



## SENTENCING GUIDELINES

## Expert Analysis

# Non-Guideline Sentences For White-Collar Defendants

A recent series of decisions by the U.S. Supreme Court and the U.S. Court of Appeals for the Second Circuit have ushered in a new era of sentencing discretion, leaving the Sentencing Guidelines truly serving only as advisory guidelines. Yet despite this new legal authority, questions have remained as to just how much discretion district courts would exercise, and how that discretion would be scrutinized on appeal. Recent decisions by district courts within the Second Circuit demonstrate that judges are taking full advantage of the new, discretionary sentencing regime for white-collar crimes, using their experience and judgment in determining what price an individual defendant should pay for his or her crime.

In particular, district judges are using their discretion to issue non-guideline sentences in cases where an extraordinarily severe guideline sentence is principally driven by the loss amount. In these cases, which are described below, courts have taken little or no issue with the government's analysis of the loss. Rather, the district courts concluded that the loss amount was staggeringly high—high enough, in most cases, to justify a sentence of life in prison.

Nevertheless, in all of these cases, the district court noted that such a sentence was plainly excessive and imposed a non-guidelines sentence. In light of the Second Circuit's most recent decision on the appropriate standard of appellate review of the substantive unreasonableness of sentences, it will not be at all surprising if this trend of non-guideline sentences continues.

### 'Treacy'

*United States v. Treacy* involved James Treacy, the former chief operating officer and then president of Monster Worldwide Inc., the owner of the well-known job search Web site Monster.com. At trial, he was convicted of a long-term scheme to backdate numerous stock option grants. By backdating the grants, the government argued, Mr. Treacy was able to obtain stock options at historically low exercise prices, while failing to properly account for the option grants, thus giving the appearance that such grants had been given at fair market value.<sup>1</sup>

The government initially calculated the applicable guideline range at 324 to 405 months, or between 27 and 34 years (a calculation



By  
**Alan  
Vinegrad**



And  
**Gretchen  
Hoff Varner**

which it later reduced to 121 to 151 months). The driving factor behind the government's guideline calculation was its position that the loss amount included both profits from Mr. Treacy's exercise of backdated options as well as bonus payments for reaching company financial targets.

At the sentencing hearing, the court rejected the attempt to include bonus payments in the loss calculation but accepted the government's proposed figures with respect to the amount of profits Mr.

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Treacy gained from the backdated options.<sup>2</sup>

After calculating the appropriate guideline range at 121 to 151 months, Southern District Judge Jed Rakoff proceeded to issue a non-guideline sentence of two years. In doing so, he cited the history of relatively modest sentences in other stock option backdating prosecutions as well as the outpouring of support that Mr. Treacy received.

To be sure, Judge Rakoff emphasized that stock option backdating was "appalling" and "disgusting," and acknowledged that "one cannot but feel—as so much of the public does feel in these and other such scandals—a desire to see the miscreants brought to justice, punished, deterred, and the moral order of society reestablished."<sup>3</sup> However, the sentence eventually imposed also reflected the individual characteristics of the defendant and other mitigating factors, rather than any reliance on the proposed sentencing enhancement for the large loss amount.

### 'Ferguson'

In 2008, five former insurance executives from AIG and the General Re Corporation were convicted of conspiracy, securities fraud, mail fraud, and making false statements to the SEC. The charges stemmed from what the government called "sham reinsurance contracts" between AIG and Gen Re in late 2000 and early 2001 that made it appear that AIG reinsured Gen Re for \$500 million of insurance contracts.<sup>4</sup> The government claimed that as a result of these transactions, AIG was able to report that it had increased its loss reserves by \$500 million, thus allegedly misleading stock market analysts, AIG shareholders and the investing public.

Prior to sentencing, the government argued that the loss to shareholders exceeded \$1 billion, which would result in a 30-level enhancement under the guidelines and a sentencing range of life. By contrast, the defendants argued that the offense did not result in any loss. Judge Christopher Droney held in *United States v. Ferguson* that a 30-level enhancement was appropriate, finding that government provided a reasonable estimate of the loss through its expert reports. The judge noted that even the lowest end of the government expert's estimate, \$544 million, was more than the highest level of loss specified in the guidelines.<sup>5</sup>

In the face of this extraordinarily high guideline calculation—a calculation that (with other adjustments) was, quite literally, off the charts—the judge handed down non-guidelines sentences ranging from a year and a day for two defendants, 18 months for a third, two years for a fourth, and four years for the fifth. In doing so, Judge Droney cited not only the individual characteristics of the defendants, including their history of good works and other exemplary behavior, but also the fact that none of the defendants was motivated by personal gain and, for some defendants, their relatively less culpable role.

### 'Stinn'

Bradley Stinn was the chief executive officer of Friedman's Inc., a public company that owned a nationwide chain of jewelry stores. After trial in *United States v. Stinn*, he was convicted of securities fraud, mail fraud and conspiracy for orchestrating a securities fraud scheme that made the company's reported financial results appear better than they actually were.

For these crimes, Mr. Stinn faced a guideline range of life imprisonment, cabined by the 70-year statutory maximum permitted by the counts of conviction.

The guideline calculation was, as in the *Ferguson* and *Treacy* cases, driven by the government's calculation of the loss amount—in this case, over \$100 million, which warranted a 26-level enhancement under the guidelines.

At sentencing, the government conceded that a 70-year sentence was excessive but nevertheless sought a “lengthy sentence of incarceration.”<sup>6</sup> Judge Nina Gershon, after determining that the total loss was easily over \$20 million, calculated the guidelines at life imprisonment. She also denied the defendant's requests for downward departures.<sup>7</sup>

Nevertheless, Judge Gershon imposed a non-guideline sentence of 12 years' imprisonment, finding that the sentence suggested by the guidelines was “clearly too high.”<sup>8</sup> Rather than focus on the amount of loss, the judge noted the defendant's individual circumstances, including his background, family, and employment. She also focused on the fact that one of the factors to be considered in sentencing is the avoidance of unwarranted sentencing disparities among defendants in similar cases.<sup>9</sup>

### 'Dreier'

Marc Dreier, the sole equity partner of Dreier LLP, was arrested in late 2008 for a series of frauds, including selling fraudulent promissory notes to individual investors and clients of his firm and misappropriating escrow funds from his clients. He used these proceeds to finance a lavish lifestyle, including a \$16 million yacht, beachfront property in the Hamptons, and expensive artwork. All told, Mr. Dreier collected approximately \$700 million from his note fraud victims and more than \$46 million in stolen funds from his clients. Mr. Dreier eventually pleaded guilty in *United States v. Dreier* to eight counts, including conspiracy, securities fraud, wire fraud, and money laundering.

Under the guidelines, Mr. Dreier faced a sentence of 145 years' imprisonment, a sentence largely dictated by a 30-level enhancement for a loss of more than \$400 million.<sup>10</sup> At sentencing, Judge Rakoff noted that unlike those cases where the loss amount was calculated based on stock market prices and other variables, the loss in the *Dreier* case was a real amount, based on the amount missing from individual victims on the day that Mr. Dreier was arrested.<sup>11</sup>

Nevertheless, the judge went on to describe loss as an “overstated factor in the guidelines”<sup>12</sup> and sentenced Mr. Dreier to 20 years. The judge was influenced by the fact that such a term of imprisonment would allow for the possibility that Mr. Dreier (who was 59 years old) could serve his sentence while still having some meaningful life after his prison term.<sup>13</sup> In light of the guideline calculation of 145 years and the government's request for life imprisonment, Mr. Dreier's sentence, while lengthy, still represented a substantial downward variance.

### Lessons From the Cases

The decisions described above reflect an increasing exercise of judicial discretion in sentences for white collar offenses. While there may be some outliers, such as the high-profile sentencing of Bernard Madoff,<sup>14</sup> the trend in the Second Circuit appears to be towards non-guideline sentences in fraud cases.

Not only do these cases demonstrate the willingness of district judges to exercise their

discretion over sentencing, they also may suggest increasing discontent with the impact that the loss calculations have on the Sentencing Guidelines in white-collar cases.

Judge Rakoff, the sentencing judge in both *Dreier* and *Treacy*, has previously written that the guidelines' “fetish with abstract arithmetic” can result in an “utter travesty of justice.”<sup>15</sup>

And in each of these cases, the sentencing judges diligently resolved disputes and calculated the loss amount—even issuing a lengthy written decision to determine the loss amount, as in *Ferguson*—but then refused to rely on that number when imposing sentence, instead focusing on the individual characteristics of the defendants and other mitigating factors.

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guidelines may in fact result in the guidelines becoming even less useful to sentencing courts, who, faced with such extraordinary sentences, are compelled to fashion their own decisions in light of the 18 U.S.C. §3553(a) factors without the aid of the guidelines.

In such cases, the guidelines provide little meaningful guidance to sentencing judges. One wonders whether it is high time for the Sentencing Commission to reconsider the appropriateness of the now-astronomical sentences called for by its fraud guidelines.

### Success on Appeal

The Second Circuit's most recent pronouncement on sentencing law suggests that the Court of Appeals is increasingly reluctant to overturn a sentence as substantively unreasonable. In *United States v. Rigas*, the court considered the 12- and 17-year sentences imposed by Judge Leonard Sand on John and Timothy Rigas, respectively.<sup>16</sup> The two men, former executives at Adelphia Communications Corporation, were convicted at trial of conspiracy, bank fraud and securities fraud. In both cases, the sentence was far below the guideline range of life imprisonment.

In addition to unsuccessfully challenging the procedural reasonableness of the sentences, the defendants also challenged the substantive reasonableness.

Writing for the court last week, Judge Jose Cabranes acknowledged that the definition of substantive reasonableness is “obviously circular” in that it “define[s] as unreasonable a sentence that cannot be located within the range of permissible decisions.”<sup>17</sup>

In reckoning with this circular standard, the

court drew on a range of concepts from other areas of the law in an effort to give greater meaning to the concept of “substantive unreasonableness.”

Substantive unreasonableness, the court wrote, can be likened to the “manifest injustice” standard employed in determining whether to grant a motion for a new trial in a criminal case or the “shocks-the-conscience” standard used in cases involving intentional torts by state actors. Applying these standards to the *Rigas* sentences, the court concluded that the sentences at issue were not substantively unreasonable.

### Conclusion

While the Second Circuit has not provided numerical targets or hard-and-fast rules as to what constitutes a substantively unreasonable sentence, the *Rigas* decision makes clear that only a sentence that is “shockingly high, shockingly low, or otherwise unsupported as a matter of law” is substantively unreasonable.<sup>18</sup>

Furthermore, the Second Circuit has already held that policy disagreements with the guidelines, which would presumably include disagreements with the methodology used to calculate loss, are not unreasonable.<sup>19</sup> In light of this increasingly deferential appellate standard of review, we are unlikely to see many sentences overturned as substantively unreasonable, and may, in turn, see more non-guideline sentences in the face of extraordinarily high guideline ranges driven by the amount of loss.

1. *United States v. Treacy*, No. 08 Cr. 366 (S.D.N.Y.), Government Sentencing Memorandum, dated Aug. 26, 2009, at 2.

2. *Id.* at 11, 24, 44.

3. *Id.* at 86-87.

4. *United States v. Ferguson*, No. 3:06-cr-00137-CFD (D. Conn.), Government Sentencing Memorandum, dated Sept. 5, 2008, at 6.

5. *United States v. Ferguson*, 584 F. Supp. 2d 447, 455 (D. Conn. 2008).

6. *United States v. Stimm*, No. 07-CR-00113 (NG) (E.D.N.Y.), Sentencing Tr. dated April 29, 2009, at 25, 27.

7. *Id.* at 41.

8. *Id.* at 41, 43.

9. *Id.* at 42-43.

10. *United States v. Dreier*, No. 09 CR 00085 (JSR) (S.D.N.Y.), Government Sentencing Memorandum, dated July 8, 2009, at 11; Defendant's Sentencing Memorandum, dated July 8, 2009, at 3.

11. *United States v. Dreier*, Sentencing Tr. dated July 13, 2009, at 27.

12. *Id.* at 45.

13. *Id.* at 46.

14. Madoff was sentenced to 150 years in prison. In *Dreier*, Judge Rakoff distinguished to the Madoff sentence, stating that “Mr. Dreier's crimes, despicable though they may be, pale in comparison to Mr. Madoff's, whether in terms of loss or the length of the fraud or the number of the victims or the misery created.” *Id.* at 43.

15. *United States v. Adelson*, 441 F. Supp. 2d 506, 512 (S.D.N.Y. 2006), *aff'd*, 237 Fed. Appx. 713 (2d Cir. 2008). In addition, Judge Frederic Block has described the Sentencing Guidelines for white collar crimes as “a black stain on common sense.” *United States v. Parris*, 573 F. Supp. 2d 744, 745 (E.D.N.Y. 2008).

16. *United States v. Rigas*, Nos. 08-3485-cr (L), et al. (2d Cir. Oct. 5, 2009).

17. *Id.* at 18 (internal quotation marks omitted).

18. *Id.* at 19-20.

19. *United States v. Cavera*, 550 F.3d 180, 191 (2d Cir. 2008); see also Alan Vinegrad and Douglas Bloom, Cavera, Adelson: Second Circuit Gives Truly Advisory Guidelines, 240 NYLJ 3 (Col. 1) (Dec. 17, 2008).