

**COPY**

BEFORE THE

1 UNITED STATES SENTENCING COMMISSION

2 Public Hearing on Organizational Sanctions

3  
4 Held

5 Friday,  
6 December 2, 1988

7 At

8 Courtroom 3  
9 United States Court of Appeals  
10 125 S. Grand Avenue  
11 Pasadena, California

12 APPEARANCES:

13 Honorable William W. Wilkins, Jr., Chairman  
14 Commissioner Michael K. Block  
15 Commissioner Stephen G. Breyer  
16 Commissioner Helen G. Corrothers  
17 Commissioner George E. MacKinnon  
18 Commissioner Ilene H. Nagel

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INDEX OF SPEAKERS

		<u>Page</u>
1		
2		
3	PAUL THOMSON, Deputy Assistant Administrator for Criminal Enforcement, Environmental Protection Agency	3
4		
5	ARTHUR N. LEVINE, Deputy Chief Counsel for Litigation, Food and Drug Administration	19
6		
7	JAN CHATTEN-BROWN, Special Assistant to the District Attorney, Los Angeles County	36
8	ROBERT M. LATTA, Chief U. S. Probation Officer, Central District of California	55
9		
10	ROBERT A. G. MONKS, President, Institutional Shareholders Services	68
11	CHRISTOPHER STONE, Professor, University of Southern California Law Center	96
12		
13	RICHARD GRUNER, Associate Professor, Whittier College School of Law	129
14	CHARLES B. RENFREW, Vice President, Chevron	145
15	JEROME WILKENFELD, Health, Environment & Safety Department, Occidental Petroleum	170
16		
17	BRUCE HOCHMAN, ESQ., Hochman, Salkin & De Roy, Beverly Hills, California	187
18	IVAN P'NG, Assistant Professor, University of California School of Management	207
19		
20	ERIC ZOLT, Acting Professor of Law, UCLA School of Law	205
21	MAYGENE GIARI, Citizens United for the Reform of Errants (CURE)	219
22		
23		
24		
25		

P R O C E E D I N G S

1  
2 JUDGE WILKINS: Let me call this public meeting  
3 to order. I welcome all of you to another of several public  
4 hearings the Commission is having, addressing the issue of  
5 Organizational Sanctions.

6 We are still in the early stages of our debate in  
7 consideration of this important topic and have made no de-  
8 cisions as yet. Indeed, we have other, many other steps to  
9 take before we will come to the decision-making process for  
10 promulgation for publication in the Federal Registry, which  
11 will lead toward sending guidelines to the Congress hope-  
12 fully some time next year; but this is an important step in  
13 our proceedings, and we are very pleased to have such a  
14 distinguished list of witnesses who will present their views  
15 of some of their Agencies and some of their personal views  
16 to us, to assist us in this decision-making process.

17 We have a number of witnesses who will testify and,  
18 as all witnesses have been advised, we would request that  
19 you summarize your testimony and spend not more than ten  
20 minutes in the summary of your testimony for we have re-  
21 ceived it in advance and are familiar with what your posi-  
22 tion will be, and then it would thus give us some opportunity  
23 to address and question you about specific areas that we  
24 feel are particularly important.

25 Without being discourteous to anyone in order to

1 allow for a full discussion from all witnesses throughout  
2 the day I will attempt to try to hold people to their time  
3 limit so that we do not slight anyone who will testify at  
4 a later point in the day.

5 With that said, let me call on our first witness  
6 to come forward, Mr. Paul Thomson.

7 Mr. Thomson is a Deputy Assistant Administrator  
8 for Criminal Enforcement of the Environmental Protection  
9 Agency.

10 Also with Mr. Thomson is Mr. Bruce Bellin, who is  
11 with the Counsel's Office of EPA.

12 We are delighted to have both of you with us today,  
13 and will be happy to hear from you at this time.

14 MR. THOMSON: Thank, Your Honor. Appreciate the  
15 opportunity to speak with the Commission on this very impor-  
16 tant matter.

17 The Agency has worked very closely with the Commis-  
18 sion and has enjoyed an excellent relationship. We have made  
19 special efforts to provide information in the environmental  
20 area because we feel so strongly that what your work is go-  
21 ing to accomplish is very important to us.

22 I am here at the direction of the EPA Administra-  
23 tor, Mr. Lee Thomas, who has also taken a personal interest  
24 in this matter.

25 He participated in the White House Domestic Policy

1 Council preparation of the Principles of Corporate Sentenc-  
 2 ing which was presented to the Commission on April 5th of  
 3 this year, and by letter on October 14th of this year he  
 4 conveyed to the Commission EPA's concern about a key aspect  
 5 of the draft guidelines that also brings me before the  
 6 Commission today, that is, the restricted use of probation  
 7 for organizational defendants.

8           The draft guidelines, both in the language of the  
 9 actual guidelines and in the accompanying commentary sets  
 10 out very limited circumstances, in our opinion, in which the  
 11 imposition of probation would be permissible, only if the  
 12 offense were a felony and we have a problem with them simply  
 13 because several of our statutes still have only misdemeanor  
 14 penalties. That does not mean that they are necessarily  
 15 not egregious.

16           For example, in a case recently decided, on  
 17 November 16th of this year, as a matter of fact, United  
 18 States vs. Orkin Company, a case that was decided in the  
 19 Western District of Virginia, a misdemeanor FIFRA pesticide  
 20 violation was linked to two deaths of elderly persons.

21           Here the Court imposed a five-year probation  
 22 sentence on the Orkin Corporation, after a two-day sentencing  
 23 hearing.

24           Then, also, only if a organization has a criminal  
 25 history of one or more felony convictions if the same were

1 similar types as the instant offense would probation be  
2 considered under the current guidelines.

3 In the environmental area this would mean we would  
4 have to wait the conclusion of the second prosecution for an  
5 environmental misconduct by a corporate offender before the  
6 rehabilitative probation could be imposed. In the meantime,  
7 grave environmental harm could be resulting from such en-  
8 vironmental criminal activity.

9 If all six of the conditions had to be satisfied  
10 before a sentence of probation could be imposed, this would  
11 virtually mean the elimination of probation as a criminal  
12 sanction for convicted corporate environmental defendants.  
13 We think this would be a radical departure from the current  
14 practice.

15 Our examination of our records indicate about 75  
16 percent of the corporate defendants that we have had are  
17 placed on some term of probation. It would exclude a few  
18 that would be those persons whose businesses are going to  
19 fold through bankruptcy, or where the enterprise was a par-  
20 ticularly small one, and where the major operator was per-  
21 sonally found guilty.

22 With regard to conditions of probation, even if  
23 the prerequisites for imposition of probation were met, the  
24 only condition of probation that could be imposed by a  
25 sentencing Court would be a requirement that the organization

1 develop and submit a plan for avoiding a recurrence of the  
2 type of felony for which it was convicted.

3 While such a condition is desirable, it surely  
4 does not represent the sole probationary condition that  
5 would be appropriate for all organizations convicted of  
6 environmental crimes.

7 In addition, such a plan would not require the  
8 organization, in the words of the commentary, to terminate,  
9 restrict, or unduly burden any lawful business operation.

10 In the context of environmental offenses, to avoid  
11 undertaking, from a business viewpoint, the inherently  
12 burdensome measures compliance requires is exactly the  
13 reason underlying the commission of most environmental  
14 offenses, in our experience.

15 We've chosen three cases that we think illustrate  
16 the beneficial uses of allowing a sentencing Court some  
17 degree of leeway with regard to structuring conditions of  
18 probation appropriate to the offenses of a particular corpor-  
19 ate defendant.

20 The United States vs. Nabisco, a case decided in  
21 the Western District of Washington, involved, of course, a  
22 major corporation that was convicted of willful violations  
23 of the Clean Water Act.

24 It received a \$300,000 fine, and was required to  
25 fund a \$150,000 environmental trust fund for the enhancement

1 of fish and game resources and hatcheries in the water bodies  
2 which were unlawfully polluted.

3 While the pollution that had been involved had  
4 cleared by the time of the sentencing there was no question  
5 that the quantity and quality of fishing in those waters had  
6 been severely reduced by the previous pollution, and so it  
7 was most appropriate that it was made a condition of the  
8 probation that the fishing resources be restored through this  
9 use of probation and the setting up of the trust fund.

10 In another recent case, The United States vs.  
11 Protects Industry, decided in the District of Colorado, it  
12 involved a violation of the Ricker Statutes in knowing  
13 endangerment of the lives of the employees who were handling  
14 toxic, hazardous waste materials.

15 The order involved restitution for the three  
16 employees who during the course of the criminal trial were  
17 shown to have suffered great physical harm, and as a condi-  
18 tion of probation it required payments of fines and restric-  
19 tion -- I'm sorry, and restitution before payment of the  
20 cleanup cost, since the payment of the cleanup costs, them-  
21 selves, would have benefited the corporate defendant, by  
22 enhancing the value of the corporate real estate.

23 To prevent unjust enrichment of the civil attor-  
24 neys who were representing the three employees the Court  
25 saw fit to prevent any windfall share of this and ordered



1 the criminal restitution be reviewed by the Court.

2 Two of the conditions represented just the --  
3 I'm sorry, these two conditions represented just two types  
4 that a sentencing Court needs to have available to make the  
5 conditions appropriate to particular facts of the case be-  
6 fore it.

7 In The United States vs. Wykoff Company, another  
8 Western District of Washington case, there were criminal  
9 violations of the Hazardous Waste Statutes and the Clean  
10 Water Act. Here the consequences of the environmental  
11 crimes might not have been known for a number of years, and  
12 in addition the financial position of the corporation was  
13 such that it would not permit the payment of the \$150,000  
14 fine and simultaneous payment of all the potential cleanup  
15 costs.

16 Consequently, to spread out the time period over  
17 which the cost would be incurred the Court set up a several-  
18 year payment schedule by the company for the creation of an  
19 environmental trust fund which could be used not only for  
20 cleanup cost, but also for long term preventative measures.

21 If I could return for just a moment to the Nabisco  
22 case, it illustrates another important aspect of probation  
23 that the draft guidelines would severely restrict.

24 It was a condition of a probation in that case  
25 that Nabisco comply specifically with all Federal, State,

1 and Local laws relating to environmental matters, and that  
2 Nabisco conduct itself as a law abiding and industrious  
3 citizen.

4 As Administrator Thomas has stated, the Agency  
5 does not perceive any reason why an organizational defendant  
6 should not be treated the same as an individual defendant,  
7 and that both can benefit from being required and on notice  
8 that they had better become scrupulously environmental good  
9 citizens during the period of probation.

10 That probation induces a habit of environmental  
11 compliance as much for business entities as it does for indi-  
12 viduals. To accomplish this objective the Agency and the  
13 State Compliance Monitoring personnel were alerted to  
14 Nabisco probationary status. This was so that they could  
15 monitor the Nabisco facilities as warranted during the  
16 probation, and also as would be done with any other proba-  
17 tioner, to conduct an inspection of such facilities before  
18 probation expires to insure that the criminal conduct has  
19 not been repeated.

20 EPA provides such notification to all corporate  
21 and individual defendants placed on probation. We recognize  
22 that probation offices often lack the resources and exper-  
23 tise to effectively monitor environmental compliance, and  
24 as such the Agency supplements the probation officer's  
25 effort in this regard by scheduled inspections.

1           Such monitoring can identify conditions and prac-  
2 tices that may be continuing to contribute to non-compliance  
3 and help prevent environmental violations from arising again  
4 to a level of willful and knowing violations that would  
5 warrant criminal prosecution.

6           Through this process repeated violations have been  
7 discovered. In the case of The United States vs. James  
8 Holland, a case decided in the Southern District of Florida,  
9 the owner of Middle Key Construction Company committed addi-  
10 tional Clean Water Act violations, and on May 27th his proba-  
11 tion was revoked and he was required to serve a suspended  
12 six-month term of imprisonment.

13           In the case of The United States vs. Seaport Bar  
14 Company, a Western District of Washington case, here the  
15 repeated Clean Water Act violations were discovered after  
16 the one-year period of probation had lapsed, and, thus, the  
17 Government was required to begin a new prosecution.

18           In conclusion, we would recommend that the Commis-  
19 sion give serious consideration to broadening the circum-  
20 stances in which Courts can impose probation. Under Section  
21 8(d)2.1(c), it unduly restricts the circumstances in which  
22 sentencing Courts can use probation, in our opinion.

23           The guidelines need to be developed to allow con-  
24 ditions of probation to be structured to the facts of the  
25 offense, and to the character and organizational defendant.

1           The EPA fully agrees that conditions need to bear  
2 a close relationship to the nature of the illegal activity  
3 and serve the purposes of sentencing.

4           Thank you.

5           JUDGE WILKINS: Thank you very much, Mr. Thomson.

6           I agree that the appropriateness of making a dis-  
7 tinction between a felony and a misdemeanor is sometimes very  
8 questionable, and this is one area that you point to.

9           You would suggest, I assume, that regardless of  
10 the guidelines for probation for organizations that we make  
11 no distinction in imposing this sanction between an organiza-  
12 tion committing a felony and one committing a misdemeanor,  
13 for, indeed, the misdemeanor may be more serious than the  
14 way it is committed in the felony; is that correct?

15           MR. THOMSON: That is correct, sir.

16           JUDGE WILKINS: Just abolish that distinction?

17           MR. THOMSON: Yes, sir. Yes, sir.

18           JUDGE WILKINS: All right, sir.

19           Let me ask any Commissioners to my right if you  
20 have any questions of Mr. Thomson?

21           Commissioner Nagel.

22           COMMISSIONER NAGEL: Yes. Thank you very much.

23           I thought your testimony was very important,  
24 especially in terms of some of the information you provided.

25           You mentioned that 75 percent of the corporate

1 defendants in your records are now put on some form of  
2 corporation probation. Could you provide us with some body  
3 of examples, for example, when you get back to Washington,  
4 because our records would not have shown that, and we have  
5 dated, going back to '84 and '85, but I don't know that we  
6 would have found that, and that would be a compelling statis-  
7 tic.

8 JUDGE WILKINS: What period of time are we talking  
9 about, too; this --

10 MR. THOMSON: Well, our criminal program has been  
11 effective since 1982.

12 JUDGE WILKINS: Right. So you're talking about  
13 the life of that program, 75 percent of your --

14 MR. THOMSON: Well, actually the submission relat-  
15 ing to the corporate individual defendants which I believe  
16 the Commissioners have at this time, that went back to 1984,  
17 because that was as far as our records went as far as having  
18 a really in-depth assemblage of records relating to proba-  
19 tion defendants. Actually that relates to the last two or  
20 three years, as --

21 JUDGE WILKINS: All right. Go ahead and follow up  
22 on it. I'm sorry.

23 COMMISSIONER NAGEL: Oh.

24 JUDGE WILKINS: Go ahead.

25 COMMISSIONER NAGEL: Okay. In any case, let me

1 raise this, a different point.

2 In Mr. Levine's testimony, which will proceed in a  
3 second, he talks about the fact that the multiple that is  
4 specified in the discussion draft is far too low in part  
5 because it assumes, basically, a 50 percent detection rate,  
6 and I think that the same commentary will be made this after-  
7 noon by Professor Stone, and has been made by several other  
8 persons.

9 I know this is only a guess, but could you guess  
10 if you have any sense at all, what percentage of your of-  
11 fenses, criminal violations are detected?

12 MR. THOMSON: Of the total body of potential --

13 COMMISSIONER NAGEL: Of the total body.

14 I mean, obviously the problem is, with murder it  
15 is easy because there are all those bodies, but, you know,  
16 we don't have a way of going out and finding out every time  
17 there is a violation, but do you have a sense for the per-  
18 centage?

19 MR. THOMSON: I think it would vary under the  
20 statute. We have a number of different statutes that we  
21 enforce; but I would say that 50 percent is very high.

22 COMMISSIONER NAGEL: That is what everyone else  
23 has said.

24 Everyone has told us so far that 50 percent is  
25 very high. I'm wondering. Some people have said 1 percent,

1 2 percent, 5 percent. I'm wondering if you were to guess,  
2 and I recognize it is a guess.

3 MR. THOMSON: It would be the most "wild" of  
4 guesses.

5 I would say if we had 20 percent I would think  
6 that we were extremely effective.

7 COMMISSIONER NAGEL: Okay. Thank you very much.

8 JUDGE WILKINS: Auestions?

9 COMMISSIONER BREYER: When you say corporate  
10 individual defendants you mean, you're thinking of corpora-  
11 tions being put on probation, right?

12 MR. THOMSON: Business entities; yes.

13 COMMISSIONER BREYER: Not business entities.

14 MR. THOMSON: Business entities. Yes. That's  
15 correct, Your honor.

16 COMMISSIONER BREYER: And in the submission, which  
17 I haven't seen yet, do you go into the conditions that are  
18 imposed?

19 I mean, what other, what I -- the word "probation"  
20 is a, it's a procedure, it isn't a substantive punishment,  
21 it's a procedure for making certain that some other punish-  
22 ment is imposed, --

23 MR. THOMSON: Yeah.

24 COMMISSIONER BREYER: -- or that something occurs.  
25 And so what I want to know is, underneath what is

1 occurring?

2 MR. THOMSON: Your Honor, I think probation is a  
3 uniquely valuable tool to help bring a corporate entity  
4 back into the "fold", if you will.

5 My experience is both as a prosecutor for eight  
6 years, and as a corporate counsel, a division counsel.

7 I had the experience of having my client be  
8 placed on probation when I was in corporate practice; and  
9 it was very effective. It made a very lasting impression  
10 on those --

11 COMMISSIONER BREYER: What does it mean, though?  
12 What are the conditions of the probation?

13 MR. THOMSON: Well, the conditions in this, in the  
14 situation that I was experienced with, was another regu-  
15 latory scheme, not environmental, but it required that they  
16 show affirmatively, actions taken to correct (a) the  
17 situation that got them convicted; and (b) preventative  
18 measures to assure that they would not be placed in that  
19 position again; and it caused the thinking within that  
20 group to change markedly from looking at this regulatory  
21 scheme as a cost of doing business, and get them into  
22 thinking as a positive way of doing their business in a  
23 lawful and upright manner.

24 COMMISSIONER BREYER: See, I have no problem with  
25 putting in the probation. I think it is difficult to figure  
out in an organized way what typical terms of probation are



1 going to be.

2 MR. THOMSON: Earlier this week I submitted the  
3 actual Wykoff, Protects, and Nabisco --

4 COMMISSIONER BREYER: Good.

5 MR. THOMSON: -- sentence of probation, judgment  
6 sentence judgments.

7 COMMISSIONER BREYER: Okay. Good.

8 Thank you.

9 MR. THOMSON: Sometimes you see a probation  
10 agreement, --

11 COMMISSIONER BREYER: Good. Good. Exactly.

12 MR. THOMSON: -- and see the type of conditions  
13 that are constructed.

14 To us one -- the standard condition that you obey  
15 all Federal, State and Local laws is very important to us  
16 because it enhances our ability to monitor compliance.

17 COMMISSIONER BREYER: Right.

18 MR. THOMSON: That's probably the only boiler  
19 plate point in there, Your Honor.

20 COMMISSIONER BREYER: Yeah.

21 MR. THOMSON: The other ones we've seen are highly  
22 specific to the particular offense, and the corporate entity  
23 involved.

24 COMMISSIONER BRYER: Thank you.

25 COMMISSIONER MacKINNON: Probation is limited in

1 time. Would an injunction be more effective in a number of  
2 cases?

3 MR. THOMSON: I'm not sure, sir.

4 COMMISSIONER MacKINNON: That's unlimited.

5 MR. THOMSON: I understand, sir.

6 I do think there is an advantage to having a fixed  
7 period of time. I think if you want to get the willing  
8 cooperation of folks in the corporation it is nice to have  
9 them have a fixed period of --

10 COMMISSIONER MacKINNON: You're talking about a  
11 active --

12 MR. THOMSON: Yes. Yes, sir.

13 COMMISSIONER MacKINNON: -- program of doing some-  
14 thing; but on an injunction you can carry over your, you  
15 can increase the penalty for a future violation.

16 MR. THOMSON: I understand, sir.

17 The problem we have is in a future violation it  
18 takes approximately 18 months to two years for us to work  
19 up a criminal case.

20 The idea of having an entity on probation and  
21 having somebody scrutinizing their performance for a fixed  
22 period of time, is a much more effective tool for us if the  
23 person is going to, or the entity is going to be recalci-  
24 trant.

25 COMMISSIONER MacKINNON: Do you report to the

1 Court?

2 MR. THOMSON: No, sir.

3 Our monitoring is a function of the --

4 COMMISSIONER MacKINNON: So we are not imposing  
5 restrictions or duties on the Court?

6 MR. THOMSON: No, sir, that's -- No. No, this  
7 would be too --

8 COMMISSIONER MacKINNON: Let me ask you one other  
9 question:

10 When I used to live in Colorado, why, in the  
11 mining areas, the streams for miles and miles and miles had  
12 no fish in them due to the cyanide mills that were there.

13 I wondered what the situation is now? Has that  
14 been corrected?

15 MR. THOMSON: We're working on it, sir.

16 COMMISSIONER MacKINNON: Good.

17 MR. THOMSON: I'm a trout fisherman. I want to  
18 see those streams come back.

19 COMMISSIONER MacKINNON: Thank you.

20 JUDGE WILKINS: Thank you both, very much.

21 MR. THOMSON: Thank you, sir.

22 JUDGE WILKINS: We look forward to a continuing  
23 working relationship with you and your Agency.

24 MR. THOMSON: Thank you, sir. We've enjoyed it.

25 JUDGE WILKINS: Our next witness is Mr. Arthur N.

1 Levine.

2 Mr. Levine is the Deputy Chief Counsel for Liti-  
3 gation for the Food and Drug Administration.

4 We received a great deal of written testimony in  
5 advance, and a lot of hard work went into it by a number of  
6 people.

7 I do want to commend you, Mr. Levine, for the  
8 excellent submission that you have given us.

9 MR. LEVINE: Thank you.

10 It's a pleasure to be here this morning and I have  
11 been asked to attend by the Commissioner of the Food and  
12 Drug Administration, Dr. Young.

13 As my written remarks suggest, there are some  
14 themes which cause me to reach the suggestions that I have,  
15 and the conclusions.

16 I would like to begin by articulating what those  
17 are.

18 First: In a majority of FDA referrals to the  
19 Department of Justice for Criminal Prosecution, we include  
20 recommendations that organizations and individuals both be  
21 charged; and where Assistant United States Attorneys are  
22 sometimes tempted to consider suggestions by defense counsel  
23 that individuals be dropped in exchange for a corporation,  
24 a plea by the corporation, we vigorously oppose such sugges-  
25 tions.

1           The fact that our criminal enforcement program is  
2 directed both at individual agents and at organizations has  
3 a very important impact on our attitude towards the Commis-  
4 sion's draft concerning set offs for individuals in sentenc-  
5 ing organizations.

6           Second of all, in the majority of our referrals  
7 for criminal prosecution, the FDA has already taken some  
8 civil or administrative action. Seizures of products that  
9 are adulterated or misbranded, injunctions against companies  
10 that are either making or distributing such goods.

11           In addition, companies also engage in a certain  
12 form of voluntary action in order to preclude an FDA seizure  
13 and with an eye towards tort liability companies increasing-  
14 ly have begun to recall defective products from the market  
15 before or in conjunction with FDA interest in the problem.

16           I noted that in the paper from Professor Cohen  
17 the, he discussed some of the impact of prior civil and ad-  
18 ministrative sanctions, but observed that the data were  
19 simply inadequate.

20           Third, the FDA has had a very positive experience  
21 with injunctions. The injunctive relief that we seek is  
22 relatively well-established, the terms of that relief; and  
23 they correlate well, we believe, with the desire of the  
24 Agency to be sure that similar violations are corrected and,  
25 indeed, prevented in the future; so our attitude towards the

1 draft guidelines view on probation is very, very similar to  
2 that that has been expressed this morning by the representa-  
3 tives from the EPA.

4 We encourage the Commission to be much more recep-  
5 tive to the concept of organizational probation. It paral-  
6 lels our experience in bringing civil injunction action.

7 Fourth, we believe that the data that the Commis-  
8 sion has gathered, and to some extent is relying on in  
9 setting its levels of fines, is dated, and the data are not  
10 as instructive as they might be.

11 Between 1938 and 1984 someone who violated the  
12 Food and Drug Act was subject to a penalty of \$1,000. When  
13 Congress set that penalty in 1938 it was a lot of money.  
14 In 1984 it was very little money.

15 The new increases in fines have had a very signi-  
16 ficant impact on FDA's average fine.

17 As Professor Cohen pointed out in the materials  
18 that you submitted just before the hearing, this change,  
19 alone, seems to account for approximately a tripling of the  
20 average criminal fine, and I would suggest that in the FDA  
21 area the increase is much more dramatic.

22 Fifth, FDA has a very, very strong interest in its  
23 ability to make inspections. Our ability to determine the  
24 underlying cause of a defective product or misbranded pro-  
25 duct stands at the heart of our regulatory program.

1           We have also found that it is very hard to draw  
2 a line between so-called record-keeping violations and more  
3 substantive violations since record-keeping violations  
4 except where they are completely inadvertent always have at  
5 least as a consequence, if not as an intended purpose, the  
6 covering up, to one degree or another, of a more significant  
7 substantive offense.

8           Finally, as a general matter, our experience has  
9 been that the differences between misbranding and adultera-  
10 tion or between a mislabeled product and a contaminated pro-  
11 duct or one that creates a safety risk are always not that  
12 clear.

13           Indeed, one more of misbranding articulated in the  
14 statute is that a product is dangerous to health, as labeled.  
15 A form of violation which, for which the consequences would  
16 be catastrophic.

17           Having articulated these views which form the basis  
18 of our approach to the Commission's draft I would now like  
19 to briefly review where I think those observations take us,  
20 as I have in my paper.

21           On the question of the overlap between adultera-  
22 tion and misbranding or mere mislabeling and product safety,  
23 the Commission, I think, has recognized this, and has  
24 created a great deal of overlap, bringing to bear four of  
25 its seven categories of criminal offense in the Food and

1 Drug area.

2 The Commission's draft is very, very careful to  
3 cross-reference in notes and in commentary between one  
4 applicable guideline and another, creating essentially a  
5 common theme, and that is that misbranding and other forms  
6 of mislabeling will be treated essentially as fraud, and  
7 product contamination, or what we would call adulteration,  
8 almost always considered under the Food and Drug category.

9 The one area in which that doesn't break out very  
10 cleanly is the regulatory reporting; and as my written  
11 remarks suggest, I think that the Commission might reconsider  
12 that category altogether, particularly in the food and drug  
13 offenses to see whether such violations would not more  
14 properly fall within substantive categories.

15 The particular overlapping jurisdiction between  
16 the categories raised the problem which I described in my  
17 paper; namely, that if the Food and Drug Administration is  
18 doing its job and is doing it properly, then it often will  
19 come to pass that before a significant amount of a defective  
20 product is introduced into commerce the Agency will have  
21 interdicted and will have stopped this activity. As a re-  
22 sult, under the food and drug category which turns on the  
23 amount of goods actually sold, the loss, base loss might be  
24 low, and that is of some concern to me.

25 In that situation, comparing the base loss for



1 actual shipment compared to the base loss under the fraud  
2 category for value, including the general rule that all  
3 acts or omissions are to be considered, there are situations  
4 where I envision a much larger penalty for mislabeling than  
5 I do for product contamination.

6 Another potential solution to the overlap problem  
7 is to create a, the "greater of" standard, where the Courts  
8 and prosecutors would be free to in some cases argue over  
9 the most applicable category as between the four into which  
10 food and drug offenses seem to fall, but allow for the loss  
11 to be that which is the greatest under any one of the cate-  
12 gories.

13 Such a rule might bring some leveling between  
14 Judges and between jurisdictions.

15 As I have said in my paper, the FDA feels very  
16 strongly that the refusal to permit an inspection is a very  
17 serious offense. Currently under the reporting category in  
18 which that activity is listed the minimum fine is \$500, and  
19 the loss computation would be very low. We feel that sends  
20 an inappropriate message.

21 As a general matter, we find the minimums to be  
22 very low, particularly considering that the Commission's  
23 guidelines apply to all the offense conduct, it -- minimums  
24 in the range of \$500 to \$2,000 may suggest to a Judge that  
25 when a prosecutor gets through with the computation of loss

1 and comes up with a figure like a half a million dollars the  
2 prosecutor must obviously be wrong because the minimum has  
3 got to mean something; and I would suggest that the Commis-  
4 sion reconsider the use of minimums lest they become a mis-  
5 leading point of reference.

6 On the question of multiples, as I have pointed  
7 out in my paper, one of our biggest concerns is the adjust-  
8 ments.

9 As I read the Commission's paper, very serious  
10 forms of obstruction and false statements would lead to an  
11 increase in the multiple of only one. I'm not sure that  
12 that kind of an increase sufficiently reflects the serious-  
13 ness of the activity, nor necessarily engenders a respect  
14 for law.

15 I think the multiple's area is an extremely diff-  
16 cult one, and I sense that it is the point in the Commis-  
17 sion's work in which it tried to grapple with some of the  
18 intangibles in sentencing, particularly not making a distinc-  
19 tion between felonies and misdemeanors; but that particular  
20 area is troublesome to me; and as I mentioned in my paper,  
21 the concept that a multiple, and thus a fine would be de-  
22 creased because a violation was open and obvious is, in the  
23 day-to-day world of enforcement very, very difficult to  
24 accept, and I would ask the Commission to reconsider its  
25 views, or maybe articulate what underlying principle might be

1 applying there, so as to eliminate that particular conse-  
2 quence. I found that very distressing.

3 On the question of fines and set offs, the broad  
4 definition of restitution equivalence calls into question  
5 this prior FDA enforcement activity. Indeed, if under the  
6 Food and Drug category clean up and recall are two of the  
7 things that the Commission envisions will be added in the  
8 loss column under ameliorative activity, it is important  
9 for the Commission to recognize that product recall and  
10 plant clean up may very well already have taken place under  
11 civil or administrative action. As a result, in the loss  
12 category, under the Commission's guidelines, it will have  
13 giveth to the loss, to the amount of loss, and then in  
14 restitution will have taketh away.

15 And it was unclear to me, from reading the Commis-  
16 sion's draft whether it envisioned that the clean up and  
17 recall which was part of the ameliorative sanction in com-  
18 puting the total loss would be set off against the civil  
19 or administrative penalties. It certainly seemed that way  
20 to me.

21 I believe, Commissioner, that I've run out of  
22 time.

23 JUDGE WILKINS: Let me ask you this: Do you  
24 believe that restitution should be addressed as a separate  
25 issue; for example, the guidelines would require restit-

1 tion and then address separately the amount of fine and/or  
2 the imposition of probation, but not have restituion effect;  
3 that is reduce the appropriate fine?

4 MR. LEVINE: My personal view is "yes"; although  
5 from reading the statute as it has been refined, it seems  
6 that Congress wants the Courts to consider restitution, and  
7 so I think either the designation of some characteristics  
8 which would call resitution set off into play, not unlike  
9 characteristics of the kind set forth in the multiplies, or  
10 a percentage of restitution set off reflecting certain  
11 characteristics would likely be more consistent with the  
12 Congressional mandate.

13 JUDGE WILKINS: Of course, if you make the fine  
14 high enough it really doesn't matter, I guess, as far as a  
15 deterrence is concerned?

16 MR. LEVINE: Yes, that's true.

17 Are you referring, Commissioner, to the total  
18 monetary sanction, or the resulting fine after the set offs?

19 JUDGE WILKINS: The total monetary sanction.

20 MR. LEVINE: Yes.

21 My concern, as I've tried to state, is that in the  
22 food and drug area the set offs might be quite significant,  
23 leaving an amount of criminal fine which possibly doesn't  
24 reflect society's judgment, notwithstanding everything that  
25 has befallen the corporation to, nevertheless, bring criminal

1 charges.

2 If there is going to be such a separate statement,  
3 societal statement, then there ought to be some kind of  
4 corresponding minimum fine, because I agree completely with  
5 the Commission that monetary sanctions and fines in parti-  
6 cular are very, very -- they serve the objectives of de-  
7 terrence and punishment quite well for a corporation.

8 JUDGE WILKINS: Thank you very much.

9 Let me ask Commissioners to my right: Questions?

10 COMMISSIONER BLOCK: Mr. Levine, I have two  
11 comments, and hopefully we can help each other on this.

12 The comment that is supposed to be written  
13 testimony and that you have repeated orally about, this  
14 problem about the construction of the loss categories, I  
15 guess the guidelines are probably not as clear as they  
16 should be on that, but if you take the two loss categories,  
17 there's a fraud category and then the food and drug  
18 category, --

19 MR. LEVINE: Yes.

20 COMMISSIONER BLOCK: I'd like to make two points  
21 about it.

22 One, the categories are not usually exclusive, so  
23 that if there's a fraud with a food and drug violation, both  
24 loss rules could be used as long as it wasn't double counting  
25 the harms and we tried to address that in the commentary.

1           The other point which I would like you to address,  
2 not here, but giving an example of, if you consider the two  
3 prongs of the food and drug loss, both the ameliorative as-  
4 pect and the amount actually sold, whether you'll actually  
5 get this reversal that you talk about, I can tell you the  
6 reason for putting -- the reason, the difference in wording  
7 between the fraud guideline and the second prong of the food  
8 and drug was that we ran into a problem if you used only  
9 the ameliorative prong then, in fact, if you couldn't  
10 ameliorate, in fact the commodity was consumed or it was  
11 impossible to have a recall, you needed the second prong to  
12 get at that, but the standards, of sort of intended and  
13 probable, apply to the first part of the food and drug in  
14 the same way that they apply to the entire fraud standard.

15           You might look that over again in context, we can  
16 spend some time talking about that, after.

17           MR. LEVINE: I was very concerned that that might  
18 be the Commission's intent, and I have read the document  
19 many times, and, as Paul Martin knows, had quite a bit of  
20 anxiety over giving some testimony only to find that on Page  
21 something someone said something that dealt exactly with the  
22 point that I made, and I missed it each time.

23           I can only say that on both the points you have  
24 made I have missed them on several readings.

25           First of all, the mutually, the fact that they are

1 not mutually exclusive was something that I did not glean  
2 from the document in the commentary.

3 COMMISSIONER BLOCK: It's probably not as clear  
4 as it should be; it's a fairly subtle document, but it is  
5 probably too sublet in that respect.

6 MR. LEVINE: And --

7 COMMISSIONER BLOCK: But let me make one addi-  
8 tional point, and then you can respond, and that is on  
9 multiple, and it's a general point. I mean, other people  
10 are going to make it and one of my fellow Commissioners has  
11 just made the point this morning.

12 The multiple is a criminal multiple, so -- and I  
13 think we actually refer to that on Page 840 in the com-  
14 mentary, that you can't read the two as implying a 50  
15 percent chance apprehension to the extent that the overall  
16 multiple should be related to the probability of detection.  
17 It's the multiple calculated with the civil penalties.

18 The multiple that we use in the fine provision is  
19 really just the criminal multiple; and that's base. It's  
20 true, it is anchored in current practice simply because we  
21 don't know what the overall multiple should be and we can't  
22 observe the civil penalties, so we look at, well, what have  
23 the criminal multiples been like in the recent past?

24 I think, you know, it is important to distinguish  
25 between the overall multiple, which is tied to the likeli-

1 hood of detection, and this criminal multiple, which is  
2 simply the multiple that's left over for the fine.

3 MR. LEVINE: Yes.

4 COMMISSIONER BLOCK: Now one thing that will be  
5 extremely useful, and we have not been able to get, is some  
6 idea of what the other penalties are, so that in some food  
7 and drug cases if I could get information about what are  
8 the overall penalties like, so what are the overall multiples  
9 like, it's clear that two is too low a multiple if you were  
10 looking at it as an overall multiple, and it's not clear to  
11 me that it is so far from the mark if you're looking at just  
12 the criminal multiple.

13 THE REPORTER: Excuse me for a tape change,  
14 please.

15 I'm sorry.

16 (Tape change.)

17 THE REPORTER: We're on the record.

18 COMMISSIONER BLOCK: I will welcome your comments  
19 and additional information.

20 MR. LEVINE: Yeah. I am not sure that the time  
21 that I have permits me to respond, nor am I in a position to  
22 be; I'd love to think about all those things that you have  
23 said and possibly submit a letter or something to the  
24 Commissioner to put into the record to amend my written  
25 remarks.



1           COMMISSIONER BLOCK: Extremely useful.

2           JUDGE WILKINS: That would be very helpful to us,  
3 and the record will remain open for a period of 30 days  
4 following this hearing, so there will be ample time for you  
5 and others to supplement their testimony. We would welcome  
6 that input from you.

7           Commissioner Corrothers.

8           COMMISSIONER CORROTHERS: I think you got into  
9 this area briefly in response to Chairman Wilkins, but I  
10 concur in your belief that societal judgment, that the cost  
11 of doing business are not an adequate penalty and that  
12 further punitive measures are appropriate.

13           You further indicated in your testimony I believe  
14 on -- written testimony on Page 18 that the criminal fine  
15 portion of the total monetary sanction should go beyond law  
16 enforcement costs to reflect societal judgments. That the  
17 fine's minimum would be appropriate to the seriousness of the  
18 offense; further, that a fixed amount is not necessary.

19           How would be accomplish that? Would we determine  
20 appropriate factors or designated characteristics to be con-  
21 sidered in order to arrive at a fine commensurate with the  
22 seriousness of the offense?

23           I wonder if you would just expand on the idea of  
24 insuring that the seriousness of the offense is reflected in  
25 the fine or total monetary sanction?

1           MR. LEVINE: I think what I had envisioned would  
2 be as you have suggested, a set of characteristics which  
3 would be used then to relate to the non-criminal set offs,  
4 so that if you had restitution and restitution equivalents  
5 of 2 million dollars, but under a set of characteristics you  
6 would only give someone credit for 25 percent of that, or  
7 50 percent of that, that activity would then represent the  
8 criminal fine aspect of the total sanction; otherwise, I  
9 think you get back into just picking numbers for a mis-  
10 demeanor or a felony which the law already now provides; so  
11 I guess that's what I had envisioned; and I also suggest in  
12 my paper that the Section 3572(a)7, which provides for con-  
13 sideration of efforts to discipline responsible individuals,  
14 in setting organizational fines might be a factor whether a  
15 corporation seems to have acted responsibly since discovery  
16 of the offense might be a factor to use in that equation.

17           COMMISSIONER CORROTHERS: Thank you.

18           JUDGE WILKINS: Thank you.

19           Question to my left.

20           COMMISSIONER NAGEL: I would just like to thank  
21 you for your obviously very insightful and thoughtful  
22 comments and ask that you communicate as well to Commissioner  
23 Frank Young how much we appreciate his support and your  
24 efforts on our behalf, both in this particular hearing, but  
25 before as well. You've come many times to the Commission

1 and been very helpful, and we appreciate it.

2 MR. LEVINE: Thank you.

3 COMMISSIONER BREYER: Are you aware that the  
4 Justice Department has been writing drafts and has made  
5 some pretty useful contributions, or is the FDA involved?

6 I bring that to your attention deliberately.

7 MR. LEVINE: I am not aware that we have partici-  
8 pated in the department--

9 COMMISSIONER BREYER: Because there are -- they  
10 have been soliciting views as I think of other Agencies of  
11 the Government, as well; and they come up with some really  
12 useful ideas, I think; and I think it would be useful for  
13 you to make your views known to the department, as well.

14 MR. LEVINE: I intend to.

15 The FDA's referrals for criminal and injunctive  
16 relief are directed to the Office of Consumer Litigation  
17 of the Civil Division, and we work closely --

18 COMMISSIONER BREYER: She got it over at the  
19 Criminal Division. Right.

20 MR. LEVINE: Yeah.

21 For historical reasons we used to be in Anti-Trust;  
22 we used to be everywhere.

23 Now we're in the Civil Division, but they handle  
24 all our criminal work.

25 Our seizure actions are addressed directly to the

1 United States Attorney in the location where the goods  
2 exist; but I do intend to send copies of my remarks to OCL.

3 COMMISSIONER BREYER: And you want to look at  
4 what they are doing, as well.

5 MR. LEVINE: Not in a participatory way, but  
6 obviously the policy, such as the principles of prosecution  
7 of the Department of Justice are very, very important to the  
8 FDA, and we need to meet them in order to get our cases  
9 accepted for filing by the Department of Justice.

10 COMMISSIONER MacKINNON: What -- Do you use the  
11 injunction as part of the criminal process?

12 MR. LEVINE: Our -- No.

13 Primarily we have used --

14 COMMISSIONER MacKINNON: That's all I needed to  
15 know.

16 MR. LEVINE: Okay.

17 COMMISSIONER MacKINNON: I want to compliment you  
18 on the submission that you made, and upon your testimony.

19 MR. LEVINE: Thank you.

20 JUDGE WILKINS: Thank you, Mr. Levine; and we look  
21 forward to continuing to work with you and your Agency; and  
22 we appreciate all the assistance you have given us.

23 MR. LEVINE: Thank you.

24 JUDGE WILKINS: Thank you.

25 Our next witness is Jan Chatten-Brown, Special

1 Assistant to the District Attorney, Los Angeles County.

2 We appreciate you allowing us to visit your part  
3 of the world, and we understand why you, I am sure, and we  
4 know that our former Chief Counsel David Lombardero believes  
5 that no other place quite measures up to where we are today.

6 MS. CHATTEN-BROWN: We did arrange some rather  
7 nice weather right now.

8 JUDGE WILKINS: You sure did.

9 Thank you.

10 MS. CHATTEN-BROWN: It's hard to think of  
11 Christmas in this weather, but it is delightful.

12 Thank you very much.

13 My role as Special Assistant to the Los Angeles  
14 District Attorney is specifically for Environmental Protec-  
15 tion and Occupational Safety and Health.

16 Since beginning my legal career I have exclusively  
17 practiced Environmental and Occupational Safety and Health  
18 Law, with the exception of a three-year assignment as the  
19 manager of the Special Operations Division in the Los Angeles  
20 City Attorney's Office.

21 During that time I additionally supervised Consumer  
22 Housing and Obscenity prosecutions.

23 Those of us in both the Los Angeles City Attorney's  
24 Office and Los Angeles District Attorney's Office involved  
25 with so-called "white collar" or "organizational crime"

1 emphasize creative sentence advocacy.

2 Substantial jail time and penalties are simply  
3 not enough. We routinely require as part of any disposi-  
4 tion agreement the acceptance of conditions of probation  
5 tailored to the conditions which caused the initial viola-  
6 tion.

7 For example: We have prosecuted 22 occupational  
8 safety and health cases since the District Attorney's OSHA  
9 Section was established. That, by the way, was the first  
10 of its kind in the country.

11 Of these cases 20 involved fatalities. In all  
12 completed cases we've required comprehensive accident pre-  
13 vention and protection programs as conditions of probation.

14 Attached to my testimony is a copy of the pro-  
15 bationary terms imposed in a fatality prosecution against  
16 Reliance Steel and Aluminum Company and several individual  
17 corporate officials.

18 In the Reliance case the accident prevention plan  
19 requires the hiring of a full-time safety and health pro-  
20 fessional, restructuring of the labor/management safety and  
21 health committee, daily safety inspections, weekly safety  
22 meetings, and the retention of an outside expert to conduct  
23 job safety analyses.

24 COMMISSIONER NAGEL: Could I just interrupt for a  
25 second. Could I ask her to use the mike?

1 MS. CHATTEN-BROWN: Certainly.

2 JUDGE WILKINS: That won't help.

3 COMMISSIONER NAGEL: Oh.

4 MS. CHATTEN-BROWN: I'm sorry. I have a very bad  
5 winter cold right now. I will speak up.

6 COMMISSIONER NAGEL: Okay. I thought the mike was  
7 working.

8 JUDGE WILKINS: That mike hooks only into the  
9 recorder there, but --

10 COMMISSIONER NAGEL: I see. Okay.

11 Go ahead.

12 MS. CHATTEN-BROWN: I'll be happy to speak up.

13 JUDGE WILKINS: Thank you.

14 MS. CHATTEN-BROWN: Based upon my experience over  
15 the past 16 years, I have several observations and recom-  
16 mendations regarding the organizational probation sanctions  
17 of the Commission's discussion materials on organizational  
18 sanctions.

19 Let me begin by commending the contributors to the  
20 materials on the organizational sanctions for their thought-  
21 ful and provocative papers.

22 The clear articulation of the rationale for deter-  
23 mining monetary sanctions will be of immeasurable help to  
24 prosecutors and to the Court. In particular, I must say,  
25 in regard to toxic waste cases where we have really, I think,

1 demonstrated substantial leadership; brought more cases than any  
2 other local prosecutor in the country, and obtained over a  
3 hundred convictions. We often feel we are thrashing about  
4 for an appropriate criteria, and over and over again in our  
5 internal discussions where we discuss cases and try to de-  
6 cide what is an appropriate sentence to argue for, we often  
7 throw up our hands and say, "This process still seems so  
8 arbitrary."

9 I applaud the commitment to utilizing organiza-  
10 tional probation as a means to achieve responsible corporate  
11 conduct. In several cases that we have prosecuted, the indi-  
12 vidual defendants charged are no longer in a management  
13 position at the time of sentencing.

14 Under California law probationary conditions are  
15 normally in force by suspension of a monetary fine, or by  
16 placing the responsibility for compliance upon an individual  
17 where a violation could result in jail time.

18 In the civil law field an individual may be held  
19 in contempt for failure to comply with an order of the Court  
20 even if they were not a named defendant, but we do not know  
21 whether this would be extended to criminal conditions of  
22 probation where the individual was not charged as a de-  
23 fendant.

24 As a result, imposing organizational probation as  
25 a supplement to other penalties has considerable appeal,



1 especially if an individual corporation official is desig-  
2 nated as accountable for violations of the conditions.  
3 However, in my opinion, the proposed criteria for imposition  
4 of organizational probation are too narrow.

5 Let me focus my comments on proposed Section  
6 8(d)2.1, Sub (c).

7 First, I recommend that the offenses justifying  
8 probation not be restricted to felonies.

9 In the area of occupational safety and health  
10 alone such a restriction would nullify use of this very  
11 appropriate remedy.

12 Willful violations of occupational safety and  
13 health regulations resulting in death are misdemeanors  
14 under Federal law. The facts and cases filed under the  
15 Federal OSHA law often show serious disregard for safety.  
16 Imposition of probationary terms in these cases are appro-  
17 priate.

18 Second, the requirement that the senior manage-  
19 ment of an organization "participated in or encouraged the  
20 offense" ignores the fact that most environmental and occu-  
21 pational safety and health violations occur as the result of  
22 negligence, albeit sometimes gross negligence.

23 Negligent failure to comply with the law also  
24 warrants imposition of organizational probation. Without  
25 such a provision some senior management officials will close

1 their ears and eyes to environmental and occupational and  
2 safety and health hazards.

3 Third, the requirement that the organization or  
4 senior management has a criminal record of one or more  
5 felonies is unduly restrictive.

6 Prosecutions for even the most egregious occupa-  
7 tional safety and health or environmental violations still  
8 are sufficiently infrequent so that it would be extremely  
9 rare to have a prior criminal history even where repeat  
10 violations exist.

11 I believe it is appropriate to impose probation  
12 where there is a regulatory history of violations of the  
13 same or similar type as that charged.

14 The changes I have recommended would substantially  
15 expand the use of organizational probation. Understandably  
16 Courts are reticent to undertake supervision of complex and  
17 details conditions of probation even in situations where  
18 protection of worker and public safety and health warrant.

19 The commentary on the organizational probation  
20 assumes all probationary terms will be supervised. In  
21 California State Court probationary terms routinely are  
22 summary. We return to the Court if the regulatory agency  
23 finds a violation.

24 The Environmental Protection Agency, Occupational  
25 Safety and Health Administration and similar agencies might

1 appropriately assume substantial responsibility for the  
2 initial development of the terms of probation, and for  
3 assuring compliance with those terms.

4 The recommended conditions for a probation policy  
5 statement drafted by Messrs. Coffee, Gruner & Stone, are  
6 extremely helpful; however, two concerns warranting atten-  
7 tion are found on Page 28 of their discussion paper.

8 First, they argue conditions restricting the dis-  
9 missal of employees are inconsistent with statutory law.  
10 The reality is that in both environmental and occupational  
11 safety and health prosecutions protecting employees who  
12 provided the prosecutor with information from retaliatory  
13 action is of significant concern.

14 We repeatedly make it clear to defense counsel  
15 that any such retaliatory action shall be prosecuted to the  
16 full extent of the law.

17 I believe that a specific probationary condition  
18 on retaliatory action may be appropriate in some circum-  
19 stances.

20 Second, the prohibition on requiring financial  
21 conditions to any organization not a victim of the crime  
22 would prevent a useful remedy.

23 For example, in the last three settlements of  
24 occupational safety and health cases and in several environ-  
25 mental cases contributions to appropriate educational

1 institutes have been required as conditions of probation.

2 In the three most recent OSHA cases we required  
3 contributions to the UCLA Institute of Industrial Relations  
4 Center for Labor Education and Research. Such contributions  
5 are utilized in the development of safety training materials  
6 related to the types of hazards which caused the fatalities  
7 in the cases at issue. Those materials, then, are available  
8 not only to the Defendant, to the Probationer, but also for  
9 use statewide, and, hopefully, nationwide.

10 We believe that the use of such funds is appro-  
11 priate.

12 Finally, I note that the reference to U. S. vs.  
13 Atlantic Richfield, on Page 29 of the Coffee, Gruner &  
14 Stone analysis. In that case the Appellate Court set aside  
15 the Trial Court's requirement that the Defendant establish  
16 a program to handle oil spillage.

17 The provision was set aside for lack of specifi-  
18 city.

19 It is our belief that it is desirable to involve  
20 the Defendant in the development of a work plan for achieving  
21 compliance with applicable laws. The key may be in having  
22 the Prosecutor, an appropriate regulatory Agency, review the  
23 plan developed by the Probationer and then report back to  
24 the Court, at which time the conditions of probation could  
25 actually be imposed.

1           Thank you very much for the opportunity to comment  
2 upon these important materials.

3           JUDGE WILKINS: Thank you very much.

4           We have sought and will continue to seek the views  
5 from a wide variety of witnesses who bring different view-  
6 points to the witness table; but I feel, and I think I  
7 speak for all the Commission, we know it is particularly  
8 important to hear from those who have had firsthand ex-  
9 perience in the prosecution or defense of corporations or  
10 other organizations; and I think the bottom line as far as  
11 probation is concerned, you correct me if I'm wrong, you  
12 would say from your personal observations that not only  
13 should monetary sanctions be imposed, but that probation  
14 is a very effective tool in the sanctioning of organiza-  
15 tions, and that it should be used liberally and not re-  
16 strictively; is that correct?

17           MS. CHATTEN-BROWN: Absolutely. Especially in the  
18 occupational safety and health and environmental area.

19           First of all, our experience is that the Judges,  
20 at least at the State Court level but I assume also at the  
21 Federal Court level are really hesitant to impose the level  
22 of sanctions that really would be sufficient deterrents;  
23 and even more than that, there is what was referred to this,  
24 the spill-over effect, the concern that you're penalizing  
25 not the managers that have made the errors, but the stock-

1 holders, the board of directors and the public, generally,  
2 and that the cost of products will simply go up.

3 It is often a matter of getting management off on  
4 the right foot. In the occupational fatality cases we  
5 respond to the scene every time there's an occupational  
6 fatality in L. A. County, and so I see firsthand the re-  
7 actions of the various managers; and in rare cases is there  
8 anything but horror at what has just occurred; but you look  
9 at their practices and they have simply given insufficient  
10 attention to safety.

11 In the Reliance Steel case the disposition that we  
12 reached after lengthy discussions with their legal counsel  
13 was an 18-page safety and health program, and after imposi-  
14 tion of those conditions the President of the corporation  
15 said:

16 "This has turned us around."

17 You know, there was never any malicious intention,  
18 but a young man was killed in really, I think, egregious  
19 circumstances, and they had had prior fatalities, and they  
20 had many other injuries, and now with short experience with  
21 the plan they say that their worker compensation claims are  
22 coming down and other industries are turning to them for  
23 recommendations for a safety program. Unfortunately, the  
24 monetary penalty alone simply would not have achieved that.

25 JUDGE WILKINS: Mm-hmm. Thank you.

1 Questions to my right?

2 COMMISSIONER BLOCK: I just have a question about  
3 how the organizational probation works in the State of  
4 California. Is it an alternative sanction as opposed to  
5 the complementary?

6 MS. CHATTEN-BROWN: Yes, it is an alternative.

7 You, normally it's achieved if -- if there's an  
8 individual who is charged then our task is fairly easy if  
9 that person still has managerial responsibility; but in two  
10 of our more recent cases the Defendants that were convicted,  
11 that had been in one case, well, in both cases, the general  
12 manager of the facilities, although they were convicted,  
13 they had been assigned to other responsibilities, and no  
14 longer had management responsibility.

15 In one case the general manager of Golden State  
16 Foods which is a large meat processor had actually left the  
17 company entirely, and, as a result we could not have his  
18 condition of probation be in compliance with the accident  
19 prevention plan.

20 We do routinely require anyone that's going to  
21 continue to have supervisory responsibilities to have safety  
22 training themselves to attend a certain number of safety  
23 training seminars, et cetera, but there there was going to  
24 be no impact upon the industry, and so the only thing that  
25 we could do was we, in that case, had the complete fine

1 suspended, and then we had a \$17,000 contribution, which  
2 really, considering the type of violation, and the size of  
3 the corporation, which is extremely large, is nothing, but  
4 it was the maximum that could have been achieved with the  
5 penalty assessments. We had that as a contribution to UCLA;  
6 and so because it's a contribution rather than a fine, if  
7 there's a violation of their accident prevention plan we can  
8 go back to Court and try to levy the entire fine, but what  
9 we are really most interested in is having the individual  
10 responsible for the compliance with the conditions.

11 COMMISSIONER BLOCK: Now, just to come back to the  
12 organization again, in the cases that you have been in-  
13 volved in, if you put aside the individuals for a moment,  
14 which I think this is an extremely important area, but just  
15 looking at the organization itself, then rather than imposing  
16 a fine, you routinely asked for the suspension of the fine  
17 and the imposition of probation on the organization?

18 MS. CHATTEN-BROWN: Yes. And then one of the  
19 conditions of probation is a contribution for development of  
20 appropriate materials or some similar thing.

21 Of course, in all the environmental cases we have  
22 cleanup, to cover the costs of cleanup, but we always do  
23 something substantial in addition to that.

24 Bringing in outside auditors to conduct an environ-  
25 mental audit, for example, in an environmental case.



1           COMMISSIONER BLOCK: And it's your feeling from  
2 your experience that the fines are insufficient and you get  
3 more out of the probationary sentence of the organization?

4           MS. CHATTEN-BROWN: Well, we would, obviously,  
5 very much like to have both, and after reviewing the material,  
6 and, quite frankly, not being involved with Federal practice  
7 I wasn't aware of the provision in Federal law allowing this  
8 as a supplement, until I reviewed the materials, but I think  
9 that our office will be proposing that in the State Legis-  
10 lature this year because it's a very, very useful remedy.  
11 We think that it should be; but if we have to choose between  
12 having probationary conditions and the fine we will choose  
13 the probationary conditions, which always includes a sub-  
14 stantial monetary commitment, in any case.

15           COMMISSIONER BLOCK: I see. Thank you.

16           JUDGE WILKINS: Well, pardon me.

17           You have a question? The monetary commitment, you  
18 can call it that, but it's something that the corporation  
19 has got to pay.

20           MS. CHATTEN-BROWN: Correct. Yes.

21           JUDGE WILKINS: And so we'd call it fine or mone-  
22 tary commitment.

23           MS. CHATTEN-BROWN: Absolutely.

24           JUDGE WILKINS: But in effect you used both  
25 approaches, monetary commitment and probation?

1 MS. CHATTEN-BROWN: Yes. The corporations prefer  
2 to refer to it as a contribution, although I've, you know,  
3 made it very clear that since it's a condition of probation  
4 the likelihood of their obtaining any tax benefit from that,  
5 of course, we advise them to contact their own tax attorneys  
6 on that, that re very slim, but they prefer the term "con-  
7 tribution" and we've been willing to go along with that.

8 JUDGE WILKINS: All right. Thank you.

9 Questions to my left.

10 COMMISSIONER NAGEL: In your experience has there  
11 been any problem when you implement the terms of probation,  
12 the probationary agreement, has there been a problem with  
13 somehow impeding the normal business practice, that is, with  
14 the probation having a negative effect because it interferes  
15 with otherwise normal business?

16 MS. CHATTEN-BROWN: Not at all. That was one of  
17 the comments that were in the written materials, and I think  
18 the key to that is, you know, working out, obviously, a  
19 reasonable plan, having broad input, there were a lot of  
20 situations in most of the negotiations that I have personally  
21 been involved in that I said, for example, on requiring all  
22 training to be in the language that's spoken by the person  
23 to be trained. That is something that most industries to  
24 my horror, are very, very reticent to commit to; they really  
25 object to that; and yet it's fundamental to safety at the

1 workplace, and so there are some places that we say:

2 "No. I'm sorry. We're," you know, "we're going  
3 back to jail time. If we can't work this out as a condition  
4 of probation, then we will not have an acceptable disposi-  
5 tion. We'll go to Court and we'll argue for the jail time."

6 And in -- But in most of the things, in terms of  
7 the composition of the committee, how often they work, what  
8 kinds of labeling should be on various machines in terms of  
9 warnings, in terms of their procedures on handling hazardous  
10 wastes, et cetera, we receive as much information, as  
11 possible from them, and if they are fortunate enough to al-  
12 ready have a written safety program, in most cases they  
13 don't, but in a few cases they have, or procedures for  
14 handling hazardous materials, we start with that, and then  
15 try to identify, "Where did it break down?" You know, "What  
16 is the problem?"

17 COMMISSIONER NAGEL: Thank you.

18 MS. CHATTEN-BROWN: Mm-hmm.

19 JUDGE WILKINS: Stephen.

20 COMMISSIONER BREYER: Well, I think what you said  
21 is very interesting to me. There is no doubt in my mind  
22 that there should be terms of probation.

23 Our problem is a step beyond that, and maybe, the  
24 more I listen to you and others, the more I am not certain  
25 we can solve our problem.

1           See, our problem is, in addition, what should the  
2 terms of probation say; and our mandate is to try to create  
3 somewhat uniform sentences across crimes. Now when I listen  
4 to you and the gentleman from the FDA and the gentleman from  
5 the EPA it sounds to me as if what is most useful might be  
6 the opposite. That is, it sounds to me is what you --  
7 actually what you do is that you are an intelligent prose-  
8 cutor. You see the case before you. You work out 18 pages  
9 of detail, and, of course, that detail will be crime speci-  
10 fic, and firm specific, perhaps.

11           Now, is that going to be useful to use? Do you  
12 have, or can you -- if you sat down and thought about what  
13 sort of general types of things there are, i.e., general  
14 terms of probation, or general types of circumstances that  
15 might call for certain kinds of terms of probation, is there  
16 such a document? Do you think you could write such a docu-  
17 ment? You think if you got together with the FDA person and  
18 the EPA person that we could produce such a document that  
19 would cut across several crimes? I mean, so far that's why  
20 I am quite interested in what Mr. Monks is going to testify  
21 later on this morning. I hope you'll be around for it;  
22 about the possibility of imposing certain general conditions  
23 on directors, but I put that problem to you, and it may be  
24 your answer is, "Well, Commission, just say, 'Impose proba-  
25 tion', and leave the rest to us." That might be your answer.

1 Or maybe your answer is, "There are certain crime specific  
2 rules which can be general but within an area of crime."

3 Or maybe you think, do you see the type of  
4 problem?

5 MS. CHATTEN-BROWN: Absolutely. Absolutely.

6 COMMISSIONER BREYER: Mm-hmm.

7 MS. CHATTEN-BROWN: I do think that there probably  
8 are, and I am hesitant to recommend any right now, because  
9 I haven't given it the kind of thought or had dialogue, I  
10 would very much enjoy having that discussion with the FDA  
11 and the EPA representatives, --

12 COMMISSIONER BREYER: Mm-hmm. Mm-hmm.

13 MS. CHATTEN-BROWN: -- but my, I think that the  
14 conditions should be tailored, but you can still provide  
15 some general guidelines.

16 COMMISSIONER BREYER: Mm-hmm.

17 MS. CHATTEN-BROWN: The Judges that I have  
18 appeared before have been very pleased that we have worked  
19 it out, --

20 COMMISSIONER BREYER: Yes, of course. Of course.

21 MS. CHATTEN-BROWN: -- because they have said,  
22 you know, --

23 COMMISSIONER BRYER: You'll know more about it.

24 MS. CHATTEN-BROWN: -- "We had no idea what to do  
25 with this Defendant." They are so much out of the main-

1 stream; but certainly if it could be done by categories,  
2 by occupational safety and health, by environmental, and  
3 there may -- those are the two, and consumer, with -- the  
4 three with which I am the most familiar; but certainly in  
5 those areas there are general parameters that could always  
6 be established, and then the specifics adapted to the  
7 specific industry.

8           Going beyond that I suppose there are still some  
9 general principles that would apply to any conditions of  
10 probation, but they, in my opinion, becomes less and less  
11 useful --

12           COMMISSIONER BREYER: Yeah. Right.

13           MS. CHATTEN-BROWN: -- giving guidance to the  
14 Court.

15           COMMISSIONER BREYER: Right.

16           Thank you.

17           COMMISSIONER MACKINNON: Are fines deductible  
18 under the California income tax?

19           MS. CHATTEN-BROWN: No. No, no.

20           COMMISSIONER MACKINNON: When you start talking  
21 about contributions did you ever think of entering into some  
22 agreement that it would not be deductible? I mean, just as  
23 a cost of doing business?

24           MS. CHATTEN-BROWN: Well, I have been advised by  
25 a number of people that most, at least conservative tax

1 attorneys, feel that when it is a condition of probation it  
2 is not deductible, that it will be treated by the IRS in  
3 the nature of a fine and will not be deductible. I have  
4 never checked to see what the various corporations that have  
5 paid those fines have actually tried to do, but I have always  
6 communicated to them to their defense attorneys, what infor-  
7 mation has been provided to us.

8 COMMISSIONER MacKINNON: I had a case about 35  
9 years ago involving a million dollar fee (sic), fine, and we  
10 stipulated that it would not be deducted.

11 MS. CHATTEN-BROWN: That's certainly something,  
12 you know, that we can consider.

13 I've been just as happy since I -- the advice that  
14 I got I thought was from a very good source, and perhaps we  
15 should confirm that, but upon the advice that they wouldn't  
16 be successful, if they want to use that as the sales thing  
17 that's between the defense attorney and the defendants.

18 COMMISSIONER MacKINNON: Thank you.

19 JUDGE WILKINS: Thank you very much. We appre-  
20 ciate your attendance and the testimony that you've given.

21 MS. CHATTEN-BROWN: Thank you.

22 JUDGE WILKINS: I hope we may call upon you in the  
23 future if we have additional questions.

24 MS. CHATTEN-BROWN: Absolutely. I would be de-  
25 lighted.

1 JUDGE WILKINS: Thank you.

2 Let me thank all the witnesses and the Commis-  
3 sioners who, thus far, we've stayed on schedule pretty well,  
4 and I think we'll have a full hearing from every witness if  
5 we continue to adhere to the schedule, reminding witnesses  
6 to please summarize their remarks to ten minutes and then  
7 that will give us a chance to discuss other matters with  
8 you.

9 Our next witness is Mr. Robert M. Latta. He's  
10 the Chief United States Probation Officer for the Central  
11 District of California.

12 Bob, we'd be delighted to hear from you at this  
13 time.

14 I think with Mr. Latta is Alan MacLean, who is the  
15 Deputy Chief United States Probation Officer. We are de-  
16 lighted to have both of you here at the witness table.

17 And, Bob, let me express once again publicly how  
18 much this Commission appreciates you and your officers'  
19 assistance, not just today, but for the last three years,  
20 and you've made your contributions to the work of this  
21 Commission, and we appreciate it very much.

22 MR. LATTA: Thank you.

23 I'd like to return that compliment and thank the  
24 members of the Commission and all its staff for the training  
25 support and computer assistance. Let you know that that's



1    been very helpful to us.

2                   The other thing I would like to say, it is extreme-  
3    ly unusual to attend a meeting where any prosecutors are  
4    present and hear great words about the use of probation as  
5    any kind of an effective criminal sanction.

6                   (Laughter.)

7                   MR. LATTA:  So, I already feel quite at home.

8                   Another thing I would like to say, however, and  
9    let the Commission know this in a positive spirit, that we  
10   do find the guidelines generally complicated to apply, so  
11   whatever the Commission can do in your deliberations to  
12   simplify the guidelines will not only help the Probation  
13   Officers throughout the country, but I think it will improve  
14   the reliability of the information received by the Court and  
15   the Commission.

16                   And in that view, at the present time, my pro-  
17   fessional staff is 20 percent under their allotted entitle-  
18   ment.  Because of the pay of U. S. Probation Officers in  
19   this District, it's not competitive with the county and  
20   state, and I can't hire qualified people to do this job.

21                   Many of my positions have been vacant for 18  
22   months, and I would be less than candid if I told you that  
23   we could do the job you're asking us to do as required, so  
24   that when you get down to that level in terms of how we are  
25   going to implement this, that's not going to be easy.  It's

1 not easy now, and it won't be in the future.

2 But, putting that aside, I would like to -- my  
3 comments will relate to the role of the Probation Service  
4 in carrying out the goals or organizational probation.

5 Your materials describe two basic goals to support  
6 monetary sanctions and to prevent repetition of criminal  
7 activities, and within that you list three basic applica-  
8 tions.

9 Overall, it would appear that the proposed mone-  
10 tary sanctions, together with probation as an independent  
11 sanction should greatly improve the criminal justice system's  
12 ability to deal more effectively with illegal behavior on  
13 the part of organizations.

14 In the past, monetary sanctions were often in-  
15 adequate and this fact alone caused Courts, throughout the  
16 country, to fashion some of the creative sentences described  
17 in your discussion materials.

18 The Judge's in the Central District of California  
19 have come up with their share of sentences which would have  
20 more meaning than a mere slap on the wrist, but might be  
21 in conflict with the way the job is usually done.

22 The traditional job of Probation Officers are to  
23 investigate individuals referred to the Court and to aid  
24 the Court in fashioning an appropriate sentence. In addi-  
25 tion, we're supervising individuals in the community at the

1 direction of the Court or paroling authority.

2 The education and training of Probation Officers  
3 prepares them to work with people on a one-to-one basis.  
4 Federal Probation Officers, perhaps, are more experienced  
5 in supervising organizations than are their counterparts at  
6 the local level because of the nature of Federal crimes;  
7 however, their degree of competence is the result of on-the-  
8 job experience rather than formal training.

9 Even though individual officers do a creditable  
10 job of supervising organizations, the Probation Service, as  
11 a whole, isn't equipped to give effective supervision to  
12 complex business organizations.

13 When the intention of the Court is to enforce  
14 restitution, provide notice to victims, satisfy forfeiture  
15 agreements, we can do that job and collect installment fines.  
16 Then we have the know-how to do that.

17 When community service is seen by the Court as an  
18 appropriate sanction, this can be coordinated by the Proba-  
19 tion Officer; however, staff assistance from the convicted  
20 organization will be needed to work with the Probation Offi-  
21 cer.

22 When appropriate, the staff could be an employee  
23 of the organization, itself, or, if not, someone compensated  
24 by the organization to work with us.

25 There are currently many examples of this kind of

1 arrangement throughout the Federal Courts.

2           The remaining two basic applications of organiza-  
3 tional probation appear to me to require the use of an  
4 expert if the organization is at all complex.

5           In situations where an expert is used during the  
6 period of supervision that expert should work through the  
7 Probation Officer and not independently of him. The persons  
8 monitoring reports and other written materials should be  
9 submitted to the Probation Officer, who then reports to the  
10 Court.

11           Your discussion materials also speak to the  
12 appointment of a person other than the Probation Officer  
13 to prepare the presentence report in accordance with 18  
14 U.S.C. 3552.

15           Section 3552(a) specifies that U. S. Probation  
16 Officers shall make a presentence investigation.

17           Sections 3352(b) and (c) seem to me to refer to  
18 psychological or psychiatric examinations rather than an  
19 organizational presentence investigation.

20           The present investigative expertise of Probation  
21 Officers should be sufficient to provide the Court with  
22 information necessary to properly sentence a corporation.  
23 Prior to sentencing most individuals, as well as corpora-  
24 tions, tend to be more forthcoming with information. It is  
25 after sentencing and during supervision that we'll need

1 expert assistance in complex cases.

2 One of the central aims of the guidelines is to  
3 encourage voluntary compliance; and you indicate it is  
4 anticipated that the corporation will normally take a lead-  
5 ing role in proposing the conditions and internal controls  
6 that should be imposed. In my opinion, this is an overly  
7 optimistic view.

8 Another area of concern is the expected level of  
9 coordination among the civil and criminal authorities in  
10 this process. I can't speak to the level of coordination  
11 prior to sentencing; however, once a sentence of probation is  
12 imposed, continued coordination is the exception and not the  
13 rule. This is in spite of good intentions. I feel this is  
14 because of the burden of work, and staff turnover mitigate  
15 against this kind of continued cooperation.

16 As a final concern, I found that when a corpora-  
17 tion and an individual officer are both placed on probation  
18 the level of compliance to the orders of the Court are signi-  
19 ficantly enhanced. In my experience, it is not unusual for  
20 a corporate defendant to quickly declare bankruptcy and that  
21 ends our participation.

22 Again, I want to thank the group for allowing me  
23 to speak, and we're here to answer any questions you have.

24 JUDGE WILKINS: Thank you, Mr. Latta.

25 In the case where you say a complex problem, per-

1 haps, or a major corporation is under your supervision, you  
2 would need assistance from an expert of some type who has  
3 worked with you, or through you. I assume the corporation  
4 would pay for the services of an expert?

5 MR. LATTA: As indicated in your --

6 JUDGE WILKINS: Would that be in addition to any  
7 monetary sanctions imposed?

8 MR. LATTA: Yes, sir.

9 JUDGE WILKINS: All right, sir.

10 MR. LATTA: Definitely.

11 JUDGE WILKINS: Okay.

12 Questions to my right?

13 COMMISSIONER BLOCK: Yes, sir.

14 I have a related but not specific question on your  
15 testimony.

16 In going over the presentence reports for organiza-  
17 tions when I was in the process of looking at a number of  
18 these cases, one thing struck me, and that was that there's  
19 a much lower proportion of presentence reports for organiza-  
20 tions than are for individuals. Nearly every individual has  
21 a presentence report, but probably not much over half in the  
22 organizations, though.

23 What is the reason for that?

24 MR. LATTA: I think part of the reason is because  
25 the sanction was felt to be so limited on the part of the

1 Court that there was really no reason going into great de-  
2 tail. When they just had a corporation, and no individual  
3 with it, then what was the point in referring the matter to  
4 us for any sort of investigation?

5 COMMISSIONER BLOCK: Mm-hmm.

6 MR. LATTA: Now, the law has changed, and I think  
7 what you're doing here will influence that in the future.

8 COMMISSIONER BLOCK: Has it changed, the '84 law  
9 changed sanctions significantly, as well as the '87 law.  
10 Has there been some change in the proportion of presentence  
11 reports, the new law cases, or, at least, the intermediate  
12 law cases, the '84? '84 to '87?

13 MR. LATTA: I really would hesitate to say that.  
14 I can't give you a meaningful answer. I would look at it  
15 and see; but I think there is more general interest overall.  
16 Perhaps the U. S. Attorney's Office could reflect more on  
17 that.

18 COMMISSIONER BLOCK: Mm-hmm.

19 MR. LATTA: It takes a while for this to get into  
20 the Court system, and as indicated, it takes a while for  
21 these matters to get to Court.

22 COMMISSIONER BLOCK: Thank you.

23 JUDGE WILKINS: Commissioner Corrothers.

24 COMMISSIONER CORROTHERS: Good to see you again,  
25 Bob. I wouldn't mind if we met with you in this lovely

1 state for each and all of our public hearings.

2 MR. LATTA: I think this is misleading in terms  
3 of the way we're doing the job.

4 (Laughter.)

5 JUDGE WILKINS: I say, they ought to see your  
6 offices. It's nothing compared to this; is that right?

7 COMMISSIONER CORROTHERS: But, beyond that, I  
8 think I just have a comment that because we've had a  
9 literal flood of support for the imposition of organization-  
10 al probation your testimony is timely and sorely needed on  
11 the role of the Probation Officer. I think that -- So we  
12 thank you for that; and we may be contacting you in the  
13 future as we continue our effort in this area.

14 Beyond that, I wish you luck in your recruitment  
15 efforts. I see it's not getting any better than when I was,  
16 was out West.

17 MR. LATTA: Thank you.

18 JUDGE WILKINS: Questions? Stephen?

19 COMMISSIONER BREYER: Well, I think you ought to  
20 get involved with the Criminal Division's effort there, too,  
21 and in particular if the EPA and FDA are. I mean, I agree  
22 with Commissioner Corrothers. You see what you point out  
23 is you have limited resources, and you are all the ones who  
24 get very much involved in administering the probation, and  
25 you are the moment struggling with, really, what was our



1 main job, which is the sentencing guidelines for individuals.  
2 That's a big drain on your resources.

3 And from the institutional perspectives of FDA and  
4 EPA, and the SEC, for that matter, who deal with large  
5 corporations, they would like to use the criminal law as a  
6 regulatory program in part. It would help them.

7 Well, fine, if they're going to do it; but if you  
8 are going to be the ones to do it, I don't know where you  
9 are going to get that manpower and expertise, and I think  
10 it would be useful for you to talk to the Criminal Division,  
11 and the people in these, what I would call the regulatory  
12 agencies, to make certain that something doesn't evolve  
13 that's too complex for us to work out in practice.

14 I mean, again, I think we see the need for some  
15 form of probation. I think we don't see, at least, I don't  
16 see what the specific recommendations are going to be in  
17 these regulatory areas other than the general kind of  
18 recommendation:

19 "Well, Judge, if you feel this calls for proba-  
20 tion, fine. Give him probation and work out the details  
21 with the help of the prosecutor."

22 That's -- So you can get involved. I mean, you  
23 were going to stay involved with these other Agencies, were  
24 you? That's what I most --

25 MR. LATTA: Right.

1           COMMISSIONER BREYER: That's why I bring this up.  
2 Good.

3           COMMISSIONER MacKINNON: You usually get a sen-  
4 tence on a crime one one count, a criminal sentence, and on  
5 another count on probation, don't you?

6           MR. LATTA: Now you're talking about a corpora-  
7 tion?

8           COMMISSIONER MacKINNON: Yes. Or --

9           MR. LATTA: With an individual and --

10          COMMISSIONER MacKINNON: Well, individuals or  
11 corporations or anybody, doesn't --

12          MR. LATTA: Well, that's, of course --

13          COMMISSIONER MacKINNON: Doesn't the United States  
14 Attorney usually hold enough counts, at least two counts  
15 so that you get a criminal sentence on the first count, and  
16 you suspend the imposition of sentence on the second county,  
17 and impose probation.

18          MR. LATTA: Not necessarily. No, sir.

19                 That would be --

20          COMMISSIONER MacKINNON: Are you restricted, do  
21 you think?

22          MR. LATTA: I think in many cases we're restricted,  
23 yes; to one count.

24          COMMISSIONER MacKINNON: And that, that restricts  
25 you to probation?

1 MR. LATTA: Well, it restricts the whole criminal  
2 sentence.

3 COMMISSIONER MacKINNON: Yeah. And that's the  
4 part --

5 MR. LATTA: Yes, sir.

6 COMMISSIONER MacKINNON: That's the failure of the  
7 Department of Justice and the United States Attorney; isn't  
8 it?

9 MR. LATTA: Well, I don't know it's necessarily  
10 a failure, but that's the result, is a one-count conviction.

11 COMMISSIONER MacKINNON: Well, I was United States  
12 Attorney for a long time and I always gave the Judge maximum  
13 authority to impose a fair sentence, and that generally was  
14 impose a criminal sentence, and a second one where he could  
15 impose a probationary sentence and the suspension of sen-  
16 tence.

17 MR. LATTA: Well, see, that's something that you'd  
18 really have to discuss with the Department of Justice.

19 We see the results, we're not -- we don't parti-  
20 cipate in the -- how you get there.

21 COMMISSIONER MacKINNON: And you are restricted by  
22 being restricted to one count?

23 MR. LATTA: In some cases, yes. Not in all cases.

24 COMMISSIONER MacKINNON: Yes.

25 Thank you.

1 JUDGE WILKINS: Thank you very much.

2 Again, thank you both for coming, and your  
3 participation, not just today, but over the past few years;  
4 and I'm glad to hear that the word processors are being  
5 of some assistance to you.

6 MR. LATTA: Thanks, Judge.

7 MR. MacLEAN: Thank you.

8 JUDGE WILKINS: Good.

9 Rusty has probably got several he'll give you on  
10 your way out, Bob, if you --

11 (Laughter.)

12 THE REPORTER: May we have a tape change, please?

13 JUDGE WILKINS: Yes, sir.

14 (Tape change.)

15 THE REPORTER: We're on the record.

16 JUDGE WILKINS: Thank you.

17 Our next witness is Mr. Robert A. G. Monks.

18 He is the President of Institutional Shareholders  
19 Services.

20 Mr. Monks has communicated with the Commission a  
21 few weeks ago, and as a result of that he is listed as a  
22 witness.

23 Is Mr. Monks present?

24 Yes, sir. Come around, please.

25 MR. MONKS: Good morning.

1 JUDGE WILKINS: Good morning.

2 MR. MONKS: I am very glad of the chance to appear  
3 before you today and thank you for making it possible.

4 I apologize for not having been able to get my  
5 written testimony in your hands before probably 30 seconds  
6 ago, but I think under the circumstances I feel quite well  
7 at 48 hours' turnaround time.

8 Now, I think I should introduce myself to you in  
9 order that you can the most appropriately evaluate what it  
10 is I have to say.

11 I have a, in view of my age, a fairly long back-  
12 ground; but I am a practicing lawyer, indeed, today is the  
13 beginning of my fourth decade as being entitled to appear  
14 before the Supreme Judicial Court of the Commonwealth of  
15 Massachusetts.

16 I have been a businessman in a variety of different  
17 capacities. I've been Chief Executive Officer of a number  
18 of corporations. I am now a director of a number of corpo-  
19 rations.

20 I, most recently, was chairman of the board of a  
21 bank holding company of a bank in Boston, called The Boston  
22 Company.

23 And I have, also been a public official. Most  
24 cogently to your own circumstances, those of you at least  
25 on the Federal payroll, I am a Trustee of the Federal

1 Employee Retirement System, and I administer the investment  
2 of those funds.

3 And I have been the Administrator Assistant  
4 Secretary in charge of running the ARISA Program, which is  
5 the portion of the Department of Labor that regulates the  
6 private pension system.

7 In all of these guises in the last 20 years I have  
8 been particularly interested in the questions of corporate  
9 governance; and it is from those various perspectives that  
10 I prepared my testimony for you and would like to make a  
11 few summary remarks, if that's convenient.

12 I'd like to start, perhaps you'd indulge me in  
13 view of it being a special day for a Massachusetts practi-  
14 tioner by quoting several sentences from one of our more  
15 distinguished lawyers from the Commonwealth, former Supreme  
16 Court Justice Louis Brandeis.

17 "A shareholder may be innocent in fact but  
18 socially he cannot be held innocent. He accepts the bene-  
19 fits of a system. It is his business and his obligation  
20 to see that those who represent him carry out a policy  
21 which is consistent with the public welfare. If he fails  
22 in that so far as a shareholder fails in producing a result  
23 that shareholder must be held absolutely responsible,  
24 except so far as it shall affirmatively appear that the  
25 stockholder endeavored to produce different results and

1 was overridden by a majority."

2 Mr. Chairman, what I want to call to your atten-  
3 tion today is that in the United States, at the present  
4 time, fiduciary institutions own approximately 50 to 70  
5 percent of the total outstanding stock. These are insti-  
6 tutional -- these are fiduciaries who are accountable under  
7 various, usually Federal laws. Under ARISA about 25 per-  
8 cent; by far the largest shareholder. Under the Federal  
9 Reserve and the Controller of the Currency are the various  
10 bank fiduciary obligations under the SEC are the Mutual  
11 Fund and Investment Company obligations; so when you talk  
12 about owners of corporations in America today, you're  
13 talking, for a change, about a fairly small group. You're  
14 talking about hundreds, and not very many hundreds of people  
15 who are not just ordinary people, they are trustees with  
16 duties that can be understood in terms of traditional trust  
17 concepts.

18 The firm that I have started, ISS, is organized  
19 in order to advise these large institutions on their re-  
20 sponsibilities as owners; and the thrust of our work as  
21 far as it relates to the Sentencing Commission, and the  
22 reason why I wrote you was that I had hired a former head  
23 of the Criminal Division, William Weld, to give me some  
24 advice as to what we could do in terms of governance repre-  
25 senting people who were owners to tell the people who worked

1 for them, the corporate officers, that they do not want  
2 their corporation -- "their" being the shareholders'  
3 corporation, to be run in a way that permits criminal  
4 activity.

5 And it, in effect, says:

6 "To the extent that you view criminal activity  
7 as being susceptible to cost benefit evaluation, don't do  
8 it. We want you to observe the law of the land, and we  
9 put the burden onto you."

10 My suggestion is relatively simple. It is that  
11 in considering sentences there should be taken into account  
12 the extent to which a corporation through its internal  
13 governance processes has taken on the responsibility at the  
14 highest level to forestall criminal activity.

15 To put it in the vernacular, what I am suggesting  
16 is that the directors bet their jobs on it; and my specific  
17 proposal has been, and I got before you, I wrote you, and  
18 I think in my testimony you'll find letters that we've sent  
19 out in the last month, as it were, to the Chief Executive  
20 Officers of a number of American corporations, saying to  
21 them:

22 "Look! You really should take on, as a governance  
23 matter, this responsibility. The buck stops somewhere. It  
24 should stop on you, the directors, and you should have a by-  
25 law that conditions eligibility to serve as a officer or a



1 director of a company on, first of all, an individual  
2 freedom from having committed particular kinds of crimes;  
3 but, secondly, that they should not be eligible if during  
4 the period of their service acts occur which constitute  
5 particular kinds of criminal activity."

6 And I am frank to say that I defer to Bill Weld  
7 in the drafting of various bylaw provisions, that we're  
8 not trying to go to an absurd extent.

9 We're talking about the kinds of criminal activity  
10 in which there is a knowledge, there is, what should I say?  
11 I'll just call them heinous crimes, if you'll excuse me in in-  
12 exactness.

13 It is our view, it has been my experience that  
14 fines are really relatively in apposite concept with very,  
15 very large corporations. You know, in a day like today  
16 when you see that R. J. Reynolds got bought in an LBO it  
17 really does cause you to think about, "What does money  
18 mean to a large corporation?"

19 To be perfectly direct with you, it doesn't mean  
20 anything. I mean a million dollars, two million dollars,  
21 a hundred million dollars to a large corporation doesn't  
22 really have significance. I mean, it is not related to its  
23 value.

24 Many American corporations today could run without  
25 capital, which is what we have seen in this LBO phenomenon.

1 So the notion of imposing a dollar-fine on a large corpora-  
2 tion it simply doesn't attack the person who is a position  
3 to be able to do something about criminal activity. And,  
4 of course, at the very least it imposes a burden on people  
5 I refer to in a presumptuous way as "my pensioners", dating  
6 from the time that I was the Government official responsible  
7 for them.

8 I think in terms of judicial supervision of  
9 corporate activities for periods of time that my experience  
10 with large organizations is that they tend to sort of in  
11 a biological way manufacture counter-bodies.

12 That if you have, say, 12 people who come in to  
13 investigate a corporation, the corporation will generate  
14 24 people who will provide the appropriate information for  
15 those people, and keep them happy, and send them out the  
16 door.

17 So, to my way of thinking, and from a governance  
18 point of view, this is a critical point for myself, because  
19 if we can't, if owners can't ensure that corporations  
20 function in a way that is at least as congenial to society's  
21 goals as to abstain from heinous criminal activity, what's  
22 the legitimacy of corporations?

23 Thank you very much.

24 JUDGE WILKINS: Thank you very much.

25 The points you make are very interesting.

1           How can sentencing affect this goal that you would  
2 suggest?

3           MR. MONKS: Well, if you took a hyperbolic view,  
4 which as you've probably gathered, I'm not allergic to,  
5 what you'd say is, in considering sentencing, that you would  
6 be inclined on the scale to go on the harsher side, to the  
7 extent that there is no indicated competency or willingness  
8 by the corporation to govern itself, and that you would be  
9 inclined to the lenient side of the scale to the extent that  
10 the corporation has, in effect, taken responsibility.

11           I mean, a corporation is a structure that can  
12 organize information and penalties the way it wants to,  
13 and to the extent that a corporation says, I'm thinking  
14 way, way, way back to the GE case in the late '50s, where  
15 they actually sent some people to jail, that there the  
16 information flow was organized in such a way that the  
17 directors simply never got the information. Well, it is  
18 within the power of the directors to organize incentives  
19 so that information goes as they want it to go, and so by,  
20 in effect, putting the directors' job on the line, you are  
21 creating a value system within the corporation that says,  
22 "We want to know about it and we want you to take steps to  
23 stop it, and it is more important to stop criminal activity  
24 than it is to maximize profits; and if you don't like the  
25 law, you can go and lobby before the Legislature and change

1 the law, but don't take it into your own hands to decide  
2 what is acceptable social conduct. Obey the law."

3 JUDGE WILKINS: But if the corporation is organized  
4 such that intentionally the information flow does not reach  
5 the top floor, what can the Court do to sanction that  
6 corporation, as far as the directors are concerned?

7 MR. MONKS: Well, it would, of course, depend if  
8 it was before the fact or after the fact; but I think that  
9 if you have it, as I understand your mandate, to the extent  
10 that the word goes out that people who are going to sentence  
11 are going to consider when they do sentence the extent to  
12 which direct corporations have adopted appropriate governance  
13 mechanisms, I think that would be very useful.

14 I mean, when I send letters out to the corpora-  
15 tions, as you've seen, the ones I have sent out today, in  
16 my testimony, the answers I get are somewheres defensive and  
17 hostile.

18 I mean, people, they, the chief executives of  
19 corporations don't associate with criminal activity, at  
20 least not "the Great American Corporations". I mean, they  
21 don't, you know, they may overcharge for oil, but they  
22 don't think that's a crime.

23 And you tell them:

24 "Well, the law says it's a crime."

25 And, you know, he says:

1 "Well, I don't really think it's a crime."

2 There's no sort of connection between an activity  
3 and a criminal intent by the CEO; so I think what you can  
4 do in terms of sentencing is to make it very clear that to  
5 the extent that a crime, in fact, is committed, that the  
6 sentence will be very, very much related to the extent to  
7 which the corporation, itself, has taken on responsibility.

8 And I think that if that's part of your pleasure  
9 and your conclusion that the word will go out and that then  
10 there will be bylaws adopted, and there will be a taking-on  
11 of responsibility.

12 JUDGE WILKINS: I see. I see. Very good.

13 Thank you.

14 To my right.

15 COMMISSIONER BLOCK: Yes. Thank you very much,  
16 Mr. Monks. That's certainly very interesting testimony,  
17 and I appreciated the letters to the Board members.

18 A couple of things that, points that you made are  
19 interesting and I would like to follow those out, so bear  
20 with me.

21 The first comment that you made which boggles my  
22 mind is that money doesn't matter to big corporations. What  
23 do you really mean by that? I mean, I guess I have a hard  
24 time putting that in context.

25 MR. MONKS: Well, I do, too. You know, it really

1 is -- it's so anomalous, it's almost like saying that light  
2 is black.

3 It's really a result of seeing a number of phe-  
4 nomenon that seem to me to be very different now than they  
5 always used to be.

6 One of them is this: Virtually nothing, in this  
7 country, at least, fails to be done by business corporations  
8 because of an absence of cash.

9 I mean, how long ago has it been since you heard  
10 that a project didn't get done because there was no money?

11 When somebody does, when a company has been  
12 running for 50, 100 years, and all of a sudden somebody  
13 comes along and borrows all the money and buys it up at 50  
14 percent over the previous stock price what does that tell  
15 you about the relevance of accumulating earnings over the  
16 previous 50 years? It has nothing to do with value.

17 In other words, value of companies is their  
18 capacity as an organization to generate profits, and it has  
19 virtually -- the amount of cash they have, the amount of  
20 assets that they build up are not really related to value  
21 unless you have a, you know, a sale at bankruptcy or at an  
22 auction in which, you know, you distribute the cash as cash;  
23 but almost invariably in valuing a business as a going  
24 enterprise the amount of cash in the enterprise is virtually  
25 irrelevant to value.

1           COMMISSIONER BLOCK: Let me, sir, now take what  
2 I think to be this disposition, a little further; and that  
3 is, your suggestion that boards of directors put their  
4 seats on the line.

5           MR. MONKS: Right.

6           COMMISSIONER BLOCK: The criminal line.

7           Okay. You have on one hand the fact that somehow  
8 cash doesn't matter, and you place the board of directors  
9 now in a position where any serious criminal activity will,  
10 that's conducted while they're on watch will, in fact, re-  
11 sult in their removal.

12          MR. MONKS: Diseligibility.

13          COMMISSIONER BLOCK: Diseligibility.

14          MR. MONKS: Right.

15          COMMISSIONER BLOCK: Will that fact be in the  
16 interest of the shareholders?

17          Now, as you represent, --

18          MR. MONKS: Yes.

19          COMMISSIONER BLOCK: -- shareholder, if it is a  
20 consulting firm that represents shareholders, and I guess  
21 I, what I don't, I'm not clear on is whether such a re-  
22 striction in the bylaws would be in the interest of share-  
23 holders.

24          I mean, there's a real Agency problem if the  
25 directors don't care about money; they'll spend anything to

1 protect themselves; and in that sense share prices will go  
2 down as they spend too much finding out things about be-  
3 havior of the corporation.

4 I have a hard time reconciling your testimony  
5 with your position of being consultant to shareholders. It  
6 sounds to me like you're recommending to us:

7 "Well, just do this and if share prices decline,  
8 well, so be it. The law is respected."

9 MR. MONKS: Yes, I can see how I might have  
10 created a certain amount of confusion. Let me try and --

11 COMMISSIDNER BLOCK: I am just trying to under-  
12 stand.

13 MR. MONKS: Let me try and address that directly.

14 My own concern and my own calling, as it were,  
15 for this line of work, is that I believe that large economic  
16 institutions, like corporations are in the public interest,  
17 but that it is important that they should have a long-term  
18 viewpoint, and one of the elements of a long-term viewpoint  
19 is that they now do have permanent shareholders in these  
20 institutions. They don't act like it, but they are, after  
21 all, people who are going to be shareholders there for a  
22 long time. They are beneficiaries or pensioners, and by  
23 and large pensioners are people, I think, who care for not  
24 only getting a dollar when they retire that buys a dollar's  
25 worth of merchandise, but they're also interested in living



1 in a clean country, they're interested in a law-abiding  
2 country, they're interested in living in a country presumab-  
3 ly administered by Americans and not by Russians, or any-  
4 body else; so, my view is that one of the things that my  
5 shareholders who are long-term people can do is to under-  
6 stand that their large enterprise is a fundamental part of  
7 the quality of the civility of the society, and that it is  
8 far more important to them in the long-run that they be in  
9 a law-abiding country than it is in the short-run that they  
10 make 5 cents more a share, and because my people are fidu-  
11 ciaries I feel that this is a decision they can appropriately  
12 make for people who have an interest in the long-run.

13 COMMISSIONER BLOCK: Okay. So they have laws to  
14 reconcile, in terms of retirement funds; what this approach  
15 implies is that going forward this way may be in the economic,  
16 not the economic self-interest of the pension-holders, but  
17 by some view of the public interest it's better that we  
18 proceed in this manner; is that --

19 MR. MONKS: Well, there's --

20 COMMISSIONER BLOCK: So there's nothing, I --  
21 what I am trying to get from this is there, is there sort of  
22 like a logical basis for this as opposed to an ethical  
23 basis. I guess what I've, I've come away from now is  
24 essentially you've said:

25 "Well, there's an ethical basis for this."

1 I mean, and you can't establish whether there is  
2 a logical basis for holding the directors responsible in  
3 this manner.

4 MR. MONKS: There may be a missing link, and maybe  
5 it's this:

6 People like to be directors. In other words,  
7 directors like to continue service.

8 I think there may be a recorded case where some-  
9 one voluntarily stopped being a director, but I don't  
10 recall when it was. I mean, it's good work if you can get  
11 it; and so the self-interest here is that a director wants  
12 to continue to be a director, he doesn't want to have  
13 conduct in the corporation that will diseligibalize him,  
14 therefore, he, acting in his self-interest, will cause  
15 there to be a compliance with the law; --

16 COMMISSIONER BLOCK: But --

17 MR. MONKS: -- and, as far as I can see, no  
18 economist, I mean Milton Friedman says that the only purpose  
19 of corporations is to maximize shareholder values within the  
20 rules.

21 Now, what I'm saying is, is that it is beyond the  
22 power, it is inappropriate for corporation officials to make  
23 a determination that it is cost-effective to disobey the  
24 law; and it isn't as if they had it in their power to do as  
25 you are suggesting. It isn't as if that is an appropriate

1 choice for them. It isn't theirs', --

2 COMMISSIONER BLOCK: Well, no, I mean, no, no.

3 MR. MONKS: -- to make that choice.

4 COMMISSIONER BLOCK: Wait a minute. That's a  
5 "purple herring".

6 MR. MONKS: I beg your pardon?

7 COMMISSIONER BLOCK: That's a "purple herring".

8 MR. MONKS: A "purple herring".

9 COMMISSIONER BLOCK: It's a "purple herring" in  
10 the following sense, it's not free to obey the law if you  
11 are a director, in your firm, in the sense that you have to  
12 spend something on compliance programs. It's not free to  
13 get that information.

14 I mean, that's what bothers me about your sugges-  
15 tion is the inability to defend the optimality of the  
16 directors being responsible in the following sense.

17 I agree with you that it appears as if people want  
18 to be directors. The reason question is: Will they squan-  
19 der resources under your regime? Do they want to do that  
20 so much that they in a sense squander the resources of the  
21 residual claimants, protecting their directorships. That  
22 seems to me to be an important problem.

23 MR. MONKS: I think it's a legitimate question.

24 COMMISSIONER BLOCK: Because you can't waive  
25 your answer.

1 MR. MONKS: I think it's a legitimate question.  
2 I'd like to have the experience available to be  
3 able to answer it, but I think without it conceptually it  
4 has merit.

5 COMMISSIONER BLOCK: Thank you.

6 JUDGE WILKINS: Commissioner Corrothers.

7 To my left.

8 COMMISSIONER CORROTHERS: I just want to say that  
9 I think the idea is a marvelous one, and I would like to  
10 encourage you and to do anything I can to help promote it,  
11 too.

12 MR. MONKS: Thank you. I accept.

13 JUDGE WILKINS: Stephen.

14 COMMISSIONER BREYER: I'd say, first, I'd like  
15 to thank you very much for coming out here and preparing  
16 this on such short notice, and I agree, it's a very  
17 interesting proposal, and I think perhaps practical.

18 I have a suggestion: I'd like you to -- Well, my  
19 suggestion is basically I'd like you to, if you would be  
20 willing to, to get Mr. Well, possibly, to talk to  
21 Ms. Chatten-Brown, or the equivalent.

22 This is why I say that, --

23 MR. MONKS: Mm-hmm.

24 COMMISSIONER BREYER: -- your proposal, it solves  
25 a fairly good-sized problem, in my mind.

1 I mean, what is the reason, why do people indict  
2 corporations? It seems like a cop-out. If there's a crime,  
3 there's an individual who committed the crime. Go indict  
4 that individual. The individual who committed the crime  
5 may applaud when the prosecutor indicts the corporation,  
6 because what does he care about the corporation? You know,  
7 he's free.

8 All right. Now the response to my question is:  
9 Well, we indict corporations sometimes to get ahold of the  
10 assets and also because we want to encourage them to spend  
11 money to stop crime within their company. Okay.

12 So, if we're focusing on that we're probably  
13 focusing on environment, we're focusing on drugs, we're  
14 focusing on, maybe, large defense procurement, maybe anti-  
15 trust. We're not focusing on the situation where a  
16 corporation is the cat's paw for the criminal. I mean, you  
17 know, he has this fly-by-night.

18 We're not focusing on the closed corporation. We  
19 are focusing on the large, publicly-held corporation which  
20 is, in a sense, a brave new world because it's a brave new  
21 world in criminal law federally only since the change in Fine  
22 Act; and we're not going to get a lot of experience there.

23 All right. You now come in with the proposal that  
24 sounds as if it might be somewhat general, and it goes right  
25 to the heart of putting a big incentive on a person who is

1 responsible in the company, because, believe me, nothing  
2 concentrates the mind quite so much as when you think,  
3 "My job is at stake." That does have quite a lot to be  
4 said for it.

5 MR. MONKS: That's right.

6 COMMISSIONER BREYER: What I wonder is, if you  
7 could get, perhaps, Mr. Weld, together with some of the  
8 other people, to work out what I would see as a number of  
9 practical details.

10 That is, if we were to put it in a guideline when  
11 should it go in? When?

12 MR. MONKS: Mm-hmm.

13 COMMISSIONER BREYER: What crimes? And what crimes  
14 in respect to how they were committed or not?

15 I mean, where I see immediate dilemma, I think,  
16 "Okay. If we were to say this was always..." --

17 MR. MONKS: Mm-hmm.

18 COMMISSIONER BREYER: -- "...a necessary punish-  
19 ment" then I wonder about her corporation, because she seemed  
20 as if she had a corporation which had committed a number of  
21 safety violations, and she wanted to get the cooperation  
22 of management, and she might have indicted those managers,  
23 i.e., she might have indicted the corporation, --

24 MR. MONKS: Mm-hmm.

25 COMMISSIONER BREYER: -- so that she could produce

1 a program in her 18 pages that would have brought that  
2 corporation under control from the point of view of safety.

3 MR. MONKS: Mm-hmm.

4 COMMISSIONER BREYER: Now, to get that worked  
5 out, she might need those managers; or she might need some  
6 of them.

7 MR. MONKS: Yeah. Right.

8 COMMISSIONER BREYER: And yet your plan might say,  
9 "Okay. As soon as she brings the indictment, they're all  
10 gone, because they've had to quit."

11 MR. MONKS: Mm-hmm. Mm-hmm.

12 COMMISSIONER BREYER: And, no, that isn't an in-  
13 superable problem by any means.

14 What that simply means is that there are techni-  
15 cal details in terms of discretion or when or where and how,  
16 et cetera, this might come into play as a penalty that would  
17 have to be worked out before it actually got written into  
18 language that Courts might tend to see as guiding. So I  
19 hope very much you'll continue this.

20 MR. MONKS: If the Commission is interested in our  
21 doing that, --

22 COMMISSIONER BREYER: Mm-hmm. Yeah.

23 MR. MONKS: -- I would retain Mr. Well, and I  
24 will try to provide you with such.

25 COMMISSIONER BREYER: Yeah. Yeah.

1 JUDGE WILKINS: Good. Thank you.

2 George.

3 COMMISSIONER MacKINNON: Do you really that share-  
4 holders are effective policemen?

5 MR. MONKS: I think that as Justice Brandeis said:

6 "There is no innocent shareholder."

7 And I think that a fiduciary shareholder has an  
8 enforceable obligation, and I think that, therefore, in  
9 order to retain his position as a fiduciary he will take  
10 such steps as are necessary.

11 COMMISSIONER MacKINNON: Now, wait a minute.

12 You're saying the shareholder is a fiduciary?

13 MR. MONKS: I'm saying that, yes. About 70 per-  
14 cent of the shareholding in America today is held by  
15 fiduciaries.

16 COMMISSIONER MacKINNON: Well, you're talking  
17 about their ownership being a fiduciary ownership.

18 MR. MONKS: That's correct.

19 COMMISSIONER MacKINNON: Not that they are, have  
20 any fiduciary relationship with respect to the corporation  
21 in which they own stock?

22 MR. MONKS: That is correct.

23 COMMISSIONER MacKINNON: Well, --

24 MR. MONKS: I think their only power, Your Honor,  
25 is obviously to elect directors, and what I am saying is



1 that to the extent that fiduciaries collectively own a  
2 majority of a corporation it seems to me that it is not a  
3 vast act of common sense to think that those directors  
4 might act in concert, and that as fiduciaries that they  
5 should take on the responsibilities of ownership.

6 COMMISSIONER MacKINNON: Well, I have followed a  
7 lot of the litigation in the name of shareholders throughout  
8 the United States in large corporations for roughly 60  
9 years, and the cases are few and far between. You are not  
10 making a new suggestion that shareholders have rights which  
11 they can enforce, but generally they don't know enough about  
12 what is going on, and neither has achieved some success.  
13 But I think in the overall total you would agree that it is  
14 minimal compared to what is out there. Wouldn't you?

15 MR. MONKS: Your Honor, the 50, the 60-year period  
16 of your service coincides, as it were, with the Burley and  
17 Meins work in this area and the separate of ownership and  
18 control, and I think that what may have happened now is with  
19 the ARISA Statute in '74, and with the reinstitutionaliza-  
20 tion of ownership you may now have got to the point where  
21 it is practical to look to owners, as there may be few  
22 enough of them; you couldn't look to 2 million shareholders  
23 in the American Telephone Company.

24 COMMISSIONER MacKINNON: Well, all you need is one.

25 MR. MONKS: What you need is enough, you need

1 enough, few enough people that you can point a finger to  
2 that they collectively have a significant enough share that  
3 it is realistic to think of them committing resources to  
4 being responsible. And I think that's been, that, over the  
5 last 50 years has been the great gap in the system, and I  
6 think we now have a lucky -- no one ever thought -- I asked  
7 Sen. Javitz, when I was carrying out his statute, if he  
8 ever thought when he passed the ARISA Statute that he was  
9 creating a mechanism whereby ownership would be reagglo-  
10 rated in fiduciary hands, and he said:

11 "Bob," he said, "no one will ever accuse me of  
12 being modest, but I never thought of it at all."

13 COMMISSIONER MacKINNON: Well, I'll tell you this:  
14 We did think of it when we wrote the Taft-Hartley Act, --

15 MR. MONKS: Mm-hmm. Mmmm!

16 COMMISSIONER MacKINNON: -- and we provided that  
17 the assets should be put in trust. If you know, if you'll  
18 read the Statute you'll find that.

19 MR. MONKS: Mm-hmm.

20 COMMISSIONER MacKINNON: And at that time we en-  
21 visioned what subsequently developed, --

22 MR. MONKS: Mm-hmm.

23 COMMISSIONER MacKINNON: -- and ARISA was intended  
24 to correct, --

25 MR. MONKS: Mm-hmm.

1           COMMISSIONER MacKINNON: -- and, but it didn't  
2 work out that way.

3           We figured that the, being a trust in a state that  
4 they would come within the jurisdiction of the state laws  
5 on trusts, --

6           MR. MONKS: Mm-hmm.

7           COMMISSIONER MacKINNON: -- and be subject to the  
8 review of state courts wherever they were located. Now, it  
9 didn't work out that way. No person tried it.

10          And then they led to ARISA.

11          The other thing is: Do you really think that it  
12 is practical for directors of a corporation that tradi-  
13 tionally meet once a month to become familiar with the de-  
14 tails of some of these crimes that happen?

15          They don't get into details. They're setting  
16 broad policy generally. And, of course they get reports  
17 from time to time, and, of course, once in a while they'll  
18 unearth something; but their broad policy job is what they  
19 are supposed to do.

20          MR. MONKS: Your Honor, I'd like if I --

21          COMMISSIONER MacKINNON: Now, I'm thinking of  
22 concrete cases.

23          MR. MONKS: Yeah.

24          Your Honor, I'd like to speak to three questions,  
25 if I might.

1                   COMMISSIONER MacKINNON: Yeah.

2                   MR. MONKS: One is, I'm very flattered to be  
3 mentioned in the same breath with Ralph Nader, who by  
4 virtue of the vagueries of seating in the law school I  
5 went to I -- of "MO" and "NA" I actually sat next to for  
6 three years; but his -- he's far more of an idealist than  
7 I am. I'm really grounded in commerce, and what my sugges-  
8 tions are are based on a belief that they create value in a  
9 commercial sense, that it is good business.

10                   I have no apology for having a lower "soul" than  
11 Ralph's, but there it is.

12                   I think in terms of directs being involved in  
13 details, I have misspoken myself if I have given the im-  
14 pression that that's what I suggest. I don't think that  
15 all the directors can be involved in details.

16                   I think what they can do is they can make very  
17 clear, directors run compensation committees, and they can  
18 make very, very, very clear that a principal ingredient of  
19 someone getting a discretionary bonus is whether or not in  
20 that person's department there is compliance with the law.

21                   COMMISSIONER MacKINNON: With 5,000 employees, for  
22 instance?

23                   MR. MONKS: Well, if you have one person who is  
24 the vice president in charge of personnel you hold him  
25 responsible. These are hierarchical organizations.

1           COMMISSIONER MacKINNON: Yeah. Well, he's not a  
2 director.

3           MR. MONKS: But the directors pay his bonus.

4           COMMISSIONER MacKINNON: Yes.

5           MR. MONKS: And so in terms of how they run the  
6 allocation of promotion in the company, how they run the  
7 allocation of bonuses, stock options. They say one of the  
8 performance characteristics that we value most highly is  
9 how effective you have been in your area in creating an  
10 atmosphere within which intelligence comes up about po-  
11 tential crimes, and in which criminal activity is --

12           COMMISSIONER MacKINNON: Well, you can't --

13           MR. MONKS: -- effectively inhibited.

14           COMMISSIONER MacKINNON: You can't envision some  
15 of the crimes that develop --

16           MR. MONKS: Quite right.

17           COMMISSIONER MacKINNON: -- within these corpora-  
18 tions.

19           Now I'm familiar, for instance, with a large  
20 corporation where a lot of these offenses are, by virtue  
21 of people of moderate authority, who have a department, and  
22 they are interested in getting a raise and they want to  
23 make a showing in their particular department, and so they  
24 go off on their own, and do something that's in violation of  
25 the law, so they can say, "Well, I had a good year last

1 year and I ought to get a raise." And that runs through  
2 much of this corporate crime.

3 MR. MONKS: Mm-hmm.

4 COMMISSIONER MacKINNON: Now, the other thing is:  
5 I noticed your list, who you are sending letters to.

6 Lord Almighty! As they say.

7 You never sent one to General Motors. You never  
8 sent one to Standard Oil.

9 MR. MONKS: I did send one to Standard Oil.  
10 Actually the letter to Mr. --

11 COMMISSIONER MacKINNON: I didn't see it in here.

12 MR. MONKS: I apologize, sir.

13 It's on Page --

14 COMMISSIONER MacKINNON: And you didn't send one  
15 to Firestone. You didn't send one to Phillips. And you  
16 didn't send one to Mac Truck.

17 And 41 years ago, this year, those corporations  
18 were held guilty of probably one of the largest conspiracies  
19 ever conceived, --

20 MR. MONKS: Getting rid of the subway here.

21 COMMISSIONER MacKINNON: -- with the most damaging  
22 results.

23 MR. MONKS: Getting rid of the public transporta-  
24 tion in Los Angeles.

25 COMMISSIONER MacKINNON: Yes.

1 MR. MONKS: Yeah.

2 COMMISSIONER BREYER: They did?

3 COMMISSIONER MacKINNON: Forty-five --

4 MR. MONKS: Yes. I recall the case.

5 COMMISSIONER MacKINNON: Forty-five cities --

6 MR. MONKS: Yeah.

7 COMMISSIONER MacKINNON: -- in America, they  
8 destroyed the public transportation system as it existed  
9 and substituted buses.

10 COMMISSIONER BREYER: That was Roger --

11 MR. MONKS: Your Honor, with --

12 COMMISSIONER MacKINNON: And I would -- I would --

13 MR. MONKS: With humility, I did send a letter to  
14 Mr. Rohl, the Chairman of Exxon, Page 16 of my testimony.

15 COMMISSIONER MacKINNON: Exxon. Yeah.

16 Well, I am not going to talk to you about what  
17 the punishment should have been in that case, because it is  
18 still with us.

19 The pollution that existed, and the change in  
20 public transportation in America.

21 And I'll say this: It didn't stop with the street  
22 railways, it extended to the railroads in getting them to  
23 drop their public transportation.

24 They weren't, that wasn't as conspiratorial as  
25 some of the other, but it was influenced.

1           COMMISSIONER BREYER: Just to be clear here on one  
2 thing: You're not suggesting that the directors be criminal-  
3 ly punished.

4           MR. MONKS: No, sir.

5           COMMISSIONER BREYER: You're just saying they'd  
6 lose their job, just like a politician.

7           I mean, a Government may -- somebody in his  
8 organization does something wrong, it's not really his fault,  
9 but he doesn't get elected the next time.

10          MR. MONKS: Well, with --

11          COMMISSIONER BREYER: He's in charge.

12          MR. MONKS: Exactly right.

13          COMMISSIONER BRYER: Is that -- That's the idea;  
14 right.

15          MR. MONKS: With, having taken some time from my  
16 succeeding testified, I have also taken his lines out of his  
17 book as my summary, in which he says exactly what you are  
18 saying.

19          He said that, you know, if all you're talking  
20 about is diseligibility of a job there's much more chance  
21 of it being enforced, as you are not really penalizing --  
22 imposing a fine on it.

23          Excuse me for my long-windedness.

24          JUDGE WILKINS: No; this has been very interesting.

25          MR. MONKS: And thank you for the chance of being



1 with you.

2 JUDGE WILKINS: And as with the other witnesses  
3 and following up on what Judge Breyer said, we are looking  
4 forward to working with you in the future.

5 MR. MONKS: Thank you very much.

6 JUDGE WILKINS: Good.

7 Thank you.

8 Our next witness is Christopher Stone.

9 Professor Stone is a Professor at the University  
10 of Southern California Law Center.

11 Professor, we are delighted to have you with us.

12 PROFESSOR STONE: I am delighted to be here. I  
13 am really delighted by the work the Commission has done to  
14 air some really fundamental issues, and in a very good way.

15 I am very appreciative and admiring of the work  
16 that the staff has done, even where I take issue with some  
17 of the details.

18 I am pretty familiar with the literature, and it  
19 is just marvelous to have so many really fundamental issues  
20 that have been buried in the Law Reviews over a period of  
21 years, moved out onto a public agenda, and so expertly it  
22 seems to me.

23 The prepared testimony that I submitted in advance  
24 divided itself into two parts.

25 First, I make some comments about the non-

1 probationary sections of the recommendations of the discus-  
2 sion draft; and, secondly, about the probationary sections,  
3 because those are the ones in which I am probably particu-  
4 larly oriented towards, because of my, the draft that Richard  
5 Gruner and Jack Coffee and I prepared.

6           Very briefly on the non-probationary provisions,  
7 my principal reservations have to do with the exclusive re-  
8 liance on loss, on offense loss.

9           I think that there are many offenses in which  
10 neither loss nor gain is really significant. One can think  
11 of violations of trust going all the way up to providing  
12 atomic secrets to the Soviets.

13           I would imagine it would be very, very hard to try  
14 to figure out, supposing that Congress wanted anyone to sit  
15 around and figure out what is the net present probable re-  
16 duction in value of New York City real estate as it is, you  
17 know, and so forth and so on.

18           There are a lot of offenses where even in the  
19 corporate area where loss, social loss in an economic sense  
20 is neither here nor there.

21           I think there are number of other cases in which  
22 I probably would be more troubled not by the use of loss in  
23 principal, so much as trying to figure out how loss would  
24 be calculated. And in the material that we receive it is  
25 very hard to see how offense loss in prior, the prior years

1 studied were reached.

2 For example, in this tax fraud, I can't really  
3 believe that the social loss represented by tax fraud can  
4 be established by adding the lost revenue to the Government.  
5 There's a -- the demoralization that goes on.

6 People feel if others aren't paying their taxes,  
7 I ought not to pay taxes. Now this may be, lead to a sort  
8 of a shifted equilibrium in which one magnifies, therefore,  
9 the multiple. But I don't even think by increasing the  
10 multiple you can get it at all, because it's a citizenship  
11 loss that takes place, and it is very hard to measure.

12 Third on that score, on the score of the economic  
13 considerations, I think it is generally true that losses  
14 exceed gains, but I think there are many cases in which  
15 gains may exceed losses.

16 For example, in the environmental area, one can  
17 imagine savings by a company that's subject to the environ-  
18 mental law. Savings just from not implementing a compliance  
19 program. And if the effluent is, by good fortune, blown  
20 away, there's no, by nature there's no cleanup costs.

21 In situations of that sort, I would be inclined to  
22 recommend that insofar as economic considerations are going  
23 to be subject to a multiple that one takes either loss or  
24 gain, whichever is higher.

25 That is, if, in those cases in which gain appears

1 to be higher than loss, I would take gain rather than loss.  
2 And I also recommended that the, that the higher of ex ante  
3 or ex post be also taken into account.

4 In other words, if someone did something that was  
5 highly jeopardize but it turned out to be okay, nothing  
6 blew up, I would then take the expected, the reasonably  
7 expected loss; whereas if after the fact a worse outcome  
8 than would have predicted occurred, I would take the ex post.

9 That's all I have to say about that, those pro-  
10 visions. We can talk about them in the questioning.

11 In respect to the probation, I was really pleased  
12 to see that corporate probation, particularly corporate  
13 probation of a remedial sort has gathered a considerable  
14 amount of support.

15 I think, however, that the proposal that appears  
16 in the discussion draft is much too restrictive. It's  
17 restrictive in the sense, as, first, it requires for a  
18 triggering that there be a felony.

19 Many -- Now, we're talking about felony. Let's  
20 remember that under the probation law Class A and Class B  
21 felonies are not, don't trigger probation, so we're talking  
22 about C and D, just to start with.

23 Many violations of the environmental laws and the  
24 safety laws are misdemeanors, and some pretty serious things  
25 can take place out of the Atomic Energy Act. Some fairly

1 hazardous activity can take place that is not a felony.  
2 I'll return to that point in such a moment, because it gets  
3 compounded.

4 The second element that's required for triggering  
5 under the proposals is that senior management either have  
6 participated in or encouraged the violation that has brought  
7 the company before the bar.

8 Now, I understand that under traditional state  
9 laws of criminal liability the criminal -- the way the  
10 law developed, the criminal liability of a corporation often  
11 was made to turn upon the participation by higher manage-  
12 ment. I don't think that is or ought to be relevant in  
13 probation.

14 Indeed, I come out inclined almost the opposite,  
15 in a sense. It seems to me that probation may most be  
16 needed. A probation order that induces the company to come  
17 up with a compliance plan that forces certain information  
18 that has been suppressed down below to percolate upwards to  
19 top management. That they are, that's particularly called  
20 for in those cases in which there is no provable culpability  
21 of top managers.

22 Now, the managers, as we know, have a number of in-  
23 centives to avoid knowing in some cases. I very much appre-  
24 ciated the line of questioning you raised earlier.

25 One is just from vulnerability of shareholder

1 derivative suits. There is a, some wedge between the incen-  
2 tives of the directors and the incentives of the company  
3 considered as a balance sheet, and I think they become par-  
4 ticularly acute in areas of law where the company may be  
5 subject to some criminal liability in the wake of which  
6 shareholders may come in and try to transfer through essen-  
7 tially employer indemnity action, to transfer the loss back  
8 to the directors.

9 Now, the way the cases have been going, even  
10 under Delaware law, which is pretty -- has gone through a  
11 period of getting -- of allowing more liability, more  
12 vulnerability of records, it really isn't realistic to  
13 suppose that directors are going to be, in paren, (non-  
14 insurably, non-indemnifiably) exposed if they knew nothing.

15 So I think this restriction, Restriction No. 2, is  
16 probably misplaced. I wouldn't tie a Judge's hands on that.

17 A third, the third restriction is that the same  
18 company would have had to have committed a felony of the  
19 same sort.

20 Now, in most of the laws that I find interesting,  
21 environmental laws, the atomic energy Law, the flammable  
22 fabrics law, the insecticide laws, marine protection,  
23 toxic substances, the first, the first violation tends to  
24 be a misdemeanor. I mean, it's built into the law. It's  
25 not a matter of prosecutorial discretion; so that I would

1 have strong reservations about restricting the Judge to this  
2 felony sequence as a triggering condition; and I think that  
3 some study of the laws that apply to corporations ought to  
4 be made, perhaps. Maybe the staff ought to prepare a memo  
5 just to see if I am not right, that there is a broad spec-  
6 trum of legislation to which corporations are subject, that  
7 the public feels fairly strongly about, that rely at least  
8 in the first bite on, on misdemeanors.

9 I wanted just to address myself to why it is that  
10 the probation provisions are drafted in such a restrictive  
11 manner. I think it reflects several misconceptions about  
12 corporate probation.

13 One, that it is costly. This keeps Jeff Parker,  
14 whose work I have really like and watched mature, but  
15 Mr. Parker is several, continues to assert that the corporate  
16 probation is costly.

17 The kind of provisions that those of us who  
18 favored corporate probation have in mind are not costly in  
19 any traditional sense. What we have in mind is that the  
20 company implement a plan whereby certain information about  
21 problems that are occurring in the laboratory, problems that  
22 are occurring at the, when animals are being tested, or some-  
23 thing down at the lowest level, be advanced upward.

24 The cost, in one sense of cost is simply scratching  
25 a pen on a piece of paper, and moving it upward. The private

1 cost to the executives who don't want to be tainted by  
2 having these pieces of paper across their desk, those are  
3 costs, of course, but they're not the kind of costs with  
4 which we're concerned.

5           The second misconception is that this is somehow  
6 very novel and untried. The Securities Exchange Commission  
7 has been doing things like this under the Toxic Substance  
8 Law. The administrator can require the company to test, to  
9 stipulate what is the quality review that's going on.

10           The Nuclear Regulatory Act is full of provisions  
11 that invade, as it were, the corporate autonomy. That es-  
12 tablish lines of communication that say, "You've got to  
13 audit. That the company that's a nuclear licensee has to  
14 establish auditing procedures." And those procedures, by  
15 law, require that the auditors not be subject to the same  
16 officer, superior officer whose terrain is being audited.

17           There's a history of these sorts of interventions  
18 within companies. It's not quite -- It's quite -- Not  
19 quite unique and untried. I don't think they're going to  
20 hobble the company.

21           If you look at the case under the Securities  
22 Laws, companies that have had a history of violating report-  
23 ing requirements, have had to establish a litigation  
24 committee, a compliance committee. They've just placed  
25 responsibility for review.



1 I'm a little more concerned with Judge Breyer's  
2 question, which I think is, there is this problem that it,  
3 you raised to Chattan-Brown, and I find it hard to answer,  
4 too.

5 It does seem as though here you people are charged  
6 with trying to narrow down the range of discretion and almost  
7 the nature of what we are proposing to some extent is subject  
8 to the criticism that you made, that there is a tailoring  
9 going on. It's very hard. Once one admits the legitimacy  
10 of corporate probation and perhaps relaxes some of these  
11 constraints about prior sequence of felonies in top manage-  
12 ment and so forth, it does seem hard to have general rules,  
13 and maybe part of the answer is that, I don't contemplate  
14 widespread use of this sort of corporate probation, so we  
15 are talking about unusual cases.

16 I think we all agree that probation would be  
17 reserved for unusual cases.

18 I, myself, am an advocate of the technique, and I  
19 have steadfastly maintained in all my writings that the  
20 first line of dealing with corporations ought to be the  
21 fine; and I really do congratulate the Commission for going  
22 in the right direction in increasing fines and making fines  
23 more realistic so the universe of cases in which there would  
24 be probation probably is so narrow that it may not be for  
25 that reason amenable to general rules.

1           The kind of case I would be thinking of is airline  
2 safety, for example, where some company has just a pattern,  
3 a history of neglecting to abide by FAA Rules.

4           In that case it seems to me quite inappropriate  
5 to say to the company:

6           "Well, if your planes fall out of the sky we're  
7 going to fine you. It will be a very heavy fine on you."

8           I think at that point, after a pattern of viola-  
9 tions the society is warranted in saying:

10           "Look. Come forward with a compliance plan. What  
11 do you plan to do? Identify the officers within the company  
12 that can be responsible for carrying out the obligations  
13 under this plan."

14           And if a Judge feels that's the thing to do,  
15 having heard a presentence report -- ought to be more pre-  
16 sentence reports of corporations, it is interesting. They  
17 ought to have the power to do it, it seems to me.

18           Anyway, that's all I have to add to what I have  
19 done, said before.

20           THE REPORTER: May I change the tape, please.

21           JUDGE WILKINS: Yes, sir.

22           (Tape change.)

23           THE REPORTER: We're on the record.

24           PROFESSOR STONE: Very well constrained, but it  
25 does turn, but I am reminded it's a changed tape to sort of

1 deflate my sense that I had been unprofessionally con-  
2 strained in my talk.

3 (Laughter.)

4 PROFESSOR STONE: Tell me when you are -- Are we  
5 back?

6 THE REPORTER: Yes. We're on the record.

7 PROFESSOR STONE: On record/tape.

8 Okay. Mr. Chairman.

9 JUDGE WILKINS: Thank you very much.

10 Let me ask to my right: Any questions?  
11 Commissioner Block.

12 COMMISSIONER BLOCK: I have a couple of followup  
13 questions.

14 Thank you for coming today, and I enjoyed your  
15 testimony and I enjoyed the written comments.

16 Moving back to the non-monetary aspects of the  
17 discussion draft, I just want to go over an issue that you  
18 raised.

19 You raised some two cases where the gain might be  
20 greater than the loss. One is where serendipitously the  
21 gain was larger than the loss.

22 I don't think that's one that the guidelines are  
23 particularly concerned with.

24 The major concern, I think, were being, in this  
25 case is where the expected or probable gain will be greater

1 than the expected or probable loss.

2 I don't know how many cases there are.

3 PROFESSOR STONE: Yes.

4 COMMISSIONER BLOCK: I would assume there are few.

5 PROFESSOR STONE: Yes.

6 COMMISSIONER BLOCK: And mostly coming from the  
7 fact that I think that the way statutes are drawn, have  
8 to be quite broad, and there's be some cases where the gain  
9 from, say, an environmental regulation will be larger than  
10 the loss simply because you can't cover all of the possible  
11 characteristics in a statute.

12 Now, I think quite correctly the discussion draft  
13 tries to emphasize, looking at the loss, as a way to guide  
14 everyone to those cases that are more important from a  
15 social point of view, making the assumption that the loss is  
16 an attempt to get at social values. Imprecise. And, I  
17 think the discussion draft makes it very clear that where  
18 there are a lot of non-economic aspects monetizing the loss  
19 is difficult, but --

20 PROFESSOR STONE: Yeah.

21 COMMISSIONER BLOCK: But in some sense necessary  
22 if you're going to put a metric on relative seriousness.

23 I mean, one attempt, one way to view this attempt  
24 to use loss is really to introduce proportionality into  
25 the fine system -- to get at -- to get at how serious is the

1 underlying offense.

2           So, we come back to, say, use the greater of the  
3 expected gain or expected loss. What's the standard by --  
4 that gives you that, as a rule.

5           I can see the standard that gives you the loss as  
6 a rule, but I can't see the standard that gives you the  
7 greater of the two is all.

8           PROFESSOR STONE: Yeah. Yeah. You know, it  
9 arises from sort of a conflict of world views between sort  
10 of pure economists and reformed economists, or something like  
11 that, because I think the loss, the emphasis on loss is, of  
12 course, will see its place in a compensated-oriented scheme  
13 in the civil side.

14           It does seem to me that there's a foundation for  
15 being concerned about gain; but it links to the sense of  
16 irateness, of outrage, that I think really drives histori-  
17 cally the criminal law.

18           I think that the kind of work that a Steigler  
19 has done, and other people have done, you know, looking back  
20 at the law, and trying to rationalize it, one finds it  
21 easier and more manageable and cleared to focus on the loss,  
22 but I can't dismiss the fact that historically most crimes,  
23 most common law crimes were made, were criminalized not  
24 because of a social loss. No one was even thinking in those  
25 terms, but because people became indignant, and it seems to

1 me that most of the common law crimes don't apply to corpora-  
2 tions.

3           Nonetheless, even in the corporate area, I think  
4 that the spectre of ill-got gains incites as much public  
5 outrage as losses that have been caused. That is, if some-  
6 body could take the case outside the environmental area, of  
7 a seller of goods who sells by virtue of "puffing", of  
8 violating, you know, various sorts of consumer laws, you  
9 might say that the loss, if measured in classic terms by the  
10 difference between the value that the purchaser received,  
11 and the value -- and what was paid, might be rather minimal.

12           The guy might have lied about some -- the seller  
13 might have lied about some product that wasn't as good as  
14 he said, but wasn't so bad, so that the aggregate loss isn't  
15 large, if so measured.

16           But there still would remain in the public eye a  
17 sense that, of indignation that someone is retaining ill-got  
18 gain.

19           Now, I agree that the, one has to fetch about.  
20 The very fact that I had to think of a case, after having  
21 thought of the theoretical problem, you then start to think,  
22 "What are the cases that meet this description?" And it  
23 isn't that easy.

24           Nonetheless, to answer your question: The basis  
25 would be outrage. There's a limit -- There certainly is a

1 clear historical link between outrage and the criminal law,  
2 legitimates the criminal law historically, and I think that  
3 those historical roots of the criminal law haven't been  
4 abandoned. Whatever -- Whether they -- they would still be  
5 in good order and academe, not as much as they were year's  
6 ago. Everybody wants to do supply and demand curves, and  
7 things like that, but I think outside, where people have  
8 more sense, outside the universities, --

9 (Laughter.)

10 PROFESSOR STONE: -- they still get mad at crime.

11 And I think that their getting mad should be  
12 legitimated in some way as, in the law.

13 JUDGE WILKINS: We all appreciate those astute  
14 remarks.

15 (Laughter.)

16 JUDGE WILKINS: Question?

17 Go ahead.

18 COMMISSIDNER BLOCK: Well, in that sense, it would be  
19 more sense outside, but returning just, just for a footnote  
20 again here, on this business about gain and loss, that if  
21 the loss does a better job of tracking the social outrage --

22 PROFESSOR STONE: Yeah.

23 COMMISSIONER BLOCK: -- then using the standard  
24 of the greater of the two interferes with the ranking.

25 I mean, don't you want to give prosecutors, in

1 particular, clear signals as for what is the worst of the  
2 crimes.

3 PROFESSOR STONE: Mm-hmm.

4 COMMISSIONER BLOCK: I mean, we, there's a  
5 scarcity problem. And --

6 PROFESSOR STONE: There always is. Which one did  
7 you have in mind?

8 COMMISSIONER BLOCK: It's -- It's not --

9 PROFESSOR STONE: Right now it's the scarcity of  
10 having an immediate answer for your question, so I --

11 COMMISSIONER BLOCK: And there's a scarcity prob-  
12 lem of prosecutorial resources and sentencing resources.  
13 You've got to make choices.

14 The question is: Isn't a loss based system do a  
15 better job of signaling prosecutors which crime is important?

16 PROFESSOR STONE: No, not by that standard. In  
17 fact, I would think the opposite.

18 It seems to me that identifying a loss is much more  
19 time-consuming than identifying gain. I would think if your  
20 standard is the drain on prosecutorial resources once you've  
21 raised that I think it cuts in the opposite direction. It  
22 favors gain.

23 Think how difficult it is to determine losses in  
24 toxic spills when you are on the civil side; when you have  
25 available -- when the judicial system has before it witnesses



1 who have been injured, when you have class action lawyers,  
2 when you have years of complex litigation, one still may be  
3 somewhat uncertain as to what was the loss.

4           The civil side is far better equipped to produce  
5 a valid estimate of the loss, and gain, it seems to me, is  
6 probably much more available through examining documents  
7 that can be located in-house; so I would say it cuts in  
8 the other direction.

9           COMMISSIONER BLOCK: I meant if you -- I mean,  
10 take a rough guess at it, you would rather have them rough-  
11 guess the loss as a way of ranking than bringing some crimes  
12 up that have a large gain but the loss may be larger than  
13 the gain.

14           PROFESSOR STONE: Yes. To get that, my hand on  
15 the tape; yes.

16           (Laughter.)

17           PROFESSOR STONE: Yes, I think that's -- I have  
18 sympathy with the loss, but I still think in those cases  
19 which I suspect are probably a minority of cases, where the  
20 gain exceeds the loss, in that domain in which either gain or  
21 loss is significant, then it ought to be the higher of gain  
22 or loss, because I have said there are a number of crimes  
23 that one can readily envision in which economic considera-  
24 tions of the gain to the person who gives, you know, atomic  
25 secrets to another nation or the loss to the country is

1 neither here nor there. Something has been done that is  
2 very wrong; and how does one decide what the appropriate  
3 level of penalty is. It's why it's very hard, I expect,  
4 to be a Judge.

5 JUDGE WILKINS: Helen.

6 COMMISSIONER CORROTHERS: Professor Stone, I  
7 share your reservations relative to placing exclusive em-  
8 phasis on loss, since it appears more just to use gain  
9 if it exceeds loss; and, of course, there are offenses, and  
10 I agree, where a calculation of either is either difficult,  
11 if not impossible.

12 I also share your lack of concern, from your  
13 written testimony, that there is a clear and present danger  
14 in over-deterrents.

15 One respondent has commented that there are in-  
16 stances in our discussion materials where fines for organiza-  
17 tions could be lower than for individual offenders under  
18 existing guidelines; and, of course, we realize that indivi-  
19 duals are also subject to incarceration.

20 Indeed, you found that in some areas the fines or  
21 total monetary sanctions average less than the estimated  
22 social loss.

23 My questions pertains to multiples. I think you  
24 identified that area as being somewhat mysterious.

25 Do you have any suggestions or helpful comments

1 on whether or how multiples should be utilized; or which  
2 factors should be incorporated, i.e., are there factors in  
3 addition to or other than the probability of detection that  
4 you would recommend, such as civil or criminal history?

5 PROFESSOR STONE: Well, I think it is unavoidable  
6 to deal with multiples. I think that the, all the staff  
7 papers are correct to work with multiples.

8 The mystery to me is where the multiplies come  
9 from; because in the instance of many crimes, like murder,  
10 one has a sense there, a number of bodies out there; we know  
11 that pretty well from markings that here is the denominator,  
12 this is the number of murders. How many murderers did one  
13 get.

14 We just, you know, that's easy. That's available.

15 With "white collar crime", with so much corporate  
16 crime, I think it's just very, very difficult to figure out  
17 what the appropriate multiple ought to be. I would have been  
18 interested in seeing a little more, as to how it was arrived  
19 at, because I think everyone acknowledges it's difficult.  
20 That doesn't mean you don't try.

21 In some areas it may be easier than others. That  
22 is, if one knows about a production process, one may have a  
23 sense on a particular river that here is the input, and here  
24 is what's being reported. Here is the -- They're producing  
25 so much plastic, and we know plastic is made with this

1 amount of input, and something is missing, and there's got  
2 to be so much violation going on; maybe multiples can be  
3 rationalized in some areas; but I think it's just as I said,  
4 "mysterious". I'd like to see more on it. It's very hard  
5 to do.

6 I thought it was a mistake, I'm glad you reminded  
7 me, to talk about the likelihood of detection. One wants  
8 not merely detection, but one wants to know about the --  
9 about successful prosecutions. This raises questions:  
10 What if you detected somebody and there's not a successful  
11 prosecution, was the person, therefore, innocent within the  
12 sense that the person designing multiples wants to know  
13 about; but also you need a discount rate, too. I mean, the  
14 time, over different offenses, between detection and, and  
15 the actual paying of the fine post appeal can be very, very  
16 extended; and I think that has to be, that has to be dealt  
17 with.

18 I think Mark Cohen's new paper, which is very  
19 good in many respects, picks up on that.

20 But the multiple, I do think that pursuing the  
21 notion of multiple is unavoidable. I think people have to  
22 talk about multiples. I thought these were terribly low.

23 They seem to suggest that half of the corporations,  
24 or something close to that is indicted.

25 We're getting -- I missed something on those.

1 COMMISSIONER BLOCK: It's a criminal multiple, --

2 PROFESSOR STONE: Criminal.

3 COMMISSIONER BLOCK: -- not the overall multiple.

4 PROFESSOR STONE: It's a criminal multiple.

5 COMMISSIONER CORROTHERS: Okay. Thank you.

6 PROFESSOR STONE: Okay.

7 JUDGE WILKINS: Questions?

8 COMMISSIONER NAGEL: I take it, Professor Stone,  
9 from your comment in the written testimony, that you think  
10 that the past practice in this particular area is excessive-  
11 ly lenient, and it would be somewhat analogous to saying  
12 the average sentence in the past for rape was one year, so  
13 if we raise it to three years, that's a major increase. To  
14 which your answer would be, "If the average in the past was  
15 a year, raising it to three is not necessarily the appro-  
16 priate punishment."

17 PROFESSOR STONE: That's -- That's --

18 COMMISSIONER NAGEL: I think the same point was  
19 made by Art Levine.

20 Is it, then, your view, and I guess this is sort  
21 of a policy question, as you know in setting the individual  
22 guidelines we felt it important to look to the past practice,  
23 not as an anchor -- excuse me -- not as dispositive, but as  
24 an anchor to setting the new guidelines. In view of your  
25 stance that past practice here is, as you call it, very

1 lenient, should we feel comfortable abandoning it in our  
2 search for the appropriate penalty level, or should we feel  
3 like we have to some way be bound by it?

4 PROFESSOR STONE: Well, --

5 COMMISSIONER NAGEL: The statute instructs us to  
6 look at it. What would you say to the public if we decide  
7 to set penalties that are substantially higher; and, one  
8 thing, we can give Mr. Levine's explanation in the past  
9 that fines were limited, the change in the statute makes a  
10 difference, but what else might you say?

11 PROFESSOR STONE: Well, the, as I mentioned in  
12 my testimony, it appears as though the new guidelines would  
13 be a step in the right direction, then Mark Cohen's paper  
14 then bears that out with the statistics, I received that  
15 after I had done my, prepared my testimony.

16 On the other hand, I don't know once corrections  
17 adjustments are made, whether it would be an increase in  
18 the net threat, monetary threat to corporations, because --

19 COMMISSIONER NAGEL: Suppose for a moment --

20 PROFESSOR STONE: Yeah --

21 COMMISSIONER NAGEL: Let me just give you one  
22 more --

23 PROFESSOR STONE: The only -- But that has an --  
24 Let me just clarify that, the -- because your question, I  
25 understand is slightly different, but certainly raising this

1 point: Is it a step in the right direction, even. It  
2 would appear to be, the proposed guidelines, a step in  
3 the right direction in the sense of it would intensify  
4 the threat, but even that's not clear because although  
5 in the first instance the criminal fines would be higher,  
6 they might then be offset by civil penalties, and other  
7 forms of ancillary --

8 COMMISSIONER NAGEL: Yeah; that's what I was  
9 going to say.

10 Suppose you agreed that we would not have the  
11 offsets and the multiples were, as many people have  
12 encouraged us, to be much higher; instead of two, they were  
13 five or ten, whatever the case may be; and, indeed, then  
14 the fines became in realty, under the new guidelines,  
15 substantially higher than past practice, you could argue  
16 that they were appropriate for the sake of deterrence,  
17 for the sake of just punishment, for all the other reasons  
18 we have given.

19 PROFESSOR STONE: Yeah.

20 COMMISSIONER NAGEL: My question is, in part:  
21 Would you be offended or would you think it would be some-  
22 thing wrong politically or from a policy perspective if  
23 you came forth, if you promulgated guidelines that were,  
24 indeed, much higher than the fines were on an average in  
25 '84, '85, '86?

1           PROFESSOR STONE: Yeah. I don't know what else  
2 the Commission can do. I mean the Commission is charged  
3 with making up some guidelines; and it is very, very hard.

4           It is very easy to criticize from different  
5 points of view, but I think that the -- this -- a lot of  
6 this represents very good work, and if it could be higher,  
7 levels -- levels are required.

8           Congress wants some levels.

9           I think they ought to be established in some very  
10 well-informed way, and I'm not the person who could best  
11 inform on that. I think that the people who will be testify-  
12 ing from the prosecutor's offices, from the investigative  
13 offices, have a much better sense of what the multiples ought  
14 to be.

15           I think that at the multiple, there is a possibili-  
16 ty of multiples being too high, not just from the point of  
17 view of over-deterrence, which as I've indicated I think it  
18 is not a clear and present danger, but, also, you know, the  
19 more that you increase the multiples there is a moral re-  
20 straint on Judges; there's got to be, because the more you  
21 say:

22           "Look. So few people are getting caught that the  
23 1 in 100 who do get caught, we're going to slam that person.  
24 We are going to authorize a fine of, you know, 100 times..." --

25           COMMISSIONER NAGEL: So, it might be structurally



1 better to go the other way?

2 PROFESSOR STONE: Yeah. You're using a particu-  
3 lar -- the Judge is going to feel constrained to make that  
4 poor guy who happened to be caught bear the punishment for,  
5 it might be characterized as the bad -- the bad job of in-  
6 vestigation and prosecution of other people. And I think  
7 that that's one of the explanations for the Court's not  
8 invoking penalties even at this point up to the level that  
9 would be authorized.

10 COMMISSIONER NAGEL: Thank you.

11 JUDGE WILKINS: Steve.

12 COMMISSIONER BREYER: Well, I mean, a 2 billion  
13 dollar fine on a corporation is not going after some poor  
14 guy, but it may reduce the value of the stock, --

15 PROFESSOR STONE: Yeah, about --

16 COMMISSIONER BREYER: -- and the people you are  
17 hurting are the Union pension fund.

18 PROFESSOR STONE: I've been teaching corporation  
19 so long I refer to --

20 COMMISSIONER BREYER: And the Union pensioners;  
21 right. I mean, --

22 PROFESSOR STONE: -- to the corporations as  
23 "guy"; but --

24 COMMISSIONER BREYER: I mean, it's the Union  
25 pension fund who you are hurting, and they may consider

1 it, so I think you're right, --

2 PROFESSOR STONE: Sure. Sure.

3 COMMISSIONER BREYER: -- that at some level the  
4 Judge is going to say:

5 "The Union people didn't do anything wrong."

6 But the -- I want to stay away from that.

7 PROFESSOR STONE: Yeah.

8 COMMISSIONER BREYER: That is, I want to stay away  
9 from these numbers because my personal opinion is that we  
10 are on to some good ideas in the sense that, sure, it harms  
11 and the probabilities of detection have something to do with  
12 it, but I would be surprised if the draft in its present  
13 form doesn't undergo -- I mean, it will undergo major radi-  
14 cal changes, so I'll, I think in my opinion, so I think I'll  
15 just stay away from that.

16 The other -- and I -- The other thing that I am  
17 interested in is the probation part which I don't have quite  
18 worked out in my mind, and though I think there should be  
19 probation.

20 I do see problems of how that's written, and in  
21 particular I would like you to focus, if you would, on  
22 what -- I'd like -- be interested in what you think of  
23 Mr. Monks' proposal.

24 See, you said, "Well, the cost of imposing a  
25 complex probation decree is like paper and pencil in the

1 corporation.

2 Well, I mean, that's not the cost that worries me.  
3 The cost that worries me is Mr. Latta.

4 I mean the cost that worries me is who the hell  
5 is going to administer this thing? And if you have too  
6 many of them you have, "Who is doing it?"

7 I mean, she can do it once, or twice. I don't  
8 know how many people in her office they have, and I have  
9 some experience in the anti-trust division where decrees  
10 like this, we have meat-packing decrees which made great  
11 competitive sense when it was entered. It simply froze the  
12 industry for 30 or 40 years and ended up hurting the con-  
13 sumer it was trying to protect.

14 I mean, that's the kind of costs, --

15 PROFESSOR STONE: Mm-hmm. Yeah. Well, --

16 COMMISSIONER BREYER: -- it's the administrative  
17 costs, and the fact that complex decrees can remain in  
18 existence for a long period of time and end up being counter-  
19 productive.

20 PROFESSOR STONE: Okay. But --

21 COMMISSIONER BREYER: How do we take that into  
22 account?

23 PROFESSOR STONE: Okay.

24 COMMISSIONER BREYER: That's why suddenly see  
25 Mr. Monks, and he has something rather simple. Or is it --

1 PROFESSOR STONE: Okay. But -- But, yeah. But,  
2 (a) I did not say complex --  
3 COMMISSIONER BREYER: Or is it -- Yeah.  
4 PROFESSOR STONE: -- actually.  
5 COMMISSIONER BREYER: Yeah.  
6 PROFESSOR STONE: What I said was, --  
7 COMMISSIONER BREYER: But what is it?  
8 PROFESSOR STONE: -- they needn't be; and,  
9 secondly, the duration --  
10 COMMISSIONER BREYER: Well, what is it. What --  
11 That's what -- You're --  
12 PROFESSOR STONE: -- the duration of a consent to  
13 create --  
14 COMMISSIONER BREYER: What?  
15 PROFESSOR STONE: -- is a little bit --  
16 COMMISSIONER BREYER: Yeah.  
17 PROFESSOR STONE: -- I'll pick up on what I had --  
18 I'll give you in a moment what I take to be what I had  
19 envisioned as sort of a normal sort of probation.  
20 COMMISSIONER BREYER: What?  
21 That's what I want to know.  
22 PROFESSOR STONE: And the other point -- The  
23 other point, before -- I want to get back to it, is, the  
24 20 years is a consent to create an anti-trust -- It --  
25 COMMISSIONER BREYER: Well, forget my example.

1 PROFESSOR STONE: Yeah. Yeah.

2 COMMISSIONER BREYER: I -- I mean, I just --

3 PROFESSOR STONE: But 20 -- For the 20 years;  
4 but I want to -- But I really want to clarify a misconcep-  
5 tion, that it seems to be that the probation order that  
6 we're talking about now could not extend beyond the, you  
7 know, the period of the sentence --

8 COMMISSIONER BREYER: No, but I want to know what  
9 these terms are. That's what I would like to --

10 PROFESSOR STONE: Okay.

11 Now, -- Okay. Now, I'll go back to the terms.  
12 I want to clarify the 20 years.

13 Let's remove -- Let's withdraw the 20 years --

14 COMMISSIONER BREYER: I didn't mean to argue with  
15 you.

16 I meant to elicit the --

17 PROFESSOR STONE: Yeah. It would be -- Yeah.  
18 Okay.

19 COMMISSIONER BREYER: I meant to elicit your  
20 ideas as to what the --

21 PROFESSOR STONE: Okay.

22 COMMISSIONER BREYER: -- terms would be.

23 PROFESSOR STONE: One the -- First, as we both  
24 agreed, the structure, the style, the details of the degree  
25 would be a function of the wrong, so, you know -- of the --

1 of the industry and the problem.

2 The kind of -- The model that I had in mind, when  
3 I entered the advocacy of probation involved what seemed to  
4 be fairly minor internal tamperings with reporting systems  
5 in the company.

6 For example, under the Food and Drug Act a company  
7 that is going to be submitting a drug for approval has to  
8 show that it has designed an internal system so that cer-  
9 tain problems that develop in the laboratory have to be  
10 signaled in advance, recorded in writing, and advanced to  
11 someone in a superior position.

12 Under the Nuclear Regulatory Act there are pro-  
13 visions that state in essence that if there have been de-  
14 fects defined in the operation of the facility they must  
15 be reported to the Board of Directors.

16 I sort of like that. It's just, well, the people  
17 down below have to advance up and up and everybody has to  
18 sign, and it's got to go to the Board of Directors and the  
19 Board has got to simply report that to the NRC.

20 Now, that -- Using that as a model, you're not  
21 constraining the way in which people do business. You're  
22 not saying --

23 COMMISSIONER BREYER: I'm not worried about that.

24 PROFESSOR STONE: Yeah. Yeah.

25 COMMISSIONER BREYER: I want to know what the

1 decree says?

2 PROFESSOR STONE: That's what the decree says.

3 The decree says --

4 COMMISSIONER BREYER: What does it say?

5 PROFESSOR STONE: The decree says that -- that,  
6 at this point you have violated the pollution laws. You  
7 know, you have been polluting this, the river six times.  
8 From now on you must gather data from your effluent pipes.  
9 And here is the data that you must gather. And you must  
10 have one of your employees responsible for gathering that  
11 data. And that person must be identified in the papers that  
12 you submit to the Court. It's going to be so-and-so. And  
13 his position now includes gathering data on pollutants A,  
14 B, and C, and those logs must be signed off every day. He's  
15 got to sign them every day. Every period.

16 Any -- what they call excursion, what they call  
17 excursion, any deviation from the standard of the EPA has  
18 to be recorded and it has to be reported upstream in the  
19 company, and has to go to someone who may be identified as  
20 the vice president for environmental affairs, and part  
21 cloned onto his job, this person's job, is that the EPA  
22 must be notified. Just has to be notified in writing that  
23 there were so many "excursions" they call them. Deviations  
24 over a period of time from the allowable level of pollution.

25 COMMISSIONER BREYER: Since, in other words, the

1 Judge has decreed it, says everybody -- certain people in  
2 the corporation, let's say it's General Dynamics, so I  
3 don't have 4,000 pipelines somewhere, and what the effluent  
4 that comes out is being written on pieces of paper, and  
5 every day there will be these pieces of paper going from one  
6 person to another --

7 PROFESSOR STONE: At the offending plant. Yeah.

8 COMMISSIONER BREYER: -- and then there is going  
9 to be a Judge and a probation officer who are supposed to go  
10 around and check all of these pipelines to see if the guy  
11 is really doing the reporting, and if the stuff came out --  
12 Well, Judge Green could do that, I guess.

13 PROFESSOR STONE: Yeah, but you know --

14 COMMISSIONER BREYER: I mean, it's not quite --

15 PROFESSOR STONE: You know --

16 COMMISSIONER BREYER: It --

17 PROFESSOR STONE: Yeah, but you know, first of  
18 all it's not every plant.

19 I presume it would be the offending plant.

20 Secondly, the -- what you've really done is not  
21 necessarily mean that someone has got to go by every day  
22 and read it, of course. That would be silly; but if the --  
23 if the logs have -- the logs are available for inspection,  
24 and if somebody has falsified the logs, if someone whose  
25 job requires the advancement of the information upward has



1 not done so, then that person will be in violation of a  
2 decree.

3           You know, under the Equal Employment Acts, the  
4 Fair Employment Acts, AT&T was subject to such a decree,  
5 and what she -- what they did was they designed -- the  
6 company has to design an internal compliance plan and the  
7 plan involves cloning onto the jobs of certain people  
8 within the personnel office, certain other -- certain func-  
9 tions, and those functions tend to be functions that ac-  
10 tually reduce the costs of monitoring, I should think.

11           I mean, if -- Assuming that the society wants to  
12 monitor this firm, and the choice is, then, is it cheaper  
13 to monitor at arm's length across the river or to monitor  
14 using the resources of the company, the cheapest, to take  
15 a play on the cheapest cost avoider, you know, the cheapest  
16 monitor, most effective, inexpensive monitor, is going to be  
17 the company; the people within the company. And that's all  
18 we're saying.

19           So, sure you can point to expenses the company  
20 will bear, but it seems to me they're going to be, in most  
21 cases, fairly insignificant, and, secondly, by comparison  
22 to the expenses that would be, externalize them to the society  
23 to watch at arm's length quite -- relatively low.

24           JUDGE WILKINS: Let me ask you if we can continue  
25 this dialog perhaps through correspondence?

1 COMMISSIONER BREYER: The plaintiff rests.

2 JUDGE WILKINS: Sir?

3 COMMISSIONER BREYER: I rest.

4 JUDGE WILKINS: Oh, you rest.

5 But we have exceeded our allotted time.

6 We appreciate very much your testimony, and I  
7 hope that you will continue to work with us, and we -- we  
8 are still a long ways before we will settle on how we will  
9 resolve these issues.

10 PROFESSOR STONE: Well, thank you very much.

11 JUDGE WILKINS: Thank you.

12 Our last witness before we recess is Richard  
13 Gruner.

14 Professor Gruner is an Associate Professor at  
15 Whittier College School of Law.

16 Professor, thank you for coming. We look forward  
17 to hearing from you.

18 PROFESSOR GRUNER: Well, let me say that it is a  
19 pleasure to be here and to have participated before in  
20 preparation of materials for the Commission's consideration.

21 I come before you in two capacities, one with some  
22 perspective on how corporate executives have reacted to  
23 legal standards in the past; and that I served for five  
24 years as an inside counsel to the IBM Corporation; and  
25 also as a legal academic who has studied the issue of

1 corporate sanctions in some detail; most recently in  
2 connection with preparation of an article on corporate  
3 probation under the Sentencing Reform Act that will appear  
4 this winter in Volume 16 of the American Criminal Law  
5 Journal.

6 I would like today to address two types of topics,  
7 both of which are presented in more detail in my prepared  
8 statement.

9 One is the historical use of corporate probation  
10 as a Federal remedy, Federal sanction.

11 There is some history under the Federal Probation  
12 Act regarding the applications that organizational probation  
13 might be used for; and I think that history is instructive  
14 as to the types of organizational probation that might be  
15 imposed under the new act, as well.

16 Perhaps the best known application of organiza-  
17 tional probation under the Federal Probation Act involved  
18 probation conditions requiring specific reforms in subse-  
19 quent conduct by the convicted organizations.

20 For example, in United States vs. Atlantic Rich-  
21 field Company, a Trial Court required the defendant corpora-  
22 tion to develop and implement improvements in its programs  
23 to control oil spillages at a particular plant.

24 These probation terms were aimed at requiring the  
25 firm to reform practices that had already led to several

1 illegal spills at that plant.

2           While the particular probation terms imposed in  
3 that case were overturned on appeal as too vague, the  
4 Appellate Court in the ARCO case recognized that corporate  
5 probation terms requiring specific reforms by organizational  
6 offenders would be appropriate.

7           Some other Federal Courts had used corporate pro-  
8 bation as a means to ensure that criminal sentences while not  
9 requiring specific reform steps at least were not a barrier  
10 to corporate reform.

11           For example, in the Danola Pastries case,  
12 the sentencing Court was concerned that it not impose so  
13 harsh a fine as a punishment for the defendant firm that  
14 reform was precluded altogether by forcing the firm out of  
15 business.

16           The firm felt that the failure of the defendant --  
17 excuse me. The Court felt that the failure of the defendant  
18 firm would place the real economic burden of the corporate  
19 punishment on the innocent employees and shareholders. It's  
20 solution was to substitute probation terms requiring  
21 community service by the firm at a level that did not pre-  
22 clude profitable corporate operations, substituting that  
23 probation requirement for the fine that the Court otherwise  
24 would have imposed.

25           Another use of corporate probation under the former

1 law was simply to adjust corporate punishments; and adjust  
2 them both upward and downward from the level that fines  
3 might have imposed.

4 The adjustments downward were generally either  
5 through a total suspension or reduction of the fines or  
6 through the alternate scheme of transforming a fine into a  
7 charitable contribution, often, also, of lesser amount than  
8 the fine might have been.

9 The practice of requiring charitable contributions  
10 as a term of corporate probation was ultimately struck down  
11 by all of the Circuit Courts that considered it, in part  
12 under fairly narrow statutory grounds that the Federal  
13 Probation Act limited the nature of monetary sanctions that  
14 could be imposed as a criminal sentence, limited the types  
15 other than fines that might be imposed as a Federal sentence.

16 That statutory limitation is gone under the new  
17 act, but some of the policy reasons for rejecting charitable  
18 contributions as probation terms seem to be the same now as  
19 they were under the prior law.

20 Those reasons to reject charitable contributions  
21 as legitimate probation terms include the fact that the  
22 charitable contributions often provide too little economic  
23 impact on the sentenced firms, that the contributions may  
24 prevent public use of the monies paid by the defendant  
25 firms, that such charitable contributions involve no

1 standards for Courts to determine the proper amount of the  
2 contribution; that the contributions may involve the  
3 Courts in a process of picking and choosing among countless  
4 worthy charitable organizations, with no standards for  
5 making that choice; and, finally, that choices as to which  
6 organizations should receive these charitable contributions  
7 may raise issues of conflicts of interest for the sentencing  
8 Courts involved.

9 Other types of corporate probation sentences aimed  
10 at punishment were actually designed at raising or imposing  
11 substantial punishments, in part because the sentencing  
12 Courts involved felt frustrated at the type of punishment  
13 they might impose through fines.

14 For example, one sentencing Court required several  
15 bakery firms convicted of price-fixing to give their pro-  
16 ducts to charitable organizations for local redistribution,  
17 in part to draw public attention to the defendant's crimes.

18 Another Court required the corporate probationer  
19 to employ several former convicts, presumably as a symbolic  
20 means to emphasize to persons inside and outside the  
21 corporation the criminal-nature of the firm's conduct.

22 As the second part of my testimony today I'd like  
23 to say just a little bit about some of the limiting principles  
24 on corporate probation as it might be imposed under the  
25 act.

1           Specifically principles that might be imposed  
2 within the rubric of measuring what are reasonable corporate  
3 probation terms.

4           The act, as a general standard, requires that  
5 all probation, discretionary probation terms be reasonably  
6 related to the nature of the defendant's offense, and the  
7 goals of sentencing under the act.

8           In connection with that standard, and applying it  
9 to the specific setting of corporate probation terms, I  
10 would suggest that the following types of factors would jus-  
11 tify probation terms having some substantial burdens of  
12 compliance on the affected corporations.

13           Substantially burdensome terms might be appropriate  
14 and, therefore, reasonable, where substantial social harm  
15 was inflicted or threatened by the defendant's offense; and  
16 by implication the social harms that can be prevented through  
17 probation are similarly significant.

18           The defendant's firms' assets or size will undercut  
19 the punitive effect of fines or other monetary sanctions.  
20 The involvement of top management in illegal activity  
21 suggests that the internal -- that internal reforms may not  
22 occur without probation requirements. The compartmentaliza-  
23 tion of firm management has facilitated past illegal be-  
24 havior.

25           The defendant firm has failed to take its own

1 steps to study the sources of its offense, and to implement  
2 preventative reforms, or the offender's crimes involve con-  
3 cealment or numerous small injuries to victims, causing the  
4 offenses to go undetected for a substantial period and future  
5 crimes of the same character are likely to go similarly  
6 undetected absent probation monitoring mechanisms.

7 Well, that is really all I wanted to address in  
8 connection with the prepared statement.

9 I had one further point that I wanted to raise in  
10 connection with the material that Commissioner Block had  
11 ensured that we receive, the second report by Professor Cohen;  
12 and this shifts my emphasis from the probationary to your  
13 other topic of concern involving corporate fines.

14 Professor Cohen's study seems excellent, but I am  
15 very concerned about the implications of what I view as his  
16 major conclusion, and on -- that being on Page 8 where he  
17 summarizes the review of past sentencing practices in connec-  
18 tion with corporate fines, and uses the information he had  
19 on 159 prior corporate convictions to estimate how they might  
20 have been sentenced under the discussion draft standards,  
21 and then takes an average of that practice to estimate what  
22 level of corporate penalty would be imposed for every dollar  
23 of loss caused, and he comes up with results that the  
24 corporate penalties would range from \$1.80 per dollar loss  
25 to \$2.25 for every dollar loss, and I, rather than deal



1 with that range, I take that as meaning that the average is  
2 somewhere around \$2 per every dollar loss caused, which  
3 sounds like a substantial penalty in a given case, but it  
4 seems to me that the rational corporate executive is not  
5 going to think about the given case, he's going to think  
6 about the long-run.

7           So, for example, if you had a situation like the  
8 following: Consider a corporate fraud where the estimated  
9 loss due to the fraud is something like \$20,000 an instance,  
10 the fraud probably produces a similar gain to the firm, so  
11 we're talking about a crime that every time it is committed  
12 the corporation can gain, let's say, \$20,000.

13           The corporate executive looks at these kinds of  
14 figures, if this is the system that's going to be imposed,  
15 and says, "Well, I'm at risk for maybe a \$40,000 fine, if I  
16 am caught."

17           The problem is that over the course of, let's say,  
18 ten instances of this fraud he might be caught once. Mean-  
19 ing that the total gain of a \$20,000 per instance crime  
20 is \$20,000 times 10 repetitions, or \$200,000, the total  
21 sanction is, he's caught once, he pays his fine once, the  
22 total sanction there is \$40,000 against a \$200,000 gain,  
23 it sounds like "crime pays" to me.

24           What this really means is that the multipliers here  
25 are far, far too low.

1 I would suggest that in investigating what the  
2 proper level of multiplier is that we need far more informa-  
3 tion on the fraction of total crimes of the sorts addressed  
4 by the guidelines. The fraction of those crimes that are,  
5 in fact, successfully prosecuted, whether the multiplier  
6 has to reflect the total rate of prosecution is arguable.  
7 I think some multiplier slightly lower than the inverse of  
8 the prosecution rate might be appropriate if only because  
9 the fines involved are not the only penalties that the  
10 corporate executive would consider, but multipliers as low  
11 as two would suggest that something like 50 percent of the  
12 crimes committed are, in fact, penalized, seem to be  
13 drastically low.

14 Those are all of my prepared comments.

15 I would like to say one final thing, which is that  
16 I would also like to thank the Commission for its assistance  
17 in our efforts at the Whittier Law School to republish the  
18 discussion draft and the other materials before the Commis-  
19 sion as part of the Whittier Law Review's most recent  
20 edition.

21 I am happy to say that it exists, and I have  
22 copies for you today. It's going to be mailed to our sub-  
23 scribers, or the Law Review subscribers next week, which  
24 ought to further public discussion of these issues.

25 And I thank you for your help in promoting that.

1           JUDGE WILKINS: Well, thank you, Professor; and we  
2 appreciate the Law School's dissemination of this draft of  
3 material, because I believe it will assist in encouraging  
4 public input, and that's what we are all about at this  
5 stage.

6           And I think the bottom line is: Probation as  
7 an organization of sanctions as far as you are concerned  
8 should be used far more often than this draft suggests;  
9 is that correct?

10          PROFESSOR GRUNER: That's right.

11          I would share Professor Stone's concern with the  
12 triggering circumstances in the discussion draft; in other  
13 words, the narrow set of factors that must all be present  
14 before probation is even considered, and I am specifically  
15 troubled by the notion that there has to be direct involve-  
16 ment by top management in each of these crimes.

17          Past literature on corporate criminal behavior  
18 suggests suggests that the great bulk of past corporate  
19 crimes have involved middle management conduct; and that  
20 top executives have been unaware and uninvolved in the  
21 specific criminal actions.

22          JUDGE WILKINS: It may be just the reverse. When  
23 top management is not involved we may need even more to  
24 encourage staying off of it.

25          PROFESSOR GRUNER: Exactly. Exactly.

1 JUDGE WILKINS: Thank you very much.

2 Questions to my right?

3 COMMISSIONER BLOCK: Professor Gruner, thank you  
4 for testifying. That is quite useful discussion of probation.

5 My comments will be restricted really to your  
6 characterization of a Cohen report.

7 I think it's, as I said, on at least one previous  
8 occasion this morning, I think it is somewhat of a mis-  
9 characterization to use the multiple of two and then say,  
10 "Well, that implies a pretty low multiple given the like-  
11 hood of detection.

12 After all, the theoretical argument is about the  
13 overall multiple; and you, yourself, alluded to the fact  
14 that there are many other penalties, say, in that fraud case.

15 You know, better than half the frauds prosecuted  
16 by the Federal Government of procurement frauds, or Govern-  
17 ment fraud, and there, there's debarment. There are treble  
18 civil remedies.

19 So, there are many other penalties, so that it's  
20 really not fair to characterize the draft as saying, "Well,  
21 there'll be a \$10,000 fraud and a twenty -- you know,  
22 \$20,000 penalty." The actual expectation of gain is really  
23 much higher than that. The truth is, we really don't know  
24 that. We really don't know the colateral penalties.

25 Now, the way the discussion draft is structured,

1 is to say, "Okay. Here's the criminal multiple. It's two."

2 It's related to, to past practice, but because  
3 we picked the average rather than the median it generates  
4 a set of fines that is substantially higher.

5 Now, it seems to me that given that you don't --  
6 we really don't know what the overall multiple should be,  
7 and I couldn't agree more that we ought to know that in  
8 the future. I mean, and I'd like to devote some resource  
9 to that; because I don't think the guidelines or the  
10 guidelines or policies statements will really wait for that.  
11 Because that's a long process.

12 Assuming we don't know that, we can't observe the  
13 other collateral penalties; all we can really observe are  
14 the criminal penalties. We have this information on 150.  
15 We can extend that maybe to two or three hundred cases.

16 We know that what we've done is we've move up  
17 somewhat from that. It can't be any less incentive now to  
18 commit those crimes.

19 PROFESSOR GRUNER: No; and I --

20 COMMISSIONER BLOCK: Not any more incentive.

21 In fact, it's less incentive.

22 So to move, I would say, in the right direction --

23 PROFESSOR GRUNER: Is that --

24 COMMISSIONER BLOCK: -- but I do object to the  
25 mischaracterization as two as the overall multiple because it

1 does look like we're encouraging corporate crime.

2 That's not at all what's happening.

3 PROFESSOR GRUNER: Well, two comments:

4 One is that certainly the discussion draft is  
5 a step in the right direction from past practice. Unfor-  
6 tunately past practice was drastically insufficient, and  
7 I'm afraid that the discussion draft result is still in-  
8 sufficient, so it's a step in the right direction, but  
9 not a sufficient step. Yet --

10 COMMISSIONER BLOCK: Do you have any evidence on  
11 the insufficiency?

12 PROFESSOR GRUNER: Well, the evidence would be  
13 the logic I just went through before. In other words,  
14 the notion that we don't know what the total multiple is  
15 does not prevent the corporate executive from going through  
16 exactly the logic I just described to you?

17 COMMISSIONER BLOCK: No, it does in the fact that  
18 we don't know the total penalties; it may be that the exist-  
19 ing penalty structures are approximately right.

20 PROFESSOR GRUNER: Well, how do you know that?

21 COMMISSIONER BLOCK: Well, I mean --

22 PROFESSOR GRUNER: See, that's the difference,  
23 is that it --

24 COMMISSIONER BLOCK: I'm saying that there is no  
25 evidence one way or another and what we do is essentially --

1           PROFESSOR GRUNER: Right. I agree with that,  
2 but I -- but -- but --

3           COMMISSIONER BLOCK: -- enter an opinion on  
4 -- with some increase, given the Congressional interest.

5           PROFESSOR GRUNER: I'm taking it as a given that  
6 we don't know what the theoretical multiple should be.

7           I am just observing that a corporate executive  
8 will apply some practical knowledge to your multiple, which  
9 is --

10          COMMISSIONER BLOCK: But he won't say why. He'll  
11 say I might be debarred, if it's procurement fraud; I  
12 might be debarred. I'd also have trouble -- damage ex-  
13 posure under civil fraud provisions in that area. I have  
14 my reputation. He doesn't simply go through -- the  
15 criminal penalty is only one of the possible remedies.

16          PROFESSOR GRUNER: I don't contest that and it  
17 certainly -- there are some aspects of what you're des-  
18 cribing like reputation and the implications of disbarment,  
19 that will never be monetarily quantifiable in a manner that  
20 allows you to totally factor them into the multiple, but  
21 I think as a matter of practical sense, most persons would  
22 react to the notion that the multiple ought to be two, as  
23 saying, gee, that doesn't sound anywhere near the capture  
24 rate and that's all I was trying to raise.

25          COMMISSIONER BLOCK: But, again, we're back to the

1 same thing. The criminal penalty -- the criminal multiple  
2 isn't the capture rate and we never stated it's the capture  
3 rate. It's the overall multiple.

4 JUDGE WILKINS: Thank you. Any questions?  
5 Questions to my left?

6 COMMISSIONER MacKINNON: What was your assignment  
7 at IBM?

8 PROFESSOR GRUNER: I was an internal counsel first  
9 at the corporate headquarters and later at one of the  
10 field offices concerned with one of the marketing divisions  
11 with IBM.

12 COMMISSIONER MacKINNON: You were mainly con-  
13 cerned with sales and not --

14 PROFESSOR GRUNER: Sales, and in my headquarters  
15 assignment, certain labor law problems.

16 COMMISSIONER MacKINNON: In the five years you  
17 were there, did you ever appear before the Board of  
18 Directors?

19 PROFESSOR GRUNER: No. No. There was --

20 COMMISSIONER MacKINNON: Do you know anybody that  
21 did?

22 PROFESSOR GRUNER: Other members of the internal  
23 legal staff certainly did. But at the higher levels,  
24 obviously.

25 COMMISSIONER MacKINNON: Thank you.





AFTERNOON SESSION

1  
2 JUDGE WILKINS: Our lead off witness for the  
3 afternoon is Charles B. Renfrew. We're delighted to see you,  
4 Mr. Renfrew, and we look forward to your testimony. The  
5 Commission is all familiar with Judge Renfrew. He's a  
6 former Deputy Attorney General and a former Federal Judge  
7 and now a Director and Vice President of Chevron Corporation.  
8 So, we look forward to your testimony.

9 JUDGE RENFREW: Thank you, Mr. Chairman. Can I  
10 be heard?

11 JUDGE WILKINS: Well, that microphone records only  
12 for the record, but -- so speak up.

13 JUDGE RENFREW: All right, fine. I shall, Mr.  
14 Chairman.

15 Mr. Chairman, members of the Commission, as you  
16 noted, I am a Director and Vice President of Chevron, but  
17 I should note that my views are solely mine that I express  
18 here today.

19 I bring three different perspectives to organi-  
20 zational sanctions; the perspective of a former sentencing  
21 Judge who imposed such sanctions; from the perspective of  
22 Deputy Attorney General, where I had supervisory responsi-  
23 bilities over federal criminal law enforcement; and the  
24 Director of the Federal Bureau of Prisons reported to me,  
25 and as an officer and a director of a large corporation,

1 whose responsibilities include the establishment of compliance  
2 programs to ensure that we meet the law, in over 100 countries  
3 in which we operate.

4           What I'd like to do is just offer some general  
5 observations about the approach used in the discussion  
6 materials, address the two sanctions that are recommended  
7 and conclude with a few general recommendations. I don't  
8 think anybody that has seriously studied or considered the  
9 problem of sentencing cannot help but come away with a  
10 feeling of how profoundly awesome a task that is and I think  
11 that this Commission has done a very commendable job in the  
12 work that it's done to date. I think your economic model  
13 is a new perspective. I think it's a very interesting, a  
14 very useful and analytical tool. The discussion papers are  
15 based upon the assumption that all businessmen act in an  
16 economic manner; that they take a look at the potential  
17 gain from any particular course of conduct as offset by the  
18 adverse consequences that may flow from it and base their  
19 judgment accordingly.

20           I question whether economic motivation is suf-  
21 ficiently universal to cover all criminal misconduct. Even  
22 corporations like Chevron for profit corporations, respond  
23 in noneconomic incentives and I think it would be a mistake  
24 to ignore them.

25           In the corporate setting, where you have an

1 individual in the corporation that may be responding to  
2 perceived individual gains as discounted by individual  
3 detriments, I question whether the appropriate measure of  
4 fine against the corporation should be some sort of economic  
5 loss which was a concept never considered by the culpable  
6 individual. I think there should be some relationship between  
7 the sanction imposed and the motivation of the person who  
8 committed the criminal act.

9 I think the guidelines also don't distinguish  
10 between the types of organizations involved; a small par-  
11 tnership; a sole proprietorship; a mafia family; all differ  
12 drastically in the way they conduct themselves from a Fortune  
13 500 publicly-owned company. And, I think that the con-  
14 sequences, I think the appropriateness of any sanction may  
15 vary drastically depending upon the type and nature of the  
16 organization involved.

17 I think in today's world, the business organizations  
18 are increasingly decentralized. I know Chevron is. The  
19 policy and practices are established at the headquarters  
20 but they're implemented in the field and new policies and  
21 new practices are also established at headquarters, but I  
22 think most of the violations of law occur in the field at  
23 the lower levels. And I think that not all of those cul-  
24 pable acts come about as a result of a cold, calculated  
25 economic decision. I think sometimes there's a breakdown in

1 communication. I think people don't understand the im-  
2 plications of their conduct or its consequences. This is  
3 particularly true in many areas of compliance with the  
4 anti-trust laws, for example, and they may not really under-  
5 stand the corporate policies and practices. To me, this  
6 suggests there's a breakdown in compliance programs and  
7 educational programs and perhaps the supervisory res-  
8 ponsibility, not that everyone within the corporation was  
9 guilty of culpable criminal misconduct.

10 I think that in a corporation, the use of a fine  
11 does not always serve as the effective deterrent that one  
12 hopes because its impact is diffused because the res-  
13 ponsible parties, either the actor, or negligent management  
14 don't pay the fine; the shareholders do. And the share-  
15 holders have little knowledge, in most cases, of the act  
16 involved, let alone any role in it. So, I think we have to  
17 be -- we have to be rather careful in these circumstances.  
18 I do think that the economic model is a very helpful thing  
19 in, usually, many cases, but I don't think it can be a com-  
20 plete substitute for the individual consideration given in  
21 a specific case. I think that a sentencing judge has to  
22 consider factors such as who was the culpable person; at  
23 what level in the organization did that person operate; what  
24 was the nature of the conduct; was the act clearly proscribed  
25 by law, or regulation; did the organization have compliance

5  
1 and educational programs; was the act in furtherance of  
2 corporate policy or against corporate policy; were private,  
3 civil remedies adequate to protect the parties that may have  
4 been injured by the act; would sanctions impose a hardship  
5 an injury to innocent parties?

6           These, and as many factors as the human mind can  
7 come up with, need to be taken into account in any sentencing  
8 decision.

9           Let me turn to the first principle, the total  
10 economic unit that is being used to assess the amount of the  
11 fine. As I understand it, the total harm, including the risk  
12 of potential harm, is translated into some kind of a monetary  
13 value and then multiplied by a factor that takes into account  
14 the degree of difficulty in detecting the crime and punish-  
15 ing the wrongdoer, and then enforcement costs are added to  
16 that, and this gives the total economic sanction.

17           Now, I have several problems here. In the first  
18 place, it seems to me that to the extent that you take into  
19 account potential harm, I think, in some cases, for example,  
20 environmental cases, it could just be astronomical, it could  
21 run literally into the billions of dollars. Imagine for a  
22 moment, a case like Bhopal where a release had been made but  
23 detected in time and corrected. There were some injuries  
24 but the potential of this could have run into the many  
25 millions of dollars.

1 Under these circumstances, it doesn't seem to me  
2 that that would be an appropriate measure of any fine that  
3 would be imposed against the corporation. Would it make a  
4 difference if the corporation, through its own safety pro-  
5 grams, detected the criminal release and corrected it? Or,  
6 would it make a difference if it had been brought to its  
7 attention by an enforcement agency? Would it make a dif-  
8 ference whether the actor was a disgruntled employee who  
9 was bent on corporate sabotage, or was an act that had been  
10 performed before by the company personnel in total dis-  
11 regard of the community safety.

12 I'm concerned also about the multiplier because  
13 I think the multiplier really doesn't always take into  
14 account some important factors, such as the degree of cul-  
15 pability of the act and the fact that it may be difficult to  
16 determine an offense had been committed, doesn't necessarily  
17 mean that that was a more serious offense; for example,  
18 littering on the highway, and under the guidelines, an argu-  
19 ment could be made that the more serious offense is to speed  
20 in a county land rather than in a crowded city. But, to me,  
21 the more serious problem presents itself with the use of  
22 a multiplier in the corporate setting where a corporation  
23 has a higher multiple applied against it because an employee  
24 has sought to cover the commission of the offense.

25 To me, it is simply wrong to punish the corporation

7  
(  
1 in a case where the employee sought to cover the commission  
2 of the offense, because the employee was concerned that if  
3 the corporation found out about it, that that employee would  
4 be disciplined by the corporation. I think that simply  
5 isn't correct. I think you have to be able to distinguish  
6 that situation from the situation where the employee was  
7 acting pursuant to company policy and practice.

8           At this point, I should say that I am in  
9 complete agreement with the staff working paper on the  
10 use of the second sanction on the probation sanction. I  
11 think it should be used very sparingly. I think the mone-  
12 tary sanction is more important because like the staff working  
13 paper, I am concerned about the use of the probation sanction  
14 and the potential direct interference with the operation of  
15 a business and the adverse consequences that could flow  
16 from that.

17           To the extent that the alternative draft proposal  
18 contemplates greater use of the probation sanction, I am  
19 against it. I think the authority they cite, the imposition  
20 of internal accounting controls and compliance programs makes  
21 imminent sense, and I favor that. Indeed, I think one thing  
22 this Commission should do is make sure that sufficient in-  
23 centives are given to organizations to put into effect  
24 compliance, educational supervisory programs to do away  
25 with some of the problems that a breakdown in communication



1 and other factors could lead to some criminal conduct.

2 I should also say I am in complete agreement with  
3 the third principle or organizational sanction and that is  
4 the coordination between the several criminal sanctions and  
5 whatever civil remedies may apply. I think it's par-  
6 ticularly important that that be coordinated in order to  
7 come up with a final sanction that's appropriate under all  
8 the circumstances. And I suggest to you it's particularly  
9 important that that be done when we have, in many situations  
10 in the civil remedies, joint and several liability that  
11 impose, or at least can impose awesome liability on the  
12 parties found liable in those situations.

13 And I just thought -- I didn't put it in my pre-  
14 pared statement, but I was just thinking, the use of this  
15 potential, the risk of potential harm, may raise questions  
16 under the 8th Amendment, excessive fines. Certainly, to  
17 determine potential risk, and particularly in the situation  
18 with the environmental release, where the potential harm  
19 could easily be measured in the billions of dollars, the  
20 uncertainty, the subjective nature of such an assessment may  
21 run afoul of the 8th Amendment. I'm not a constitutional  
22 scholar, but that may well be an excessive fine and not  
23 bear the type of proportionality to the nature of the offense  
24 that gave rise to it.

25 I think it's also important when we look at the

1 problem of organization sanctions, that in this country, we  
2 impose criminal sanctions more than any other industrialized  
3 society. We have criminalized offenses that we disapprove  
4 of. Now, and this is particularly true in the regulatory  
5 scheme. I think it may be just to give people an additional  
6 enforcement alternative, but I think we need to look at the  
7 laws as a mother society, and to the extent we make criminal  
8 an act that they do not, we should be very careful before  
9 imposing a very severe sanction for that type of conduct.

10           And, finally, I think as far as the recommendation,  
11 I would hope that the Commission would not use, or consider  
12 the use of a single sanction. I think that multiple san-  
13 ctions may be appropriate, depending completely on the  
14 circumstances. Probation may be appropriate in one case; a  
15 fine may be appropriate in the other. I'm afraid that the  
16 mandatory use of a formula may not be appropriate. I think  
17 that formula have a tendency to break down when you try to  
18 apply them just to the endless -- to actual situations that  
19 can come up in any particular sentencing matter, and I think  
20 that to the extent that you do use a formula, it should be  
21 used in the nature of a policy statement, a suggestion,  
22 rather than as a mandatory guideline. I feel also, as I  
23 said, that it's terribly important to provide incentives  
24 for compliance programs, for educational programs within  
25 organizations of this type. I think the work that's been

1 by this Commission and the study groups and -- has really  
2 enriched the literature in the field in sentencing. I think  
3 your work is commendable and I think it's terribly important.

4 I leave with one thought. Don't take all the  
5 discretion away from a sentencing judge. I'd like to give  
6 you an example of a case where I think it's important. This  
7 doesn't deal directly with the matters under discussion here  
8 today, but it does, I think, point out the need for flexi-  
9 bility. And that is in the case, for example, of draft  
10 evasion. Under your guidelines now in effect, probation can-  
11 not be granted for draft evasion. The minimum sentence is  
12 10 years -- 10 months incarceration and it's likely to be  
13 increased if the evasion took place in time of war or armed  
14 conflict. When I first went on the bench, in the Northern  
15 District of California, we had a large number of such cases  
16 because at one time, a young man could select the area in  
17 which he was going to refuse induction. And in some cases,  
18 I'm sure, prison was an appropriate sentence. In other  
19 cases, it would have destroyed young men. You have to visit  
20 prisons. You have to be in prisons to know what a prison  
21 would do a naive, young, innocent man. And when you take  
22 this human destruction and you view it against a backdrop  
23 of the wiser young men, extending their education in order  
24 to avoid the draft, or joining the National Guard as poli-  
25 tical leaders of both our parties did, or learning simple

1 litanies that will qualify you for conscientious objector  
2 status, I think we have to be very careful and not take away  
3 the flexibility the sentencing judge can have, to fashion  
4 an appropriate remedy. I think probation, conditioned upon  
5 years of community service, doubtless saved many, many lives,  
6 and I just urge that this Commission, in its wisdom, not  
7 lose sight of the fact that the history of the law has been  
8 experience. It's not been logic and that we get our experience  
9 with the fact that we have hundreds of judges that have been  
10 sentencing and we have learned as you pulled together, the  
11 sentencing guidelines in the individual case from the experi-  
12 ence that went on before, with organizations we simply don't  
13 have that much experience. We need to get experience before,  
14 I think, guidelines could be appropriately developed to im-  
15 pose on organizations.

16           And those are the thoughts that I leave you, and  
17 I'll be delighted to try and answer any questions you all  
18 may have.

19           JUDGE WILKINS: Thank you, Judge Renfrew, we  
20 appreciate your very thoughtful oral and written testimony  
21 and I agree with much of what you say. The experience factor  
22 is lacking as far as corporate sanctions are concerned as  
23 compared to what we had before.

24           Let me ask to my right, any questions?

25           COMMISSIONER BLOCK: Judge Renfrew --

1 JUDGE RENFREW: Yes, sir.

2 COMMISSIONER BLOCK: I have two issues that I  
3 wanted your advice on. There was a suggestion made this  
4 morning about holding directors responsible for the criminal  
5 acts of the corporation in the following sense; that if a  
6 corporation was convicted of a certain set of crimes, and  
7 leave for a moment, the set, then the directors on watch  
8 at that time would be ineligible to continue serving or  
9 could not be reelected. What's your view of using that type  
10 of mechanism to induce compliance?

11 JUDGE RENFREW: Well, my reason is pretty similar  
12 to going after mosquitos with a can and I think it depends  
13 so much on the particular circumstances of the case that  
14 if you had a director of General Motors and some dealer gave  
15 some kind of a payment under the table to a city commission  
16 in order to get some kind of extension for his facility to  
17 hold a director responsible for that criminal conduct or to  
18 say that that man or woman couldn't stand for reelection the  
19 next time the board was elected, to me would be absolutely  
20 wrong and the abstract, you'll to give me a more concrete  
21 example; the size of the organization; the nature of the  
22 offense; whether the director is being punished because he  
23 or she had been put on notice that criminal conduct was  
24 going on in the organization, and they failed to put in an  
25 appropriate compliance program or an educational program.

1 Where you have an institution of thousands or hundreds of  
2 thousands of employees, to hold a person responsible for  
3 the criminal conduct of any one of those people, seems to  
4 me very questionable. I think you have some real con-  
5 stitutional questions there.

6 COMMISSIONER BLOCK: But if it was -- I think the  
7 suggestion was made to be fair to the suggestion, that it  
8 would be serious criminal conduct. And, no suggestion was  
9 made about knowledge, but rather about serious criminal  
10 conduct, so to be fair to the suggestion, I guess I'd give  
11 you a little more specificity that it would be a really  
12 serious criminal conduct by the corporation, by an agent of  
13 the corporation.

14 JUDGE RENFREW: By an agent of the corporation. I  
15 think that we've had, for example, in cases such as Federal  
16 Probation Act, where under that Act, people are required to  
17 install internal audit and accounting principles and make  
18 reports to the SEC and everything about payments, that if  
19 an illegal payment had been made by the corporation or one  
20 of its employees and one of the branches or countries in  
21 which it did business, to hold the director responsible, to  
22 me, just doesn't make any sense and one of the problems you  
23 will have, I think, is you are going to preclude able,  
24 competent people from serving on boards if they're going to  
25 face that kind of liability and I think that the presence of

1 outside directors can be very important in the running of  
2 American business.

3 COMMISSIONER BLOCK: I appreciate your views on  
4 that.

5 One other issue, and that is something which I  
6 think is -- you know, seems to me to get us in a direction  
7 that might be quite positive, and that is, your suggestion  
8 -- if I interpret it correctly, is that we not go into this  
9 with guidelines necessarily on the first round, but rather  
10 maybe something like policy statements which give some  
11 guidance but don't really reduce the judge's discretion  
12 quite as much.

13 Would you view that we'd use policy statements for  
14 everything; for fines, for probation; and just generally just  
15 use policy statements while you get experience?

16 JUDGE RENFREW: I would think so. And I think that  
17 it would be terribly important to set a time in which, Mr.  
18 Block, you'd have the benefit of seeing of how these policy  
19 statements were followed and one of the really important  
20 things in criminal sentencing, and in my prepared statement,  
21 and I alluded to my crude effort to try and find out the  
22 efficacy of the sentence I imposed in a white collar crime  
23 case, one of the real problems we have in criminal sentencing  
24 is nobody knows whether the sentence was effective, whether  
25 it really worked and one of the problems with guidelines is

1 guidelines can be sort of a self-fulfilling prophecy because  
2 then, all the sentences are going to generally fall within  
3 those guidelines and that's what it will be and you won't have  
4 had the benefit, really, of a broader experience that may  
5 point out, maybe you should be at one end, or at the other  
6 end of the guideline or off the guideline a little bit.

7 I just think gaining more experience is a terribly  
8 important thing to assist you.

9 COMMISSIONER BLOCK: Thank you.

10 JUDGE WILKINS: Questions?

11 COMMISSIONER BREYER: I can't resist, you realize  
12 if you were talking about the guidelines that are already  
13 published, if they're law; that depends on whether we're  
14 constitutional --

15 JUDGE RENFREW: Oh, yes.

16 COMMISSIONER BREYER: Judge Wyzansky is just  
17 upstairs.

18 JUDGE RENFREW: Oh, yes, I understand. I under-  
19 stand.

20 COMMISSIONER BREYER: -- that if I tell him there's  
21 unconstitutional activity taking place down here; he'd better  
22 call the federalism police.

23 In our guidelines that are out, you realize you  
24 would not have to send the draft evader to jail?

25 JUDGE RENFREW: Well, maybe, perhaps the problem



1 is the difficulty of reading the guidelines.

2 COMMISSIONER BREYER: No, I just wanted you to  
3 know because --

4 JUDGE RENFREW: As I read the guidelines --

5 COMMISSIONER BREYER: -- that any judge can depart  
6 from any guideline. All he has to do is write his reasons  
7 and I take it that you had a reason for not sending that  
8 draft evader to jail and I make that point since you raise  
9 it because there seemed to be about 400 of the 540 judges  
10 in the United States who don't understand, but it says at  
11 the beginning of the guidelines that we have not considered  
12 any --

13 JUDGE RENFREW: Oh, I do understand that one can --

14 COMMISSIONER BREYER: -- yes.

15 JUDGE RENFREW: -- depart from the guidelines.  
16 The problem that I see is that, as I said earlier, I think  
17 the guidelines can be in the nature of a self-fulfilling  
18 prophecy because that will be the sentence that is important.

19 COMMISSIONER BREYER: They might not depart. You  
20 might not have departed but if you wanted legally to depart  
21 with a draft evader, you could.

22 JUDGE RENFREW: But I think there's also a re-  
23 striction to, certainly in some terms, a percentage that one  
24 can go, is that not so, in the case of fines or, no?

25 Is that --

1           COMMISSIONER BREYER: Well, I was thinking of the  
2 draft evader.

3           JUDGE RENFREW: Yes. Okay.

4           COMMISSIONER BREYER: The other thing I wanted to  
5 know, what you think of; what are the incentives that you --  
6 you said it's a good idea to produce an incentive to find --  
7 the lead the company to introduce self-policing mechanisms;  
8 what? I mean, I take the proposal this morning, which was  
9 Bob Monks produced this proposal, that he's been working on,  
10 evidently, with Bill Weld, and the notion was not to hold  
11 the director responsible criminally. The notion was to say  
12 to the director, it's not your fault, but if you are in  
13 charge of the ship, when a major crime takes place and they  
14 indict the company, you're out, just as, say, a politician  
15 if often out, through no fault of his own. He just happened  
16 to hire somebody who made a mistake and, therefore, -- and  
17 the notion would be, could we find a set of crimes and a  
18 set of circumstances that might at least roughly be defined  
19 so that we tell to those in the corporation, if you get into  
20 this circumstance, even though it's not your fault, you have  
21 been captain of this ship at a time it ran aground and so  
22 we're going to get a new captain and it may be the engine  
23 room's fault.

24           Now, that has the virtue, I take it, of providing  
25 quite a palapable incentive to the directors and others in

1 the corporation, to have those self-policing, reporting,  
2 screening, other institutional requirements that are bound  
3 in many circumstances to the tech crimes. Now, so, that's  
4 one device which is designed to put pressure on the cor-  
5 poration at least for major crimes where corporations would  
6 be indicted, et cetera, not to run the ship aground, and to  
7 make certain others don't.

8 Now, that's one thing that was brought up and I  
9 thought maybe you -- maybe there are others, maybe there are  
10 others. I mean, I'm not so certain that's a bad one, but  
11 maybe it is a bad one.

12 JUDGE RENFREW: Let me tell you, the answers to  
13 your questions as you gave them to me. I think that the way  
14 you give an incentive is that if a corporation has been  
15 found guilty through some kind of respondeat superior, of  
16 a criminal act, but that that corporation had put into  
17 effect compliance program, and internal audits and had con-  
18 tinually supervised its people, but you just had an employee  
19 that acted on his or her own in violation of those policies  
20 and whatever penalty is imposed against the corporation,  
21 should surely take that conduct into account.

22 COMMISSIONER BREYER: So, maybe you'd say that  
23 where there are certain large crimes; where the corporation  
24 has been indicted, the director should resign. That's a  
25 possible thing for the judge to impose but the judge should

1 be careful not to impose that should the judge determine  
2 that the incentive, anti-crime, et cetera, structures within  
3 the corporation were as adequate as called for, or something  
4 like that.

5 JUDGE RENFREW: Yes, and that meant, what any  
6 reasonable person could have done and could have expected  
7 to have been done, and let me deal with your analogy of a  
8 captain of a ship and outside directors. I don't think that  
9 holds because an outside director is someone who gives a  
10 number of hours a month to serving on a board and reads the  
11 material and participated at the board meetings whereas a  
12 captain of a ship generally is someone who has spent an  
13 entire lifetime in that particular service; is on duty 24  
14 hours a day in the Navy and has a direct line authority with  
15 all of those who are carrying out his orders. A director  
16 doesn't hire anybody. He selects.

17 COMMISSIONER BREYER: Um-hum.

18 JUDGE RENFREW: And she selects, the Chief  
19 Executive Officer who then delegates the hiring function to  
20 people beneath them, but --

21 COMMISSIONER BREYER: Right.

22 JUDGE RENFREW: -- but the directors don't them-  
23 selves hire anybody.

24 COMMISSIONER BREYER: Yes, but sometimes when  
25 there's a --

1 JUDGE RENFREW: They're very far removed from the  
2 field where these acts take place.

3 COMMISSIONER BREYER: Of course, sometimes when  
4 there's a scandal, people throw out the whole political  
5 party. See, I recognize that and what was put to us this  
6 morning was that the directors would be -- they like being  
7 directors. Mr. Monk said he doesn't recall an outside dir-  
8 ector voluntarily resigning. There probably have been some,  
9 but most people who do it, like it. They find it interesting.  
10 They're paid to some degree and they would focus their  
11 attention, perhaps more, on the importance of these screening  
12 incentive devices within the corporation, were they aware  
13 that their own jobs were on the line if later on, those  
14 devices proved to be inadequate.

15 JUDGE RENFREW: Well, I really don't see how -- I  
16 think you have to balance that against the ability to get  
17 competent, qualified people to serve on boards and to lose  
18 outside directors who bring a different perspective and  
19 background and ability, would be a loss to the company. You  
20 have to balance that. But, moreover, if the directors did  
21 everything that was reasonable; put in programs, had reports,  
22 had surprise inspections and as far as they could tell,  
23 everything was all right, and if all of a sudden -- Bhopal  
24 is a very interesting case, for example. I've talked to the  
25 general counsel of Union Carbide and he has told me on

1 several occasions that they can prove without question, this  
2 was an act of industrial espionage by an employee of their  
3 company and if that is the case, and assume that to be the  
4 case, to say that the directors of Union Carbide would face  
5 criminal sanctions or couldn't stand for reelection because  
6 of this employee --

7 COMMISSIONER BREYER: No, no, it's not a question  
8 of --

9 JUDGE RENFREW: -- makes no sense to me.

10 COMMISSIONER BREYER: It's not a question of punis-  
11 hing them. It's a question of imposing -- I mean, you say  
12 you're just not going to be a director anymore. That's  
13 not a punishment. I mean you might treat it as such but it  
14 -- this --

15 JUDGE RENFREW: Oh, I think it's a punishment to  
16 the corporation to deprive them of the benefit of the  
17 counsel and the skills of those directors.

18 COMMISSIONER BREYER: Is it better to get the  
19 incentive through a very large fine? How would you get this  
20 incentive on the corporation to impose all these very de-  
21 sirable screening, et cetera, mechanisms?

22 JUDGE RENFREW: Well, the way you would do it, was  
23 that if a company was indicted, for example --

24 COMMISSIONER BREYER: Yes.

25 JUDGE RENFREW: -- with a criminal offense, and

1 during the course of the trial, or during the pretrial  
2 proceeeings, it came out that this company had instituted  
3 an educational program, a compliance program, internal audits,  
4 internal accounting procedures which were the absolute state  
5 of the art, that they conducted surprise inspections and  
6 audits to see that those procedures were followed and that  
7 they had absolutely no reason to believe they were not, then  
8 in that case, I think that if any sanction is imposed against  
9 them, it should be very slight and the corporation that did  
10 not have such provisions, should receive a much more severe  
11 sanction.

12 COMMISSIONER MacKINNON: Well, that people that are  
13 saying that directors don't resign, don't know much about  
14 some corporations. They do, and I know about it.

15 Now, what you're really stating is that directors  
16 should be held responsible where there is some direct in-  
17 volvement of the director in that particular act that in-  
18 cludes a criminal intent and everything else. Isn't that  
19 right?

20 JUDGE RENFREW: Yes, sir.

21 COMMISSIONER MacKINNON: Now, this on-watch argu-  
22 ment, that does not hold water. It never held water when  
23 the court martials I had in World War II; it didn't hold  
24 water the other day when the captain gave the order to shoot  
25 down the Iranian airliner in the Persian Gulf; the fact that

1 he was the captain of the ship, he was not disciplined.

2 And it's against all criminal theory to hold some  
3 person liable merely because he's got a position when he  
4 doesn't participate, when he has some authority that he  
5 might have used if he knew about it, to hold him liable is  
6 I say, against all criminal theory. You've got to show  
7 intent of that particular individual. I was wondering what  
8 kind of crimes or offenses, let me say, you have at Chevron?  
9 Spillage and -- or alleged.

10 JUDGE RENFREW: I'm not going to take the Fifth  
11 Amendment, Your Honor, but the nature of the type of criminal  
12 laws that may be applied to our operations, that certainly  
13 cover operations, are the environmental laws.

14 COMMISSIONER MacKINNON: Yes.

15 JUDGE RENFREW: And there's just a wealth of  
16 environmental laws that cover almost every aspect of our  
17 operations and every one of them's got a criminal penalty.

18 Securities law; anti-trust law. There's just a  
19 myriad of laws that cover our operation.

20 COMMISSIONER MacKINNON: Of course, if you can  
21 prove direct involvement of any director, or maybe just a  
22 chief executive officer, well, you can have a case against  
23 him, but if you can't the fact that he's sitting on the  
24 board of directors and somebody thinks, that don't know  
25 much about how corporations work, that he should have known



1 about it, that's a nonargument. It's an argument that doesn't  
2 hold up.

3 One other statement you made, I would gather,  
4 concurs in the statement that I've made from time to time,  
5 that the sentence in every case has the possibility of being  
6 an amalgam of a number of various details. And, of course,  
7 which are going to be predominant, and which are going to  
8 be imposed in one particular case, will depend on the facts  
9 of that case and no two cases are very much the same.

10 That's all I have, thank you.

11 COMMISSIONER BREYER: I want to add something.  
12 because you're agreeing with Judge MacKinnon. Why does it  
13 make so much sense as I've heard here all the time; the  
14 corporation commits a major crime. Everybody seems to think  
15 it's fine to go out, and perfectly okay to put incentives on  
16 the corporation by having a two or three hundred million  
17 dollar fine, which, of course, comes right out of the pocket  
18 of the pension fund that --

19 JUDGE RENFREW: I don't know who thinks that's  
20 perfectly okay. I --

21 COMMISSIONER BREYER: Or maybe it would be a  
22 fifty million dollar fine. Well, you want some --

23 JUDGE RENFREW: I hope my testimony did not in-  
24 dicate that I thought that was perfectly okay.

25 COMMISSIONER BREYER: No, but, well, but I mean,

1 but every day of the week, we're saying fines, which actually  
2 fall upon the shareholders, which could well turn out to be  
3 pension funds, but that's okay to have that kind of an in-  
4 centive to make the corporation put in anti-crime devices.  
5 But you're punishing innocent people there just as much as  
6 you're punishing these directors. So, why is the one sup-  
7 posed to be okay, and the other is not supposed to be okay?

8 JUDGE RENFREW: Well, of course, my answer to that,  
9 Your Honor, would be that I wouldn't punish innocent parties  
10 in either case. And I think you have to be very careful  
11 about the imposition of a fine on a corporation which does  
12 injure the shareholders and other innocent employees where  
13 you have really, as you say, a "serious crime" involving  
14 really culpable conduct.

15 I think the best sanction is the one that's directly  
16 imposed upon the culpable individual.

17 COMMISSIONER BREYER: I agree with you there.

18 JUDGE WILKINS: Judge, thank you very much.

19 COMMISSIONER MacKINNON: You're going to have to  
20 have fines against corporations but they should be propor-  
21 tional to the offense.

22 JUDGE RENFREW: Yes, sir.

23 JUDGE WILKINS: We thank you for your time and  
24 your expertise. We look forward to working with you in  
25 the future.

1 JUDGE RENFREW: Thank you Mr. Chairman.

2 JUDGE WILKINS: Good to see you.

3 Our next witness has had a very distinguished  
4 career. He presently is a consultant to the Health,  
5 Environment and Safety Department of Occidental Petroleum  
6 Corporation, Jerome Wilkenfeld. Glad to see you.

7 MR. WILKENFELD: Thank you.

8 I appreciate this opportunity to meet with you.  
9 Sitting here this morning and this afternoon, I note that  
10 I'm probably the only non-lawyer that you're seeing. At  
11 least so far.

12 JUDGE WILKINS: So far, perhaps. We have several  
13 others, I think, who --

14 MR. WILKENFELD: Okay.

15 All right, I'm talking of people testifying.

16 As you noted, I'm a consultant to Occidental  
17 Petroleum at present in the environment health and safety  
18 program area and until 1986, I was Director of -- Corporate  
19 Director of Health, Environment and Safety for Occidental.  
20 I've had, as you know, over 45 years of experience in in-  
21 dustrial operations and management, developing environment,  
22 health and safety programs and also, at the same time,  
23 served for over 22 years on the New York State Air Pollution  
24 Control Board and its successor, the Environmental Board.  
25 Also involved on a lot of trade association committees, and

1 conservation organizations and that sort of thing.

2 Frank Friedman who is Occi's Vice President, Health  
3 Environment and Safety, would have been here today, but  
4 he's out of town and he asked me to extend his regrets and  
5 if he could be of any use to you, he'd be happy to meet or  
6 discuss with the Commission his opinions on this.

7 He and I have looked at the discussion papers that  
8 were sent us, and feel that our experience in developing and  
9 implementing environmental protection programs for large,  
10 multi-industry corporations, can be helpful to you in con-  
11 sidering your sentencing guidelines. The -- approximately  
12 eight years ago, Occi signed a consent agree, without ad-  
13 mitting liability with the Securities and Exchange Commission  
14 in settlement of a claim that Occi hadn't adequately advised  
15 shareholders of the extent of liability on environmental  
16 matters amongst other things. And while the settlement  
17 didn't call for any specific long term actions by Occidental,  
18 the company decided to formalize the management controls and  
19 oversight that we had in the corporation. To this end, they  
20 appointed an outside director to review the program and  
21 come up with recommendations which the Board adopted, and  
22 this program has been very successful over the last eight  
23 years or so in bringing us a real time close knowledge of  
24 issues of significance in the corporation in this area, to  
25 avoid the possibility of problems arising which could lead to

1 the kinds of things you're trying to prevent here. The  
2 importance of these -- this type of organizational program  
3 is spelled out in some papers that I sent in as attachments  
4 to my oral statement. These cover effective organization  
5 in a practical guide to environmental management that was  
6 just published by the Environmental Law Institute.

7           Now, we're not trying to imply that the only thing  
8 that's important is the establishment of tight corporate  
9 control. There are situations, I'm sure, under which, and  
10 circumstances under which the recover of costs and damages  
11 and attendant profits, where they're determinable, should be  
12 assessed. I know there are situations where fines have to  
13 be imposed by law and for the public good. But on the other  
14 hand, in large corporations, it has to be recognized that  
15 financial penalties can have one or two results. They'll  
16 either -- if they're very substantial, they could cripple  
17 or destroy a corporation or company, which will throw people  
18 out of work or reduce the availability of materials to the  
19 public and that sort of thing, or they result in a pass-along  
20 of added costs to customers and the shareholders. This has  
21 been mentioned several times before.

22           I think we have to recognize that one of the basic  
23 functions of a corporation is to generate profits and in  
24 a simplistic way, it's nothing more than a money pass-through  
25 vehicle. So fines against a corporation either have a very

1 significant effect or they just get lost in the shuffling  
2 of dollars.

3           On the other hand, if a company being sanctioned  
4 is required to institute a strong management program, as  
5 part of a probation program, the Court will assure that by  
6 implementing such requirements, a recurrence of the actions  
7 that caused the violations can be either minimized or totally  
8 obviated. The Occi program that I'm going to describe  
9 briefly here and extensively describe in the papers, will  
10 cover that and there are really four key elements to such a  
11 program. It's not a very complicated thing and does not  
12 take a very large organization to operate such a program.  
13 We find it very effective at Occi. Corporate philosophies  
14 differ and corporate structures differ and for that reason,  
15 what works well at Occi may not work in quite the same form  
16 at other companies. And I've spent a fair amount of time  
17 talking with people on their organizations in other companies  
18 and see how these things can be done.

19           But the objectives of such a program are really  
20 fourfold. A regular timely and uniform reporting from the  
21 operating line through senior management to the board of  
22 directors, all the way up the line; no business of don't tell  
23 me, I don't want to know because if I don't know then I can't  
24 be held liable to it.

25           A prompt identification and resolution of

1 environmental issues or issues of concern. This is par-  
2 ticularly important because if you identify it, you'd better  
3 do something about it, at least from my lay viewpoint, or  
4 you're going to leave yourself open for criminal penalty.

5 Establishment of preventive programs and procedures  
6 and identification of developing issues or trends; you have  
7 to know what's coming down the road, otherwise, you're going  
8 to find yourself in noncompliance, no matter how hard you  
9 try.

10 Now, the key elements of the programs to meet  
11 these objectives are, again, five-fold in this case -- no,  
12 four-fold. I thought I added -- I did have a fifth, yes.  
13 I didn't count right.

14 The keystone of this program is a computerized  
15 information and issue management system. It's a management  
16 by exception approach which allows us to know on a real time  
17 basis of issues of significance, and these are carefully  
18 identified throughout the corporation. And we have well over  
19 300 facilities worldwide, with approximately 50,000 people  
20 in several very diverse industries, ranging all the way from  
21 oil and gas exploration and production to beef slaughtering  
22 and packing with things in between like coal mining and  
23 chemical manufacture.

24 A facility assessment program, which some people  
25 call an audit program; we don't feel audit is the correct

1 term for that, though we have recently added a protocol to  
2 our internal audit program to do checks on documentation and  
3 document trails. This kind of program is one of your double-  
4 checks, to make sure that all the information is coming in  
5 through your information system.

6 An internal planning document and timetable; and  
7 the purpose of this is to make sure that all identified  
8 issues are being handled and that you're looking down the  
9 road several years in the future to where you should be in  
10 the protection of human health in the environment.

11 A capital expenditures review system which allows  
12 you to know what's coming down the road, what's new in the  
13 corporation, and allows you to determine whether these things  
14 are -- whether environment, health and safety matters have  
15 been adequately covered.

16 A legislative and regulatory action program to  
17 allow you to see what the legislature and regulators are  
18 doing, where they're going and what you have to do to up-  
19 grade your program.

20 Now, you'll notice that each of these key elements  
21 tie into an objective or at least one objective. The program  
22 is very much in keeping with what the USEPA has included in  
23 their auditing guidelines, and also in their guidelines for  
24 ordering requirements and consent decrees. As you no doubt  
25 know, in many of the consent decrees agreed to by EPA as well



1 as some of the states, they're including requirements for  
2 audit -- environmental audits and program improvement to  
3 assure that the kinds of situations that have arisen, don't  
4 -- aren't repeated.

5 Our Occi program has demonstrated its effectiveness  
6 and measured its ability to provide prompt and complete  
7 reporting of significant matters by the number of items that  
8 we find reported. We've had orders of magnitude reduction  
9 in the number of excursions and reportable incidents, ex-  
10 cursions being those things that have to be reported to  
11 state agencies or a local agency, either by permits or by  
12 regulations. Citations are pretty clear what those are.  
13 And tracking these allows us at the corporate level, and at  
14 the divisional level also, to know where the issues are,  
15 where the problems are in the corporation and assure that  
16 something is done about it. These things are reported  
17 rather fully to the environmental committee of the board of  
18 directors who oversee on a functional basis the program.

19 Additionally, the line management; the president,  
20 the executive vice presidents and general counsel, all have  
21 clear understanding of what these issues are.

22 (off record to change tape)

23 MR. WILKENFELD: As I said, this demonstration of  
24 effectiveness by objective indices that are measurable, have  
25 been very helpful in us improving the situation at Occi over

1 the years. We feel the program demonstrates that the best  
2 sanctions on an industrial organization is a requirement for  
3 a strong management oversight, rather than just financial  
4 penalties.

5 One thing I forgot to mention, that this corporate  
6 program in this roughly 18 billion dollar corporation, with,  
7 as I said, over 300 facilities worldwide, is conducted for  
8 environment, health and safety by three people in Los Angeles,  
9 and we're able to know what's happening throughout the cor-  
10 poration.

11 At this stage, I'll be happy to answer any  
12 questions you might have.

13 JUDGE WILKINS: Thank you very much, Mr. Wilkenfeld.

14 Question; all right. Commissioner Block.

15 COMMISSIONER BLOCK: Mr. Wilkenfeld, the program  
16 that you describe sounds quite interesting. I just wanted  
17 to elicit some information on how it differs from what Occi  
18 might have put in place has been induced, say, by either  
19 the threat of large fines or the sort of suggestion that's  
20 been passed this morning and this afternoon that the director  
21 seats be subject to removal if, in fact, a crime is committed.

22 How would the program differ as a compliance pro-  
23 gram as opposed to a probation program? And aren't you  
24 really describing a compliance program and isn't that what  
25 we're trying to accomplish by one of several different ways;

1 either the threat of financial penalties, the threat of  
2 individual responsibility, or management through a court  
3 which is the probation system?

4 MR. WILKENFELD: Two things: I'd like to address  
5 the question of sanctions against directors by forcing them  
6 to retire. I sat here listening to this discussion and one  
7 thing that confuses me is how are you going to determine  
8 which director to approach? In most cases, on a board of  
9 directors, I don't think any one director is responsible for  
10 an operation like this.

11 COMMISSIONER MacKINNON: Well, they have executive  
12 committees.

13 MR. WILKENFELD: All right.

14 COMMISSIONER BLOCK: All the directors, I guess.

15 MR. WILKENFELD: Well, the point is, then you're  
16 going to say, if there's a noncompliance item or a criminal  
17 penalty imposed then the entire board of directors has to  
18 resign.

19 COMMISSIONER BLOCK: Can't stand for reelection.  
20 I guess that's the proposal.

21 MR. WILKENFELD: Can't stand for reelection. All  
22 right. Well, that's --

23 COMMISSIONER BLOCK: I'm not the author of the  
24 proposal.

25 MR. WILKENFELD: Okay. I find that hard to believe.

1 I think you've skipped a level there in that the executive  
2 officers of the corporation are more of the ones that are  
3 liable to be involved in this kind of thing than the dir-  
4 ectors, per se. I doubt very much you'd find the board of  
5 directors -- I'm talking large corporations; the caliber of  
6 the people you get there, that would knowingly, willingly  
7 go along with a blatantly criminal action --

8 JUDGE WILKINS: I don't think the proposal was  
9 even that; that if it happens, even though they were totally  
10 ignorant of it, that they would be required to resign and  
11 the theory being, is that that be the penalty, they would  
12 ensure that it did not happen. At least, that was the way  
13 I would summarize the testimony of --

14 COMMISSIONER BLOCK: I think the proposal was made  
15 as an alternative. There are two ways to induce this --  
16 there are three ways to induce compliance, but there are  
17 two ways that have been discussed as alternatives; one is  
18 to use a large fine which ultimately places the responsibility  
19 on the stockholders, directly; or this indirect method of  
20 putting the directors at risk. But there wasn't any know-  
21 ledge requirement.

22 MR. WILKENFELD: My feeling is that putting the  
23 directors at risk isn't the right approach. To answer your  
24 other question though, on how it might have differed, I don't  
25 think it would have differed very much. In my experience

1 in talking with people and observing programs, in other  
2 large corporations where they've had serious problems occur  
3 such as we did, they all have immediately jumped in and ex-  
4 panded their programs, some through expanded organizations  
5 and centralized controls; others through decentralized opera-  
6 tions but clear reporting responsibilities and audit, as  
7 we have. I have also noted that many of these companies  
8 who start with very extensive programs, centralized programs  
9 of monitoring and reporting and documentation, have drifted  
10 back, once they feel that they are in good shape, to one not  
11 necessarily the same as Occi's, but along those lines where  
12 they have good reporting setups and good auditing programs  
13 but not necessarily centralized operation.

14           Most of the divisions in a large corporation are  
15 essentially free-standing corporations that could operate  
16 very well if they were independent and many of them were  
17 before they were required. Occi is a good case there, where  
18 almost all the parts of it were independent corporations that  
19 were acquired, and they ran well before they were bought  
20 and that's why they were bought and they continue to run  
21 well and don't need too much corporate oversight, except  
22 that there needs to be assurance that there's some equivalence  
23 between the corporation -- the divisions.

24           I think the thing you get -- the only thing you'd  
25 have if you had it, as a criminal sanction, or requirement,

1 of a criminal finding, is that there would be more over-  
2 sight of what the corporation is doing and that could be  
3 done readily without an awful lot of additional staff and  
4 personnel by requiring documentation and the ability to go  
5 in and observe what happens. We've had people come in and  
6 look at our program, not on any formal basis, not because of  
7 any legal requirement, but we've had EPA in and people from  
8 the state governments and local governments and other com-  
9 panies, and recognize that it's an easy way to assure that  
10 you know what's happening throughout the corporation and  
11 that if issues do arise, you'll know about it, very rapidly.

12           COMMISSIONER BLOCK: I mean, could you, essentially,  
13 if you look at it as a compliance program, but you sort of  
14 take your experience and Renfrew's suggestion, that there  
15 be a significant reduction in any fine, if there's a state  
16 of the art compliance program as a way to induce firms to  
17 put into place the same sort of system that you've put into  
18 place at Occi?

19           MR. WILKENFELD: Oh, I think that definitely is  
20 -- should be in there. The recognition that if people are  
21 exerting due diligence and good effort, that that be re-  
22 cognized.

23           COMMISSIONER BLOCK: Do you think that would be  
24 a powerful -- the reduction of the fine against the cor-  
25 poration, would that be a power incentive to actually put a

1 compliance program in?

2 MR. WILKENFELD: It would be an incentive. I don't  
3 know how powerful.

4 COMMISSIONER BLOCK: Thank you.

5 COMMISSIONER CORROTHERS: I have one question.  
6 Mr. Wilkenfeld, I certainly agree with your testimony to  
7 the extent that you believe that organizational probation is  
8 effective in assisting in the achievement of both of the  
9 goals and both deterrents and rehabilitation via preventing  
10 future violations. I am somewhat troubled that maybe you  
11 advocate a system that would almost exclude the utilization  
12 of fines, although I think just a moment ago, you indicated  
13 that you weren't going quite that far. But, to what extent  
14 do you feel that fines are appropriate?

15 MR. WILKENFELD: We were talking about that a little  
16 bit at lunch and, myself and the college professors who  
17 proceeded to lunch, and the problem you have with fines is  
18 it's a judgment call; what is an appropriate level of fine,  
19 and how do you determine what the fine should be and what  
20 should the multiplier be. There's no real good way of  
21 measuring that and you come down to judgment. Now, I know,  
22 to a certain extent, you can calculate what the environmental  
23 damage might be, the damage to individuals; you can calculate  
24 in some cases, what the added profit is, if any; in most  
25 cases I think there's no added profit. It's a loss that

1 accompanies when they have environmental incidents. But,  
2 so you could do that kind of thing and if there's a need for  
3 a multiplier, I think the history, and as I say, I'm not a  
4 lawyer; I don't know all the history on how you determine  
5 what is an appropriate penalty. It can be there and I  
6 expect it's there in many of the laws and it should be. You  
7 need an iron fist and a velvet glove. There's no question  
8 about that. You can't just go to someone and say, you did  
9 wrong; if you establish a good program, you're off the hook.  
10 There's going to have to be something, but I don't know what  
11 it is.

12                   COMMISSIONER CORROTHERS: You somewhat, though,  
13 feel that there should be a discouragement of the levying of  
14 fines; that you shouldn't really search diligently for a  
15 way to do that if you can find another probationary con-  
16 dition that would get at --

17                   MR. WILKENFELD: I think fines shouldn't be the --

18                   COMMISSIONER CORROTHERS: -- you feel that --

19                   MR. WILKENFELD: -- overriding factor because my  
20 feeling, as I said earlier, was that fines, in large cor-  
21 porations, while they have a short-term impact and a short  
22 term -- get the attention of people for a short term, in the  
23 long term I think they get lost in the bookkeeping.

24                   COMMISSIONER CORROTHERS: Thank you.

25                   JUDGE WILKINS: Any other questions?



1           COMMISSIONER BREYER: Do you have anything else  
2 you want to say, because at the moment, I'm thinking, let's  
3 call the Occi-type anti-crime program the ideal. I don't  
4 know if it's really the ideal, but it sounds pretty good.  
5 Okay.

6           MR. WILKENFELD: It's the best we could think of.

7           COMMISSIONER BREYER: All right. So, now we know  
8 there is such a program and it's possible. Then the problem  
9 is, why would you really indict corporations unless you're  
10 -- I mean, opposed to individuals, unless what you were trying  
11 to do is encourage people to have an Occi-type program? That's  
12 a major reason for indicting the corporation as compared to  
13 indicting the individuals. Normally, you'd indict the in-  
14 dividuals. Or if you want to indict corporations to encourage  
15 them. All right. But now, our problem is get get between  
16 the indictment and the program, how do we get there? One  
17 way is we provide an incentive through a big fine and that  
18 incentive may be -- it's even rebated if that gives them an  
19 incentive to adopt the Occi-type program. But you're  
20 skeptical about that.

21           A second way is we could tell the judge, judge, you  
22 do it directly. You impose the Occi-type program. And only  
23 the probation department really understands what a morass  
24 we're bringing the judge into when he tries to supervise all  
25 that, or the probation officer has to. But that may be a

1 solution in some cases.

2 The third possibility is we give them the incen-  
3 tive by saying in certain extreme cases, the directors will  
4 lose their job unless they have this kind of a program in  
5 there, and there are problems with that third one, too.

6 Is there a fourth? I mean, or do we choose the  
7 first, do we choose the second but, you know --

8 MR. WILKENFELD: Yes, I think there is a fourth;  
9 that if you went back to the corporation, I think you're  
10 automatically implying that the officers of the corporation  
11 -- I'm not talking about the directors necessarily; they  
12 may be officers and corporate directors; but the officers of  
13 the corporation have some culpability, have had some in-  
14 volvement in this, or some knowledge, or should have known.

15 COMMISSIONER BREYER: Well, often, they will indict  
16 them without the corporate directors having should have  
17 known because the idea, what we were told is the reason the  
18 division sometimes goes out and indicts corporations is  
19 because they want to encourage these corporations to put in  
20 anti-crime devices.

21 MR. WILKENFELD: Um-hum.

22 COMMISSIONER BREYER: That doesn't say the  
23 president should have known. I mean, maybe he should have,  
24 maybe he shouldn't.

25 MR. WILKENFELD: You know, just the mere indictment

1 of the corporation --

2 COMMISSIONER BREYER: Will help.

3 MR. WILKENFELD: -- I think is penalizing them to  
4 a great extent, not necessarily more than a financial penalty  
5 but it is a penalty.

6 You know, one of the things that we joke quite  
7 often in the environmental field when people who are in-  
8 volved in the corporate environmental program, is that we  
9 look at ourselves as "designated inmates", the term that we  
10 throw around, and I think that this kind of thing needs to  
11 be applied not just to the environmental offices of the cor-  
12 poration, but the corporate -- the operating officers because  
13 they are usually the ones that have the responsibility for  
14 what happens in the corporation. The environmental people are  
15 usually staff types who can give guidance, suggestion, in-  
16 formation, but can't make the decisions directly.

17 JUDGE WILKINS: Any other questions?

18 COMMISSIONER MacKINNON: Was Occidental involved  
19 in the case in the District of Columbia in which Armand  
20 Hammer was sentenced by Chief Judge Jones; do you recall?

21 MR. WILKENFELD: I'm not familiar with that.

22 COMMISSIONER MacKINNON: You were talking about  
23 your litigation, I think with the SEC --

24 MR. WILKENFELD: Um-hum.

25 COMMISSIONER MacKINNON: Where Occidental had not

1 informed the shareholders of a risk.

2 MR. WILKENFELD: It was alleged that they hadn't.

3 COMMISSIONER MacKINNON: Yes, and what was the  
4 type of risk that they were throwing at you?

5 MR. WILKENFELD: The extent of liability for clean-  
6 up of hazardous waste sites.

7 COMMISSIONER MacKINNON: On money passing through,  
8 of course, some of it gets diverted and that's where some of  
9 the problems come. I don't think, however, that any guide-  
10 line will hold that sanctions can be imposed vicariously on  
11 directors or any personnel so you can't prove a criminal  
12 intent against them are going to hold up. You cannot impose  
13 vicarious liability in the criminal field, in America. I've  
14 never heard of it. I don't know why they talk about it.

15 Thank you.

16 JUDGE WILKINS: Thank you very much. We appreciate  
17 your testimony.

18 Our next witness is Bruch Hochman. Mr. Hochman is  
19 a member of Hochman, Salkin & De Roy of Beverly Hills,  
20 California. We appreciate your attendance and look for-  
21 ward to your testimony.

22 MR. HOCHMAN: Thank you, Mr. Chairman, members of  
23 the Commission.

24 Take, at face value, my respect and deference and  
25 I think I serve you best if we put that behind us and get

4  
1 to some items that are troubling me. There are three, in  
2 particular. Number one, I feel there's been no sensitivity,  
3 strong words, to the realization that to the extent you take  
4 away discretion from a District Court Judge in criminal  
5 matters, you are lodging it with the Department of Justice  
6 and the United States Attorney, because you increase the power  
7 of that office to craft an indictment, and secure a  
8 plea on pain of having a different looking indictment.

9           Now, with the turnover of the United States Attorneys  
10 and Assistant United States Attorneys in most districts, we  
11 are now going to be peopled, on balance, by the young and  
12 inexperienced, including myself when I was young and in-  
13 experienced. I viewed my stint in the United States Attorney's  
14 Office in this district as my residency in law. I had emerged  
15 from the United States Air Force as a JAG officer after the  
16 Korean police action and began my civilian career as a member  
17 of the Tax Division of this District, United States Attorney's  
18 Office. I became, therefore, an individual who tried cri-  
19 minal and civil tax cases and when I left 33 years ago, I  
20 simply switched hats. And, primarily, that's what I've been  
21 doing ever since.

22           I am a trench lawyer. I deal with the criminal  
23 section of the Tax Division of the Department of Justice  
24 regularly. I deal with the Criminal Investigation Division  
25 of the Internal Revenue Service upwards of 5,000 times. The

1 discretion in those offices, who shall live and who shall  
2 die, Ecclesiastes in the tax field would boggle the mind;  
3 cases involving \$80,000 of unreported income go to a negligence  
4 penalty in a civil disposition. Other cases with \$25,000  
5 worth of unreported income go up the ladder in the criminal  
6 administrative process and can end up in the courtroom.

7           We have a quagmire in this field. It's very  
8 difficult. I'm not passing judgment, but I'm commending to  
9 your attention some very, very serious problems. I have  
10 more faith in having a District Court Judge have wide dis-  
11 cretion to fashion a sentence against the actual facts and  
12 have counsel in open court in the sentencing process have  
13 the opportunity to persuade the court to go to the lesser  
14 level of sanctions than not, with the United States Attorney  
15 cross-examining. I've been involved in sentencings that  
16 lasted 15 minutes and sentencings that have lasted 15 hours,  
17 with evidentiary hearings, CPS's, examination, direct, cross-  
18 examination, redirect and recross, all of which permitted  
19 the sentencing judge to have a much clearer picture.

20           I'm the author and editor of Tax Management's  
21 Corporate Tax Crimes which is another reason I'm here today.  
22 That was in 1983 and we want a new edition, but believe it  
23 or not, we're waiting for this Commission to conclude its  
24 work so that we can redo that folio and --

25           COMMISSIONER BLOCK: It will be a long wait.

1 MR. HOCHMAN: Well, I understand, but I'm hesitant  
2 to have it done, at least by me, twice.

3 In any event, that's where I'm coming from. I'm  
4 comfortable with the District Court Judges having guidance  
5 but then having discretion so that they can use fines,  
6 community service, and I am a member of the Board of Direc-  
7 tors of Foundation for People, Inc., which is an exempt  
8 organization spawned in this district to assist the pro-  
9 bation office in the handling of community service hours so  
10 that they're functional, rewarding and meaningful; so they  
11 don't just sound good and have no implementation and it  
12 works. And it works.

13 Those are some of my concerns. I am extremely  
14 worried about rules. Your sentencing guidelines on indi-  
15 viduals in the tax field is pre-inflation. You have numbers  
16 in there, and I'm not saying this accusatory, that are below  
17 the guidelines of the department to bring a case. Now,  
18 either you knew it or you didn't know it and it bothers me.  
19 If you knew it, why is it in there, and if you didn't know  
20 it, why didn't you know it? Judge Wyzanski, for example,  
21 said -- Chief Judge Wyzanski, in 1965, who declared as  
22 follows, in a paper that ended up in the Ninth Circuit  
23 sentencing institute, "For many years", he said, "I followed  
24 the line of the Department of Justice, Internal Revenue and  
25 put people in jail and my colleagues on the Massachusetts

1 bench did the same."

2           Then, when he was visiting a prison, he asked the  
3 Department of Justice people, is the deterrence effect on  
4 taxpayers in Massachusetts greater because we put people in  
5 jail, than not; than in other districts?

6           No answer. He then changed and began fashioning  
7 sentences for the particular people, and you should know  
8 there is no hard evidence on whether or not jailing tax  
9 evaders does or doesn't affect the deterrence for others.  
10 You should know there is a task force that came out in 1968  
11 under the aegis of Ramsey, Clark, and the findings were they  
12 didn't know. And nothing in the literature, at least in the  
13 tax field, has emerged ever since. Very difficult stuff,  
14 very difficult.

15           I like the enhancement of this Commission's work  
16 and it's staff has done to the field. We now have an abun-  
17 dance of literature on which to focus; somebody said "en-  
18 hancement"; I say enhancement and enlargement because some  
19 of it I didn't really understand, I must say in all candor.

20           But it's been very helpful. It's not just an  
21 exercise. But when it comes to corporate situations, I think  
22 the panoply of opportunity for the sentencing judge, under  
23 guidelines coming from the hard core fact that you do develop,  
24 is a vast improvement. I believe that you're headed for  
25 rules. I beg you, if you're headed for rules, reconsider it



1 because all you're doing then is moving discretion from the  
2 visible, open courtroom to the back room of the Department  
3 of Justice; no fair. I don't mind looking at any trial  
4 lawyer that has to try a case against me in an open court-  
5 room. I just don't want some supervisor 3,000 miles away  
6 from me, who never confronts me, to determine the configura-  
7 tion of an indictment under sentencing rules. That becomes  
8 extremely troublesome.

9           Those are, hopefully, helpful views. I hope I've  
10 been more illuminating, what is it, more heat than light. I  
11 like what the Commission is doing, but I have these fears  
12 which I have shared with you.

13           Thank you, Mr. Chairman.

14           JUDGE WILKINS: How many years was it that you  
15 worked in that back room at the Department --

16           MR. HOCHMAN: Four years, sir.

17           JUDGE WILKINS: How many?

18           MR. HOCHMAN: Four years.

19           JUDGE WILKINS: Four years, okay. I appreciate  
20 your concern. We all do, about the transferring discretion  
21 from the public forum of the courtroom to the prosecuting  
22 attorney and I must say that this was foremost on our minds  
23 when we drafted the guidelines for individuals and we did  
24 all we think we could do, given the constraints of the  
25 sentencing for legislation, not to transfer that power from

1 one member of the judicial family to the other and given  
2 more time, I think we could sit down and go through those  
3 guidelines. I think you will see there are many areas where  
4 the power could have been transferred but it was not, because  
5 of the way the guidelines were, in fact, structured. But  
6 it is of great concern to us, and we certainly don't want  
7 that to occur with corporate sanctions as well.

8           It is a problem, but if we're going to be true  
9 to our mandate from the Congress, we've got to do more than  
10 write general policy statements and say, Judge, you can use  
11 a fine or you can use probation, or you can use the im-  
12 position of something else, and just say take your pick,  
13 because the corporation that you represent appearing before  
14 me, will be sentenced in a greater differing fashion than  
15 he would have been -- than it would have been, that it  
16 appeared down the hall, and that's what Congress has told us  
17 we want to avoid. So, it's very difficult to try to fashion  
18 that balance.

19           MR. HOCHMAN: But keep in mind, sir, there is  
20 a basic inconsistency in the way cases get into the pipeline  
21 at the outset in Internal Revenue Matters.

22           JUDGE WILKINS: Right. Right.

23           MR. HOCHMAN: So that, you know, we pride our-  
24 selves in this republic of having life under a rule of law  
25 and we cannot blind our eyes to the fact that, in fact, we

1 have to live with our own infirmities. I had a Fortune 500  
2 corporation -- may I have another moment?

3 JUDGE WILKINS: Certainly.

4 MR. HOCHMAN: Twelve years ago; the reason I know  
5 I'm in my new office, and this happened in the old office,  
6 and I've been here 12 years. So, it was about 13 years ago.  
7 He did approximately a billion dollars worth of business.  
8 In the State of Illinois, one of its smaller managers, for  
9 lack of a better word, below middle management, in a sub-  
10 sidiary, but it was a consolidated return, paid a \$5,000  
11 bribe in connection with some zoning. He buried in cost of  
12 goods sold and the outside CPA's, on a certified audit, missed  
13 it. Too small. They didn't do everything. They couldn't.  
14 It surfaced. IRS took the position of having a civil fraud  
15 penalty because of that transaction, and in those days, the  
16 law has changed slightly now, but in those days you had a  
17 50 percent penalty under Section 6653(b) if there was any  
18 fraud on the return. So, it set up a four million dollar  
19 deficiency and a two million dollar fraud penalty because of  
20 that \$5,000 item, with a straight face. We got rid of the  
21 problem. That's neither here nor there. But, again, we're  
22 not in isolation. This is part of an overall system that is  
23 impacting people and for a self-assessment system to work,  
24 people have to have confidence in those regulating them and  
25 even in those sentencing them and that's why I, as I say,

1 express my views as, he that believes I'm doing it.

2 JUDGE WILKINS: We appreciate your remarks very  
3 much. Questions to my right?

4 COMMISSIONER CORROTHERS: I guess one of clarifi-  
5 cation. You made mention of having three major concerns and  
6 I wanted to make sure to get them and I'm not sure; either  
7 I got lost, or I'm not sure that you made them. The one  
8 you mentioned was your concern about the transfer of dis-  
9 cretion and then you mentioned in connection with rules that  
10 we have utilized pre-inflation guidelines, or pre-inflation  
11 figures in the tax guidelines.

12 MR. HOCHMAN: Yes, ma'am.

13 COMMISSIONER CORROTHERS: I'm not sure I heard  
14 the third?

15 MR. HOCHMAN: Community service.

16 COMMISSIONER CORROTHERS: Oh, okay.

17 MR. HOCHMAN: I said I'm a member of the Board of  
18 Directors of Foundation for People, Inc., an exempt organi-  
19 zation that implements community service, and I like that  
20 very much because in some communities, if you were to fine  
21 a corporation, for example, too much, you'd put it out of  
22 business and you're going to have 250 jobs lost in a com-  
23 munity never to be replaced. So, the community service  
24 aspect sometimes fits where a fine would not fit.

25 COMMISSIONER CORROTHERS: Um-hum.

1           MR. HOCHMAN: And, as I say, we have here, this  
2 organization, that helps the probation office look after it  
3 because that's a big burden on a probation office. Absent  
4 an organization such as ours; when I say "ours", that I am  
5 a member of the Board; I think our probation office would  
6 have much more difficulty in implementing community service  
7 hours. But by having such an organization and they will  
8 proliferate, I do think this becomes a viable option, help-  
9 ful to the community that's been insulted by that corpora-  
10 tion. So, there's some quid pro quo and I'm not a maverick.  
11 Fines that go into the general treasury are often helpful,  
12 but they are often not repairing the harm to that community  
13 because it's too remote.

14           COMMISSIONER CORROTHERS: Thank you.

15           JUDGE WILKINS: Thank you.

16           Any other questions?

17           COMMISSIONER NAGEL: I was just going to say that  
18 I think, as in most things, the position people take often  
19 depends on where you sit and as a defense counsel, I'm very  
20 sympathetic to position you take. I would only ask that  
21 you sort of consider the fact that Congress obviously was  
22 very concerned about lack of uniformity, a lack of certainty,  
23 and I think it's fair to say in the corporate area, a per-  
24 ception of excessive leniency and when we are given our  
25 mandate by the enabling legislation, from our vantage point,

1 where we sit, we have to be responsive to those concerned.  
2 I think it would be particularly helpful if you and your  
3 colleagues in the defense bar, might give thought to, given  
4 that mandate, about the problems of certainty, uniformity,  
5 and a perception of excessive leniency in the past for cor-  
6 porate sanctions, how we might best structure the derivation  
7 of fines and the use of probation, the question that Mr.  
8 Monks raised this morning about taking away the opportunity  
9 to sit on a board, et cetera; given that's our mandate, then  
10 if you could be helpful to us in responding, I think that  
11 would be a good thing.

12 MR. HOCHMAN: We'll do it and we'll supplement.  
13 Let me make one observation, though, because there are grayer  
14 heads than mine around this table, 25 years ago, the Commit-  
15 tee on Civil and Criminal Penalties of the ABA Section of  
16 Taxation, commended to Congress' attention that the then  
17 maximum fines under 7201 were totally inadequate as a mone-  
18 tary sanction. It fell on deaf ears. Nor did Treasury or  
19 Justice at that time, pick up the cudgels and we, of the  
20 ABA's committees that were worried about it, or even the  
21 California committees, we ended up a burpse in a tornado  
22 because nobody, strangely enough, we are the ones saying,  
23 hey, a \$10,000 lid at this point, a maximum fine of up to  
24 \$10,000 wasn't per count, wasn't enough to take care of  
25 certain situations because after all, you know, many tax

1 crimes are motivated by simple, pure greed and hitting them  
2 in the pocket book is one of the way of deterring. It took  
3 forever. We don't have enough experience, Ms. Nagel, under  
4 September 3rd, '82 is a critical date. That's when the fines  
5 went up from \$10,000 to a hundred and to two-fifty and then  
6 in '84, we had another enhancement. We have had not enough  
7 living experience, you know, to be able to report it's im-  
8 pact.

9 COMMISSIONER NAGEL: Well, that's if you argue as  
10 you had earlier, that the major goal and perhaps the major  
11 way to assess impact is to look at the terms. Our statute  
12 lays out four purposes, only one of which is deterrents.  
13 So even if it never had a deterrent impact to raise the  
14 sentences, there would be three other justifications for  
15 changing the sentences, not the least of which is to provide  
16 some sort of just punishment for the offense, whatever you  
17 want to call it; retribution, just punishment, punitive  
18 response, et cetera. Judge MacKinnon said this morning,  
19 our statute provides for an amalgam. So, it's not a mandate  
20 for us to demonstrate that any sentence has a deterrent  
21 effect and, in fact, you don't necessarily have to look to  
22 experience to determine whether you think the sentences  
23 right now are appropriate. I think that if you look at the  
24 recent Congressional action, they don't raise the sentences  
25 or raise the maximum fine each time because they think

1 they're getting satisfactory sentences now, in addition to  
2 which, you could argue, and I think quite persuasively, that  
3 one reason the Sentencing Commission was established is  
4 because Congress felt that they weren't getting the responses  
5 that were appropriate from the judiciary with its unfettered  
6 discretion. I only raise that because I think it's most  
7 helpful to us when you put yourself in our position of having  
8 a statute that gives us a specific task and then asking how  
9 we can best respond to that task while not wrecking havoc  
10 with the system.

11 But I think that you have to keep in mind that  
12 deterrence is only one goal and there is no onus or burden  
13 on the Commission to prove that the sentences in the past  
14 were ineffective before they can change them. There is also  
15 a sense of a public perception that the sentences, at least  
16 in the corporate area, have been not only too low, but ex-  
17 cessively lenient and have not accomplished the goals.

18 MR. HOCHMAN: TWA landed safely last night in  
19 New York; will not be in the newspapers this morning in  
20 Los Angeles.

21 COMMISSIONER MacKINNON: They did what?

22 MR. HOCHMAN: They landed safely, sir, in New  
23 York; will not be in the L.A. Times this morning.

24 If TWA happens to land in the Hudson, it will be  
25 in the morning Times. The problem of that kind of perception



1 is an unfamiliarity with the process. We have had, in my  
2 judgment, and I follow all of the sentences in the tax  
3 cases, all over the country, with a network of other lawyers,  
4 so I kind of know what the action is. That's part of the  
5 reason I stay home, but in any event, -- in any event, you  
6 know, one of the problems is that we have had, the judges  
7 have done, I think, a fine job most of the time. You have  
8 this aberrational sentence that will catch public attention  
9 like TWA going into the Hudson. And then it gets a dis-  
10 proportionate response.

11           COMMISSIONER NAGEL: I think your point is well  
12 taken. I would also refer you to the public opinion polls  
13 that show that upwards of 75 percent of the public year in  
14 and year out, thinks the sentences for certain kinds of  
15 offenses are excessively low. Now, that doesn't mean they're  
16 right. It just means that is their view and I think it is  
17 colored by what you read in the paper, but it is also  
18 colored by the public's perception about what is an ap-  
19 propriate sentence.

20           Let me not take up more time because we could de-  
21 bate this --

22           MR. HOCHMAN: I'm not an elitist, but let me  
23 conclude with this, because I know you have a schedule. I  
24 am mindful of what the public thinks of lawyers today, ranks  
25 with Shakespeare and Dickens, "until they need one". And

4  
1 it's amazing how the people who walk into my office don't  
2 think lawyers are scoundrels. They don't look at me as a  
3 scoundrel; they don't argue with me as a scoundrel. They  
4 need me. No, I think there's a danger in going with certain  
5 kinds of perceptions in terms of certain communication media  
6 that have to fill their tubes for their own reasons and they  
7 don't show all the lovely acts of the community because it  
8 is the other side that will get more viewers or readers and  
9 I would pray, really, that, you know, within the bounds of  
10 your own discretion, that you take that step backwards.

11 JUDGE WILKINS: Thank you, any other questions.

12 COMMISSIONER BREYER: Yes, anyway, we didn't, for  
13 your information, the reason that the tax in the individual  
14 case is what it is, starts at zero is it's a monetary crime  
15 and we started all the monetary crimes on a scale of zero.

16 So, obviously, theft, fraud, all of them, catch  
17 certain things that won't be prosecuted. That's just a  
18 mechanical reason we started them at zero. As far as the  
19 numbers in the tax guideline are concerned, they reflect an  
20 effort to rationalize the sentences in monetary crimes;  
21 fraud, theft; tax; and we tried to make them roughly uniform.

22 I mean, we have a theory, whether it's a correct  
23 theory or not.

24 COMMISSIONER MacKINNON: You mean to tell me that  
25 prosecution of tax evasion doesn't induce compliance?

1 MR. HOCHMAN: Sir, the Internal Revenue Service  
2 misplaces its concept of deterency by looking for the  
3 criminal sanction.

4 COMMISSIONER MacKINNON: I'm not talking about  
5 them. I'm talking about my experience. Go ahead.

6 MR. HOCHMAN: No, I have inquired of, for example,  
7 the example I give to the sentencing judges before I argue  
8 on a clean case; now, I'm talking about a first offender;  
9 I'm talking about clean money. In other words, the un-  
10 reported income has been earned without question --

11 COMMISSIONER MacKINNON: I'm talking about all  
12 tax cases.

13 MR. HOCHMAN: Right. Well, no, no, I have to  
14 distinguish between case and case, but let me answer you, I  
15 think, very directly. The doctor that I commend to his  
16 attention, that Dr. Ginsburg went to jail in the 50's; how  
17 come you didn't notice it, sir; and he said, "I assumed that  
18 Dr. Ginsburg was an abortionist."

19 When I talked to Dr. McGillicuddy in the '60's,  
20 didn't you notice that so and so went to jail, a peer; he  
21 said, "I assumed he was a pill pusher." And when I talked  
22 to the same chap in the '70's, he assumed he was writing  
23 prescriptions for narcotics.

24 Unfortunately, when the United States Attorney holds  
25 press conferences, they pillow their cases. They do not say

1 I am indicting an ordinary doctor and let every doctor be-  
2 ware. They always have this body english so that everybody  
3 else disassociates from the sentence; he must have been a  
4 mafia chief; he must have been the cousin of a mafia chief.

5 Judge MacKinnon, the problem is they're not com-  
6 municating with the people they want to communicate with.

7 COMMISSIONER MacKINNON: Well, my experience is,  
8 and when I became a U. S. Attorney and started prosecuting  
9 some tax cases, a former Internal Revenue Agent came to me  
10 and said, "Mac, keep going." He says, "They're coming into  
11 my office in droves to file amended statements."

12 MR. HOCHMAN: Judge, if they would have an amnesty  
13 program --

14 COMMISSIONER MacKINNON: Well, they've had them.  
15 And they didn't work.

16 MR. HOCHMAN: They never had a federal amnesty  
17 program.

18 COMMISSIONER MacKINNON: Yes, they have. And all  
19 you've got to do is look it up.

20 MR. HOCHMAN: I have, sir.

21 COMMISSIONER MacKINNON: Well, look at the Shotwell  
22 case and the trial of Sullivan, which went to the Supreme  
23 Court, and tried in the Northern District of Illinois, and  
24 the defense there, by Sullivan who was found guilty, was  
25 that he had made a --

1 MR. HOCHMAN: Voluntary disclosure.

2 COMMISSIONER MacKINNON: A voluntary disclosure.  
3 That's right.

4 MR. HOCHMAN: Sir, in the voluntary disclosure  
5 period, was five years, and in that case, what happened is  
6 the IRS came in the front door and he fled the back. It was  
7 not a voluntary disclosure and the court so held.

8 But, we haven't had, since 1947, and, see, this  
9 happened during the war, and was basically a forgiveness  
10 year of '43.

11 COMMISSIONER BREYER: In Massachusetts we have it.

12 MR. HOCHMAN: Yes, and California had it, raised  
13 a lot of money, but in any event, I'm digressing. I apologize.

14 JUDGE WILKINS: Thank you, Mr. Hochman, we've  
15 enjoyed this lively conversation and we look forward to  
16 working with you in the future.

17 Our next two witnesses -- by the way, let me  
18 advise everyone, we seem to be halfway keeping to our  
19 schedule this afternoon, but let me remind the witnesses  
20 we're asking you to summarize your testimony in not more  
21 than ten minutes, so that we can have an opportunity to  
22 question you.

23 Our next witnesses are two; Ivan P'ng, Assistant  
24 Professor, University of California School of Management;  
25 and Eric Zolt, Acting Professor of Law, UCLA School of Law.

1           Gentlemen, we're delighted to have you with us  
2 today.

3           (off record for tape change)

4           JUDGE WILKINS: Professor P'ng and Professor Zolt,  
5 we'll hear from you in any order that you choose.

6           PROFESSOR ZOLT: Thank you.

7           JUDGE WILKINS: That microphone is recording only  
8 for our future purposes, but it does not amplify your voice  
9 so speak up.

10          PROFESSOR ZOLT: Okay, thank you for allowing us  
11 to appear here today, especially since this hearing con-  
12 flicts with a faculty meeting.

13          My name is Eric Zolt and I'm here with Ivan P'ng.

14          I'm a Tax Professor at the UCLA School of Law.

15          Mr. P'ng is a Professor of Business Economics at the UCLA  
16 Graduate School of Management.

17          Our contribution to your hearing is relatively  
18 simple and straightforward. We believe that any rational  
19 scheme of deterrence must consider the income tax conse-  
20 quences of the sanctions. Our testimony today is based on  
21 an article, "Fines for Business Offenses, Optimal Enforcement  
22 in the Presence of Income Taxation", a copy of which was just  
23 provided to you.

24          The draft sentencing guidelines for organizational  
25 defendants relied primarily on monetary sanctions. Monetary

1 sanctions are a function of three factors. First, the  
2 offense loss based on the total harm caused by the offense,  
3 multiplied by a second, the offense multiple, based on the  
4 difficulty of detecting and punishing the offender; plus,  
5 third, enforcement costs. The guidelines do not consider  
6 tax consequences.

7           The tax law does not treat monetary sanctions  
8 imposed on organizational defendants in a coherent fashion.  
9 Congress disallows deductions for amounts paid for fines or  
10 similar penalties; for bribes and kickbacks; and for the  
11 punitive portion of certain anti-trust violations. De-  
12 ductions are generally allowed, however, for damages paid  
13 even as a result of fraud and for those penalties that are  
14 compensatory.

15           While our paper adopts the harm based deterrent  
16 approach in the analysis of tax considerations, we believe  
17 failure to consider tax consequences as sanctions, is a  
18 deficiency common to all deterrent schemes discussed today.  
19 Tax consequences have not been considered in the optimal  
20 deterrence literature, upon which much of the testimony  
21 before you today derives, or included in any of the reports  
22 prepared by the Sentencing Commission staff. Tax conse-  
23 quences will either magnify or diminish the effect of the  
24 sanctions.

25           We believe that failure to consider such consequences

1 results in a deterrent scheme that is both inefficient and  
2 inequitable. Such scheme is inefficient because it inter-  
3 feres with the firm's efficient use of inputs. It is in-  
4 equitable because it treats offenders differently depending  
5 on their respective tax position and whether the tax system  
6 allows the deduction for amounts paid as sanctions.

7 PROFESSOR P'NG: Let us illustrate the potential  
8 inefficiency from the guidelines' failure to consider tax  
9 consequences with a simple example. Taking as a benchmark,  
10 the socially efficient mix of inputs, whether or not such  
11 inputs give rise to external harm. The example is, an oil  
12 refinery that can choose between two inputs; one, an input  
13 of labor that costs \$100; and two, an input that costs \$50  
14 and generates pollution that causes harm to others of \$40  
15 for a total social cost of \$90.

16 From the standpoint of social efficiency, the firm  
17 should choose the lowest cost input; namely, the input that  
18 generates the pollution. Now, let's assume that there are  
19 no problems of detection or costs of enforcement. Following  
20 your draft guidelines, the proper sanction imposed on the  
21 firm for use of the input causing the pollution, would be  
22 \$40, the amount of harm cost. Now, let's say the oil  
23 refinery pays tax at a marginal rate of 35 percent, then  
24 the after tax cost of the input of labor would be \$66;  
25 \$100 input cost, less \$34 tax benefit. If the monetary



1 sanction for the use of the pollution input is nondeductible,  
2 the after-tax cost of the input generating pollution would  
3 be \$73; \$50 input cost, less \$17 tax benefit, plus \$40  
4 sanction. You see, then, the firm would choose the  
5 socially inefficient input that is in this case, the tax  
6 consequences would be that the firm would choose the labor  
7 input.

8           The result of all -- of such nondeductibility, is  
9 that there would be higher costs of production and in-  
10 efficient use of resources.

11           Our second point is with regard to equity. While  
12 the draft guidelines purport to reject the use of size of  
13 the organization or financial performance as measures of  
14 sanctions, this may not be true. Disallowing tax deductions  
15 for amounts paid as sanctions, increases the amount of the  
16 penalty. Offenders with higher marginal tax rates bear  
17 greater costs from the disallowance than offenders in lower  
18 tax brackets. No, or little additional cost is imposed on  
19 offenders who are either exempt from taxation, such as  
20 tax exempt hospitals and universities, or have substantial  
21 net operating losses. There's no apparent justification  
22 for such disparate treatment. The failure to consider tax  
23 consequences also results in disparate treatment for dif-  
24 ferent offenses. The current tax system provides for  
25 deductibility of amounts paid for some sanctions but not

1 for others. While the draft guidelines may present a  
2 coherent treatment of monetary sanctions on a pretax basis,  
3 the post-tax results will likely be quite different.

4 In light of our two arguments, we recommend that  
5 the sentencing guidelines for organizational defendants  
6 consider the tax consequences of monetary sanctions.

7 There are two alternatives. First, coordinate  
8 with Congress to allow for full tax deductibility for mone-  
9 tary sanctions and set such sanctions in accordance with  
10 your draft guidelines. Alternatively, the second approach,  
11 for those sanctions that are not deductible, adjust the  
12 amount of the monetary sanction to reflect the marginal  
13 tax rate of the offender.

14 For instance, if the offender bears a marginal  
15 tax rate of 34 percent, then the monetary sanction should be  
16 multiplied by a factor of .66, that is, one minus the mar-  
17 ginal tax rate. With regard to our earlier example, the  
18 amount of the sanction should not be \$40, but it should be  
19 \$26.40.

20 We believe that either of these approaches would  
21 ensure an efficient use of scarce economic resources by  
22 organizations producing goods and services, and also result  
23 in a more equitable treatment of potential offenders.

24 JUDGE WILKINS: Thank you very much.

25 Let me ask you, in a related area, do you think

1 that civil assessments should be deducted from the criminal  
2 sanction?

3 PROFESSOR ZOLT: Commissioner Wilkins, do you mean  
4 the civil assessments, a coordinated approach between civil  
5 assessments and criminal sanctions?

6 JUDGE WILKINS: Well, since we can't control the  
7 civil assessments, we would have to view it as -- yes,  
8 coordinated, but if it's going to be coordinated, we would  
9 have to do it under the guidelines, the same as restitution.  
10 Do you think that should be deducted from the monetary  
11 sanction imposed as a criminal punishment?

12 PROFESSOR ZOLT: I think if you adopt the harm  
13 based deterrent approach, yes, it should be, but our point  
14 really doesn't hinge on the harm basis deterrent approach.  
15 Certainly, civil damages are, in almost all cases, deduc-  
16 tible and if you're coordinating civil and criminal damages  
17 and the criminal damages are not, you can see a firm much  
18 preferring to settle civilly than it would for criminal  
19 sanctions. So, you create some perverse incentives here  
20 because the income tax would favor civil penalties over  
21 criminal penalties. And if you're seeking to make the laws  
22 more uniform and consistent, then the failure to consider  
23 the tax consequences would raise such problems, especially  
24 in the case you brought up here.

25 JUDGE WILKINS: Thank you very much. Questions

1 to my right?

2 COMMISSIONER BLOCK: I have a couple of questions.

3 I wanted to thank you for appearing. Is this  
4 really second order effects -- I mean, tax consequences of  
5 criminal penalties; is that, you know, really second, or  
6 maybe third order effects?

7 PROFESSOR ZOLT: Well, I don't think it's second  
8 or third order effects the way economists traditionally use  
9 the term. If you are saying that the imprecision which you  
10 are arriving at the estimates because of imprecision in  
11 determining the amount of harm or the enforcement mechanism  
12 will swallow any tax effects, I don't think that's the case.

13 Certainly, if you're off by a substantial factor  
14 on the multiplier, the tax consequences may have little or  
15 no difference in the amount of the penalty. But if you're  
16 concerned about consistent treatment between taxpayers, I  
17 think you have to consider the tax consequences.

18 COMMISSIONER BLOCK: Well, I mean, you're dealing  
19 with organizations. Give me some examples of how much  
20 disparity would be created?

21 PROFESSOR ZOLT: Well, the maximum corporate --  
22 right now, it's 34 percent. You have many corporations  
23 that are in a tax loss position so they'll have substantial  
24 net operating losses which will pay no tax at all. It seems  
25 to me unfair that one corporation will, indeed, bear a

1 greater liability from fines and penalties than another  
2 corporation. In addition, you have a large number of  
3 violators which are not subject to the tax system, like  
4 University of California, Los Angeles. And in that case,  
5 the fines may be set at too high or too low a level,  
6 depending on how the fines are assessed to begin with.

7 COMMISSIONER BLOCK: Well, just as a point of  
8 information, the 1,200 cases that we looked at, from '84  
9 to '87, there wasn't one nonprofit in the federal system.

10 PROFESSOR ZOLT: There was no hospitals?

11 COMMISSIONER BLOCK: No.

12 PROFESSOR ZOLT: Or universities engaged in --

13 COMMISSIONER BLOCK: No, well, I don't know --

14 PROFESSOR ZOLT: -- pollution --

15 COMMISSIONER BLOCK: -- I don't know what they  
16 were engaged in, but they weren't sentenced in federal court.  
17 I can't speak for what they were engaged in, but I guess  
18 I'm still unpersuaded by the importance of the effect, given  
19 all the other uncertainties there are in calculating the  
20 loss, calculating the multiple. That seems to me to be,  
21 you know, gilding an unknown rose.

22 PROFESSOR P'NG: Well, calculating -- say we did  
23 a multiple and you multiplied by three, that's to multiply  
24 the sanction by three, then the taxes to divide by -- to  
25 multiply by two-thirds; they're the same sorts of numbers

1 that you're multiplying, which is what you say with the  
2 offense multiple, or divide by, which is what we say we  
3 would do with a tax rate. I mean, if you think one is small,  
4 the other is going to be small, too.

5 COMMISSIONER BLOCK: Your suggestion, then, as  
6 we're looking now -- we're looking at firms here, no non-  
7 profits, okay.

8 PROFESSOR P'NG: Um-hum.

9 COMMISSIONER BLOCK: Some may be firms, I mean,  
10 your suggestion comes down to the following, I think, that  
11 essentially, if you have a firm that's not generating the  
12 profit in the current year, well, then in fact, you pass  
13 through -- there are no taxes, so there's no adjustment. If  
14 you have a successful firm, a very profitable firm, then  
15 you reduce the fine down to .66 so that, you know, if it's --  
16 I mean, this will translate in terms of small, large firms,  
17 very often having proportionally higher fines for small  
18 firms than large firms in a pretax environment, although  
19 the post-tax is going to be the same.

20 PROFESSOR ZOLT: If you made such an adjustment,  
21 you could achieve the same thing by making the sanctions  
22 deductible.

23 What we're concerned about is -- we're not arguing  
24 for fines or penalties to be raised or lowered; we're just  
25 saying that you have to consider the tax considerations.

1           COMMISSIONER CORROTHERS: I guess I'm not clear;  
2 maybe I will be after I study your testimony which I just  
3 received, but when you consider tax consequences in es-  
4 tablishing the monetary sanctions, are you providing ap-  
5 propriate punishment to the violating organization and are  
6 you leaving sufficient incentive to the prosecutor to spend  
7 time and effort on the case? I guess I'm not clear about  
8 that.

9           PROFESSOR P'NG: As far as the appropriate level  
10 of deterrence, what we're doing, we're taking your guide-  
11 lines and we point out that so far, your guidelines have  
12 not taken into account this tax factor. If there were no  
13 taxes, then your guidelines would be the correct guidelines  
14 in our opinion.

15           We are submitting -- we submit that we should  
16 adjust for the tax guidelines, for the tax consequences so  
17 that your guidelines will then be the correct ones, to ensure  
18 the efficient level of deterrence of potential offenses to  
19 -- that might be committed by organizations. In fact, the  
20 general thrust of our submission is to get that level of  
21 deterrence. And as far as incentives for prosecutors,  
22 I don't know what -- I don't know -- have no answer on that.  
23 It seems, I cannot see any reason why the incentives would  
24 be any greater or less under our approach.

25           COMMISSIONER CORROTHERS: So you don't really see

1 the punishment being lessened through a consideration of  
2 the tax consequences because that's what I was seeing. Per-  
3 haps I have not studied your testimony sufficiently.

4           PROFESSOR ZOLT: There's really two ways to look  
5 at this. If a fine is set at a before-tax level, and you  
6 give a tax benefit, you can say that that tax benefit  
7 reduces the sting, lessens the impact of the penalty, but  
8 if you consider the fact that a tax benefit will be applied  
9 and set the level at that level, providing the tax benefit  
10 just gets it at the right level. If you set the fine with  
11 the concept of nondeductibility in mind, then granting  
12 deduction reduces the sting. If you set the fine with the  
13 concept of deductibility in mind, then the policy of non-  
14 deductibility imposes an additional federal fine on the  
15 particular offense.

16           COMMISSIONER CORROTHERS: I guess I was just  
17 getting hung up on the fact that I don't like the idea of  
18 reducing the sting, thank you.

19           JUDGE WILKINS: Any questions to my left?

20           Well, Professor Zolt and Professor P'ng, we  
21 appreciate -- oh, excuse me, Judge, you have some questions?  
22 Go ahead.

23           COMMISSIONER MacKINNON: You're proposing that  
24 the fines be adjusted to take care of the tax consequences,  
25 not that the taxing statutes be amended in a certain way to



1 allow certain deductions or not?

2 PROFESSOR ZOLT: Well, Commissioner, we're pro-  
3 posing either of the two solutions which we think will get  
4 to the same result; that either you would allow a deduction  
5 for all fines and sanctions in which case your guidelines,  
6 we think, produce the correct result under a theory of  
7 harm-based deterrence; or if you cannot coordinate with  
8 Congress to change the rules on the tax deductibility of  
9 certain sanctions, then, yes, we're suggesting that the  
10 fines be amended for individual offenders to reflect their  
11 tax rates.

12 COMMISSIONER MacKINNON: You admit that we'd  
13 have to amend the tax statutes to get to the other -- to  
14 the second objective that you seek?

15 PROFESSOR ZOLT: That's correct. That's correct.

16 PROFESSOR P'NG: So, it's in that light that we  
17 presented two alternatives; one would require the joint  
18 action with Congress, whereas the other would be simply to  
19 adjust the guidelines and perhaps the latter would be  
20 easier to accomplish.

21 JUDGE WILKINS: I would suggest, sir, you don't  
22 really think that Congress would amend the tax laws to  
23 provide a deduction for those who pay criminal fines? I  
24 don't know how far we'd get with that suggestion if we were  
25 to go there with it.

1           PROFESSOR ZOLT: You would have gotten pretty far  
2 up to 1969 from the time income tax were first passed, until  
3 1969, the tax system was viewed as a neutral tax authority  
4 and you would have gotten a deduction for that, provided you  
5 can establish it being related to your business. The Court  
6 did, in 19 --

7           COMMISSIONER MacKINNON: You mean a fine?

8           PROFESSOR ZOLT: What the Court did in 1969 was  
9 codify the public policy doctrine, Judge MacKinnon, which  
10 I'm sure you're familiar with.

11          COMMISSIONER MacKINNON: You mean that fines were  
12 deductible prior to '69?

13          PROFESSOR ZOLT: In some cases yes, in some cases  
14 no. It was a very inconsistent treatment and then you had  
15 the Supreme Court case in 1956, Tank Truck Rentals, which  
16 led Congress to codify the public policy doctrine in 1969.  
17 But, Commissioner Wilkins, before 1969, Congress did allow  
18 the deductibility of those amounts. Congress allows de-  
19 ductibilities for punitive damages, fraud payments --

20          COMMISSIONER NAGEL: But, you're saying for  
21 criminal fraud?

22          PROFESSOR ZOLT: For certain type of fraud pen --  
23 I don't know what the answer is for criminal fraud. I  
24 suspect --

25          COMMISSIONER NAGEL: I think he was talking about

1 criminal; that's the question.

2 JUDGE WILKINS: Only criminal. That's all we're  
3 talking about.

4 But in any event, the other alternative we could  
5 take care of in the guidelines or follow the other -- the  
6 alternate approach that you suggest.

7 PROFESSOR ZOLT: That's correct.

8 COMMISSIONER BLOCK: Is restitution deductible?

9 PROFESSOR ZOLT: Yes, it is. All compensating --  
10 all compensatory damages are deductible.

11 COMMISSIONER BLOCK: Including criminal resti-  
12 tution?

13 PROFESSOR ZOLT: That, I don't know. I suspect  
14 yes.

15 COMMISSIONER BLOCK: Is that easy for you to find  
16 out?

17 PROFESSOR ZOLT: Not too hard.

18 COMMISSIONER BLOCK: I'd appreciate it.

19 PROFESSOR ZOLT: Okay. Thank you.

20 JUDGE WILKINS: Professor Zolt, Professor P'ng,  
21 thank you very much.

22 PROFESSOR ZOLT: Thank you very much.

23 JUDGE WILKINS: Our next witness is Maygene Giari.  
24 Giari -- did I pronounce your first name correctly? Maygene?

25 MS. GIARI: It's an Italian name but not even

1 Italians can pronounce it.

2 JUDGE WILKINS: Well, I certainly won't try again,  
3 then. I will say and introduce you to those assembled here,  
4 that Ms. Giari is a member and advisor to CURE, Citizens  
5 United for the Rehabilitation of Errants and we are no  
6 strangers to your organization and we have participated with  
7 CURE and its Executive Director, and Administrator, Charles  
8 and Pauline Sullivan from the inception of our work and we  
9 appreciate the efforts of your organization and the efforts  
10 that you have made in presenting the written testimony that  
11 we have received and we look forward to your oral statement.

12 Thank you.

13 MS. GIARI: Thank you. I appreciate the opportunity  
14 to appear on behalf of CURE.

15 Just a couple of background comments so that you'll  
16 know why CURE asked me to represent them. Studies by the  
17 League of Women Voters on the prison system, on sentencing  
18 and parole in Oklahoma, made me realize that I had had a  
19 great many misapprehensions about the entire criminal  
20 justice system. And that was sort of a challenge so for  
21 the last 15 years, I've been studying quite diligently.  
22 It's been my major occupation, and on the assumption that  
23 many of my fellow citizens are equally misinformed, I'm  
24 writing a book, which, essentially, comes down to a concerned  
25 citizen looks at the criminal justice system.

1           My testimony today relates to the question, should  
2 organizational sanctions be based on past sentencing  
3 practices? Now, earlier, the Commission expressed concern  
4 about a public perception of a double standard of justice,  
5 one for the affluent and influential, and another for every-  
6 one else.

7           Past sentencing practices are the cause of that  
8 belief in a double standard of justice and the use of  
9 those practices as the basis for organizational sanctions  
10 could only perpetuate public skepticism without a quality  
11 of justice. And perhaps as a concerned citizen, rather  
12 than a more objective professional, I can give a little  
13 additional insight into the problem of the public per-  
14 ception.

15           Now, many of the features in the discussion  
16 materials could go far toward restoring public faith in  
17 the single standard of justice. The emphasis on victim  
18 restitution compensation wherever feasible, is certainly  
19 an excellent departure from present sentencing practices.  
20 But even greater emphasis given to coordinating compensa-  
21 tory remedies through civil administrative -- through  
22 administrative or civil enforcement raises some serious  
23 questions. Now, the draft guidelines do mention once, that  
24 the court should consider whether alternative compensation  
25 would be more burdensome, more costly or longer delayed than

1 criminal restitution for victims. The Deputy Chief Counsel  
2 suggested that collateral remedies might be ignored,  
3 possibly with the right to petition for modification if  
4 such remedies are provided. But the more frequent mention  
5 that civil remedies are more likely to be available,  
6 practicable, less costly and less difficult to enforce,  
7 does suggest a preference for those remedies and other  
8 comments that civil or administrative enforcement actions  
9 far outnumber criminal prosecutions against organizations  
10 also suggests this type of action may be preferred to  
11 criminal prosecution.

12           There are several problems involved in this  
13 approach, and I'm speaking most particularly of the  
14 regulatory agencies whose violations have the most effect  
15 on sickness, injury or death.

16           Now, administrative enforcement actions, by the  
17 regulatory agencies, have been minimal in some of the most  
18 serious cases involving product and worker safety, or other  
19 life and health threatening situations, or such actions  
20 have come only after a number of nongovernmental civil  
21 injury suits have been filed, or even settled. Administra-  
22 tive inaction may well be the reason why the report on  
23 sentencing practices showed more economic offenses than  
24 violations of environmental and health and safety regu-  
25 lations. When administrative actions have been taken, too

1 often, they've been inadequate in terms of the harms caused.  
2 The sanctions that have been imposed on organizations, and  
3 their responsible officers for policies that have caused  
4 many deaths, injuries, or serious illnesses, are in no  
5 way comparable to the penalties imposed on the blue collar  
6 offender who commits only one such offense.

7 One example is the fines imposed on Eli Lilly, on  
8 one of its former officials in the Arthritis Drug Oraflex  
9 case.

10 The Government's interest in achieving regula-  
11 tory objectives will not be achieved if the regulatory  
12 agencies' record in their enforcement of violations does  
13 not improve. Now, another problem is that civil litigation  
14 puts the burden of enforcement on citizens instead of  
15 on the Government. But nowhere is Government enforcement  
16 more appropriate than in life or health threatening  
17 situations.

18 In addition, civil injury suits are likely to  
19 result in inadequate compensation for harm. Many victims  
20 may not be aware of their rights, or lack the resources to  
21 pursue legal remedies. Victims may be forced to accept  
22 the lower settlement than their cases warrant.

23 The pressure to settle is often strongest on  
24 those who have been injured the most and those who can  
25 least afford the delay of a civil suit.

1           The notice to victims and criminal restitution  
2 outlined in the guidelines, if ordered by the sentencing  
3 court, would not only avoid unwarranted duplication of  
4 effort, resulting from litigation in many courts, but  
5 would promote greater efficiency and consistency in remedy-  
6 ing the harms done.

7           Organizational probation as a supplement to  
8 monetary penalties as outlined in the discussion draft on  
9 probation, would be a very desirable departure from  
10 present practices. Preventive probation to provide both  
11 the means and the incentive for the organization to  
12 strengthen its own controls, or to carry out remedial  
13 measures is an especially worthy objective. The conditions  
14 for imposing preventive probation, as enumerated in the  
15 discussion draft, seemed quite clear and comprehensive.  
16 After reviewing these conditions, the court shouldn't have  
17 any difficulty in determining whether preventive probation  
18 was appropriate without needing to rely on subjective  
19 judgment.

20           Preventive probation is especially desirable when  
21 the offense involves danger to the public health and safety  
22 such as the improper disposal of toxic chemicals, suppres-  
23 sion of design safety defects or sale and promotion of  
24 products known to be carcinogenic. Such harms are so  
25 serious that preventive probation monitored by excerpt. (sic)



1 should surely be warranted to prevent repetition of the  
2 offense.

3 In that connection, the discussion draft of the  
4 guidelines on upward departures if the offense resulted in  
5 the substantial risk of serious bodily injury or death,  
6 is less comprehensive than in the sentencing guidelines.  
7 The latter include any article, product or commodity  
8 produced or distributed for consumption by individuals.  
9 This more inclusive definition, it seems to me, is needed  
10 for organizations as well as for individuals. Nor do the  
11 discussion guidelines include any specific reference to  
12 ultimately fatal illnesses, such as brown lung, silicosis,  
13 cancer or asbestos related diseases resulting from exposure  
14 to harmful substances in the workplace. Nor do the  
15 departures authorized by passage of time include any re-  
16 ference to such fatal illnesses which developed long after  
17 the regulatory violation has been knowingly risked.

18 Additional departures, thus, should be authorized  
19 for organizational sentencing.

20 The concern that direct Government intervention  
21 is likely to harm the economy, appears to assume that the  
22 greatest possible social loss is economic harm. Protection  
23 of its citizens is a major purpose of Government, and  
24 surely, protection of life and health threatening protection  
25 against life and health threatening organizational policies

1 is at least as important as protection against external  
2 threats.

3           Primitive man is said to have considered human  
4 sacrifice necessary to ensure good crops. Civilization  
5 can't have advanced very far if human sacrifice is accepted  
6 as necessary to promote a flourishing economy. Preventive  
7 probation as a supplementary sentence could do more to  
8 restore public confidence and equality of justice than  
9 almost any other sanction. The explanation of Professors  
10 Coffee, Gruner and Stone, of why this would be true, can  
11 hardly be improved on. I hope you'll bear with me if I  
12 read it. I think it's so well done.

13           "In the public's eye, a precisely calibrated  
14 system of fines may be perceived as amounting to a tariff  
15 system that permits corporations to engage in criminal  
16 behavior so long as they're prepared to pay the specific  
17 tax. And quite possibly, some corporations also share  
18 this view. Ultimately, the aim is to prevent the prohibited  
19 behavior not simply raise the cost of engaging in it. It  
20 is particularly important to communicate clearly that  
21 probation, as a supplementary sentence, makes clear that  
22 there is no price that when paid entitles the organization  
23 to engage in the misbehavior."

24           Now, finally, in the staff working paper, the  
25 Deputy Chief Counsel many times reiterates such statements

1 as, "The social costs of punishment can outweigh its  
2 benefits. Enforcement and punishment are also uncertain.  
3 More deterrence is not always better and will be worse when  
4 the conduct deterred is less harmful than the effects of  
5 the deterrent itself." These arguments are presented eloquently  
6 and convincingly and they are also applicable to many blue  
7 collar crimes. But these cost benefit considerations ap-  
8 parently were not included in the preparation of the  
9 sentencing guidelines and policy statements. Applying  
10 these considerations solely to organizational crime could,  
11 again, increase the public's perception of a double standard  
12 of justice.

13 JUDGE WILKINS: Thank you, Ms. Giari. As you know,  
14 the publication, the draft proposal as you refer to it, has  
15 not been approved by the Commission. It was published and  
16 distributed to generate and provide a vehicle for public  
17 input.

18 MS. GIARI: I understand that.

19 JUDGE WILKINS: That draft proposal is on the --  
20 I think, characterized, it takes a -- or at least suggests  
21 the use of probation for organizational -- as an organi-  
22 zational sanction, as a limited means or in a limited way.  
23 You would suggest that probation for organizations is an  
24 effective means of dealing with corporate criminal violations  
25 and should be used more extensively than the proposal might

1 suggest, is that correct?

2 MS. GIARI: Yes, I am.

3 JUDGE WILKINS: I see. Well, thank you very much.

4 Let me ask, any questions to my right?

5 COMMISSIONER BLOCK: Just a short query on your  
6 comment about, you mentioned the so-called double standard  
7 of justice. I'm wondering, and you've spent a reasonable  
8 amount of time looking at this area; have you done any  
9 systematic work on the comparisons of so-called blue collar  
10 punishment and so-called white collar punishment? Did you  
11 make that available to us?

12 MS. GIARI: Yes. I've read quite a bit on it. I  
13 have read quite a bit about it, yes.

14 COMMISSIONER BLOCK: And would you make that  
15 available to us, whatever work you've done on that?

16 MS. GIARI: I can work it up, yes.

17 COMMISSIONER BLOCK: Thank you.

18 COMMISSIONER CORROTHERS: Ms. Giari, the concern  
19 that you attributed to the Commission about the public  
20 perception of a double standard of justice, one for the  
21 affluent and influential, and another for others, I hope is  
22 accurate in terms of being the Commission's opinion. Those  
23 specific, in fact, those exact words have been uttered by  
24 yours truly, again and again, since 1986. I hope they also  
25 share that. But, so, I therefore, do share your and CURE's

1 concern for equality of justice.

2           You have noted in your testimony, the existence of  
3 unwarranted disparity in penalties between organizational  
4 offenses and those for blue collar offenses. In my experi-  
5 ence with the criminal justice system, it appears at least  
6 possible that with regard to sanctions for individual  
7 offenders, the overall purposes of sentencing are emphasized  
8 to a greater extent than with organizations. For example,  
9 cost effective concerns; fears of being too intrusive; fears  
10 of overdeterrence; do not appear to be a primary concern  
11 when we look at the incarceration rate or individual san-  
12 ctions in general.

13           Do you think that as a general thing, that we can  
14 improve the system's handling of organizational sanctions  
15 by concentrating more on the overall purposes of sentencing,  
16 such as punishment deterrents and rehabilitation which can  
17 be achieved through probation, et cetera? Do you think that  
18 as a general way of looking at it, we could improve this  
19 equality of justice if we concentrated in looking at overall  
20 purposes of sentencing?

21           MS. GIARI: Yes, I think that's a part of it that's  
22 necessary. I certainly go along with the idea that in  
23 organizational sanctions, you need to provide the incentive  
24 and the direction for avoiding any future violations and  
25 for remedying any that have already occurred. It seems to

1 me that would be of equal importance with the purposes of  
2 sentencing.

3 COMMISSIONER CORROTHERS: Okay, thank you.

4 JUDGE WILKINS: Thank you. Any other questions?

5 COMMISSIONER NAGEL: I just wanted to thank you  
6 again for your thoughtful comments. You've been most help-  
7 ful as CURE has been throughout our proceedings.

8 MS. GIARI: Thank you.

9 COMMISSIONER MacKINNON: I'd just like to say a  
10 word about diversity. It's been dealt with in a very  
11 general way, with practically everybody, the assumption  
12 being that if you've got something that isn't completely  
13 like every other sentence, why, you're creating diversity.

14 As we read the legislative history of the Act,  
15 and as our hearings around the country have shown, it  
16 isn't just diversity that they're talking about. It's wide  
17 diversity, and consequently, if you take out the sentences  
18 on the top and the bottom that are just not supportable,  
19 that you have in the middle a group of sentences that are  
20 fairly reasonable and which can be relied upon as a starting  
21 point. And, so it isn't just plain diversity. It's wide  
22 diversity that is the real objective of the guidelines.

23 MS. GIARI: Yes.

24 COMMISSIONER MacKINNON: On diversity.

25 MS. GIARI: I understand that and you certainly

1 need a starting point.

2 JUDGE WILKINS: Again, thank you very much.

3 In keeping with the policy we followed the last  
4 three years, we now make the microphone available to anyone  
5 who wishes to address the Sentencing Commission on the  
6 subject of corporate sanctions or any related issue.

7 Seeing no one wishes -- all that have spoken have  
8 done so, now, we have concluded our business. This hearing  
9 is now adjourned.

10 Thank you very much for your participation.

11 (Whereupon, at 3:42 p.m., the hearing in the above-  
12 entitled matter was adjourned.)

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This is to certify that the attached proceeding before the United States Sentencing Commission, Public Hearing on Organizational Sanctions, held Friday, December 2, 1988, at Pasadena, California were had as herein appears, and that this is a true, accurate and complete transcript prepared from the tape made by electronic recording.

*Ralph [Signature]*  
V/ARS, Inc. *eg*