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TAX LITIGATION ISSUES

Sentencing Commission Addresses Inconsistent Definitions of "Loss"

By Jeremy H. Temkin

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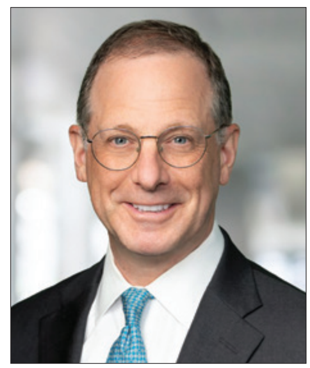
In fraud cases, the sentencing guidelines are largely predicated on the amount of loss attributable to the defendant's conduct. Typically, the greater the loss suffered by the victim, the higher the defendant's guidelines sentencing range. And while sentencing judges have substantial leeway to vary from the guidelines, they are required to use the properly computed guidelines range as the starting point for deciding the appropriate sentence in each case.

Section 2T1.1(c)(1) of the guidelines defines loss as "the total amount of loss that was the object of the offense (i.e., the loss that would have resulted had the offense been successfully completed)." By contrast, the guidelines calculations for most other economic crimes are governed by Chapter 2B, which, until a recent amendment, relegated the definition of loss to commentary adopted by the U.S. Sentencing Commission. That commentary incorporated the concept of "intended loss," which encompassed "the pecuniary harm that the defendant purposely sought to inflict." U.S.S.G. §2B1.1, cmt. n.3(A)(ii).


Jeremy Temkin

Circuit Courts of Appeals faced with challenges to the inclusion of "intended loss" in guidelines calculations have split over the extent of deference due to the commentary, with the Third Circuit rejecting application of the commentary to increase a defendant's guidelines calculation, while the Second, Fourth, and Sixth Circuits have all taken the opposite view.

In an amendment effective Nov. 1, 2024, the Sentencing Commission addressed the Circuit split by moving the concept of intended loss from the commentary to the text of section 2B1.1(b)(1), thereby obviating the question of whether the commentary was entitled to deference. While the amendment may foreclose arguments regarding the inclusion of "intended loss" in cases governed by Chapter 2B, the cases provide an important reminder to counsel that commentary found in the guidelines is not entitled to ironclad deference.

Deference Due to Guidelines Commentary

The sentencing guidelines are set forth in a manual that includes policy statements and commentary that reflect the Sentencing Commission's interpretation of individual guidelines. See U.S.S.G. §1B1.7. In Stinson v. United States, 508 U.S. 36, 38, 44 (1993), the Supreme Court likened the Sentencing Commission to an administrative agency that "promulgates the guidelines by virtue of an express congressional delegation of authority for rulemaking," and held that commentary in the Guidelines Manual "that interprets or explains a guideline is authoritative unless it violates the constitution or a federal statute, or is inconsistent with, or a plainly erroneous reading of, that guideline."

More recently, in Kisor v. Wilkie, 588 U.S. 558 (2019), the Supreme Court held that before deferring to an agency's interpretation of its own regulations, a court must determine that the regulation in question is actually ambiguous, which involves asking whether the agency's reading falls "within the bounds of reasonable interpretation," and that the agency has substantive expertise to inform its interpretation. While Kisor did not involve the sentencing guidelines, courts have applied it in deciding how much deference to afford the commission's commentary.

United States v. Banks

In United States v. Banks, 55 F.4th 246 (3d Cir. 2022), the defendant attempted to defraud his victim out of $264,000. Because the scheme was unsuccessful, Banks argued that "the loss enhancement . . . should not apply since there was no actual loss." Relying on the guidelines commentary, the sentencing court included the $264,000 "intended loss" in the guidelines calculation, which resulted in a substantial increase in Banks' offense level and ultimately his 104-month sentence.

On appeal, the United States Court of Appeals for the Third Circuit reviewed common dictionary definitions of the word "loss." The court noted that each definition was dependent on there being actual harm, and that none of the definitions suggested that "loss" encompassed "intended loss." Applying Kisor, the court concluded that since no genuine ambiguity existed with respect to the meaning of "loss" in Chapter 2B, the sentencing court's deference to the commentary was plain error. The court vacated Banks' sentence and remanded for resentencing without the intended loss enhancement.

***Boler* and the Majority Approach**

In United States v. Boler, 115 F.4th 316 (4th Cir. 2024), the defendant was convicted of both filing false claims against the United States arising out of her preparation and filing of six false tax returns and making a false statement in a Paycheck Protection Program (PPP) loan application. Post-conviction, the Probation Department calculated Boler's Guidelines under section 2B1.1(b)(1) and included a loss enhancement based on the $20,833 PPP loan she had received, $116,106 in tax refunds the IRS had issued based on fraudulent tax returns she had prepared, and $42,283 in fraudulent refund claims the IRS had rejected. The inclusion of the rejected refunds increased Boler's sentencing range from 24-30 months to 30-37 months.

On appeal, Boler argued that, following Kisor, the Fourth Circuit should not afford deference to the guidelines' commentary since "loss" is not ambiguous and cannot be read to include intended loss. She also relied upon section 2T1.1's definition of "tax loss" to support an "expressio unius" argument that the Sentencing Commission knew how to incorporate intended loss in section 2B1.1 if it had wanted to do so.

The government responded by arguing that "loss" is ambiguous and although section 2B1.1 controlled Boler's calculation, because the disputed loss amount was based upon a rejected tax refund claim, the inclusion of the intended loss in tax cases provided relevant context for Boler's loss calculation. Boler replied that the government either waived or forfeited its context argument since it chose not to prosecute her for tax fraud, which would have required proof of willfulness, but rather a non-tax offense controlled by section 2B1.1.

The court started by applying the Kisor analysis, concluding that "loss" has a number of meanings "depending on the dictionary of one's choice." While the Third Circuit in Banks had noted that none of the common definitions can be read as including "intended loss," the Fourth Circuit relied on the mere existence of multiple definitions to conclude that "loss" as used in section 2B1.1 is ambiguous without addressing the fact that none of the applicable definitions could be read as expanding the notion of loss to unsuccessful schemes.

In his dissenting opinion, Judge A. Marvin Quattlebaum highlighted the apparent irrelevance of the multiple definitions, explaining that although loss may include a wide variety of categories, "breadth does not equal ambiguity." Having affirmed the sentencing court's application of the commentary and its reliance on intended loss to calculate Boler's sentencing range, the Fourth Circuit rejected the government's contextual argument, noting that section 2T1.1 was "not a useful comparator" and "simply [did] not apply."

In United States v. You, 74 F.4th 378 (6th Cir. 2023), and United States v. Rainford, 110 F.4th 455 (2d Cir. 2024), the courts also addressed challenges to the inclusion of "intended loss" under section 2B1.1 and reached the same result. In You, the Sixth Circuit applied Kisor and upheld an enhancement where the defendant was arrested before the putative victims of her trade secrets and economic espionage scheme suffered any actual loss.

Like the Fourth Circuit in Boler, the Sixth Circuit applied Kisor and found the multitude of definitions of loss created ambiguity. In Rainford, the Second Circuit applied Stinson to find that section 2B1.1's commentary "is neither inconsistent with nor a plainly erroneous reading of the guideline." The Second Circuit acknowledged that the validity of Stinson "is subject to debate" after Kisor modified the standard for relying on an agency's interpretation of its own rules, but the court adhered to Stinson since it has direct application as a case that decided the weight due to guidelines commentary.

Nov. 1, 2024 Amendment

Effective Nov. 1, 2024, the Sentencing Commission has eliminated the need to rely on the commentary in calculating loss under section 2B1.1. Recognizing the inconsistency in loss calculations across the circuits, the Sentencing Commission amended section 2B1.1 to move the rule establishing loss from the commentary to the text. Thus, section 2B1.1(b)(1) now defines "loss" as "the greater of actual loss or intended loss," and "intended loss" as "the pecuniary harm that the defendant purposely sought to inflict . . . includ[ing] intended pecuniary harm that would have been impossible or unlikely to occur." See U.S.S.G. Amendment 831. By moving the concept of intended loss to the text of section 2B1.1(b)(1), the commission has foreclosed challenges to the inclusion of "intended loss" based on an argument that the commission's commentary is not entitled to deference.

Conclusion

As noted above, the text of section 2T1.1(c)(1) encompasses the concept of intended loss by defining "loss" to include "the total amount of loss that was the object of the offense (i.e., the loss that would have resulted had the offense been successfully completed)." While the precise issue resolved by the amendment to section 2B1.1 was not in dispute in tax cases, the Sentencing Commission has addressed other aspects of Chapter 2T through commentary that may or may not be entitled to deference.

For example, section 2T1.1(c)(1) provides that "tax loss shall be treated as equal to 28% of the unreported gross income [or improperly claimed deduction or exemption] (34% if taxpayer is corporation), . . . unless a more accurate determination of the tax loss can be made." Prior to 2001, a circuit split emerged as to how tax loss should be calculated in corporate diversion cases, where the defendant has evaded both corporate and individual taxes.

While the Second and Seventh Circuits calculated the losses sequentially, with the 34% corporate rate being applied to the entire amount of unreported income followed by application of the 28% individual rate to the "after tax" balance (resulting in an effective rate of 52.48%), see United States v. Harvey, 996 F.2d 919, 921 (7th Cir. 1993); United States v. Martinez-Rios, 143 F.3d 662, 672 (2d Cir. 1998), the Sixth Circuit combined the two amounts, holding the defendant responsible for an aggregate 62% tax rate. See United States v. Cseplo, 42 F.3d 360, 364 (6th Cir. 1994).

While the sequential approach is arguably consistent with the Guidelines goal of using the most accurate calculation of the loss caused by the defendant's conduct, in 2001, the Sentencing Commission adopted commentary explicitly rejecting the sequential approach. As a result, the Guidelines commentary now directs courts to calculate loss using "the aggregate tax loss from the individual tax offense and the corporate tax offense added together" so that the unreported income is taxed twice. U.S.S.G. § 2T1.1, cmt. n.7.

Because the Second Circuit has not issued a published opinion addressing the issue since the amendment, rather than assuming tcases should consider arguing that Harvey and Martinez-Rios were correctly decided and the commentary is not entitled to deference under either Kisor or Stinson.

More generally, while the Sentencing Commission may have resolved the conflict over the interpretation of "loss" in section 2B1.1 through recent amendment, there is much to be learned from the Circuit split over the deference due to Guidelines commentary.

Jeremy H. Temkin is a principal in Morvillo Abramowitz Grand Iason & Anello P.C.

Emily Smit, an associate of the firm, assisted in the preparation of this article.