"Property" Fraud in the Intangible Age

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The federal mail and wire fraud statutes make it a crime to effect "any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises." 18 U.S.C. §§ 1341, 1343. The Supreme Court has long construed the word "property" to mean "something of value." *See, e.g., Kelly v. United States*, 140 S. Ct. 1565, 1573 (2020) (referring to property as a "valuable entitlement"); *Pasquantino v. United States*, 544 U.S. 349, 355 (2005) ("[The] right to uncollected excise taxes . . . is 'something of value.'"); *McNally v. United States*, 483 U.S. 350, 358 (1987) ("[T]he words 'to defraud' commonly refer 'to wronging one in his property rights . . . and 'usually signify the deprivation of something of value[.]"); *Carpenter v. United States*, 484 U.S. 19, 27 (1987) (mail fraud statute targets schemes that deprive the victim of "something of value").

These fraud statutes were written long before the age of intangibles. Exclusive control is an ingredient of value. But exclusive control of intangibles is not always clear—particularly when the intangible is a shared thing alleged to be privately held, like the pathways that connect users on the internet. As such, courts are increasingly facing the first impression task of applying the property prong of old fraud statutes to a new age concept. This article aims to help counsel better understand how this disconnect can raise a potential defense for their clients.

The Evolution of the Federal Fraud Statutes

The outer boundaries of the term "property" have expanded and contracted since the wire fraud statute's enactment in 1952. In the early 1980s, prosecutors used the federal mail and wire fraud statutes to attack various forms of corruption that deprived victims of "intangible rights"—like the electoral body's right to a fair election and a client's right to his attorney's loyalty—that are seemingly unrelated to "property." In 1987, the Supreme Court "stopped the development of the intangible-rights doctrine in its tracks," holding in *McNally v. United States* that the mail fraud statute did not reach the intangible right to "good government." *Skilling v. United States*, 561 U.S. 358, 401-402 (2010) (citing *McNally v. United States*, 483 U.S. 350, 356 (1987)). In response to *McNally*, Congress passed the honest services fraud statute, which expressly states that the phrase "scheme or artifice to defraud" includes a scheme to deprive another of the intangible right to honest services, but did not disturb *McNally*'s central holding that mail fraud requires a showing of intent to obtain "property." *See* 18 U.S.C. § 1346.

Months after *McNally*, however, in *Carpenter v. United States*, the Supreme Court clarified that the wire and mail fraud statutes *do* apply to some intangible interests. 484 U.S. 19 (1987). There, a writer for the *Wall Street Journal* (the *Journal*) leaked advance information as to the timing and contents of one of the

newspaper's columns. *See id.* at 23. The Supreme Court affirmed the conviction, explaining that the "the Journal's interest in the confidentiality of the contents and timing" of the column is a property right. 484 U.S. at 25. In so holding, the Court reasoned that confidential information, "however little susceptible of ownership or dominion . . . is stock in trade . . . to be distributed and sold to those who will pay money for it." *Id.* at 26. The Court added that the defendants had "deprived [the *Journal*] of its right to exclusive use of the information," which it deemed an "important aspect" of most private property. *Id.* at 26–27.

In *Cleveland v. United States*, the Court considered the mail fraud convictions of defendants who were alleged to have defrauded the State of Louisiana by applying for licenses to operate a video poker business under their children's names while concealing from the state the true ownership of the business. 531 U.S. 12, 16–17 (2000). The Court reversed the convictions, holding that a business license was not "property" for purposes of the mail fraud statute. *Id.* at 26–27. The Court reasoned that the licenses themselves had no "economic" value until they were issued to the applicant, and the state's right to control the issuance of its licenses "implicated [its] role as sovereign, not as property holder." *Id.* at 22–24.

Five years later, in *Pasquantino v. United States*, the Court affirmed the wire fraud convictions of defendants accused of defrauding Canada of tax revenue by smuggling liquor into the country without paying the liquor tax. 544 U.S. 349, 354–55 (2005). There, the Court held that Canada's entitlement to tax revenue did constitute "property." *Id.* at 355–56.

By contrast, in *Kelly v. United States*, the Supreme Court recently reversed wire fraud convictions of public-official defendants who ordered the realignment of highway lanes as an act of political retribution, falsely claiming that the realignment was done for the purpose of conducting a traffic study. 140 S. Ct. 1565, 1568 (2020). Relying on *Cleveland*, the Court first explained that the "intangible rights of allocation, exclusion, and control"—there, defendants' decision that certain drivers should get two fewer lanes while other drivers should get two more—did not count as property for purposes of the wire fraud statute. *Id.* at 1573. The Court further rejected the argument that employee labor used to implement the scheme was property, reasoning that the property loss must be the "object of the fraud," rather than "an incidental byproduct of the scheme." *Id.*

McNally, *Carpenter*, *Pasquantino*, *Cleveland*, and *Kelly* are examples of the Court applying the term "property" under the wire and mail fraud statutes to an intangible right, but only *Carpenter* involved the taking of arguably private "property." The others all involved an alleged fraud against a governmental body or the public at large. For this reason, some courts have observed that *Kelly* did not alter the Court's precedent regarding what constitutes property, but rather reaffirmed precedent holding that the "exercise of regulatory power" is not property. *See, e.g.*, *United States v. Khoury*, No. 20-CR-10177-DJC, 2021 WL 2784835, at *3 (D. Mass. July 2, 2021) ("*Kelly* . . . did not alter the Court's precedent regarding what constitutes property."); *see also United States v. Percoco*, 13 F.4th 158, 164 n.2 (2d Cir. 2021) ("*Kelly* is inapposite here because this case does not concern the exercise of regulatory power."); *United States v. Gatto*, 986 F.3d 104, 116 n.4 (2d Cir. 2021), *cert. denied*, No. 21-169, 2021 WL 5869415 (U.S. Dec. 13, 2021) ("Defendants did not make any regulatory decisions. . . . Thus, the Court's holding in *Kelly* that the regulatory decisions were not punishable under a property fraud theory is inapposite to the case at hand.").

Characteristics of Intangible "Property"

While *Kelly* circumscribes the reach of the federal property statutes, it raises new questions about the application of these statutes in the intangible age, particularly to what is alleged to be private property. Judges are faced with the challenge of applying fraud statutes from a pre-digital age to rapidly evolving technology, which turns the whole concept of property on its head. Post-*Kelly* decisions, which focus

on the right to control, informational rights, and the existence of a market, may serve as guideposts for judges considering whether the bundle of intangible rights imbued to technology users rank as "property" for purposes of the wire fraud statute.

"Control" of Intangibles

Although the Supreme Court has never expressly endorsed a "right to control" theory, federal prosecutors have long relied on it to argue that new types of intangibles are the object of property fraud schemes. In three recent cases, district courts opined on the adequacy of the "right to control" as a means for determining whether intangibles like university admissions slots and the right to control scholarship decisions are "property" for purposes of the federal fraud statutes, with differing outcomes.

For example, in *United States v. Gatto*, the District Court for the Southern District of New York found, post-trial, that a university's right to control scholarship decisions is a property interest protected by the wire fraud statute. 986 F.3d 104, 126 (2d Cir. 2021), *cert. denied*, No. 21-169, 2021 WL 5869415 (U.S. Dec. 13, 2021). There, the defendants paid top-tier high school basketball recruits in order to entice those players to enroll at certain universities. 2021 WL 5869415, at *111. To further the scheme, the defendants concealed these payments from the universities so that the players would still be awarded financial aid. The court found that "[t]here is no doubt that the Universities' scholarship money is a property interest with independent economic value," explaining that because there are a "finite number" of scholarships, the universities would not have awarded certain players this aid had they known that they were ineligible to compete. As a result, the court concluded that "withholding that information *is a quintessential example of depriving a victim of its right to control its assets*." *Id.* (emphasis added).

Similarly, in *United States v. Khoury*, the District Court for the District of Massachusetts applied the right to control theory, concluding that a university admissions slot constitutes property under the wire fraud statute. No. 20-CR-10177-DJC, 2021 WL 2784835 (D. Mass. July 2, 2021). *Khoury* was part of the so-called *Varsity Blues* college admissions prosecutions. There, Mr. Khoury paid $200,000 to Georgetown University's head tennis coach, Gordon Ernst, in exchange for the coach's promise to designate the defendant's daughter as a tennis team recruit, facilitating her admission to the university. *See id.* at *1–2. In denying Khoury's motion to dismiss, District Judge Casper found that admissions slots are property, explaining that they have "tangible value," in part because they are "limited and highly coveted." *Id.* at *2 (citation omitted). The court then focused on the *"longstanding property right" to control*, finding that the scheme "facilitated the withholding of valuable information" from the university—namely, the existence of the payment in exchange for designating the defendant's daughter as a recruit—which may have caused the university not to "dispense with their property" by giving up an admissions slot. *Id.* at *3 (emphasis added). As of the writing of this article, Mr. Khoury's case was still pre-trial. Either Khoury or another defendant who was convicted at trial, such as Gamal Abdelaziz or John Wilson, will no doubt raise the property issue on appeal. In both *Gatto* and *Khoury*, the courts declined to extend *Kelly*, explaining that defendants had not made any regulatory decisions in concealing the payments from the universities.

Just down the hall from Judge Casper in the Massachusetts federal courthouse, Judge Talwani was presiding over the prosecution of Mr. Ernst. In contrast to Judge Casper's ruling, in *United States v. Ernst et al.*, Judge Talwani rejected the government's same right to control theory. 502 F. Supp. 3d 637 (D. Mass. 2020). As a threshold matter, the court explained that admissions slots are not a form of property because they confer no "ownership over the universities' property rights . . . that [the admittees] may trade or sell in the open market.'" *Id.* at 650–51 (citing to *Kelly*, *Carpenter*, and *Cleveland*). Nor do "universities hold onto admission slots in order to trade or sell admission to the universities in the ordinary commercial sense of the word." *Id.* The court likewise held that the defendant had not interfered with the university's

"right to control" the use of its assets, explaining that the defendant neither deprived the university of "potentially valuable economic information" nor "implicate[d] tangible economic harm." *Id.* at 651. Finally, following the precedent set by *Kelly*, the court rejected the government's argument that the universities had been deprived of their employees' services, explaining that the wrongful taking of the time and labor of the universities' staff was merely the "incidental byproduct" of the admissions scheme. *Id.* at 652. Judge Talwani wrote that if there is any doubt, the rule of lenity requires dismissal of the fraud claims under this control theory. *Id.* Mr. Ernst later pled guilty to bribery and tax offenses.

Supreme Court Limitations on the Right to Control

The right to control theory, though expansive, is not unlimited. In *Dowling v. United States*, the Supreme Court concluded that a copyright was not "property" for the purpose of the stolen goods statute even as it recognized that the Copyright Act did confer a limited set of property rights to the copyright holder. 473 U.S. 207, 216–17 (1985). The Court reasoned that while the copyright holder was entitled to a "bundle of exclusive rights" to "publish, copy, and distribute" the author's work, copyright protection "has never accorded the copyright owner *complete control* over all possible uses of his work." *Id.* (emphasis added). Acknowledging the distinctive nature of copyrights, the Court concluded that "interference with copyright does not easily equate with theft, conversion, or *fraud*." *Id.* at 217 (emphasis added).

Consistent with *Dowling*'s ruling that the "bundle of rights" need not include "complete control," Supreme Court decisions considering intangibles in the property fraud context have similarly circumscribed the right to control. *See, e.g.*, *Carpenter*, 484 U.S. at 26 (newspaper "had a property right in . . . exclusive use," but only "*prior to publication*") (emphasis added); *Cleveland*, 531 U.S. at 15 (video gaming licenses are not government property, although they *may later "become property"* in the recipient's hands) (emphasis added).

Informational Rights Are Bound by the Requirement That They Be "Economic" in Nature

Although confidential business information has long been protected by Supreme Court precedent, recent cases suggest that such information must be "economic" in nature to constitute property under the wire fraud statute.

For example, in *United States v. Blaszczak*, defendants were convicted of wire fraud, among other charges, on the theory that they misappropriated confidential information regarding contemplated regulatory action from the Centers for Medicare and Medicaid Services (CMS). 947 F.3d 19 (2d Cir. 2019). Although the Second Circuit did not view the Supreme Court's precedent in *Carpenter* and *Cleveland* as requiring the government's property interest to be "economic" (*see id.* at 33), on remand from the Supreme Court in light of *Kelly*, the government took that position. The government argued:

> [I]t is now the position of the Department of Justice that in a case involving confidential government information, that information typically *must have economic value* in the hands of the relevant government entity to constitute "property" for purposes of 18 U.S.C. §§ 1343 and 1348.

Brief for United States on Remand at 7–8, *United States v. Blaszczak*, No. 18-CR-2811(L) (2d Cir. Apr. 2, 2021) (emphasis added). The government further acknowledged that although CMS does have an economic interest in its "confidential predecisional information" because the agency "invests time and resources into generating and maintaining the confidentiality of" that information, in light of *Kelly*, the CMS employee time at issue did not constitute "an object of the fraud," and thus the associated labor costs could not sustain the convictions. *Id.* at 8.

In the same vein, in *United States v. Yates*, the Ninth Circuit considered whether the "right to accurate

information," among other things, could constitute property for purposes of the bank fraud statute. 16 F.4th 256 (9th Cir. 2021). The indictment alleged that the defendants conspired "to conceal the true financial condition of the Bank and to create a better financial picture of the Bank" for the Board of Directors, shareholders, regulators, and the public by concealing material information about the performance of the bank's loans. *Id.* at 263. The government argued (and the district court agreed) that the right to accurate information is "something of value" because, without accurate information, the board could not adequately perform its duties. *Id.* at 265. On appeal, the Ninth Circuit rebuked this theory, explaining that "*[t]here is no cognizable property interest in 'the ethereal right to accurate information*.'" *Id.* (emphasis added). The court reasoned that "[a]lthough a property right in trade secrets or confidential business information can constitute 'something of value . . . the right to make an informed business decision' and the 'intangible right to make an informed lending decision' cannot." *Id.* In so holding, the court cautioned that "[r]ecognizing accurate information as property would transform all deception into fraud." *Id.* (citations omitted). The court also addressed (and rejected) the government's theory that defendants' salaries and bonuses constituted property rights under the wire fraud statute, explaining that "there is a difference between a scheme whose object is to obtain a new or higher salary and a scheme whose object is to deceive an employer while continuing to draw an existing salary—essentially, avoiding being fired." *Id.* at 266. Moreover, while the court agreed with the government that a bank has a property interest in its funds, which includes the "right to decide how to use" them, the court nevertheless reversed the defendants' convictions, finding that the entire district court proceedings were "permeated with the prohibited [property fraud] theories." *Id.* at 268–69.

A Market for Transfer or Sale

One way to determine the scope of property in the fraud context is to consider how property is treated under other federal statutes. The Hobbs Act targets "property" obtained through extortion. *See* 18 U.S.C § 1951(b)(2) ("The term 'extortion' means the obtaining of property from another, with his consent, induced by wrongful use of actual or threatened force, violence, or fear, or under color of official right."). Similarly, the RICO Act imposes a standing requirement, limiting actions to those involving injury to "business or property." *See* 18 U.S.C. § 1964(c) ("Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor. . . ."). Under these statutes, certain types of intangibles would not qualify as "property" because no market exists for them.

For example, in *Scheidler v. National Organization for Women, Inc.*, plaintiffs brought a class action against a group of protesters, alleging that they violated the RICO Act by engaging in a conspiracy to shut down businesses through a pattern of racketeering activity, which included acts of extortion in violation of the Hobbs Act. 537 U.S. 393 (2003). The plaintiffs argued (and the lower courts agreed) that doctors' rights to perform their job and medical clinics' rights to conduct their business were "property" for purposes of the Hobbs Act. *See id.* at 399. The Supreme Court disagreed, explaining that although the protesters had "interfered with, disrupted, and in some instances completely deprived [plaintiffs] of their ability to exercise their property rights," they did not "obtain" the plaintiffs' property. *Id.* at 402. Moreover, although the protesters had deprived plaintiffs of "exclusive control of their business assets," they did not receive "something of value' . . . that they could *exercise, transfer, or sell*." *Id.* at 404–05 (emphasis added). In so holding, however, the Court expressly declined to "trace . . . the outer boundaries" of liability based on obtaining "something as intangible as another's right to exercise exclusive control" over their business assets. *Id.* at 402.

As noted above, there is precedent for taking a market-based approach to property in the wire fraud context. For example, in concluding that the intangible right to confidential business information is "property" under the wire fraud statute, the Supreme Court in *Carpenter* reasoned, in relevant part, that such information "is stock in trade . . . *to be distributed and sold to those who will pay money for it*." 484

U.S. at 26 (emphasis added). Likewise, in *Ernst*, the court favored a market-based approach over the right-to-control theory of property, finding that college admissions slots are not property because they are not a "product that [the admittees] *may trade or sell in the open market*." 502 F. Supp. 3d at 651 (emphasis added).

The Application of the Wire Fraud Statute to Internet Protocol (IP) Addresses

Using these cases as guideposts, judges will need to usher in a new era of federal wire fraud jurisprudence that addresses the concept of property in the digital age. Recent cases involving the assignment, registration, transfer, and use of IP addresses have given federal courts an opportunity to do so.

An IP address is a number that identifies each device on the internet. Much like a phone call requires a unique number, IP addresses uniquely identify each device so that information can be sent to and from it. *Guide to Internet Number Resources*, ARIN, https://bit.ly/3M3nhMN. IP addresses may be treated differently based on when and how they were originally assigned. Before 1997, IP addresses were assigned informally, without any contractual agreement defining the address-holder's rights in those IP addresses. These early IP addresses are called "legacy" IP addresses. *See Legacy Resource History*, ARIN, https://bit.ly/3jBwNuv. Starting in 1997, ARIN, a nonprofit corporation that serves as the Regional Internet Registry for North America, took over IP address allocation. *See History of ARIN*, ARIN, https://bit.ly/3JBH44s. IP addresses allocated by ARIN are called "non-legacy" IP addresses and are subject to contractual limitations on their use and transferability. Specifically, ARIN's policies permit ARIN to allocate IP addresses on a needs-based basis, to take back IP addresses from registrants who fail to demonstrate continued need, and to place restrictions on registrants' ability to transfer IP addresses. ARIN's position is that non-legacy IP addresses are not property. *See Number Resource Policy Manual—Version 2021.2*, ARIN, §§ 6.4.1, 8.1, 10.1.3, 12.5 (Mar. 22, 2021), https://bit.ly/3vkOILy.

Against this backdrop, legacy and non-legacy IP addresses each appears to confer a different set of interests. This distinction may play a critical role in determining whether an IP address ranks as "property" for purposes of the federal wire fraud statute. For example, in *United States v. Bychak*, the government brought wire fraud charges against a group of defendants who work for a digital advertising company, alleging that they devised a scheme that involved acquiring blocks of legacy IP addresses called "netblocks" that appeared to be "inactive." No. 18-CR-4683-GPC, 2021 WL 734371 (S.D. Cal. Feb. 25, 2021). Defendants then allegedly used these netblocks without the authorization of the entities to whom they were originally assigned. *See id.* Defendants moved to dismiss the indictment, arguing, among other things, that the netblocks do not constitute "property" under the wire fraud statute. *See id.* at *2. The court declined to determine at the motion to dismiss stage whether netblocks are a species of property covered by the wire fraud statute. Instead, relying on precedent set by *McNally*, *Carpenter*, and *Cleveland*, that court explained that:

> To prove that . . . IP netblocks are "property", the Government will have to show that the netblocks constitute "something of value". To show netblocks are "something of value", the trier of fact will learn, among other things, what legacy IP addresses are, how legacy IP netblocks were assigned, how they were used, what limitations existed on a legacy registrant's use of an IP address, whether the assignee had exclusive control and use of the netblocks, whether, how and when a legacy IP address could be transferred, and whether a market for the transfer of netblocks existed at the time alleged in the indictment.

Id. at *11 (citations omitted). (Note: The authors represent a defendant in this case; following opening statements at trial, the government was persuaded to dismiss all charges against their client.)

Other judges have likewise denied motions to dismiss premised on the argument that IP addresses are not

"property" under the wire fraud statute, but for reasons other than the distinctions between legacy and non-legacy IP space. In *United States v. Golestan*, the government alleged that Golestan and his company, Micfo, LLC, had, under the guise of nonexistent individuals who worked for nonexistent companies, submitted false information to ARIN in order to obtain rights to IP addresses, which he then sold to third parties for millions of dollars. Order at 1, *United States v. Golestan*, No. 19-cr-00441-RMG (D.S.C. July 21, 2021). In denying Golestan's motion to dismiss, the court rejected his argument that IP addresses are services rather than property, explaining that "[w]hether IP addresses are services or products . . . the indictment states Defendants 'fraudulently obtained the *rights to*' them" and "the victim of wire fraud 'need only be deprived of some right over that property, such as the right to exclusive use.'" Id. at pp. 3–4 (emphasis in original). Although Golestan's case proceeded to trial, after two days, both Golestan and his company pleaded guilty to the government's wire fraud counts. *See* Press Release, U.S. Att'y's Off., Dist. of S.C., Tech Company and CEO Plead Guilty to Twenty Counts of Wire Fraud Mid-Trial (Nov. 18, 2021), https://bit.ly/3OnRLeL.

Similarly, in *United States v. Persaud*, the government alleged that Persaud had falsely promised various network owners that he would not use those networks to send "spam" emails, in violation of the networks' policies. Order at 1, *United States v. Persaud*, No. 16-cr-00793 (N.D. Ill. Nov. 7, 2018). The court denied Persaud's motion to dismiss, concluding that Persaud's alleged conduct "deprived the victims of a property right—namely the ability to control and exclude the individuals using its networks," which it deemed "one of the most essential sticks in the bundle of rights that are commonly characterized as property." *Id.* at 2 (citing *Kaiser Aetna v. United States*, 444 U.S. 164, 176 (1979)). Persaud's case also headed toward trial but, before the trial began, the government entered into a deferred prosecution agreement with Persaud. Deferred Prosecution Agreement, *Persaud*, No. 16-cr-00793 (N.D. Ill. June 25, 2021).

Neither the motion to dismiss opinion in *Golestan* nor that in *Persaud* offered much analysis. We have found no appellate decisions yet on the question of whether IP addresses constitute property under the wire and mail fraud statutes.

Notice and Vagueness

The due process clause of the Fifth Amendment requires federal statutes to provide "a person of ordinary intelligence fair notice of what is prohibited." *United States v. Williams*, 553 U.S. 285 (2008). The term "property" is undefined by the federal fraud statutes. There is significant debate within the Internet community as to whether ARIN's policies apply to legacy IP addresses, thereby limiting the bundle of rights they imbue on assignees. Further, while the Supreme Court has considered the "property" element of the federal criminal fraud statutes as it applies to certain intangibles (primarily those involving rights of governmental bodies), it has never articulated a clear framework for lower courts to apply to decide whether something intangible is property, particularly something involving access to a common public resource such as the Internet. This lack of clarity creates due process issues arising from vagueness and lack of fair notice. As a result, to the extent that the word "property" is ambiguous as used in the federal fraud statutes, the Supreme Court has instructed that "ambiguity concerning the ambit of criminal statutes should be resolved in favor of lenity." *Cleveland*, 531 U.S. at 25.

How Does This Affect Your Practice?

There is a lot of uncertainty in the law over what is covered by the term "property" in the federal fraud statutes. The Internet, untethered digital currency, shared arrangements, and now the metaverse are stretching our minds and causing us to question traditional understandings of things and possessions. Legislatures need to provide greater clarity about how older statutes apply to newer concepts. But while that is in progress, prosecutors will continue to grapple with whether prosecutions involving intangibles

are fair applications of older statutes. And defense attorneys will need to make sure that judges don't permit prosecutions to go forward in the face of due process concerns simply because a defendant's conduct suggests wrongdoing. Indeed, as the Supreme Court recognized in *Kelly*, the "federal fraud statutes . . . do not criminalize all such conduct." *Kelly*, 140 S. Ct. at 1568.