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Representing the White-collar Client at Sentencing

Prior to the Sentencing Reform Act of 1984, which brought us the United States Sentencing Commission and the Sentencing Guidelines, defendants convicted of white-collar crimes—tax evasion, fraud, antitrust offenses, insider trading, and embezzlement—could often expect to receive sentences of probation. The Sentencing Commission saw this as a "problem," which it "solved" with "guidelines that classify as serious many offenses for which probation previously was frequently given and provide for at least a short period of imprisonment in such cases." (U.S.S.G. ch. 1, pt. A § 4(d).) Because so many white-collar defendants are now looking at serious time, the challenge to the criminal defense attorney in these cases is clear—find a way to lower the offense level, and then look for mitigating factors that would permit the court to depart downward even further.

Lowering the offense level

Because the guidelines for economic crimes are driven by monetary factors, the first challenge is to ensure that those figures are accurately calculated. For example, defense counsel must first make sure that the figure proposed by the Presentence Investigation Report does not count the same money twice. The guidelines recognize that:

> In certain cases, an offense may involve a series of transactions without a corresponding increase in loss. For example, a defendant may embezzle $5,000 from a bank and conceal this embezzlement by shifting this amount from one account to another in a series of nine transactions over a six-month period. In this example, the loss is $5,000 (the amount taken), not $45,000 (the sum of the nine transactions), because the additional transactions did not increase the actual or potential loss.

(U.S.S.G. § 2B1.1, Appl. Note 2.)

Loss in embezzlement cases also "does not include the interest that could have been earned had the funds not been stolen." (U.S.S.G. § 2B1.1, Appl. Note 2.) A similar rule applies in fraud cases. (*See* U.S.S.G. § 2F1.1, Appl. Note 8.) (*But cf. United States v. Nolan*, 136 F.3d 265 (2d Cir. 1998) (interest included in loss calculation where money embezzled included both principal and agreed-upon interest).)

Although fraud and embezzlement victims may both lose money, the Guidelines recognize that in some cases, fraud victims *do* receive something of value for their money. For example:

> A fraud may involve the misrepresentation of the value of an item that does have some value (in contrast to an item that is worthless). Where, for example, a defendant fraudulently represents that stock is worth $40,000 and the stock is worth only $10,000, the loss is the amount by which the stock was overvalued (i.e., $30,000). In a case involving a misrepresentation concerning the quality of a consumer product, the loss is the difference between the amount paid by the victim for the product and the amount for which the victim could resell the product received.

(U.S.S.G. § 2F1.1, Appl. Note 8(a).)

Application of this principle can sometimes have dramatic results. In *United States v. Chatterji*, 46 F.3d 1336 (4th Cir. 1995), for example, the Fourth Circuit found the victims suffered no loss at all. In that case a generic pharmaceutical company fraudulently obtained permission from the Food and Drug Administration to market its products. Although the sentencing court measured the loss to victims by the money received by the company for the products it did not have permission to sell, the court of appeals reversed. Even though the company did not have permission to sell its products, the court found that defrauded customers suffered no loss, because the products they purchased were in

Some fraud victims receive value for lost money.

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fact safe and effective. (*See* also *United States v. Fiorillo*, 186 F.3d 1136 (9th Cir. 1999) (per curiam) (loss does not include price paid by victim for disposal of hazardous waste that defendant properly handled); *United States v. Sublett*, 124 F.3d 693 (5th Cir. 1997) (loss does not include value of counseling provided by qualified counselors); *United States v. Parsons*, 109 F.3d 1002 (4th Cir. 1997) (legitimate expense reimbursement requests not included in loss); *United States v. Maurello*, 76 F.3d 1304 (3d Cir. 1996) (loss in case of disbarred attorney providing legal services does not include fees paid by satisfied clients); *United States v. Alburg*, 818 F. Supp. 1306 (N.D. Cal. 1993) (loss reduced by value of work performed).)

Losses not caused by fraud should not impact sentence.

Just as there are fraud cases in which victims receive something of value, there are also fraud cases in which defendants have no intent to cause financial loss to anyone. For example, a defendant may lie about his or her debts to obtain a loan that he or she fully intends to repay. If the defendant then defaults after repaying a portion of the debt, the loss under section 2F1.1 is *necessarily* the loss the victims actually sustain, since there is no intended loss. This is significant, because the guidelines provide that if the loss a defendant *intends* to inflict is greater than the loss the victims actually sustain, the sentencing court is to consider the intended loss in setting the offense level. (U.S.S.G. § 2F1.1, Appl. Note 8.) If a defendant who intends no loss had pledged assets to secure the debt, then the loss would be reduced by the value of those assets. (U.S.S.G. § 2F1.1, Appl. Note 8(b).) (*See United States v. Henderson*, 19 F.3d 917, 927–28 (5th Cir. 1994) (applying this principle); *United States v. Kopp*, 951 F.2d 521 (3d Cir. 1991) (same); *United States v. Wells*, 127 F.3d 739 (8th Cir. 1997) (loss reduced by value of future payments to bank on leases assigned as collateral); *United States v. Downs*, 123 F.3d 637 (7th Cir. 1997) (loss reduced by value of assets pledged).)

Where defendants *intend* loss, the intended loss is used if it is greater than the actual loss. (U.S.S.G. § 2F1.1, Appl. Note 8.) Courts have differed on how to apply this principle in Ponzi schemes, where defendants do not *intend* for *all* victims to lose money. In a Ponzi scheme, the defendant deceives the victims into "investing" money, which the defendant steals, rather than invests. Defendants in such cases will often use "investments" by later victims to pay "profits" to earlier ones. This practice helps keep the scheme going by making it appear that the "investments" are producing significant returns for investors. In *United States v. Holuisa*, 13 F.3d 1043 (7th Cir. 1994), the court of appeals reduced loss by the money returned to investors as part of the scheme, because the defendant never intended that money to be part of the loss. Other courts have refused to reduce the loss in such schemes by the money returned to victims as part of the scheme. (*See United States v. Loayza*, 107 F.3d 257 (4th Cir. 1997) (money returned to victims as part of Ponzi scheme not deducted from loss); *United States v. Carrozzella*, 105 F.3d 796 (2d Cir. 1997) (same); *United States v. Dobish*, 102 F.3d 760 (6th Cir. 1996) (same).)

Defense counsel in fraud cases also need to ensure that losses that were not caused by the fraud do not affect the guideline offense level. For example, in *United States v. Randall*, 157 F.3d 328 (5th Cir. 1998), a bankruptcy fraud case, Housing and Urban Development and the Veterans Administration lost money when they foreclosed on properties whose mortgages they insured. Although the district court included these losses in the guideline calculus, the court of appeals reversed, because they were not caused by the defendant's fraud (i.e., her lying about her name, Social Security number, and prior bankruptcies). The court found that the agencies would have incurred the same losses even without the bankruptcy fraud. (*See also United States v. Daddona*, 34 F.3d 163 (3d Cir. 1994) (where defendant, a registered agent of Employers Insurance of Wausau, did not purchase construction bond as promised, loss was not cost of completing failed project, since fraud did not cause project to fail; loss was money insurance company was required to pay); *United States v. Marlatt*, 24 F.3d 1005 (7th Cir. 1994) (where defendant misrepresented that he had clear title to condominiums, loss was cost to clear title, not unrelated reduction in value of condominiums); *United States v. Stanley*, 12 F.3d 17 (2d Cir. 1993) (although defendant used fraudulent mailing to induce purchases of overpriced bonds, people who did not receive the mailing also bought bonds; court excluded losses incurred by the latter group from guideline calculation).)

In general, only losses to victims that are directly caused by fraud are included in loss. Consequential damages, such as "interest that could have been earned on such funds had the offense not occurred," U.S.S.G. § 2F1.1, Appl. Note 8, are not included. (*See United States v. Izydore*, 167 F.3d 213, 223 (5th Cir. 1999)

(explaining this principle).) In *Izydore*, the court of appeals held that a $210,158 bankruptcy trustee's fee should not have been included in loss, because, although it was a consequence of the defendant's fraud, it was not money "taken" by the defendant. (*See also United States v. Sablan*, 92 F.3d 865 (9th Cir. 1996) (value of bank employee's time spent meeting with FBI and each other to discuss offense is consequential loss not included in guideline calculation).

A similar principle applies in tax cases, where "tax loss does not include interest or penalties." (U.S.S.G. § 2T1.1, Appl. Note 1.) (*See United States v. Hopper*, 177 F.3d 824, 832 (9th Cir. 1999) (applying this principle); *United States v. Pollen*, 978 F.2d 78, 91 n.29 (3d Cir. 1992) (criticizing, but applying rule in evasion of collection case).)

The Guidelines handle price-fixing cases somewhat differently. The offense level in such cases is not controlled by "loss," but by "volume of commerce," i.e., sales made as part of the price-fixing scheme. Significantly, the Guidelines limit the application of relevant conduct in price-fixing cases, by providing that:

> For purposes of this guideline, the volume of commerce attributable to an individual participant in a conspiracy is the volume of commerce done by him or his principal in goods or services that were affected by the violation.

(U.S.S.G. § 2R1.1(b)(2).)

This limitation of the "relevant conduct" principle of U.S.S.G. § 1B1.3 is important, since without it, a defendant would also be responsible for the volume of commerce attributable to other companies involved in the price-fixing (so long as they were "reasonably foreseeable [and] in furtherance of the jointly undertaken criminal activity," and met the other criteria of U.S.S.G. § 1B1.3. (*See United States v. Heffernan*, 43 F.3d 1144, 1147 (7th Cir. 1994) (applying this principle).)

A more contentious question in price-fixing cases is whether all sales during the period of price-fixing are included in the "volume of commerce." The Sixth Circuit has held that they are, regardless of whether the sales were at or below the fixed price. (*United States v. Hayter Oil Co.*, 51 F.3d 1265 (6th Cir. 1995). Although *Hayter Oil* has been criticized, *see* Henry D. Fincher, *Fining the Market: The Bumbling Price-Fixer and the Antitrust Guideline*, 8 FED. SENT. REP. 244 (1996), at least one other court has followed the Sixth Circuit's lead. (*See, e.g., United States v. Andreas*, 1999 WL 51806 (N.D. Ill, Jan. 27, 1999). Recently, however, the Second Circuit broke ranks with the Sixth Circuit, holding in *United States v. SKW Metals & Alloys, Inc.*, __F.3d __, 1999 WL 977044 (2d Cir. Oct. 28, 1999), that the government must prove that sales were in some way "affected" by the price-fixing scheme before they may be included in the volume of commerce. The court of appeals nevertheless granted the government's appeal and remanded for resentencing, because the district court had excluded *all* sales below the fixed price. (*See United States v. SKW Metals & Alloys, Inc.*, 4 F. Supp. 2d 166 (W.D.N.Y. 1997).) The court of appeals disapproved of this finding, reasoning that some sales below the fixed price could nevertheless have been "affected" by the scheme.

Departures

Although courts have departed downward in white-collar cases for the same "offender-related" reasons they depart downward in other cases, other mitigating "offense-related" circumstances are unique to white-collar offenses. For examples of "offender-related" departures, *see* Alan Ellis, *Let Judges Be Judges! Downward Departures After* Koon 12 CRIM. JUSTICE 4, 49–51 (Winter 1998); *Part 2: Post-Offense Rehabilitation,* 13 CRIM. JUSTICE 1, 51–63 (Spring 1998); *Part 3: Aberrant Behavior*, 13 CRIM. JUSTICE 2, 56–58 (Summer 1998); *Part 4: Civic, Charitable, or Public Service*, 13 CRIM. JUSTICE 3, 39–40 (Fall 1998); *Part 5: Combination of Factors*, 13 CRIM. JUSTICE 4, 55–56 (Winter 1999); *Part 6: Substantial Assistance*, 14 CRIM. JUSTICE 1, 53–57 (Spring 1999); *Part 7: Family Ties and Responsibilities*, 14 CRIM. JUSTICE 2, 48–52 (Summer 1999); *see also* ALAN ELLIS, *Answering the "Why" Question: The Powerful Departure Grounds of Diminished Capacity, Aberrant Behavior, and Post-Offense Rehabilitation*, FERDERAL SENTENCING REPORTER (May/June 1999).

Money-laundering guidelines provide a chance to depart.

The history of the Sentencing Commission's formulation of the money laundering guidelines provides important opportunities for departures for white-collar defendants. When the Commission formulated the guidelines for money laundering offenses, shortly after the money laundering statutes were enacted in 1986, it set the offense levels high, "to penalize the conduct about which Congress seemed most concerned when it enacted the money laundering statutes, namely . . . situations in which 'laundered' funds derived from serious underlying criminal conduct such as a significant drug trafficking operation or organized crime." (*Report to the Congress: Sentencing Policy*

for Money Laundering Offenses, Including Comments on Department of Justice Report, UNITED STATES SENTENCING COMMISSION (Sept. 18, 1997), at 4.) However, it has become apparent that the high offense levels provided by the Guidelines were even more severe than the Commission had intended for white-collar offenses. In 1995 the Commission proposed to revise the money laundering guidelines to make the base offense level correlate more closely with the offense level applicable to the underlying conduct that was the source of the illegal proceeds. (*See also* David Yellen, *Highlights of the 1995 Amendments*, FEDERAL SENTENCING GUIDELINES MANUAL xii (West 1995).) Unfortunately, Congress rejected these amendments. Pub. L. No. 104–38, 1, 109 Stat. 334 (Oct. 30, 1995).

Because the Sentencing Commission obviously did not consider the appropriateness of high offense levels required by the money laundering guidelines where the money laundering was simply incidental to underlying frauds or other white-collar crime, many courts have granted departures in such cases, using the offense level for the underlying conduct as a guide. (*See United States v. Hemmingson*, 157 F.3d 347 (5th Cir. 1998) (approving departure where money laundering incidental to Federal Election Campaign Act violation); *United States v. Threadgill*, 172 F.3d 357 (5th Cir.) (fact that defendants' money laundering activities were incidental to their gambling operation was permissible basis for departure), *cert. denied*, 120 S. Ct. 172 (1999); *United States v. Woods*, 159 F.3d 1132 (8th Cir. 1998) (affirming departure where underlying offense was bankruptcy fraud, not drug trafficking or some other offense typical of organized crime); *United States v. Skinner*, 946 F.2d 176, 179–80 (2d Cir. 1991) (money laundering de minimis, because the transactions in reality represented only the completion of the underlying criminal transaction); *United States v. Gamez*, 1 F. Supp. 2d 176 (E.D.N.Y. 1998) (departure based on small amount of proceeds laundered and resemblance of offense conduct to typical structuring offense); *United States v. Caba*, 911 F. Supp. 630 (E.D.N.Y. 1996) (granting downward departure toward guidelines for food stamp fraud where the money laundering convictions produced unjust inflation of offense level), *aff'd*, 104 F.3d 354 (2d Cir. 1996) (table).)

Other departures are unique to fraud cases.

Not all circuits have accepted this approach. (*See United States v. Ripinsky*, 109 F.3d 1436 (9th Cir. 1997) (reducing disparity between fraud guideline and money laundering guideline no basis to depart); *United States v. Adams*, 74 F.3d 1093 (11th Cir. 1996) (disapproving departure in money laundering case where money laundering was incidental to fraud). Some cases disapproving departure on this basis may be distinguished because they were handed down prior to the Supreme Court's landmark decision in *Koon v. United States*, 518 U.S. 81 (1996), which gave sentencing courts great discretion in granting departure. (*See, e.g., United States v. LeBlanc*, 24 F.3d 340 (1st Cir. 1994).) Others may be distinguished because they involve underlying offenses that are arguably related to organized crime. *See, e.g. United States v. Ford*, 184 F.3d 566 (6th Cir. 1999) (gambling).)

The Third Circuit has taken a unique approach to this issue. In a case in which the district court recognized its power to depart, but refused (a decision that is unreviewable on appeal), the court of appeals held that the district court's use of the money laundering guideline itself was a misapplication of the Guidelines. The court held that since the money laundering was incidental to the underlying fraud, the district court should have applied the fraud guideline. (*United States v. Smith*, 186 F.3d 290 (3d Cir. 1999).)

At least one court has granted a downward departure in a money laundering case from level 23 (required by section 2S1.1(a)(1) where the money laundering promotes the underlying offense) to level 20 (required by section 2S1.1(a)(2) in all other cases). Since the defendant in *United States v. Bifield*, 42 F. Supp. 2d 477 (M.D. Pa. 1999), was convicted of conspiring to launder money to promote the underlying criminal activity, as well as to conceal it, the court concluded that section 2S1.1(a)(1) (base offense level 23) applied. The court nevertheless departed downward to level 20 pursuant to section 2S1.1(a)(2), because the promotion goal was minor in that conspiracy—and therefore outside the heartland of typical section 2S1.1(a)(1) cases.

Other departures are unique to fraud cases. The fraud guideline suggests the appropriateness of a downward departure where loss is caused by factors unrelated to the offense. (U.S.S.G. § 2F1.1, Appl. Note 8(b).) The application note gives the example of a defendant who understates his debts to obtain a loan to expand his grain export business, and then defaults when the bottom falls out of the market. (*See, e.g., United States v. Gregorio*, 956 F.2d 341 (1st Cir. 1992) (downward departure

(Continued on page 58)

(Continued from page 44)

appropriate where degree of loss was caused by downturn in economy). The guideline also suggests the appropriateness of a downward departure where the "loss determined under subsection (b)(1) may overstate the seriousness of the offense." (U.S.S.G. § 2F1.1, Appl. Note 11.) (*See, e.g., United States v. Graham*, 146 F.3d 6 (1st Cir. 1998) (loss overstates culpability where lower loss attributed to similarly situated defendants); *United States v. Monaco*, 23 F.3d 793 (3d Cir. 1994) (loss overstates seriousness where defendant had no intent to steal); *United States v. Stuart*, 22 F.3d 76 (3d Cir. 1994) (affirming loss calculation based on face value of stolen bonds, but suggesting appropriateness of departure on remand where defendant received little money for participation in offense, causing loss to overstate seriousness of offense).

Downward departures have also been granted where:

- The defendant did not profit personally from the fraud. (*See, e.g., United States v. Broderson*, 67 F.3d 452 (2d Cir. 1995).)
- The defendant had a good faith belief that his conduct was lawful. (*See, e.g., United States v. Jasin*, 25 F. Supp. 2d 551 (E.D. Pa. 1998), *aff'd*, 191 F.3d 446 (3d Cir. 1999) (table).)
- The defendant's business would fold and his or her innocent employees suffer if he were imprisoned. (*See, e.g., United States v. Olberes*, 99 F.3d 28 (1st Cir. 1996); *United States v. Milikowsky*, 65 F.3d 4 (2d Cir. 1995); *United States v. Somerstein*, 20 F. Supp. 2d 454 (E.D.N.Y. 1998). *But see United States v. Crouse*, 145 F.3d 786 (6th Cir. 1998) (rejecting departure); *United States v. Morken*, 133 F.3d 628 (8th Cir. 1998) (same); *United States v. Rutana*, 18 F.3d 363 (6th Cir 1991) (same), *cert. denied*, 502 U.S. 907 (1991); *United States v. Reilly*, 33 F.3d 1396 (3d Cir. 1994) (same).)
- It was improbable that the scheme would succeed. (*United States v. Stockheimer*, 157 F.3d 1082 (7th Cir. 1998) (victims paid $500 for a pad of blank certified money orders that the defendant said could be presented to creditors to pay off debts. The debtors attempted to pay off $80 million in debt, which the district court held as the loss, even though no creditors fell for the transparently bogus scheme. Court of appeals reversed to allow district court to consider departure); *United States v. Ensminger*, 174 F.3d 1143 (10th Cir. 1999) (rejecting loss enhancement where fraud had no possibility of success).)

In a wage tax withholding case, the First Circuit acknowledged that the district court could depart downward based on the defendant's intent to pay the withholding tax once his business became stable, but remanded for resentencing and for the district court to consider the concerns of the court of appeals with respect to the extent of the lower court's previous departure. (*United States v. Brennick*, 134 F.3d 10 (1st Cir. 1998).) The court also held that unlike in fraud cases, multiple causes for the extent of loss in a tax case is not a basis for departure. In a tax evasion case, the Third Circuit has approved a departure based on prosecutorial manipulation of the indictment where the tax evasion was incidental to the underlying embezzlement case and the sentencing court found that in such a case it was unusual for the government to charge tax evasion in addition to embezzlement. (*United States v. Lieberman*, 971 F.2d 989 (3d Cir. 1992).)

The guidelines for white-collar crime are harsh, but solid investigation, creative thinking, and persuasive advocacy can often be combined to protect our clients from overly severe and excessive punishment. Indeed, an out-of-the-heartland atypical case can be fertile territory—particularly when coupled with an offender-based departure for an appropriately mitigated sentence. ■