Text only of letters sent from the Committee on Energy and Commerce Democrats

March 21, 2001

The Honorable David M. Walker
Comptroller General
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Walker:

We are writing to request your assistance with respect to a matter of significant importance to the protection of investors. It involves the abysmal collection rate on court-ordered disgorgement funds. The purpose of the disgorgement sanction is to ensure that securities law violators do not profit from their illicit activities and to compensate investors harmed as a result of the violations.

First, we request that the General Accounting Office (GAO) update its August 1994 report, **Securities Enforcement: Improvements Needed in SEC Controls Over Disgorgement Cases, GAO/GGD-94-188 (August 23, 1994)**, to the Chairman of the Energy and Commerce Committee's Subcommittee on Oversight and Investigations, and inform us of the extent to which the Securities and Exchange Commission (SEC) has implemented GAO's recommendations or taken other steps to improve the agency's procedures and management controls and ultimately to improve the collection rate. GAO reported that federal district courts had imposed an estimated $2 billion in disgorgement sanctions in about 600 cases from 1987 through April 1994 and that about 50 percent of that amount was actually collected. GAO found that SEC (1) did not maintain aggregate information on the amount of disgorgement collected from defendants and distributed to investors or to the U.S. Treasury that could help it better assess the effectiveness of its disgorgement efforts and monitor trends in receiver costs; (2) lacked formal qualification standards and guidelines for selecting receivers in administratively-imposed disgorgement cases to ensure that receivers SEC recommends to the court are selected on an impartial basis; and (3) had weak controls over receivers and the funds in their possession which deficiency could provide the opportunity for fraud, waste, and abuse. While GAO did not uncover any evidence of fraud or abuse in its investigation, it did find one case involving high, poorly-documented attorney fees, and it is important to keep in mind that receiver fees and expenses are paid from the disgorgement fund, decreasing the amount available for distribution to investors. Accordingly, GAO recommended that the SEC:

- Ensure that systems used to manage disgorgement cases include aggregate and individual case information on disgorgement ordered, disgorgement collected, amount and recipients of disgorgement distributed, and information about receivers and funds in their possession.

- Establish formal guidelines for SEC attorneys to use for recommending individuals as receivers and allow interested parties whom SEC determines meet these criteria to place their names on a roster from which a receiver could be chosen for a particular case.

- Establish a standard format for fee applications submitted by receivers and establish formal written guidelines for SEC attorneys to use for monitoring

receivers' activities and the funds they handle. In establishing such procedures, SEC should recommend, where appropriate, that the court orders include requirements that (1) receivers file periodic reports with SEC on the funds they hold and (2) the funds may be subject to an audit if SEC believes it necessary after reviewing the periodic reports.

Second, recent press reports, *e.g.*, **"Conned Investors May Never See Refunds, SEC Collection Rate Falls Sharply Since '94," USA Today cover story**, Tuesday, January 9, 2001, indicate that the SEC has fallen badly behind, having collected only 16.9 percent of the more than $1.7 billion in illegal gains that securities fraudsters have been ordered to hand over since 1995. This recovery rate – about $1.69 of every $10 owed – is an outrage. It represents a sharp drop from the 50 percent rate disclosed in GAO's 1994 report. Furthermore, it is totally unacceptable. Defrauded investors deserve better results than this. In addition to the low collection rate, USA Today reported that the SEC has not collected one penny in 10 large cases involving violators who collectively owe $540 million under disgorgement orders. Additionally, the SEC didn't appoint its first collections administrator to track the hundreds of cases scattered across the country until October 1999, more than five years after GAO's 1994 report focused attention on the need for improvements in SEC controls. We request that GAO examine the entire disgorgement collection process, identify the reasons for this steep fall-off, and develop recommendations for improvement.

Thank you for your cooperation and attention to our request. We intend to work vigorously to correct this significant hole in the fabric of investor protection.

Sincerely,

John D. Dingell
Ranking Member
Committee on Energy and Commerce

Paul E. Kanjorski
Ranking Member
Subcommittee on Capital Markets, Insurance,
and Government Sponsored Enterprises
Committee on Financial Services

cc: The Honorable W. J. "Billy" Tauzin, Chairman
Committee on Energy and Commerce

The Honorable Michael G. Oxley, Chairman
Committee on Financial Services

The Honorable John J. LaFalce, Ranking Member
Committee on Financial Services

The Honorable Laura Unger, Acting Chairman
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Prepared by the Committee on Energy and Commerce
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