Testimony of

# The Honorable Glen B. Gainer, III

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Chairman Biden, Ranking Member Grassley, and members of the Subcommittee:

I am Glen Gainer, West Virginia State Auditor and Chairman of the Board of Directors for the National White Collar Crime Center (NW3C), a non-profit corporation that provides nationwide support services for enforcement agencies involved in the prevention, investigation, and prosecution of economic and high-tech crime. I commend you for holding this hearing, and I am pleased to appear before you today to discuss the issue of penalties for white collar criminals, particularly as it relates to investment and securities fraud.

Before starting any discussion of punishment, it is important to outline the magnitude of the problem. Like many other types of economic crime, those individuals involved in securities and investment fraud represent a cross-section of society. The Securities and Exchange Commission (SEC) and state and federal courts have imposed both civil and criminal sanctions upon such diverse groups ranging from organized criminal enterprises to high school students. These offenders also include industry professionals, such as corporate officers, stockbrokers, promoters, accountants, and lawyers. The types of behaviors that fall under the umbrella of securities and investment fraud can also widely vary. These 'areas' of crime include, but are not limited to, market manipulation, affinity fraud, telemarketing fraud, foreign currency fraud, entertainment scams, investment adviser and financial planner fraud, abusive sales practices by brokers and agents, and ponzi and pyramid schemes.

The economic costs are difficult to quantify, but securities regulators and other prominent groups have estimated that securities fraud alone totals $40 billion per year. This is compared to $10 billion in estimated annual economic loss from 'street' crime, according to the FBI's Uniform Crime Report (UCR). Keep in mind that the dollar amount lost as a result of securities fraud does not measure the financial impact resulting from the volatility of the financial markets themselves, as over 50% of households in the United States now invest either directly or through pension funds and mutual funds. Another potential cost to consider is the documented relationship between terrorism and white collar criminal activities which directly impacts on our national security interests; some groups have used ill-gotten gains from fraudulent schemes to fund the operation of their organizations.

Despite the potential and visible impact associated with securities and investment fraud, a great disparity exists in punishment of white-collar and conventional crime offenders. This disparity exists at many levels, including likelihood of incarceration, and the length of the prison sentence imposed. In fact, due in part to mandatory drug-sentencing laws, the federal white-collar inmate population decreased in proportional terms, from 2.8% of the total in 1985 to 0.6% in 2001. During 1999, in cases terminated in U.S. District Courts, nearly 60% of offenders convicted of a fraudulent offense were incarcerated. This compares to 65% for burglary and 70% for motor vehicle theft. When looking at their prison sentences, the white-collar offenders received an average sentence of 22 months, while the burglary and motor vehicle theft offenders received 31 and 27 months, respectively. However, most of these white-collar criminal offenders were involved in smaller scale frauds and investment schemes, and are not reflective of the group of crimes that may net millions of dollars in profits at the expense of hundreds or thousands of innocent victims. And what do statistics regarding this group of offenders show us? For the year 2000, federal prosecutors indicated they charged 8,766 defendants with a white-collar crime. Of the 4,000 individuals who went to prison, only 226 were involved in securities fraud cases. From 1992 to 2001, SEC officials felt that 609 of its civil cases warranted criminal charges and were referred to U.S. Attorneys for consideration. Of these SEC referrals, only 142 defendants of 525 disposed cases were found guilty. Eighty-seven of these individuals went to prison. In terms of sentence length, research conducted in the early 90's clearly demonstrates the disparity between offenders. Those incarcerated for losses in excess of $100,000 or more as a result of the savings and loan scandals received an average of 36.4 months in prison. During the same time period, those nonviolent federal offenders who committed burglary got 55.6 months, car theft received 38 months, and first-time drug dealing averaged 65 months. While some of this disparity may have been corrected by revisions to the federal sentencing policy for economic crimes, disparate sentencing can still be seen between 'white-collar' cases involving substantial monetary loss, and other crimes with similar financial impact.

These unfavorable trends in punishment persist in an era where there is a strong public sentiment against white-collar crime. Recent data collected by the National White Collar Crime Center demonstrates that Americans view this type of behavior as more costly and problematic than 'traditional' or 'street' crime. Furthermore, many feel the punishment does not fit the crime. While most individuals feel white collar offenders should receive a tougher sentence, the consensus is that the criminal justice system is more likely to hand out lengthier prison terms for street crime offenders. These findings have been brought to light in recent months in the wake of the Enron and Andersen debacle, as the public continues to express frustration that more serious punishments are not meted out for corporate fraud and greed.

The conclusion we can safely draw from this body of information is that white-collar criminals, particularly those involved in large, complex frauds that impact hundreds, if not thousands of victims, do not receive punishment that is proportionate to the harm that they cause. This is not to say that all such offenders walk away from their actions with no repercussions from the criminal justice system. In May, Donald Allyson Williams was sentenced to 15 years in a California state prison as a result of a boiler room operation that would contact elderly individuals and eventually convince them to invest in speculative, high-risk oil and gas partnerships, partnerships that were purportedly safe. The result? These elderly investors lost $7.2 million, while Williams spent the bulk of the money on a lavish lifestyle.

What makes this case unique is not the nature of the crime -- unfortunately we see this type of behavior on a regular basis from individual and corporate entities alike. The unusual aspect of this example is that we had a successful conviction at all. For every Donald Allyson who serves time for investment or securities fraud, there are dozens of others people similar crimes who will not spend a day in court, let alone a day in prison. It is not merely enough to examine disparities in white-collar punishment from a sentencing perspective. It is also imperative that our enforcement agencies and our courts properly investigate, prosecute, and convict these individuals. Certainly sentences must deter criminal activity and protect the public. When weighing the low probability of conviction with the reality of a probationary period or minimal prison term, many white-collar offenders see these risks as an acceptable cost of doing business. We must change these attitudes and work toward sending a clear message to others who might be involved in, or who are planning, similar fraudulent activity. Research has clearly demonstrated that the most effective deterrent to crime is not only to increase the severity of punishment, but to increase the certainty of punishment. This two-pronged approach to the punishment issue is where our focus must be.

The difficulties of investigating and prosecuting securities and investment frauds are a result of the increased globalization of fraud, the complexity of the cases, and the limited resources of regulators and law enforcement officials. Prosecutors are often unwilling to bring forward economic crime cases that involve complex legal issues and extensive paper trails; following such trails becomes much more difficult because of the time that often elapses between criminal offending and discovery and subsequent investigation efforts. This is a problem inherent in many types of financial crime. For example, interviews with identity theft victims have found that several years may pass before the crime is discovered. Because the statute of limitations is often based on the date of the criminal occurrence rather than date of discovery, many criminals never face a judge because of the overwhelming task of gathering extensive evidence. The gap between the criminal act and its discovery also allows offenders to effectively cover tracks and destroy information that may otherwise prove invaluable to the investigative efforts.

In addition to a lack of resources as it relates to unraveling the complex underpinnings of an investment or securities fraud, criminal cases are not being brought because state and local law enforcement and prosecutorial agencies lack the technology and training to effectively investigate and prosecute them. In economic crimes, the attribution of responsibility, the development of facts, the tracing of funds, the establishment of the criminal fraud elements and the presentation of evidence are much more difficult to achieve than conventional crimes. Prosecutor's look to the referring agency for continued investigative, accounting and legal support in the case, which may be in the form of certificates of search, jury instructions, co-counsel, investigative support, accounting support, case funding, subpoenas, search warrants or expert witnesses. Often, this assistance is inadequate because the law enforcement and judicial systems are not prepared to deal with serious multi-jurisdictional white-collar crime cases. Preparation will require not just more criminal justice personnel devoting more time to such cases, but the commitment of ingenuity, technology, and training to develop the expertise for effecting ways of expediting the investigation, processing, and prosecution of such cases.

Coming back to the topic of this hearing, it is time for me to answer the question, are we really tough on white-collar offenders? Over the past several years, there have been a number of criminal convictions involving high-profile individuals who abused their positions of trust with stockholders, employees, and individual investors for their own financial benefit. And while most of the information I have shared with you today has focused on criminal enforcement issues, punishment continues to be handed out as a result of civil actions. In 2001, the SEC took in nearly $2.5 billion in civil fees, disgorgements, and penalties. However, these remedies, often sporadic and rarely commensurate with the monetary and emotional damage inflicted on victims, fail to send the resounding message that financial injustices against honest consumers will not be tolerated. Stiffer penalties and longer prison sentences are but part of the solution. We must also provide support for enforcement efforts that get defendants before a judge and jury. As recent events have shown us, our ability to fight crime relies on our ability to effectively leverage the resources of local, state, and federal agencies. We live in a time when technological advances have made white collar crimes more easy to commit on a widespread basis and, in some instances, more difficult to investigate and successfully prosecute. It has been said that fraudsters upgrade their equipment on the average every six months, while government agencies upgrade every four years. We must make investments in technology and training to provide for the type of analytical and investigative support an investment fraud case requires. As I alluded to before, white-collar crime is a multi-jurisdictional crime. This means we must enhance networking at the state and federal levels by fostering the sharing of antifraud information between various enforcement and regulatory agencies. To accomplish this, enforcement has to use technology to successfully combat the "mobile information era criminal fraudster." Information and the timely sharing of it are key ingredients to ensure a successful fraud investigation. When enforcement does not have access to the vast sources of electronic data to combat crime, it is equivalent to the law enforcement officer using a revolver against a criminal with a pistol. In either case, there is no excuse for allowing this disparity to continue if we are serious in addressing this ever-increasing fraud, which crosses states and international borders. And, it is important to remember that white-collar offenses are not crimes of passion; innocent individuals are the victims of these premeditated offenses. Not only must we raise the costs of committing fraud but also we must, through ethics training and other awareness efforts, communicate the seriousness of this behavior to industry leaders of today and of tomorrow. Without admitting or denying SEC findings of fraud, a 15-year old high school student from New Jersey agreed to return $285,000 from an Internet-based "pump and dump" scheme that netted him almost a million dollars. Both the teenager and his parents felt he had done nothing wrong, which clearly indicates a lack of moral duty and obligation.

For people to take these fraud issues seriously, we must continue to treat these fraud issues seriously, and strengthening the response from our criminal justice system is crucial to our efforts. I pledge the support of the National White Collar Crime Center to work with you and provide any additional information or assistance you may need. Thank you for the opportunity to testify before you today.