

**PREPARED STATEMENT
of
MARK FLANAGAN
to the
UNITED STATES SENTENCING COMMISSION**

March 5, 1998 Public Hearing

Let me begin by thanking the Commission for extending to me an invitation to testify in the March 5, 1998 public hearing. I welcome the opportunity. I have closely followed the Commission's efforts this past year to clarify and to improve the definition of loss as used in the Theft and Fraud guidelines. The views expressed here are refinements of those presented in my article published last September in *The Legal Times*. I am appearing in my capacity as a member of the private defense bar.

Introduction

The Commission has proposed numerous amendments relating to the guidelines for Fraud and Theft, but, in my view, Proposed Amendment No. 4--the definition of "loss"--is by far the most critical. "Loss" is the bedrock upon which the guidelines for fraud and theft rest. Indeed, the calculation of a sentence begins with the calculation of loss. A fair and uniform application of the loss tables depends upon this concept.

Nonetheless, the current guidelines definition has no causation requirement, and places no true limit on the amount of damages for which a defendant can be held responsible. The guidelines all but eliminate the connection between a defendant's act, the effect of the defendant's act, and the defendant's punishment. There is no clear definition of loss, and as a result,

different courts use different approaches when measuring loss, and different defendants get different--and perhaps unjust--sentences.

The Commission's Proposed Amendment No. 4, as refined in its February 1998 Working Draft, goes a substantial way towards accomplishing the Commission's mission to promote uniform and just sentences. The first order of business, as reflected in these papers, must be to better define loss. The February Working Draft already captures much of what needs to be done, and in and of itself represents a remarkable improvement and many hours of hard work. My comments below are intended to emphasize the compelling need to go forward with the concepts embodied in the February Working Draft and to consider additional revisions to make it even better.

Within this context, I believe the Commission could markedly improve the definition of loss if it were to do the following: 1) Define and adopt, as proposed, a "reasonably foreseeable" causation standard; 2) Eliminate "intended loss" from the definition of loss, and use it only as a grounds for departure; 3) Eliminate, as proposed, consequential damages as a term used in the definition of loss, and predicate loss on the recovery of reasonably foreseeable damages only; and 4) Eliminate defendant's gain from the definition of loss, and use it only as a grounds for departure.

Add A Causation Element

The most serious flaw of the current definition is that there is no causation requirement. Under the current guidelines, loss can conceivably include *all* harm, no matter how remote, from the acts or omissions of a defendant. Section 1B1.3(a)(3) defines "harm" to include "all harm" resulting from a defendant's acts

or omissions, and the guidelines state that loss need not be determined with precision. This combination of holding a defendant responsible for "all harm" while at the same time applying a loose standard of proof does not promote fairness, uniformity, or proportionality in sentencing. A court may hold a defendant criminally responsible for losses that were, at best, remotely caused and unforeseen. But if a purpose of the guidelines is to deter a defendant's conduct, the defendant only should be held liable for the reasonably foreseeable results. The guidelines cannot justly deter conduct that has unforeseeable results.

That is why the single most important improvement offered by Proposed Amendment No. 4 and the February Working Draft definition of loss is the addition of the "reasonably foreseeable" standard. For the first time since the introduction of the U.S. Sentencing Guidelines, the Commission has proposed a recognizable link between a defendant's criminal conduct and the damages caused by that conduct. This causation standard puts coherent limits on the amount of harm attributable to a defendant. It will prevent such anomalous sentences as in United States v. Neadle, 72 F.3d 1104 (3rd Cir. 1996), where a defendant who had posted a \$750,000 bond to open an insurance company was held responsible \$20 million in unpaid property damage that resulted from a hurricane. The Court in Neadle imposed a sentence on the defendant without applying any causation standard whatsoever.

I strongly support the Commission's effort to define loss by introducing the "reasonably foreseeable" standard. But it must go a step further by defining "reasonably foreseeable;" if it does not, it will be left to the courts to define this causation standard and the results may vary. For example, the Commission

should consider adopting the definition offered by Professor Frank Bowman in his proposed definition of loss set forth in his law review article scheduled for publication this Spring. The definition defines "reasonably foreseeable" as harm that "ordinarily follows from one or more of the acts . . . in the usual course of events, or that a reasonable person in the position of the defendant would have foreseen as a probable result." Adopting such a definition will promote uniformity of interpretation.

Eliminate Intended Loss From Definition of Loss

Section § 2F1.1, Application Note 7(b) of the current guidelines specifies that "where the intended loss is greater than the actual loss, the intended loss is to be used," but nowhere in the guidelines is "intended loss" defined. I understand that use of "intended loss" is primarily meant to ensure that inchoate crimes are punished, but "intended loss" is an unnecessarily vague concept which seems to require a court to analyze a defendant's deepest thoughts on what the benefits of a particular crime might be. It is a complex and uncertain analysis, and depends not on evidence of what the defendant actually did, but what the defendant had hoped, thought, or dreamed of doing. It is time consuming, with no uniform result. It should be employed in limited circumstances only, not in the ordinary course.

Unfortunately, Proposed Amendment No. 4 and the February Working Draft definition retain "intended loss" as a key component. Both provide that loss is the "greater of the actual loss or the intended loss," thus requiring a court to contemplate intended loss in every case. Using "the greater of the actual loss or the intended loss" is unduly confusing because it requires the court to choose

between the objective standard of "reasonably foreseeable" and the subjective standard of "intended loss." While in a perfect world, with unlimited resources and time, it might be preferable for a court to always consider what intended loss might be, we do not live in such a world.

The solution is to remove "intended loss" from the definition of loss and to make it available as a possible grounds for an invited departure to cover those limited cases when a defendant's intended gain is so markedly different from the actual loss that a different punishment is warranted. In the ordinary case, though, the defendant should only be held responsible for the actual loss caused.

Eliminate Consequential Damages

The current guidelines single out procurement fraud and product substitution cases as the only cases where consequential damages are recoverable. The sole justification given for limiting consequential damages to these two types of cases is the summary and questionable assertion in § 2F1.1, Application Note 7(c), that such damages "frequently are substantial." Singling out these cases also implies that all other cases are limited to direct damages. The result is that there is confusion among the courts as to whether to include consequential damages.

The February Working Draft definition of loss resolves this issue. By adopting a "reasonably foreseeable" standard, the Commission has obviated the need to include the term consequential damages in the guidelines. Under the reasonably foreseeable standard, a defendant will be held liable for damages that are foreseeable. There is no need to attempt to apply a consequential damages analysis to determine if the damages are immediate and direct or indirect; include

only those damages that are reasonably foreseeable regardless of whether they are direct and immediate or indirect damages.

But for one caveat, I recommend that the Commission proceed with its proposal to eliminate the term consequential damages from the guidelines, and to use only the reasonably foreseeable standard. The caveat concerns the suggestion that costs incurred by government agencies in a criminal investigation or prosecution of a defendant routinely should be considered reasonably foreseeable damages. I disagree. The Commission should consider adding language to the definition of reasonably foreseeable, as Professor Bowman has proposed in his article, to make it clear that loss does not include such costs.

Make Gain a Departure

The current guidelines seem to allow courts to use the offender's gain as the measure of loss instead of the victim's loss. See § 2F1.1, Application Note 8. The February Working Draft definition of loss expressly incorporates gain as a factor in the determination of loss. The Commission should not include gain in the definition of loss because it muddles the calculation of loss. To simplify and to promote clarity and uniformity, the Commission should focus only on the harm to the victim when determining loss. For those unusual cases when the loss does not reflect the seriousness of the offense, or when gain is vastly lower than the actual loss, the Commission should propose language to invite an upward or downward departure. For example, a defendant who is only a pawn or functionary--like an employee of a corporate defendant in a complex white collar case--may gain little or none of what the victim has lost. In such cases, it may well be unfair to sentence the individual based on actual loss.

Conclusion

My colleague, Will O'Brien, and I focused on the proposed amendments to the Theft and Fraud Guidelines when we realized that the Commission was considering amending the loss tables without correcting the defects in the definition of loss. Since then, various groups from a variety of sources have urged the Commission to tackle the tough issue of defining loss either before or together with amending the loss tables. It is a tribute to the Commission that it has acted so swiftly to meet this challenge.