Apples and Oranges: Securities Market Losses Should Be Treated Differently for Major White-Collar Criminal Sentencing under the Federal Guidelines

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Apples and Oranges: Securities Market Losses Should Be Treated Differently for Major White-Collar Criminal Sentencing Under the Federal Guidelines

John D. Esterhay

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I. INTRODUCTION

On December 16, 2008, the United States District Court for the District of Connecticut sentenced Ronald E. Ferguson, CEO of Gen Re Corporation, on charges of conspiracy, securities fraud, and mail fraud for his role in orchestrating an illegal scheme that resulted in almost $600 million in market
decline of AIG Corporation's stock price. Despite the Federal Sentencing Guidelines (Guidelines) recommending life in prison for these crimes, the court sentenced Ferguson for two years. At sentencing, the court emphasized that Ferguson did not gain directly from this loss amount. Instead, this amount resulted from later marketplace transactions.

Ferguson’s direct responsibility involves the issue of market loss, a unique type of victim loss that a court calculates for sentencing purposes, which consists of losses third-party shareholders suffer, normally after revelation of the fraud. This Article will discuss how the victim loss amount influences the Guidelines for fraud under section 2B1.1 and how these Guidelines provide harsh imprisonment terms when loss amounts reach the hundreds of millions of dollars. Such dollar amounts are common when employing market loss. When the fraud becomes public knowledge, the price of a security listed on an efficient market quickly will incorporate the new information, causing a sharp decrease in the security's price. Because defendant responsibility is unclear with market loss, judges often are hesitant to apply severe Guideline sentences to such defendants, as was the case with Ferguson. Such hesitance creates disparities between judges who apply the Guidelines, and those judges who do not. This Article will examine these problems and how they result from a failure to differentiate market loss from direct loss.

Part II analyzes the history of market loss, a calculation of loss that arose as a damage calculation in private plaintiff civil securities fraud actions. This Part describes the evolving theory of loss causation in order to understand the foundation for market loss at criminal sentencing. This Part also explains how market loss might have been used in sentencing before the Guidelines.

After the codification of the Guidelines, victim loss became the official driving factor in fraud sentencing. Thus, Part III examines the loss table and how a large loss finding leads to a long prison term recommendation. Because the court must calculate victim loss to adhere to the Guidelines, courts determine market loss in a manner similar to previous civil securities fraud cases. Part III also analyzes the subsequent developments in federal court.

2. Esterhay, supra note 1, at 170-71.
3. Id. at 170.
4. Transcript of Sentencing at 102-03, Ferguson, 584 F. Supp. 2d 447 (No. 06-137).
5. Id.
7. Id. at 1152.
8. Id. at 1149.
Part IV argues that market loss is inappropriate for criminal sentencing in its current form, because it differs from direct victim loss due to weaker causation. A defendant might be civilly liable for market loss, but he is not responsible for that loss in the way that criminal sentencing should require. Loss causation, even if sufficient in civil cases, should be afforded special treatment for sentencing purposes.

Part V presents a solution in which market loss punishes the defendant less severely than direct loss because of the weaker causal link. Adopting a parallel loss table for market loss can accomplish this differentiation. Such an amendment to the Guidelines would help solve the problems this Article identifies.

II. THE CIVIL DAMAGES ORIGINS OF MARKET LOSS AT SENTENCING

Before the adoption of the Guidelines, courts were not required to precisely define loss for criminal sentencing. Consequently, courts first developed the theory of market loss for civil securities fraud cases and later applied it to sentencing. While courts now use market loss in any type of fraud case, the history of civil securities fraud continues to resonate in criminal sentencing.9

A. Securities Fraud in Private 10b-5 Actions

In response to the 1929 stock market crash and subsequent Great Depression, Congress enacted the Securities Act of 1933 ('33 Act) and the Securities Exchange Act of 1934 ('34 Act). Section 10(b) of the '34 Act authorized securities fraud enforcement pursuant to the Securities and Exchange Commission (SEC) Rule 10b-5, which states:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

9. See infra Part II.A.
(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.\textsuperscript{10}

Rule 10b-5 authorizes three enforcement mechanisms: "(1) criminal enforcement via prosecution by the U.S. Department of Justice (DOJ), (2) civil enforcement actions by the SEC, and (3) civil enforcement by private parties."\textsuperscript{11}

While criminal prosecution was an option from the beginning,\textsuperscript{12} neither Rule 10b-5 nor any statute contemplated civil enforcement by private parties.\textsuperscript{13}

After the SEC advocated for a private cause of action in an amicus brief,\textsuperscript{14} courts began endorsing this right in 1946.\textsuperscript{15} In 1971, the U.S. Supreme Court affirmed private 10b-5 enforcement.\textsuperscript{16} In the first few decades of securities lawsuits, private remedies were successful,\textsuperscript{17} mitigating the necessity for criminal prosecution.\textsuperscript{18} Additional procedural hurdles including a lack of resources in federal regulatory agencies like the SEC, complexity and difficulty of proof in major fraud cases combined with the lack of federal prosecutor security fraud expertise, the requirement for coordination and cooperation between the SEC and DOJ, and the SEC’s focus on civil actions further limited the incidence of criminal enforcement.\textsuperscript{19} Therefore, criminal securities fraud prosecutions did not begin to flourish until the civil doctrine was established.

\textbf{B. Victim Loss}

When private plaintiffs began filing securities fraud 10b-5 actions, courts had to develop a theory for calculating damages. The first question

\begin{itemize}
  \item \textsuperscript{10} 17 C.F.R. § 240.10b-5 (2010).
  \item \textsuperscript{11} McCormick, \textit{supra} note 6, at 1152.
  \item \textsuperscript{12} Id.
  \item \textsuperscript{13} See 15 U.S.C. § 78j(b) (2006 & Supp. IV 2010); 17 C.F.R. § 240.10b-5s; \textit{see also} Ernst & Ernst v. Hochfelder, 425 U.S. 185, 196 (1976) ("10(b) does not by its terms create an express civil remedy for its violation, and there is no indication that Congress, or the Commission when adopting Rule 10b-5, contemplated such a remedy").
  \item \textsuperscript{15} \textit{See} Kardon, 69 F. Supp. at 514; \textit{see also} William S. Feinstein, \textit{Pleading Securities Fraud with Particularly - Federal Rule of Civil Procedure 9(b) in the Rule 10-5 Context: Kowal v. MCI Communications Corporation}, 63 GEO. WASH. L. REV. 851, 854 (1995).
  \item \textsuperscript{16} Superintendent of Ins. v. Bankers Life & Cas. Co., 404 U.S. 6, 13 n.9 (1971).
  \item \textsuperscript{17} \textit{See} McCormick, \textit{supra} note 6, at 1154.
  \item \textsuperscript{18} \textit{See id.} at 1153, 1155.
  \item \textsuperscript{19} Id. at 1155-56.
\end{itemize}
MARKET LOSS IN WHITE-COLLAR SENTENCING

was whether damages should consist of loss to the plaintiff or gain to the defendant. While many frauds result in the defendant taking exactly what the plaintiff lost, in securities fraud, these amounts often diverge due to the attenuated nature of loss in a widely-held security. Courts decided that victim loss was the more appropriate figure for damages. Private plaintiff civil cases use victim loss as the amount for damages, because such claims arise as a remedy for losses the plaintiffs sustained. Secondly, from a practical standpoint, "causation is already built into civil securities fraud cases as a factor the plaintiff must prove in order to show liability." Neither of these characteristics hold true for criminal cases. Yet, courts adopted the civil remedy approach when first confronted with damages in criminal cases after the Guidelines endorsed victim loss as well.

C. Calculation Method

With market loss established as the benchmark for damages, civil courts were tasked with creating a method for calculating the loss in Rule 10b-5 cases. Many possible methods for calculating market loss exist, the advantages and disadvantages of which are beyond the scope of this Article. In early securities cases, courts could not reach consensus on the calculation

20. Id. at 1156 & n.70 (citing Kohler v. Kohler Co., 208 F. Supp. 808, 825 (E.D. Wis. 1962)).
21. See id. at 1150 ("When a bank robber steals $1000, there is little question in anyone's mind of the loss sustained by the robber's victims. Not surprisingly, the loss would be exactly equal to the actual gain of the robber: $1000.").
22. See, e.g., United States v. Snyder, 291 F.3d 1291, 1295 (11th Cir. 2002) (describing how the district court had calculated plaintiff loss and defendant gain to be $34.4 million and between $200,000 and $350,000 respectively).
23. McCormick, supra note 6, at 1156.
24. Id.
25. Id. at 1156-57.
26. See, e.g., United States v. Kopp, 951 F.2d 521, 536 (3d Cir. 1991) (reversing the district court for defining loss as the "amount fraudulently obtained [i.e. defendant gain], regardless of intended or actual loss"); United States v. Brach, 942 F.2d 141, 143 (2d Cir. 1991) (finding loss "is not restricted to the harm that a defendant intended to inflict [i.e. gain] but instead may consist of the 'probable' loss resulting from the fraud"); United States v. Hughes, 775 F. Supp. 348, 352 (E.D. Cal. 1991) (finding the law did not allow "courts to use a defendant's gross receipts generally in increasing the offense level" because "'[g]ross receipts' are not the same thing as 'loss'").
27. See U.S. SENTENCING GUIDELINES MANUAL § 2B1.1 cmt.3(B) (2010) ("The court shall use the gain that resulted from the offense as an alternative measure of loss only if there is a loss but it reasonably cannot be determined.").
28. See McCormick, supra note 6, at 1163-72 (describing each of the major market loss theories at work in securities fraud cases); see also Philip J. Leas, Note, The Measure of Damages in Rule 10b-5 Cases Involving Actively Traded Securities, 26 STAN. L. REV. 371, 371-85 (1974).
method, but courts began to gravitate toward the “out-of-pocket” calculation method because of its simplicity and its consistency with the common law understanding of damages. Ultimately, Congress enacted the 1995 Private Securities Litigation Reform Act (PSLRA), mandating that courts use the rescissory method, which attempts to make the “victim whole by restoring that person to the position he was in before the fraudulent transaction occurred,” in private 10b-5 civil actions. By that point, courts were applying multiple competing theories of civil damage calculations, and because the PSLRA does not concern loss calculations at sentencing, any of these theories – or even other new ones – could be available in the criminal context.

D. Causation

Once courts had settled on market loss and had created suitable calculative theories, the crucial issue of causation remained. In a private securities fraud action under Rule 10b-5, any stock purchaser or seller is a potential victim of the defendant’s fraud when the defendant’s actions have illegally manipulated the security’s price during a period of time including the victim’s transaction. For a widely-held security, this activity can result in countless victims, and each victim is a potential plaintiff. As a result, courts needed a way to differentiate instances where the defendant’s fraud caused the plaintiff’s loss from instances where opportunistic holders of the security were trying to profit through litigation arising from the disclosed fraud.

Early on, courts looked to the common law of torts for an answer, creating a definition of causation similar to the common law principle of proxim-

29. Leas, supra note 28, at 385.
30. Id. at 383-84 (“If anything is currently the rule of damages under 10b-5, it is the out-of-pocket award.”).
31. The theory defines damages as “the difference between the contract price, or the price paid, and the real or actual value at the date of the sale, together with such outlays as are attributable to the defendant's conduct.” Id. at 383 (quoting Estate Counseling Serv., Inc. v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 303 F.2d 527, 533 (10th Cir. 1962)).
33. McCormick, supra note 6, at 1164.
35. Id.
37. This fact follows directly from the text of Rule 10b-5: a scheme to defraud or material misstatement “in connection with the purchase or sale of any security” comprises a violation, so any purchase or sale tainted by that fraud will constitute a distinct cause of action. Id.
38. See, e.g., List v. Fashion Park, Inc. 340 F.2d 457, 462-63 (2d Cir. 1965) (citing RESTATEMENT (FIRST) OF TORTS §§ 546 & 538(2)(a) (1938) for definitions of reliance and materiality in adopting the common law rule of affirmative misrepresen-
The Restatement of Torts defines proximate cause in situations involving securities as follows:

[O]ne who misrepresents the financial condition of a corporation in order to sell its stock will become liable to a purchaser who relies upon the misinformation for the loss that he sustains when the facts as to the finances of the corporation become generally known and as a result the value of the shares is depreciated on the market, because that is the obviously foreseeable result of the facts misrepresented. On the other hand, there is no liability when the value of the stock goes down after the sale, not in any way because of the misrepresented financial condition, but as a result of some subsequent event that has no connection with or relation to its financial condition. There is, for example, no liability when the shares go down because of the sudden death of the corporation’s leading officers. Although the misrepresentation has in fact caused the loss, since it has induced the purchase without which the loss would have occurred, it is not a legal cause of the loss for which the maker is responsible. 40

Courts identified two distinct types of causation at work in securities fraud cases: 41 transaction causation – otherwise known as reliance 42 – and loss causation, which requires a showing “that the untruth was in some reasonably direct, or proximate, way responsible” for the plaintiff’s loss. 43 In other words, a plaintiff proves transaction causation by showing that the defendant’s fraud caused the plaintiff to engage in the transaction in the first place. Once a plaintiff establishes transaction causation, that plaintiff proves loss

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41. See Schlick v. Penn-Dixie Cement Corp., 507 F.2d 374, 380 (2d Cir. 1974); Fox, supra note 38, at 836; Zweifach, supra note 39, at 332.

42. Schlick, 507 F.2d at 380 (“to show transaction causation a plaintiff must demonstrate that he relied on the misrepresentations in question when he entered into the transaction which caused him harm”); Fox, supra note 38, at 840 (“Transaction causation, as we have seen, involves a showing that the plaintiff would not have purchased but for the misstatement. Thus, transaction causation is just another name for traditional reliance.”).

causation by showing that the defendant’s fraud caused him or her to incur actual economic damages.44

1. Transaction Causation

Transaction causation seems impossible to prove in a situation where purchasers or sellers of the securities might not be aware of the defendant’s fraudulent actions. But, in the 1988 case Basic, Inc. v. Levinson,45 the U.S. Supreme Court bypassed the reliance requirement with the “fraud-on-the-market” theory.46 “This theory substitutes for reliance a rebuttable presumption that the securities markets relied on a material misrepresentation made by the company in question and that the misled investor relied on the market; in essence, reliance is reflected in the market price of the securities.”47 The “fraud-on-the-market” theory presupposes that the price of the security on a public market reflects the defendant’s fraud.48 Thus, absent a defendant introducing evidence to rebut the presumption, plaintiffs need not show that the fraud caused their transaction.

2. Loss Causation

Despite Basic’s guidance on transaction causation, courts continue to struggle with the loss causation doctrine, even after the PSLRA codified it in statute.49 Loss causation is linked to the security price, and hence, the theory of damage calculation, because loss causation involves “a showing by the plaintiff that the purchased security declined in value from what was paid or was sold at a loss and that the decline or loss is in some way reasonably relat-

44. See Schlick, 507 F.2d at 380; Zweifach, supra note 39, at 332-33.
45. 485 U.S. 224, 243-44 (1988) (“The modern securities markets, literally involving millions of shares changing hands daily, differ from the face-to-face transactions contemplated by early fraud cases, and our understanding of Rule 10b-5’s reliance requirement must encompass these differences.”).
46. Fox, supra note 38, at 840 (“If courts were seriously to impose a transaction causation requirement in fraud-on-the-market cases, they would be acting in direct contradiction to Basic. The whole purpose of Basic was to provide the purchaser in the secondary trading markets, for whom demonstrating traditional reliance would be an unrealistic evidentiary burden, an alternative way to demonstrate the causal connection between a defendant’s misrepresentation and her injury.”).
47. Feinstein, supra note 15, at 862.
48. Id. at 862-63.
ed to" the defendant's fraud. Determining how much the defendant's fraud or other factors caused the alteration in price is complex. Though the differing calculative theories attempt to provide some guidance, the question remains difficult.

In the 2005 case Dura Pharmaceuticals, Inc. v. Broudo, the U.S. Supreme Court held that, in interpreting the PSLRA, "an inflated purchase price will not itself constitute or proximately cause the relevant economic loss." The Court astutely noted that

Given the tangle of factors affecting price, the most logic alone permits us to say is that the higher purchase price will sometimes play a role in bringing about a future loss. It may prove to be a necessary condition of any such loss, and in that sense one might say that the inflated purchase price suggests that the misrepresentation (using language the Ninth Circuit used) "touches upon" a later economic loss. But, even if that is so, it is insufficient. To "touch upon" a loss is not to cause a loss, and it is the latter that the law requires.

Although Dura is an important step toward delineating loss causation, it is a narrow holding and leaves many questions unanswered, questions that future courts likely will address in private plaintiff 10b-5 cases. Part IV discusses criminal courts' responses to Dura, but first, we must examine how market loss made the jump from private plaintiff 10b-5 actions to sentencing criminal defendants.

E. Pre-Guidelines Market Loss in Sentencing

Because of the Guidelines, reduction in securities price plays a central role in determining the defendant's accountability for loss, as Part III discusses, but as Rule 10b-5 criminal prosecutions of securities fraud ramped up in the early 1980s, courts had to consider factors like victim loss at sentencing. Pre-Guidelines sentencing was indeterminate, and thus judges rarely noted their reasoning through written opinions.

50. Fox, supra note 38, at 842.
51. See McCormick, supra note 6, at 1163-64.
53. Id. at 342.
54. Id. at 343 (emphasis removed) (citations omitted).
55. See Fox, supra note 38, at 846-47.
56. See McCormick, supra note 6, at 1158.
57. The Federal Sentencing Guidelines were enacted in part to end this indeterminacy. See S. REP. No. 98-225, at 40 (1984), reprinted in 1984 U.S.C.C.A.N. 3182, 3223 ("The sentencing provisions of current law were originally based on a rehabilitation model in which the sentencing judge was expected to sentence a defendant to a
Michael Milken was the most famous criminal from the savings-and-loan frauds of the 1980s. While the Guidelines had been implemented prior to Milken’s sentencing, Milken’s conduct had occurred before their implementation, and thus he received “the last of the great pre-guidelines sentences.” Consequently, his sentence provides insight into the use of market loss before the Guidelines.

Judge Kimba Wood sentenced Milken to ten years in prison, which was more than the Guidelines would have provided and was unprecedented in severity for a white-collar crime. In doing so, Judge Wood relied on Milken’s role in obliterating substantial capital in the securities markets. Judge Wood ordered Milken to pay $600 million in restitution and fines. Yet, Judge Wood did not reference a calculation that led to that number. Only the newly-implemented Federal Sentencing Guidelines would require such calculations.

III. THE FEDERAL SENTENCING GUIDELINES AND EVOLUTION IN CRIMINAL CASES

A. The Guidelines

The Guidelines require courts to calculate loss, including market loss, leading to the indispensable role of market loss at sentencing. Congress created the U.S. Sentencing Commission in 1984 in response to perceived inequities in sentencing, particularly in major white-collar crime. Congress
MARKET LOSS IN WHITE-COLLAR SENTENCING

In their original form, the Guidelines were mandatory, requiring federal district court judges to sentence defendants according to specified parameters with little variation. As is often the case with significant Congressional action, a national disaster provided the catalyst for major legislative intervention. The ongoing savings-and-loan crisis of the 1980s generated much of the impetus for increased white-collar criminal penalties.

In addition to expanding potential sentences for white-collar crime beyond pre-Guideline levels, the Sentencing Commission identified economic “loss” as the most significant factor in pre-Guideline sentences for fraud and created a “Loss Table” providing for escalating punishment alongside increasing levels of loss. Like quantity of drugs in narcotics cases, loss is the dominant factor in white-collar sentencing under the Guidelines. While

74. Compare id. § 2D1.1(c) (providing a base offense level anywhere from 6 to 38 based on drug quantity), with id. § 2B1.1(b)(1) (providing an enhancement to offense level anywhere from 0 to 30 based on dollar loss amount).

75. To demonstrate, a recommendation for a first-time offender, even when considering only base offense level and loss amount under the fraud Guideline, can range from total offense level 6 to 37, id. § 2B1.1, which yields a guideline-range minimum
creating a navigable loss table may be easy, defining and determining economic loss in a meaningful way for large-scale fraud has proven difficult. Until the Sarbanes-Oxley Act of 2002,\textsuperscript{76} the Commission issued amendments clarifying this term almost annually in an attempt to provide direction to district courts applying the Guidelines.\textsuperscript{77} To illustrate, older Guidelines pronounced that

\begin{quote}
[T]he loss need not be determined with precision. The court need only make a reasonable estimate of the loss, given the available information. This estimate, for example, may be based upon the approximate number of victims and the average loss to each victim, or on more general factors such as the scope and duration of the offense.\textsuperscript{78}
\end{quote}

Meanwhile, the 2009 Guidelines contain the following statements toward the same end:

\begin{quote}
Estimation of Loss. – The court need only make a reasonable estimate of the loss. The sentencing judge is in a unique position to assess the evidence and estimate the loss based upon that evidence. For this reason, the court’s loss determination is entitled to appropriate deference. See 18 U.S.C. § 37421 and (f).

The estimate of the loss shall be based on available information, taking into account, as appropriate and practicable under the circumstances, factors such as the following:

(i) The fair market value of the property unlawfully taken, copied, or destroyed; or, if the fair market value is impracticable to determine or inadequately measures the harm, the cost to the victim of replacing that property.

(ii) In the case of proprietary information (e.g., trade secrets), the cost of developing that information or the reduction in the value of that information that resulted from the offense.

(iii) The cost of repairs to damaged property.
\end{quote}
(iv) The approximate number of victims multiplied by the average loss to each victim.

(v) The reduction that resulted from the offense in the value of equity securities or other corporate assets.

(vi) More general factors, such as the scope and duration of the offense and revenues generated by similar operations.79

As new situations emerged with each prosecution, the Commission struggled to keep the definition of loss appropriate for every case.

B. Federal Courts’ Calculations of Loss

Of course, individual federal court decisions regarding loss definition are where the Guidelines are applied to individual defendants, and much of the evolution in this area of the Guidelines was in response to key rulings on calculating economic loss. As noted in Part II.E, some courts probably used reduction in stock price to aid in pre-Guidelines sentence determination, but this exercise became crucial only when the Guidelines identified “loss” as the appropriate factor to drive ever-increasing terms of imprisonment. After the inception of the Guidelines, courts needed to have specific, defensible, and precise calculations of loss for purposes of the loss table. The use of reduction in stock price was, therefore, transformed from a factor that received general consideration to a carefully-constructed calculation in any case where issues of reduction in stock price were present. The Guideline comment highlighted above that codified the usage of reduction in stock price for loss determination80 was added in 2003 following the passage of Sarbanes-Oxley,81 but by then courts had been applying similar reasoning in prior cases to the point where such calculations had become routine.

Even so, courts differed in how rigorously they defined market loss for sentencing purposes. Early in the Guidelines’ history, not all courts found reduction in the price of securities to be an appropriate measure of loss under the fraud Guideline. In United States v. Bertoli, a 1994 ruling, the District of New Jersey declined to calculate this loss in applying the Guidelines following a prosecution and trial on RICO charges82 that included fraud in the form...
of stock sold through manipulative techniques to increase artificially the price on the market leading to an eventual crash and significant loss to investors.\textsuperscript{83} The court decided that because “the victims of the Stock Manipulation Schemes were the investors who purchased the stock on the public market, as well as the entire marketplace . . . it would be impossible to precisely quantify the total loss to the investing public.”\textsuperscript{84} Instead, the court relied on defendant’s gains from the scheme, as courts typically do when victim loss is truly impossible to calculate.\textsuperscript{85}

However, courts abandoned such cursory conclusions as the evolution of loss under the fraud Guidelines continued, because in situations involving market loss resulting from reduction in stock price, the courts can estimate the impact on the victims. For instance, in \textit{Bertoli}, the government identified forty brokers and investors who suffered loss from the scheme, but the court dismissed the value of such an exercise.\textsuperscript{86} Nevertheless, as identified above, the Guidelines assert that a reasonable estimate will suffice, and courts caught on, often looking toward developments in civil damages calculations for answers.\textsuperscript{87}

Courts follow civil damage calculation theory where the criminal prosecution arises from security fraud violations of Rule 10b-5 since a direct civil analog for damages calculation from market loss exists.\textsuperscript{88} In fact, in 10b-5 cases with corresponding civil suits, the court can refer to loss analysis conducted in the civil proceeding. This tactic can be useful because of the complexity of loss calculations and “the greater precision required in civil loss causation.”\textsuperscript{89} In \textit{United States v. Moskowitz}, the Second Circuit affirmed a securities price-reduction loss calculation from the Southern District of New York because “[t]he district court also had an analysis from the class action

\begin{itemize}
\item \textsuperscript{83} \textit{Id.}
\item \textsuperscript{84} \textit{Id. at} 1147-48.
\item \textsuperscript{85} \textit{Id.} (citing \textit{United States v. Badaracco}, 954 F.2d 928, 937 (3d Cir. 1992); \textit{United States v. Cherif}, 943 F.2d 692, 702 (7th Cir. 1991)) (both cases involving bank executives whose fraud only harmed their banks, and by extension, their banks’ investors)).
\item \textsuperscript{86} \textit{Id. at} 1148.
\item \textsuperscript{87} See, \textit{e.g.}, \textit{United States v. Olis}, 429 F.3d 540, 546 (5th Cir. 2005) (“Useful guidance appears in the applicable principles for recovery of civil damages for securities fraud.”); \textit{see also} McCormick, \textit{supra} note 6, at 1158.
\item \textsuperscript{88} See, \textit{e.g.}, \textit{United States v. Grabske}, 260 F. Supp. 2d 866, 874 (N.D. Cal. 2002) (“Since Congress believes the rescissory method is the best means of achieving uniformity and certainty in securities fraud civil cases, it follows that it is at least an appropriate method for criminal cases, where certainty and consistency are particularly important.”); \textit{see also} McCormick, \textit{supra} note 6, at 1163-72 (discussing theories of market loss deriving from civil cases).
\item \textsuperscript{89} \textit{Olis}, 429 F.3d at 547.
\end{itemize}
plaintiffs’ expert determining loss to the plaintiffs to be [higher than what the
district court eventually found.]”

The district court, however, performs its own market loss calculation,
although usually based on evidence and loss theories that are similar to evi-
dence and loss theories utilized in Rule 10b-5 civil cases. In some cases,
the sentencing court is able to rely on the presentence investigation report
when the calculation is not in dispute. Because several market loss theories
carry over from civil securities fraud actions, the district court must decide
which theory it will use. Congress passed the PSLRA in 1995, requiring
courts to use the recissory method for civil securities fraud damage calcula-
tions, but Congress did not provide a corresponding requirement for loss cal-
culation at sentencing. Nevertheless, some courts have found the PSLRA
persuasive in criminal settings. For instance, in the 2002 case United States
v. Grabske, the Northern District of California found that the PSLRA sug-
gested courts use the recissory method in 10b-5 criminal prosecutions.

Even courts that refrain from relying on the PSLRA have been moving
toward the recissory calculations. In United States v. Bakhit, the Central Dis-
trict of California used a modified recissory method incorporating the difference
between the average selling price of stock during the fraud and the aver-
age selling price after the fraud. This method was viable in Bakhit because
all outstanding stock was “purchased during the life of the fraud.” Meanwhile,
in United States v. Olis, the Fifth Circuit rejected the “oversimplified” non-recissory model the Southern District of Texas used at sentencing
and remanded for resentencing identifying with approval the “more nuanced

90. 215 F.3d 265, 272 (2d Cir. 2000) (per curiam).
91. The government always introduces its own expert in the criminal proceeding,
even if there was a parallel civil case, because relying on the plaintiff expert would
seem to run counter to the prosecutorial mandate to “do justice” and not simply cause
pecuniary harm. See, e.g., United States v. Grabske, 260 F. Supp. 2d 866, 873 (N.D.
Cal. 2002). Nevertheless, nothing prevents the defendant from using the same expert
as the plaintiff, and they often do so.
92. See, e.g., United States v. Hedges, 175 F.3d 1312, 1315 (11th Cir. 1999)
(affirming the district court’s market loss calculation where the court adopted the
PSI’s loss amount of $92 million and “[t]he only ‘evidence’ the district court relied on
to support its finding that [the defendant] was responsible for the entire loss was the
PSI’s conclusory statements that described his role in the conspiracy”).
93. See supra note 28 and accompanying text.
94. See supra notes 32-35 and accompanying text.
95. See Grabske, 260 F. Supp. 2d at 874.
96. 218 F. Supp. 2d 1232, 1241-42 (C.D. Cal. 2002); see also Grabske, 260 F.
Supp. 2d at 872 (discussing Bakhit’s calculation as “a form of the recissory method”).
97. Id. at 1242.
98. 429 F.3d 540 (5th Cir. 2005).
99. Id. at 547-49.
approach modeled upon loss causation principles," the Grabske and Bakhit courts used.100

While market loss theories originated in civil securities fraud lawsuits, prosecutions need not arise from Rule 10b-5 or any type of securities fraud to incorporate the same reasoning at sentencing. The fraud Guideline also covers larceny, embezzlement, property damage, forgery, and general theft,101 providing sentencing levels for almost 100 criminal statutes.102 Any criminal violation that causes harm to a corporation with outstanding stock can involve securities price reduction as a factor at sentencing if the harm were substantial enough to cause such a reduction. The Eleventh Circuit dealt with such a case in United States v. Snyder,103 where the defendants falsified data from clinical drug studies, causing the stock price to be inflated fraudulently due to a misplaced expectation by investors that the Food and Drug Administration would approve the product.104 In Snyder, the Northern District of Alabama found that calculating victim loss was not feasible due to the nature of the loss, despite the fact that the government's expert testified that the defendant destroyed approximately $34.4 million in stock value.105 Instead, the court sentenced the defendant based on intended gain, which it found to be between $200,000 and $350,000.106 After the government appealed, the Eleventh Circuit rejected the district court's approach, remanding for calculation of market loss.107 Like the Fifth Circuit in Olis,108 however, the appeals court was careful to emphasize that the calculation method should be sophisticated enough to incorporate principles of loss causation; namely, not all shareholders suffer a loss when the stock has value after the fraud.109

Interestingly, in Olis, the Fifth Circuit relied on Snyder in its rejection of the district court's original calculation,110 but on remand, the Southern District of Texas went through an exhaustive analysis of market loss calculation theories111 and decided that "it [was] not possible to estimate with any degree of reasonable certainty the actual loss to shareholders attributable" to the de-

100. Id. at 547.
102. Id. cmt. Statutory Provisions.
103. 291 F.3d 1291 (11th Cir. 2002).
104. Id. at 1293.
105. Id. at 1295.
106. Id.
107. Id. at 1296.
108. United States v. Olis, 429 F.3d 540, 547 (5th Cir. 2005) ("[B]ecause a company's stock price is affected before and after the fraud, by numerous extrinsic market influences as well as the soundness of other business decisions by the company, the calculation of loss attributable to securities fraud requires careful analysis.").
109. Snyder, 291 F.3d at 1296.
110. Olis, 429 F.3d at 547.
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fendant.112 Two characteristics, however, distinguish the Otis resentencing from the Snyder sentencing. First, the Otis court conducted a thorough inquiry into market loss factors rather than giving up at the outset;113 and second, the court found the defendant responsible for $79 million in intended losses to the U.S. Treasury through fraudulent accounting for tax purposes, which was close to the lower end of the original $161 million calculation.114 Despite these differences, both Otis and Snyder demonstrate the difficulties extant at the district and appellate level in market loss sentencing calculations.

Thus, the U.S. Sentencing Commission’s 2003 amendment to the fraud Guideline, section 2B1.1, endorsing the usage of reduction in value of securities or other corporate assets,115 was not revolutionary when compared to past federal court practices. The amendment came after directives in the 2002 Sarbanes-Oxley Act required the Commission to review and update the Guidelines for major white-collar crimes,116 although the legislation did not demand the inclusion of stock value reduction language in the fraud Guideline.117 Sarbanes-Oxley was a result of the Enron-WorldCom accounting scandals of 2001-2002,118 prompting the Commission to expand the loss definition. Unfortunately the Commission “publish[es] amendments with little or no explanation of their rationale or intended effect . . . leaving the community of guidelines users – lawyers, probation officers, and judges – to speculate about why the rules ha[ve] changed.”119 In this instance, the Commission acknowledged without any further description that the comment “was added to provide courts additional guidance in determining loss in certain cases, particularly in complex white collar cases.”120 Given this history, the Commission appears to have been encouraging what most courts were doing already.

A more dramatic development in federal sentencing was the 2005 case United States v. Booker, which turned the mandatory sentencing Guideline

112. Id. at *9.
113. Id. ("The court’s conclusion that it is not possible to estimate with reasonable certainty the actual loss to shareholders attributable to corrective disclosures about Project Alpha is based on the facts of this case; it is not a conclusion that such estimates are never possible.").
114. Id. at *9-10.
116. See supra notes 80-81 and accompanying text.
118. Esterhay, supra note 1, at 137-38.
regime into an advisory system. Booker turned a loss table that the Guidelines required federal district court judges to use in setting white-collar sentences into a loss table that the Guidelines required district court judges to calculate but not necessarily follow. The freedom of judges to ignore the loss table has exacerbated problems with using securities price reduction to set sentences.

IV. CURRENT PROBLEMS WITH SECURITIES PRICE REDUCTION AS LOSS

While the potential for error in market loss calculation is obvious, the most troubling aspect of incorporating securities price into loss-related sentencing is the issue of causation. Why should a corporate executive who benefits tangentially from a perpetrated fraud be responsible for the entire amount of any eventual loss in the securities market? Can the executive cause such loss by any reasonable understanding of causation? In United States v. Snyder, Judge James Hill of the Eleventh Circuit wrote a concurring opinion which highlights the rationale and the underlying difficulty with using market loss at sentencing:


In addition, a subsequent line of cases have clarified U.S. Supreme Court opinions on sentencing. See Gall v. United States, 552 U.S. 38, 51 (2007) (holding appellate courts may not presume a non-Guideline sentence is unreasonable); Kimbrough v. United States, 552 U.S. 85, 89, 111 (2007) (holding district courts may impose non-Guideline sentences, even if their reasoning for doing so is based on substantive policy disagreements with the Guidelines, and not specific defendant characteristics); Rita v. United States, 551 U.S. 338, 347 (2007) (holding appellate courts may presume within-Guideline sentences are reasonable). Thus this Article will not cover issues with appellate review of sentence reasonableness in any detail.

122. One other article has been written on the usage of market loss in sentencing for corporate fraud, see McCormick, supra note 6, and it focuses primarily on practical concerns like calculation complexity and effect on the markets. See id. at 1173-76. Such issues are crucial to address, but this Article focuses on theoretical problems surrounding causation.
The type of crime committed here tends to provide a relatively small and certain amount of expected gain to defendants and a far larger and less certain loss to innocent investors throughout the market. Here the perpetrators seek something of value for themselves with reckless disregard for their faceless victims. The extent of their wrongdoing will usually greatly exceed what they hoped to derive from their nefarious conduct.

The district court, looking at the defendants' expected gain, concluded that for sentencing purposes, the amount of loss attributable to the defendants was between $200,000 and $350,000. The government's expert concludes that the loss impact upon investors was $34.4 million! The great difference in the two figures describes and defines the callousness of defendants who, in order to obtain relatively little, acted in utter disregard of the vast financial loss consequence they inflicted on so many. It is not appropriate therefore to limit sentencing consequences to defendants' gain, thereby ignoring victims' loss.

Of course, the estimated loss must not be based upon pure guesswork or speculation. If however, there is a good basis for a reasonable estimate, the sentencing court should tend to overlook fine-tuned objections demanding precise dollar and cent calculations of loss.123 Judge Hill is correct on both accounts. In market loss cases, sentencing defendants solely based on their limited gains is inappropriate, but sentencing defendants for loss they are not responsible for also is inappropriate. When dealing with astronomical numbers, it can be difficult to identify loss beyond "pure guesswork or speculation."124

In sentencing Ronald Ferguson to two years in prison despite his lifetime Guidelines for conduct resulting in a $600 million market loss,125 Judge Christopher Droney of the District of Connecticut went one step further, emphasizing the absence of a link between gain to the defendant and loss to the victims:

Another factor here that is different from so many other corporate fraud prosecutions is that Mr. Ferguson did not personally gain in a direct way from his criminal conduct, and his motivation was not one of obtaining direct personal gain. That certainly does not excuse his conduct and perhaps does not warrant a departure from the

123. United States v. Snyder, 291 F.3d 1291, 1296-97 (11th Cir. 2002) (Hill, J., concurring) (internal citation omitted).
124. Id. at 1297.
125. See supra notes 1-5 and accompanying text.
offense level under the Sentencing Guidelines. But, surely, it is relevant under the federal sentencing statute. Unlike so many other recent stock market fraud cases, there was no motivation of direct personal profit. There was substantial loss caused to AIG stockholders here, over 500 million dollars, and Mr. Ferguson surely was aware of how harmful his conduct could be to the integrity of the market, but his intent was different from the usual fraud defendant, which is to make money personally and directly from the illegal conduct.126

Judge Droney’s concern in imputing so much financial loss to the defendant is well-founded, but his conclusion that Ferguson’s case is “different from so many other corporate fraud prosecutions”127 is unwarranted. Ferguson is identical to the other cases discussed, but few judges have focused on the dilemma inherent in these cases. Judge Droney misses the mark when he says that “Ferguson did not personally gain in a direct way from his criminal conduct, and his motivation was not one of obtaining direct personal gain.”128 Ferguson benefited in some way, likely through executive compensation tied to performance of the company, or through additional business opportunities for himself.129 However, this case and other cases like it present an issue that few judges other than Judges Hill and Droney have addressed head-on.

Loss is defined in the commentary as “the greater of actual loss or intended loss.”130 “‘Actual loss’ means the reasonably foreseeable pecuniary harm that resulted from the offense”131 while “‘[i]ntended loss’ [...] means the pecuniary harm that was intended to result from the offense.”132 Intended loss is irrelevant in these cases because market loss is calculating real “reduction that resulted from the offense in the value of equity securities or other

127. Id.
128. Id.
129. See Government’s Response to Defendant Ronald E. Ferguson’s Sentencing Memorandum at 25, United States v. Ferguson, 584 F. Supp. 2d 447 (D. Conn. 2008) (No. 06-137), 2008 WL 4360457 (“Moreover, Ferguson’s motivations here were not altruistic. As set forth above, he was able to pull in $5 million for Gen Re and was able to ingratiate himself with his largest client and its CEO, something extremely important for Ferguson and Gen Re.”) (citations omitted).
130. U.S. SENTENCING GUIDELINES MANUAL § 2B1.1 cmt. 3(A) (2010). Loss is, curiously, neither reviewed by Congress nor given the same precedential weight as the text of the Guidelines. See Stinson v. United States, 508 U.S. 36, 37-40 (1993) (holding that the commentary to the Guidelines is authoritative unless it violates the Constitution or a federal statute, or is inconsistent with, or a plainly erroneous reading of, that Guideline).
132. Id. cmt. 3(A)(ii).
corporate assets.\textsuperscript{133} So, the pertinent definition of loss is the reasonably foreseeable harm that resulted from the offense. This definition raises more questions than answers, though. First, what does it mean that the loss resulted from the offense? Is this requirement the same as civil loss causation? Second, is any market reaction to fraud ever reasonably foreseeable? The following sections address these two questions.

### A. Civil Causation Should Be the Bare Minimum for Criminal Sentencing

The previous two Parts explained that the methodology for using reduction in securities pricing as a loss factor at sentencing has its origins in private 10b-5 securities fraud actions and takes important cues from the civil fraud landscape. But judges in criminal proceedings, while acknowledging their use of civil fraud concepts, rarely opine on the appropriateness of applying such concepts to criminal sentencing. Due process is a sacred value in American criminal proceedings,\textsuperscript{134} and consequently loss causation should have a more limited definition when judges apply it at sentencing.

As a threshold matter, the government needs to prove the facts at sentencing only by a “preponderance of the evidence,”\textsuperscript{135} the same standard of proof used in civil proceedings. Judges can rely on conduct for which the defendant was acquitted at trial under the standard of “beyond a reasonable doubt,” due to the different evidentiary burden.\textsuperscript{136} Use of the same standard of proof may seem to imply that courts should use the same theories of causation. However, this conclusion ignores the divergent goals of private enforcement and criminal prosecution. Private 10b-5 securities fraud actions allocate damages in order to “return... the injured party to the position he occupied before he was induced by wrongful conduct to enter the transaction.”\textsuperscript{137} Meanwhile, calculating market loss in criminal cases satisfies the statutory considerations for sentencing, including the nature of the offense,\textsuperscript{138} the need for just punishment,\textsuperscript{139} adequate deterrence,\textsuperscript{140} and safety of the pub-

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\textsuperscript{133} Id. cmt. 3(C)(v).
\textsuperscript{135} See Harris v. United States, 536 U.S. 545, 559-60 (2002) (plurality opinion) (reaffirming that a judge may sentence an individual within the Guidelines range under a preponderance of the evidence standard).
\textsuperscript{137} United States v. Grabske, 260 F. Supp. 2d 866, 872 (N.D. Cal. 2002).
\textsuperscript{139} Id. § 3553(a)(2)(A).
\textsuperscript{140} Id. § 3553(a)(2)(B).
lic, among other factors. Judge Hill was correct to note that loss to victims is the appropriate quantity for gauging offense seriousness, but in situations with substantial causal ambiguity like securities fraud, courts should not necessarily calculate market loss with the exact same methodology as in civil cases. The criminal courts' reactions to the U.S. Supreme Court's decisions in Basic and Dura, and Congress's intervention with the PSLRA, provide examples of how criminal courts incorporate developments in civil market loss calculation.

1. Basic's Fraud-on-the-Market Should Not Apply at Criminal Sentencing

Part II.D.1 described how the Supreme Court in Basic adopted fraud-on-the-market to eliminate the requirement of transaction causation. While the Court's adoption of a "rebuttable presumption of reliance" makes sense in a civil case where the goal for plaintiffs is to recoup their losses, in a criminal case the justification is less clear. First, victims are not parties in criminal prosecutions, so a defendant will have more difficulty attacking individual plaintiffs' arguments for reliance in order to overcome the presumption. Second, Basic's reasoning and holding was limited to private 10b-5 securities fraud actions, while courts can employ market loss under the Guidelines for any crime sentenced under section 2B1.1. Finally, based on the distinctions between the purposes of sentencing and civil claims, causation should be a stricter requirement when calculating loss for the Guidelines. In order to label the defendant as criminally responsible for conduct, the defendant should have caused the loss in a more concrete way than what fraud-on-the-market allows. Abolishing the transaction causation link does not make sense from a due process standpoint when the defendant's personal freedom is at stake.

Courts employ a cursory level of analysis at sentencing as indicated by the fact that only one court has even acknowledged that it adopted Basic's reasoning, despite the fact that almost all market loss calculations require it. In sentencing Bernie Ebbers for the WorldCom accounting fraud, the Second Circuit noted, "[T]he loss is that suffered by those investors who bought or held WorldCom stock during the fraud period either in express reliance on the accuracy of the financial statements or in reliance on what

141. Id. § 3553(a)(2)(C).
142. See generally id. § 3553(a).
143. See supra notes 45-48 and accompanying text.
145. Id. at 243-44.
146. See supra notes 101-02 and accompanying text.
147. See generally United States v. Ebbers, 458 F.3d 110, 112 (2d Cir. 2006).
148. Id. at 112.
Basic, Inc. v. Levinson described as the ‘integrity’ of the existing market price.” The court neither expounded on the distinction between proving these two types of loss nor provided any justification as to why the latter type should be incorporated.

Of course, from a practicality standpoint, abolishing fraud-on-the-market at sentencing would require an individual analysis of the history and motivations of each victim, eliminating market loss from consideration at sentencing. Perhaps market loss is appropriate to consider in a highly restricted and refined form to ensure that the defendant caused the loss. One would expect that civil loss causation would provide a baseline from which additional criminal protections are attached. Ironically, the opposite is true.

2. Civil Doctrine Should Apply to Criminal Market Loss Calculations

The PSLRA was Congress’s attempt to regulate private 10b-5 actions, and it provided some guidance on damage calculation, while Dura required plaintiffs in such cases to show more than price inflation in order to establish loss causation. Section I.2.D established that loss causation is a tricky concept in securities fraud actions with widely-held stock, and civil courts struggle with identifying the correct balance. Criminal courts have noted these issues as well, such as the difficulty in assessing what investor conduct would have been, absent the fraud, and the difficulty in establishing the underlying value of a stock. Thus, when Congress or the courts act to limit the definition in civil actions, “considerations relevant to loss causation in a civil fraud case should . . . apply, at least as strongly, to a sentencing regime in which the amount of loss caused by a fraud is a critical determinant of the length of a defendant's sentence.” Shockingly, however, criminal defendants do not always get the benefit of developments in civil fraud, as courts’ responses to Dura show. While the Second Circuit and the Fifth Circuit have endorsed Dura in criminal sentencing, the Ninth Circuit rejected it, claiming that:

149. Id. at 126-27 (emphasis added).
150. See supra notes 32-35 and accompanying text.
151. See supra notes 52-55 and accompanying text.
152. Ebbers, 458 F.3d at 127.
153. United States v. Zolp, 479 F.3d 715, 719 (9th Cir. 2007) (“[T]he court may not assume that the loss inflicted equals the full pre-disclosure value of the stock; rather, the court must disentangle the underlying value of the stock, inflation of that value due to the fraud, and either inflation or deflation of that value due to unrelated causes.”).  
154. United States v. Rutkoske, 506 F.3d 170, 179 (2d Cir. 2007).
155. Id.
156. United States v. Olis, 429 F.3d 540, 546 (5th Cir. 2005).
In criminal sentencing, however, a court gauges the amount of loss caused, i.e., the harm that society as a whole suffered from the defendant's fraud. Whether and to what extent a particular individual suffered actual loss is not usually an important consideration in criminal fraud sentencing. Therefore, where the value of securities have been inflated by a defendant's fraud, the defendant may have caused aggregate loss to society in the amount of the fraud-induced overvaluation, even if various individual victims' respective losses cannot be precisely determined or linked to the fraud. As a result, the principle underlying the Dura Pharmaceuticals Court's reluctance to allow mere overvaluation as a basis for establishing loss is generally not present in the criminal sentencing context, and we are not persuaded that it would be appropriate to expand the Dura Pharmaceuticals rule to the criminal sentencing context.158

On its face, this argument is flawed. One can compare what the result would be for simpler crimes that use loss as the driving sentencing factor. It would be similar to tacking on lost wages to the amount stolen in a bank robbery where a teller is afraid to come to work the next day or adding against an extortionist the cost of the phone call communicating the threat. In any crime many types of "loss to society" occur, but some losses are too attenuated to apply to defendants under any reasonable understanding of causation. Civil securities fraud jurisprudence up to and including Dura has tried to define this boundary, and justifying why defendants in criminal prosecutions should receive less protection than defendants in civil cases is difficult.

This phenomenon is indicative of a broader problem, in that courts at criminal sentencing seem to take the loss calculation less seriously than they do for civil damages, although the situation seems to be changing for the better with more district courts issuing written findings on victim loss in securities fraud cases.159 Nevertheless, commentators universally perceive that "greater precision [is] required in civil loss causation,"160 because the Guidelines require only a "reasonable estimate."161 Again, determining why courts should conduct criminal proceedings exposing defendants to enormous terms of imprisonment with any less precision than civil proceedings is difficult.

158. Id. at 1044 (citation omitted).
160. Olis, 429 F.3d at 547.
161. U.S. SENTENCING GUIDELINES MANUAL § 2B1.1 cmt. 3(C) (2010).
B. Market Loss Is Not Reasonably Foreseeable as Required by the Guidelines

Loss causation touches upon issues extending beyond the scope of the Guidelines, but within the Guidelines, the requirement that the loss be reasonably foreseeable seems impossible to meet with market loss. The fraud Guideline, in commentary, states that, "'reasonably foreseeable pecuniary harm' means pecuniary harm that the defendant knew or, under the circumstances, reasonably should have known, was a potential result of the offense."¹⁶² In examining market loss for sentencing, courts occasionally cite this definition,¹⁶³ but no court has attempted to explain how eventual fluctuations in securities markets can be reasonably foreseeable at the time the defendant is committing the fraud. The factors that complicate loss causation such as volatility in the markets, unpredictable investors, and unknowable underlying stock value contribute to the impossibility of foreseeing market price response. Thus, reasonable foreseeability is similar to loss causation but limited in application to sentencing under the Guidelines, further solidifying the notion that civil loss causation should provide only the starting point for examination at sentencing.

One could argue that the defendant should know that some negative market response is possible from major fraudulent transactions on the open market, so courts should hold him responsible even if the exact harm is unknown. But the paradigmatic defendant for whom market loss is the main sentencing factor does not perpetrate the fraud with a potential drop in securities price in mind; like Ferguson, he is trying to benefit his company or its clients, personally profiting through the rewards of performing his job successfully. Such defendants deserve substantial punishment due to the seriousness of their offense, but the claim that market loss was reasonably foreseeable is untenable.

Because courts have not extracted reasonable foreseeability from general loss causation, no decisions address this topic, and defense attorneys have not picked up on it as a separate attack on Guidelines loss calculations.¹⁶⁴ Nevertheless, many market loss sentences could be assailable on these grounds. No matter what, "'[g]iven the potentially draconian sentences that can be meted out in securities fraud prosecutions, it can be expected that the role of loss causation in criminal sentencing proceedings will continue to be vigorously contested by the government and the criminal defense bar.'"¹⁶⁵

¹⁶². Id. cmt. 3(A)(iv).
¹⁶³. See, e.g., Ferguson, 584 F. Supp. 2d at 450-51; Olis, 2006 WL 2716048, at *3.
¹⁶⁴. None of the defendant briefs or sentencing memos for any of the cases cited in this Article contain an argument that loss was not reasonably foreseeable.
¹⁶⁵. Zweifach, supra note 39, at 341.
C. United States v. Booker

The transformation of the Guidelines from mandatory to advisory in United States v. Booker is not by itself a problem for market loss sentencing. But when combined with the issues this Part discusses, Booker has and will continue to lead to enormous disparity in major white-collar sentencing where market loss is a factor. Major white-collar crimes have downward departure rates and magnitudes far above major "street" crimes, and many white-collar crimes with the highest Guideline ranges implicate market loss due to the loss numbers in the hundreds of millions or billions of dollars. Booker allows judges to depart downward based on whims, and the Government almost never appeals such departures. Additionally, at least one author posited that the increased discretion Booker affords might lead to longer sentences because "calculation of loss is a fairly defendant-unfriendly exercise." When courts do not have to apply rigorously the Guidelines and the various protections therein, the calculations could become sloppier. When confronted with a Ferguson-type defendant who gains only indirectly from his fraud through typical job-related perks, many judges will be tempted to depart downward based on Booker as Judge Droney did, rather than create a more relevant definition of loss. Different judges will find other loss quantities to substitute, as in the Olis case on remand. Still other judges will stick to the stratospheric Guideline range. The result is wide-ranging disparity without any meaningful evolution in the definition of market loss.

166. See Esterhay, supra note 1, at 152-65.

167. See U.S. SENTENCING GUIDELINES MANUAL § 2B1.1(b)(1). A sentence driven by market loss can easily result in a Guidelines recommendation of life in prison, because such loss is often well above $400 million, the maximum on the loss table, id. § 2B1.1(b)(1)(P), and price reduction for widely held securities will always have at least 250 victims, id. § 2B1.1(b)(2)(C). Adding the base offense level of 7, id. § 2B1.1(a)(1), the resulting offense level is 43, which is a lifetime Guideline recommendation for even a first-time offender. Id. § 5A.


169. Gonzalez, supra note 121, at 185.

170. See generally id.


172. See supra notes 110-14 and accompanying text.

173. See, e.g., Esterhay, supra note 1, at 169-71 (comparing Ferguson, who received two years in prison, to a similarly-situated defendant, who received thirty years in prison).
As Judge Hill noted in Snyder, victim loss should not be ignored, but Booker allows judges to do so when they view high Guidelines as inappropriate for the defendant.

One could contend that the true culprit is not Booker but the notable extension of Guideline terms for major white-collar criminals, most recently with the passage of Sarbanes-Oxley. High Guidelines ranges lead to more disparity between judges who reject the Guidelines and those judges that accept them. But this argument ignores the Executive and Legislative branches’ stance that the instances of financial disaster in the last decade warrant more extreme penalties. The argument also ignores the differences judges might perceive between a Ferguson-type defendant, who does not benefit directly from his billion-dollar fraud and a Bernie Madoff-type defendant, who stole billions of dollars and is more deserving of a long prison term. While some judges might perceive this difference, the Guidelines do not. However, Congress could modify the Guidelines to account for this recognized distinction, and the next Part presents one way to do so.

V. A WORKABLE SOLUTION

The solution to the problems discussed supra is to draft a parallel loss table for market loss that enhances offense level less severely than the current loss table. As the previous discussion illustrates, loss related to stock price movement is different from any other type of victim loss, and the Guidelines should recognize this distinction. The different manner of loss corresponds to the distinction in culpability between defendants like Ferguson and Madoff. If loss occurs only through subsequent fluctuations in stock price on the market, then the causal link is weaker, and the defendant is less culpable. Because market losses occur as a result of market transactions, the defendant in such cases has no direct profit from or connection with the loss amount. Accordingly, Congress should modify the Guidelines to address this fact.

The high sentence ranges the Guidelines provide are appropriate for fraud where loss exists beyond the market. In Madoff’s case, the multi-billion dollar loss amount was staggering, but individual victims of Madoff’s scheme suffered this loss. Direct investment in Madoff’s fraudulent organ-

175. See Esterhay, supra note 1, at 139-152.
176. Id.
178. Id.
ization was the cause of their financial loss. His sentence of 150 years\textsuperscript{180} is not problematic because he is the type of defendant that courts should punish most severely. His offense is similar to simple theft, as he stole the money included in the loss calculation.

Meanwhile, Ferguson had no direct contact with the approximately $600 million in losses. These losses resulted from third-party transactions over an efficient securities market after the revelation of the fraud.\textsuperscript{181} The emphasis on issues of loss causation throughout this Article shows that causation is tenuous in such cases, and the defendant's responsibility for the loss is therefore more attenuated. The Guidelines should not treat such market loss equivalently to direct theft. Although the court based Ferguson's lenient sentencing in part on his exemplary character,\textsuperscript{182} it also identified the defendant's indirect connection to the loss.\textsuperscript{183} Such reasoning is warranted when the distinction between market loss and direct loss is accepted.

The unique character of market loss has been masked by its evolution at criminal sentencing, but it has roots in civil securities fraud and common tort law. Market loss should have a place at sentencing because criminal culpability must be classified based on victim loss, as Judge Hill observed.\textsuperscript{184} However, it should not provide the same level of prison term severity as directly established victim loss.

The most obvious solution is to create a separate corresponding loss table with less severe enhancements. The actual numbers should be based on study and debate at the U.S. Sentencing Commission, but for purposes of discussion, this Article provides the following as an amended loss table for the fraud Guideline:

Guideline range based on $13 billion in losses uncovered from the scheme up to that point).


\textsuperscript{181} See United States v. Ferguson, 584 F. Supp. 2d. 447, 453 (D. Conn. 2008) ("Davis' standard event study of February 14, 2005, March 14, 2005, and March 15, 2005 does result in a reasonable estimate of the loss between $544 million and $597 million. On each of these days, new and significant information related to the LPT fraud was disclosed, and there was a statistically significant price reaction in AIG's stock price.").

\textsuperscript{182} Transcript of Sentencing at 100-02, Ferguson, 584 F. Supp. 2d. 447 (No. 06-137).

\textsuperscript{183} See supra notes 126-29 and accompanying text.

\textsuperscript{184} United States v. Snyder, 291 F.3d 1291, 1297 (11th Cir. 2002) (Hill, J., concurring) (citation omitted).
§2B1.1

(b) Specific Offense Characteristics

(1) If the loss exceeded $5,000, apply the greater increase from (A) and (B) to offense level.

(A) For loss calculated from securities price changes in an exchange or other efficient securities market, increase the offense level as follows:

<table>
<thead>
<tr>
<th>Loss (Apply the Greatest)</th>
<th>Increase in Level</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) $1,000,000 or less</td>
<td>no increase</td>
</tr>
<tr>
<td>(ii) More than $1,000,000</td>
<td>add 2</td>
</tr>
<tr>
<td>(iii) More than $5,000,000</td>
<td>add 4</td>
</tr>
<tr>
<td>(iv) More than $10,000,000</td>
<td>add 6</td>
</tr>
<tr>
<td>(v) More than $50,000,000</td>
<td>add 8</td>
</tr>
<tr>
<td>(vi) More than $100,000,000</td>
<td>add 10</td>
</tr>
<tr>
<td>(vii) More than $200,000,000</td>
<td>add 12</td>
</tr>
<tr>
<td>(viii) More than $400,000,000</td>
<td>add 14</td>
</tr>
<tr>
<td>(ix) More than $1,000,000,000</td>
<td>add 16</td>
</tr>
<tr>
<td>(x) More than $5,000,000,000</td>
<td>add 18</td>
</tr>
<tr>
<td>(xi) More than $10,000,000,000</td>
<td>add 20</td>
</tr>
</tbody>
</table>

(B) For all other calculated loss, increase the offense level as follows:

--Present Loss Table Placed Here--

The market loss table is designed as an alternate loss table, such that courts can use the original table for other types of demonstrable loss that provide a greater enhancement than market loss. Multiple types of loss might arise from the same case, so these losses must factor into sentencing even if market loss is at play. This setup allows for situations like the Olis case on remand, where the district court found that the defendant was responsible for $79 million in tax losses to the U.S. Treasury, regardless of what the market loss might have been. 186

To demonstrate how this loss table would work, this Article will apply the proposed rules to the Ferguson sentencing. Ferguson received the maximum loss enhancement, 187 a victim enhancement, 188 and an organizer-leader

186. See supra notes 111-14 and accompanying text.
188. Id. § 2B1.1(b)(2)(C).
VI. CONCLUSION

The unique character of loss on the market should justify a separate treatment in calculating losses for purposes of criminal sentencing, but while appropriating the theory from civil securities law, few judges have emphasized this distinction. The causal link that civil jurisprudence has established between the defendant’s conduct and the eventual loss on the market is questionable at best when viewed in terms of the defendant’s personal responsibility. Although perpetrators of major fraud deserve harsh punishment, direct losses and market losses are different.

While victim loss is and should continue to be the driving factor in fraud sentence length, this loss must be well-defined, and therefore, market loss should impact sentencing, but under a less severe loss table than direct loss. Until the Guidelines account for market loss peculiarities, judges will continue to view Guideline sentences for all major frauds with skepticism and likely will refuse to apply the harshest sentences in market loss situations. A separate loss table is just one solution to this problem; whatever the ultimate resolution, courts must consider market loss in a new light to ensure fair and reasonable sentencing for major white-collar frauds.