Day One—Revising the Definition of Loss

Group Breakout Session Four

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Assistant Facilitators: **Professor Michael Goldsmith**, *J.P. Reuben Clark School of Law, Brigham Young University, and Former U.S. Sentencing Commissioner*

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LOSS BREAKOUT SESSION — GROUP FOUR SUMMARY

Main Topic: "Is 'loss' a gross or net concept, and if net, what crediting rules should be adopted?"

Secondary Topics: (1) "Particular crediting problems in investment schemes, particularly 'Ponzi' schemes" and (2) "items of *de minimus* value to the victim."

Professor Michael Goldsmith of Brigham Young University, a former U.S. sentencing commissioner, presented an overview of the field test conducted in 1998 and a history of the economic crime package. The concept of loss in the fraud guideline as a net or gross concept was introduced. One panelist made the argument that the current application notes argue for loss being a gross concept and that only certain types of fraud (fraudulent loan application and product substitution cases) require the use of a net loss concept. Although the guidelines are not clear, he noted that caselaw expands the limited net loss rule to a general rule for section 2F1.1. As an example, he offered the *Haddock* case in the Tenth Circuit.

Jonathan Rusch, special counsel for fraud prevention at DOJ, offered that application note 8 illustrates the fundamental tension between intended loss and actual loss in guideline 2F1.1. He indicated that the net loss concept was best illustrated by the intended loss concept introduced in application note 8; however, in his opinion, loss should be a gross concept. He also questioned the necessity for a net loss concept in fraudulent loan application and product substitution cases because it may seriously underrepresent the harm that resulted.

Mark Flanagan, a partner at McKenna & Cuneo, noted that net loss is necessary because it is a better measure of culpability than is a gross loss figure. Gross loss too often overstates the severity of the offense and the defendant's culpability, especially when it is clear from the defendant's actions (*e.g.*, repayment of embezzled funds) that he did not intend to commit the larger crime.

Some participants expressed concern that loss as a net concept is problematic for a couple of reasons: (a) determining intent at the sentencing phase is often difficult and burdensome on the court; and (b) there is not an objective standard for determining intended loss. For these reasons, in the view expressed by some, great disparity occurs with regard to the determination of intended loss. For example, in a fraudulent loan application case in which the defendant has been caught after making three years of payments, the defendant's loss will most likely be credited with the principal portion of the payments he made during those three years. If the same defendant was caught after making only one year of payments, his loss amount would be higher even though the intent may have been the same. However, the loss determination seems to indicate that these offenders are different and deserving of different penalties. The group indicated that in many cases, the determination of loss implies a degree of precision that is artificial. In this example, when the offense is discovered may have a large impact on the sentencing outcome. In a sentencing scheme that seeks to eliminate unwarranted disparity, the use of subjective standards (such as that used to determine intended loss) seems contrary to the overall goal.

The group also discussed efforts to reduce disparity, such as crafting additional rules (*e.g.*, credits, the inclusion of interest in loss calculations). They agreed that in many cases, additional attempts at refinement further complicate the guidelines which also results in disparity. In some cases, the disparity that results from complex guidelines, may be as bad or worse than the disparity involved in allowing courts to use their own discretion.

Some participants preferred a general rule regarding loss that would give the court guidance but allow for discretion in applying the rule to individual cases. Because there are so many variations of fraud offenses, in that view, it is easier for the courts to interpret a general rule and apply it to the facts in front of them. They opposed creating a general rule that has numerous exceptions because it complicates application. They felt strongly that the guidelines cannot address every possible permutation of facts. By adding numerous exceptions to a general rule, it makes it more difficult for the courts to interpret the general rule and apply it to individual cases.

There were several other issues that the group briefly discussed:

(a) Plea Practices—Some participants expressed concern that they were seeing plea agreements that did not accurately reflect the facts of the case. One judge opined that he sees a great reluctance on the part of judges and attorneys to punish white collar offenders.

(b) Role in the Offense—Some participants wanted to see the organizers of schemes punished more harshly. They did not believe that there was enough of a distinction between the organizers/leaders and the lower-level defendants in fraud schemes.

(c) Ponzi Schemes—Although the group agreed that a true net loss figure would underrepresent a defendant's culpability, they were split on whether a gross loss figure or "loss to losing investors" was more appropriate. Some were concerned that the losing-investors concept implies that the only victims of the offense are those that actually lost money, when in reality, all investors are victims regardless of whether their money is returned. Some thought a gross loss concept more adequately reflected the seriousness of the offense. The group agreed that even a specific rule regarding Ponzi schemes may be inadequate to address all of the issues. Therefore, some departure provisions may be necessary.