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UNITED STATES SENTENCING COMMISSION

Loss Issues

Working Paper

October 14, 1997

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LOSS ISSUES - WORKING PAPER

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I. Introduction

This memorandum discusses issues raised about the definition of loss in the case law, in training, and on the helpline, and presents some general options to address those issues to achieve greater sentencing uniformity and predictability. It is not intended as a comprehensive compilation of all case law addressing these issues. The memorandum also incorporates the input received to date on these issues from Frank Bowman, the Criminal Law Committee, the Department of Justice, the Practitioners' Advisory Group, and the Probation Officers' Advisory Group. Except for the input from the Department, the referenced input is the formal submission of each individual or group in connection with the public hearing on loss (page numbers reference those submissions). The Department's input on loss was in the Department's annual report to the Commission on the Sentencing Reform Act (Letter from Commissioner Mary Harkenrider to Chairman Conaboy, December 3, 1996).

The following issue areas are discussed in this memorandum:

A. Actual Loss

1. Causation
2. Consequential Damages
3. Interest
4. Value Received - Credits Against Loss
5. Diversion of Government Benefits

B. Alternatives to Actual Loss

1. Intended Loss
    a. Gain
    b. Risk of Loss

C. Miscellaneous

II. Issues for Possible Amendments

A. Actual Loss

1. Causation

Current rule: There is no explicit standard of causation in the definition of loss. The relevant conduct guideline provides that relevant conduct includes "all harm that resulted from the acts and omissions specified in subsections (1)(A) and (1)(B) above that were part of the same course of conduct or common scheme or plan as the offense of conviction." §1B1.3(a)(3).

Issue: Should the Commission adopt an explicit causation standard, address multiple causation situations, or add commentary language allowing departures when substantial unforeseen losses occur?

Impetus: The guidelines have three arguably distinct and inconsistent standards for loss causation. First, the Relevant Conduct rule in §1B1.3 holds a defendant responsible for all losses, foreseen or unforeseen, that result from the defendant's actions or the foreseeable actions of his or her associates. *See, e.g., United States v. Sarno*, 73 F.3d 1470, 1500 (9th Cir. 1995) ("A sentence calculated pursuant to the loss tables . . . is properly based on actual loss notwithstanding the fact that this loss may be greater than the intended, expected, or foreseeable."); *United States v. Catalfo*, 64 F.3d 1070, 1082-83 (7th Cir. 1995) (holding defendant accountable for loss caused by acts of co-conspirator), *cert. denied*, 116 S. Ct. 1683 (1996). Second, §2F1.1's commentary limits the loss amount to "the value of the money, property, or services unlawfully taken." *See United States v. Marlatt*, 24 F.3d 1005, 1007-08 (7th Cir. 1994) (refusing to count foreseeable losses in loss figure because they did not represent "the thing actually taken"); *see also United States v. Wilson*, 993 F.2d 214, 217 ("The phrase 'property taken, damaged or destroyed' [from §2B1.1] does not allow for inclusion of incidental or consequential injury. . . ."). Finally, the commentary's explicit inclusion of "consequential damages" in the loss figure for contract procurement and product substitution cases implies that only "non-consequential" or "direct" damages are included in other cases. *See, e.g., United States v. Thomas*, 62 F.3d 1332, 1346-47 (11th Cir. 1995), *cert. denied*, 116 S. Ct. 1058 (1996).

Case law:

Although there is no explicit requirement of causation in the definition of "loss", the relevant conduct guideline provides that relevant conduct includes "all harm that resulted from the acts and omission specified in subsections 1(a) and 1(b) above, and all harm that was the object of such acts and omissions." §1B1.3(a)(3). This requirement that relevant harm "result from" the defendant's criminal conduct would seem to imply that the defendant's offense behavior must be a cause of all harm which becomes part of the loss calculation. The question which emerges is whether the defendant should be held accountable where events beyond his control greatly magnify the harm caused.

An illustration of this question is provided by *United States v. Neadle*, 72 F.3d 1104 (3d Cir. 1996). Neadle was convicted of one count of mail fraud in connection with his misrepresentation that he had the necessary assets, $700,000 in unencumbered initial working capital, to justify the issuance to him of a license to write property and casualty insurance in the Virgin Islands. While the $700,000 asset which Neadle offered for this purpose was encumbered, he subsequently purchased $4,000,000 in reinsurance to cover his clients. Insurance regulations in the Virgin Islands did not require the purchase of any reinsurance.

About 20 months after Neadle's company received its insurance license Hurricane Hugo devastated the Virgin Islands. Neadle's company was able to pay more than $4,000,000 to its clients who sustained damage from Hurricane Hugo. However, because of the scope of the damage caused by Hugo, Neadle's assets were exhausted before claims in excess of an additional $20,000,000 could be paid.

The majority affirmed the district court's conclusion that this $20,000,000 shortfall was caused by Needle's criminal conduct and was the proper measure of loss on which to base Neadle's offense level.[1] The dissent reasoned that Neadle's criminal conduct did not cause these catastrophic losses and, as such, Neadle should not be held responsible for the entire amount of the shortfall. The dissent did not see Neadle's conduct as a "cause in fact" of the shortfall and would have held Neadle responsible only for the $700,000 which he had misrepresented as unencumbered assets.[2]

In grappling with the question of how much restitution the defendant should pay in a bank bribery case, the First Circuit has articulated a "modified but for" standard of causation. *United States v. Vaknin*, 112 F.3d 1579 (1st Cir. 1997). In that case the First Circuit declined to hold the defendant accountable, for restitution purposes, for amounts which were attributable more to a drop in the value of the collateral which secured the fraudulently obtained loans than to the defendant's conduct. The First Circuit stated:

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[1]To date, *Neadle* has not been followed by any other jurisdiction or cited in subsequent Third Circuit Cases.

[2]Even if the fraud guideline contained a "cause in fact" requirement for any damages to be included as loss, the result in Neadle would have been the same. It is unclear whether the majority would have seen $20,000,000 as the loss here if a more stringent, "proximate cause" standard existed.

> ... the government must show not only that a particular loss would not have occurred but for the conduct underlying the offense of conviction, but also that the causal nexus between the conduct and the loss is not too attenuated (factually or temporally). The watchword is reasonableness.

Vaknin, at 590.[3]

Thus, at least for restitution calculations, the First Circuit requires not only that the defendant's conduct be a cause of the harm for which restitution is sought, but also that the defendant's conduct be reasonably closely linked to any damages which result.

Helpline Report:

No specific Helpline calls explicitly on causation. However, a few calls have been received on the issue of direct versus indirect victims. Callers are confused about whether or not losses to indirect victims should be included.

Options:

(1) Make no amendment dealing with causation.

(2) Do not provide a new causation standard, but add commentary language to the definition of loss that provides: "If loss includes substantial unforeseen harm, it may be a ground for downward departure."

(3) Provide a causation standard requiring that the conduct was the cause "in fact" of the harm at issue (also called "but for" causation). Consider adding commentary language that provides: "If loss includes substantial unforeseen harm, it may be a ground for downward departure."

(4) Adopt a "modified but-for" causation standard that requires "but for" causation but also requires that to be included in loss any harms must have been reasonably foreseeable.

Recommendations of Outside Groups:

Bowman: Consistent with other areas of criminal and civil law, the defendant should be accountable for those harms that (1) his or her relevant conduct was a "substantial factor" in producing and (2) were reasonably foreseeable as a "probable

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[3]To date, *Vaknin* has not been followed by any other jurisdiction or cited in subsequent First Circuit cases.

result" of that conduct. "Consequential damages" is a term from contract law that has no place in this context. (pp. 8-12)

Criminal Law Committee: The Commission should adopt a causation standard with the familiar legal concept of foreseeability as the touchstone. "This clearer standard would not only provide guidance and a central theme, but it would also eliminate the current inconsistency of including foreseeable consequential damages only in certain kinds of cases." (pp. 2-4)

Department of Justice: The Department has not recommended an amendment dealing with causation.

Practitioners' Advisory Group: Adoption of a "proximate cause" causation standard is essential to ensuring that loss is an accurate proxy. Such a standard would reduce both unwarranted disparity and unnecessary litigation. The Commission should also account for situations in which causal factors other than the defendant's conduct affect the loss figure. (pp. 4-5)

Probation Officers' Advisory Group: The group "strongly opposes" "the introduction of causation into the determination of loss." The group feels that no causation standard is needed, and that creating one would "greatly increase the complexity of the guidelines." (p. 2)

2. Consequential damages

Current rule: Neither §2B1.1 or §2F1.1 is explicit about inclusion of consequential damages. In §2B1.1 "reasonable replacement cost to the victim" is one way loss may be measured "[w]here the market value is difficult to ascertain or inadequate to measure harm to the victim." Although §2F1.1 does not explicitly provide a rule on the general use of consequential damages, it is fair to infer that they generally are not to be included, because there is a specific rule allowing their use in procurement fraud and product substitution cases.

Issues: Should the Commission amend the commentary to include consequential damages in loss calculation?

Impetus: As part of the effort to make the definition of loss more clear, it might be helpful to provide explicitly how consequential damages should be handled in the determination of loss. The Practitioners' Advisory Group believes that calculating consequential damages is an unnecessary attempt at precision, given that loss is only a rough surrogate for culpability.

Case law: Section 2F1.1, n. 7(c) states: ". . . loss in a procurement fraud or product substitution case includes not only direct damages, but also consequential damages that were reasonably foreseeable." Thus, by clear implication, the Commission has ruled out consequential damages as an element of loss in other types of frauds. Nevertheless, by taking an expansive view of the definition of "loss" (*i.e.* "the value of the property taken, damaged or destroyed") some courts have arguably included consequential damages within loss in cases other than procurement frauds or product substitution frauds. Examples of such holdings are: *United States v. Gottfried*, 58 F. 3d 648 (D.C. Cir. 1995) and *United States v. Berkowitz*, 927 F. 2d 1376 (7th Cir. 1991); *cert. denied* 502 U.S. 845 (1991).

In *Gottfried*, 58 F. 3d at 649-50, an attorney for the Board of Veterans Appeals wrongfully removed documents from files of cases he was working on and then recommended remand to the various hearing officers on the basis of "incomplete files." The object of this charade was to avoid doing substantive work on the appeals. The defendant was convicted of destruction of government documents in violation of 18 U.S.C. § 2071, an offense that is sentenced under §2B1.3. Despite the fact that the documents he destroyed had no inherent value, the D.C. Circuit upheld the inclusion, in the loss calculation, of the subsequent cost of processing the 32 files with which Gottfried tampered. This sum included the pro rata overhead expenses, such as utilities and cost of paying support staff, of running the Board during the time these 32 cases were prepared and heard. One could arguably view these sums as consequential damages that would not properly be included as loss in this non-procurement, non-product substitution case.

The court refused to limit loss to the fair market value, in this case, the nominal value of the paper destroyed, reasoning that such a result would make "no sense," where "the purpose of the exercise is to measure the economic harm Gottfried caused." *Id.* at 651, citing §2B1.1, comment. (backg'd), that provides that "'Where market value is difficult to ascertain or inadequate to measure harm to the victim, the court may measure loss in some other way . . ..' U.S.S.G. §2B1.1, comment. (n.2)."

The court even upheld the inclusion in loss of the Board's pro rata overhead expenses that would have been incurred even if the criminal offense had not been committed, concluding that including such expenses "in the amount of the Board's loss, or 'fee,' for reprocessing the thirty-two appeals merely attributed to Gottfried the cost of undoing the damage he had done." *Id.*

Regarding decisions that hold that incidental or consequential damages may not be included in the loss calculation, the D.C. Circuit said those cases stand for the proposition that only "direct" losses count. *Id.* at 652.

Similarly, in *Berkowitz*, the Seventh Circuit upheld the inclusion of the cost of reorganizing a file, re-interviewing witnesses and recreating documents where a taxpayer trashed the government's investigative file regarding his alleged tax fraud, and was convicted of obstruction of justice (18 U.S.C. § 1503) and stealing government property (18 U.S.C. § 641). The amounts included in loss did not represent the value of properly assessed taxes that went unpaid, but instead represented the cost to the government of determining the size of the tax shortfall.

Similarly, in *Berkowitz*, the Seventh Circuit concluded that the value of the documents was their "replacement cost." 927 F. 2d, at 1391. However, in that case the appellant did not make an argument that the disputed costs should be excluded because they represented consequential damages; rather, he argued that the government did not introduce sufficient evidence to support the estimated cost of replacing the documents.

Helpline Report: A few Helpline calls have been received on this issue. Callers are confused about when and to what extent consequential damages should be included.

Option:

(1) Modify the commentary on loss to indicate that consequential damages generally are not to be included in loss in any type of case, but may be considered as a ground for upward departure.

(2) Adopt a more comprehensive definition of loss which specifies when consequential damages will be part of loss and includes a precise causation standard for determining the scope of consequential damages.

(3) Allow consequential damages to be included in loss in all types of cases provided there is a reasonable connection between the defendant's conduct and the harms the government seeks to characterize as consequential damages.

Recommendations of Outside Groups:

Bowman: "Consequential damages" is a term from contract law that has no place in this context. Issue would be handled by adoption of proposed causation standard. (pp. 8-12)

Criminal Law Committee: Recommends an amendment addressing issues of causation and consequential damages. Believes the recommended "clearer" causation standard "would not only provide guidance and a central theme, but it would also eliminate the current inconsistency of including foreseeable consequential damages only in certain kinds of cases." (pp. 2-4)

Department of Justice: The Department of Justice has not recommended an amendment dealing with consequential damages.

Practitioners' Advisory Group: Recommends that consequential damages be left for departure, because the issue would "frequently cause protracted litigation, uncertainty and disparity in application, and, at the end of the entire process, sheer speculation." Identifies the issue of consequential damages as a "perfect candidate for departure" where consequential damages "are out of proportion to the direct loss caused by the defendant's conduct." (pp. 2, 4, 5-6)

Probation Officers' Advisory Group: Recommends against an amendment regarding consequential damages, preferring that the current rule be retained that allows inclusion of consequential damages in loss only in contract procurement and product substitution cases. (p. 2)

3. Interest

Current rule: Section 2F1.1, n. 7 provides that loss "does not, for example, include interest the victim could have earned on such funds had the offense not occurred." In a fraudulent loan case "the loss is the amount of the loan not repaid at the time the offense is discovered, reduced by the amount the lending institution has recovered (or can expect to recover) from any assets pledged to secure the loan." §2F1.1, comment. (n. 7(b)).

Issue: Should the Commission clarify the rule regarding when interest is included in loss?

Impetus: Although the Commission included language in its definition of loss that excludes interest the victim could have earned, an apparent split in the circuits has developed about whether interest the defendant agreed to pay (*e.g.*, on a fraudulently procured loan) should be included in loss. *United States v. Gilberg*, 75 F.3d 15, 18-19 (1st Cir. 1996) (including in loss interest on fraudulently procured mortgage loan); *United States v. Goodchild*, 25 F.3d 55, 65-66 (1st Cir. 1994) (holding accrued finance charges on credit cards are not "opportunity costs," and may be included in amount of loss); *United States v. Henderson*, 19 F.3d 917, 928-29 (5th Cir.) ("Interest should be included if, as here, the victim had a reasonable expectation of receiving interest from the transaction."), *cert. denied*, 513 U.S. 877 (1994); *United States v. Lowder*, 5 F.3d 467 (10th Cir. 1993); *But see United States v. Hoyle*, 33 F.3d 415, 419 (4th Cir. 1994) ("[I]nterest shall not be included to determine loss for sentencing purposes."), *cert. denied*, 513 U.S. 1133 (1995). As in consequential damages, the Practitioners' Advisory Group believes that calculating interest is an unnecessary attempt at precision, given that loss is only a rough surrogate for culpability.

If interest the defendant agreed to pay plays no part in the determination of loss, the defendant who makes some payments may face the same penalty as a similar defendant who makes none, because many loans are structured so that a large percentage of the early payments are allocated to interest. For example, the defendant who makes early payments in a loan application case may face a principal balance upon discovery of the offense that is only slightly reduced by the payments made. Should that defendant face a loss amount that is virtually identical to that faced by another defendant who made no payments?

Case law: Although the Commission has promulgated commentary (see "Current rule" above), that can plausibly be read to indicate the Commission's disapproval of including interest in any form as loss, most circuits that have addressed whether "bargained for" interest should be included in the calculation of loss have concluded that it should on the theory that the Commission intended to exclude only opportunity cost interest. The one apparent exception has been the Fourth Circuit's decision in *Hoyle*.

In *Hoyle*, the appellants had been convicted of submitting false student loan applications in violation of 18 U.S.C. §§ 1001 and 371, resulting in the disbursement of over $19,000. The Fourth Circuit reversed the inclusion of interest in the calculation of loss, concluding that the "clear import" of the 1992 amendment to the commentary to §2F1.1 adding language excluding interest, was that "interest should not be included to determine loss for sentencing purposes." *Hoyle*, 33 F.3d at 419. In doing so the Fourth Circuit explicitly declined to follow the decision of the Tenth Circuit in *Lowder* that distinguished between opportunity cost interest (excluded) and interest the defendant has promised and indicated had been earned (properly included).

In *Lowder* the appellant was convicted of numerous offenses, including making false statements to a financial institution and mail fraud (18 U.S.C. §§ 2(b) and 1014; 18 U.S.C. §§ 2(b) and 1341), in connection with a 1990 investment scheme in which he promised investor-victims a low-risk investment with a guaranteed 12 percent return. Rejecting the argument that interest should be excluded because it amounted to lost profit, the Tenth Circuit distinguished *United States v. Bailey*, 975 F.2d 1028 (4th Cir. 1992), where the Fourth Circuit limited loss to actual loss and refused to include projected profits. The court said that "*Bailey* did not involve the promise to pay a specific rate of return, nor did the defendant send account summaries showing specific amounts owed." *Lowder*, 5 F.3d at 471. In support of its position the Tenth Circuit noted the rule allowing use of intended loss amounts in loss, and its interpretation of the commentary language on interest "as disallowing 'opportunity cost' interest or the time value of money stolen from victims." *Id.*

In *Henderson*, 19 F. 3d at 928, the Fifth Circuit included interest in loss, rejecting reliance on the commentary language on interest finding "that this commentary sweeps too broadly and, if applied in this case, would be inconsistent with the purposes of

§2F1.1. *Stinson v. United States*, 508 U.S. 36 (1993)." The Fifth Circuit found that interest "should be included if, as here, the victim had a reasonable expectation of receiving interest from the transaction." *Henderson*, 19 F. 3d at 928.

In *Goodchild*, 25 F. 3d at 65-66, the First Circuit invited Commission action on this issue, saying there is "a clash between the ambiguous language used in the Commentary [about interest] and the complexity of what constitutes interest and when it is an integral part of the value of the 'money, property or services unlawfully taken.'" Commentary 7. Our holding will not solve the problem; such resolution lies with the Sentencing Commission."

The First Circuit held that in a case involving fraudulent use of unauthorized credit cards, finance charges and late fees are not excluded pursuant to the commentary language on interest because they do not represent the narrow kind of "opportunity cost interest" proscribed by the rule. *Id.* at 66. In the view of the First Circuit the credit card agreement details the applicability of late fees and finance charges that are "part of the price of using credit cards" which the company "has a right to expect . . . will be paid." *Id.*

Helpline Report: A few Helpline calls have been received on this issue. Specifically, it has been pointed out that the example in Application Note 7 is too narrow, leaving room for various interpretations about the use of interest in other types of cases.

Option:

(1) Provide that interest "of any kind" should not be included in loss, but that "bargained for" interest may be considered as a possible ground for departure.

(2) Reinforce the current rule that opportunity cost should not be included in loss, but provide that loss does include interest the defendant agreed to pay (or the victim reasonably relied upon) but had not yet paid at the time of discovery of the offense.

Recommendations of Outside Groups:

Bowman: "Interest" is simply a special causation category, and so the solution to the interest issue will be "readily inferable from a properly conceived set of causation rules." (p. 12)

Criminal Law Committee: The Commission should promulgate an amendment to clarify which kinds of interest, if any, are to be included in the loss figure. (p. 4)

Practitioners' Advisory Group: There is no good reason to include interest in loss. Even if there were, interest will usually be a small part of the overall loss figure, and so the added complexity of calculating interest would not result in a significantly improved measure of culpability or offense severity. (p. 6)

Probation Officers' Advisory Group: "[I]nterest should never be considered as part of loss." (p. 2)

4. **Value Received - Determination of credits to reduce loss.**

Three discrete issues can be identified under this subject category: payments made after discovery of the offense, what payments and services received by victims should be credited against loss, and timing of valuation of collateral.

Current rule: Section 2F1.1 currently allows a defendant to receive "credits" against the loss figure in two specific types of cases, but is silent on others. In product substitution cases, the value of the fraudulently substituted product is credited against the loss amount. In loan application cases, the amount of payments made before the crime is discovered plus the value of "any assets pledged to secure the loan" are credited against the amount of the loan. *See* §2F1.1, comment. (n. 7(a), (b)). The current guidelines give no explicit guidance for cases like *Maurello* and *Reddeck*; those courts extracted a general crediting principle from application notes 7(a) and 7(b) to §2F1.1.

Issues: Generally, should the Commission clarify whether loss is net loss? Should the Commission clarify the commentary to ensure that only collateral pledged and payments made *prior to* discovery are credited to reduce the loss figure? Should payments to early victims in Ponzi schemes be credited against loss? Should the valuation of pledged collateral be made at the time it is pledged, or should subsequent fluctuations in its value affect the loss calculation?

Impetus: Case law and helpline questions have shown uncertainty about these issues.

Post discovery payments. Confusion exists in the Sixth Circuit as to whether post-discovery payments in loan application cases can reduce the loss calculation in cases where the defendant is not a borrower. This practice would be contradictory to the current rule that limits credits in such cases to pre-discovery payments plus the value of "any assets pledged to secure the loan." See §2F1.1, comment. n. 7(b).

In *dicta* in *U.S. v. Lucas*, 99 F.3d 1290 (6th Cir. 1996), a Sixth Circuit panel alluded to a supposed judicial exception to n. 7(b) that permitted "the amount of loss calculation payments that borrowers might be expected to make in the future" to be credited against the loss calculation in situations where the defendant was not among the borrowers. The *Lucas* court cited *U.S. v. Chichy*, 1 F.3d 1501 (6th Cir. 1993), for the foregoing proposition. However, a close reading of *Chichy* discloses that the *Chichy* court did not base its loss calculation on the fact that the borrowers did not include the defendant. In addition, the *Chichy* court did not reduce loss by any post-discovery payments.

Crediting payments/services received by victims. Some courts have raised questions about crediting things of value against loss. *E.g., United States v. Maurello*, 76 F.3d 1304, 1311-12 (3d Cir. 1996) (calculating loss by subtracting value of satisfactory legal services from amount of fees paid to bogus lawyer); *United States v. Reddeck*, 22 F.3d 1504, 1513 (10th Cir. 1994) (reducing loss by value of education received from bogus university); *United States v. Castner*, 50 F.3d 1267, 1275-77 (4th Cir. 1995) (refusing to reduce loss by value of functional but fraudulently substituted products); *United States v. Morris*, 18 F.3d 562, 570 (8th Cir. 1994) (giving no credit for property pledged as security).

For example, courts have had difficulty with the issue of whether payments to early investors should count as a credit against the loss to later investors, such as in a Ponzi scheme. In *United States v. Mucciante*, 21 F. 3d 1228, 1237-38 (2d Cir.), the Second Circuit refused to reduce the loss by the amount that the defendant "repaid . . . as part of a meretricious effort to maintain [the victims'] confidences" in a non-Ponzi scheme), *cert. denied*, 513 U.S. 949 (1994).

The Seventh Circuit took a different approach in a Ponzi scheme. In *United States v. Holiusa*, 13 F.3d 1043, 1044-45 (7th Cir. 1994), where the defendant perpetuated a Ponzi scheme by appropriating $11,625,739 from "investors" and returning approximately $8,000,000 in "interest," the district court found that the defendant intended "to defraud all of the victims of their money" and therefore held him accountable for the full $11,625,739. *Id.* at 1045; *see also* U.S.S.G. §2F1.1, comment. (n. 7) ("[I]f an intended loss that the defendant was attempting to inflict can be determined, this figure will be used if it is greater than the actual loss."). The Seventh Circuit reversed, holding that "[t]he full amount invested was not the probable or intended loss because [the defendant] did not at any point intend to keep the entire sum... . Because he did not intend to and did not keep the full $11.6 million, that amount does not reflect the actual or intended loss, and is not an appropriate basis for sentencing."[1] *Holiusa*, 13 F.3d at 1046-47; *see also United States v. Wolfe*, 71 F.3d 611, 618 (6th Cir. 1995) (following *Holiusa*). *Wolfe* is an example of a case in which a legitimate investment plan turned into a Ponzi scheme when the defendant's previously sound investment strategy turned sour. *See* 71 F.3d at 612.

The Eleventh Circuit took a slightly different approach in *United States v. Orton*, 73 F.3d 331 (11th Cir. 1996), crediting only payments made to "losing investors," not payments to investors who made a profit. In *Orton* the defendant had received $525,865.66 from and returned $242,513.65 to the "investors." Twelve investors received more than they had invested; the total lost by the other investors was $391,540.01. *Id.* at 333. The Eleventh Circuit adopted what it dubbed the "loss to losing victims" method: it held the defendant accountable for "the net losses of all victims who lost all or part of the money they invested." *Id.* at 334. The money that the defendant received from and returned to those investors who ended up with a net gain did not enter into the loss calculation.

Timing of valuation of collateral. Questions have arisen about changes in the value of assets securing a fraudulently procured loan after the assets are pledged. The question is whether this variation should affect the loss calculation. *See, e.g., United States v. Barrett*, 51 F.3d 86, 90-91 (7th Cir. 1995) (including in loss drop in value of property securing fraudulently obtained loans).

A rule that gives credit for what collateral was worth when it was pledged would ensure that fortuitous increases or decreases in the value of the property have no impact on the sentence. The current rule, however, specifies no fixed time for valuing collateral; it instructs the court to reduce the loss figure by "the amount the lending institution has recovered (or can expect to recover) from any assets pledged to secure the loan." §2F1.1, comment. (n. 7(b)). A lender's decision regarding when to sell a foreclosed property can therefore significantly affect the loss amount.

Helpline Report: A significant number of Helpline calls have been received on this issue. It appears that predominantly in fraudulent loan application cases there is significant disparity in terms of the calculation of the determination of credits. This is particularly true with regard to valuation of collateral. No standard use of credits is discernible.

A number of calls have been received about whether a case should be sentenced under §2B1.1 or §2F1.1 for a given statute or similar conduct under a different statute. One can view this issue in terms of whether potential credits available if §2F1.1 is used, can and should be available if §2B1.1 is used. More specifically, several Helpline calls have been received on two similar issues. Several statutes refer (in Appendix A) to both §2B1.1 and §2F1.1. Loss is calculated differently under §2B1.1 and §2F1.1. These two guidelines can produce very different results because the loss figure is often higher using §2B1.1 because the assets pledged or the money recovered prior to discovery is not deducted as it would be if using §2F1.1.

Secondly, some statutes which refer only to §2B1.1, cover offenses which are more like fraud than theft, however, under §2B1.1 the loss for these offenses is calculated differently than a fraud covered under §2F1.1. In other words, frauds under §2F1.1 use a net loss figure, while theft-like frauds under §2B1.1 do not receive similar credits. To some practitioners, this seems confusing and somewhat unfair because they do not see a distinction between the offenses.

Option:

(1) Provide a general principle that the amount of loss shall be reduced by the value of the money, property, or service(s) received by, or pledged to, the victim in connection with, and prior to discovery of, the offense. Include an example for Ponzi schemes to make clear that the same principle requires that loss be reduced by the payouts made to victims. Add commentary that encourages great deference to judges in the determination of the "value" received by victims.

(2) Establish the magnitude of the credit for pledged collateral based on the value at the time of pledging, so that subsequent fluctuations in value do not affect the determination of the loss amount.

(3) This option (based on recommendations in Frank Bowman's article regarding the timing for measurement of the net loss calculation) is twofold; it addresses when to measure loss and the related issue of how to measure net loss.

Loss should ordinarily be measured <u>at the time the crime is detected</u> *except*: (a) if the loss was higher at the time the crime was legally complete, the loss should be measured at that time, or (b) if the defendant continues to engage in criminal conduct which increases the loss after the crime is detected, the increased loss should be included as loss.

Moreover, the loss should be the <u>net loss</u> to the victim(s). This option, like the Guidelines' current approach, requires that: (a) the amount of loss be reduced by the value of money or property transferred to the victim(s) in the course of the offense, (b) the amount of the loss be reduced by the value of property pledged as collateral as part of a fraudulently inducted transaction, and (c) the loss not be reduced by payments made by the defendant to a victim after detection of the crime. The principal change proposed by this option is in <u>measuring the time at which the collateral is to be valued</u>. Consistent with the approach to time of loss measurement, discussed above, the collateral is to be valued at its sale price if sold before discovery of the crime or, if not sold, at its fair market value at the time of detection.

(4) Provide that payments made on fraudulently obtained loans are not to be direct credits against loss, but may support a downward departure where they demonstrate the defendant's intent to make good on the loan.

Recommendations of Outside Groups:

Bowman: With two exceptions, "loss" should be measured as of the time the crime is detected, and a "net loss" approach that largely tracks current case law should be adopted. (pp. 12-13)

Criminal Law Committee: The current definition is incomplete and inconsistent regarding the valuation of loss and credits against loss, resulting in litigation and disagreement among courts. The Commission should promulgate an amendment to clarify how and at what point in time to value loss and credits. Specific guidance on Ponzi schemes is also needed. (pp. 2-4)

Practitioners' Advisory Group: "The actual loss figure should be reduced by all amounts received or readily recoverable from the defendant at the time law enforcement authorities discover the offense." Credits should be measured in a way that ensures that subsequent fluctuations in their value will not affect the loss calculation. (pp. 6-8)

Probation Officers' Advisory Group: "The Commission should clarify whether loss is net or gross," focusing on the heartland of cases. Losses should not be offset by services rendered, nor by money paid to earlier victims in a Ponzi scheme. Collateral should be valued as of the time of the offense, so that subsequent market fluctuations will not affect the loss calculation. (p. 3)

5. Diversion of Government Program Benefits

Current rule: §2F1.1, n. 7(d) provides that in cases involving diversion of government program benefits loss is the "value of the benefits diverted from intended recipients or uses."

Issue: Should the Commission base loss in diversion cases on the value of the government benefits fraudulently obtained without deducting the value of the benefits that the defendant does allocate to "intended recipients or uses?"

Impetus: DOJ prosecutors indicated to us that the rule is not clear on whether total proceeds should be used, and that it is difficult to determine loss and gain in such cases, resulting in very small (if any) loss amounts in such cases. For example, in a kickback to a doctor who refers patients to a health care provider, it is difficult to determine loss, both because it is hard to prove that the patients received unnecessary services and because it is difficult to determine how much some alternative health care provider "lost." Similarly, it is difficult to determine the gain to the health care provider, assuming that net proceeds from the referred patients is likely to overstate the net gain.

The appellate courts that have considered loss calculations under §2F1.1, n.7(d) have uniformly concluded that n.7(d) requires a "net" figure. In other words, the defendant receives a credit to the extent that the federal funds or benefits he wrongfully obtains are allocated by him to the intended recipients or uses of the federal program from which the funds or benefits are purloined.[4]

In *U.S. v. Peters*, 59 F.3d 732 (8th Cir. 1995), the defendant, who bilked the federal government under the grant program of the Asbestos School Hazard Abatement Act, 20 U.S.C. § 4011 et. seq., was not assessed loss for the funds that were utilized to actually remove asbestos from the premises of his client, a Nebraska school district. The loss was calculated as the amount of federal funds diverted from asbestos relief for a qualifying school district, their "intended use."

In *U.S. v. McGee*, 41 F.3d 1508 (6th Cir. 1994), the court found that the defendant, who had defrauded HUD by applying for funds under a program to repair abandoned housing for the homeless, would not be responsible for rents collected from unauthorized persons. Rather, the loss she caused was seen as the value of benefits diverted from intended uses. The court concluded that this was the fair rental value of the houses involved that were not rented to homeless persons (the "intended recipients" of the program).

In *U.S. v. Barnes*, 117 F.3d 328 (7th Cir. 1997), the court held that the defendant, who had illegally discounted the value of food stamps in a cash-for-food stamps scheme, was not responsible for the gross value of all food stamps his retail store redeemed. Rather, the defendant received credit against loss for the value of the food stamps his store redeemed for items that could be legitimately purchased with food stamps. Interestingly, the scope of the credit was determined by painstaking analysis of the defendant's documents that were submitted to the IRS for tax purposes. His "gross sales" of food items was set off against the value of food stamps redeemed in his store to determine "legitimate food sales from food stamps coupon redemption." The defendant received this amount in credit against his loss calculation. In this way his sentence was calculated only on the value of the government benefits "diverted from intended recipients or uses."

Finally, in *United States v. Arnous*, 1997 WL 484575 (6th Cir.Aug. 25, 1997), the

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[4] A seeming anomaly in this case law is *U.S. v. Adam*, 70 F.3d 776 (4th Cir. 1995). The *Adam* court declined to engage in fact finding as to what percentage of the Medicare funding spent on patients who were referred by the defendant doctor for certain tests pursuant to a kickback scheme was spent for appropriate purposes. However, *Adam* does not represent an actual circuit split since, for reasons that are unclear, the *Adam* court did not decide the case in light of §2F1.1, comment. (n. 7(d)). Accordingly, the court did not focus upon the "value of the benefits diverted from intended recipients or uses" as required by n. 7(d).

appellate court remanded the case for resentencing because of an error in calculation of loss. The defendant was convicted of making a false statement in her application for participation in the food stamp program and for presenting false food stamp redemption claims. The district court found that the loss was the total amount of the food stamp redemption claims she submitted under the fraudulently-obtained authorization number. The Sixth Circuit's conclusions were two-fold. First, the circuit court found that properly authorized retail establishments could be considered "intended recipients or uses" for purposes of Note 7(d). The court relied on the opinion in *Barnes*, which defined "intended use" as "the purchase of specified food products from authorized retailers." The Sixth Circuit, likewise, found that the amount of loss caused by the defendant's diversion was "the amount of the profits that properly authorized retailers failed to realize as a result of the business having gone to the [defendant] instead of to them." Second, the circuit court stated that the "net loss" should be the difference between the cost of the inventory to the other stores and the face amount of the food stamps. Accordingly, the court vacated the court's decision to base loss on the total amount of the food stamps rather than the net loss to authorized retailers.

Helpline Report: Very few Helpline calls have been received on this issue.

Option:

(1) Leave the current rule unchanged and provide additional commentary that judges should be given great deference in such cases both in the determination of loss and gain and in the decision about whether or not to depart, because of the special problems in such cases.

(2) Modify the existing rule to specify that loss includes all funds received by the defendant without regard to whether any or all of these funds ultimately went to intended uses or recipients.

Recommendations of Outside Groups:

Criminal Law Committee: The "Commission should clarify its intent on this issue so that the courts are not required to guess what the Commission's intent was." (p. 4)

Department of Justice: Believes "there are cases in which gross gain is the appropriate measure — namely, where the offense endangered (or could have endangered) the health or safety of any person or the public or where the offender intentionally or recklessly disregarded the risk to the health or safety of any person or the public." (p. 3)

Probation Officers' Advisory Group: The courts should have great discretion in these cases, both in deciding the amount of loss and gain and in deciding whether to depart. (p. 3)

B. Alternatives to Actual Loss

1. Intended loss

Current rule: Application note 7 to §2F1.1 instructs the courts to use the higher of actual and "intended loss," a term not used in the §2B1.1 commentary, and in doing so, makes a vague reference to the attempt provisions in §2X1.1.

Issue: Should the Commission adopt an amendment providing that the amount of intended loss should be reduced by any amounts that could not have been obtained by the offense, or that the defendant was not reasonably capable of causing?

Impetus: Sprinkled throughout the commentary to §§2B1.1 and 2F1.1 are references to various alternatives to actual loss, and the guidelines are arguably unclear and inconsistent about when to use alternatives.

This discussion of alternatives to actual loss arguably has created some confusion in application. For example, in *United States v. Morris*, 18 F.3d 562, 570 (8th Cir. 1994), the Eighth Circuit considered "possible loss," a concept that does not appear anywhere in the guidelines. *Id.* In *United States v. Kopp*, 951 F.2d 521, 529-30 (3d Cir. 1991), the Third Circuit advocated using "intended loss" in *theft* cases, despite the court's recognition that term appeared only in the commentary to the *fraud* guideline.

Some courts have limited intended loss by a concept that they have called "economic reality" or by use of the amount actually "put at risk" (*e.g.*, reverse sting case; insurance claim in excess of fair market value). Should the concept of intended loss be eliminated from the required calculation of loss and left for potential departure, or clarified? The Tenth Circuit refused to find loss where because government agents were the intended "victims" there could be no loss. *United States v. Galbraith*, 20 F. 3d 1054, *cert. denied* 513 U.S. 889 (1994). The Seventh Circuit has modified the intended loss concept to encompass only those losses that stood a realistic chance of occurring. *United States v. Sung*, 51 F.3d 92, 95-96 (7th Cir. 1995); *see also United States v. Moored*, 38 F.3d 1419, 1425 (6th Cir. 1994) (focusing on loss that defendant "realistically intended"). *But see United States v. Lorenzo*, 995 F.2d 1448, 1460 (9th Cir.) ("[T]he amount of [intended] loss . . . does not have to be realistic."), *cert. denied*, 510 U.S. 881 (1993).

In a contract procurement case, the question has arisen whether "expected loss" in application note 7(b) to §2F1.1 is always the full amount of the contract, or whether the defendant's ability and intent to perform the contract should play a role in loss calculation. *See United States v. Schneider*, 930 F.2d 555, 557-59 (7th Cir. 1991) (drawing distinction between defendant who intends to perform contract and defendant who intends to pocket proceeds and skip town).

Helpline Report: A significant number of Helpline calls have been received on this issue demonstrating overall confusion in the field. The field is confused about the differences between intended and attempted loss and how §2F1.1 interacts with §2X1.1. It appears from these calls that there is inconsistency in the use of intended versus actual loss.

Option:

(1) Eliminate references to "attempted" loss and make clear that intended loss is designed to reflect appropriately "the culpability of the defendant, and thus should not be limited by the fact that the defendant could not have been successful in achieving the intended loss." Eliminate references to attempt, solicitation, and conspiracy provisions in §2X1.1 (consistent with the separately proposed amendment that would eliminate the possibility of the three-level reduction for incomplete attempts, solicitations, and conspiracies).

(2) Eliminate use of intended loss to determine loss, but provide that if intended loss substantially exceeds actual loss it may be a ground for departure.

Recommendations of Outside Groups:

Bowman: The intended loss concept should be retained as a way of ensuring that inchoate crimes are not underpunished. (p. 13) "[F]actual impossibility or improbability of success of a criminal plan should, in general, be no defense." A defendant should therefore be accountable "for losses he intended, so long as they 'might reasonably have occurred if the facts were as he believed them to be.'" (p. 13)

Criminal Law Committee: Intended loss is a frequently occurring issue, and so the Commission should provide specific guidance rather than leaving it for departure. (pp. 3-4) The Commission should provide specific rules for handling these cases. (pp. 4-5)

Department of Justice: Recommends that "the Commission clarify that intended loss includes the loss that would have resulted or that the defendant intended to inflict in the case of a law enforcement 'sting' operation. Although such an operation may avoid any actual loss, the loss that could have been caused is an appropriate measure of the defendant's culpability." (p. 4)

Practitioners' Advisory Group: "[I]ntended loss should only be used as an encouraged departure ground where it differs significantly from actual loss." (pp. 10-11) "[W]here the defendant is incapable of causing the loss intended, the defendant's offense level should be based on the loss which would have been caused had the defendant's fraud been successful." (p. 10) An amendment is recommended that would modify the concept of intended loss so as to incorporate some concept of "economic reality."

Probation Officers' Advisory Group: Recommend an amendment to provide that intended loss only includes those losses that had a realistic chance of occurring. (p. 5)

2. **Gain**

Current rule: Application note 8 to §2F1.1 provides that courts need not determine loss "with precision" but "need only make a reasonable estimate of the loss, given the available information." It further provides that the "offender's gain from committing the fraud is an alternative estimate that ordinarily will underestimate the loss."

Issues: Should the Commission clarify the rule on use of gain as an alternative to actual loss?

Impetus: Although we are aware of no circuit split on the issue, courts have struggled with the issue of when to use gain as an alternate estimate of loss. *Compare United States v. Kopp,* 951 F.2d 521, 530 (3d Cir. 1991) (holding that gain cannot be used if loss is measurable even if loss is zero), *with United States v. Haddock,* 12 F.3d 950, 960 (10th Cir. 1993) (allowing gain to be used as alternative when gain corresponds to an actual, intended, or probably loss). Similarly, in *United States v. Andersen,* 45 F.3d 217 (7th Cir. 1995), the Seventh Circuit held that gain may be used only as an alternative method of calculation when there is in fact a loss, and only if use of the gain results in a reasonable estimate of the loss. Furthermore, the Practitioners' Advisory Group has urged the Commission to account for the lesser culpability of a defendant whose personal, intended gain from the offense is considerably less than the calculated loss amount.

In *United States v. Chatterji,* 46 F.3d 1336, 1341 (4th Cir. 1995), the Fourth Circuit found no loss where the prescription drugs that the defendant manufactured and for which he fraudulently gained FDA approval were just as effective as their FDA-regulated counterparts. *Id.* More importantly, the court refused to use gain as an alternative to loss, finding that when loss is determined with certainty, gain is not to be substituted, even when loss is zero. *Id.* at 1342. In contrast, when drugs for which FDA approval was fraudulently obtained are *not* as good as their counterparts, gain may be used to measure loss. *See United States v. Marcus,* 82 F.3d 606, 610 (4th Cir. 1996) (holding manufacturer liable for over $10 million in gross proceeds as the proper measure of loss because the drug did not meet FDA specification and, thus, had no value).

Case law: The appellate courts review the definition of loss using a *de novo* standard. "While the question of the amount of loss is generally subject to review for only clear error, the application of a loss enhancement to undisputed facts is a question of law for which we review *de novo*." *United States v. Chatterji*, 46 F.3d 1336, 1340 (4th Cir. 1995).

In *Chatterji* the Fourth Circuit, using a *de novo* standard, held that a defendant's gain may be an appropriate estimate of loss only when there is some actual, intended, or probable loss. The Fourth Circuit found no loss where the prescription drugs that the defendant manufactured and for which he fraudulently gained FDA approval were just as effective as their FDA regulated counterparts. The district court had concluded that the gross sales of two prescription drugs was a loss to consumers because of false statements in an FDA application. The Fourth Circuit reversed, holding that despite the false statements there was no loss to the consumers because the drugs were exactly what they purported to be. Because the consumers had received what they bargained for, no loss resulted from the manufacturer's conduct. The appellate court stated that "when a drug possesses FDA approval, poses no threat to the health and well-being of the consumer, and meets all of the goals of FDA requirements for safety and efficiency, there can be no actual, monetary loss attributable to the regulatory fraud by which FDA approval was obtained." Therefore, because there was no loss, the defendant's gain could not be used to calculate loss.

In *United States v. Adam*, 70 F.3d 776 (4th Cir. 1995), the Fourth Circuit using a *de novo* standard, distinguished *Chatterji*, and affirmed the district court's decision to use the amount of appellant's gain to determine the amount of loss. The defendant was convicted of receiving kickbacks paid out of welfare funds. The Fourth Circuit held that USSG §2F1.1, note 8 appears designed for just such circumstances because the amount of loss caused by the appellant's conduct cannot be determined with any certainty, but the amount of appellant's gain is an available, alternative measure of estimating that loss. The Fourth Circuit agreed with the government's argument that losses are almost always incurred when welfare fraud occurs because taxpayers must pay higher costs from kickback schemes, and that welfare fraud surely does impose enormous, unnecessary financial burdens on the public. Thus, because there was a loss to the United States, the defendant's gain could be used to calculate loss.

In *United States v. Castner*, 50 F.3d 1267 (4th Cir. 1995), the Fourth Circuit held that gain (illegal profit) could be used to calculate loss because the Navy did not receive what it bargained for under the contract. In *Castner*, the defendant substituted parts from a different manufacturer than what was stated in the contract with the Navy. The appellate court stated: "[b]ecause the Navy was unaware that the GRI parts were not OEM-approved, it did not subject those parts to the rigorous testing required to assure the quality and long-term reliability of substitute parts." Therefore, because there is a loss, illegal profit is an adequate measure of actual loss under §2F1.1. The appellate court distinguished *Chatterji* on the grounds that in *Chatterji* there was no product substitution where the product sold was not what it claimed to be because the product was exactly what it purported to be.

In *United States v. Parsons,* 109 F.3d 1002 (4th Cir. 1997), the Fourth Circuit held that because the government suffered no loss of the funds it had authorized the employee to spend it vacated the sentence and remanded. The defendant was convicted of mail fraud when she filed false travel reimbursement forms. The district court counted legitimate travel expenses (that she rightfully used) along with the false expenses to calculate the amount of loss. The Fourth Circuit reversed, stating that the Sentencing Commission's instructions and precedent in the circuit mandate that the loss should be attributed to the payment fraudulently obtained in excess of the amount to which the defendant was lawfully entitled. Only the amounts that the government actually lost could be used in the loss calculations, not the gross amount of the checks.

In *United States v. Marcus,* 82 F.3d 606 (4th Cir. 1996), the Fourth Circuit affirmed the district court's conclusion that the generic drug manufacture's gross sales were appropriate measure of actual loss calculation under USSG §2F1.1. The district court determined that economic gain to the manufacturer was the proper measure of loss because the drug did not meet FDA specification, and thus had no value. The appellate court stated that although in some cases gain may prove to be an alternative measure of loss, there must be actual, probable, or intended loss to the victims. The Fourth Circuit distinguished this case from *Chatterji* on the grounds that the change in the formula posed the potential to affect the bioequivalence of the drug and that the drug was of unknown safety and efficacy. In *Chatterji,* the modification of the formula was merely an insignificant change that implicated only the shelf life of the drug, and that the modification in no way affected the safety or therapeutic value of the drug. In *Marcus* the defendant had no way of knowing that the drug was safe and effective without conducting additional tests. Thus, the change to the formula had an unknown effect on the safety and efficacy of the drug and as such, consumers did not receive that for which they expected--an FDA approved drug of known safety and efficiency. Thus, such a change prevents the drug from being that which it purports to be, and thus there was a loss to consumers. The appellate court held that the gross profit could be used to determine loss.

Helpline Report: A few Helpline calls have been received on this issue; however, the issue usually arises when there appears to be little or no loss or loss does not reflect the seriousness of the offense.

Option:

(1) Provide explicitly that gain may only be used if there is a loss but it is difficult to estimate (*i.e.*, gain cannot be used if loss is zero) and that where gain exceeds the loss it may be a ground for departure. Clarify that

gain generally means net gain and not gross proceeds.

(2) Provide that gain may be used when it exceeds the loss or loss is difficult to estimate.

Recommendations of Outside Groups:

Bowman: "[T]he 'gain' problem largely disappears once 'loss' is properly defined." (p. 12)

Criminal Law Committee: The Commission "should give careful analysis to these [frequently occurring] issues [intended loss, risk of loss, and gain], with a mind toward clarification rather than relegation to departure as some have suggested." (pp. 3-4)

Department of Justice: Recommends an amendment that would allow the use of gain when actual or intended loss is difficult or impossible to calculate and where gain is greater than loss. The Department also "believe[s] there are cases in which gross gain is the appropriate measure — namely, where the offense endangered (or could have endangered) the health or safety of any person or the public or where the offender intentionally or recklessly disregarded the risk to the health or safety of any person or the public." (p. 3)

Practitioners' Advisory Group: Recommend that "[a]ctual or intended gain must be included as a recognized ground for departure in certain cases in which gain differs substantially from loss." (p. 8) Encouraging departures when gain differs significantly from loss is essential to achieve fairness, as well as to reduce litigation. In fraud cases, the defendant's gain often bears no relation to the loss. Where the loss is minimal but the defendant obtains a significant gain from criminal activity, an upward departure should be encouraged. By the same token, where the loss is extremely large but the defendant's gain is minimal or zero, a downward departure should be encouraged. (pp. 3-4, 8-10)

Probation Officers' Advisory Group: Recommend an amendment to clarify that gain should not be used as an alternative to loss when loss is zero, but only when loss is too difficult to estimate. When gain is used, the court should focus on net gain, not gross proceeds. Recommends that if the loss can be estimated but gain exceeds the loss, gain should not be used in lieu of loss for guideline application, but may be appropriate as a departure consideration. (p. 2)

3. Risk of loss

Current rule: Guideline 2F1.1 is silent about including risk in the determination of loss, except application note 7(b) to §2F1.1 that suggests an upward departure when a defendant fraudulently obtains a loan, thus exposing the lender to the possibility of a loss, even though he pays it back before discovery of the fraud. This is based on the theory that at the time that a defendant receives fraudulent loan proceeds (*i.e.*, at the completion of the crime), the risk of loss is arguably the full amount of the loan, because there is no guarantee that any payments will be made or that any pledged security will retain its value. In fraudulent loan application and contract procurement cases, courts are told to use "expected loss" if no actual loss has occurred, and may consider departures when the final loss figure does not adequately reflect the "risk of loss." *See* §2F1.1, comment. (n. 7(b)).

Issues: Should the Commission revise the loss definition to cover risk of loss? (For example, if a fraudulently obtained loan of $100,000 is collateralized with $50,000 of collateral, should the minimum loss amount be the $50,000 even if the payments and collateral reduced the actual loss to a lower figure?)

Impetus: At least one court has found in a fraudulent loan case that the full loan amount can be used rather than the smaller actual loss amount. *See United States v. Brewer*, 60 F.3d 1142, 1145 (5th Cir. 1995) ("[W]e have found it proper to calculate loss based on the risk engendered by the defendant's criminal conduct, even where the actual loss was lower.")

Case law: In *Brewer* the Fifth Circuit reviewed an appellant's challenge to his counsel's failure to object to the use of the full amount of the $89,000 fraudulently obtained loan rather than the actual loss of $35,000 after sale of the real property collateral. The court conceded that counsel should have filed an objection, but found no prejudice for two reasons. First, the court stated that in fraudulent loan cases the guidelines advise that "loss is the actual loss to the victim or, where the intended loss is greater, the intended loss. U.S.S.G. §2F1.1, Application Note 7(b)." *Id.* at 1145. The court also observed that "applying this reasoning, we have found it proper to calculate loss based on the risk engendered by the defendant's criminal conduct, even where the actual loss was lower. *See, e.g., United States v. Wimbish*, 980 F.2d 312, 316 (5th Cir. 1992), *cert. denied*, 508 *U.S.* 919 (1993)."

Second, the court reasoned that the two-level reduction that would have resulted, had the lower loss amount been used, would result in a maximum sentence reduction of six months, and the appellant's 30-month sentence "would remain within the new range." *Id.* The court stated that it could not say there is "any probability that a lower sentence would have resulted." *Id.*

In *Wimbish* the defendant pled guilty to bank fraud (18 U.S.C. § 1344) and possession of stolen mail (18 U.S.C. § 1708), in connection with his disposition of personalized blank checks and bank statements that had been stolen from the mail. The defendant and a companion forged stolen checks drawn on one account, deposited them into another account (with stolen deposit slips), and requested cash back at the time of the deposit. The Fifth Circuit upheld the use of the face value of the deposited checks ($100,944) in the calculation of loss rather than the amount obtained, that was the actual loss to the bank ($14,731). The Fifth Circuit reasoned that because the appellant proffered as genuine a check in the full amount (although he obtained only a portion of that amount for himself) he "put the victims at risk for the full loss," making the act "much more akin to theft than to obtaining a loan fraudulently." *Wimbish*, 980 F.2d at 312.

Helpline Report: Several Helpline calls have been received on this issue. This usually arises when there appears to be little or no loss, or loss does not reflect the seriousness of the offense.

Option:

(1) No amendment.

(2) Delete language on risk of loss that suggests that an upward departure may be appropriate in any false loan application case in which payments or collateral have significantly (or completely) eliminated the actual loss. To encourage an upward departure in such a run-of-the-mill case seems to contradict the rule on the determination of loss that credits payments and collateral, and encourage unwarranted disparity.

Recommendations of Outside Groups:

Criminal Law Committee: Risk of loss is a frequently occurring issue, and so the Commission should provide specific guidance rather than leaving it for departure. (p. 4)

Probation Officers' Advisory Group: No amendment pertaining to risk of loss is needed. (p. 2)

C. Miscellaneous

The Department of Justice recommends an amendment that would provide that where the fraud guideline applies to bribery or commercial bribery cases, "the loss is the greater of the amount of the bribe or kickback or the value of the benefit received or to be received in return for the payment." (p. 4)