



March 12, 2003

US Sentencing Commission
C/O Office of Public Affairs
Suite 2-500 South Lobby
One Columbus Circle, NE
Washington, DC 20002
Attn: Michael Courlander

Dear Mr. Courlander:

LRN, The Legal Knowledge Company, is pleased to have the opportunity to respond to the U.S. Sentencing Commission's January 17, 2003 request for public comment. LRN commends the Commission for addressing the important issues raised in the proposed amendments to the sentencing guidelines, particularly given the short time-frame in which the Commission was required to act.

As a leading provider of Web-based legal, ethics, and compliance training, LRN has worked with many of the largest companies in the world to develop effective systems for communicating the organization's values and standards, as well as their compliance training. In addition, LRN's network of over 1,000 legal experts research legal and compliance issues across a broad range of topics for the law departments of many of these same companies. Based on LRN's experience and research, we provide the following comments with regard to Issue 1 of the Commission's Issues for Comment for consideration.

Issue 1(A): Corporate Fraud—The Loss Tables

As part of the emergency amendment, the Commission expanded the loss table in

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§2B1.1(b)(1), providing for two additional levels to the table: and increase of 28 levels for offenses in which the loss exceeded \$200,000,000 and an increase of 30 levels for offenses in which the loss exceeded \$400,000,000. The Commission asks whether, when it repromulgates the emergency amendment as a permanent amendment, the loss table should be modified more extensively to provide increased levels for offenses involving lower loss amounts and provides three alternatives for public comment. Additionally, the Commission requests comment regarding whether it should amend §2B1.1(a) to provide an alternative base offense level, either in conjunction with, or in lieu of, an amendment to the loss table, that would apply based on the statutory maximum term of imprisonment applicable to the offense of conviction—for example, five, ten, fifteen, or twenty years.

LRN believes that modifying the lower loss amounts in the loss table will likely have little or no impact in addressing the conduct that was the focus of the Sarbanes-Oxley Act (the Act). The corporate scandals that largely led to the Act's creation involved substantial losses to investors and employees, and the 28- and 30-level increases the Commission has promulgated for those substantial losses address, for the most part, the intent of the Act. Indeed, it is likely that any fraud committed by an officer or director of a public company, once revealed, will result in substantial loss of shareholder value and the lower loss amounts in the loss table will be largely irrelevant.

For example, public disclosure of securities fraud at a publicly traded company often leads to a material decrease in the company's share price. And as the guidelines now contemplate such a reduction as a "loss" for purposes of the loss tables, it is highly likely that the loss will quickly exceed the \$1 million mark. Thus, a 10% drop in market value of a corporation with a \$1 billion market capitalization, will result in a loss of \$100 million. We therefore suggest that, if the Commission's purpose is to address the types of misconduct witnessed in the corporate scandals of 2002, the lower loss amounts are irrelevant. This is particularly true when the additional enhancements the Commission has promulgated for officers and directors of public companies who commit fraud offenses are applied.

However, the Commission's proposal to increase the base offense level in §2B1.1(a) from six to seven for offenses that the Congress deemed most egregious seems appropriate. We therefore suggest that §2B1.1(a) be amended to read as follows:

(a) Base Offense Level:

(1) 7, if the defendant was convicted of an offense referenced to this

guideline for which the maximum term of imprisonment prescribed by law is 20 years or more; or
 (2) 6, otherwise.

Again, our focus is on the intent of Congress in passing the Act. Our basis for the twenty-year maximum term provision is derived from what we perceive as Congress's intent to address the most egregious cases. For example, in the Act, Congress

- increased the maximum penalty for mail and wire fraud from five to twenty years,
- increased the criminal penalties for securities fraud from ten to twenty years,
- created new criminal laws for destroying documents or otherwise obstructing federal investigations with a maximum twenty years imprisonment
- created ten and, in the case of willful violations, twenty year prison terms for failure of corporate officers to certify financial reports
- created a ten-year maximum prison term for retaliating against a whistleblower, and
- created a new securities fraud statute with a twenty-five year maximum prison term.

The increase in the base offense level, coupled with the addition of the 28-and 30-level increases for very high losses, appears to satisfy Congress's intent that the sentencing guidelines adequately address those fraud offenses that are particularly extensive and serious. And it does so without a wholesale revision of the loss table, thereby avoiding a lengthy analysis of the appropriateness of the relatively incremental changes among the lower loss amounts.

Issue 1(B): Corporate Fraud—Enhancement at §2B1.1(b)(13)

As part of the emergency amendment, the Commission promulgated a new enhancement at §2B1.1(b)(13) that provides a four level enhancement if the offense involved a violation of securities law and, at the time of the offense, the defendant was an officer or director of a publicly traded company. The Commission asks whether, when it repromulgates the emergency amendment as a permanent amendment, it should expand the scope of at §2B1.1(b)(13) to include other individuals or entities that may have a fiduciary or similar statutory duty of trust and confidence to the investor. Possible examples included brokers, dealers, and investment advisers, as well as their associated persons, and other market professionals who may not be a regulated entity under the securities laws.

We have found that the successful implementation of an effective system to communicate the organization's standards and procedures largely depends on the commitment to the program by senior management. Thus, the "tone at the top" set by the

most senior leaders of an organization plays a crucial role in how compliance and ethics are viewed by the rest of the organization. In this regard, and based on LRN's experience and research, we agree that a four-level enhancement for fraud offenses committed by officers and directors of publicly traded companies is appropriate.

However, before addressing the proposed expansion of the emergency amendment to other persons, LRN first suggests that the Commission clarify certain elements of the emergency amendment. As currently drafted, the subsection applies in the case of a defendant convicted under a general fraud statute if the defendant's conduct also "violated" a securities law. We assume that such a "violation" must be proved by a preponderance of the evidence by the prosecution at sentencing, but this is not clear. Moreover, many securities prosecutions are brought parallel to civil actions brought by the Securities and Exchange Commission. In fact, many such cases may be settled with the SEC without admitting or denying the allegations. But the SEC still often makes findings in such settlements. Such a finding by the SEC could be tantamount to the *de facto* establishment of a securities law violation, without any additional evidence being presented. LRN therefore suggests that the Commission provide guidance in the application notes as to its intent with regard to how a securities law "violation" is to be established.

In addition, by including all "violations" of the securities laws, the amendment could have the effect of criminalizing conduct that would otherwise purely be a technical violation. For example, under §13 of the Securities Exchange Act of 1934, a company must keep accurate books and records of its financial transactions. The SEC may bring an action against individuals--typically an administrative proceeding--seeking an order that they cease and desist from "causing" the company to fail to keep accurate records. And while the materiality of a particular record is often examined by the SEC to determine whether to charge an individual or organization with a §13 violation, the statute does not require it. Thus, even a single inaccurate--and possibly immaterial--record caused to be created by an individual could lead to the enhanced sentence. Furthermore, under new disclosure and reporting requirements, a number of disclosures are required to be filed within short time periods. Even a one-day delay in making an appropriate filing--and thus a technical violation of the securities laws--could lead to the enhanced sentence. We do not believe this is the Commission's intent and we suggest the Commission provide further guidance as to its intent with regard to the application of this provision.

Furthermore, LRN notes that proposed expansion of the amendment to market professionals may have the unintended effect of bringing within it many persons who were not the focus of Congress when passing the Act. The expansion may thus have the effect of diluting the Act's emphasis on corporate governance. In passing the Act, Congress identified a particular problem--namely, that those at the very top of an organization set the tone for the entire organization. The potential for serious losses arising from the example they set is therefore much greater. These factors--the leadership role they play in the organization and the potential for great losses--caused Congress to

substantially increase regulations and sanctions to address these leadership shortcomings.

By expanding the amendment to others who are not officers or directors of their companies, that is, not the leasers of their organizations, the amendment casts a much wider net. For example, the amendment would likely cover a registered representative employed at a broker-dealer who churns a single customer's account. While the employee certainly deserves to be punished, is the application of the enhancement consistent with congressional intent? Furthermore, §3B1.3 (Abuse of Position of Trust or Use of Special Skill) seems to already address just this scenario, causing a 2 level increase to the employee's sentence, without having to go through the exercise of establishing a securities law violation at sentencing. LRN therefore suggests that the Commission narrowly apply the amendment to those market professionals who, because of their positions of trust, have the potential to cause the greatest amount of harm. In that regard, perhaps the amendment is appropriate for the leadership of market participants, such as the officers and directors of a brokerage firm or other regulated entity (which may or may not be a publicly traded company) because their illegal conduct could cause great losses and even threaten the integrity of the capital markets. But for the low-level employees who happen to work for such an entity, LRN suggests the Commission utilize already existing sentencing guidelines, as their status in the marketplace and their duties vis-à-vis the investing public do not rise to the same level as the officer or director of a public company.

If this argument is rejected by the commission and it is the intent to extend the amendments to lower-level employees, LRN notes that certain professionals, such as investment advisers, have statutorily-defined fiduciary duties under specified circumstances, and clearly are closer to the status of an officer or director of a public company because of their similar position of trust and confidence. However, other market professionals do not have statutory fiduciary duties, but may, under certain circumstances, accept such a duty by offering certain products or services.

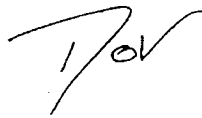
For example, case law suggests that no fiduciary duty arises between a securities broker and his customer simply by virtue of the broker-customer relationship. Of course, because of their position in the marketplace, market professionals are held to high standards of business conduct and fair dealing. To avoid confusion, we therefore suggest the Commission simply identify those market professionals to which the enhanced standard will apply, based on the Commission's policy determination that such professionals are similar enough to the public company officer or director, and then offer the courts guidance for determining which additional individuals, not otherwise identified in the amendment, may be covered by it. We also suggest that the Commission insert language into the guidelines explaining the intent for including these marketplace professionals and the types of duties or responsibilities the Commission expects would bring an individual into the provision as a "similar" person.

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LRN appreciates the opportunity to respond to the Commission's request for

public comment. We hope the Commission finds our response helpful.

Sincerely,

A handwritten signature in black ink, appearing to read "Dov", with a stylized flourish extending from the end.

Dov Seidman
Chairman and Chief Executive Officer