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PENALTY RELIEF AVAILABLE: RECENT JURISPRUDENCE OFFERS THE OPPORTUNITY FOR SIGNIFICANTLY LOWER FINES AND OTHER PENALTIES IN WHITE COLLAR RESOLUTIONS WITH DOJ AND OTHER AGENCIES

To Our Clients and Friends:

A new ruling by a federal court of appeals could dramatically reduce the penalties that the Department of Justice and other federal agencies are able to extract in many cases, including negotiated resolutions. The U.S. Court of Appeals for the Third Circuit in Philadelphia held in *United States v. Banks* that judges may not use intended loss—instead, they may rely only on actual loss—to calculate the range of criminal penalties applicable in fraud cases. As significant as that ruling is, the court's reasoning extends beyond criminal sentencings for fraud offenses. It will reduce the penalties that courts can impose for a wide array of other federal criminal offenses. But more broadly, its impact will be felt in deferred prosecution agreements ("DPAs"), non-prosecution agreements ("NPAs"), and other negotiated resolutions where a penalty is based on the United States Sentencing Guidelines.

The *Banks* decision, and other cases following its reasoning, may result in significantly lower penalties in a wide array of settlement agreements and contested criminal proceedings, such as:

- **Fraud cases** where the penalty is based on either intended loss or gain, rather than actual loss;
- **Money laundering cases** that involve commingled funds;
- **Financial transaction structuring cases** involving a "pattern of unlawful activity";
- **Tax cases** involving multiple alleged violations; and
- **Any corporate resolution** where a company seeks credit for self-reporting, cooperation, or acceptance of responsibility.

When sentencing criminal defendants—both natural persons and corporations—federal courts are required to consider the sentencing range calculated using Guidelines promulgated by the United States Sentencing Commission (the "USSG" or "Sentencing Guidelines").[1] These sentencing ranges are

expressed as months in prison or monetary fines. Courts need not sentence within the calculated range, but those ranges have a strong influence on the outcome. In 2021, for example, federal courts sentenced defendants within the Guideline range nearly half the time.[2] Moreover, the Department of Justice and other federal agencies such as the Securities and Exchange Commission frequently look to these sentencing ranges as the starting point for settlement resolutions, including DPAs and NPAs.

Each Sentencing Guideline includes "commentary," which provides additional instruction from the Commission on how that Guideline is to be applied to particular cases. With very few exceptions, courts have traditionally treated the commentary as binding on a court's Guideline calculation.[3] That is because the Supreme Court held in 1993 in *Stinson v. United States*, consistent with the agency deference doctrine the Court set forth in *Bowles v. Seminole Rock & Sand* (and reinforced later in *Auer v. Robbins*), that the Commission's commentary amounts to an agency's interpretation of its own legislative rule, and as such the commentary must be given controlling weight unless it is plainly erroneous or inconsistent with the Guideline.[4]

However, in 2019 the Supreme Court held in *Kisor v. Wilkie*[5]—a VA benefits case—that deference is not appropriate to agency interpretations of their own rules unless, after exhausting all the "traditional tools" of construction, the rule is "genuinely ambiguous."[6] Without such ambiguity, there is no plausible reason to defer to the agency: "the regulation then just means what it means—and the court must give it effect, as the court would any law."[7] Only if genuine ambiguity remains after considering the text, structure, history, and purpose of a regulation, may a court consider binding the agency's comments; and even then the agency's reading must still fall "within the bounds of reasonable interpretation" before it binds a court.[8]

Courts across the country have begun applying the rationale in *Kisor* to Guidelines commentary, most recently in *United States v. Banks*.[9] There, the Third Circuit analyzed USSG § 2B1.1, the Guideline for fraud and theft offenses. Under that Guideline, the offense level increases as the amount of "loss" resulting from the defendant's offense increases.[10] For its part, the commentary defines loss as the higher of "actual loss" or "intended loss," the latter of which includes the "pecuniary harm that the defendant purposely sought to inflict" even if such harm "would have been impossible or unlikely to occur."[11] The defendant in *Banks* tried to execute a check kiting scheme in which he deposited $324,000 in bad checks into an account and sought to withdraw the funds before the bank learned the checks were not supported by sufficient funds.[12] There was no actual loss—the banks did not allow the attempted withdrawals—so the court relied on an *intended* loss of $324,000 to more than double the offense level, leading to a much longer sentencing range.[13] The Third Circuit reversed and sent the case back for resentencing. Invoking *Kisor*, the court concluded there was no genuine ambiguity in the meaning of "loss" in § 2B1.1 and, thus, the Commission's commentary had "impermissibly expand[ed] the word 'loss' to include both intended loss and actual loss."[14]

The Third Circuit is not alone in concluding that *Kisor* limits the deference courts owe to commentary in the Sentencing Guidelines. Earlier, in 2021, the Sixth Circuit in *United States v. Riccardi* struck down another part of the definition of loss in the commentary to Section 2B1.1, this time rejecting a requirement to treat each stolen credit card or gift card as a loss of at least $500.[15] Four other circuits—the First, Second, Tenth, and Eleventh—have resisted the impact of *Kisor*, at least where circuit

precedent has expressly addressed a particular provision in the commentary, unless and until the Supreme Court holds that *Kisor* changes the deference owed in the Sentencing Guidelines context.[16] In the Fourth Circuit, two three-judge panels came to contradictory holdings regarding the impact of *Kisor*.[17] And the Fifth Circuit has granted *en banc* review in a case where the panel had determined it was bound by pre-*Kisor* circuit precedent.[18]

The Supreme Court will likely be called upon to resolve the split in the circuits over the deference that courts owe to Commission commentary after *Kisor*. In the meantime, a number of enhancements to penalties based on commentary in the Guidelines Manual—enhancements that form the basis for settlement negotiations with DOJ in many white collar matters—are vulnerable to challenge in circuits where courts apply *Kisor* to the Guidelines. These include:

- *Intended Loss in Fraud and Theft Cases*: This is the part of the definition of "loss" that the Third Circuit rejected in *Banks*. In many cases a fraud scheme is stopped before any loss occurs, meaning the sentencing range—which can no longer be based on the intended loss—will be significantly lower than in the past.[19]

- *Pecuniary Gain in Fraud and Theft Cases*: The Commission commentary to USSG § 2B1.1 also directs courts to "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." But the word "gain" does not appear in the Guideline; only the word "loss" does. Thus, when a sentence range is determined under Section 2B1.1, the government will no longer be able to fall back on the amount of gain as an alternative to loss.

- *Commingled Funds in Money Laundering Cases*: The money laundering guideline, USSG § 2S1.1(a)(2), ties the offense level to the "value of the laundered funds." Yet the Commission commentary states that court should use the value of commingled funds if the defendant is unable to "provide[] sufficient information to determine the amount of criminally derived funds without unduly complicating or prolonging the sentencing process." This commentary tries to do two things that are not found in the language of the Guideline: it would allow an enhancement for more than the "value of the laundered funds" and it would shift the burden from the government to the defendant to prove the amount that was laundered. *Kisor* and *Banks* prevent courts from deferring to this commentary.

- *Pattern of Unlawful Activity in Offenses Under the Bank Secrecy Act*: In the Guideline covering structured transactions and similar offenses, USSG § 2S1.3(b)(2), the penalty is increased if the defendant "committed the offense as part of a pattern of unlawful activity." The Commission commentary defines a "pattern" as "at least two separate occasions." Under the reasoning of *Kisor* and *Banks*, that commentary is vulnerable because conventional definitions generally suggest at least three instances to be considered a pattern.[20]

- *Penalties for Related Conduct in Tax Offenses*: In the Guideline applicable to tax offenses, USSG § 2T1.1(c), the tax loss is defined as "the total amount of loss that was the object of the offense." The Commission commentary expands on this language by directing courts to consider

"all conduct violating the tax laws . . . as part of the same course of conduct or common scheme or plan unless the evidence demonstrates that the conduct is clearly unrelated." This commentary is vulnerable to attack for expanding the meaning of "the offense" and creating a presumption that other conduct is related to (and thus included within) the offense.[21]

- *Credit for Cooperation by Corporate Defendants*: In calculating the appropriate fine range for corporate defendants, the Guidelines direct courts to determine the entity's "culpability factor," which includes consideration whether that entity "fully cooperated."[22] The Commission commentary purports to require more than "full[]" cooperation, though, by stating it must be "thorough" *and* "timely." Moreover, the commentary states that "[t]o be thorough, the cooperation should include the disclosure of *all* pertinent information," which implicates important privilege protections including the attorney-client privilege. Corporations will have strong arguments that they deserve cooperation credit without satisfying the language in the commentary.

These are just a few ways in which cases like *Banks* threaten to upend sentencing outcomes. And because the Department of Justice and some other agencies rely on Sentencing Guidelines calculations in negotiated resolutions, this recent development will also be an important tool in settlement discussions, including those leading to NPAs and DPAs. These types of resolutions have become a mainstay in recent years,[23] and counsel representing individuals and corporations will want to be alert to the opportunity to challenge government efforts to increase penalties in ways that were accepted as unavoidable for many years. Simply put, the normal government playbook in settling white collar criminal matters may no longer rest on solid footing, and savvy advocates can strategize how to gain from these opportunities.

It will be important for counsel to be prepared to engage with the government on its expected efforts to distinguish cases like *Banks* on various grounds, including that the challenged commentary for other Guidelines is within a realm of ambiguity or that it is a reasonable interpretation. Gibson Dunn will continue to monitor the impact of *Kisor* on the Sentencing Guidelines and ways in which penalties can be reduced based on this development.

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[1] 18 U.S.C. § 3553(a)(4)(A).

[2] United States Sentencing Commission, *Statistical Information Packet Fiscal Year 2021*, available at https://www.ussc.gov/sites/default/files/pdf/research-and-publications/federal-sentencing-statistics/state-district-circuit/2021/1c21.pdf

[3] *Stinson v. United States*, 508 U.S. 36, 42-43 (1993).

[4] *Id*. at 44-45; *Bowles v. Seminole Rock & Sand Co.,* 325 U.S. 410 (1945); *Auer v. Robbins*, 519 U.S. 452 (1997).

[5] 139 S.Ct. 2400 (2019).

[6] *Id*. at 2404.

[7] *Id*. at 2415.

[8] *Id*. at 2404.

[9] *See United States v. Banks*, No. 19-3812, 2022 WL 17333797 (3d Cir. Nov. 30, 2022).

[10] *Id.* at *1.

[11] USSG § 2B1.1, app. note. 3.

[12] *Id.*

[13] *Id.*

[14] *See id.* at *6-7.

[15] *United States v. Riccardi,* 989 F.3d 476 (6th Cir. 2021).

[16] *See United States v. Lewis*, 963 F.3d 16, 24 (1st Cir. 2020), *United States v. Tabb*, 949 F.3d 81 (2d Cir. 2020), *United States v. Richardson*, 958 F.3d 151 (2d Cir. 2020), *United States v. Lovelace*, 794 Fed App'x 793 (10th Cir. 2020); *United States v. Mellon*, No. 21-12248, 2022 WL 4091736 (11th Cir. Sept. 7, 2022).

[17] *Compare United States v. Campbell*, 22 F.4th 438 (4th Cir. 2022) (holding that *Kisor* limited *Stinson's* scope); *United States v. Moses*, 23 F.4th 347 (4th Cir. 2022) (holding that "*Kisor* did not overrule *Stinson*'s standard for the deference owed to Guidelines commentary").

[18] *United States v. Vargas*, 35 F.4th 936 (5th Cir. 2022).

[19] For example, bank fraud cases based on alleged misrepresentations on loan applications often involve intended loss values (the value of the loan) that are far greater than the actual losses sustained by the banks. In *United States v. Morgan*, 18-CR-108-EAW, (WDNY 2019), a case in which Gibson Dunn was counsel, DOJ alleged $500 million in losses in a 114-count indictment when the actual losses were far lower. The government's recent wave of Paycheck Protection Program ("PPP") and related COVID-19 related fraud cases show similar disparities between intended and actual losses. In December 2021, DOJ charged four defendants in connection with a PPP fraud scheme where the intended losses (the amount sought in forgivable PPP loans) was $35 million, but the defendants obtained only $18 million. *See* Four Charged in $35 Million COVID-19 Relief Fraud Scheme, Dec. 15, 2021, *available at* https://www.justice.gov/opa/pr/four-charged-35-million-covid-19-relief-fraud-scheme.

[20] *See Sedima, S.P.R.L. v. Imrex Co., Inc.*, 473 U.S. 479, 496 n.14 (1985) ("Indeed, in common parlance two of anything do not generally form a 'pattern.'").

[21] USSG § 1B1.3.

[22] USSG § 8C2.5(g).

[23] *See* Gibson Dunn 2021 Year-End Update on Corporate Non-Prosecution Agreements and Deferred Prosecution Agreements, February 3, 2022, *available at* https://www.gibsondunn.com/2021-year-end-update-on-corporate-non-prosecution-agreements-and-deferred-prosecution-agreements/; *see also* U.S. Sent'g Comm'n, The Organizational Sentencing Guidelines: Thirty Years of Innovation and Influence 12, 12 n.101 (Aug. 2022), https://www.ussc.gov/sites/default/files/pdf/research-and-publications/research-publications/2022/20220829_Organizational-Guidelines.pdf (acknowledging that "criminal prosecutions resulting in a sentencing are only one method by which an organization's violations of the law can be addressed by the authorities" and citing both the DOJ Justice Manual and Gibson Dunn's year-end alert on corporate DPAs and NPAs).

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding these developments. Please contact the Gibson Dunn lawyer with whom you usually work, or any of the following leaders and members of the White Collar Defense & Investigations or Global Tax Controversy & Litigation practice groups:

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