

Who Gets Caught?: Prosecutions for Financial Fraud⁺

by

Cindy A. Schipani^{*}

High profile cases, by definition, make the news headlines. Recently, the Securities Exchange Commission (SEC) filed charges against Dallas Mavericks owner Mark Cuban alleging violations of securities laws.¹ Goldman Sachs is also currently under investigation.² In recent years, the accounting firm of Arthur Andersen was charged with obstruction of justice³ as was former business magnate, television host and magazine publisher, Martha Stewart.⁴ While these events captured the attention of the public, the question might be asked whether less famous individuals and entities might be able to escape criminal investigation by virtue of flying under the radar screen. That is, does fame, with respect to individuals, and perhaps size, with respect to organizations, influence prosecutorial discretion? If so, are prosecutors missing other firms appropriate for investigation?

To address these issues, this paper reviews the literature regarding prosecutorial influences as well as the empirical studies addressing prosecution of financial fraud. This paper begins in Part I with a discussion of prosecutorial influences and discretion. Part II then considers issues of criminal prosecution for financial fraud and how federal prosecutors appear to select cases worthy of investigation while Part III examines the types of firms that attract the attention of the Securities Exchange Commission. Concluding remarks follow.

I. Prosecutorial Influences-The Decision Whether to Prosecute

In private civil enforcement actions, the decision whether to file a claim against a firm rests with the derivatively injured shareholders and their attorneys. The high potential costs of civil litigation make private claims unattractive when there is a low prospect of recovery. The decision whether to bring a private suit hinges on a cost benefit analysis. Plaintiffs and their attorneys will bear the costs of litigation, but will also win any potential rewards.

In public enforcement actions and criminal cases, decisions regarding whether to bring a case are more complicated. In such instances, society has certain interests which it seeks to vindicate by way of prosecution, and theoretically, a prosecutor will make the decision on behalf of the people after weighing the costs and benefits.

Occasionally agency problems arise if prosecutors do not act in the interests of society.⁵ Prosecutors may derive personal benefits from prosecution or non-prosecution. In some cases, potential personal benefits will not be aligned with the societal benefits. If prosecutors consider potential personal benefits in reaching their decision, they may bring cases where the public interest would be best served by non-enforcement, and they may decide against bringing cases where society's interests favor enforcement. The next section considers the interests of society in prosecution, while section B considers influences on prosecutorial discretion.

A. Societal Interests in Criminal and Civil Prosecution

Society has many interests when it comes to the enforcement of regulations. There are regulatory interests at stake, for which individuals and companies incur civil liability.⁶ Additionally, U.S. criminal law applies to corporations when the corporation is vicariously liable or directly liable for criminal acts.⁷ In this way, the criminal law extends the traditional societal interests of prosecution and punishment of individuals, such as retribution, incapacitation, rehabilitation, and deterrence,⁸ to the corporation.⁹

As is the case with individuals, society may seek to prosecute and punish corporations out of retributivist interests. Though traditional retributivist theorists argue that moral culpability can only be assigned to individual actors, recent scholarship has argued that the criminal prosecutions satisfy public demand for condemnation and retribution.¹⁰ In extreme situations, society may have an interest in incapacitating firms by punishing them to the point that they must close shop.¹¹ When an organization exists primarily for a criminal purpose, or operates primarily by criminal means, the Federal Organizational Sentencing Guidelines provide a fine “sufficient to divest an organization of all its net assets.”¹² Additionally, recent scholarship has argued that other factors related to mere prosecution, including negative publicity to the firm and the cost of criminal defense, may drive a firm to bankruptcy or liquidation.¹³

Criminal prosecution may also be justified as a means to rehabilitate corporations. Though not criminal sanctions, deferred prosecution agreements use the threat of criminal liability to impose sanctions in exchange for a promise not to seek prosecution. These agreements often force companies to develop plans to prevent future criminal behavior, and may involve the use of independent corporate monitors who oversee the implementation of the agreement. The agreements may also include clauses directing the corporation to assist in the prosecution of former executives or board members that are individually culpable. This will often force companies to rid themselves of executives and directors responsible for criminal behavior.¹⁴

Finally, society seeks to deter corporations, and their directors and executives, from breaking criminal laws.¹⁵ General deterrence might explain law enforcement’s focus on larger firms.¹⁶ Publicity and exposure from charges against large firms would likely have a greater deterrent effect to the public. However, general deterrence is most effective “when the deterrent examples appear sufficiently similar to those to be deterred to elicit the degree of identification necessary for the conclusion that what happened to the deterrent examples might well happen to the observers, should they violate the law.”¹⁷

Weighing against the societal interest favoring prosecution, there are many social costs. Society has vested prosecutors with discretion- allowing them to decide which cases are in the best interests of society. There are many common justifications for prosecutorial discretion. For example, prosecutors have only limited resources to available; consequently it is not possible for them to prosecute every crime.¹⁸ There is, moreover, a need for individualized justice because every case is unique.¹⁹ And finally, prosecutorial discretion serves as a check on the tendency of legislators to over criminalize conduct.²⁰

B. Prosecutorial Discretion

It is often said that prosecutors have almost unchecked discretion.²¹ As long as a prosecutor has probable cause to believe an accused committed a crime, he or she may decide to

bring a charge; a decision that is essentially unreviewable by the courts.²² Not all commentators, however, agree that prosecutors have unfettered discretion. Their power is counterbalanced by the doctrine of supervisory powers, the doctrine of separation of powers, professional discipline, and the political process.²³ Further, in the case of white collar crime, it has been said that prosecutors do not play as great of a role in selecting cases as is commonly thought.²⁴ This is because most investigations are initiated by regulatory agencies such as the SEC, and not by the Department of Justice (DOJ).²⁵

It is generally agreed that notwithstanding these safeguards, prosecutors still have substantial powers.²⁶ This may be, in part, because many purported safeguards are inadequate. For example, although federal prosecutors are, in theory, guided by the *Principles of Federal Prosecution of Business Organizations*²⁷ and by several other manuals²⁸ and ethical standards,²⁹ these principles may be, in practice, too vague and meaningless to provide any real guidance.³⁰

Prosecutors are vested with broad discretionary powers in order to weigh the interests of society when making a decision to charge or not.³¹ However, the interests of prosecutors are not perfectly aligned with society. The next part considers possible motivations of prosecutors in exercising discretion. It appears that they mostly use their discretion in a way that furthers their career.³² At the same time, politics and institutional structures influence the way in which prosecutorial discretion is used.³³

1. Winning and Career

According to some scholars the overriding interest of prosecutors is winning.³⁴ This desire to win is said to sometimes be so strong that it may trump ethical obligations, concerns over procedural fairness, or prosecutors' own possible concerns regarding the harshness of the federal sentencing guidelines and mandatory minimums.³⁵ To support the claim that prosecutors care about winning above all else, it has been suggested that prosecutors' desires to maintain high conviction rates, in part explains the strong resistance of prosecutors to post-conviction claims of innocence.³⁶ The argument is that if prosecutors did not care so much about their conviction rates, i.e. winning, and securing them, but instead cared more about justice, there would not be such resistance.³⁷ That prosecutors frequently make generous plea offers when a case is weak would also show that prosecutors ultimately care about winning.³⁸

Several reasons are given regarding why winning cases is so important to prosecutors. They involve the institutional structure prosecutors find themselves in and their ability to advance professionally. First, winning cases puts the prosecutor's office in a good light; conviction rates are used as leverage by offices in budget negotiations.³⁹ But not only are conviction rates an indication of how well an office is doing, the number of prosecutions matters too. At the federal level the perception is that offices that continue to increase the number of cases prosecuted have more resources allocated to them, while offices with declining prosecution rates are penalized.⁴⁰

Second, winning helps careers. Because it is difficult to measure a prosecutor's job performance, superiors often look at conviction rates for lack of a better measure.⁴¹ Prosecutors with the highest conviction rates have the best reputation.⁴² This in turn means that these prosecutors have the best chances of advancement internally; hence the desire to win cases is strong.⁴³ Even if prosecutors do not wish to stay in a prosecutor's office but have other aspirations, winning can be important. If prosecutors want to run for mayor, governor, or judge, and many do, high conviction rates can be used to gain the support of the public.⁴⁴ Some

commentators further suggest that being able to dwell on past convictions is crucial to the electoral chances of a prosecutor.⁴⁵

Chief prosecutors at the state level have a special interest in obtaining high conviction rates.⁴⁶ Because they are elected and usually may be reelected any number of times, they care about conviction rates not merely to advance, but simply to maintain their position.⁴⁷ Even federal prosecutors, who are appointed and not elected, are not free from political influences; high conviction rates may be important to secure their positions.⁴⁸

It is also worth noting that the desire to win becomes stronger over time.⁴⁹ Prosecutors who care most about conviction rates on average have twice as much as experience as prosecutors who seem to also have a great concern for justice.⁵⁰ This might mean that prosecutors may come into office expecting to do justice, but after a while realize that if they want to advance professionally, be it internally or elsewhere, their main focus needs to be on conviction rates.⁵¹ This is an important point if they are primarily seeking to maximize professional gains.⁵²

A study analyzing prosecutors' decisions on whether to allocate a drug case to the state or federal level supports the career maximization idea.⁵³ The main finding of this study is that federal prosecutors focus on prosecuting individuals who are older, more successful in their (legal) careers, more likely married, more likely to be Army veterans, and less likely to have a criminal record than the individuals prosecuted by their state counterparts.⁵⁴ They in particular take on more cases in which the defendants have private attorneys, or are likely to hire private attorneys.⁵⁵

These findings can be interpreted in two ways. One is that the defendants prosecuted by federal prosecutors are more difficult to prosecute, and more likely to have crossed state lines and are therefore charged in federal court. Another plausible explanation is that these defendants are more likely to be high-profile. Federal prosecutors would therefore take these cases not because they necessarily belong in federal court, but because they are most helpful in advancing their careers.⁵⁶ The latter possibility is further supported by the tendency of federal prosecutors to focus on these types of cases in states where high salaries can be earned in the private sector.⁵⁷ Because prosecutors may care about securing a lucrative job, this career advancement technique is employed most widely in those states. This study seems to support the claim that prosecutors ultimately care about their careers and strategize accordingly.⁵⁸ Thus, it seems clear that both winning and professional goals play a role in prosecutorial motivation.

2. Politics, Public, and Agents

It has been said that all prosecutors are political.⁵⁹ United States Attorneys are political appointees and their sponsor is usually a United States Senator.⁶⁰ Anyone who offends the federal prosecutor may thus risk falling out of favor with powerful people. That prosecutors are political often means they are interested in seeking higher office.⁶¹ Those interested in higher office may try to prosecute as many high-profile cases as possible to put themselves a favorable light with important figures and the public.⁶² Apart from being motivated by a desire to climb up the political ladder, prosecutors may also be motivated by ideological ideas.⁶³ These prosecutors may care less about the high-profile nature of the cases and more about cases that fit well with their ideological convictions, whatever they may be.⁶⁴ Based on the foregoing, however, one wonders how often, and for how long, ideology is the main drive for prosecutors.⁶⁵

That prosecutors are political does not only mean they have political aspirations; at its core it simply means that they may yield to political pressure—although the reason could be political aspirations.⁶⁶ Declination rates indeed are low when there is public pressure on prosecutors to take action. For example, when states were calling for stricter enforcement of immigration laws, immigration prosecutions in federal border districts increased more than sevenfold between 1994 and 2000.⁶⁷

Prosecutors do not only try to appease the electorate and their superiors, but they also try to maintain good relationships with other law enforcement agents. For instance, the high declination rate for civil rights offenses (92.8% in 1999), may be because many of the suspects are law enforcement officers.⁶⁸ A prosecutor who questions the conduct and integrity of agents may not be able to expect much cooperation from officers in subsequent cases.⁶⁹

It appears that whether the motivation is to please the public, the office, or to advance one's own career, and the former two perhaps reinforce the latter, prosecuting high-profile cases is important to prosecutors. As described by one commentator, prosecutors "hold[] the promise of institutional and personal glory."⁷⁰ Thus, prosecutors may focus on high-profile cases because they enable them to move on to lucrative jobs, although at the same time such a focus may be seen as an appropriate response to a public outcry, and reflect a preference of the administration.⁷¹ These interests may possibly trump the deterrent or remedial effects of such high-profile prosecutions.⁷²

One area where prosecutors may try to make a name for themselves through high-profile prosecutions is white collar crime.⁷³ In the 1980s corporate consolidations led to job losses and the public perceived corporate America as ruthless.⁷⁴ Prosecutors responded to this perception by bringing a number of high-profile cases, among them one against Michael Milken.⁷⁵ Many of the cases brought were overturned which suggests that prosecutors were responding to public sentiment more than anything else.⁷⁶

Similarly, in the wake of the collapse of Enron, prosecutors also brought a number of high-profile cases. These cases made national headlines and attracted public attention.⁷⁷ Yet, Martha Stewart, for example, was not prosecuted for insider trading, the conduct that prompted and was the focus of the government's investigation, but for lying during the investigation.⁷⁸ This again suggests that the prosecutors were mainly responding to a public outcry to take action.

Prosecutors appear to be thus influenced by politics and may often be motivated to act in a way that will please those they depend on for support; their superiors, the public and other law enforcement officials. Bringing high-profile cases is one way of achieving these goals. Prosecutors may also act out of a desire to service the public and do justice, but for many of them a chief concern will be their own career, which may influence their decisions on whether to proceed with a prosecution.

II. Criminal Prosecution for Financial Fraud

A prosecutor's decision whether to proceed with a criminal prosecution is of great significance to individual defendants,⁷⁹ but an indictment against a corporation may be its death knell.⁸⁰ In dealing with white collar crime, the already broad discretionary powers of prosecutors are enhanced because prosecutors have discretion regarding whether to characterize the wrong as civil or criminal.⁸¹ Moreover, neither the SEC nor individual shareholders generally have sufficient resources to deal with the white collar cases prosecutors decide not to file, augmenting the importance of the decisions they make in this field.⁸²

Virtually all individual defendants indicted in relation to financial fraud scandals between 1978 and 2004 have pled or have been found guilty.⁸³ Of those found guilty, the majority received a prison sentence for an average of 4.2 years.⁸⁴ Regarding the impact an indictment may have on a firm, an oft-cited example is Arthur Andersen; with the firm closing its doors leaving 28,000 people without a job, even though its conviction was ultimately reversed by the Supreme Court.⁸⁵

After the wave of corporate scandals at the beginning of the millennium and the more recent backdating scandals, the prosecution of corporate employees and of corporations, has received heightened attention.⁸⁶ In deciding how to best respond to the scandals, prosecutors not only need to decide whether to focus their attention on entities or individuals, but also on the types of individuals and entities that merit their scrutiny. Do they, for example, pursue high-ranking executives, large corporations, or lower level employees and small firms?

This Part will first discuss general studies concerning the type of cases prosecutors bring. It will then discuss studies that have tracked prosecutorial data specifically relating to recent scandals, addressing issues surrounding prosecution of corporations and those surrounding prosecution of individuals.

A. Empirical Studies – Criminal Charges in General

In his empirical analysis of data covering the period from 1994 to 2000, Michael O'Neill examined the types of cases federal prosecutors declined along with the reasons behind declination.⁸⁷ The data showed that although the number of cases referred to prosecutors increased substantially, (44%) during that period, the number of cases in which prosecution was declined went down from 36% to 26%.⁸⁸ This increase in prosecution suggests that more resources have been allocated to investigators and prosecutors, increasing their ability to effectively deal with crime.⁸⁹ The study also showed that larger districts decline fewer cases; presumably because more crime occurs in these districts and they have more resources to their availability.⁹⁰ Whether a certain matter is designated as an enforcement priority by Congress and receives significant public attention, also affects declination rates.⁹¹ If a certain offense is a national priority, or both a national and a district priority, it is more likely to be prosecuted than when it is only a district priority or not a priority at all.⁹²

There were also some interesting findings relating to fraud cases. For the period the data covered, fraud cases were among the most likely to be declined for prosecution.⁹³ Forty-four percent of all fraud cases were declined, while only 20% of all drug offenses and 34% of violent crimes were declined by the prosecutors.⁹⁴ A possible explanation for this may be that fraud cases are complex, and therefore prosecutors tend to stay away from them.⁹⁵ Another explanation offered is that alternative means of dealing with fraud cases are commonly used, such as fines or civil forfeiture.⁹⁶ In addition, fraud cases may also be prosecuted by the states, and so to conserve federal resources, federal prosecutors may choose to leave many fraud cases to the states.⁹⁷

This study showed that cases involving large dollar amount frauds were more likely to be declined for prosecution than cases involving smaller losses.⁹⁸ Ranking all fraud cases based on dollar loss, cases in the top third percentile had a 55% declination rate, while cases in the bottom third percentile only had a 42% declination rate.⁹⁹ This may be because larger, substantial frauds are harder to prosecute than smaller ones.¹⁰⁰ Given that corporate fraud has become a national

priority, however, and has received significant media attention, one would now expect to see a high rate of prosecution in financial fraud cases.

O'Neill suggests there is an indication that fraud cases, even though they had high a declination rate during the period under analysis, were of particular interest to federal prosecutors.¹⁰¹ Policy reasons are relatively less likely to be given for declining to prosecute fraud offenses than for regulatory public-order offenses.¹⁰² In contrast, evidentiary reasons are more likely to be given as a reason for declining to prosecute fraud cases than drug or public-order offenses.¹⁰³ Presumably this suggests that prosecutors as a matter of policy prefer to pursue fraud cases, but are often kept from doing so because of evidentiary concerns.¹⁰⁴

Another study looked at prosecutorial decision-making with regard to white-collar offenses at the state level.¹⁰⁵ Identifying all white-collar cases referred to the Wisconsin Department of Justice's Criminal Litigation Unit ("CLU") between January 1990 and May 1995, the study attempted to uncover prosecutors' justifications for prosecuting white-collar cases, including fraud cases.¹⁰⁶ During the period under analysis, 124 white-collar cases were referred to the CLU, but only 76 cases were prosecuted.¹⁰⁷ This finding seems consistent with the results of O'Neill's study,¹⁰⁸ in the high declination rate for fraud cases in the federal system. In addition, the Wisconsin study found that criminal prosecution was saved for the cases where the intent to defraud was obvious, whereas in less egregious cases the state relied on civil penalties.¹⁰⁹ This is also consistent with O'Neill's study in so far as he suggests that the declination rate for fraud cases in the federal system may be high, in part, due to other means available for addressing fraud, such as the imposition of civil penalties.¹¹⁰ Yet, if it is assumed that the most egregious cases will often be cases where a large monetary loss is involved,¹¹¹ the Wisconsin study would seem contrary to O'Neill's finding on the federal level, where O'Neill found that frauds involving high dollar losses were most likely to be declined for prosecution.¹¹² Moreover, if O'Neill is correct that federal prosecutors prefer to prosecute fraud cases but decline at least part of them because states may also pursue them, federal prosecutors may be incorrect in assuming states will prosecute a large number of fraud cases, if the high declination rates in Wisconsin are representative of other states.

B. Prosecution of Corporations

Corporate criminal liability was established by the Supreme Court in 1909.¹¹³ In that year, the Court held that any criminal act committed by a corporation's employee within the scope of employment, and in part intended to benefit the corporation could be imputed to the corporation.¹¹⁴ After the collapse of Enron and the ensuing wave of corporate scandals much has been written about the response of the prosecutors to corporate fraud.¹¹⁵ Since 2003, however, rather than prosecute a corporate entity, prosecutors have been frequently entering into Deferred Prosecution Agreements (DPAs) and Non-Prosecution Agreements (NPAs).¹¹⁶ Under a DPA, the government indicts a company but does not prosecute the claim. Instead, the government enters into an agreement with the firm and if the company fulfills its obligations under the agreement, the charges are dropped when the agreement expires. In contrast, a company entering an NPA is not indicted, but, similar to a company entering a DPA, the firm must agree to certain conditions. If the company violates the terms of the agreement charges may still be filed.¹¹⁷ Because in some cases an indictment alone may have severe consequences for a corporation, NPAs, which may be taken by the market to signify a lower level of culpability than DPAs, are preferable.¹¹⁸ DPAs and NPAs had traditionally been used in the sanctioning of

juvenile and drug offenders,¹¹⁹ but they now are a powerful tool in handling corporate fraud cases.¹²⁰ Before 1993, DPAs and NPAs had not been used to deal with federal criminal charges against a corporation.¹²¹ Between 1993 and 2002 only thirteen such agreements were concluded,¹²² while in the following three years thirty-five were concluded.¹²³

There are several reasons supporting the popularity of DPAs and NPAs. One is that entering into a DPA or NPA avoids the collateral consequences associated with an indictment, such as closing the company which, in turn, may leave thousands of people jobless.¹²⁴ Moreover, the prosecution of companies is complex and firms can afford experienced defense counsel.¹²⁵ By entering into DPAs and NPAs prosecutorial resources are saved.¹²⁶ Prosecutors also claim that they could not obtain broader, or even the same relief through the courts.¹²⁷ In addition, the corporation may be less blameworthy than the individual employees and therefore resources are best spent prosecuting those individuals.¹²⁸

Another explanation for why DPAs and NPAs are frequently used in the corporate context may be the result of the Thompson Memorandum.¹²⁹ Then Deputy Attorney General Thompson issued a Memorandum in 2003, stating that prosecutors will only bring charges against a corporation in a minority of cases; prosecution of individuals should always take precedence over the prosecution of corporate entities.¹³⁰ DPAs and NPAs are claimed to be a useful aid in prosecuting individuals.¹³¹ Yet, even without the Thompson Memorandum and the use of DPAs and NPAs, individuals were more likely to face criminal prosecution than corporations, and the prosecution was rather successful in obtaining convictions.¹³²

Even though the focus may have already been on individuals, it looks as if due to the proliferation of DPAs and NPAs even fewer companies are actually indicted and go to trial. Since 2003, nearly every major federal case of corporate misconduct has been resolved without filing an indictment against the firm.¹³³ The major indictments were the prosecution of Arthur Andersen in 2002 and Milberg Weiss in 2006. Generally, it has been only the cases involving small companies that have gone to trial—many of the companies that enter into agreements with the DOJ are Fortune 500 companies.¹³⁴ But there are exceptions. When the current leadership of a corporation has played a role in the fraud, they may be less likely to agree to settle with the DOJ because it could have far-reaching consequences for them.¹³⁵ This may be what happened in the case of Arthur Andersen and Milberg Weiss, but may more commonly be the case with smaller companies.¹³⁶

It may be that prosecutors choose to focus their resources on select group of well-known companies after a major scandal, even if in the form of an NPA or DPA, to send a strong message to other companies that the conduct in question may have serious consequences.¹³⁷ Viewed in this light, prosecutors would not only be giving heed to politics and public outcry or trying to advance their own careers, but would also be trying to achieve optimal deterrence. This approach is known as the optimal penalty theory.¹³⁸

Further evidence of the propensity of prosecutors to focus on large companies in the wake of the Enron and Worldcom scandals are the large amounts of fines, restitution and compensation paid under DPAs and NPAs.¹³⁹ Between 2003 and 2006, the DOJ entered into 35 DPAs and NPAs,¹⁴⁰ the average amount of compensation paid was \$141 million.¹⁴¹

Thus, with regard to companies, the focus seems to be on the larger ones. In the past cases against large companies were almost never pursued.¹⁴² It is still true today that large companies are almost never indicted, it may even be the case that there are fewer indictments than in the past. But this statistic is misleading. Instead, large firms are being investigated at a

higher rate – they are not prosecuted simply because they are entering sweeping agreements to preventing indictment.

C. Prosecution of Individuals

In the wake of the corporate scandals of the early 2000s, the federal government issued an executive order creating the Corporate Fraud Task Force (Task Force).¹⁴³ The mission of the Task Force is “to strengthen the efforts of the [DOJ] and Federal, State, and local agencies to investigate and prosecute significant financial crimes, recover the proceeds of such crimes, and ensure just and effective punishment of those who perpetrate financial crimes.”¹⁴⁴ In dealing with the scandals the government has more heavily focused on prosecuting individuals than corporations.¹⁴⁵

Scholars have found that proliferation of DPAs and NPAs has been accompanied by an increase in the prosecution of senior-executives in order to save the corporation.¹⁴⁶ Since its inception in 2002, the Task Force has convicted more than 1000 individuals for corporate fraud, including 100 CEOs and Presidents, 100 Vice Presidents, and 30 CFOs.¹⁴⁷ A possible explanation for these high numbers could be that prosecutors use agreements with the firms as leverage to prosecute high-ranking individuals. Prior to 1960, corporate executives were almost never incarcerated; instead corporations were punished with a fine for wrongdoing that occurred.¹⁴⁸

Corporations now enter into agreements with the prosecutors and at least in some instances agree to provide evidence against their senior executives to do so.¹⁴⁹ Both DPAs entered into by Computer Associates International, Inc.¹⁵⁰ and KPMG,¹⁵¹ for example, were accompanied by multiple indictments of senior management, including a CEO, and both companies agreed to cooperate in their prosecution.¹⁵² An interesting oddity, which provides support for the claim that prosecutors are pursuing high-level executives, is Boeing’s NPA.¹⁵³ This agreement provides that misconduct in violation of the agreement by someone who is not a high-level executive, as defined by Boeing, shall not constitute breach of the agreement.¹⁵⁴

Professor Brickey has tracked trials related to post-Enron scandals at seventeen major companies.¹⁵⁵ Although she points out that it is axiomatic that fraud prosecutions are resolved by guilty pleas,¹⁵⁶ looking at who ends up going to trial and what happens to them may provide a valuable insight into prosecutorial discretion as it relates to corporate fraud cases.

The data Brickey examines covers the period from March, 2002 to January, 2006, during which 46 defendants of seventeen companies went to trial in twenty-three separate prosecutions.¹⁵⁷ This shows that prosecutors generally charge multiple defendants in corporate fraud cases.¹⁵⁸ Including the number of defendants who plead guilty while their colleagues went to trial increases the number of defendants charged at the companies to 60.¹⁵⁹ Guilty pleas are important to the success of the prosecution.¹⁶⁰ In a baseline study of fraud prosecutions between March 2002 and July 2004, charges against 87 defendants were resolved, but although 90% of the defendants were convicted, only 10% of those convictions were the result of jury verdicts.¹⁶¹ Guilty pleas are also important because the defendants who plead guilty often become cooperating witnesses for the government helping secure convictions against those who proceed to trial.¹⁶²

The data indicates that individuals who go to trial are “high-level executives who held positions of responsibility and authority within their respective organizations.”¹⁶³ The 46 defendants who went to trial included twelve CEOs, COOs, Presidents, Chairmen or Senior

Partners, five CFOs, seven Executive or Senior VPs, and five Investment Advisors.¹⁶⁴ Although it thus appears prosecutorial attention has been focused on high-ranking individuals, prosecutors have only been modestly successful in securing conviction of those individuals. Eighteen defendants were convicted, while eleven were acquitted and the jury deadlocked on charges against fifteen defendants.¹⁶⁵ However, where a mistrial was declared none of the defendants were acquitted at a retrial.¹⁶⁶

In an earlier article Brickey also shows that although the trials of Martha Stewart and Frank Quattrone lead some to believe that post-Enron, individuals are charged with easy to prove crimes rather than with crimes that go to the core of the financial scandals, this is not what is happening.¹⁶⁷ These so-called sideshow prosecutions¹⁶⁸ are not typical of post-Enron corporate fraud prosecutions.¹⁶⁹ The most common offense that individual defendants were charged with between March 2003 and July 2004 was conspiracy (98 times), which almost always had fraud as its object.¹⁷⁰ Next were securities fraud (68), wire fraud (58) and false books, records, reports or filing (30).¹⁷¹ In contrast, only 13 defendants were charged with obstruction of justice.¹⁷² Looking at the data in another way, at least 75% of the defendants have been charged with at least one substantive fraud offense.¹⁷³

In response to the recent scandals, prosecutors thus not only seem to focus their attention on high-ranked individuals, but also seem to attempt to secure convictions of these individuals on substantive offenses whenever they can. Yet, it may be that prosecuting high-profile individuals, especially celebrities such as Martha Stewart, may be preferred by prosecutors even in the absence of substantive offenses to charge.¹⁷⁴ Trying a celebrity not only garners attention, having the potential to advance the career of the prosecutor, but may also have a greater deterring effect than pursuing someone the public does not know. Yet, based on the type of individuals who went to trial and the significance of guilty pleas, it may be that prosecutors pursue all levels of employees, but are more likely to enter into plea bargains with lower ranked employees.¹⁷⁵

Some commentators, however, contrary to Brickey's findings, believe that prosecutors do not, in most instances, charge the executives with substantive offenses.¹⁷⁶ Professor Oesterle claims that in dealing with the corporate scandals prosecutors are increasingly making use of sideshow prosecutions, in which main actors in a public scandal are not indicted on the essence of the scandal, but on another less serious offense that comes to light during the investigation of the scandal.¹⁷⁷ This, he says, is because corporate fraud cases are high-risk. That is, they are complex, they involve many individuals, and the defendants are wealthy.¹⁷⁸ This means that the investigation and trial will be long and expensive and that the defense may be able to outspend the government.¹⁷⁹ It also means the jury may be overwhelmed by the facts, and that it can be difficult to assign individual blame because many individuals are often involved in these schemes.¹⁸⁰ Sideshow charges, on the other hand, are easier to prove for the prosecutor, easier to understand for juries, and can still carry significant penalties.¹⁸¹ Although there is some disagreement regarding the definition of a sideshow charge, examples include tax evasion, mail and wire fraud, stock parking, money laundering and obstruction of justice.¹⁸²

Another technique used to pursue high-ranking executives, is known as "working up the ladder," or the "domino game."¹⁸³ This is when the prosecutor finds a lower-level informer and offers him or her immunity in return for testimony or documents that can be used to encourage the higher ranking executives to accept a plea bargain.¹⁸⁴ Whether prosecutors make use of sideshow charges or work up the ladder, and whether their motivation for doing so are public

pressure or advancement of their personal careers,¹⁸⁵ it seems that prosecutors are focusing their attention on the high-level individuals.

III. Civil Enforcement by the SEC

This Part discusses the enforcement activities of the SEC and the impact of the fall of Enron and the subsequent enactment of the Sarbanes Oxley (SOX) legislation¹⁸⁶ on the SEC's enforcement policies. Studies have shown that there has been an increase in enforcement actions filed by the SEC post-Enron.¹⁸⁷ Furthermore, the SEC appears to be targeting larger companies since the collapse of Enron than it did prior to the Enron scandal¹⁸⁸ and monetary penalties for securities law violations have increased.¹⁸⁹

A. SEC Enforcement Powers

The SEC has a wide variety of civil and administrative powers to address corporate fraud.¹⁹⁰ The Enforcement Division (the Division) has the authority to investigate securities law violations, bring civil actions in federal court, bring an action before an administrative judge, recommend actions to be taken by the Commission, and negotiate settlements.¹⁹¹ The Division also has the power to impose various penalties on corporations and individuals for securities law violations.¹⁹² It may order the payment of civil monetary penalties, or the disgorgement of gains that resulted from misconduct. It also has the authority to bar individuals from serving as officers or directors of public companies, suspend trading in a company's stock for up to ten days, and revoke a company's public registration.¹⁹³ After the passage of SOX, the SEC may now also order a temporary freeze over payments the company is going to pay to its executives, and order CEOs and CFOs to forfeit any bonuses, incentive compensation, and profits from the sales of securities when a company restates its financial statements due to misconduct.¹⁹⁴

It has been argued that the SEC should use its enforcement authority primarily to pursue individuals because they are usually to blame for securities violations, rather than corporate entities.¹⁹⁵ The SEC has recognized that imposing civil penalties on corporate entities may not always be a sound course of action.¹⁹⁶ It has said that because penalties against corporations are often borne by their shareholders, they should only be sought when a violation has resulted in an improper benefit to those shareholders.¹⁹⁷ Other factors the SEC takes into account in deciding whether to initiate an enforcement action against a corporate entity are the nature of the misconduct, the reason the misconduct occurred, the organizational level at which the misconduct occurred, the degree of harm to the investors, the amount of time between discovery and the implementation of effective remedies, the degree of cooperation with the SEC, whether the company conducted a thorough review, and how likely it is the violation will happen again.¹⁹⁸

The above factors and the SEC's statement on enforcement against corporate entities create the impression that its focus is on culpable individuals. Professor Langevoort, however, claims that it is not so clear where the attention of the SEC lies.¹⁹⁹ Although the SEC may have been more aggressive in going after individuals since 2002, and there may have even been some high monetary penalties imposed on individuals, the total amount recovered probably comes nowhere near the aggregate gain from their misconduct.²⁰⁰ In any event, according to Professor Langevoort, it is too early to tell whether there has been a policy shift at the SEC toward focusing on individuals.²⁰¹

The reason suggested for why the SEC may be focusing on corporations instead of individuals is lack of funds.²⁰² It may be less costly to obtain a settlement from a company because they may be more willing to settle for a penalty than an individual.²⁰³ Especially during the 1990s, the SEC seemed to have been suffering from a lack of both human and financial resources.²⁰⁴ For example, between 1991 and 2001 the number of cases the SEC Enforcement Division opened rose 65%, but its staff grew only 27%.²⁰⁵ By creating more regulatory requirements and short deadlines, SOX aggravated the situation.²⁰⁶ However, with the corporate scandals and the passage of SOX, the SEC's budget doubled between 2002 and 2005.²⁰⁷ Another explanation for why the SEC may be focusing on corporations is publicity.²⁰⁸ Corporate penalties may be large enough to make headlines, while penalties imposed on individuals may not be large enough to have the same impact.²⁰⁹

B. Empirical Studies: SEC Enforcement in General

John Karpoff and his colleagues examined all 697 enforcement actions initiated by the SEC between 1978 and 2004 and tracked them through December 31, 2005.²¹⁰ The initiated actions resulted in a total of 4469 sanctions against individuals and 719 against corporate entities.²¹¹ Monetary penalties were imposed by the SEC and the DOJ. In 368 of the 697 actions, the median penalty was \$280,000.²¹² Only in 69 cases were monetary penalties imposed on corporate entities, the median being \$2.5 million.²¹³ These numbers cast doubt on the claim that the SEC is focusing its attention on sanctioning corporations, while letting individuals off the hook.²¹⁴ They do, however, seem to support the argument that it is harder to make headlines from penalties against individuals, even in the aggregate.²¹⁵ Yet, because there are most likely many more individuals involved in wrongdoing than are corporations, it is difficult to draw any definitive conclusions from these data.

One of the main findings of the Karpoff study is that penalties for financial misconduct increase with the size of the harm caused.²¹⁶ The SEC imposes penalties that increase with shareholders' losses, the amount of time required to resolve an enforcement action, and the presence of fraud charges. Non-monetary penalties, such as suspensions and censures, increase with the number of federal codes violated, the number of respondents in the enforcement action, and the number of regulatory proceedings.²¹⁷ In addition, monetary penalties imposed also increase with a defendant's ability to pay.²¹⁸ Similarly, relatively low penalties are imposed on companies in financial distress.²¹⁹ However, contrary to finding that penalties increase with the ability to pay, Professors Cox and Thomas found that there is no significant relationship between financial distress and the amount of a settlement.²²⁰

Cox and Thomas used a data set of 389 securities class action settlements that occurred between 1990 and 2003 to examine the overall effectiveness of public (SEC) and private securities enforcement.²²¹ Seventy-three of those cases, which is 19% of the sample, also had a parallel SEC enforcement action relating to the same misconduct challenged in the private action.²²² Cox and Thomas also found that overall penalties imposed on defendants increase with the amount of loss that resulted from their misconduct. Further, the SEC also appears to pursue larger companies more than do private plaintiffs, and seeks out companies where more investors are harmed.²²³

C. Empirical Studies: Influence of Enron and SOX

The data of both Karpoff and Cox and Thomas included enforcement actions initiated after the corporate scandals of 2001 and 2002. By comparing pre-January 1, 2002 (pre-Enron) data to later data (post-Enron), Cox and Thomas attempted to ascertain whether Enron affected enforcement patterns.²²⁴

Cox and Thomas found substantial changes in the market capitalization of defendant companies post-Enron.²²⁵ The average market capitalization for SEC enforcement targets was 23 times larger in the post-Enron period than in the pre-Enron period.²²⁶

With regard to factors that influence the SEC in deciding whether to file an enforcement action, Cox and Thomas find that pre-Enron, the only significant predictor is financial distress.²²⁷ They take this to mean that pre-Enron the SEC was mostly concerned with companies experiencing financial stress because of the likelihood that investors at those companies would suffer permanent losses.²²⁸ It could also mean that the SEC has a preference to take on weak opponents.²²⁹ This would support Professor Langevoort's claim that the SEC prefers easy targets because of a lack of resources, especially when we take into account that the SEC's financial situation pre-Enron was particularly dire. Some support for the weak opponent theory also comes from the Karpoff study where it was found that, for the entire sample, 31% of all firms targeted for enforcement declared bankruptcy around the time of the enforcement action.²³⁰

Post-Enron, Cox and Thomas find that the SEC appears to prefer targets where shareholders have suffered greater provable losses, and they have a bias toward selecting smaller firms, although firm size has increased significantly since the collapse of Enron.²³¹ The move away from targeting companies in financial distress could be supported by another of theories. One is that the Director of Enforcement of the SEC changed in 2000 and the new director may have had different objectives than his predecessor.²³² The public attention around the corporate scandals may also have influenced the SEC to seek out more high profile cases.²³³

Conclusion

Not surprisingly, research discloses a myriad of factors at play when prosecutors decide whether to file charges against an individual or corporation. In deciding which cases to pursue, prosecutors may be influenced by benefits to society, political pressures as well as personal interests such as career advancement. Intuitively, it would seem that these factors may lead prosecutors to select higher profile cases for prosecution. These cases might involve famous individuals and firms with large market capitalization.

Although somewhat mixed, review of the empirical studies discussed above gives some credence to this intuition. Brickey found that although the prosecutions were only moderately successful, individuals who went to trial between 2002-2006 for financial fraud involved high level executives.²³⁴ Cox and Thomas found that the size of the firms targeted by the SEC is nearly twenty-three times larger post-Enron than pre-Enron,²³⁵ although they also note a bias toward smaller firms.²³⁶ Furthermore, although companies tend to settle with the Department of Justice there has been a substantial increase in compensation awards through DPAs and NPAs against Fortune 500 companies.²³⁷

To the extent there is an inherent bias toward pursuit of high profile cases, the question remains whether this is optimal for society. On one hand, pursuing claims that attract the attention of the public may be an efficient use of resources. In a regime for finite resources this approach may have the most impact. Yet, it is also possible that to the extent such a bias exists

and is well-known, smaller, yet similarly culpable firms, and individuals at these smaller firms, may be encouraged to flout the law because there is little risk of getting caught. In effect, society may be inadvertently giving a free pass to these groups, which would seem to be an undesirable consequence. Further research might explore, both theoretically and empirically, whether there are ways to eradicate the bias and facilitate a more optimal outcome.

Footnotes

⁺ Copyright 2010, Cindy A. Schipani. All rights reserved. Please do not quote without permission of the author. The author would like to gratefully acknowledge the research assistance of Roseanne Kross and Jules DePorre.

^{*} Merwin H. Waterman Collegiate Professor of Business Administration & Professor of Business Law, Stephen M. Ross School of Business, University of Michigan.

¹ SEC v. Mark Cuban, Civil Action No.: 3-08CV2050-D (N.D. Tex. Nov. 17, 2009).

² SEC v. Goldman Sachs & Co, ECF Case 10-CV-3229 (S. D. N. Y. Apr. 16, 2010).

³ United States v. Arthur Andersen LLP, 374 F.3d 281 (5th Cir. 2004), *rev'd*, 544 U.S. 696 (2005).

⁴ SEC v. Martha Stewart, 03-CIV-4070 (NRB) (S.D.N.Y. June 4, 2004).

⁵ For a general discussion of market failure with respect to prosecutorial discretion see Frank H. Easterbrook, *Criminal Procedure as a Market System*, 12 J. OF LEGAL STUD. 289, 301 (1983).

⁶ See *infra* Part III for a discussion of SEC enforcement actions. When the SEC determines that a case warrants criminal prosecution, the SEC will closely with the Department of Justice to bring charges. Often times this gives the SEC considerable leverage during settlements, including cases where the conduct would not be civilly actionable. See Wendy Gerwick Couture, *White Collar Crime's Gray Area: The Anomaly of Criminalizing Conduct Not Civilly Actionable*, 72 ALBANY L. REV. 1, 38 (2009).

⁷ See Eli Lederman, *Models for Imposing Corporate Criminal Liability: From Adaptation and Imitation Toward Aggregation and the Search for Self-Identity*, 4 BUFF. CRIM. L. REV. 641,650-66 (2000) (discussing the vicarious and direct liability models).

⁸ See Michael A. Simons, *Prosecutors as Punishment Theorist: Seeking Sentencing Justice*, 16 GEO. MASON L. REV. 303, 307-08 (2009); see also, *Ewing v. California*, 538 U.S. 11, 25 (2003) (“A sentence can have a variety of justifications, such as incapacitation, deterrence, retribution, or rehabilitation.”).

⁹ These interests may also be served by the imposition of civil liability. See generally V.S. Khanna, *Corporate Criminal Liability: What Purpose Does it Serve?*, 109 HARV. L. REV. 1477 (1996).

¹⁰ See Samuel W. Buell, *The Blaming Function of Entity Criminal Liability*, 81 IND. L. J. 473, 517 (2006).

¹¹ See *infra* note 80, and accompanying text (suggesting that in some cases, an indictment have the effect of closing a company).

¹² U.S.S.G. §8 C1.1.

¹³ See Mary Kreiner Ramirez, *The Science Fiction of Corporate Criminal Liability: Containing the Machine Through the Corporate Death Penalty*, 47 ARIZ. L. REV. 933, 945 (2005). The author also argues that post conviction consequences such as additional reputational costs, monetary fines and the res judicata effect on subsequent civil suits may all contribute to the demise of a criminally liable firm. *Id.*

¹⁴ See generally Wilson Meeks, *Corporate and White Collar Crime Enforcement: Should Regulation and Rehabilitation Spell and End to Corporate Criminal Liability?*, 40 Colum. J.L. & Soc. Probs. 77 (2006) (discussing the DOJ's emphasis on rehabilitation of a corporation through deferred prosecution agreements, and arguing that societal interests in corporate rehabilitation would be better served through civil liability).

¹⁵ See Khanna, *supra* note 9, at 1493-96.

¹⁶ “General deterrence refers to the effect punishment of a specific person will have on other members of society who might be tempted to engage in similar conduct. Such deterrence is thought to work particularly well in connection with white-collar offenses and less well to deter crimes of passion, in which a criminal is thought likely to engage without much forethought to the punishment meted out to similarly-situated individuals. General deterrence is particularly apt with respect to corporate criminal conduct, which tends to be the antithesis of crimes of passion.” Andrew Weissmann & David Newman, *Rethinking Corporate Criminal Liability*, 82 Ind. L. J. 411, 429 (2007).

¹⁷ Richard Board, *Operational Criteria for Determining Criminal Responsibility*, 61 Colum. L. Rev. 221, 222 (discussing general deterrence and the effects of deterrence on the insane).

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- ¹⁸ See Tracy L. Meares, *Rewards for Good Behavior: Influencing Prosecutorial Discretion and Conduct with Financial Incentives*, 64 Fordham L. Rev. 851, 862 (1995).
- ¹⁹ *Id.*
- ²⁰ *Id.*
- ²¹ Janet C. Hoeffel, *Prosecutorial Discretion at the Core: The Good Prosecutor Meets Brady*, 109 Penn St. L. Rev. 1133, 1138 (2005).
- ²² Meares, *supra* note 18, at 862.
- ²³ Alexandra White Dunahoe, *Revisiting the Cost-Benefit Calculus of the Misbehaving Prosecutor: Deterrence Economics and Transitory Prosecutors*, 61 N.Y.U. Ann. Surv. Am. L. 45, 45 (2005).
- ²⁴ Michael L. Seigel & Christopher Slobogin, *Prosecuting Martha: Federal Prosecutorial Power and the Need for a Law of Counts*, 109 Penn St. L. Rev. 1107, 1109 (2005).
- ²⁵ *Id.*
- ²⁶ See e.g., Alexandra White Dunahoe, *Revisiting the Cost-Benefit Calculus of the Misbehaving Prosecutor: Deterrence Economics and Transitory Prosecutors*, 61 N.Y.U. Ann. Surv. Am. L. 45, 46 (2005).
- ²⁷ Larry Thompson, *Principles of Federal Prosecution of Business Organizations*, (Jan. 20, 2003) available at http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm
- ²⁸ UNITED STATES ATTORNEYS' MANUAL (1997) available at http://www.usdoj.gov/usao/eousa/foia_reading_room/usam/
- ²⁹ RULE 3.8 MODEL RULES OF PROFESSIONAL CONDUCT available at http://www.abanet.org/cpr/mrpc/rule_3_8.html; see also ABA STANDARDS FOR CRIMINAL JUSTICE: PROSECUTION AND DEFENSE FUNCTION, (3d ed., 1993) available at http://www.abanet.org/crimjust/standards/dfunc_toc.html.
- ³⁰ Michael A. Simons, *Prosecutorial Discretion and Prosecution Guidelines: A Case Study in Controlling Federalization*, 75 N.Y.U.L. Rev. 893, 934 (2000).
- ³¹ A legislative constraint on prosecutorial discretion would likely result in over-prosecution, as legislatures also tend to over-criminalize behavior.
- ³² See e.g., Edward L. Glaeser et al., *What do Prosecutors Maximize? An Analysis of the Federalization of Drug Crimes*, 2 Am. L. & Econ. Rev. 259, 288 (2000).
- ³³ See e.g., Daniel S. Medwed, *The Zeal Deal: Prosecutorial Resistance to Post-Conviction Claims of Innocence*, 84 B.U. L. Rev. 125, 134-35 (2004).
- ³⁴ See e.g., Abbe Smith, *Can You Be a Good Person and a Good Prosecutor?*, 14 Geo. J. Legal Ethics, 355, 388 (2001); Medwed, *supra* note 33, at 134-35.
- ³⁵ Smith, *supra* note 34, at 389-90.
- ³⁶ Medwed, *supra* note 33, at 136-37.
- ³⁷ See *id.* In some systems, an appellate prosecutor will be assigned to a case after conviction. Professor Medwed suggests several other factors explaining individual and institutional prosecutorial resistance to claims of innocence that would also be relevant in such systems. *Id.* at 137-169.
- ³⁸ Smith, *supra* note 34, at 390.
- ³⁹ Medwed, *supra* note 33, at 135.
- ⁴⁰ Simons, *supra* note 30, at 932-33. Simons does not state whether this is actually the practice of the Justice Department. *Id.*
- ⁴¹ Medwed, *supra* note 33, at 134.
- ⁴² *Id.*
- ⁴³ *Id.* at 134-35.
- ⁴⁴ *Id.* at 154-55.
- ⁴⁵ *Id.* at 155.
- ⁴⁶ *Id.*
- ⁴⁷ *Id.* at 151.
- ⁴⁸ *Id.* at 152; see H. W. Perry, Jr., *Government Lawyering: United States Attorneys- Whom Shall They Serve?*, 61 Law & Contemp. Prob. 129, 138 (1998).
- ⁴⁹ Medwed, *supra* note 33, at 138.
- ⁵⁰ *Id.*
- ⁵¹ See Hoeffel, *supra* note 21, at 1140 (the typical...prosecutor...will only be noticed, climb the career ladder, or become a member of elected office...if he racks up the convictions).
- ⁵² Dunahoe, *supra* note 26, at 60.
- ⁵³ Glaeser et al., *supra* note 32.

⁵⁴ *Id.* at 288.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.* at 283.

⁵⁸ That this study focused on federal prosecutors does not mean state prosecutors are not motivated by the same concerns. *See id.* at 264.

⁵⁹ *See* Medwed, *supra* note 33, at 152; *see also* Perry, *supra* note 48, at 143.

⁶⁰ Perry, *supra* note 48, at 138.

⁶¹ *Id.* at 143.

⁶² *Id.* at 144.

⁶³ *Id.* at 142.

⁶⁴ *Id.*

⁶⁵ *See* Medwed, *supra* note 33, at 138 (conviction rates are more important to seasoned prosecutors, justice more to newcomers).

⁶⁶ *See* Daniel Richman, *Prosecutors and Their Agents, Agents and Their Prosecutors*, 103 Colum. L. Rev. 749, 760 (2003).

⁶⁷ *Id.* at 766.

⁶⁸ *Id.* 765; *see also* Simons, *supra* note 30, at 933.

⁶⁹ Smith, *supra* note 34, at 392.

⁷⁰ *Id.*; *see* Simons, *supra* note 30, at 933.

⁷¹ Christine Hurt, *The Undercivilization of Corporate Law*, 33 Iowa J. Corp. L. 361, 435 (2008).

⁷² *Id.*

⁷³ *See, e.g.*, Seigel & Slobogin, *supra* note_, at 1130; Hurt, *supra* note 71, at 372.

⁷⁴ J. Kelly Strader, *White Collar Crime and Punishment: Reflections on Michael, Martha and Milberg Weiss*, 15 Geo. Mason L. Rev. 45, 52 (2007).

⁷⁵ *Id.*

⁷⁶ *See id.* at 52-53.

⁷⁷ *Id.* at 53-54.

⁷⁸ Seigel & Slobogin, *supra* note 24, at 1107.

⁷⁹ Michael Edmund O'Neill, *Understanding Federal Prosecutorial Declinations: An Empirical Analysis of Predictive Factors*, 41 Am. Crim. L. Rev. 1439, 1442 (2004); Jonathan M. Karpoff et al., *The Legal Penalties of Financial Misrepresentation* 9 (May 1, 2007) (available at <http://ssrn.com/abstract=933333>).

⁸⁰ Peter J. Meitl, *Who's the Boss? Prosecutorial Involvement in Corporate America*, 34 N. Ky. L. Rev. 1, 15 (2007).

⁸¹ Ellen S. Podgor, *The Ethics and Professionalism in Discretionary Decisions*, 68 FORDHAM L. REV. 1511, 1519 (2000).

⁸² Stephen J. Choi, *The Evidence on Securities Class Action*, 57 Vand. L. Rev. 1465, 1466 (2004).

⁸³ Karpoff et al, *supra* note 79, at 8-9.

⁸⁴ *Id.*

⁸⁵ Arthur Andersen LLP v. United States, 544 U.S. 696, 708 (2005); *see also* Meitl, *supra* note 80, at 15.

⁸⁶ *See, e.g.*, Dale A. Oesterle, *Early Observations on the Prosecution of Business Scandals of 2002-03: On Sideshow Prosecutions, Spitzer's Clash With Donaldson Over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation*, 1 Ohio St. J. Crim. L. 443, 444 (2004).

⁸⁷ O'Neill, *supra* note 79, at 1444.

⁸⁸ *Id.*

⁸⁹ *Id.*

⁹⁰ *Id.* at 1446.

⁹¹ *Id.* at 1452.

⁹² *Id.*

⁹³ *Id.* at 1453.

⁹⁴ *Id.* at 1454.

⁹⁵ *Id.* at 1453.

⁹⁶ *Id.*

⁹⁷ *Id.* at 1454.

⁹⁸ *Id.* at 1457.

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ *Id.* at 1465.

¹⁰² *Id.*

¹⁰³ *Id.*

¹⁰⁴ *Id.* Backdating cases may not have the same sort of complicated evidentiary issues, explaining why the data we present in Part V does not comport with O’Neill’s findings.

¹⁰⁵ Michael Kades, *Exercising Discretion: A Case Study of Prosecutorial Discretion in the Wisconsin Department of Justice*, 25 Am. J. Crim. L. 115, 119 (1997).

¹⁰⁶ *Id.*

¹⁰⁷ *Id.*

¹⁰⁸ O’Neill, *supra* note 79, at 1454.

¹⁰⁹ Kades, *supra* note 105, at 119.

¹¹⁰ O’Neill, *supra* note 79, at 1454.

¹¹¹ See Kades, *supra* note 105, at 148.

¹¹² O’Neill, *supra* note 79, at 1457.

¹¹³ See *New York Central & Hudson River Railroad Co. v. United States*, 212 U.S. 481 (1909).

¹¹⁴ *Id.* at 492.

¹¹⁵ See Christopher A. Wray & Robert K. Hur, *Corporate Criminal Prosecution in a Post-Enron World: The Thompson Memo in Theory and Practice*, 43 Am. Crim. L. Rev. 1095 (2006); Oesterle, *supra* note 86; Meitl, *supra* note 80; Kathleen F. Brickey, *Enron’s Legacy*, 8 Buff. Crim. L. Rev. 221, 258-60 (2004); Kathleen F. Brickey, *The Changing Face of White-Collar Crime: In Enron’s Wake: Corporate Executives on Trial*, 96 J. Crim. L. & Criminology 397, 401 (2006).

¹¹⁶ Leonard Orland, *The Transformation of Corporate Criminal Law*, 1 Brook. J. Corp. Fin. & Com. L. 45, 57 (2006).

¹¹⁷ *Id.* at 56.

¹¹⁸ Erik Paulsen, *Imposing Limits on Prosecutorial Discretion in Corporate Prosecution Agreements*, 82 N.Y.U. L. Rev. 1434, 1438 (2007).

¹¹⁹ See, e.g., Wray & Hur, *supra* note 115, at 1104.

¹²⁰ Orland, *supra* note 116, at 45.

¹²¹ *Id.* at 57.

¹²² *Id.*

¹²³ Brandon L. Garrett, *Structural Reform Prosecution*, 93 Va. L. Rev. 853, 894 (2007).

¹²⁴ *Id.* at 901.

¹²⁵ *Id.*

¹²⁶ *Id.*

¹²⁷ *Id.*

¹²⁸ *Id.*

¹²⁹ Memorandum from Larry D. Thompson, Deputy Attorney General, to Heads of Department Components and United States Attorneys (Jan. 20, 2003), available at http://www.usdoj.gov/dag/cftf/corporate_guidelines.htm.

¹³⁰ Wray & Hur, *supra* note 115, at 1098.

¹³¹ Garrett, *supra* note 123, at 884; see also Brickey, *The Changing Face of White-Collar Crime*, *supra* note __, at 402; but see Orland, *supra* note 116, at 75 (indictment of executives is only reflected in 17 out of 44 DPAs and NPAs between 1993 and 2006).

¹³² Karpoff et al., *supra* note 97, at 9, 32.

¹³³ Orland, *supra* note 116, at 45.

¹³⁴ Garrett, *supra* note 123, at 888-90.

¹³⁵ *Id.* at 902.

¹³⁶ *Id.*

¹³⁷ Ashwini Jayaratnam, *Prosecuting Stock-Option Backdating: The Ethics of Enforcement Techniques*, 20 Geo J. Legal Ethics 755, 760 (2007).

¹³⁸ *Id.* at 761.

¹³⁹ *Id.* at 900.

¹⁴⁰ *Id.* at 894.

¹⁴¹ *Id.* at 900.

¹⁴² *Id.* at 883.

¹⁴³ Executive Order Establishment of the Corporate Fraud Task Force, July 9, 2002, *available at* <http://www.whitehouse.gov/news/releases/2002/07/20020709-2.html>

¹⁴⁴ *Id.*

¹⁴⁵ Lisa Kern Griffin, *Compelled Cooperation and the New Corporate Criminal Procedure*, 82 N.Y.U. L. Rev. 311, 312 (2007).

¹⁴⁶ Orland, *supra* note 116, at 47.

¹⁴⁷ Christine Hurt, *The Undercivilization of Corporate Law*, 33 Iowa J. Corp. L. 361, 379 (2008).

¹⁴⁸ *Id.*

¹⁴⁹ *Id.* at 63.

¹⁵⁰ Deferred Prosecution Agreement between the United States and Computer Associates International (Sept 22, 2004) *available at* <http://f11.findlaw.com/news.findlaw.com/nytimes/docs/ca/usca904defpagr.pdf>

¹⁵¹ Deferred Prosecution Agreement between the United States and KMPG (Aug. 26, 2005) *available at* <http://www.usdoj.gov/usao/nys/pressreleases/August05/kpmgdpagmt.pdf>

¹⁵² *Id.*

¹⁵³ *Id.* at 69-70.

¹⁵⁴ *Id.* at 70.

¹⁵⁵ Brickey, *The Changing Face of White-Collar Crime: In Enron's Wake: Corporate Executives on Trial*, *supra* note 115, at 401.

¹⁵⁶ *Id.* at 400.

¹⁵⁷ *Id.* at 401.

¹⁵⁸ *Id.*

¹⁵⁹ *Id.* at 402.

¹⁶⁰ *Id.*

¹⁶¹ *Id.* at 403.

¹⁶² *Id.*

¹⁶³ *Id.* at 404.

¹⁶⁴ *Id.* at 406.

¹⁶⁵ *Id.* at 407.

¹⁶⁶ *Id.* at 418.

¹⁶⁷ Brickey, *Enron's Legacy*, *supra* note 115, at 258-60.

¹⁶⁸ Oesterle, *supra* note 86, at 449.

¹⁶⁹ Brickey, *Enron's Legacy*, *supra* note 115, at 260.

¹⁷⁰ *Id.* at 261.

¹⁷¹ *Id.* at 262.

¹⁷² *Id.*

¹⁷³ *Id.* at 263.

¹⁷⁴ Jayaratnam, *supra* note 137, at 762.

¹⁷⁵ *See, e.g., id.* at 276.

¹⁷⁶ Oesterle, *supra* note 86, at 443.

¹⁷⁷ *Id.* at 449.

¹⁷⁸ *Id.* at 446.

¹⁷⁹ *Id.*

¹⁸⁰ *Id.*

¹⁸¹ *Id.* at 449-50.

¹⁸² *Id.* at 451. *See* Brickey, *Enron's Legacy*, *supra* note 115, at 276 (criticisms that the government [is] sidestepping the complex financial frauds that are the core of the...scandals...are fundamentally misinformed...defendants are typically charged with wire fraud...).

¹⁸³ Oesterle, *supra* note 86, at 447.

¹⁸⁴ *Id.* at 448. This could be what Brickey is referring to when she mentions that prosecutors are targeting all culpable parties, from lower level employees to high-ranking executives by using a building-block approach. Brickey, *Enron's Legacy*, *supra* note 115, at 276.

¹⁸⁵ *See* Oesterle, *supra* note 86, at 447, 483; *see also* Garrett, *supra* note 123, at 932 (prosecutors push for high-profile convictions...in order to advance their institutional interests).

¹⁸⁶ Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified as amended in scattered sections of 15 U.S.C., 18 U.S.C., and 28 U.S.C.).

¹⁸⁷ Brickey, *Enron's Legacy*, *supra* note 115, at 251-52.

¹⁸⁸ James D. Cox & Randall S. Thomas, *Public and Private Enforcement of the Securities Laws: Have Things Changed Since Enron?*, 80 Notre Dame L. Rev. 893, 901 (2005).

¹⁸⁹ Karpoff, et al., *supra* note 79, at 22.

¹⁹⁰ Brickey, *Enron's Legacy*, *supra* note 115, at 251.

¹⁹¹ *Id.*

¹⁹² Karpoff et al., *supra* note 79, at 6.

¹⁹³ *Id.*

¹⁹⁴ Donald C. Langevoort, *On Leaving Corporate Executives "Naked, Homeless and Without Wheels: Corporate Fraud, Equitable Remedies and the Debate over Entity Versus Individual Liability*, 42 Wake Forest L. Rev. 627, 653 (2007).

¹⁹⁵ *Id.* at 661.

¹⁹⁶ *Id.* at 629.

¹⁹⁷ Press Release, Sec. & Exch. Comm'n, Statement of the Securities and Exchange Commission Concerning Financial Penalties (Jan. 4, 2006), <http://www.sec.gov/news/press/2006-4.htm>.

¹⁹⁸ Brickey, *Enron's Legacy*, *supra* note 115, at 241.

¹⁹⁹ Langevoort, *supra* note 194, at 628.

²⁰⁰ *Id.* at 629.

²⁰¹ *Id.* at 629.

²⁰² *Id.* at 654.

²⁰³ *Id.* at 654.

²⁰⁴ Brickey, *Enron's Legacy*, *supra* note 115, at 242.

²⁰⁵ *Id.* at 242-43.

²⁰⁶ *Id.* at 244.

²⁰⁷ Karpoff et al., *supra* note 79, at 2.

²⁰⁸ Langevoort, *supra* note 194, at 654.

²⁰⁹ *Id.*

²¹⁰ *Id.* at 3-4.

²¹¹ *Id.* at 8-9.

²¹² *Id.* at 10.

²¹³ *Id.*

²¹⁴ Langevoort, *supra* note 194, at 628.

²¹⁵ *Id.* at 654.

²¹⁶ Karpoff, *supra* note 79, at 3.

²¹⁷ *Id.*

²¹⁸ *Id.* at 20.

²¹⁹ *Id.* at 21.

²²⁰ Cox & Thomas, *supra* note 188, at 904.

²²¹ *Id.* at 895.

²²² *Id.*

²²³ The results of the study show that, for the complete sample, class actions without parallel SEC enforcement actions result in lower average settlement amounts, are on average brought against companies with a smaller market capitalization, have shorter average class periods, and on average are more time-consuming to settle. *Id.* at 899. Thus an SEC enforcement action seems to increase the settlement amount of a corresponding class action. The study also looked the factors that seemed to influence the amount of a class action settlement. It found that, for the entire sample, the absolute dollar amount of a settlement goes up with the size of the provable loss, the size of the defendant company, the length of the class period, and a parallel SEC enforcement action. Provable loss is defined as "the difference between the price at which the investors purchased or sold the security and what that price would have been but for the misrepresentation." *Id.* at 896. Cox and Thomas also found that plaintiffs pursuing companies without a parallel SEC enforcement action have a lower average ratio of settlement to provable loss. *Id.* at 899. This seems inconsistent with the conclusions of Karpoff et al., *supra* note 79, who argue that public and private penalties act as substitutes, which may mean that the ratio of settlement to provable loss may well be higher for plaintiffs when there is no parallel enforcement action. *See id.* at 4.

²²⁴ Cox and Thomas, *supra* note 188, at 899. Their study also showed that the average private settlement amount in private actions with parallel SEC cases is more than three times as much as the settlement where only a private

action is brought post-Enron. *Id.* at 900. Pre-Enron the average private settlement with a corresponding SEC action was not even double the settlement obtained without an SEC action. *Id.* at 898.

Private settlement amounts where there is no corresponding SEC action increased too, but not as much. *Id.* at 900. The latter finding seems to be inconsistent with findings from the Karpoff study. The Karpoff study showed that private monetary penalties decreased post-SOX. Karpoff et al., *supra* note 79, at 4. Karpoff did find, however, that SEC penalties increased post-SOX.²²⁴ It thus seems reasonable to conclude that Enron and SOX increased the public penalties for financial misconduct.

²²⁵ Cox & Thomas, *supra* note 188, at 901.

²²⁶ *Id.* at 901-02.

²²⁷ *Id.* at 905.

²²⁸ *Id.*

²²⁹ *Id.*

²³⁰ Karpoff et al., *supra* note 79, at 8.

²³¹ Cox & Thomas, *supra* note 188, at 906. Although these firms are relatively small, compared to the pre-Enron period, the firms being targeted by the SEC post-Enron are on average, twenty-three times larger than firms targeted pre-Enron in terms of market capitalization. *Id.* at 902. 906.

²³² *Id.*

²³³ *Id.*

²³⁴ *Id.*

²³⁵ *Id.*

²³⁶ *Id.*

²³⁷ See Jayaratnam, *supra* note 138, at 833.