Sentencing guidelines—despite their name, they give judges little discretion—have been around since 1987. But they were stiffened in 2002 as part of "emergency" measures in the wake of the Sarbanes-Oxley corporate reform movement. The maximum punishment for wire and mail fraud, the most common white-collar infractions, was increased from 5 to 20 years. A chief executive who makes a material misstatement that causes a 50-cent drop in his company's billion-share float now faces 11 years in jail.

If he is instead caught trafficking 40 grams of heroin, he'll be back on the street in three years. If he kills someone intentionally, but not murderously, and is convicted of voluntary manslaughter, the maximum federal punishment is ten years.

"These sentences are outrageous for nonviolent, nondrug cases," says Preston Bruton, a former federal prosecutor who, as a criminal defense attorney, serves on the U.S. Sentencing Commission's practitioners' advisory group.

Okay, Enron's ex-finance chief Andrew Fastow should do hard time for a fraud that cost employees and investors billions of dollars. But the irrationality of the white-collar sentencing system became painfully apparent in March, when Jamie Olis, a 38-year-old former midlevel Dynegy executive, was given 24 years for booking a loan as revenue. Olis is no Snow White, but neither is he a thief on a grand scale. His take from the misdeed reportedly was $272,000 in salary and bonus in 2001, plus $200,000 in stock sales. "I take no pleasure in sentencing you ... but my job is to follow the law," U.S. District Judge Sim Lake said in meting out punishment from a formulaic federal sentencing grid. Nearby, Olis' wife held a baby daughter who could be out of college before her dad gets out of prison.

Olis' sentence was based on his total of 40 "offense level" points: 6 for fraud, 26 for causing $100 million in investor losses, 4 for harming 50 or more people, 2 for being a "sophisticated" executive and 2 for being a certified public accountant.

Bubble-era white-collar crooks, beware: Even crimes committed before the new guidelines took effect can be "pulled forward" for sentencing purposes if prosecutors prove a perp obstructed justice or committed another related offense later on. It's not just the Bernie Ebbers of the world who need fret either. Anyone nailed for causing more than $1 million in losses to investors faces a decade or more in prison.

There's a lot of imagination in calculating losses from a misdeed. Dynegy was a sick company in any event, as lenders fled energy traders and suits started flying over the California power scandal. But under the guidelines, an accountant who puffs up earnings can be blamed for the whole collapse.

As the law now stands, someone who artificially pumps up a stock with 100 million shares outstanding, and whose price subsequently falls $8 below where it was when the scam started, is treated as if he personally stole $800 million.

A judge can depart from the sentencing guidelines if he's willing to send a report on the matter to Capitol Hill. Judge Lake declined to take this step.

It would take over **25 miles** to show how many years, per million, he is serving.

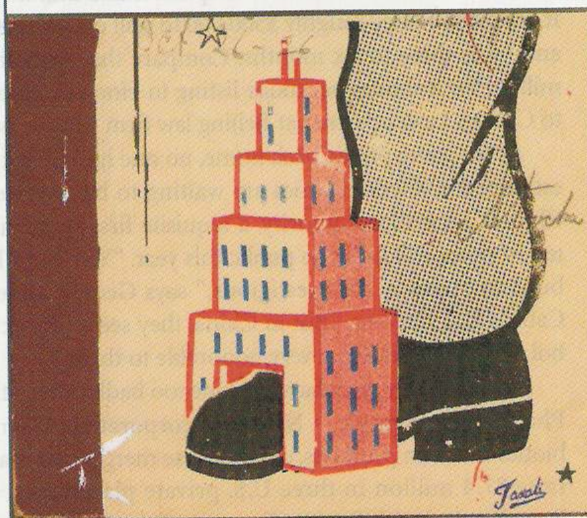
It's scary stuff, enough to coerce folks under suspicion to cop a plea. That's exactly what Olis' colleagues did, including his boss, and they're getting no more than five years. Demand a day in court, or just be a chief executive with no one higher up to snitch on, and you risk rotting away. **F**

FROM LEFT TO RIGHT: DAVID CANTOR / AP WIDE WORLD; NICK UT / AP WIDE WORLD; CHRIS HONDROS / GETTY; KEITH BEDFORD / GETTY; ASHLEY FLEMING / BLOOMBERG NEWS; SHAWN BALDWIN / AP WIDE WORLD; DAVID J. PHILLIP / AP WIDE WORLD; LAWRENCE SCHWARTZWALD / POLARIS; LOUIS LANZANO / AP WIDE WORLD; CUFFS: THOM LANG / CORBIS; ILLUSTRATION BY GARY TAXALI FOR FORBES

Through The Back Door

A growing number of Chinese companies are taking a shortcut to public listings in the U.S.

BY LUISA KROLL



TINY CHINA CABLE & COMMUNICATION HAD expansionist ideas. With zero revenues and iffy assets—49% of a $3.5 million (sales) cable venture that controls 39 channels in a region 85 miles south of Beijing—the company hadn't a prayer of going public, even in China. Not to worry: It now trades on the Nasdaq bulletin board, thanks to an old tactic of penny-stock operators—the reverse merger.

Here's how it worked. Because of China's laws and rulings on offshore listings, it first set up a vehicle in the British Virgin Islands called Solar Touch, which then turned the original company into a subsidiary. Next it found a shell into which it could merge: Nova International Films, a Vancouver, Wash. film production outfit with no operational history in a decade but with an over-the-counter listing. The marriage was consummated in March 2003, in an all-stock deal. Last September, with the legitimacy (such as it was) conferred by its public-company status, CCCI raised $4 million in private financing from U.S. investors.

While no one tracks reverse mergers, a half-dozen companies from the Middle Kingdom—ranging from health care products to manufacturers of power-steering assemblies *(see table, p. 44)*—have completed them since last year. At least a dozen are

"You and I know the bulletin board is not prestigious. But in China, they see a U.S. ticker symbol, which is something very honorable to them."

in the pipeline this year, says Halter Financial Group, an Argyle, Tex. consultancy that specializes in the transaction.

The attractions of this maneuver are clear: respect back home, access to capital here and the relative ease of reverse mergers in the States. "Wall Street is every entrepreneur's dream," says Kit Tsui, chief executive of Shenzhen-based Industries International, a maker of telephones and lithium batteries. It costs a company roughly $500,000 to pull off a reverse merger and takes three to six months. Compare that with about $2.5 million for a similar backdoor listing in Hong Kong, according to Charles Law, a partner at Beijing law firm King & Wood.

As for going public back home, no one has the patience. An estimated 1,000 companies are waiting to be reviewed by the Chinese Securities Authority, a requisite first step; only one in ten of those will likely go public this year. "You and I know the bulletin board is not prestigious," says George Raney, China Cable's U.S. director. "But in China, they see a U.S. ticker symbol, which is something very honorable to them."

Astonishingly, they haven't done too badly here, either. AXM Pharma, for example, a Nevada-incorporated maker of antibiotics and skin products, did a reverse merger and managed to raise $7.4 million in three U.S. private placements, signed a licensing deal with Sunkist Growers to use its name in making vitamins in China and moved its listing from the bulletin board to the American Stock Exchange. Its shares have quadrupled since March 2003 to a recent $5.

But then there are tales of companies like CTC Cosmetics Holdings, which did a reverse merger in 1997. Three years later its largest shareholder, Voyager Group, notified the SEC that CTC, which had been delisted from the bulletin board, had failed to provide current financial information and that it had removed its Chinese directors. Soon after, Voyager itself was embroiled in a scandal, when two of its directors were arrested and charged with securities fraud on another stock (charges against one were dropped). There is no trace of the Chinese company today.

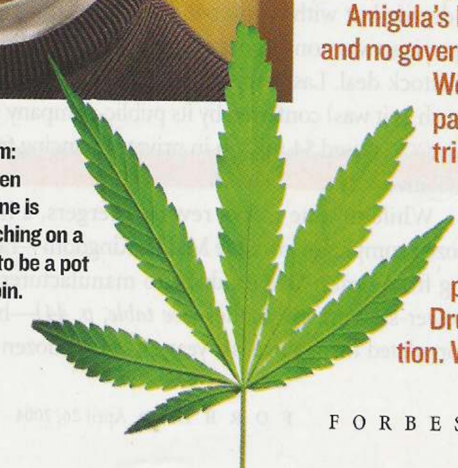
Will that curb enthusiasm for other issues? That's a tough call. As they say in the old country, there's a *sha gua* born every minute. ■

Red Hot

Reverse mergers have been good to these Chinese companies—and to their investors—so far. How long their share prices can keep soaring is anybody's guess.

Company	Sales ($mil)	Postmerger stock performance
AXM Pharma	$10	413%
China Automotive Systems	48E	22,150
China Cable	NA	207
Industries International	59	1,375
Tiens Biotech Group	39E	23,900

Performance as of Apr. 2. E: Estimate. NA: Not available. *Sources: J.M. Dutton & Associates; company reports.*



Pipe dream: Warren Eugene is munching on a plan to be a pot kingpin.

MICHAEL A. NEMETH; THE HERALD SUN / AP WIDE WORLD

JOINT VENTURE

Warren Eugene says he has made millions through an Internet gambling site he founded in 1995. His next play is to be a marijuana kingpin—through a publicly traded company.

Eugene recently did a reverse takeover of a tiny U.S. public company, renamed it Amigula, and now proposes to supply marijuana to sick people in Canada. Canadian law allows sick people to legally smoke the drug, but it prohibits companies from selling it. Not that that detail seems to bother Eugene.

"There are many investors out there who will take a gamble, figure I'll pull a monkey out of my hat again," says Eugene, 43, a Canadian native with a Bahamian passport.

Amigula's headquarters are a hotel suite in Toronto. The company has zero revenues and no government licenses to supply marijuana, despite claims on Yahoo and Bloomberg Web sites to the contrary. Eugene figures he will sign up 60,000 medical patients, change Canadian law, learn to grow top-grade pot, sell to many countries and corner a market now occupied by one agricultural company and scores of furtive growers.

Even weed-legalization fans think he is smoking something (the entrepreneur says he never touches the stuff) and have reported the company to the securities cops. Antidrug congressmen have asked the Food & Drug Administration to check it out. The SEC won't comment on any investigation. Wonder how long this high will last.

—Quentin Hardy