under another provision, of splitting of commissions.  
14 They wanted to make clear that this kind of situation is  
15 not acceptable.

16 QUESTION: Still waiting to see who's been done  
17 out of money, you know?

18 MR. AYER: Well, who has been done out of money,  
19 number one, we would dispute and there is evidence I think  
20 in the record that supports the dispute that there was  
21 simply no way for Kentucky to do anything other than pay  
22 the money that it paid and to have the premiums that were  
23 paid, I'm sorry, the commissions that were paid back to  
24 Wombwell paid in a certain amount.

25 It is true that there's a regional commission

1 that is set up. I think it's basically part of the  
2 insurance industry that studies and decides what a  
3 reasonable commission is on a certain kind of policy. It  
4 is always possible to renegotiate something like that and  
5 indeed there is testimony in the record that there, that  
6 that is a possibility. It was never done here --

7 QUESTION: That certainly isn't a crime to fail  
8 to get the lowest possible price you can for the state in  
9 dealing with insurance people, or auto people, or anything  
10 else.

11 MR. AYER: That's absolutely correct, Your  
12 Honor.

13 QUESTION: (Inaudible) making this argument to  
14 show that the state of Kentucky lost some money?

15 MR. AYER: No, I am not. I'm trying to answer  
16 Justice Scalia's question as to who was done out of money.  
17 It is indeed the case that had people been public  
18 watchdogs, looking for where the money's going, it would  
19 have come out differently. That's not the point. That's  
20 not the reason why this is illegal. This is illegal, what  
21 I'd like to do is --

22 QUESTION: Here is the analogy that I'm,  
23 patronage systems were never considered illegal. I mean,  
24 that's why we had to have a law to have the civil service.  
25 And the theory was, somebody has to have the job, you're

1 going to give the job to somebody, why not give it to our  
2 guys? That was never thought unlawful, or it certainly  
3 wasn't considered fraud.

4 Now it seems to me, you would have to persuade  
5 me that this is something any different from that to  
6 convince me that it's fraud. And so far, you haven't. I  
7 don't see how anybody has been done out of any money.  
8 Just, the money has to go to somebody. It might as well  
9 go to our guys.

10 MR. AYER: Okay.

11 QUESTION: Is that fraud?

12 QUESTION: You aren't arguing the state was done  
13 out of anything?

14 MR. AYER: No. We are not and we did not at  
15 trial.

16 QUESTION: But I take it you are arguing that  
17 simply receiving premium payments in the mail is different  
18 from getting paid for a job that you perform.

19 MR. AYER: Well, it's different. I am not sure  
20 how much we can make of that given the premise that we all  
21 start from that this patronage scheme is legal and  
22 therefore, it's perfectly legal for someone out dole out  
23 money to his friends.

24 QUESTION: I thought you were arguing that it  
25 wasn't necessary at all for Kentucky to be cheated out of



1 any money.

2 MR. AYER: That's correct.

3 QUESTION: It's just that somebody was receiving  
4 money under false pretenses and --

5 MR. AYER: That's correct.

6 QUESTION: -- by concealment and things like  
7 that, which is mail fraud.

8 MR. AYER: That's correct. What has been done  
9 here, what I'd like to do is start with the proposition  
10 that, hypothetically speaking, let's forget that these  
11 people are in fact, public officials. Let's leave that  
12 out of it.

13 As I think we have demonstrated in our brief,  
14 what was done was a, what was shown was a complete scheme  
15 for obtaining property by false pretenses. The false  
16 pretenses are the setting up a phony insurance brokerage  
17 outfit for the purpose of making it appear acceptable to  
18 channel this commission money to them.

19 Under state law it is illegal to split  
20 commissions with anyone other than an insurance broker or  
21 agency. And so what they did was to create this entity as  
22 an independent company, disassociate themselves, that is  
23 Gray and Hunt, from it by bringing in at least at a late  
24 date, McNally, to serve as its president and act like this  
25 is an independent entity that McNally is in charge of.

1 And indeed at trial the argument was that  
2 McNally owns this. This is all his, we don't own it, that  
3 is Gray and Hunt don't own it, McNally owns it. That  
4 scheme, just leaving out the element of public official  
5 and public obligation is in and of itself, that deception  
6 to allow the channeling of money to Seton, which indeed  
7 then goes essentially to the use, as is indicated on our  
8 exhibit three, to the use of these individuals in the form  
9 of condominiums. That is itself a complete mail fraud  
10 scheme. A scheme for obtaining property by false  
11 pretenses and we believe that that is the first and  
12 easiest way to resolve the case.

13 QUESTION: Doesn't the false pretense have to be  
14 a pretense to get the property? That but for that  
15 pretense, the property would not have been given?

16 MR. AYER: Well --

17 QUESTION: You don't say I defraud somebody if I  
18 go up and say, I'll buy your car for \$500 and I give him  
19 my wrong name. You wouldn't say that I defrauded him of  
20 the car so long as I give him the \$500.

21 MR. AYER: It wouldn't have been possible for,  
22 even if they weren't public officials, it wouldn't have  
23 been possible for either Gray or Hunt to walk up and say  
24 give me commissions. Even if they were politically  
25 influential because they are not insurance brokers. And

1 they do not have the requisite license to make it legal  
2 under state law to participate in this particular form of  
3 patronage.

4 QUESTION: So whoever would have gotten the  
5 insurance commissions were done out of them? I mean,  
6 because these two people got them and they weren't  
7 entitled to them, whoever was paying it to them would have  
8 kept them.

9 MR. AYER: I think, well the whole idea was to  
10 take this pot full of money which amounted \$850,000 over  
11 four years and spread it around.

12 QUESTION: Someone else would have kept the  
13 money. Someone else would have got the money (inaudible).

14 MR. AYER: Someone else would have gotten it,  
15 but I don't think it would have been somebody who could of  
16 claimed he had a right to it.

17 QUESTION: Who would the somebody else be?

18 MR. AYER: Someone else would in all likelihood  
19 of been, some other insurance brokerage, I should say some  
20 insurance brokerage outfit in the state of Kentucky who  
21 had been supportive of the governor and the  
22 administration.

23 QUESTION: And so that's the person who is  
24 economically injured? Someone else who is waiting in line  
25 and didn't get there in time. (Laughter).

1 MR. AYER: Well, our theory is that, well, I  
2 don't think it's just our theory. It's very clear as to  
3 this first cut, leaving out the public official and the  
4 public intangible right element.

5 It's very clear that what was proven on this  
6 first level was a scheme to obtain property by false  
7 pretenses. The false pretenses being the creation of this  
8 Seton outfit which is phony. Never does any business and  
9 just is there to receive money and channel it to Gray and  
10 Hunt. That, in and of itself, the obtaining of that  
11 property, forgetting about who is hurt, there is no  
12 requirement in the law that someone be harmed as a result  
13 --

14 QUESTION: Well, you said, Justice O'Connor made  
15 the point a while ago that fraud doesn't ordinarily  
16 require that the defendant may have gained, but I had  
17 thought at least fraud required that there had been some  
18 economic injury to someone.

19 MR. AYER: Well, the --

20 QUESTION: You say, not only need their be no  
21 gain, but there not need be any harm.

22 MR. AYER: I think that's correct, Your Honor.  
23 And I think that is emphatically clear --

24 QUESTION: Why is it prohibited? (Laughter).

25 MR. AYER: Well, I think it's emphatically clear



1 on the face of the statute that that is true. Because the  
2 statute has three different clauses. The first one is for  
3 creating, or putting into effect a scheme to defraud, or  
4 for obtaining money or property by false pretenses. That  
5 is exactly what was done here, was the obtaining of money  
6 or --

7 QUESTION: (Inaudible) right it. It really does  
8 you're telling, cover the case where I go up and buy a car  
9 for \$500, give my wrong name.

10 MR. AYER: No, I don't think so, because I think  
11 you're giving your wrong name is no part of inducing the  
12 obtaining of money or property. He wasn't relying on the  
13 fact that you gave a wrong name.

14 Whereas here, they very much are relying on the  
15 fact that Seton is supposed to be, and indeed to  
16 illustrate that, the Wombwell Agency, Mr. Tabeling  
17 specifically asked more than once for assurance that Seton  
18 was in fact, a legitimate insurance agency. And so what  
19 he was given --

20 QUESTION: Right.

21 MR. AYER: -- was the insurance license number  
22 of --

23 QUESTION: I have to add a fact then.

24 MR. AYER: Okay.

25 QUESTION: This automobile dealer does not sell

1 cars to government employees. And I walk up and I say,  
2 you know, my name Jones and I am not a government  
3 employee. He sells me a car for \$500. I have defrauded  
4 him.

5 MR. AYER: Well, I think that as a technical  
6 matter you may well have. If it is material and if you  
7 have a duty not to lie to him, which I think is fair to  
8 say you do.

9 QUESTION: If that were the only permissible  
10 interpretation of a federal criminal statute, I would  
11 think a court would be fairly loathe to reach that.

12 MR. AYER: Well, what we would suggest as a  
13 description of what must be shown, as a set of  
14 requirements under this intangible, first of all, let me  
15 say, I think it makes very little sense to conclude that  
16 somehow the mail fraud statute doesn't cover schemes to  
17 defraud of intangible rights.

18 If you define an intangible right as any right  
19 other than the physical possession of something. You talk  
20 about a right to a stream of income under a contract. Or,  
21 you talk about a right to purchase a piece of property.

22 You talk about almost any right in our society.  
23 Very few people walk around with gold bars in their  
24 pocket. Most people rely on intangible rights. And so,  
25 as an opening proposition, we've got to be all assuming

1 that the Mail Fraud Statute can reach some --

2 QUESTION: (Inaudible) intangible property.

3 MR. AYER: Intangible property.

4 QUESTION: That's a good old concept, intangible  
5 property. It's a little different from intangible rights  
6 in that it doesn't include the right to good government,  
7 for example.

8 MR. AYER: Well, I'm not sure I know where it  
9 begins and ends. If I have expectations that have value,  
10 is that intangible property?

11 QUESTION: (Inaudible) same category. As  
12 traditional a category as rights in stock and so forth  
13 which are intangibles.

14 MR. AYER: Do I think what is?

15 QUESTION: The right to good government is --

16 MR. AYER: Well, I think --

17 QUESTION: -- an intangible right of which one  
18 can be defrauded.

19 MR. AYER: I think in the following, when you  
20 meet the following set of requirements the answer would be  
21 yes. And this is what we would be suggesting as a  
22 substitute for what I referred to earlier as the  
23 extravagant language of some opinions.

24 Number one, that there must be the duty that  
25 you're talking about has got to be an enforceable duty of

1 some kind. The thing you're being defrauded out of is not  
2 just a moral aspiration. It's got to be a real duty. It  
3 can arise from the criminal law. It can arise from the  
4 civil law. It can rise from a statute, or the common law.  
5 And we would suggest it can arise from contract.

6 QUESTION: You don't even need standing to be  
7 able to enforce that, do you.

8 MR. AYER: No, (inaudible).

9 QUESTION: I assume I have no right to sue for  
10 good government, right? It's a right I have, but it's not  
11 a right I'm able to sue for.

12 MR. AYER: Well, I think that's correct. I  
13 think the state in dealing with --

14 QUESTION: But I can sue somebody for defrauding  
15 me of it?

16 MR. AYER: Well, I think the state can sue, or  
17 can bring a criminal action for defrauding yet of the  
18 right to honest services of its employees. Or the honest  
19 services of people who have been given trusted, trusted  
20 with responsibilities. But, that's only the first part.  
21 That's the first step.

22 The second step is that there must be a causal  
23 relationship between the breach of that duty and either  
24 the appropriation or the deprivation of a thing of value.  
25 We are not suggesting that simply the abstract non-



1 performance of a duty is a sufficient basis to bring a  
2 criminal action.

3 We think that it is quite appropriate to require  
4 that the breach of the duty have some kind of a  
5 consequence and in this case the consequence, well let me  
6 skip over this case for a minute.

7 The third element would be an element of  
8 deception. Which is a traditional element of the Mail  
9 Fraud Statute. That there must be some effort to cover up  
10 the scheme to deceive, to essentially hide what's going  
11 on.

12 And when you put those three things together, I  
13 would submit what you have is really only another way of  
14 saying what is going on in a more traditional property  
15 oriented mail fraud case.

16 QUESTION: Do you think these instructions  
17 covered those elements insofar as this theory of  
18 deprivation is concerned.

19 MR. AYER: I don't see anything in the  
20 instructions that suggest that these people had any duty  
21 to, unless you say that the Court must of thought there  
22 was a duty or they wouldn't have given this kind of an  
23 instruction about disclosure.

24 <sup>Ayer</sup>  
~~QUESTION:~~ We, just to repeat briefly, we think  
25 first that the case should be resolved as one for

1 obtaining property (inaudible) pretenses.

2 QUESTION: Yes, I understand that. I  
3 understand.

4 MR. AYER: Leaving that aside I think the  
5 instructions in their references to the directing of  
6 commissions and to the --

7 QUESTION: Without disclosing?

8 MR. AYER: Right. And to the positions, there's  
9 two different things we have to talk about. One is the  
10 position of Gray and whether his position and the duties  
11 that he owed were sufficient. And we think that that can  
12 be a basis for deciding the case under either (inaudible).

13 QUESTION: Wouldn't that be a jury question,  
14 whether they had the duty, or not? Or was that legal,  
15 some instruction the court ought to give?

16 MR. AYER: Well, I think that --

17 QUESTION: Because I don't see anything about a  
18 duty to disclose. As far as these instructions are  
19 concerned, it wouldn't make any difference whether there  
20 was a duty to disclose, or not.

21 MR. AYER: What, the discussion --

22 QUESTION: There was a failure to disclose.

23 MR. AYER: The discussion that does exist is the  
24 discussion of Gray's position as Secretary and the  
25 positions that he held.

1 QUESTION: Yes. Yes, but it doesn't say that he  
2 had a duty, or it doesn't ask the jury to find it. If he  
3 didn't disclose it that was all the jury was interested  
4 in.

5 MR. AYER: Well, I think there's two different  
6 things going on here. One is the duty to disclose. And  
7 we would not put primary emphasis on that. What I would  
8 suggest is that starting with the premise that there was  
9 an obtaining of property by false pretenses, how was it  
10 done?

11 It was done by these two individuals setting up  
12 the scheme and it happens that Hunt was imbued with  
13 official power, that is, the governor told him that he had  
14 the power to pick the insurance companies and to direct  
15 the commissions.

16 And secondly, Gray was in a position overseeing  
17 all of this and a lot of other activity. What had to  
18 happen was the, by Hunt, the misuse of his position and of  
19 his authority. He had to misuse state governmental power  
20 to direct this money to himself. That's the first thing  
21 that had to happen.

22 And, Gray had to, in his position, essentially  
23 at a minimum, look the other way and happily receive the  
24 money at the other end. And we think the use of state  
25 governmental power essentially to commit a federal mail

1 fraud and that's going back to the first step. V?

2 That is apart from their state governmental  
3 authority, they committed a mail fraud. The use of power  
4 to do that is a separate abuse of authority, that is, an  
5 abuse of the governmental authority.

6 QUESTION: (Inaudible) did say that the failure  
7 to disclose, if there was a failure to disclose it had to  
8 influence, if there had been a disclosure, the conduct of  
9 other government officials would have been different.

10 MR. AYER: I don't know if that's in here, Your  
11 Honor. I --

12 QUESTION: Well, if there had been a --

13 QUESTION: (Inaudible) and if Gray had an  
14 ownership interest, that he failed to disclose that  
15 interest to persons in state government whose actions or  
16 deliberations could have been affected by such action.

17 MR. AYER: Okay.

18 QUESTION: A jury (inaudible) find that. And so  
19 non-disclosure with that kind of a consequence.

20 QUESTION: Mr. Ayer, before you get through,  
21 you've given us the three parts of your theory and the  
22 first of which is the duty that's enforceable. What, at  
23 least with regard to Hunt, what is the duty you're talking  
24 about?

25 MR. AYER: With regard to Hunt?



1 QUESTION: Yeah.

2 MR. AYER: I think with regard to Hunt, if you  
3 have to reach that, and we submit you don't, --

4 QUESTION: That's mainly what the Court of  
5 Appeals relied on as I remember their opinion.

6 MR. AYER: Well, that's right. But, it's usual  
7 I think, not to decide cases where they are not going to  
8 affect the outcome. But the duties --

9 QUESTION: (Inaudible) you said there's  
10 sufficient evidence as to the Hunt charge, but they didn't  
11 really reach the other, so we'd have to send it back to  
12 find out.

13 MR. AYER: Right. The duty was a duty not to  
14 misuse the governmental authority which was given to him  
15 to commit what is apart from his duties as a governmental  
16 official, a criminal act. That is the scheme for  
17 obtaining property by false pretenses.

18 QUESTION: What is the criminal act, you mean as  
19 a matter of federal law?

20 MR. AYER: Yes. He --

21 QUESTION: Well, this kind of (inaudible).

22 MR. AYER: That the whole, as I indicated  
23 before, the whole scheme --

24 QUESTION: The duty is a duty not to violate the  
25 Mail Fraud Statute.

1 MR. AYER: That's right. That he as a --

2 QUESTION: If you prove a violation of the Mail  
3 Fraud Statute by proving you violated the (inaudible).

4 MR. AYER: Well --

5 QUESTION: I have difficulty following that.

6 MR. AYER: Okay. Well, what we tried to show is  
7 that the initial, the scheme to obtain property by using  
8 Seton, a phony shell company as a recipient for money.

9 QUESTION: Of course, the jury was not required  
10 to find they were phony companies, as I read the  
11 instructions. They were required that they had a secret  
12 interest in it, but they could have had a secret interest  
13 in a legitimate brokerage firm.

14 MR. AYER: Well, they were required to find a  
15 scheme for obtaining property by false pretenses.

16 QUESTION: All right.

17 MR. AYER: There's got to be some false  
18 pretenses. If there's no false pretenses then (inaudible)  
19 --

20 QUESTION: The false pretenses are not  
21 disclosing the ownership interest. That's what the  
22 instruction says.

23 MR. AYER: Well they certainly could also be  
24 the, and the bulk of the evidence in the case certainly  
25 dealt with the channeling of money to Seton.

1 QUESTION: Right.

2 MR. AYER: That's what the case was about.

3 That's what the time in court was spent on was showing  
4 this money, check after check after check going to Seton.

5 QUESTION: I understand, but you argued at some  
6 length the fact that Seton was a sort of a shell.

7 MR. AYER: Right.

8 QUESTION: But the jury wasn't instructed to  
9 find that.

10 MR. AYER: I don't believe that there's anything  
11 in the jury instructions that says the jury had to find  
12 specifically that Seton was a shell. They had to find a  
13 scheme to defraud by obtaining property.

14 QUESTION: So, then don't we have to assume the  
15 case would be the same for legal purposes even if Seton  
16 were not a shell? Cause we don't know the jury thought it  
17 was. But there still, you're not necessarily out of,  
18 totally lost because you still then would claim the  
19 failure to disclose the ownership interest, I guess, is  
20 enough. Maybe you don't want to go that far.

21 QUESTION: But then we're back to my just giving  
22 the wrong name. And not even saying that I'm not a  
23 government employee.

24 MR. AYER: Well, I think what is critical is  
25 that there be a linkage between the duty that's breached,

1 which we are arguing is --

2 QUESTION: But you're not saying that's the duty  
3 to disclose. That's what I'm trying to find out for --

4 MR. AYER: Well, I --

5 QUESTION: The duty to this breach is the duty  
6 not to violate the Mail Fraud Statute.

7 MR. AYER: I think there is a duty to disclose.  
8 The only reason I am hesitant to rely primarily on that is  
9 that I frankly think the basic scheme to defraud, that is  
10 to get the money, by using Seton is a more persuasive  
11 fraud.

12 There is indeed a duty, on the part of a public  
13 official to disclose and I think, I would argue if we had  
14 say it to get, you know, to resolve the case which I think  
15 we don't for at least two other reasons. That there's a  
16 duty on the part of Hunt to disclose based on his use of  
17 governmental authority. I see my time is expired. Thank  
18 you.

19 QUESTION: Thank you, Mr. Ayer. Mr. Phillips,  
20 you have eight minutes remaining.

21 REBUTTAL ARGUMENT OF

22 CARTER J. PHILLIPS

23 ON BEHALF OF PETITIONER

24 MR. PHILLIPS: Thank you Mr. Chief Justice. I  
25 would like to make simply three points. I hate to drag



1 you back into the jury instructions, but I think they're  
2 fairly important in this context.

3 The first statement that Mr. Ayer made with  
4 respect to the instruction, I think, requires some  
5 clarification was his suggestion that Mr. Gray and his  
6 aiding and abetting must have been a public official, that  
7 the jury must have found that.

8 Aside from the point that I believe Justice  
9 Stevens made, which is that there was no requirement in  
10 the jury instruction that that be found. The truth is  
11 that at the closing argument, the United States attorneys,  
12 the Assistant U.S. Attorney told the jury that the aiding  
13 and abetting was in setting up Seton.

14 And it is undisputed that when Seton was set up  
15 by Mr. Gray he was not a public official. So, it's both  
16 contrary to the instruction and contrary to the facts of  
17 the case.

18 Second, with the respect to the false pretenses,  
19 I guess I would just like to repeat what Justice Stevens  
20 said, this whole notion of a phony business and the  
21 various ways that that may have operated is an interesting  
22 theory.

23 It is not the theory that was presented to the  
24 jury in this case and I take that as the best evidence  
25 that the reference to false pretenses was not regarded as

1 somehow a separate item in this case at all, either to the  
2 court, or to the jury. And the court made it quite clear  
3 what it thought the appropriate theory for conviction was  
4 in this case.

5 And that set out in the portion that describes  
6 the scheme underwritten in the indictment. And finally,  
7 with respect to the government's eleventh hour effort to  
8 find some limiting principles for its mail fraud, I took  
9 it as quite interesting that in describing that there must  
10 first be a duty, Mr. Ayer suggests that he wouldn't put  
11 primary emphasis on that point and it's quite clear to me  
12 why he wouldn't do that in this case because wherever you  
13 look there is simply no duty.

14 And I think ultimately what it came down to was  
15 that the duty that exists in this case is a federal duty.  
16 But that's not what the Mail Fraud Statute requires. This  
17 Court made quite clear in Parr that you look to other  
18 sources to determine what is fraud, and the fraud in this  
19 case is based on a duty. You must look to those sources  
20 to find out where that duty exists. There are none  
21 accordingly and the petitioner's conviction should be  
22 reversed.

23 CHIEF JUSTICE REHNQUIST: Thank you, Mr.  
24 Phillips.

25 The case is submitted.

1 (Whereupon, at 2:50 p.m., oral argument in the  
2 above-entitled case was submitted).  
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# CERTIFICATION

Anderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

86-234 - CHARLES J. McNALLY, Petitioner V. UNITED STATES; and

86-286 - JAMES E. GRAY, Petitioner V. UNITED STATES

and that these attached pages constitutes the original transcript of the proceedings for the records of the court.

BY Paul A. Richardson

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