UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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UNITED STATES OF AMERICA, v. IVY WOOLF TURK, Defendant.	:	Case No. 07-CR-1062 (NRB)

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AMICI CURIAE BRIEF OF
THE NATIONAL ASSOCIATION OF CRIMINAL DEFENSE LAWYERS,
THE NEW YORK STATE ASSOCIATION OF CRIMINAL DEFENSE LAWYERS, AND
THE NEW YORK COUNCIL OF DEFENSE LAWYERS

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INTEREST OF *AMICI CURIAE* AND INTRODUCTION

The National Association of Criminal Defense Lawyers ("NACDL") is the nation's preeminent professional bar association of criminal defense attorneys. Founded in 1958, the Association has 12,000-plus direct members in 28 countries—and 90 state, provincial, and local affiliate organizations totaling more than 40,000 attorneys, who are private lawyers, public defenders, and military defense counsel. They and the NACDL seek to ensure justice for all criminal defendants.

The New York State Association of Criminal Defense Lawyers, ("NYSACDL"), formed in 1986, is a statewide organization of more than 850 attorneys. The NYSACDL is responsive to the needs of private practitioners as well as public defenders, and is dedicated to assuring equal protection of individual rights and liberties for all. The NYSACDL is one of the NACDL's largest affiliates.

The New York Council of Defense Lawyers ("NYCDL") is a not-for-profit professional association of approximately 240 lawyers, many of whom are former prosecutors, whose principal area of practice is criminal defense in federal and state courts in New York. NYCDL's mission includes protecting the individual rights guaranteed by the Constitution, enhancing the quality of defense representation, and promoting the proper administration of criminal justice. As amicus, NYCDL offers the Court the perspective of practitioners who regularly handle some of the most complex and significant white collar criminal cases in federal and state courts. NYCDL's amicus briefs have been cited by the Court or concurring justices in cases such as Rita v. United States, 551 U.S. 338, 373 (2007) (Scalia, J., concurring in the judgment), and United States v. Booker, 543 U.S. 220, 266 (2005).

This case raises questions of great interest to the *amici* organizations regarding the loss analysis to be applied under the United States Sentencing Guidelines ("Guidelines") in cases involving fraud.[1] In its response to the sentencing submission of defendant Ivy Woolf Turk, the government acknowledges a line of Second Circuit cases holding that defendants are responsible only for those losses that result from their particular offense conduct, rather than for losses that are caused by outside forces. See, e.g., United States v. Ebbers, 458 F.3d 110, 128 (2d Cir. 2006) ("Losses from causes other than the fraud must be excluded from the loss calculation."); United States v. Rutkoske, 506 F.3d 170 (2d Cir. 2007) (remanding because the district court failed to consider how factors other than defendant's fraud contributed to the decline of the company's stock price). However, the government then argues that this fundamental principle is limited to the narrow context of securities fraud matters. Gov't Sentencing Memorandum at 5-6. In other words, the government contends that while defendants charged with securities fraud should receive the benefit of proximate cause principles adopted by the United States Sentencing Commission ("Sentencing Commission") and articulated by various courts of appeals (including the Second Circuit), defendants in all other types of fraud cases are not entitled to such a loss analysis, and should instead be sentenced based on even those losses that their conduct did not proximately cause.

The government's position is not only unsupported, but also would create significant injustice. It can hardly be disputed that the Guidelines were intended to establish a principled system in which sentencing decisions would be premised upon a defendant's culpability, and in cases involving fraud, culpability is gauged primarily by the loss table set forth in Guidelines

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[1] This *amici curiae* brief is limited solely to legal issues regarding loss causation under the Guidelines. The *amici* organizations take no position as to the factual and other legal disputes at issue between the parties.

Section 2B1.1(b). However, subject to certain exceptions that are not relevant here, the method of applying the loss table does not turn on the type of fraud a defendant has committed. To the contrary, the Guidelines, case law and principles of fundamental fairness each require that defendants who are to be sentenced pursuant to Section 2B1.1(b) be held accountable only for those losses that bear a sufficient causal link to their offense, and the government's efforts to limit proximate cause analysis to securities fraud cases cannot be squared with the weight of this authority.

Further, the limitation of principles of proximate causation to only securities fraud cases would also cause what other courts have recognized as the "utter travesty of justice that sometimes results from the guidelines' fetish with abstract arithmetic." United States v. Adelson, 441 F. Supp. 2d 506, 512 (S.D.N.Y. 2006); United States v. Parris, 573 F. Supp. 2d 744, 754 (E.D.N.Y. 2008) ("While I acknowledge that the Guidelines 'reflect Congress' judgment as to the appropriate national policy for such crimes,' this does not mean that the Sentencing Guidelines for white-collar crimes should be a black stain on common sense.") (internal citation omitted). As explained in more detail below, calculating actual loss using a methodology that identifies the losses that the defendant's fraud actually caused is not only consistent with well-established precedent, but also represents an approach to sentencing that is "cabined by common sense" and will result in sentences that are just and reasonable under the circumstances presented. Adelson, 441 F. Supp. 2d at 512.

In addressing the issues raised by the government's sentencing submission, this memorandum of law is divided into three main parts. First, the memorandum discusses the body of well-settled law in which the Second Circuit has held that defendants are to be sentenced based only upon those losses that their conduct proximately caused. Second, the memorandum

addresses the government's attempt to limit this loss causation analysis to the narrow area of securities fraud matters, and demonstrates the unpersuasive nature of the government's efforts. Third and last, the memorandum discusses the manner in which the government's position, if adopted, would undermine the purposes of the Guidelines, and would result in the types of exceedingly lengthy and egregiously harsh sentences that are a "black stain on common sense." Parris, 573 F. Supp. 2d at 754.

I. THE GUIDELINES AND SECOND CIRCUIT PRECEDENT APPLYING PROXIMATE CAUSE PRINCIPLES

Section 2B1.1(b) of the Guidelines provides for an enhancement of a fraud defendant's offense level based upon, among other factors, the amount of losses involved. The amount of loss attributed to the defendant significantly impacts a defendant's Guidelines calculation—while a loss of more than $5,000 will lead to a 2 level enhancement, a loss of more than $1 million will cause a 16 level enhancement, and a loss of more than $20 million will cause a 22 level enhancement. U.S. Sentencing Guidelines Manual § 2B1.1(b)(1) (2008). In the commentary to Section 2B1.1, the Sentencing Commission explained that, for purposes of this loss table, losses should be calculated based upon either the actual loss or intended loss from the offense, whichever is greater. (The government concedes that "intended loss" is "irrelevant" in this case. Gov't Sentencing Memorandum at 14.) Actual loss is defined as "the reasonably foreseeable pecuniary harm that resulted from the offense." U.S. Sentencing Guidelines Manual § 2B1.1 cmt. n.3(A)(i). The wording of Application Note 3(A)(ii) suggests that "actual loss" under Section 2B1.1 has three components: pecuniary harm to the victim(s), that such harm was "reasonably foreseeable," and that the pecuniary harm must have resulted from the offense.

In what is now a firmly settled body of case law, the Second Circuit set forth the appropriate means by which sentencing courts applying Section 2B1.1 are to reach reasonable

estimates of both intended and actual losses resulting from an offense. The calculation of actual loss requires a purely objective assessment of the cause of the losses. In cases in which actual loss is used as the measurement of losses for purposes of Section 2B1.1(b), the case law has followed the text of the Guidelines' Application Notes in holding that "[t]he loss must be the result of the fraud," and "[l]osses from causes other than the fraud must be excluded from the loss calculation." Ebbers, 458 F.3d at 128 (citation omitted). This means that losses caused by a defendant's criminal conduct must be untangled from losses caused by outside events such as market forces, and the losses caused by such outside forces must not be included in the Guidelines calculation. Rutkoske, 506 F.3d at 179; see also United States v. Zolp, 479 F.3d 715, 719 (9th Cir. 2007) ("[T]he 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."). In other words, where the revelation of a fraud coincides with or is followed by a decline in the market value of an asset, thereby resulting in a loss to investors, actual loss is to include only that the portion of the decline in value that is directly attributable to the fraud. See Ebbers, 458 F.3d at 128 (citing United States v. Olis, 429 F.3d 540 (5th Cir. 2005)).

The Second Circuit's decision in United States v. Ebbers provides a clear demonstration of these fundamental principles. Ebbers, the former CEO of WorldCom, Inc., was convicted of a massive fraud that artificially inflated the company's stock price. For purposes of Ebbers's Guidelines loss calculation, the court took a narrow view of the loss attributable to Ebbers's fraud, explaining that actual loss consisted only of the losses "suffered by those investors who bought or held WorldCom stock during the fraud period either in express reliance on the accuracy of the [company's] financial statements or in reliance on what Basic, Inc. v. Levinson described as the 'integrity' of the existing market place." Ebbers, 458 F.3d at 126-27. The

Second Circuit further held that losses attributable to other causes, such as outside market pressures on the price of WorldCom stock, could not be included in the amount of actual loss used to enhance Ebbers's sentence. Id. at 128. Given the dramatic scale of the fraud in the Ebbers case, the exclusion of losses caused by outside forces had no practical effect, because even a correct actual loss calculation resulted in a loss figure that exceeded the top of the Guidelines. Nonetheless, the court clearly cautioned that sentencing courts must untangle the numerous factors that could contribute to victim losses, and thereby ensure that defendants are sentenced only on the basis of losses their specific criminal conduct actually caused. Id. ("Many factors causing a decline in a company's performance may become publicly known around the time of the fraud and be one cause in the difference in price between X-day and Y-day. . . . Losses from causes other than the fraud must be excluded from the loss calculation.").

The Second Circuit's subsequent decision in United States v. Rutkoske further underscores this point. Rutkoske had been the owner of a brokerage firm that encouraged its customers to invest in a company known as NetBet, the stock of which Rutkoske's firm not only owned but also manipulated. When NetBet's stock price collapsed, the brokerage firm's customers lost over $12 million. To calculate actual losses for sentencing purposes, the district court used the difference between the stock price at the time the conspiracy began and on the last date for which the parties had price information for the stock from market makers, which was after the conspiracy ended. On appeal, the Second Circuit found this to be reversible error, because the district court's actual loss calculation had "implicitly attributed the total amount of the decline in the value of NetBet shares to Rutkoske's offense conduct" without considering or accounting for the impact of non-fraud causes for the decline. Rutkoske, 506 F.3d at 178.

As the Second Circuit stated, while there are "complexities inherent in calculating the loss amount . . . the loss [for which a defendant is sentenced] must be the result of the fraud." Id. at 179 (citation and quotation marks omitted).[2]

In Rutkoske, the Second Circuit also noted that the analysis of loss causation in civil securities fraud cases "provides useful guidance" in calculating actual loss for criminal sentencing purposes. 506 F.3d at 179. Specifically, the Rutkoske court noted that in Dura Pharmaceuticals, Inc. v. Broudo, 544 U.S. 336 (2005), the Supreme Court explained that a civil securities fraud plaintiff "must prove that the [defendant's] misrepresentation proximately caused the economic loss" to establish securities fraud, and that this requirement eliminated the possibility that a defendant would be held liable for losses caused by outside market forces. Rutkoske, 506 F.3d at 179. Given that a defendant may be sentenced only on the basis of losses that are causally linked to a defendant's criminal conduct, this proximate cause analysis also provides an appropriate framework for assessing actual fraud loss under the Guidelines. Id. ("[W]e see no reason why considerations relevant to loss causation in a civil fraud case should not 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.").

II. THE GOVERNMENT'S EFFORTS TO LIMIT PROXIMATE CAUSE ANALYSIS TO SECURITIES FRAUD CASES ARE UNCONVINCING AND UNSUPPORTED

In its response to defendant Woolf Turk's sentencing memorandum, the government attempts to minimize the impact of the cases described above by arguing that proximate cause principles annunciated in these cases apply solely in securities fraud matters. Indeed, while citing no case law to support its position, the government argues in favor of two entirely different

[2] Absolute precision in calculating losses is not required, and a sentencing court "need only make a reasonable estimate of the loss." U.S. Sentencing Guidelines Manual § 2B1.1 cmt. n.3(C).

standards of loss analysis in fraud cases: one, in securities fraud cases, by which defendants would be responsible only for losses that their conduct proximately caused; and another, in all other fraud cases, by which defendants would be responsible for all losses, even those that have the most minimal connection to the conduct at issue.

In support of this position, the government rests essentially on three arguments. First, the government contends that because the specific scheme at issue here involved victims whom the government characterizes as "lenders" rather than "equity investors," proximate cause principles do not apply. Gov't Sentencing Memorandum at 5-6. Second, the government asserts that if proximate cause principles were to be applied in this case, such principles would be "extended for the first time" outside of the securities fraud context. Gov't Sentencing Memorandum at 5-6. And third, citing an isolated phrase from the Ebbers decision, the government argues that even under Ebbers, the fact that victims would have refused to lend their money had they known the truth about the fraud scheme requires that the defendant be held responsible for the full amount of the victims' losses. Gov't Sentencing Memorandum at 7. Each of these arguments is addressed in turn below, and each is without merit.

A. In Calculating Loss Under Guidelines Section 2B1.1, There is No Distinction Between Schemes Involving "Lender" Victims and "Equity Investor" Victims

The government's first effort to differentiate this case from Ebbers and its progeny is premised on the assertion that while the victims in Ebbers were "equity investors" who knowingly engaged in risky investments, Woolf Turk's victims were unsuspecting "lenders." In fact, the government goes to some length to point out the purported differences in the expectations and degree of sophistication of these two types of victims. Specifically, the government states that "shareholder[s] investing in stock or other equities . . . embrac[e] a degree

of risk," and are "aware that both market forces and the acts of management can affect [their] investment," Gov't Sentencing Memorandum at 5-6, while the victims in this case are described as "lenders" who "believed they were making a very safe investment" and "had no inkling that they could suffer the kind of downside that they have suffered." Id. at 6, 12.

It is hardly a controversial proposition that lenders and equity investors have different expectations and assume different risks; that is not a point of reasonable contention. However, to the extent the government intends to argue that this distinction makes any sort of meaningful difference for sentencing purposes, the basis for that position is hardly clear. Indeed, while drawing a distinction between lenders and investors is easily accomplished, using that distinction to justify fundamentally disparate treatment of defendants in fraud cases is not, and in the government's brief, this latter issue goes unaddressed.

In any event, the government's argument in favor of disparate, case-dependent standards of loss causation fails for two basic reasons: (1) neither Section 2B1.1 nor the related case law distinguishes between lenders and equity investors for purposes of loss calculations; and (2) the government's distinction would conflict with fundamental principles underpinning the Guidelines.

Section 2B1.1 governs the loss calculation for all fraud-based crimes. See U.S. Sentencing Guidelines Manual ch.2, pt. B, Introductory Comment (2008) ("These sections address basic forms of property offenses: theft, embezzlement, fraud, forgery, counterfeiting, … insider trading, transactions in stolen goods, and simply property damage or destruction."). Where there is no intended loss, the relevant Guidelines level is determined by examining the "actual loss," and, as discussed above, the "actual loss" analysis carries with it the loss causation principles embodied in Application Note 3(A)(i). The government does not point to any

provision of the Guidelines that would restrict the use of the relevant application note to only securities fraud cases, and in fact, no such provision exists. To the contrary, the only types of matters in which there are unique provisions regarding the determination of actual loss are specifically identified in Application Note 3(F) to Section 2B1.1, and these type of matters - i.e., credit card fraud, government benefits, and Davis-Bacon violations – are not relevant here. In any event, even these special rules for determining actual loss in Application Note 3(F) do not eliminate, modify, or address in any way the proximate cause requirement that is found in the application notes. Thus, to the extent the government argues that securities fraud cases should have their own unique loss causation standard under the Guidelines, that argument cannot be squared with the Guidelines themselves.

Case law also lends the government no support. Nowhere in the case law discussing proximate causation requirements – whether in Ebbers and its progeny, or elsewhere – have courts drawn a distinction between lenders and equity investors, relied on a unique aspect of the securities market to justify their reasoning as to the applicable causation requirements, or otherwise sought to limit their holdings to securities-related matters. In fact, even the government's attempt to characterize this matter as a loan case rather than a securities fraud case is unavailing, for while Guidelines determinations in loan fraud cases were previously governed by Section 2F1.1, see, e.g., U.S. v. Confredo, 528 F.3d 143 (2d Cir 2008), that section of the Guidelines was deleted by consolidation with Section 2B1.1, and the proximate cause principles embodied in Section 2B1.1 therefore apply to all cases involving the fraudulent procurement of loans. U.S. Sentencing Guidelines Supplement 2 App. C, Amendment 617 (November 1, 2001).

Additionally, the fact that neither the Guidelines nor the courts have advanced or adopted the distinction the government advances is not surprising because the distinction is inconsistent

with one of the major purposes of loss determination under the Guidelines – "to serve as a rough measurement of the seriousness of the offense and culpability of the offender." U.S. Sentencing Guidelines Supplement 2 App. C, Amendment 617 (November 1, 2001). Expanding the scope of loss potentially attributable to one defendant but not another, based solely on arbitrary distinctions between the specific type of fraud the defendant committed, is fundamentally at odds with this basic principle. Similarly, precluding all but a small class of fraud defendants from invoking loss-causation principles is hardly consistent with the imposition of sentences that appropriately measure culpability.

The Tenth Circuit's recent decision in United States v. Nacchio, 573 F.3d 1062 (10th Cir. 2009), underscores this point. In Nacchio, an insider trading case in which the Guidelines are driven by gain rather than loss, the court reversed a district court's sentencing calculation because the district court had "ignored the myriad of factors unrelated to [the defendant's] criminal fraud that could have contributed to the increase in the value of the securities." Id. at 1074. Addressing the policy considerations underlying its ruling, the Tenth Circuit provided the following explanation of why proximate cause considerations are fundamental to the sentencing system:

> [I]f the impact of unrelated twists and turns of the market is ignored in the sentencing calculus then an insider trading defendant is likely to suffer a sentence that is detached from his or her individual criminal conduct and circumstances. And this detachment can have a profound, detrimental impact on another objective of federal sentencing – the elimination of unwarranted disparities between similarly situated defendants.... Therefore, from a policy perspective, it makes sense to adopt a sentencing approach that is focused on a defendant's criminally culpable conduct and has the effect of excising – even if not completely – unrelated market forces from the sentencing calculus, thereby narrowing the zone of unpredictability in sentencing.

Id. at 1081-82; see also Wayne R. Lafave, Substantive Criminal Law, § 6.4(c) (2d ed. 2003) ("the requirement of [legal] causation in criminal law, more often than not, serves not to free defendants from all liability, but rather to limit their punishment consistent with accepted theories of punishment").

Here, under the government's argument, only those fraud defendants who happened to commit fraud in the securities markets would be able to invoke proximate cause principles, and only that narrow class of defendants would be able to exclude losses that were caused by "unrelated twists and turns of the market." Id. In all other fraud cases, defendants would be sentenced based on even those losses that were caused by outside forces, and such defendants would thus "suffer . . . sentence[s] that [are] detached from [their] individual criminal conduct and circumstances." Id. The harm this disparate treatment would have upon the sentencing system is clear, as are the unfair consequences it would have upon defendants. The government's efforts to impose limits on proximate cause principles are thus not only unjustified, but unjust as well.

B. The Application of Proximate Cause Principles in All Fraud Cases is Not a Novel Extension of the Law

As a further part of its effort to minimize the significance of Ebbers and Rutkoske, the government next argues that proximate cause principles "should not be extended for the first time from the limited context of securities fraud." Gov't Sentencing Memorandum at 5. Contrary to the government's suggestion, however, the proximate cause principles articulated in those cases have never been limited only to securities fraud matters.

In noting the unremarkable principle that the loss attributed to a defendant in a fraud case "must be the result of the fraud," the Second Circuit in Ebbers cited to a single case – the Fifth Circuit case of U.S. v. Olis, 429 F.3d 540. Ebbers, 458 F.3d at 128. A review of Olis thus

provides important background to understanding the proximate cause analysis that the Second Circuit conducted in Ebbers.

Olis worked as a tax lawyer and accountant for a company called Dynegy. He, along with others, implemented an accounting scheme that was designed to generate artificial positive cash flow for Dynegy. The Securities and Exchange Commission learned of the scheme and required the company to restate the cash flow, which adversely affected the company's stock price. Eventually, Olis pleaded guilty to securities fraud, mail and wire fraud, and conspiracy and was sentenced to 292 months in prison. On appeal, Olis argued that the district court erred in part because while there were multiple causes for the loss in the value of the stock, the court improperly considered the entire decline in stock value that occurred the week immediately after the fraud was disclosed. The government, on the other hand, argued that the district court properly considered the entirety of the stock decline because the definition of "actual loss" requires only "but for" causation and "obviates the need to read the doctrine of proximate causation into § 2B1.1…." Brief of Plaintiff-Appellee at 107, Olis, 429 F.3d 540 (No. 04-20322).

Rejecting the government's argument, the Fifth Circuit in Olis stated that "preexisting standards . . . h[old] a defendant responsible at sentencing only to the extent that losses are caused directly by the offense conduct," and ruled that the definition of "actual loss" in Section 2B1.1 does not "lessen" those settled standards. Olis, 429 F.3d at 546-47. The Fifth Circuit also went on to note in Olis that "[d]istrict courts must take a 'realistic, economic approach to determine what losses the defendant truly caused or intended to cause." Id. (citing U.S. v. West Coast Aluminum Heat Treating Co., 265 F.3d 986, 991 (9th Cir. 2001)).

In ruling in Olis that, under "preexisting standards," defendants are responsible at sentencing "only to the extent that losses are caused directly by the offense conduct," 429 F.3d at 545-46, the Fifth Circuit in turn relied upon two cases: U.S. v. Hicks, 217 F.3d 1038 (9th Cir. 2000) and U.S. v. Marlatt, 24 F.3d 1005 (7th Cir. 1994). Notably, although the government contends in its papers here that loss causation principles have not previously been extended to non-securities fraud matters, *neither Hicks nor Marlatt involved securities fraud*. Additionally, because the Marlatt decision is particularly helpful in illustrating how courts have applied proximate cause principles in non-securities fraud matters prior to Ebbers and Rutkoske, we discuss that case in detail here.

Marlatt, who was the owner of a title company in northern Wisconsin which sold title insurance written by Ticor Title Insurance Company, bought a resort hotel at a foreclosure sale with the idea of selling time-shared condominium units in it. Marlatt, 24 F.3d at 1006. He sold the units, and through his title company, issued to each purchaser a title insurance policy written by Ticor. Id. Each policy represented that the purchaser was obtaining clear title. Id. Marlatt knew, but did not tell either the purchasers or Ticor, that actually the titles were heavily encumbered by liens for unpaid taxes, judgments, and mortgages. Id. Eventually Ticor discovered what had happened and spent $476,000 to eliminate the liens and thus clear the titles. Meanwhile the value of the property had plummeted. Id. The purchasers of the units threatened to sue Ticor for fraud. Id. To avert such a suit, Ticor decided to buy all the units from the purchasers at the price at which the purchasers had bought them from the defendant. Id. This was done at a cost of $565,000, which the district court added to the $476,000 to compute the total loss caused by the fraud. Id.