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United States Sentencing Commission
Hearing on Organizational Sanctions

June 10, 1986

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UNITED STATES SENTENCING COMMISSION

PUBLIC HEARING ON
ORGANIZATIONAL SANCTIONS

JUNE 10, 1986

CHARIMAN WILLIAM W. WILKINS, JR., Presiding

(THE TRANSCRIPT WAS PREPARED FROM A TAPE RECORDING.)
CHAIRMAN WILKINS: Let me call this public hearing to order. This is the third in a series of public hearings that we will be conducting throughout the summer. The first hearing dealt with offense characteristics and the seriousness of criminal conduct. We just recently had a hearing on prior record of offenders. Coming up is a sentencing options hearings and plea negotiations. And as you know, today's public hearing will concentrate on the issue of organizational sanctions. I might say that the public hearings that we've held to date have been most helpful to the Commission in framing issues dealing with the subjects which were discussed.

And I feel that and I'm sure that this hearing will also be very helpful to us. I might add that the work that the witnesses have done in advance, and the written testimony that we have received exhibits a great deal of thought and effort and hard work.

And the Commission has received the testimony and we very much appreciate all the work that all of you have done in preparation for this hearing.

I might add, too, that we have received written testimony from a large number of other individuals and
organizations addressing this issue. And all of this of course is part of our public record and will be studied by the Commission staff as we address the issue of organizational sanctions.

And when you think of guidelines, most of the time, you only think of individual sanctions. What do we do about the drug dealer or the bank robber, or someone like that.

But we need to focus a great deal of our energy and work on organizational sanctions, particularly in the federal section. And to this reason, we have scheduled this hearing to address that single issue.

We have a number of fine witnesses and experts in the field. What we'll do is we'll play our timetable somewhat by ear, although we do have a schedule. But I do not want to restrict any witness because of time constraints.

In addition to that, at the conclusion of our hearing of the witnesses of the schedule, any person in attendance will be given an opportunity to comment or make any statements that he or she feels is appropriate.

Our first witness to testify are attorneys representing the American Bar Association, a Mr. William M. Brodsky and George C. Freeman, Jr.

Gentlemen, if you would like to come around and
we may sit together.

       Good morning.

       STATEMENTS OF MR. WILIAM M. BRODSKY, and
       GEORGE C. FREEMAN, JR.,
       AMERICAN BAR ASSOCIATION

       MR. BRODSKY: Good morning, Mr. Chairman, Members

       of the Commission. My name is William M. Brodsky. I'm a

       practicing attorney. All of my professional life, I've been

       involved in the criminal law, starting out as an officer in

       the Judge Adjutant General's Corps, United States Army; then

       as an Assistant U.S. Attorney. And for the last eight

       years, I've been a defense lawyer, practicing in New York

       City.

       I am active member of the American Bar

       Association. I'm the Vice Chairman of the White Collar

       Crime Committee of the Criminal Justice Section of the ABA.

       With me today is George Curman Freeman, Jr.

       Mr. Freeman is a partner in a Richmond, Virginia firm, with

       Washington, D. C. offices at Hungtinton and Williams.

       He is currently the delegate of the section of

       the Corporation Banking and Business Law, the ABA House of

       Delegates, and is a former chairman of that section of Ad


       In the past, together with Professor William

       Greenhall of the Criminal Justice Section, Mr. Freeman
testified for the ABA for various House and Senate committees that were considering federal criminal code legislation.

Mr. Freeman is very well-versed in this area and especially knowledgeable of special topics relevant to this hearing today. That is, organizational sanctions, the appropriateness or inappropriateness of criminal sanctions for regulatory -- that is, offenses not found in Title 18.

We would like to divide our testimony this morning...the Commission. I will briefly highlight, summarize the ABA standard with respect to organizational sanctions.

Mr. Freeman would like to comment with respect to appropriate treatment or regulatory Title V's.

Mr. Chairman, I understand that our printed remarks will be incorporated for the record and I will not repeat them, but just summarize them for the Commission.

CHAIRMAN WILKINS: That's correct. They will be incorporated in total. And it is a good idea to, and not only you, Mr. Brodsky, but other witnesses, if they will summarize the written testimony. And that will give us more time for dialogue between you and the Commission.

MR. BRODSKY: Essentially, Mr. Chairman, the ABA standards which are -- this is one of the many volumes of the ABA standards. That regarding the sanctions is one of
The issue of how does one punish an organization, corporation or an association, who cannot be incarcerated, is one of the most difficult.

How does one think in terms of adequate punishment and sufficient, specific in terms, on behalf of a corporation who poses a significant problem?

The ABA has recommended in effect five methods by which this can and should be achieved.

The first one is restitution. Making whole the victims of any crimes caused by a corporation. In this connection, it's significant to point out that the injury to the victim should be the approximate cause by the corporation's or association's malfeasance.

That is, that there must be a causal connection between the corporation -- and the claim for restitution. I must point out that this restitution or sanction should be in conjunction with all the other significant civil remedies that exist.

Indeed, in determining what is an appropriate sanction, any amounts paid under restitution put into our policy should be set off from any subsequent civil action, whereby the victim, under more liberal rules, may be able to recover significantly greater amounts.

The restitution sanction recommended by our
association limits the amount to be paid to the victims to actual out-of-pocket pecuniary loss, not in such things as separate other punitive damages. Those are relative, should be, to the civil side.

The fact of restitution, that restitution was ordered by a court, should not be admissible in any way in a civil proceedings that may or may not follow after the criminal process.

In any determination of how much restitution should be paid, the court should acquire a government or the claimant to establish by a preponderance of the evidence this particular claimant is one that was wronged by the corporation's wrongdoing, and that the amount of restitution is that which was felt by the out-of-pocket expenses.

In this connection, I think it's somewhat out of order, the notice of conviction, which Congress has also written -- is one that the ABA recommends as an appropriate sanction.

The goal of acquiring association or an organization convicted of a crime, to publicize that fact, one can envision as the statute and our standards indicate, can add to the Wall Street Journal for any national or local publications, and alert those groups that were harmed by the corporation's wrongdoing, put in claims under the restitution section. And thereby effectively implement the
restitution sanction.

And also to the aspect of the publicity that will come from the notice of conviction or sanction is one that is appropriate.

It is significant, however, that the notice of conviction sanction should not be used to hold up to public ridicule any individuals or corporations who may have committed a crime.

This is not, as far as the ABA standard is concerned, the intent of notice of conviction. It is designed primarily to let the public be aware that this particular entity has violated the law and gained whatever deterrents may occur to regular market forces as a result of.

And, secondly, to alert those potential victims that may have a claim they can lodge against the corporation.

Secondly, the aspect of a special fine schedule, that is, fines that would be posed on a corporation, a greater punishment, if you will, than the simple monetary amounts that are set forth in the statute.

This is important because in many institutions, the cost of compliance by a corporation with certain regulatory requirements may far exceed the potential fine that could be imposed in a criminal context.
The ABA, as many other groups, have wrestled with what amount of special fines would be appropriate for an organization that violates certain kinds of ... and the ABA standards, as approved by the House of Delegates, says that it's only the amount of pecuniary gain that the corporation made from its wrongdoing, or conversely, the amount of pecuniary loss that the corporation caused to the victim that should be imposed as a sanction.

The belief here is that one wants to make the sanction significant enough so that the corporation will be deterred from violating the law, and not simply coming up with a fine that costs much less than the cost of the crime.

At the same time, not to propose a punitive sanction on the corporation that would so distort the process that it would, in effect, be an unconstitutional violation of a principle of -- in the punishment and the offense.

Next there is the issue of misqualification from office. This is a sanction which both in the statute as adopted by Congress and in the ABA standards applies really only to individuals who have been convicted of a crime.

There is nothing in the statute, and certainly in the ABA standards; we recommend strongly against the imposition of any punitive criminal sanctions against any individual human being who has not been convicted of a
crime.

If the corporation needs to be sanctioned, that can be done through the continuing official oversight and will all come to an annulment.

But disqualification from office may be an appropriate sanction under the strict, narrow guidelines set forth in the ABA standards, and as set forth in the statute, for a person who himself or herself was convicted of a crime.

The continuing judicial oversight. This is perhaps in some respects the most significant aspect of the ABA standards with respect to an organizational sentence in that it gives the court the widest kind of authority to assure that the goals of sentencing are achieved by an organization. There is the deterrence, it won't happen again.

Punishment, more significantly that the law will be complied with both specifically by that organization and by others. While the ABA, these standards were adopted in 1979, was against the concept of corporate probation, that was resulting from the philosophy of the existing law, which meant that probation was something that could only be imposed in lieu of incarceration.

Now, under our new statute, probation may be imposed as a punishment by itself and as a condition of that
probation, an organization may be required to impose on itself certain reporting requirements, certain investigatory requirements, sufficient that the court would have an ability to supervise whether the organization has ceased the illegal activity.

It has instituted reforms to assure that it will not return, and will report to the courts. And of course the contempt power of the court exists even though the corporation still can't be incarcerated. The wide variety of coercive sanctions the court can impose on the organization itself. And if that proves insignificant or ineffective in deterring the conduct, they can, in my opinion -- and I speak for myself -- that individuals within the corporation can be assigned the task of carrying out -- the corporation the continuing additional oversight functions, and that person could be subject to sanctions of the court.

These are then the five general principles that the ABA has established for organizational functions. There are three major -- that the ABA suggests to keep in mind with personal sanctions on any organization.

These are that the special fines and even the restitution should not be imposed in cases where -- damages can be obtained by victims or government agencies, such as in anti-trust cases; that any such sanctions or use of those
sanctions should be imposed only after a full adversary hearing where both sides would have an opportunity to protest the factual predicate on which the proposed fine -- reasonableness of the penalties, so that the courts can -- the --

With that, Mr. Chairman, I have finished my --

CHAIRMAN WILIKENS: Mr. Freeman.

MR. FREEMAN: It's a pleasure to be here today and see several old friends. I'd like to emphasize two points that Mr. Brodsky's just made, and then move on to my assigned topic, which is distinction that should be made between regulatory and common law type crimes.

I'd like to talk just a minute to emphasize how important it is in your guidelines to emphasize that in a particular way you are ordering restitution on the part of a corporation that you emphasize the importance of proximal quality improvement, and no relaxation on those standards.

Recently, the administration had a task force on the current prices in insurance availability and affordability. And they had a very interesting, informative report on that crisis.

And they really attribute that crisis to the perversion of tort law in the state tort system. That is, concept of causation has been eroded. Burdens of proof have been reversed. And, in particular, the concept of joint and
several liability has been extended far beyond its common law origins, were exclusively in conspiracy or concerted action.

And it's sort of a tort that causes unprincipled search for the deep pocket. And the report recommends a number of reforms, eight major reforms in those state systems.

Now, whether the states will make those reforms or whether Congress through some sort of preemption will adopt legislation, it does that, is part of -- we don't know how that's going to turn out.

But I think you have to be very careful in your guidelines to make it clear that the concept of restitution here is not going to turn into another unprincipled search for the deep pocket, that causation must be proven in fact.

There's no relaxation of the burden, no shifting of the burden. And the concept of joint and several liability has no place absent proof of conspiracy or concerted action.

I think that's very important to prevent restitution just recurring in an ad hoc way of substituting for the present tort system.

The second thing I'd like to emphasize in what's been said here is the importance of keeping in mind the concept of proportionality. And I would like to emphasize
its constitutional dimension.

Recently, relatively recently, the Supreme Court came out with a very interesting decision in Sohm versus Helm, where Mr. Justice Powell, writing for a thin majority of one, found that concept in the 8th Amendment and particularly as it applies to length of sentence.

But that decision is very interesting because in both the majority and the minority opinion, the statement is quite clear that the rights that we have under the Constitution and under the notion of due process were at least as broad as it existed in England at the time we gained our independence.

And of course one of the principal doctrines that was in force at that time and we still honor is the Magna Carta. And there are three chapters in Magna Carta that deal with an obscure concept called an immersila (ph.) And an immersila was the form from a heavy fine that was levied by either the king or the lord. And it essentially started out by taking all of a man's property.

And it was in effect a moderation from the earlier form where if you offended the king, he simply cut off your head and you were tainted. He got all your property and your heirs were disinherited.

So rather than cut off your head, he just took all your property. So, at Runnymede, the barons were going
to put an end to that. And so they put in a requirement, one for the lord, one for the bishop and one for the common man, that any taking of property had to be proportional to the event.

And, interestingly enough, it also had to leave the person, whether lord, bishop or freeman, with the means of making his livelihood.

And that concept has come down to us through the due process clause and it's been reinforced in the 8th Amendment.

So I think that it's very important that particularly in the area of fines, that you emphasize the importance of that concept of proportionality.

And there are two aspects to it. One is that you make the fine proportionate to the blameworthiness of the conduct and, second, that you bear in mind the second requirement of Magna Carta, which is to leave a person with adequate means in which to continue his livelihood.

And in the case of a corporation, particularly a large, publicly-held corporation, where you have a number of innocent people who are at stake, even if the leaders or some official in the corporation takes off and does the wrong thing, you have a number of investors who are totally innocent in the whole process.

And that makes this concept of proportionality
even more important.

And that brings me to my third point, which is the importance for you all to do in effect what Congress didn't do at the urging of the earlier Brown Commission, and then at the urging of our ABA back when the Federal Criminal Code was being considered in Congress several years ago.

And that is we have pointed out and they did earlier that in the area of regulatory offenses there has been an unfortunate tendency over the years to over-criminalize those statutes.

And various reasons account for it. I think the principal reason why those statutes are over-criminalized is the way Congress acts through the committee system. And many of you are familiar with the committee system and how it works on the Hill.

But, if you will think back about the number of regulatory bills that have gone through the Congress -- the Clean Air Act, the Clean Water Act, The Super Fund, RECLA, Securities and Exchange Act, all these other acts -- then it's very, very, very rare that there is consecutive or joint referral to the Judiciary Committee.

So the committees that are most expertise in what should be the most appropriate form of criminal sanction, that expertise is never brought to bear.

And you also know, those of you who are familiar
with the way the Senate and the House operate, that when those bills come to the court, there is usually no meaningful debate, particularly on the criminal sanction. It's just too complex to get up to speed with. And so these things go through with huge criminal sanctions in there often for conduct which is not only nonwillful or nonknowing, but it's often unavoidable.

And of course the excuse given is, well, EPA and the Justice Department will be denied exercise of their constitutional discretion and they will never go after the truly innocent people.

But, sometimes, political pressures build up and things fall through cracks. I would hope that in your guidelines you would particularly, specifically point out the need to distinguish between regulatory offenses that are what we would call (mallum in say), that is, everybody knows who they are. No doubt about it. And the kinds of offenses that are inadvertent, where, really, criminal sanctions are really inappropriate.

And certainly even when they're mandatory matters like knowledge, willfulness, inadvertent should clearly be reflected in the level of fines or the level of offenses in the organization.

So, there's a final aspect to that, too. And that is that a lot of these environmental statutes in
particular are technology forcing statutes. EPA sets standards to get the maximum amount of cleanup based on what it thinks the technology can be extrapolated to.

Scrubbers for power plants were a very good example of that. The earlier phases of those scrubbers didn't live up to what the manufacturers said they would. They didn't live up to...

(Conclusion of side 1, tape 1.)

...the suggestions, and it just didn't work for them.

So I think it's very important to recognize that because in the long run, too, law is the self-enforcer. And to be self-enforcing, you have to know what it is and it has to be -- has to conform with common sense. And you can't be put in the situation where you're told to supply power to the City of Washington using a certain technology, and then you find out the new technology doesn't work. You still have to supply the power.

Do you cut off the power? And people are in violation of criminal sanctions. So I think it's very important in your guidelines to distinguish between those types of situations and the type situations where people knowingly, willfully do something out of the way...

CHAIRMAN WILKINS: Thank you very much, Mr. Freeman. We'll have a question and answer period at
Mr. Brodsky, you testified and I believe in your written testimony indicated that the fine imposed on a corporation should be equal or not greater than the amount of gain or the amount of loss caused.

For example, a corporation in a criminal act makes a half million dollars or causes a loss of a half million dollars, the fine should not exceed a half million dollars.

Is that...?

MR. BRODSKY: That's essentially correct.

CHAIRMAN WILKENS: Does that say to a corporation, if you get caught, all you've got to do is give it back?

MR. BRODSKY: No. I think that what that says is that there are other courses in addition to the fine. The fine is not the only sanction that would be imposed on the corporation under that scenario.

In other words, there are a full panoply of sanctions that are available to the court. And any victim that may have been harmed by the corporation, the fine is in addition to any other sanctions.

The cost of compliance itself. In other words, the corporation is in effect being punished twice, if you will. It isn't just that they're paying to the court what
they should have paid to comply initially. They had to do that anyway, with the oversight, the probation. They've got to comply with the law.

And then this fine is a punishment. And I don't think that it's simply one single -- we rolled the dice and we lost, so we'll pay what we would have had to pay had we done it right the first time.

MR. FREEMAN: If I could supplement that with a few ideas. First of all, I think it's important to recognize when we're talking about corporations, we're also talking about the public -- situation.

Again, we get back to looking at an economic entity where there are a lot of stakeholders who are totally innocent of the behavior. And not only stockholders. It also can be employees.

And that's point number one. Point number two is we do have the criminal sanctions in there for the individuals. And the individuals who ordered the conduct, who planned it, where the sanctions apply to them individually, that's where you get the control of...

CHAIRMAN WILKINS: Do you think it would be appropriate in a given case for the court to appoint an accountant or lawyer, make the corporation pay for it, and have this person charged with the responsibility of developing a report of who within the corporate structure
made the decisions to violate the law? And would have that disseminated to all stockholders?

These innocent people, the stockholders out there, they may not know the corporate officers who were really involved with making the decisions.

MR. FREEMAN: I would hope that the U.S. Attorney would do that when he's bringing the action against the corporation, and would name those individuals and charge them individually with violation of the law.

CHAIRMAN WILKINS: But I want him to make sure that a copy of that indictment gets out to the stockholder in Omaha, Nebraska...

MR. FREEMAN: When they're convicted, I think that's what we're talking about.

CHAIRMAN WILKINS: One other question I wanted to ask you about the innocent shareholders. I realize that is a problem. In a civil suit, however, there is no consideration given to the innocent shareholder when a civil judgment is handed down against the corporation for some tort action or whatnot.

But you would suggest, in the criminal area, we should somehow take into account the fact that when I bought some stock in the ABC Corporation, I had no idea that it was going to be involved in criminal conduct?

MR. FREEMAN: Well, I will say this. When we
started out and I was one of the authors of our report, ad hoc report on the Federal Criminal by Sections, we really felt that restitution had no part in the civil and criminal law.

So the ABA position on it is a compromise position because we felt one of the real problems that you'd get into in this area, and I still think you get into it, is you give -- if it is charged that a large class of people have been injured and we're going to give them restitution, it almost becomes like a mass tort case.

And the problems of witnesses testifying when they are in the criminal proceeding, when they have a stake in the civil, you know, they're going to get a nice, you know, they're going to get some money out of it, it's a pretty tricky kind of area.

So I think really this is quite different from civil law, and I think that that's one of the main things you've got to keep. You've got to keep it distinct. And it can't be just an easy road to the tort system.

I think that's the real danger you have to guard against in this whole area.

CHAIRMAN WILKINS: Any questions?

COMMISSIONERS: Yes, Mr. Chairman, I have a question for Mr. Brodsky.

Among your five recommended sanctions, I'm not
clear as to how the sanction of continuing judicial oversight differs from probation. Probation was said to utilize a method whereby conditions would ensure the court that the organization had in fact ceased its criminal activity.

Could you clarify that for me?

MR. BRODSKY: Certainly. I'm going to try to put out my other remarks. It was that the ABA policy was directed in 1979, at a time when, in effect, a corporation could not be placed on probation. And due to the law, corporations now can be placed on probation.

The terminology "continuing judicial oversight" can in fact be implemented as a condition of probation. It's one of the conditions. And, indeed, that would be the way in which...

COMMISSIONER: Thank you.

COMMISSIONER: Mr. Brodsky, I want to follow up on this special fine schedule, just ask a clarifying question.

Where the recommendation is to have a single kinds of gain, monetary gain, by a single times the loss, and the question was asked:

Isn't that really a license, for example? It's difficult to reconcile that with deterrents, the use of fines for deterrents.
And your reply was, well, there are other sanctions. And my question is:

Why would they be preferrable to a multiple of the gain -- three times, four times gain?

In other words, you'd be using the other sanctions to impose costs on a corporation.

MR. BRODSKY: The philosophy and this is pertaining to the commentary...is that a punitive fine, if you will, would not have the same kind of deterrence against the organization as it would against an individual that has to pay the fine.

Indeed, the malefactor, the corporate officers, if you will, the agents of the organization, will have caused them an expense, will just pass the fine on to its customers by raising the prices, or as Mr. Freeman points out, to the shareholders by depriving them of their dividends. And that the philosophy underlying our position is that in fact it will not have the kind of deterrence that a normal fine would have upon an individual.

So that the other sanctions are creatively designed to try to achieve the same goal without punishing those, the customers and the shareholders, who are indeed innocent.

COMMISSIONER: But they would raise the cost to the corporation.
MR. BRODSKY: The logic seems to me to follow through. So there's a certain economic model that says that if a corporation pays a large sum of money, it will either have to pass that on to its product, and the public may choose not to buy their product, but that's very, very attenuating.

And the studies and the information -- to our standards points out that the persons who sit down, if you will -- if in fact they do -- and decide not to comply with a certain regulatory practice, don't think of those aspects of it, or would not in fact -- that kind of conduct.

MR. FREEMAN: Well, if you think about it this way, the D.C. Circuit just handed down a recent decision on a case in which I was interested. I was not the partner who argued the case. But it involved -- penalties under the Clean Air Act.

And on behalf of the utility industry, we had appealed the EPA regulation that set forth how those penalties were to be calculated. Said that the economics of a public utility are quite different from the economics of a competitive corporation.

And the court was very sympathetic but said that the Congress would never let that -- in order to appeal, we had to appeal to Congress, not to them.

But, even in that opinion, they recognized that
if, for some reason, again, go back to the technology -- the scrubber won't work and you are not in technical compliance -- that simply means that the people in Washington are going to pay more for their electricity because of the fine.

It doesn't affect the stockholders pretty much. And it's just the incidence is wrong. So I come back again, what we're thinking about, when you think about crime, think about the incidence is largely going to be on the people, on a group of individuals.

And, usually, they're the group of individuals who were not responsible in any way for the conduct. And so, again, we come back to the importance, when you are thinking about sanctions against organizations, bear in mind the concept of trying to operate only on individuals and don't operate on corporations.

And the place where the prosecutor ought to concentrate is on convicting the individuals, because they are the people who did it. And if you go and get them, then it operates as a deterrent to their fears; whereas, if you just sock the corporation and hit the stockholders, you really, you're just --

CHAIRMAN WILKINS: Any question to my left?

COMMISSIONER: Mr. Brodsky or Mr. Freeman. With regard to the issue of innocent shareholders, which is a
real issue, would it be unfair to assume that a fine levied against an organization will hurt the same innocent shareholders who, for the most part, are going to be benefitted by the organization's conduct in the criminal action by persons?

MR. BRODSKY: Indirectly, yes. In the sense that to the extent that the corporation makes larger profits because it did not comply with the law. We're talking about a situation where they would save money by not complying with certain requirements.

That is correct.

COMMISSIONER: I have a question for Mr. Freeman. He very eloquently cited us to Magna Carta earlier, talking about its request, demand that punishment be proportional, which would seem appropriate.

And the requirement that the person be left with enough to continue to live.

That makes sense, I guess, doesn't it, in the case of persons. But, clearly, does that make sense in the case of organizations?

I mean, it's not as if organizations, corporations, associations are citizens. They exist unlike human beings. They exist for the benefit of the rest of society. We recognize them as legal entities. We use them for our benefit.
Is it as clear that, for example, a liquidation sanction wouldn't be appropriate?

MR. FREEMAN: Well, I would say you raise a very interesting question. I had the privilege a few years ago when I got out of law school to be Clerk to Justice Black. And Justice Black was very open and encouraged us to ask him all kinds of questions.

One of the things I asked him one time was:

Why are corporations treated as persons under the 14th Amendment?

And he said:

That's a good question, George. And he said: Not even I am willing to go back and reopen that one. You've raised a very important and fundamental issue. But I think that's the cornerstone on which the economy of this country is built, the idea that a corporation does have the right of an individual under our Constitution.

I mean, it's been there since they passed the 14th Amendment.

COMMISSIONER: I think the crude response was simply for every situation, they insisted organizations are like persons. And to the extent that organizations serve certain purposes, we might want to recognize them and treat them as persons for some cases, but not for others.
Even that aside, to the extent that we have
something called the death penalty, and to the extent that
organizations have the ability because of their structures
to cause more societal harm and disruption than a single
individual, just gauging the extent of the harmed society
might appropriately lead to liquidation as a proportional
punishment.

MR. FREEMAN: Well, I come back though to the
fact that the corporation itself never does anything. It is
merely the instrument by which other people have. And if
we're talking about deterrence, retribution -- retribution
and deterrence -- all the sanctions would fall on
individuals who use that organization for its resources for
that purpose.

COMMISSIONER: I guess my problem is, with those
two arguments together, you can justify just about
anything. Organizations are not people. No one is
responsible. But, organizations are persons entitled to
every rights of citizens of the United States.

MR. FREEMAN: It's because we decided, and I
think it was -- I don't know. It was a long time deciding--
to extend that extra form of protection to that particular
way of holding property.

COMMISSIONER: Thank you.

COMMISSIONER: Two questions. Mr. Brodsky, what
do you think should happen in the anti-trust case, the
criminal case brought against a corporation?

If you don't think the corporation should be
fined, what should happen?

MR. BRODSKY: I'm not saying, your Honor, that a
corporation should not be fined.

COMMISSIONER: There will be federal damages.

MR. BRODSKY: Federal damages would be there.

COMMISSIONER: But saying what should happen in
the criminal case, where the corporation is convicted.

Undoubtedly, there are trouble damages involved. Now, this
is a different case.

What do you think the Judge should assess as
punishment against a convicted corporation in a criminal
anti-trust case?

MR. BRODSKY: The Judge could choose from a
panoply of sanctions.

COMMISSIONER: What?

MR. BRODSKY: And require the corporation to
institute indepth compliance, on the part of the board to
form a committee that would oversee anti-trust compliance
for education of his employees; hire outside counsel to
educate.

COMMISSIONER: That sounds like no punishment.

And if you say no punishment, is that seriously what you
MR. BRODSKY: Well, I'm not arguing for no punishment. But punishment is only one of the three basic goals of sentencing. Punishing deters and will be retribution, or in this case, restitution. If there are individuals who have been convicted, they certainly will be punished.

The corporation, if it has to pay trouble damages and has to prevent itself from doing it again, the sanction...

COMMISSIONER: All right. That leads to my second question. It's a problem that I certainly don't have the answer to.

In regulatory offenses, quite often there are strict liability perhaps or negligence phase. The notion of putting a human being in jail when he doesn't have a guilty state of mind is one I think rightly criminal law finds difficult to grapple with. It's a bad idea.

An individual going to jail who is out of the guilty state of mind is very unusual. But a corporation being punished criminally without a guilty state of mind isn't quite as objectionable perhaps as punishing a human being without a guilty state of mind.

Is that so?

I mean, if that is so, maybe the application of
strict criminal liability in certain instances in corporations but not individuals is quite a good idea. I'm interested in your views on that.

MR. FREEMAN: Well, I share your initial premise, that certainly law, it's a terrible thing to send somebody to jail without them having intended either knowingly or willfully done something wrong. Strict criminality applied to individuals to me is just --

When it comes to corporations, it depends, it seems to me, on what the purpose of the law ought to be. If you are going to -- in other words, why even have criminal sanctions when you can have civil sanctions?

That's the whole --

COMMISSIONER: You brand the behavior as very objectionable behavior. And in a sense, you get the virtue of telling the world: This is a terrible thing that has happened. Without the vise of putting a human being in jail without a guilty --

MR. FREEMAN: Well, I would say that the terrible thing in the regulatory hearings in the way it happens is that the conduct is normally punished with even just strict liability on the civil side is conduct which is totally inadvertent, even on the part of the corporation.

And in its hindsight in most instances. What we start off with in these regulatory areas are statutes that
are very vague, almost total power given to the regulatory agency.

A lot of the agencies cut corners. As you know, Judge, and they don't comply with the Administrative Procedures Act, and they don't vote for rulemakings and the rules aren't very clear. And they try to get by with case by case communication, often.

So people don't know until after they've done it that they've done something that's --

So that gets us back again to what is the purpose of sanctions in the whole regulatory area. And I think that the criminal sanctions should be applied only when you have a clear rule. Everyone knows the rule or should know the rule. The conduct is deliberate.

And under those circumstances, criminal sanctions are entirely appropriate. But, again, I think they should apply -- should fall the heaviest on the individuals involved. And not through some multiple or some notion of punitive damages against the corporation.

CHAIRMAN WILKINS: All right. Any other questions?

COMMISSIONER: How would probation violations be treated? You know, that's not in our guidelines specifically, but speaking for myself, I can envision a circumstance in which the court in effect appoints a special
MR. FREEMAN: Under criminal law?


MR. BRODSKY: No, sir, I think it's not contained within the statute. Under the new law, any condition of probation is what the statute says, the court can implement this continuing judicial oversight through that vehicle.

And this special master could advise the court of progress.

COMMISSIONER: What do you mean by a special master? That's one way of doing it.

MR. BRODSKY: The tools...the court could do away with the special master and simply set down, do two things. One, cause a study to be done by the board of directors. They would have to hire an outside --

COMMISSIONER: What would he do then?

MR. BRODSKY: Well, then the court would impose certain conditions of probation.

COMMISSIONER: Well, I know he's got the probation, but they violated it now.

MR. BRODSKY: Then the court could fine the corporation.

COMMISSIONER: Well, wait a minute. You've
already fined them. You're going to do it again?

MR. BRODSKY: Yes, sir.

COMMISSIONER: Suppose they have imposed the
maximum fine? That's my problem.

MR. BRODSKY: Well, now we're dealing with
violation of a court order. That is, an order by the
court. And these are the conditions --

COMMISSIONER: So you say that you can get
contempt?

MR. BRODSKY: Yes, sir.

COMMISSIONER: And of course you can accomplish a
lot of that by just a straight out injunction to begin with.

MR. BRODSKY: Well, certainly you could.

Certainly, in those parallel proceedings where there are
civil cases that follow on, as our standards point out,
we're not suggesting that continuing judicial oversight
necessarily is appropriate.

That is, that that could be achieved through...

(Conclusion of side 2, tape 1.)
VOICE: ....disagree with your statement.

Deterrence does not work on corporations. I think -- you say it does work or doesn't work?

VOICE: I say it doesn't work.

VOICE: Yes. I disagree with that. I have any number of instances where it works, and it can work by an injunction.

The other thing, on how the "persons" got into the 14th Amendment, if you will read "The Gentleman from New York, published by Yale University Press some 30 or 40 years ago, which (inaudible), it describes in detail how (inaudible) in the case of the Supreme Court (inaudible) in the United States Senate, how he put "persons" into the 14th Amendment by virtue of testimony that when he was on the Senate committee writing the 14th Amendment that they considered "persons" to include corporations.

CHAIRMAN WILKINS: Commissioner Nagel has a question, I believe.

COMMISSIONER NAGEL: In setting the appropriate level of criminal fines, what is your position on whether the size of the corporation or corporate assets should be taken into account?

VOICE: There is in effect nothing in the ABA standards that talks about that as an appropriate criteria for imposing a fine.
CHAIRMAN WILKINS: You would limit it to the gain or the loss?

VOICE: To the gain or loss.

CHAIRMAN WILKINS: We appreciate very much, Mr. Brodsky, Mr. Freeman, you coming and sharing with us your work and your thoughts. We look forward to a continuing working relationship with you.

Thank you very much.

VOICE: Thank you.

CHAIRMAN WILKINS: Our next witness is Mr. Harvey M. Silets, a distinguished member of the Bar from Chicago. He got up at 4:00 o'clock in the morning so he could be with us today, and we appreciate that extra effort.

Thank you.

TESTIMONY OF HARVEY M. SILETS, CORPORATE DEFENSE ATTORNEY, TAX

MR. SILETS: Good morning.

CHAIRMAN WILKINS: Good morning.

MR. SILETS: Good morning, Mr. Chairman.

It was 4:30, but it was just as hard.

(Laughter.)

MR. SILETS: I guess I should begin by telling a little bit about myself, although in my tome that I submitted to the Commission I have recited some of the things that I have done.
I have been Chief Tax Attorney for the U.S. Attorney's Office in the Northern District of Illinois. I am currently the Chairman of the Federal Rules of Criminal Procedures Committee at the American College for Trial Lawyers.

I want to state a caveat, however, that what I say here today is not anyone's opinion other than my own, and indeed perhaps some of my opinions, in light of my colleagues Mr. Brodsky and Mr. Freeman's testimony, may seem somewhat heretical.

In my submission to the Commission, I spent a bit of time discussing the philosophy of the imposition of criminal sanctions on the corporate enterprise as a corporate enterprise, distinguishing it from individuals.

We recognize now that the status of the law is that corporations can be punished, and therefore the philosophy, which I term the reductionist theory, that if you punish the individuals who operate the corporation that the sanctions to be imposed upon the corporation need not be available or should be minimized, is something that I don't agree with.

As long as we have included in the law that corporations should be punished, then we should punish them if they commit an offense.

So the question then becomes not imposing
sanctions upon the individuals because if they are convicted they will be punished separately, but what should happen to the corporation itself?

The sanctions that have been established by Congress -- the factors in determining sanctions that have been established by Congress in Section 3553(a)(2) are four in number.

Two of them really are not applicable to corporations in my judgment, one of course being rendering educational, vocational guidance to the offender. I don't think that is necessary in the case of the institutional offender.

And the other is the need to protect the public from further crimes of the defendant. That is a matter which was raised by one of the members of the Commission (inaudible) considered or called incapacitation. You lock somebody up. That is one way to keep them from committing the crime again. Another way is to disenfranchise them, is to take away their charter to operate. I think Mr. Robinson raised that question.

I am opposed to that. I am opposed to that because it is contrary to society's best interest to destroy the corporation.

One does not always impose capital punishment for every offense, and I submit that there is probably no
offense that a corporate enterprise would reach the
magnitude of capital punishment.

In my view, what happens if you impose capital
punishment on a corporation is that you disenfranchise the
public, and particularly the employees of the corporation
who may be totally innocent. They will lose their job or
jobs if the corporation is incapacitated.

But the Congress has really said that there are
two basic factors that are applicable to the corporate
circumstance. Well, one is the theory of retribution, and
the other is the theory of deterrence.

Now, interestingly enough, in my view, Congress
has by this act for the first time said that retribution
really is something to be considered, an eye for an eye, a
tooth for a tooth, and so on.

In my judgment, the imposition of a sanction on
an enterprise -- perhaps I am apart from my colleagues on
this issue -- is that there should be a sanction which
results in a disutility to the corporate enterprise; that
is, that it should be disabused of any benefit which it has
obtained and be punished. So in my judgment it may be a
cumulative circumstance; that is, you can have restitution
so that they disgorge the benefits and, in addition to that,
they should be punished.

My belief is that by doing that to the corporate
enterprise that you in effect implement both of the two
applicable provisions of the factors that Congress has said
it should be considered -- retribution and deterrence.

Now, how can this happen, and should it happen?
My answer to that is, yes, it should happen, and
it can happen because the theory of restitution is not
something that is done in the blind.

Two -- at least two of the members of this panel
have bar or have been district court judges. We know -- and
I, as a trial lawyer, know -- that if restitution is being
ordered it is not being ordered in the dark. I mean, there
is an informed judgment, there is a hearing, an adversarial
hearing that will take place as to what constitutes the
appropriate restitution. It is not a number which will be
pulled out of the air.

So the concern that my colleagues express about
restitution is not my concern because, as the advocate, will
be able to speak on behalf of my client to determine what
the correct restitution should be.

I know that I am operating under a limited time,
and I don't want to go over the 46 pages of my brief. I
have always been amazed why briefs are never brief.

But Judge MacKinnon raised the problem that is
paramount in my mind in terms of sanctions. It is true that
we now have the ability to impose probation on a corporate
enterprise, and probation typically, as it applies to an individual, says to the individual you have been sentenced to a period of incarceration, suspended, or at least in part suspended. If you violate your probation, you will go to jail.

Corporations don't go to jail. So what happens if the corporation does violate its probation?

I disagree with my colleagues when they say the contempt citation. I don't believe it is possible. I don't believe that the court can order an individual within a corporation to maintain the probationary period. After all, that individual is not the person who has been prosecuted.

So what we have, in my own personal judgment, is the anomalous situation that a very good sanction, the very kind of sanction that should be used to see to it that the future does not repeat the past, may result in a nonentity. Nothing happened.

Violation of the probation, and the corporation reappears before the court, and the court says I have now -- I have already imposed the maximum punishment by way of fine. The violation of probation, as I read the statute, says you can come back and be resentenced to the maximum, or that has been provided in the first (inaudible).

But the corporation has already been fined to the maximum. Typically, that is what a court would do.
What happens?

I don't know what happens, but I would think that this Commission might have some authority or power in its report to suggest to Congress that perhaps a new offense is created or should be created by the violation of the probationary period.

In summary, then, my position is that the interaction between deterrence and retribution can be achieved through fines, through restitution, through a probationary period, through publicity, publicity which will indicate to the community that this corporation is one which is not as its advertising otherwise would depict, publicity which would tell the people who have been hurt by its action that they may have a cause of action which they might not otherwise be aware of without that publicity, and, most importantly, a totality of sanctions which will result in what I call disutility of the commission of the crimes to the corporate enterprise, make it so that it is not profitable as a corporation.

CHAIRMAN WILKINS: Thank you very much. Let me ask you about publicity.

How extensive should the publicity be after conviction of a corporation, and who should frame the language? Should it be the Department of Justice, or should the court place that burden on the defendant, then they come
back and report and show what has been done? Should the court do it?

Just what is the procedure that you would suggest that we might suggest in our guidelines be followed?

MR. SILETS: My belief is that (inaudible) prosecution bears the burden of proof, that they should go first, just like in any sentences. They should go first and propose what they feel is the best.

The defense, the corporate enterprise, should have an opportunity to comment or make its own proposal as to the contents of the publicity.

And the final arbiter of course would be the judge.

In terms of the scope of the publicity, I think that depends on the scope of the offense. If it is localized, I think then the publicity should be localized. If it is a national -- if it has a national impact, it should be publicized nationally.

But at a minimum, it seems to me that it should be in all of its filings with the SEC and all other regulatory agencies and to all of its stockholders.

CHAIRMAN WILKINS: All right, sir.

Any questions to my left?

VOICE: (Inaudible.)

Why couldn't the judge say to the officers, I am
going to put you under an order to fulfill the conditions of
the probation?

(Inaudible.)

It is an obligation that the court raise its
hands. Couldn't the judge in carrying out that obligation,
carrying out his initial order, tell the president, you do
this in the future. Then if the president doesn't do it in
the future, the president is violating the court order that
the judge imposed.

Why not?

MR. SILETS: Judge Breyer, I don't think that
that can be done because (inaudible) corporate officers are
not the persons who commit the offense.

COMMISSIONER BREYER: I know, but suppose that
you were a president of a corporation and the corporation
has a legal obligation to pay me some money. I can go in
and enforce, I take it, the corporation to pay me the money,
and you, as the officer of the corporation, again as a legal
obligation, I guess, would be forced to write the check.

MR. SILETS: Yes, on the other hand --

COMMISSIONER BREYER: So why can't you as
attorney do the same thing vis-a-vis that obligation
(inaudible)?

MR. SILETS: What would you say then -- if I
might counter with a question -- if the corporate officer
resigned, said I am not going to undertake that burden; I didn't commit the crime and I shouldn't make these -- take the steps which the court orders me to do?

I guess the point that I am making is that while it is common for the corporate enterprise to commit a crime through its agents and it is also common that the agents or officers are prosecuted as well, it is uncommon that corporations are prosecuted only, and I think it would be unfair to take in that circumstance and order an individual officer to comply with criminal probation.

COMMISSIONER BREYER: You have written this (inaudible)?

MR. SILETS: Yes, in one of my footnotes.

VOICE: How about (inaudible) contracts in government cases?

MR. SILETS: I think that that is a decision that can -- that is an opportunity for the district court, but I think the district judge has to weigh that very carefully. There may be national interests that would exceed the punishment that may be thought necessary in an individual situation.

I don't suggest that it should not be a sanction, but I don't think it should be one which should be lightly undertaken.

VOICE: I have a good deal with this notion of
disutility and punishment, but would you -- the questions that were raised this morning about innocent shareholders -- how do you reconcile the disutility and punishment with the possible effects on innocent shareholders?

MR. SILETS: Well, in my piece that I have given you I have cited a couple of situations where corporate fines have resulted in an impact on large public corporations of 33 cents a share.

I am not quite certain that with a large company that fines of the magnitude that the Criminal Code permit will have any significant effect at all.

In terms of restitution, we start on the premise that there has been an unlawful benefit for the corporation to begin with. So removing that benefit from the corporation should not injure the stockholder.

It seems to me the extreme circumstance is when you impose capital punishment.

VOICE: Let me go back to this 33 cents a share because while it sounds like a little, some of the shareholders are kind of concentrated, but if you are right that there is very little effect on shareholders, then where would you get the tax from at the organizational level?

You have got sanctions on the individuals, and that should (inaudible) their behavior. Where would you get the --
MR. SILETS: Well, you are going to get it through the combination of sanctions, not by fines alone, and that is my point. A fine alone is not sufficient to accomplish the task of deterrence. It is the combination of all of those things that I have described (inaudible) used in concert that will deter the corporation from future criminal conduct.

VOICE: I certainly agree with you when you say that liquidation is not always appropriate. Of course, the claim that Mr. Freeman was making that I thought you were agreeing with was that it is never appropriate for corporations.

It would seem to me you -- essentially two arguments that you made about why it was inappropriate, one that there is this disruption to employees and another (inaudible) not corporate conduct that would ever justify the death penalty analogy.

But I take it the first one is easy enough to resolve by -- before distribution of assets to stockholders after liquidation the corporation is required to provide -- find alternative employment, provide moving expenses or retraining or whatever. I mean, there is a good deal the corporation could do to solve the problem of disruption to employees.

So really what it comes down to is, is there
corporate conduct that is ever bad enough to justify that sort of sanction with liquidation?

Now, I suppose even if you took a standard that was tied to the death penalty for human beings you could certainly have cases where board of directors sanctioned conduct that causes death, that impairs the national security of the country, things like that. But -- so I suppose there is no reason to think that the standard for the death penalty of human beings is what is used for corporations.

If they exist for our benefit, isn't it just for us to make a judgment whether society would be better off with them or without them and that that ought to be a liquidation standard?

MR. SILETS: Let me start first by suggesting it is my belief that Congress rejected the liquidation of corporations and sanctions somewhere in the process of coming up with penalties that had been considered by committed but rejected.

But assuming that it was -- for purposes of this discussion -- (inaudible), I think that if the corporate structure was very small, with few employees, the problem of giving employment to the otherwise displaced employees would not be difficult. But just imagine the Du Pont Corporation being liquidated. The problems would be so massive they
couldn't be accomplished.

Is there an incident where corporate crime results in individual death and therefore should not capital punishment be imposed?

Perhaps, but it seems to me that the sentencing court, when it imposes judgment, has to take into consideration not only the offense but what the judgment and sentence would have -- what impact it would have on society as a whole.

And if you impose the liquidation sanction on corporations, it would seem to me that you could not make a hard and fast rule because it is so extreme, particularly in the case of a public corporation, that if it were ever to be used at all it would have to be used with the greatest discretion and on the (inaudible).

CHAIRMAN WILKINS: All right, fine. Any other questions from the Commission?

(No response.)

CHAIRMAN WILKINS: Well, Mr. Silets, we greatly appreciate you coming. We will study your written testimony in more detail.

Thank you very much, sir.

Do you want to take a five-minute break?

We are going to take a 10-minute break. At 25 minutes after 11:00 we will promptly reconvene.
Thank you.

(Recess.)

CHAIRMAN WILKINS: We are very pleased to have
with us as our next witness Mr. Stephen S. Trott, who is the
Assistant Attorney General in charge of the Criminal
Division at the Department of Justice.

Mr. Trott, we appreciate your appearance today
and the work that you and your division have put into this
appearance, and I might add, too, all of the assistance that
the Department of Justice has given us when we began our
work several months ago.

TESTIMONY OF STEPHEN S. TROTT, ASSISTANT
ATTORNEY GENERAL, CRIMINAL DIVISION, U.S.
DEPARTMENT OF JUSTICE

MR. TROTT: Mr. Chairman, thank you very much.
It is my pleasure, and we are delighted to be of help. I am
glad we have been able to be of some service to you, and we
are looking forward to continuing to work together in the
future.

I have filed a somewhat lengthy document
outlining the various positions that we have on some of the
issues before you. With your permission, I would forego
reading that document and simply make a couple of
observations and then, on the basis of some of the very
interesting and I think informative discussion that has been
held here so far today, answer some of your questions.

First off, there seems to be a divergence of opinion on an issue that I think is very, very important, and that is whether or not -- just exactly what you ought to do to an organization.

It seems to me, to paraphrase, that there has been expressed the idea that somehow it is the individuals who you really should be concerned with and by going after the individuals you handle the problem. After all, it is the individuals who did it, so why get so upset with the organization?

In my experience, which extends back over 20 years as a prosecutor, I believe on the basis of that experience that organizations, as organizations, do react to criminal prosecution and they are subject to the enforcement purposes that are contained within the idea of general deterrence.

I have seen this on many, many occasions, not the least of which involves the now interesting and well-discussed E. F. Hutton case, a case in which no individuals were prosecuted, for reasons that have been explained in public many times. Nonetheless, the effect that that case had, not only on E. F. Hutton itself in terms of changing practices, policies, procedures and the lack of control on low level individuals who were responsible for
that, but the impact of that on other corporations and other organizations similarly situated who are involved in very large cash management programs has I think been rather dramatic.

I have talked to many people who work for other companies who manage cash, and everyone has told me that after the E. F. Hutton case they immediately pulled in all of their people and examined what they were doing and in most instances changed what they were doing. They cut out the problem of the float price that we identified in the E. F. Hutton case.

Probably in excess of 25 people have told me that the E. F. Hutton case had an impact on their organization simply because they did not want to get charged with criminal conduct, and again there is a situation where no individuals were ever prosecuted.

I think if you were to talk to Hutton itself and ask them what the impact and effect the prosecution had on Hutton, they would tell you that it was enormous. People were fired right and left. They changed internal procedures. The publicity of the criminal prosecution itself had an impact on Hutton.

Then in essence it ends up in the final analysis protecting the people that were supposed to be protected, and those are the potential future victims of these kinds
of schemes.

In other cases in which I was personally involved, such as one involving Rockwell out on the West Coast, we instituted a number of sanctions and we watched the turnaround inside the company, even though no individual in that case again was prosecuted. But we put into place through something that was akin to probation a whole series of things that Rockwell had to do, and they did them, and I think it protected the government in that case, doing business with Rockwell, from any future criminal conduct.

To give you an idea of the kinds of things we did in the Rockwell case, we said to Rockwell -- we forced Rockwell essentially into accepting an injunction, and in the injunction Rockwell agreed to the labor mischarge (inaudible). They had a couple of contracts. Instead of charging it to Contract A, they were charging it to Contract B as a result of management.

And we told Rockwell, look, you are going to have to produce a movie. In that movie you are going to have to explain to your employees what their responsibilities are when it comes to labor charges, and you are going to have to show that movie to every employee involved in these divisions once a year. And they agreed.

You are going to have to put on the wall a sign that says, remember your responsibilities in terms of labor
mischarging, and if anybody suggests that you do anything else, call these numbers.

We forced them to put in place a whole new computer program for timekeeping. We forced them to serve copies of the injunction on each new employee and all the employees that were around so that everybody was fully aware of what was going on.

So through a whole range of options we were able to engage in specific and general deterrence.

I think that is really what the message is. As was so ably said by the witness before me, judges aren't going to just pick things out of the air when it comes to restitution and judges and courts aren't going to treat people arbitrarily and capriciously. Every situation is going to be somewhat different.

So what I think is necessary is a full range of options available to sentencing judges, from thermonuclear to almost an encouraging pat on the back, which a sentencing judge can choose from in order to address the kind of conduct with which that sentencing judge is confronted, and in some situations that is going to have to be very, very strong medicine.

When you have a large corporation which engages in wholesale criminal conduct which results in the loss of a lot of money in any kind of a context and it appears to be
the organizational policy to do this, you are going to want
to have a sentencing judge in a position where fines can be
enormous and where all kinds of measures can be taken to
make sure that that kind of conduct goes punished and that
people who are similarly situated watching that kind of
conduct recognizes there are costs of cheating the
government, of cheating elderly people, of cheating
whomever, that are far greater than any benefit that can
possibly be gained by this activity.

But then you are going to have to have also the
option to ratchet this down. If you have a corporate
situation where it is not the corporate policy, where it was
low level people who were engaged in this activity, such as
in the E. F. Hutton case, then a judge will want to tailor
the sanctions accordingly.

I think definitely that there should be the
availability of fines that far exceed the amount of the
loss, far exceed the amount of the loss. You are going to
find a situation where you have a huge corporation. The
provable loss is going to be a figure that in connection
with the total assets of that corporation is almost
nothing. If you impose that type of a fine, it becomes just
a joke.

So I think again you have to have a full range of
options. That has always been something that struck me as
very important for a sentencing judge. We have a tendency
to have all kinds of options for the people who need a
break, for the organizations who need a break, for the
organizations with a lot of innocent shareholders and a lot
of innocent employees, but we have to make sure that we also
have the kinds of options that are necessary when you get a
real rogue outfit that just sits down and decides it is time
to please everybody under the sun. And we are confronted
daily with those kinds of corporate or organizational
enterprises in the United States.

Then the other idea that has been talked about
briefly is -- again, it is a variant of this -- is all you
have to do is get the individual. If you have a system that
focuses just on the individuals, what you do is you create a
new position in organizations. It is called Vice President
in charge of Going to Jail.

(Laughter.)

And all they do is jettison a scapegoat here, a
scapegoat there, and there is no incentive for them to clean
up the act.

So unless you have something that can impact on
the organization, you don't have the CEO or whoever it is
running that operation or the shareholders or anybody else
with an incentive to make sure this never happens again.

General Dynamics is a good example. It was
featured recently on McNeil-Lehrer. It has been the subject of a lot of discussion in Congress and a number of lawsuits.

Without getting into any of the merits of these lawsuits, when we were discussing General Dynamics we kept saying to ourselves there has got to be a change of attitude in this organization and the attitude right now is not a good one. What changes the attitude? And the only thing that changes attitude is availability of strong medicine.

We began to see changes in attitudes in General Dynamics. All of a sudden, there was a new person in charge of the operations, and one of the first thing that the new person did was install an ethics course for the executives in General Dynamics, and they even had television cameras in the ethics course, discussing these issues of labor mischarging and all the rest, and it appeared to me that it was coming -- that the message was finally coming down from the top:

Let's clean up the act. A government contract is not just an opportunity to get rich quick. It is also an obligation to play by the law.

So again -- I don't want to get into too great a detail here. I had rather answer some of your questions -- you have to change that attitude in the organization. If all you are going to do is get the Vice President in charge
of Going to Jail, you are never going to change the attitude
of the corporation. The corporation can always say we were
clean, John Jones did it. Get rid of John Jones, and it is
business as usual.

Now, on fines we have advanced an idea in our
papers -- and I am sure that it is not a new idea -- that a
judge imposing a fine should really examine very carefully
what the impact of that fine is going to be and to ask the
organization or whomever -- probation person or a special
master, whatever -- to come up with a fine that will have
the intended impact on the company.

In other words, where is this money going to come
from? Is it going to impact a lot of innocent employees?
Is it going to adversely impact a lot of innocent
shareholders, or does the company have a bunch of money
sitting around that it was going to use to acquire some
other company that is available for this fine, and is it
going to have the real -- the hammer effect on the company,
where it belongs, and not on the people who can get swept up
in these kinds of things?

So I think that the approach is to -- when you
begin to talk about a fine -- to begin to ask, well, how is
that company going to pay the fine, where is it going to
come from? Then the fine can be tailored to have the best
possible impact; in other words, sort of a surgical impact,
corporations are concerned.

   MR. TROTTL: I agree with you, and all of the
   things that you have identified are aspects that could be
   looked into.

   It might be more valuable for us to answer that
   for the record and to put together our thoughts on the
   subject in a concise written form and get that to you just
   as soon as we can.

   CHAIRMAN WILKINS: All right, sir.

   MR. TROTTL: But I firmly believe that it has to
   exceed the amount of the loss or else it is not going to
   have the impact that you want it to have on the organization
   in question.

   CHAIRMAN WILKINS: All right, sir.

   Any questions?

   VOICE: Mr. Chairman, this is just a comment,
   that on the E. F. Hutton situation, the fact that the
   medicine must have indeed been strong was indicated by the
   fact that they expended, and I guess will be expending,
   large sums of money to hire people who are squeaky clean and
   who have credibility with the American people to in fact
   assist them in improving their image.

   MR. TROTTL: That is right.

   VOICE: So I see that as a strong indicator, and
   it is sort of a punishment in that it does involve the
expenditure of funds.

MR. TROTT: They were socked by that case, even though no individual was touched, to the extent -- as you point out -- they went out and hired one of the most popular human beings in the United States, Bill Cosby, to try to rehabilitate their image, and, you know, good luck.

VOICE: Yes.

(Laughter.)

MR. TROTT: But that again shows that an organization will respond even if -- they did not have the opportunity to jettison in a criminal case any of the scapegoat Vice Presidents in charge of Going to Jail. They had a case -- the whole thing -- as an organization right in the nose, and the important thing as far as we were concerned is that that was appropriate in that case.

The entire management structure at the upper levels of E. F. Hutton was not directly involved in the criminal conduct that was carried out by some lower level people, but they created an atmosphere in which they encouraged this type of behavior, and they absolutely looked the other way when it was going on.

So we felt that it was very appropriate to hit the organization as an organization rather than go down to a couple of lower level green eyeshade people and blast them in a small court somewhere up in Scranton, Pennsylvania.
VOICE: Management with a corporation is about the same as a military organization in that the military commander is responsible for all that the company does or fails to do. In this case it works through from management, and so that is really essentially the same:

MR. TROTT: Yes, and we did use an injunction in the E. F. Hutton case also that was able to encompass conduct that we could not have ever prosecuted criminally, but we were able to convince E. F. Hutton to submit themselves with respect to their cash management schemes to this very, very broad (inaudible).

CHAIRMAN WILKINS: Questions?

VOICE: If you are going to submit (inaudible) difficult question, but I think it would be quite interesting, the question the Chairman asked, because after all the money -- you know, the money to be used to acquire another corporation belongs to the shareholders. The money that just sits there has an owner, and the shareholder might be innocent.

So I am quite interested in how we determine the appropriateness of the fine, what level.

The other two things that I would be very interested in are how do you decide to prosecute the corporation as well as the individuals -- for example, you just said, well, look, the people up at the top of the
company -- well, they -- you are going to say you couldn't
prosecute them as individuals because they didn't have the
requisite state of mind.

MR. TROTT: That is right.

VOICE: And then you thought, well, the question
is if there is a totally innocent state of mind what are we
doing involving them at all?

And you felt, well, they are somewhere in
between. They don't have a totally innocent state of mind,
but they don't have a totally guilty state of mind, and
maybe there is nothing more to say about that issue than
that.

But you probably have some way, perhaps more
complicated than that, of figuring out when it is
appropriate to make a corporation the defendant, and I would
find that awfully interesting if you have.

MR. TROTT: Every case obviously differs, to
state the obvious, but our general policy, our normal
policy, is to prosecute both the organization and the
individual if we have of course proof with respect to each
side of that equation that there was culpability for the
crime.

But when we address an -- when we start an
investigation, we are investigating both the corporate or
the organizational responsibility and looking for the
individuals that did it.

    The best possible outcome, we get both the company and the individual.

    VOICE: If in fact over in the division -- I mean, again of the department -- you might have something on also the questions that are being raised, which I think is pretty interesting. It involves both individuals and corporations, and that is the question of when you prosecute people where they have less than an intentional state of mind, and particularly regulatory offenses.

    That is -- because there is a temptation, which he points to, I guess sometimes. When something terrible happens in the world, people want to blame somebody, and what he is worried about is sometimes it is a somewhat innocent person who gets blamed and gets hit with the whole reaction that people have.

    And so I think he in a way was looking for lines that will distinguish as to what the state of mind has to be in a regulatory offense, the individual and the corporation, and that might be something again that the people in the department have thought about.

    MR. TROTT: Yes, we have, and that is a situation where prosecuting the organization, based on the facts, could be the appropriate thing to do rather than the individuals.
But again it depends on exactly what the individuals did.

Of course, as you recognize, it is not our job to rewrite the laws that Congress gives us. If Congress says this is a crime, you know, and these are the elements of it, you know, we sort of salute. And we have wide discretion within the parameters, but we just can't go outside and say, well, Congress really didn't mean to do this, so we are going to red-line it from our code.

VOICE: You have several aspects of your case when it involves a corporation, and I presume that what you are saying is that it depends on the case. And if you have a man in a corporation that has general corporate, managerial authority and he commits a crime or directs a crime you are going to prosecute him as well as the corporation whose agent he is. But if it is some person down here selling something on the street for a particular corporation and he is out on his own and misrepresents or something like that, you are not going to attack the corporation. And it just is a question which is determined in each case by the nature of the offense.

The one point I want to make is it was always my understanding that if a corporation is acting illegally -- and I am talking about (inaudible) corporation such as you were talking about -- that it is within the power of the
Attorney General of the state to go in and cancel that corporation's charter and that they have done it and can do it in certain cases.

Now, we tend to, I think, focus too much on a lot of the large corporations. There are a lot of smaller corporations where the criminal intent can be more directly focused on the corporate officers, and throughout the country, why, those people are subject to some of the local action by the Attorney General. At least that is what I always thought (inaudible) the Attorney General to go after corporations like that.

And I don't suppose you have seen any cases of that. I have seen one or two. But that is a possibility and shouldn't be overlooked. If you have got a real bad corporation, you might try to prevail upon your local Attorney General.

MR. TROTT: That is true. Savings and loans have charters, and there are all kinds of activities. We have seen many failures around the country.

VOICE: Yes.

MR. TROTT: Maryland and Ohio. And you are accurate when you point out that there are the remedies to be brought there against these organizations.

Another point that was made earlier about debarment with respect to companies that do business with
the government. I frankly would rather see that left to the
government.

On many occasions we find that the government
would rather continue doing business with a company under
changed circumstances than find themselves unable to do
business with that company at all. Sometimes in the
interest of national security it is necessary for a company
to clean up its act rather than go out of business.

CHAIRMAN WILKINS: Mr. Trout, do you think that
the guidelines which we will ultimately promulgate take into
account the civil liability a corporation may suffer as a
result of what has been prosecuted by a criminal indictment,
albeit the fact usually the civil case comes perhaps years
after the criminal action has been concluded? Is there any
way that we could do that, and should we do that?

MR. TROTT: Well, that is hard to tell because
you have a lot of different situations, such as false
claims. You frequently will bring a charge, a criminal
charge, against a company and that is followed by a false
claim suit by the Civil Division.

Ordinarily, when I am confronted with this
problem, I have a tendency to say let the civil case take
care of itself, let the private case take care of itself,
let the charter problem take care of itself, let the
licensing problem take care of itself.
We used to become involved in what we called global settlements. I got to the point where I decided that global settlements are more trouble than they are worth. The more people you get involved -- the state attorney general, the licensing people, all these kinds of things -- the less possible it is to resolve the case.

On occasion we do settle cases with a local settlement, both the civil side and the criminal side, but I think on balance I would have a tendency to allow the other areas to take care of themselves.

But that doesn't mean for a second that I don't think restitution has a valid part in the sentencing process. I think that has got to be kept in the forefront. For too long we have ignored the victims of these kinds of crimes in the criminal justice system. Restitution I think is appropriate.

In the Hutton case, one of the keys to the settlement, for example, was the willingness of Hutton to pay back every penny from all the banks that had been fleeced plus interest and to sit still for the establishment of a special master program that would sit down with the banks and all the 7000 -- 7 million documents that we had and figure out what the loss was.

VOICE: (Inaudible) criminal also involve a civil case, and you prosecute your civil -- your criminal case
first --

MR. TROTT: Yes.

VOICE: -- and then your civil case (inaudible).

MR. TROTT: Yes. Again, sometimes when you are prosecuting that type of a case and there is a plea, an arrangement will be made to forego the civil consequences or to include them in the settlement of the case.

CHAIRMAN WILKINS: Commissioner Nagel.

COMMISSIONER NAGEL: You mentioned giving consideration to the negative impact on potentially innocent shareholders or innocent employees at the same time you yourself know that sometimes the impact of the sentence will create a positive influence because an incentive for shareholders exercising control.

Do you have any suggestions for rules that you would use to establish how we determine or how one resolves the tension between those two positions and ultimately (inaudible)?

MR. TROTT: I think again it depends on the case, and you would have to analyze the case and determine whether this was corporate policy emanating from the highest levels of the organization or whether this was some operation that got going down below that people at the top weren't aware of, and again you are sort of looking for an overall sense of the responsibility of the organization for the conduct
itself, whether it was deliberate, whether it was negligent, whether it was innocent at the levels that drive the corporation, and I think then you tailor the response around the level of criminality that you find at the various strata in the organization.

It is not all that easy, but just like I point out some of the factors in the document that I have submitted to you, if there was a distinct corporate purpose involved then it is one thing. If this was something that just kind of happened because somebody at a particular level was doing it more for personal reasons than for corporate reasons, then it is something else.

CHAIRMAN WILKINS: Mr. Trott, we appreciate very much your sharing with us....
CHAIRMAN WILKINS: Thank you.

Our next witness is also from Chicago, a distinguished member of that Bar, Mr. Mark Crane.

Mr. Crane, we're delighted to have you with us.

MR. CRANE: Thank you.

STATEMENT OF MR. MARK CRANE,
CORPORATE DEFENSE ATTORNEY, ANTITRUST

MR. CRANE: Chairman Wilkins, Members of the Commission, I'm here individually and on behalf of a small group of antitrust lawyers who are experienced in the handling of criminal antitrust cases.

I gave to the staff this morning a surprise copy of the testimony, adding the name of John Shennifield. Mr. Shennifield and Mr. McGraph, who already signed the statement, are both former Assistant Attorneys General in charge of the Antitrust Division.

We are all active in the Antitrust Section of the American Bar Association. I will be its chairman starting in August, but we are here individually and our views represent our own. They represent no views of the Antitrust Section or of the American Bar Association.

So I'm happy to say that in no major respect do I think they differ from what Mr. Freeman and Mr. Brodsky have said here today in general terms.

What I would like to do would be to orient you
for a moment to the antitrust case and summarize briefly the
positions set forth in our paper, and then submit to
questions.

We are typically talking about a price-fixing
case. We are typically talking, though not always, about a
larger corporation.

I think you should have those limits in mind in
analyzing what we are talking about.

Antitrust is unique perhaps in having nearly a
100-year history in criminal enforcement, enforcement that
involves both organizations and individuals.

And the central point of our message is that we
think that the balance that has been worked out of sanctions
in the past has been successful, and it is one that should
not be seriously tampered with for reasons relating to the
kind of offense we're talking about.

The past sanctions have consisted of sentences
for individuals, which can include jail, fine, and several
damage sanctions in subsequent cases.

We would like to talk briefly about each of these
in turn. It is our view that perhaps the most important
thing that can be done to deter organizational antitrust
offenses is to deal severely with the individuals who are
convicted of acting on behalf of the corporation.

We believe that a jail sentence for those people
should be the norm. It does not have to be long -- a few weeks to a few months is sufficient.

But the concept of going to jail we think is central to organizational deterrence. There are at least two reasons for that.

Most businessmen feel that pricing policy is a legitimate arm of sales and corporate policy. And even if they think that what they are doing when they talk to competitors about price, or about divisions of markets, is illegal. They don't consider it to be criminal.

And we believe there is no way to convince corporate executives, both in the same corporations and other corporations, of the fact that price-fixing is a criminal act, indeed, a felony, than to impose on a regular basis jail sentences on those convicted.

Secondly, we believe that the imposition of jail sentences as a regular matter changes the dynamics within the organization. Typically, the people who are involved in the front line are lower level managers, sometimes reacting, dutifully reacting, to some kind of pressure from above, maybe implicit, maybe explicit.

By raising the ante of the offense, by imposing the jail sentence on them, it will make the junior level manager who would be in the front line of the offense more resistant to it. He would be more likely to say no.
And when he says no, his superior would be likely
to do it. But we believe that when we talk about
organizational offenses, at least in the antitrust area, you
cannot do so without considering the very important impact
of fines on the people convicted -- I'm sorry. Jail
sentences on the people who are convicted.

Turning briefly to fines, they are not an
important sanction on organizational antitrust cases in most
offenses, because the corporations are simply too large and
the maximum fine is a million dollars.

In a smaller corporation, it may be very
important. But in the large corporations, it simply doesn't
matter.

We are not concerned about the possibility of
larger fines. We think that fines that were larger might be
helpful, but they are not presently authorized by law.

We do feel strongly, however, that the fines
cannot be tapered to the damage caused in an antitrust, or
to a multiple of the damage caused, because of the
complexity of the proof.

We have had a lot of experiencing in proving
damage in antitrust cases. And it's done in the civil cases
by a comparison of a hypothetical price, competitive price,
with the actual price. And this requires expert economic
testimony, statistical testimony, accounting testimony.
This is the result of perhaps a year or more of discovery and several weeks of trial. To import this complicated process into the sentencing process would unduly complicate and delay it. We think the present system works well without it.

We have similar reservations about the use of the criminal process for restitution. There, in addition to computing the amount in gross, you have to find out who all of the purchasers were and how much their purchases were. And then you multiply it, and overcharge time for the valid purchases and that's the damage.

And that simply is a major piece of litigation under class action law and not one, once again, that lends itself to the sentencing process.

Fortunately, we believe that the treble damage action is a useful device in that regard. It does provide restitution. It does provide a real deterrent. And in severe treble damage cases, they are expensive and disruptive to them and the damage can run into tens of millions of dollars.

So the bulk of our view, the crux of our view, is that the present system has worked well and that there is little that should be done to change the sentencing process in this particular area.

You will notice, however, that I have not
mentioned anything about probation or corporations. We have had relatively little experience with that, and we are trying to speak based upon our collective experience as practicing lawyers on the defense and prosecution side.

We don't believe it inappropriate to put a corporation on probation. I think we agree with most of what has been said here. This is covered in my paper, the thrust of our position.

We have some of the same reservations that Mr. Freeman expressed about probation which tries to run the business of a defendant. We think that particularly in the antitrust area, where it goes to the whole sales side of the business, where the business sells its product, this is not something that the court or a master can really run.

But we do feel that probation with certain specific, carefully crafted conditions, might be appropriate. You could debar certain of the employees from participating in the price-setting or even the sales side of the company, for example.

You could provide that there be an antitrust compliance program if it was specifically stated exactly what the organization had to do -- what subjects they had to cover, when, with what kinds of people, something like the film that Mr. Trott mentioned.

And, very important, it could include publicity
sanctions. We believe strongly that since the treble damage remedy is a cornerstone of enforcement, the victims need to know about it.

The newspaper is pretty good about that already, but the sentences make sure that the victims learn, probably by newspaper or media because of the difficulty in mail advertising to a lot of groups of purchasers; and also the purchaser's identity is long-gone, if it's kind of a small transaction that records aren't kept after the bills are paid by the purchasing organization.

So we do feel that that is significantly important. That is the thrust of what we had to say to you in writing. I think perhaps I'll stop there, if I may, and take whatever questions you might wish to ask.

COMMISSIONER: We appreciate your position regarding the complexity of measuring the appropriate fine to be imposed. Fortunately or unfortunately, that's a task that we must address.

And so I wondered if you were given the responsibility of devising a system that would appropriately calculate a fine in an antitrust case, what would be the principles that you would employ?

Bearing in mind we've got harm to the competitors, we've got harm to the public in general, that perhaps should be taken into account.
MR. CRANE: Well, first of all, I would urge you not to try to do it, but to recognize that antitrust is a special animal with respect to system in place and that the complexity makes it impossible to do it fairly.

If you have to do it, I would tie it to sales advertising. But I would use a very small percentage multiple of that sales, maybe on the order of a percentage point, or 1 percent or 2 percent, a very small amount.

I think even that would require additional legislation. And that legislation should make it clear that that fine has to then be taken into account in treble damage computation in some way, at least against the treble damages to individuals.

COMMISSIONER: Do we need legislation to accomplish that?

MR. CRANE: I believe you would.

COMMISSIONER: Thank you, sir.

CHAIRMAN WILKINS: Questions to my right?

COMMISSIONER: One followup question on this setting fines. One is if you aren't going to use the percentage of sales, what would you use?

I mean, would you have flat rate fines?

MR. CRANE: No. Then, I think you'd have to simply have flat rate fines. You could do considerable, I suppose, in terms of the size of the client by raising the
fine, actually to $10 million. And let the Judge worry
about it.

It wouldn't be good under the biggest cases, but
it would cover a very large number of regional prices.

COMMISSIONER: One more followup question on the
smaller firms. You addressed your comments to the larger
firms and the larger price-fixing conspiracies.

But, recently, if my memory serves me correctly,
many of the Justice Department cases have been -- cases,
where the firms are in fact small.

MR. CRANE: Yes.

COMMISSIONER: Does that change the nature of
your recommendation?

MR. CRANE: Well, we note in our paper at the
beginning that different considerations might apply to
smaller firms. We do not specify what those might be.

I don't think anything I said would be
inappropriate for a smaller firm. But it might be
appropriate to...

If you have a smaller firm which is essentially
the alter ego of the wrongdoers, then a harsher sentence on
the firm itself might be appropriate. You don't have as
much of a problem in fact on innocent employees. There are
few of them finding jobs in other businesses.

You don't have much impact on shareholders
because, presumably, they are connected with or are the
wrongdoers. In an extreme case, I would refer you to
corporate capital punishment, that might be appropriate.

In giving those remarks, I speak only for
myself...

COMMISSIONER: One last question. Why would you
subtract the fines if they were based on percentage of sales
from treble damage?

MR. CRANE: Because the treble damage itself is a
very large -- largely punitive. And it seems to me that if
you are talking overall penalty for the corporation, it
shouldn't have a very substantial fine -- I'd say 2 percent
of sales -- and then find that the overcharge was another 2
percent of sales, which is then trebled to 6 percent of
sales to become 12 percent of sales.

And if you're talking about a group of defendants
with $2 billion worth of sales, you are piling, I think,
penalty on penalty.

I'm not necessarily suggesting that you should
automatically deduct it, but surely that you be in the
discretion of the Judge in the civil case, which is the
second case.

And maybe you should have the discretion of
deducting it before treble...

COMMISSIONER: The general notion being then that
three times damages is an appropriate multiple?

MR. CRANE: I would say it's an appropriate multiple because it's an historical one. We talked at some length in the Antitrust Section about whether a double or quadruple would be better. And that's a highly subjective decision.

CHAIRMAN WILKINS: Commissioner Robinson.

COMMISSIONER ROBINSON: If a multiple of loss aren't workable, a percentage of sales is not workable, and if the Commissions were willing to simply set some maximum of judgment and do whatever you want within that on the theory that part of our obligation is to provide some more uniformity, we would like to look to something.

Would percentage of assets be an appropriate means? Is it appropriate to have a higher fine? In a sense, a percentage of that in an antitrust action, the fight would be the same in relation to your total assets.

So there'd be the same price between large and small companies. So, in that sense, it would be a flat rate. When we talk about flat rate, as I pointed out, $10 million for one company and $10 million for another may be a flat rate in a sense, but very different effects.

MR. CRANE: I think that it would be appropriate to take that into account as a kind of surrogate for ability to pay. And that's always a factor that is important to set
the fine.

Let me be very clear. I do not favor using the multiple of sales. I was asked by -- I think I would rather see a higher absolute fine and then a series of criteria the Judge raised to consider in deciding whether to go from zero to, say, 10 million, whatever the number is.

And there is in our report a list of factors that we think go to the question of how serious the antitrust offense was, one of which was the amount of sales. There are about six of them.

And I think that if you want to change the fines for antitrust offenses, that's the way I would attempt to do it. A higher absolute dollar, then a list of criteria the Judge was requiring. But not tie it to any formula, so much percentage of sales and so much percentage of assets.

CHAIRMAN WILKINS: Question?

COMMISSIONER: I'm not sure you didn't cover this. You used the maximum of a million dollars.

(Inaudible.) I thought it was a statutory maximum of $500,000, or twice the harm or twice the gain, whichever is the higher.

MR. CRANE: That is correct.

COMMISSIONER: So the million won't --

MR. CRANE: Well, yes and no. First of all, the language of what I call the double damage fine is in the
Criminal Fines Enforcement Act and has not yet been made law... 

And I've been talking to the Congress formerly about the unwisdom of doing that, at least in antitrust cases, for the reasons I've articulated to you.

Secondly, the language in the Crimes Control Act, I mean, Fines Enforcement Act, specifically says that you use the double damage fine only when doing so will not unduly complicate or prolong the sentencing process.

That language comes from the victim's Witness Protection Act, where there was a discussion of a legislative history which indicated that their restitution was not to be made in antitrust cases, it was under the Title 18 cases, because of the complication of computing the damage.

And we feel that no Judge who understands what would be involved would apply a double damage fine.

COMMISSIONER: Do you think there should be a distinction between, say, vertical and horizontal pricing? Horizontal pricings have got universal condemnation. And vertical pricings have (inaudible). I think are just as bad, although there are some that are not so bad.

(Laughter.)

MR. CRANE: Judge Breyer, that's a very, very difficult question. The Justice Department has guidelines
for prosecution. What they say there is that they will only prosecute in those areas where the intent was very clear. That is, there was no gray area as to whether or not it violated the law.

And this is sometimes interpreted as being the rule of reason case -- criminally. If it isn't, the per se case...

I think my feeling is, and again I'm speaking for myself, is that if the Justice Department has decided to prosecute criminally, then what I said should apply with ranges. There will be ranges in the jail sentence, there'll be ranges in the fine, and let the Judge take into account the various factors that you cite where in the range.

But that we shouldn't try to distinguish between a criminal conviction or one antitrust offense...criminal issue...if the Justice Department decided to start bringing a lot of innovative criminal cases, which has not been true in the 30 years that I've been practicing law, then we might have a little problem. But I don't think it's a real problem today.

COMMISSIONER: ...a short jail sentence. How about prison?

MR. CRANE: Well, I didn't mean to distinguish between prison or jail. I was talking about a term of incarceration. In Chicago, where I practice, short terms of
incarceration are served in the Metropolitan... but I didn't mean to suggest a location other than I would want to be reasonably certain that it was a state place for a white collar criminal to go.

I don't think I would want to see a price fixer sent for even a short time to... that's because of the tradition in our jails.

COMMISSIONER: Or to...

MR. CRANE: That's quite possible.

COMMISSIONER: What percentage of antitrust cases do you find are criminal...

MR. CRANE: Uh... that's a hard question. I think I would say in the area of 10 percent, but there are more reliable statistics than the ones I'm giving you. But you've got to remember, Judge, that there are many cases which do not lend themselves to criminal prosecutions because they are... or... merger cases, which is not a criminal statute.

Most of the price fixing cases have been genesis in a criminally... at least investigations.

COMMISSIONER: A conviction would be a felony?

MR. CRANE: Yes, sir. Yes, it would. If I may just make one brief observation on probation in response to the one question that you asked before:

In the antitrust cases directly, what can the
Judge do if the corporation doesn't go along? In the antitrust case, I don't think that's a serious problem because, generally, I think the corporations will obey.

It isn't the kind of a crime that seems to lend itself to top management saying I'm glad we did it and we'll do it again. It's the kind of crime that once the seriousness of it is brought to their attention, and the fact that people are very anxious...

That doesn't really answer your question.

COMMISSIONER: Well, some of them continue for a long time.

MR. CRANE: They do, but not usually after something like that. All I'm saying is I think, in the antitrust case, there is a good chance that the corporation will obey a probationary order that is clear.

CHAIRMAN WILKINS: Commissioner Block.

COMMISSIONER BLOCK: I have a followup on that kind of discussion on horizontal and vertical price-fixing.

MR. CRANE: Yes.

COMMISSIONER BLOCK: If I understood you, the last comment you made about the fine is that you would allow, in your own opinion, that whether it was horizontal or vertical would be a factor in determining the size of the fine?

MR. CRANE: No. I meant to say that the factors
that you would use on a horizontal case to decide whether to
give a maximum or a minimum fine would also apply in the
vertical case.

And that in a situation where the vertical case
was maybe a marginal case of price-fixing, you have plenty
of reason to bring the fine down using the same standards or
the separate standards to distinguish horizontal fine.

Have I stated it clearly enough, or...?

COMMISSIONER BLOCK: Yes. No, I'm just puzzled by
your principle that harm is distinguished in criminal
punishments. That there is broad agreement I think about
horizontal price-fixing causing substantial harm and not
very broad agreement about the degree of harm vertical
price-fixing causes.

MR. CRANE: But, certainly, the degree of harm,
even in a horizontal case, would be a factor. There, it
would probably be determined by the amount of sales. I
think the time that same principle seems to be used to
analyze the effect of the vertical pricings.

If your view was correct, the Justice Department
would agree that they would not bring the case as a criminal
case.

CHAIRMAN WILKINS: Thank you very much,

Mr. Crane.

MR. CRANE: Thank you.
CHAIRMAN WILKINS: I'm confident your remarks and your submission will be very helpful to us. We appreciate you taking the time and the effort to participate in this hearing.

MR. CRANE: Thank you, Mr. Chairman. We appreciate the opportunity to do so.

CHAIRMAN WILKINS: The final witness on our agenda today is John C. Coffee, Jr. He is Professor of Law at Columbia University.

Jack, we're glad to have you with us.

STATEMENT OF MR. JOHN C. COFFEE, JR., PROFESSOR OF LAW, COLUMBIA UNIVERSITY

MR. COFFEE: I think I should begin with one of those usual prophylactic statements that says who I am not representing.

(Laughter.)

Although I have heard that the reporters and the American Bar Association were -- I am definitely not here to represent them. They've been well-represented by George Freeman and others.

I also am not representing the American law students that I served as reporter for the Corporate Government's Project. But I am interested on just where corporate law and criminal law meet. Today, they're meeting on the Sentencing Commission.
I want to start by briefly saying a few orthodox words that I'll say quickly...

One, I think there is an obvious case for court penalties. I think there's probably a consensus among scholars who work in this area that if you can deter the principle, the principle will take care of the agent.

That is, penalties focused on a corporation will produce -- for the agent. The corporation can monitor agents much more cheaply than can society. It can find out what its managers are doing, whereas, the states cannot. It proposes constitutional obstacles and very high costs are involved.

When the corporation is interested in monitoring its agents, it seems to be very effective. Tremendous respect on antitrust compliance programs...and I think it has some impact. That's because that corporation is concerned about at least that class of liabilities.

But I think, as a practical matter, corporations are largely concerned only about antitrust liabilities, perhaps securities liabilities.

Finally, there are problems that are focused strictly on the agent. In many, many kinds of misconduct, it is terribly difficult to identify the agent.

If you look at the Ford Pinto case, it's very hard to decide there who was wrong, if you think something
wrong occurred, because decision-making is collegial, bureaucratic, it extends over a long period of time. There is no one decision-maker.

You can identify with the kind of competence that our Constitution requires before you apply sanctions. Therefore, focusing on the group, certain levels do it. Indeed, if you can find the agent, it might be just to apply a sanction to him. You might fine a person who had designed a gas tank in a Ford Pinto case with a $30,000 a year trainee who was just brought in and told to design a gas tank with the following cost parameters.

That person really shouldn't have the whole stigma applied to him. Nor is the financial executive who said to cut the costs 50 percent because, universally, he didn't know the first thing about engineering.

Thus, a corporate or entity focus is justified on justice grounds.

(Conclusion of side 1, tape 3.)

...corporation which the economists say might call the William Sony model of corporation. Caught between the rock and the hard place. He may well know that there's a criminal penalty, but he also knows there's a fairly low probability of apprehension -- expectancy rate on indictments.

On the other hand, although getting dismissed or
demoted is a much smaller sanction in its overall severity, the probability of that is quite high because of the need to keep cost production --

So he is caught between internal sanctions and social sanctions and has to determine which he will see in a given case, that's pressuring him more.

Thus, as long as he can be pressured from above implicitly, in the absence of adequate corporate penalties...he will say the higher probability of an internal sanction for not cutting costs or not complying is more severe, facing as I am mortgage payments and children going to college next semester. So I will take that chance because I'm certain that I'll be dismissed if I don't reach the quota.

That's the case, I think, in a nutshell, smaller nutshell, for looking at the corporation -- not exclusively but a dual strategy.

Now, given this, given I favor a dual strategy, that you have to look both to the corporation and the individual, and if both can be prosecuted simultaneously very economically because it doesn't cost much to add an additional name to the indictment, and it gives you very unique plea bargaining dynamics, too. Trade off one against the other. A true prisoner's dilemma between the individual and the corporation as to who will plea bargain first.
What should we do to make corporate penalties work under this dual strategy approach?

I want to recommend two, very simple policy objectives for the Commission to adopt, that I believe would be endorsed by a board of consensus of informed people.

Then I wish to suggest means by which to reach these ends for which I claim no particular success.

Finally, I want to turn to a few special problems in interpretation under your statute, where I believe legislative history provides you with very little guidance and where discretion is considerable.

I will ask for a chance to finish here fully, just go on for a bit. But I will basically, politely counsel you to do the right thing, to do the right thing because there's a very vague statute in a number of areas.

It's hence that you could either take a stonewall or merely, as suggested, that you are free to look at carefully and reach a contrary result where you're sure policy goals are caught in the opposite direction. In particular, I'm referring to problems really to identification and to the ceiling on multiple penalties, which I'll come to in a moment.

Now, my two basic intentions. First, the individual one. Based on past experience of other jurisdictions...I would say that the most important
architectural issue in the construction of sentencing guidelines is the drawing of the inhouse lie. That is, the lie between presumptive incarceration and presumptive probation or not incarcerated...

Whether or not you deviate from the traditional sentencing the other states have used in the past, whatever format you use, the Bar will quickly discover where this in/out line is, probably plea bargain around it, or it will take that into its negotiating strategy.

This in/out line, however it's presented or disguised, is the Continental Divide in the San Andreas fault of your particular structure. Everything is going to evolve around where that is.

Therefore, I think the policy goal that you should be looking to is to try to mitigate the importance of that line. And I think the best way to mitigate the importance of that line is to bridge it by making extensive use of a disqualification probation sanction.

It should be at the center qualification that you're thinking of, not at the periphery. Now I'm saying this. I do believe there has to be appropriate limitations on the use of this sanction, and I believe appropriate limitations are set forth in ABA Standards 18-2.8, Brief.

Now since this is counsel's second counsel, I won't go further in pushing the ABA standards. I'll just
get you to look at the particular limitations there.

I'd point out also that there's been a lot of case law just the last year. For example, this Circuit has disqualified a Congressman from -- probation where he was convicted of a federal elections violation, from participating in any form of political activity in the period of probation.

The claim was made there that the 10th Amendment guaranteed the citizens of his jurisdiction the right to send him back to Congress. The court dismissed that and voted that the individual couldn't represent 10th Amendment...and that this was traditionally reasonably related to the rules of probation.

Well, that case gives you a certain -- logic. You can tell citizens that they can't have their congressmen reelected. I'm sure you can tell shareholders they don't have the right to reelect particular officers, in the corporate office.

I think it's a much more constructive fiction there that shareholders wanted to do so.

There have been a bunch of other cases involving a police officer in the last year who was denied the right to serve in a law enforcement capacity during probation because they were involved in crimes which breached their trust.
Well, I think, if a corporate official is engaged in a knowing and serious violation of law -- and I'm not talking about negligence offenses or minor regulatory offenses, again, confined to the ABA standard -- I think that that is the best way to hold to a basic presumption against incarceration.

I'm not arguing against the short, sharp shock of sentence of two or three months, within their confines for split seconds. I think the disqualification sanction is the best way both on the particular kind of function, for example, that he has filed fraudulent tax returns, disqualify him from preparation of tax returns or ...reports, in that capacity. And from the particular employer during the period of that probation.

That I think does allow you to avoid sending people in their sixties and seventies to prison for a first offense. It only crowds our jails and exposes people to the terror and danger of prison; while still giving adequate deference to the notion of equality.

That's a very real penalty imposed here to disqualification...skeptical from whether there was any real penalty associated with these various community service actions that have come into increased and somewhat disreputable use.

Okay. That was the first point in terms of
organizational sanctions. When you look at the individual, think of what is to mitigate the in/out line of disqualification sanction is probably the most sensible thing.

Now we turn to the organization. I think just about everyone who has made the point that penalties both as they are authorized and as they are imposed are too low to be adequate to deter organizations that are looking at the profit and gain from any form of misbehavior.

Thus, a major aim ought to be how do you escalate the penalty structure? I'm speaking here basically about financial penalties.

You're aware of your own empirical data that shows that something like the majority of all sentences between '81-'84 were between $1,000 and $25,000. Only something like 18 percent were over $100,000, and only something like under 1 percent were over $1 million.

That's the kind, despite statutory maximum, that is considerably higher. It's not simply a problem of inability to impose. It's a problem of judicial reluctance to impose. The criminal justice system has a long tendency to be somewhat static -- returning to the same equilibrium no matter how you disturb it from the outside.

I think you've got to face the problem that there are reasons why Judges are reluctant to impose high fines.
I suspect that you know these reasons from the judicial ones to mind, but they're partly the courts see very little to gain from imposing a very high fine. They may fear that they're going to produce bankruptcy, layoffs or other kinds of crimes, either real or imagined.

They may be used to norms that were set in terms of individual or prosecution's. And also prosecutors have very little reason to indict corporations when they see only (inaudible) that are impossible.

I'm going to suggest three things here in escalating your structure. One is heavier reliance on restitution. Seeing restitution not simply as a matter of compensatory justice, as a means of restoring the victim, but seeing it as a mechanism for escalating the penalty structure because it gives Judges a reason to impose sanctions, rather than the sense that they're just pouring money into the federal treasury without any kind of a --

Also, restitution motivates Judges to get involved in sentencing, to see sentencing as an important process for something useful being done; rather it's one more burden that's already being posed by an overworked district court that has many, many things to do already.

If something looks meaningful, the courts will give it some time. If it does not look meaningful, it is going to get shortshrift.
So, restitution from that view. Immediately, let's talk about the guidelines issue. This is probably, I suppose, the $64 question.

How should you set your guidelines for organizations?

I would think at the lowest level you offer here that it would be possible and justifiable to set a guideline saying that in the case of organizations, you may want to define this really in terms of large organizations, the fine should be set at a level not below the expected gain or loss up to the statutory maximum.

That is, statutory maximum cuts you off and you can't impose the full gain or loss.

I am saying that in terms of a floor rather than in terms of a point. Of course, there's a very good argument for saying it should be a multiple of the gain or loss. But at that point, we get into rather complicated due process issues about whether or not the gain here was X or was Y.

If, however, we find that the statutory maximum is already going to cut us off, we don't have to go through that prolonged inquiry with due process obstacles that we are going to encounter there. We're going to instead just see that at a minimum, the court should be instructed -- you don't have to exercise all due discretion. You don't need
a right answer, you need to get a range.

The most sensible way of doing that is to say that the floor should be not less than the expected gain or loss where that can be calculated.

I understand that there is a statutory reference to unduly prolong -- and that word "unduly" can carry considerable weight. I think "unduly" has to be looked at in terms of the end purpose of the sentencing that you're heavily involved in.

Now what would this mean? I think you need to give examples, not just a simple statement but an illustration.

In a pollution case, it might mean that you would look at the cost of having to install adequate pollution controls rather than making the illegal...

In the case that's recently been prosecuted by the Department of Justice, such as -- failed to report to the government, the undisclosed side effects of certain drugs that are pretty well known in the last year, you might look at the profit from that particular which has jeopardized.

And the product's been recalled for further testimony and disclosure is made. And other cases involving (inaudible) statements, where there might have been a product recall, you might look at the profit from that
particular product. This doesn't exhaust the field. You need to give illustrations here if you're going to communicate to the -- that federal judges would need to read.

Now there are other things that you can think of. And here I'm going to mention some ideas that I don't endorse. When I look at the long history of sentencing and all the literature on fines -- the vast European literature dealing with the Scandanavian system of -- you could make this kind of analogy.

You could say, well, this corporation had profits on a daily basis of a million dollars a day. We fine the individual defendant in this jurisdiction something like 30 days or one month of his salary. So we'll take one month of the corporation's profits.

I have a lot of trouble with that because the corporation is not an individual. It's a conglomerate with many different product lines. Many different profit lines. It produces some really odd disparities and artifacts.

If you look at two companies, one of which is a conglomerate like IT&T and one of which is closely-held, both making the same profit from the same product, one of which you look instead at the parent company's total revenues, and in the other case, you look at the rather miniscule revenues of this particular company.
I think really the focus should be on the profits from this activity rather than the overall revenues and profits of the company.

I also share -- with Judge Breyer about any attempt to look at particular pockets or sources of funds. Money is money. I don't think it makes sense whether it's on borrowing power, unused capital, cash flow, or something else that you would have earmarked for a specific purpose.

I really do think you've got to see what -- what we're looking at, but the cost of -- not where the source of funds come from. Otherwise, you put a tremendous premium on a company that's facing prosecution to get rid of these little pockets of money in terms of its general borrowing power, because it doesn't seem to have an easy target for a particular fine.

Okay. Now in this area of how do you escalate financial penalties, I think it's particularly important that you clarify with ambiguity Section 35, 72(b). We've talked briefly before I came up here about the maximum fine, which is $500,000 for an organization, except that it could be raised to one million where there are multiple caps. That is, the premise in 35.72(b) is that the court can increase the fine and impose an aggregate of fines where up to one million dollars, where they arrive from a common theme or plan and that, quote, "do not cause separable or
distinguishable harm or damage."

That's the important escape clause. Does the misconduct cause separable kinds or distinguishable kinds of harm or damage?

The Senate report suggests that is in there in order that, for example, a company that files 15 letters to a federal agency, all of which are false, might get 15 different prosecutions or 15 maximum fines of a half million dollars -- even out of these different letters, each of which violates false claims statutes and mail and wire fraud statutes. Same thing.

On the other hand, take the case where we do have a distinct kind of harm or damage. Each of those institutions, even though they're banks, suffers a distinct loss. It's a loss for them.

Is two or three thousand dollars a day for each of 50 or 60 banks? Now that's the kind of conduct where it seems to me that it's a loss to you and a loss to you. Obviously, distinguishable in terms of what you feel.

You need to clarify that. Otherwise, there is going to be the impression, which I've already heard both here and elsewhere, that the maximum is one million dollars. Not one million. It's one million only if the kinds of harm are not distinguishable. And when we have, for example, a toxic pollution case, we have to ask
ourselves:

Are these kinds of harm sustainable as suffered by victim A, victim B, victim C?

I think they are. But I think the first reading of the statute, because it looks like -- is very scanty on this topic, might convince a court looking at it quickly or a district court to write on these issues, doesn't have the centralized perspective you have...

They think this is all the same kind of harm. This is a pollution harm. So, therefore, even though there are 80 individuals, they aren't distinguishable.

All right. What's wrong there is you say that those kinds of harms, where they are distinct to different individuals or distinct kinds of harm, should create an ability to go above a million dollars because in the case of the corporate offender, the count deliberation is the norm. That is, credibility to 1,000 counts of mail and wire fraud. That's the regular and off the charts...again. But it is normal that you'll have a number of counts.

And prosecutors will quickly learn that they can impose very high penalties if they wish to take the effort to impose additional counts.

In the case of the individual defendant, the only reason for having 35 counts is to have something to plea bargain with. Drop it down to 22 counts. Down to 114 years
from 136, whatever. Plea bargaining heart attack.

In the case of the corporation, it's not. One's adequate to deter if 35.72(b) doesn't impose an absolute barrier. That I think depends on what you say about it and how much weight you put on this language of distinguishable kinds of harm...

Okay. Let me turn now to restitution. Again, restitution is commonly thought of simply as a matter of justice, restoring the victim. But it is a totally separable kind of sanction than one that clearly can go well above any maximum one million dollar fine.

Also it is not dischargeable in bankruptcy, as our fines also are not under the particular forces there.

The statute has broadly expanded its class of eligible victims. Prior to this statute, the loss had to be actually part of the indictment and proven as part of the prosecutor's case.

The statute clearly has phrased it differently, and the case law has rushed in the last year to embrace that statute. I think you have memos of your own which indicate what Durham, Richard, Allison, Keytext all say, and they are also all covered in my own memorandum to this body. And I have submitted a copy of it to the record, which shows that the case law now is really permitting the court -- the courts are embracing this opportunity. They are not always
loathe to expanding sentencing options -- is embracing the opportunity in a number of interesting cases:

To give restitution where it's caused even though it has no connection with the actual offense charged in the indictment or proven at trial.

There are cases such as Durham, which involve an individual who is a bankrobber, but in the course of escaping, commits arson and he winds up with a restitution for that uncharged, unproven arson to the insurance company that owns the car.

There is the case of a woman who was subject to a sexual attack, who later needs to apply this to your penance, as a kind of personal therapy. That cost of the air and travel expense is picked up on your restitution statute on the grounds that, although it was not proven at trial anyway, it was approximately proven...

Those are ways of escalating your penalty structure to recognize that the penalty structure needs to be escalated in this area.

And the case law goes to really all kinds of variations. My suggestion here is really that you should examine that case law closely, take it up and clarify it, and I think you will embrace this new standard, because it does focus around statutory options.

At the same time that we do that, however, there
are also problems here. I think this is a very two-sided statement I make here.

The due process accorded by the statute for restitution hearing is, in my judgment, not adequate and, in time, particularly in a large case, could result in constitutional obstacles and in cases which effectively take away this power unless it's handled separately in advance.

Here I think you need to enhance due profits beyond that accorded by Section 36.64. In particular, some kind of prior notes by the government to indicate exactly the kinds of losses.

We don't mean full-scale discovery. In a week or two. But, notes of losses properly specified in a particular fashion before the restitution hearing is convened.

I would also think that the use of -- should be -- as well, the individual probation officer...as possible.

There are again a number of offenses notes in the ABA standards that I would draw your attention to; particularly the notion of any civil defense would be available, including the causation. Offsets should be allowed in the restitution hearing.

Otherwise, we create a strange situation in which the restitution hearings are given a much larger award than it could in an available civil action.
Finally, I do think it's important that you try to adopt guidelines and carve out those areas in which civil litigation is already adequate to handle the problem, such as anti-trust, securities type liabilities, and not get involved in giving restitution for those kinds of impossibly broad classes.

The restitution hearing is not going to serve as a substitute for the class action. And I think that the best way to focus on this is not simply the number of complainants who were injured, but whether there is a viable other alternative litigation remedy, such as -- antitrust and securities liabilities.

Okay. I want to turn to identification very briefly. There's a curious statement in Section 35.72(F) of your statute which submits the corporation to pay the individual fine if state law permits. I'm not quoting exactly, but that's the substance of what it says.

From my ARR, where I serve as the reporter for the identification area, I can tell you that, essentially, state law does permit such a crime under the -- Act, does permit the Board or direct committee directors to identify, as long as the Board makes the finding that this was not a knowing illegal conduct.

Dealing with criminal law, it means knowledge of illegality rather than knowledge of the conduct. As a
result, identification is likely to be ignored.

Now, The sentence board again has a rather confused sentence that says:

We don't mean to disrupt the internal corporate government, but leave it to the state whether or not to permit identification.

All right, really you shouldn't disrupt traditional governments, but I think that that statement seems to ignore a very well-developed body of law on the limits of identification.

There are case laws in really all the principal circumstances. For example, with respect to securities -- liabilities, there cannot be identification even of civil liabilities. It's against public policy in virtually every circuit today to identify even civil liabilities where there is -- indicates the Securities Act liabilities -- more in criminal liabilities that should be identified.

What is involved here is not a question of overriding state law, recognizing your federal public policies in federal criminal statutes that cannot be identified.

I do think that you have a rule here to say a number of things in your standards that limit identification from at least some kind of liabilities.

Finally, even if you are -- I think you need to
look for procedures surrounding identification. One thing I think you clearly can do is to require notice at the sentencing hearing whether or not the corporation intends to identify, that notice would be such that it would be a false statement to make false notices.

I don't think corporations would dare do that.

(Conclusion of side 2 of tape 3.)
...considerable discretion, given the number of counts that could possibly have been prosecuted, to escalate the penalty to the crime (inaudible) to deter the corporation.

The minimum (inaudible) to find out who is (inaudible) and if this is a case in which the corporation has been identified, the penalty should be set with that fact in mind, at least within the limits of the maximum number of counts that they have been convicted of.

Okay, I have a few very brief concluding comments about probation.

I think that you should recognize that the ABA standards (inaudible). They didn't reject probation. They rejected some of the broader notions of probation under which the probation officer effectively had (inaudible).

They endorsed the notion of oversight, and what should oversight mean?

Well, here I think you have well-developed experienced from the SEC (inaudible). The SEC has time and again appointed special counsel for the corporation, and indeed this has now become a voluntary process.

E. F. Hutton did it in a special study and eventually changed the composition of their board of directors (inaudible) to an outside board.

To my mind, it is illusory to think that we are
going to have many cases of individuals violating a judicial order with respect to probation.

The case was presented this morning of the treasurer who simply resigns from office. Well, let him resign. Then look at the assistant treasurer and see if he wishes to resign. If he wishes to resign, move on to the assistant cashier. If all the corporate officers resign, you can now impose trusteeship, and an equity receivership is well-known in the SEC context.

The capacity of course to design remedies is well-known in many other areas of civil litigation. School boards, for example, without being convicted have been subjected to all kinds of novel decrees, and there has not been much problem.

Also, the collateral consequences of criminal convictions are so high (inaudible). Hutton shows this, as they were subject to blue sky commissioners in every state, and they were losing their right to manage mutual funds under different statutes. There was so much pressure on them (inaudible) strikes me as a very, very unlikely scenario.

But if it were to happen (inaudible) possibility of contempt and ultimately it is a criminal charge, obstruction of justice, which could apply to these kinds of proceedings. There was deliberate attempt to resist. I see
nothing here beyond the case law to deal with 50 years ago when they tried to figure out how to fine a corporation, again (inaudible).

I do think that there is much that can be done in the properly limited, properly constrained probation sanction, but essentially I am not proposing anything now or I am not proposing that you look to the SEC experience, how to generalize that. The publicity, the need to rehabilitate yourself is properly recognized by many within the company, and at a minimum, rather than simply looking to existing officers, the power to appoint special counsel to conduct an intensive self-study as the corporation's own counsel, so that he is able to pierce the attorney/client privilege and prepare a study of what went on among the directors. That to me is really the baseline (inaudible).

I don't mean this in a run of a mill sense, but in an important (inaudible) where the corporation's own internal processes appear to have been somewhat (inaudible). I think that is an important sanction.

Okay, I have spoken long enough. If you have got any questions I can answer, I would be happy to.

CHAIRMAN WILKINS: What about using net assets as a basis on which to calculate fines?

VOICE: Well, why should we distinguish between two companies, one of which has only one division and one of
which is ITT?

They both are expecting to make a $50,000 profit, and we are going to have one of these companies now pay a 5 percent of net assets penalty, a $10 billion penalty, and the other one million. We wind up using a very different level of deterrence. We over-deter large corporations and may under-deter small corporations. I had rather look at the profit.

And when we start using any kind of set percentage, we wind up having overkill, (inaudible) effects (inaudible) very large corporations. I just think it is (inaudible) of net assets.

CHAIRMAN WILKINS: Questions to my right?

VOICE: Looking at this question of escalating fines and penalties, is that because the (inaudible), I mean using different forms to escalate rather than using simply a fine --

MR. TROTT: I was suggesting that within the (inaudible). All I was looking at was the ceiling on the fine, which (inaudible), about whether there was a ceiling on the aggregate number of fines for each count, and I was (inaudible).

(Inaudible.)

Why am I doing this? I am really essentially at the lowest level of (inaudible).
VOICE: I was really talking about the question of these other types of --

MR. TROTT: Restitution or probation?

VOICE: Probation.

MR. TROTT: I think probation can be an incapacitative remedy. Others have dismissed that this morning, but I think you do have to look at corporations not only through an economic lense but as a culture. There are different kinds of cultures out there.

When you change the composition of the board of directors, you suddenly tell people that the ground rules have changed, that there is a new board (inaudible). The new one coming in (inaudible) to be very careful monitors, and it has a real impact on the corporate culture.

VOICE: Let me follow up on that.

We heard some testimony this morning that nothing changes the culture like sanctions in terms of threatened fines.

The question is do you need any direct control over the corporation; do you need to sort of be a consultant to the corporation; or can you just establish large monetary fine and then let the corporation find its own way in terms of --

MR. TROTT: We may have an extended discussion here because I do have a concern about who bears the cost
of very, very large monetary fines.

I tend to think that small fines are meaningless, as the information cost of monitoring your agents can be greater than the cost of most fines. The corporation isn't going to bother to find out what is really going on at that (inaudible) level until the costs of finding out are less than the costs of incurring business as usual. That might be a large level to begin with.

But once we get up to very large fines, at that point the cost of those fines may well be imposed on creditors as well (inaudible).

The logic of deterrence here is (inaudible). You want to focus on the shareholder, even though he is innocent, because he is the one party who can change the behavior of managers, and eventually when the penalties are high enough the monitoring will begin to price corporate securities in terms of the (inaudible) probabilities of future recidivism.

That kind of market-based remedy seems to me to -- one should focus on the shareholder (inaudible) no particular point, with very large fines upon creditors.

When you look at the financial structure of a large part of corporate America today, it is highly leveraged, and well before you could impose the kind of fine that reaches 25 percent of revenues you are going to thrust
that company into Chapter 11 because (inaudible) volatile, interest rates change (inaudible).

VOICE: We should follow this up.

VOICE: Yes, I was just thinking on that point, the very fact that you say that (inaudible) for bankruptcy (inaudible) less likely that you could collect it. If it is not dischargeable, the company has to dissolve, and you can't resurrect the company.

(Simultaneous voices.)

VOICE: This is no different than (inaudible).

VOICE: (Inaudible.)

VOICE: Things do get worked out.

My point was that creditors -- when you change the debt/equity ratio of the company, you are imposing a cost on creditors that to my mind accomplishes very little because they are not in a position (inaudible).

If you instead -- I don't want to go into full equity (inaudible) notion here, but when you break up (inaudible), that kind of notion simply imposes a cost on shareholders without any impact on the (inaudible).

VOICE: My actual question was -- at one point you seemed to suggest that there might be like a rule, and the rule would be when you fine a corporation the fine must be at least equal to the expected gain.

VOICE: Or loss.
VOICE: Or loss.

VOICE: That would be a guideline. You can deviate from all kinds of guidelines, but I would suggest rather than focusing on multiple (inaudible).

VOICE: I guess so, but I understand that once you say that then the judge looks at it, and I guess he has to do it, and what worries me a little, or at least (inaudible) and various others, is, my god, sometimes that will be possible.

But think of an antitrust case -- I mean think of your pollution case. I mean, let's imagine that. In some instances, you say, oh, that is what we will do, is we will just assess a fine equal to the cost of the pollution in question.

Well, the company will say, what do you mean the cost of the pollution in question? That wasn't an alternative. The reason we did this is the pollution equipment, if we purchase it, will put us out of business, and therefore we -- the gain. It was a saving on the pollution equipment. The expected gain was staying in business.

What is that worth? An imaginative lawyers like you or maybe me or some others here can think of 50 arguments that it would be totally crazy, right, and then they will have enormous hearing.
VOICE: We can have this tremendous game of (inaudible).

My answer to that would be even under the current statute, even under 3611, (inaudible) how you can make the payment, the court can modify the method of payment by installment schedules. He can do it through all kinds of mechanisms.

(Inaudible.)

You can pay not simply in cash (inaudible).

VOICE: That is not my point. My point is the absolute rule as this Commission sets it will cover both cases --

VOICE: I said a guideline. A guideline is not the same thing as an absolute rule.

VOICE: Could we say suggest that you leave it up to the district courts as to when (inaudible).

VOICE: Well, again, when the district court goes below that guideline, I think the appellate review of what is the reasons for going below that guideline then is justified.

(Inaudible.)

VOICE: They can go outside the guideline only for aggravating (inaudible).

VOICE: No, I think they can go outside the guideline for factors that are not set forth in the
guideline table, and you can indicate that deviation from
the guideline will be justifiable (inaudible).

But I think that that will be asserted far more
often than it would occur.

CHAIRMAN WILKINS: Ron.

COMMISSIONER GAINER: ' (Inaudible.)

VOICE: Yes, that is a very big problem. That is
the reason for not looking at a point (inaudible); that is,
you can say a court could reach a decision much more easily
(inaudible).

COMMISSIONER GAINER: (Inaudible.)

VOICE: The guidelines are, after all, ranges,
and I think that you may find it easier to set a range
(inaudible) fixation of the exact point (inaudible).

Am I answering you or (inaudible)?

COMMISSIONER GAINER: (Inaudible.)

CHAIRMAN WILKINS: Any other questions?

VOICE: Follow-up on Commissioner Gainer's point
about expected gain.

You don't mean that in a mathematical sense of
(inaudible) times the gain; you mean that in --

VOICE: When I look at the expected gain, I do
not mean really that the court should be in the business of
trying to figure out (inaudible) because that would be the
pure (inaudible) formula, and I don't think that a court of
law should really get involved in making computations
(inaudible).

VOICE: So you essentially would -- the
requirement could be translated as the necessity for the
crime to be punitive in the sense that a necessary
(inaudible).

VOICE: (Inaudible) more than simply (inaudible)
with respect to a gain that was never really received
(inaudible).

VOICE: What about -- did I understand you to say
that (inaudible)?

VOICE: No, I think it is difficult to convince
courts to impose fines. I don't think once it is imposed
(inaudible) that they are paid immediately. They may be
paid under installments, but they are paid.

VOICE: What about the corporation paying fines
(inaudible)? Do you say there is some difficulty in that?

VOICE: Well, I think -- my premise initially was
that you can't safely rely on a system of justice that
focuses exclusively on either the individual or the
corporation to the extent that identification is the norm --
now I am not saying it is the norm, but I am saying
(inaudible).

VOICE: Well, is it possible? I mean under state
law.
VOICE: Under the model (inaudible) Corporation Act, Section 5 of the (inaudible) Corporation Act, directors can identify an agent with respect to criminal fines provided they find that the conduct was not knowingly engaged in -- (inaudible).

VOICE: Is this a Delaware law?

VOICE: The Delaware law uses the phrase "good faith," also. This is a decision made not by the courts, but by directors. The board may well find that the (inaudible).

CHAIRMAN WILKINS: Thank you very much, Professor.

Would anyone else like to make any comments?

(No response.)

CHAIRMAN WILKINS: The record of this hearing will remain open for the next 30 days so that additional submissions can be received.

I want to thank our witnesses who have testified today and again to express to all of you our appreciation not only for you coming but all the hard work that you did prior to your arrival here in Washington, and I am confident that the comments and submissions will be very helpful to this Commission.

There being nothing further, we stand adjourned until our next hearing.
(Whereupon, the hearing was adjourned.)