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United States District Court
for the Northern District of California
San Jose Division, Judge Edward J. Davila Presiding

United States of America, **Plaintiff,**	**Case No. CR 09-00670-EJD** **Case No. CR 11-00554-EJD**
vs.	**Defendant Foley's Supplementary Motion per Local Rule 32-5(b) for Downward Departure or Variance and Request for Findings of Fact re Sentencing Objections to the Guideline Sentencing Recommendation ["GSR"] That Remain Unresolved**
DAVID RUSSELL FOLEY AND, MICHAEL DADDONA, **Defendants.**	**Date for Sentencing: December 18, 2013** **Time: 9:00 A.M.** **Court: Honorable Edward J. Davila**

Request for Amended Probation Report, Findings of Fact re Sentencing Objections to PSR and Downward Departure or Variance

Introduction/Synopsis

Pursuant to Local Rule 32-5(b), David Russell Foley, by counsel, hereby files this *Request for Amended Probation Report, Evidentiary Hearing, Findings of Fact and Downward Departure or Variance* in anticipation of Mr. Foley's sentencing hearing now set for December 18, 2013, at 9:00 A.M. This motion is styled by counsel as "*Supplementary*," because Mr. Foley filed an earlier *Motion for Downward Departure and for Evidentiary Hearing*. At the last court appearance, the court's partial response to the earlier motion, was to rule that the court's findings entered on January 29, 2013, as to the

subject of the loss enhancement calculation for the GSR was final and that the court would receive no further evidence on that topic. The court then continued the matter for a sentencing hearing to December 18, 2013, in order, among other things, to rule on Mr. Foley's numerous objections to the GSR.

This supplementary motion is predicated on the confident belief that this court has long been familiar with the holdings of the United States Supreme Court in certain controlling cases which will be referenced by their shorter names of *Apprendi*, *Blakely*, *Booker, Rita, Gall*, *Kimbrough, and Spears*.[1]

The grounds for these motions are set out in the following enumerated documents and are therefore incorporated by reference.

1) ATTACHED STATEMENT OF DEFENDANT DAVID R. FOLEY in support of this *Motion for Downward Departure or Variance* to the *Guideline Sentencing Recommendation* in which he personally addresses the § 3553 factors in the case [hereinafter, the "GSR"].
2) A PROFFERED STATEMENT OF DAVID R. FOLEY FOR ALLOCUTION OR TESTIMONY AT SENTENCING, IN THE COURT'S DISCRETION;
3) PREVIOUS ATTACHMENT ONE TO REQUEST FOR EVIDENTIARY HEARING OF DEFENDANT DAVID FOLEY. (This is Mr. Foley's personal statement addressing the content of the Final Presentence Investigation Report that was submitted to the Court by the USPO on August 5, 2013.
4) STATEMENT OF DAVID R. FOLEY. (This is Mr. Foley's original personal statement that he submitted to Probation Officer Flores to assist in preparation of the *draft* Presentence Investigation Report.)
5) OBJECTIONS OF DAVID RUSSELL FOLEY TO PRESENTENCE INVESTIGATION REPORT. (This is the set of objections that Mr. Foley submitted as to the *draft* report (as distinguished from the *final* report) of Probation Officer Flores.)

The United States Probation Office (USPO) has called no presentence conference regarding unresolved objections to the Final Presentence Report pursuant to FrCrP 32(b)(6)(B) and Local Rule 32-4(d). Mr. Foley has identified numerous unresolved objections in the Final Presentence Report, and pursuant to Local Rule 32-5(b)(1), Mr. Foley has elaborated on these objections and articulated additional objections in both a previous statement and one attached to this sentencing memorandum. Mr. Foley requests an evidentiary hearing and findings of fact to resolve all of the objections enumerated in his attached statement.

[1] *Apprendi v. New Jersey* (2000) 530 U.S. 466; *Blakely v. Washington* (2004) 542 U.S. 296; *United States v. Booker* (2005) 543 U.S. 220; *Rita v. United States* (2007) 551 U.S. 338; *Gall v. United States* (2007) 552 U.S. 38; *Kimbrough v. United States* (2007) 552 U.S. 85; *Spears v. United States* (2009) 555 U.S. 135.

Mr. Foley requests a downward departure and grant of probation with conditions at the court's discretion primarily on the grounds that stated in this memorandum and in his attached written statement.

Introduction.

This case did not go to trial, but it has generated two evidentiary proceedings to date: a grand jury proceeding of some length, and a "loss" hearing before this court solely for the purpose of determining "loss" within the meaning of U.S. Sentencing Guideline 2.B.1.1, the "fraud guideline," and more to the point, to determine the applicability (or not) of a specific offense characteristic (loss amount) per the loss table set out at 2.B.1.1.(b) of the guidelines.[2]

The facts of the case have been well briefed previously by both the Government and previous defense counsel, both before and after the loss hearing that the court conducted on December 6, 2012, and December 11, 2012. The Federal Probation Office was represented at these hearings and offered insightful and prescient observations at the time of the court's ruling as to loss on January 29, 2013.[3] The case has presented the

[2] Where is is necessary to refer to the transcripts of these proceedings in this memorandum, the notation will be to "GJTX" for the grand jury proceedings, and "LHTX" for the transcript of the loss hearing proceedings on 12/06/12, 12/11/12, and 1/29/13.

[3] **PROBATION OFFICER:** WELL, I THINK THERE ARE A NUMBER OF ISSUES HERE THAT I'M NOT VERY FAMILIAR WITH AND **THE MOST TELLING ONE FOR ME, YOUR HONOR, IS PREEXISTING INVENTORY PRIOR TO THE ABC**.

I THINK THAT THAT'S SOMETHING THAT THE COURT AND THE PROBATION OFFICE NEEDS TO FOCUS ON. I JUST DON'T KNOW THE ANSWER BECAUSE IF THERE WAS SOME WAY TO DISTINGUISH A PRE-ABC ULTRACADE GAME PACK AND A POST-ABC AND WE COULD DETERMINE WHICH WAS MANUFACTURED OR WHICH WAS PURCHASED BY DADDONA PRIOR TO THE ABC, I THINK THAT HAS AN IMPACT ON ULTIMATELY THE LOSS.

I BELIEVE THAT IT IS IMPROPER IN THIS PARTICULAR TYPE OF CASE TO USE A RETAIL VALUE, AND IN PARTICULAR, A RETAIL VALUE THAT, AS I UNDERSTAND, IS BASED ON A PROJECTION.

I DON'T KNOW THAT—QUITE FRANKLY, I DON'T KNOW WHO THE RETAILER WAS OTHER THAN MR. DADDONA AND IF HE WAS SELLING IT FOR A LOWER PRICE, I MEAN, THAT'S POSSIBLE WHEN YOU BUY IN BULK. [LHTX 01/29/13; 40:25]

SO I THINK THAT THOSE ARE THE ISSUES. I BELIEVE THAT IT'S WHATEVER THE—DEPENDING ON THE TYPE OF PRODUCT, IF IT COSTS A COMPANY $10 TO MANUFACTURE SOMETHING AND THAT PRODUCT IS

Court with a confluence of not commonly understood Federal Sentencing Guideline application [2.B.1.1], a bit of electronic game technology ["key fob burners"] and the jargon of the high-tech business world in Silicon Valley ["MOU's and ABC's"].

A 641-word summary of a complex case, primarily for chronology.

In late 2005, as the national economy entered the doldrums, and the market for certain electronic entertainment products declined, two business entities, Global VR, and a smaller company, UltraCade, were looking for new ways to survive financially. Global VR noticed UltraCade and perceived some clear and exciting potential for profit in some, but not all, of the smaller company's assets, product line, human resources and business activities. After some negotiations between officers of the companies (primarily James DeRose for Global VR, and David Foley for UltraCade) the two companies entered into an agreement on December 8, 2005, (the Memorandum of Agreement, or "MOU"). The

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STOLEN, THEN IT'S $10 THAT THAT COMPANY LOST.

SO I WOULD SAY REPLACEMENT VALUE AS OPPOSED TO RETAIL VALUE.

BUT I'D HAVE TO LOOK AT IT A LITTLE BIT CLOSER. **BUT TO ME THE BIGGEST ISSUE IS CAN THE COURT USE, IF THERE'S A WAY TO DETERMINE, AND MY UNDERSTANDING IS THAT IT MAY BE A LITTLE BIT DIFFICULT, INVENTORY THAT EXISTED PRIOR TO THE ABC, PRIOR TO THE JUNE 2006?**

I DON'T KNOW THAT THE COURT CAN USE THAT INDIVIDUAL GAME PACK VALUE ON SOMETHING THAT WAS OTHERWISE LEGALLY ACQUIRED. I DON'T KNOW THAT ANSWER. THAT SEEMS TO ME MORE OF A CIVIL QUESTION IN TERMS OF PRODUCT LIABILITIES AND SO FORTH.

THE OTHER THING THAT I WOULD LOOK AT IS THAT AS MS. KNIGHT POINTED OUT, WE ALSO NEED TO DETERMINE IF THERE IS ANY RESTITUTION. SO THOSE ARE TWO DIFFERENT THINGS, THE LOSS AND THEN THERE IS THE RESTITUTION.

SO IF LOST PROFITS ARE $150 PER GAME PACK, AND WE KNOW HOW MANY GAME PACKS WERE ACTUALLY SOLD AND MANUFACTURED, MANUFACTURED AND SOLD AFTER JUNE 2006, THEN THAT WOULD BE SOMETHING THAT WE WOULD BE LOOKING AT FOR RESTITUTION AND IN THIS PARTICULAR CASE I THINK THAT IN THIS TYPE OF A FRAUD IT WOULD BE ALMOST THE SAME FIGURE, THE LOSS FIGURE AND THE RESTITUTION FIGURE. [LHTX 01/29/13; 41:1-25]

THE COURT: OKAY.

PROBATION OFFICER: SO THOSE ARE THE TYPES OF ISSUES THAT I'M LOOKING AT.

AS FAR AS THE MORTGAGE LOAN, I THINK WE'RE SETTLED ON THAT, OTHER THAN I NEED TO SEE THAT THE VALUE OF THE—THE FAIR MARKET VALUE OF THE COLLATERAL EXCEEDS THE AMOUNT OF THE LOAN.

IF THE HOUSE IS WORTH 2 MILLION TODAY, AND THE LOAN IS 3 MILLION, THEN THE BANK WOULD STILL BE OUT 1 MILLION. SO THERE WOULD STILL BE SOME TYPE OF A LOSS ON THE MORTGAGE SIDE. SO THAT'S THE OTHER THING I MENTIONED EARLIER.

QUICKLY?

THE COURT: OKAY. THANK YOU FOR THOSE OBSERVATIONS. [LHTX 01/29/13; 42:1-18]

primary purpose of the MOU was to document written evidence of the intentions of the companies to carry out a later acquisition of UltraCade by Global VR. The immediate challenge was to keep UltraCade alive as a business entity, and to get a handle on Mr. Foley's personal financial situation. One step the companies took was for Global VR to act as a sort of sales agent for incoming purchase orders of UltraCade's game packs (thumb drives with games on them). For this service Global VR took a 15 per cent charge, presumably off the gross sales price. Global VR expected the revenue from the sale of the game packs would offset some of the financial disbursements it was making on behalf of the UltraCade company and Mr. Foley.

In accordance with the MOU, the two companies then entered into what is known as the "due diligence" period (90 days in this case) in which Global VR officers and others would carefully examine the state of Ultracade, particularly its financial health. Sadly, Global VR discovered that UltraCade had the business equivalent of terminal cancer. To make things worse, Global VR was in no condition itself to assume both the business-related debt load that was crushing the UltraCade entity and the personal debt load of UltraCade's CEO, David Foley.

Deciding firmly against an outright purchase of UltraCade, Mr. DeRose sounded the alarm to all concerned and then immediately sought other ways for Global VR to get the benefits of UltraCade without the burdens, or in any event, without the full load of burdens. DeRose chose an assignment for the benefit of creditors ("ABC") as a favorable mechanism for doing this, and so on Friday, June 2, 2006, Global VR and UltraCade, executed this arrangement. By doing so, Global VR effectively absorbed UltraCade at a cost far more favorable than it would have incurred in a straight purchase or in a bankruptcy proceeding of UltraCade—it looked like a good idea at the time.

But by June 2, 2006, most certainly, and even much earlier, Mr. DeRose noticed that the revenue stream that he expected UltraCade to generate with the sale of game packs had all but dried up. After investigating the matter, Mr. DeRose concluded that David Foley had been selling game packs to Mr. Dadonna contrary to the provisions of the MOU and the ABC.

On Friday, September 22, 2006, Mr. DeRose had a long telephone conference call with Mr. Dadonna on the east coast. Dadonna was a distributor (a middleman in the distribution chain between wholesalers like UltraCade and Global VR on the one hand, and consumers on the other) of the game packs produced by UltraCade. In that conversation, Mr. DeRose confirmed his worst fears and heretofore unconfirmed suspicions about the revenue stream expected from the sale of game packs: Mr. Foley had been selling game packs to Dadonna independent of Global VR.

The next day, Saturday, September 23, 2006, Mr. DeRose terminated Global VR's employment agreement with David Foley, an agreement which had been formed in the ABC of June 2, 2006.

Eventually, Mr. DeRose brought these facts to the attention of the FBI, which ultimately resulted in this prosecution of Mr. Foley and Mr. Dadonna.

The court should consider the value of UltraCade to Global VR as a credit against the $450,000 loss that the court determined on January 29, 2013.

Backing up the punitive loss table provision in guideline 2.B.1.1. for the calculation of a numerical sentencing enhancement for "loss," is the following application note which finds its origin in Amendment 617 of the guidelines:

Application Notes:

3. Loss Under Subsection (b)(1).—This application note applies to the determination of loss under subsection (b)(1).

(E) Credits Against Loss.—Loss shall be reduced by the following:

(i) The money returned, and the fair market value of the property returned and the services rendered, by the defendant or other persons acting jointly with the

> *defendant, to the victim before the offense was detected. The time of detection of the offense is the earlier of (I) the time the offense was discovered by a victim or government agency; or (II) the time the defendant knew or reasonably should have known that the offense was detected or about to be detected by a victim or government agency.*

A strictly literal interpretation of the word "returned" in this provision can produce absurd results. For example, if a person commits a federal offense of fraud in acquiring a shipping container of oranges worth $100,000, but later (and before the "time of detection") leaves a note in an envelope for the victim saying, "I'm sorry I took your oranges the way I did. Here is $50,000 thousand dollars in cash." If the word "returned" is limited in comment note 3.(E)(i) to mean that the perpetrator of the fraud must return exactly the same oranges to benefit from the specified exclusion, then the exclusion would probably never apply.

The Sentencing Commission never intended that the loss sentencing enhancement of 2.B.1.1., which has long been recognized as a proxy for the seriousness of the offense, be applied that in that strictly literal sense. The Commission intended something broader and more just, but came up short in choosing a more appropriate word. To understand this requires a closer examination of Amendment 617 in Appendix C of the U.S. Sentencing Guidelines. The Commission has provided Appendix C in entirety on its web site as part of Amendment 617.

What follows is verbatim excerpt, from the **"Reason for the Amendment:"** found in Appendix C—Volume II, Amendment 617, of the U.S. Sentencing Guidelines. Regrettably, not all the paragraphs of Amendment 617 are numbered, but the pagination as it appears on the web is preserved:

Appendix C—Volume II, Amendment 617 [pages 172 to 182]

Reason for Amendment: This "Economic Crime Package" is a six-part amendment that is the result of Commission study of economic crime issues over a

number of years. The major parts of the amendment are: (1) consolidation of the theft, property destruction, and fraud guidelines; (2) a revised, common loss table for the consolidated guideline, and a similar table for tax offenses; (3) a revised, common definition of loss for the consolidated guideline; (4) revisions to guidelines that refer to the loss table in the consolidated guideline; (5) technical and conforming amendments; and (6) amendments regarding tax loss.

Consolidation of Theft, Property Destruction, and Fraud; Miscellaneous Revisions

The first part of this amendment consolidates the guidelines for theft, §2B1.1 (Larceny, Embezzlement, and Other Forms of Theft; Receiving, Transporting, Transferring, Transmitting, or Possessing Stolen Property), property destruction, §2B1.3 (Property Damage or Destruction), and fraud, §2F1.1 (Fraud and Deceit; Forgery; Offenses Involving Altered or Counterfeit Instruments Other than Counterfeit Bearer Obligations of the United States) into one guideline, §2B1.1 (Theft, Property Destruction, and Fraud). Consolidation will provide similar treatment for similar offenses for which pecuniary harm is a major factor in determining the offense level and, therefore, decrease unwarranted sentencing disparity that may be caused by undue complexity in the guidelines. Consolidation addresses concerns raised over several years by probation officers, judges, and practitioners about the difficulties of determining for particular cases, whether to apply §2B1.1 or §2F1.1 and the disparate sentencing outcomes that can result depending on that decision. Commentators have noted that inasmuch as theft and fraud offenses are conceptually similar, there is no strong reason to sentence them differently.

The base offense level for the consolidated guideline is level 6. This maintains the base offense level for fraud offenses, but represents a two-level increase for theft and property destruction offenses, which prior to this amendment was level 4. The increase of two levels in the base offense levels for theft and property destruction offenses will have minimal impact for low-level theft offenses involving offenders in criminal history Category I or Category II. Commission analysis indicates that only a few defendants will move from Zone A (where probation without conditions of confinement is possible) to Zone B or Zone C, and those that are moved into a zone at higher offense levels in the Sentencing Table generally will have criminal history categories above Category I. As a result, the Commission decided against promulgating a two-level reduction for offenses involving loss amounts less than $2,000.

The amendment deletes the two-level enhancement for more than minimal planning previously at §§2B1.1(b)(4)(A) and 2F1.1(b)(2)(A). The two-fold reason for this change was to obviate the need for judicial fact-finding about

this frequently occurring enhancement and to avoid the potential overlap between the more than minimal planning enhancement and the sophisticated means enhancement previously at §2F1.1(b)(6) and now, by this amendment, at §2B1.1(b)(8).

– 172 –

The amendment also eliminates the alternative prong of the more than minimal planning enhancement, at §2F1.1(b)(2)(B) prior to this amendment, which provided a two-level increase if the offense involved more than one victim. The amendment replaces this enhancement with a specific offense characteristic for offenses that involved large numbers of victims. This change addresses three concerns. First, as a result of the consolidation, the more-than-one-victim enhancement, if retained, would apply in cases that, prior to this amendment, were not subject to such an enhancement. Second, a two-level increase in every case involving more than one victim is arguably inconsistent with the approach in subsection (b)(2) of §3A1.1 (Hate Crime Motivation or Vulnerable Victim), which provides a two-level increase if the offense involved a large number of vulnerable victims. Third, in practice, the more than minimal planning enhancement was so closely linked with this enhancement that the decision to eliminate the former argues strongly for also eliminating the latter.

The amendment provides a two-level enhancement for offenses involving ten or more, but fewer than 50, victims, and a four-level increase for offenses involving 50 or more victims. This provision is designed to provide a measured increment that results in increased punishment for offenses involving larger numbers of victims. Its applicability to those cases in which victims, both individuals and organizations, sustain an actual loss under subsection (b)(1) or sustain bodily injury.

A special rule is provided for application of the victim enhancement for offenses involving United States mail because of (i) the unique proof problems often attendant to such offenses, (ii) the frequently significant, but difficult to quantify, non-monetary losses in such offenses, and (iii) the importance of maintaining the integrity of the United States mail.

In addition, the amendment moves the mass-marketing enhancement into the new victim- related specific offense characteristic, as an alternative to the two-level adjustment for more than ten, but fewer than 50, victims. The

provision is retained to remain responsive to the congressional directive that led to its original promulgation and reflects the Commission's expectation that most telemarketing cases, or similar mass-marketing cases, will have at least ten victims and, receive this enhancement. The mass-marketing alternative enhancement also will continue to apply in cases in which mass-marketing has been used to target a large number of persons, regardless of the number of persons who have sustained an actual loss or injury.

In addition, the amendment provides that if a victim enhancement applies, the enhancement under §3A1.1(b)(2) for "a large number of vulnerable victims" does not also apply because the more serious conduct already would have resulted in a higher penalty level.

In response to issues raised in a circuit conflict, the amendment revises the commentary related to subsection (b)(4)(B) of §2B1.1 to clarify the meaning of "person in the business of receiving and selling stolen property." The amendment addresses an issue that has arisen in case law regarding what conduct receives a defendant for the 4-level enhancement.

In determining the meaning of "in the business of", some circuits apply what has been termed the "fence test", under which the court must consider (1) if the stolen property was bought and sold, and (2) to what extent the stolen property transactions encouraged others to commit property crimes. Other circuits have adopted the "totality of the circumstances test" that focuses on the regularity and sophistication of the defendant's operation. Compare *United States v. Esquivel*, 919 F.2d 957 (5th Cir. 1990), with *United States v. St. Cyr*, 997

– 173 –

F.2d 698 (1st Cir. 1992). Under either test, courts consider the sophistication and regularity of the business as well as the control, volume, turnover, relationship with thieves, and connections with buyers. Although the factors considered by all of these circuits are similar, the approaches are different.

After consideration, the Commission adopted the totality of circumstances approach because it is more objective and more properly targets the conduct of the individual who is actually in the business of fencing. See *United States v. St. Cyr, supra*.

In addition, this amendment resolves a circuit conflict regarding the scope of

the enhancement in the consolidated guideline for a misrepresentation that the defendant was acting on behalf of a charitable, educational, religious, or political organization, or a government agency. (Prior to this amendment, the enhancement was at subsection (b)(4)(A) of §2F1.1). The conflict concerns whether the misrepresentation enhancement applies only in cases in which the defendant does not have any authority to act on behalf of the covered organization or government agency or if it applies more broadly to cases in which the defendant has a legitimate connection to the covered organization or government agency, but misrepresents that the defendant is acting solely on behalf of that organization or agency. Compare, e.g., *United States v. Marcum*, 16 F.3d 599 (4th Cir. 1994) (enhancement appropriate even though defendant did not misrepresent his authority to act on behalf of the organization but rather only misrepresented that he was conducting an activity wholly on behalf of the organization), with *United States v. Frazier*, 53 F.3d 1105 (10th Cir. 1995) (application of the enhancement is limited to cases in which the defendant exploits the victim by claiming to have authority which in fact does not exist).

The amendment follows the broader view of the Fourth Circuit. It provides for application of the enhancement, now, by this amendment, at §2B1.1(b)(7)(A), if the defendant falsely represented that the defendant was acting to obtain a benefit for a covered organization or agency when, in fact, the defendant intended to divert all or part of that benefit (for example, for the defendant's personal gain), regardless of whether the defendant actually was associated with the organization or government agency. The Commission determined that the enhancement was appropriate in such cases because the representation that the defendant was acting to obtain a benefit for the organization enables the defendant to commit the offense. In the case of an employee who also holds a position of trust, the amendment provides an application note instructing the court not to apply §3B1.3 (Abuse of Position of Trust or Use of Special Skill) if the same conduct forms the basis both for the enhancement and the adjustment in §3B1.3.

The amendment implements the directive in section 3 of the College Scholarship Fraud Prevention Act of 2000, Public Law 106–420, by providing an additional alternative enhancement that applies if the offense involves a misrepresentation to a consumer in connection with obtaining, providing, or furnishing financial assistance for an institution of higher education. The enhancement targets the provider of the financial assistance or scholarship services, not the individual applicant for such assistance or

scholarship, consistent with the intent of the legislation.

This amendment makes two minor substantive changes to the enhancement for conscious or reckless risk of serious bodily injury, now, by this amendment, at subsection (b)(11)(A). First, it increases the minimum offense level from level 13 to level 14 to promote proportionality within this guideline. For example, within the theft and fraud guidelines

– 174 –

prior to this amendment, there were other specific offense characteristics that had a higher floor offense level than the risk of bodily injury enhancement: (1) "chop shops" (level 14); (2) jeopardizing the solvency of a financial institution (level 24); and (3) personally receiving more than $1,000,000 from a financial institution (level 24). Second, it inserts "death" before the term "or serious bodily injury" to clarify that the risk of the greater harm also is covered. Including risk of death also provides consistency with similar provisions in other parts of the Guidelines Manual, where risk of death is always included with risk of serious bodily injury.

The amendment modifies the four-level increase and minimum offense level of level 24 for a defendant who personally derives more than $1,000,000 in gross receipts from an offense that affected a financial institution, now, by this amendment, at subsection (b)(12)(A). The amendment retains the minimum offense level but reduces the four-level enhancement to two levels because of the increased offense levels that will result from the loss table for the consolidated guideline. The two-level increase was retained because elimination of the enhancement entirely would not provide an appropriate punishment for those offenders involved with losses that are in the $1,000,000 to $2,500,000 range of loss.

The enhancement also was modified to address issues about what it means to "affect" a financial institution and how to apply the enhancement to a case in which there are more than one financial institution involved. Accordingly, the revised provision focuses on whether the defendant derived more than $1,000,000 in gross receipts from one or more financial institutions as a result of the offense.

The amendment includes a new cross reference (subsection (c)(3)) that is more generally applicable and intended to apply whenever a broadly applicable fraud statute is used to reach conduct that is addressed more

specifically in another Chapter Two guideline. Prior to this amendment, the fraud guideline contained an application note that instructed the user to move to another, more appropriate Chapter Two guideline, under specified circumstances. Although this note was not a cross reference, but rather a reminder of the principles enunciated in §1B1.2, it operated like a cross reference in the sense that it required use of a different guideline.

This amendment also makes a minor revision (adding "in a broader form") to the background commentary regarding the implementation of the directive in section 2507 of Public Law 101–647, nullifying the effect of *United States v. Tomasino*, 206 F. 3d 739 (7th Cir. 2000).

Loss Tables

The amendment provides revised loss tables for this consolidated guideline and for the tax offense guidelines. A principle feature of the new tables is that they expand the previously existing one-level increments into two-level increments, thus increasing the range of losses that correspond to an individual increment, compressing the table, and reducing fact-finding. The new loss tables also provide substantial increases in penalties for moderate and higher loss amounts, even, for fraud and theft offenses, notwithstanding the elimination of the two- level enhancement for more than minimal planning. These higher penalty levels respond to comments received from the Department of Justice, the Criminal Law Committee of the Judicial Conference, and others, that the offenses sentenced under the guidelines consolidated by this amendment under-punish individuals involved with moderate and high loss amounts, relative to penalty levels for offenses of similar seriousness sentenced under

– 175 –

other guidelines.

Some offenders accountable for relatively low dollar losses will receive slightly lower offense levels under the new loss table for the consolidated guideline because of (1) the elimination of the enhancement for more than minimal planning; (2) the change from one- level to two-level increments for increasing loss amounts; (3) the selection of the breakpoints for the loss increments (including $5,000 as the first loss amount that results in an increase); and (4) the slope chosen for the relationship between increases in loss amount and increases in offense level at the lower loss amounts. This

amendment reflects a decision by the Commission that this effect on penalty levels at lower loss amounts is appropriate for several reasons: (1) the lower offense levels provide appropriate deterrence and punishment, generally, (2) at lower offense levels more defendants will be subject to the court's ability to fashion sentencing alternatives as appropriate (see, e.g., §5C1.1 (Imposition of a Term of Imprisonment)); and (3) these penalty levels may facilitate the payment of restitution.

The loss table for the consolidated guideline provides the first of incremental increases for cases in which loss exceeds $5,000, rather than $2,000 provided previously in §2F1.1, or $100 provided previously in §2B1.1. The Commission believes this will reduce the fact- finding burden on courts for less serious offenses that are generally subject to greater sentencing flexibility because of the availability of alternatives to incarceration.

The amendment also provides a revised loss table in §2T4.1 (Tax Table) for tax offenses that ensures significantly higher penalty levels for offenses involving moderate and high tax loss in a similar manner and degree as the loss table for the consolidated guideline. The new table is designed to reflect more appropriately the seriousness of tax offenses and to maintain proportionality with the offenses sentenced under the consolidated guideline.

The tax loss table is similar to the loss table for the consolidated guideline, except it does not reduce generally any sentences for offenders involved with lower loss amounts. The tax table provides its first increment for loss at $2,000, rather than the $5,000 threshold under the consolidated guideline (and the $1,700 threshold under the tax loss table prior to this amendment). These differences are intended to avoid unintended decreases that would occur otherwise. The increases in the new tax loss table for offenders involved with lower loss amounts are intended to maintain the long-standing treatment of tax offenses relative to theft and fraud offenses.

Definition of Loss

This amendment provides a new definition of loss applicable to offenses previously sentenced under §§2B1.1, 2B1.3, and 2F1.1. The revised definition makes clarifying and substantive revisions to the definitions of loss previously in the commentary to §§2B1.1 and 2F1.1, resolves a number of circuit conflicts, addresses a variety of application issues, and promotes consistency in application.

Significantly, the new definition of loss retains the core rule that loss is the greater of actual and intended loss. The Commission concluded that, for cases in which intended loss is greater than actual loss, the intended loss is a more appropriate initial measure of the culpability of the offender. Conversely, in cases which the actual loss is greater, that amount is a more appropriate measure of the seriousness of the offense.

– 176 –

A definition is provided for intended loss that is consistent with the rule regarding the interaction of actual and intended loss.

The amendment includes a resolution of the circuit conflict relating to the meaning and application of intended loss.

The amendment resolves the conflict to provide that intended loss includes unlikely or impossible losses that are intended, because their inclusion better reflects the culpability of the offender. Compare *United States v. Geevers*, 226 F.3d 186 (3d Cir. 2000) (agreeing with the majority of circuits holding that impossibility is not in and of itself a limit on the intended loss for purposes of calculating sentences under the guidelines . . . impossibility does not require a sentencing court to lower its calculations of intended loss); and *United States v. Coffman*, 94 F.3d 330 (7th Cir. 1996) (rejecting the argument that a loss that cannot possibly occur cannot be intended); *United States v. Koenig*, 952 F.2d 267 (9th Cir. 1991) (holding that §2F1.1 only requires a calculation of intended loss and does not require a finding that the intentions were realistic); *United States v. Klisser*, 190 F. 3d 34, 36 (2d Cir. 1999) (same); *United States v. Blitz*, 151 F. 3d 1002, 1010 (9th Cir. 1998) (same); *United States v. Studevent*, 116 F. 3d 1559, 1563 (D.C. Cir. 1997) (same); *United States v. Wai- Keung*, 115 F. 3d 874, 877 (11th Cir. 1997) (same), with *United States v. Galbraith*, 20 F. 3d 1054, 1059 (10th Cir. 1993) (because intended loss only includes losses that are possible, in an undercover sting operation the intended loss is zero); and *United States v. Watkins*, 994 F.2d 1192, 1196 (6th Cir. 1993) (holding that a limitation on the broad reach of the intended loss rule is that the intended loss must have been possible to be considered relevant).

Accordingly, concepts such as "economic reality" or "amounts put at risk" will no longer be considerations in the determination of intended loss. See *United States v. Bonanno*, 146 F.3d 502 (7th Cir. 1998) (holding that the

relevant inquiry is how much the scheme put at risk); and *United States v. Wells*, 127 F. 3d 739 (8th Cir. 1997) (citing *United States v. Morris*, 18 F.3d 562 (8th Cir. 1994)) (holding that intended loss properly was measured by the possible loss the defendant intended, and did not hinge on actual or net loss).

This amendment also resolves differing circuit interpretations of the standard of causation applicable for actual loss, an issue that was not addressed expressly in the prior definition of actual loss. Various circuits recognized three arguably inconsistent standards for loss causation. First, §1B1.3 (Relevant Conduct) provides that a defendant is responsible for all losses – foreseen or unforeseen – that result from the defendant's actions or that result from the foreseeable actions of co-participants. See *United States v. Sarno*, 73 F.3d 1470 (9th Cir. 1995) (holding that "[a] sentence calculated pursuant to the loss tables . . . is properly based on actual loss notwithstanding the fact that this loss may be greater than the intended, expected or foreseeable loss"), cert. denied, 518 U.S. 1020 (1996); and *United States v. Lopreato*, 83 F.3d 571 (2d Cir. 1996) (holding that in a bribery case, the defendant is responsible for all losses, foreseeable or not). A second view is premised on the fact that prior to this amendment commentary in §2F1.1 limited the loss amount to the value of the money, property, or services unlawfully taken. See *United States v. Marlatt*, 24 F.3d 1005 (7th Cir. 1994) (refusing to count foreseeable losses in loss figure because they did not represent the actual thing taken). A third view is that the commentary's explicit inclusion of consequential damages in the loss determination for contract procurement and product substitution cases implies that only non-consequential or direct damages are included in other cases. See *United States v. Thomas*, 62 F.3d 1332 (11th Cir. 1995), cert. denied, 516 U.S. 1166 (1996) (only non-consequential or direct damages are included in loss). See also

—177—

United States v. Daddona, 34 F.3d 163 (3d Cir.), cert. denied, 513 U.S. 1002 (1994) (holding that merely incidental or consequential damages may not be counted in computing loss); and *United States v. Newman*, 6 F.3d 623 (9th Cir. 1993) (holding that loss caused by the defendant arsonist was only the value of the property destroyed by the fire, not costs of putting out the fire).

The amendment defines "actual loss" as the "reasonably foreseeable pecuniary harm" that resulted from the offense. The amendment incorporates this causation standard that, at a minimum, requires factual causation (often

called "but for" causation) and provides a rule for legal causation (i.e., guidance to courts regarding how to draw the line as to what losses should be included and excluded from the loss determination). Significantly, the application of this causation standard in the great variety of factual contexts in which it is expected to occur appropriately is entrusted to sentencing judges.

"Pecuniary harm" is defined in a manner that excludes emotional distress, harm to reputation, and other non-economic harm, in order to foreclose the laborious effort sometimes necessary to quantify non-economic harms (as in some tort proceedings, for example).

"Reasonably foreseeable pecuniary harm" is defined to include pecuniary harms that the defendant knew or, under the circumstances, reasonably should have known, was a potential result of the offense. The Commission determined that this standard better ensures the inclusion in loss of those harms that reflect the seriousness of the offense and the culpability of the offender.

The definition deletes the previous rule that, by negative implication, excludes consequential damages (except in specified cases), thus resolving a circuit conflict. Compare *United States v. Izydore*, 167 F.3d 213 (5th Cir. 1999) (the fact that the Commission prescribed consequential losses in only specific fraud cases, and not others, is strong evidence that consequential damages were omitted from the general loss definition by design rather than mistake), with *United States v. Gottfried*, 58 F.3d 648 (D.C. Cir. 1995) (holding that merely incidental or consequential damages may not be counted in computing loss). The Commission decided, however, not to use the term "consequential damages," or any similar civil law distinction between direct and indirect harms. Rather, the Commission determined that the reasonable foreseeability standard provides sufficient guidance to courts as to what type of harms are included in loss.

In addition, this amendment preserves the special provisions addressing loss in protected computer offenses and the inclusion of consequential damages in product substitution and contract procurement offenses; however, these special cases are re-characterized as rules of construction to avoid any negative implications regarding other types of offenses.

The amendment reflects a decision by the Commission that interest and

similar costs shall be excluded from loss. However, the amendment provides that a departure may be warranted in the rare case in which exclusion of interest will under-punish the offender. Thus, the rule resolves the circuit split regarding whether "bargained for" interest may be included in loss. Compare *United States v. Henderson*, 19 F.3d 917 (5th Cir.), cert. denied, 513 U.S. 877 (1994) (holding that interest should be included if the victim had a reasonable expectation of receiving interest from the transaction); *United States v. Gilberg*, 75 F.3d 15 (1st Cir. 1996) (including in loss interest on fraudulently procured mortgage loan); and *United States v. Sharma*, 190 F.3d 220 (3d Cir. 1999) (holding that Application Note 8 of

—178—

§2F1.1 requires the exclusion of "opportunity cost" interest, but did not intend to exclude bargained-for interest), with *United States v. Hoyle*, 33 F.3d 415 (4th Cir. 1994), cert. denied, 513 U.S. 1133 (1995) (excluding interest from the determination of loss for sentencing purposes); and *United States v. Guthrie*, 144 F.3d 1006 (6th Cir. 1998) (holding that when the defendant concealed assets in a bankruptcy proceeding, the lower court's determination that loss to creditors included interest was erroneous). This rule is consistent with the general purpose of the loss determination to serve as a rough measurement of the seriousness of the offense and culpability of the offender and avoids unnecessary litigation regarding the amount of interest to be included.

The loss definition also excludes from loss certain costs incurred by the government and victims in connection with criminal investigation and prosecution of the offense. Such losses are likely to occur in a broad range of cases, would present a fact-finding burden in those cases, and would not contribute to the ability of loss to perform its essential function.

The loss definition also provides for the exclusion from loss of certain economic benefits transferred to victims, to be measured at the time of detection. This provision codifies the "net loss" approach that has developed in the case law, with some modifications made for policy reasons. This crediting approach is adopted because the seriousness of the offense and the culpability of a defendant is better determined by using a net approach. This approach recognizes that the offender who transfers something of value to the victim(s) generally is committing a less serious offense than an offender who does not.

The amendment adopts "time of detection" as the most appropriate and least burdensome time for measuring the value of the transferred benefits. The Commission determined that valuing such benefits at the time of transfer would be especially problematic in cases in which the offender misrepresented the value of an item that is difficult to value. Although the time of detection standard will allow some fluctuation in value which may inure to the defendant's benefit or detriment, the Commission determined that, because the time of detection is closer in time to the sentencing and occurs at a point when the authorities are aware of the criminality, its use generally would make it easier to determine a more accurate value of the benefit.

The definition of "time of detection" was adopted because there may be situations in which it is difficult to prove that the defendant knew the offense was detected even if it was already discovered. In addition, the words "about to be detected" are included to cover those situations in which the offense is not yet detected, but the defendant knows it is about to be detected. In such a case, it would be inappropriate to credit the defendant with benefits transferred to the victim after that defendant's awareness.

The definition of "loss" also provides special rules for certain schemes. One rule includes in loss (and excludes from crediting) the benefits received by victims of persons fraudulently providing professional services. This rule reverses case law that has allowed crediting (or exclusion from loss) in cases in which services were provided by persons posing as attorneys and medical personnel. See *United States v. Maurello*, 76 F.3d 1304 (3d Cir. 1996) (calculating loss by subtracting the value of satisfactory legal services from amount of fees paid to a person posing as a lawyer); and *United States v. Reddeck*, 22 F.3d 1504 (10th Cir. 1994) (reducing loss by the value of education received from a sham university). The Commission determined that the seriousness of these offenses and the culpability of these offenders is best reflected by a loss determination that does not credit the value of the

– 179 –

unlicensed benefits provided. In addition, this provision eliminates the additional burden that would be imposed on courts if required to determine the value of these benefits.

Similarly, the definition of loss provides a special rule that includes in loss

(and excludes from crediting) the value of items that were falsely represented as approved by a regulatory agency, for which regulatory approval was obtained by fraud, or for which regulatory approval was required but not obtained. The Commission determined that the seriousness of these offenses and the culpability of these offenders is best reflected by a loss determination that does not credit the value of these items. This decision reflects the importance of the regulatory approval process to public health, safety, and confidence.

Regarding investment schemes, the amendment resolves a circuit conflict regarding whether and how to credit payments made to victims. Compare *United States v. Mucciante*, 21 F.3d 1228 (2nd Cir. 1994) (under the Guidelines, loss includes the value of all property taken, even though all or part of it was returned.); *United States v. Deavours*, 219 F.3d 400 (5th Cir. 2000) (intended loss is not reduced by any sums returned to investors); and *United States v. Loayza*, 107 F.3d 257 (4th Cir.1997) (declining to follow the approach of net loss and holding defendants responsible for the value of all property taken, even though all or a part is returned), with *United States v. Holiusa*, 13 F.3d 1043 (7th Cir.1994) (holding that only the net loss should be included in loss, thus allowing a credit for returned interest), and United *States v. Orton*, 73 F.3d 331 (11th Cir. 1996) (only payments made to losing investors should be credited, not payments to investors who made a profit).

This amendment adopts the approach of the Eleventh Circuit that excludes the gain to any individual investor in the scheme from being used to offset the loss to other individual investors because any gain realized by an individual investor is designed to lure others into the fraudulent scheme. See United States v. Orton, supra.

The definition retains the rule providing for the use of gain when loss cannot reasonably be determined. It clarifies that there must be a loss for gain to be considered. In doing so, the Commission resolved another circuit conflict. Compare *United States v. Robie*, 166 F.3d 444 (2d Cir. 1999) (holding that use of defendant's gain for purposes of subsection (b)(1) is improper if there is no economic loss to the victim), with *United States v. Haas*, 171 F.3d 259 (5th Cir. 1999) (stating that "if the loss is either incalculable or zero, the district court must determine the §2F1.1 sentence enhancement by estimating the gain to the defendant as a result of his fraud"). The Commission decided not to expand the use of gain to situations in which loss can be determined but the gain is greater than the loss because such instances should occur

infrequently, the efficiency of the criminal operation as reflected in the amount of gain ordinarily should not determine the penalty level, and the traditional use of loss is generally adequate.

The amendment revises the special rule on determining loss in cases involving diversion of government program benefits to resolve another circuit conflict. The revision is intended to clarify that loss in such cases only includes amounts that were diverted from intended recipients or uses, not benefits received or used by authorized persons. In other words, even if such benefits flowed through an unauthorized intermediary, as long as they went to intended recipients for intended uses, the amount of those benefits should not be included in loss. Compare *United States v. Henry*, 164 F.3d 1304 (10th Cir. 1999) (holding that loss includes the value of gross benefits paid, rather than the value of benefits improperly received or diverted in determining the loss), with *United States v. Peters*, 59 F.3d 732 (8th

– 180 –

Cir. 1995) (determining that loss is the value of benefits diverted from intended recipients); and *United States v. Barnes*, 117 F.3d 328 (7th Cir. 1997) (holding that the sentence is calculated only on the value of the government benefits diverted from intended recipients or users). This net loss approach is more consistent with general rules for determining loss.

Referring Guidelines for Theft and Fraud

The amendment includes revisions to the guidelines that, prior to this amendment, referred to the loss tables in §2B1.1 or §2F1.1. Pursuant to this amendment, these guidelines will refer to the loss tables in the consolidated guideline. Prior to this amendment, the referring guidelines used the tables in §§2B1.1 and 2F1.1, which provided the first loss increment for losses in excess of $2,000. Because the consolidated loss table provides the first loss increment for losses in excess of $5,000, the referring guidelines are amended to provide a one-level increase in a case in which the loss is more than $2,000, but did not exceed $5,000. This increase is provided to avoid a one-level decrease that would otherwise occur for an offense involving losses of more than $2,000 but not more than $5,000.

Two referring guidelines (§§2B2.1 (Burglary of a Residence or a Structure Other than a Residence) and 2B3.1 (Robbery)) that use the definition of loss previously in §2B1.1 will retain that definition of loss rather than the new

loss definition in the consolidated guideline. The existing definition has not proven problematic for cases sentenced under these guidelines.

Technical and Conforming Amendments

The amendment includes a number of technical and conforming amendments, most of which are necessitated by the consolidation and the deletion of the more than minimal planning enhancement.

Computing Tax Loss

This amendment addresses several issues related to tax loss. It addresses a circuit conflict regarding how tax loss under §2T1.1 (Tax Evasion) is computed for cases that involve a defendant's under-reporting of income on both individual and corporate tax returns. Such a case often arises when (1) the defendant fails to report, and pay corporate income taxes on, income earned by the corporation; (2) the defendant diverts that unreported corporate income for the defendant's personal use; and (3) the defendant fails to report, and to pay personal income taxes on, that diverted income. The amendment provides that the amount of the federal tax loss is the sum of the federal income tax due from the corporation and the amount of federal income tax due from the individual.

The amendment thereby resolves a circuit conflict as to the methodology used to calculate tax loss in cases involving a corporate diversion. Two circuits use a sequential method to aggregate the tax loss. Under this method, the court determines the corporate federal income tax that would have been due, subtracts that amount from the amount diverted to the defendant personally, then determines the personal federal income tax that would have been due on the reduced diverted amount. See *United States v. Harvey*, 996 F.2d 919 (7th Cir. 1993); and *United States v. Martinez-Rios*, 143 F.3d 662 (2d Cir. 1998). The Commission adopted the alternative method used in *United States v. Cseplo*, 42 F.3d 360 (6th Cir. 1994), in which the court determines the corporate federal income tax due on the diverted amount,

– 181 –

and adds that amount to the personal federal income tax due on the total amount diverted. This clarifies the prior rule in Application Note 7 of §2T1.1 that "if the offense involves both individual and corporate tax returns, the tax loss is the aggregate tax loss from the offenses taken together" and reflects

the Commission's conclusion that, in cases of corporate diversions, the method for computing total tax loss adopted by the Sixth Circuit in Cseplo more accurately reflects the seriousness of the total harm caused by these offenses than would be reflected by the alternative method.

In evasion-of-payment tax cases, the Commission amended the definition of "tax loss" to include interest and penalties because, in contrast to evasion-of-assessment tax cases, such amounts appropriately are included in tax loss for such cases. This amendment limits the inclusion of interest or penalties to willful evasion of payment cases under 26 U.S.C. § 7201 and willful failure to pay cases under 26 U.S.C. § 7203. The nature of these cases is such that the interest and penalties often greatly exceed the assessed tax amount constituting the bulk of the harm associated with these offenses.

This amendment also revises the sophisticated concealment enhancement in subsection (b)(2) of §§2T1.1 (Tax Evasion) and 2T1.4 (Aiding, Assisting, Procuring, Counseling, or Advising Tax Fraud) to conform to the sophisticated means enhancement in the consolidated guideline, including imposition of a minimum offense level of level 12. This revision is appropriate inasmuch as certain tax offenses can be committed using sophisticated means in addition to being concealed in a sophisticated manner. Indeed, tax offenses committed in a sophisticated manner are more serious offenses, and reflect a greater culpability on the part of the offender (just as a tax offense concealed in a sophisticated manner reflects greater culpability). Consequently, this revision will allow the enhancement to apply to a somewhat greater range of tax offenses than the previously existing sophisticated concealment enhancement.

In addition, the amendment revises "offshore bank accounts" by substituting "financial" for "bank", to ensure that the enhancement applies to conduct involving similar kinds of accounts, consistent with language in §2S1.1 (Laundering of Monetary Instruments; Engaging in Monetary Transactions in Property Derived from Unlawful Activity). A similar revision is made in §2B1.1.

Effective Date: The effective date of this amendment is November 1, 2001.

—182—

The provision of the excerpt above from Amendment 617 that is most crucial to securing Mr. Foley's Constitutional right to due process of law is the 16th full paragraph which states:

> The loss definition also *provides for the exclusion from loss of certain economic benefits transferred to victims*, to be measured at the time of detection. This provision codifies the "net loss" approach that has developed in the case law, with some modifications made for policy reasons. *This crediting approach is adopted because the seriousness of the offense and the culpability of a defendant is better determined by using a net approach. This approach recognizes that the offender who transfers something of value to the victim(s) generally is committing a less serious offense than an offender who does not.*

Consistent with the spirit and intent of guideline Amendment 617, as explained in its *Reason for Amendment*, the Court has not completed its calculation of "net loss" per the punitive sentencing enhancement loss table of guideline 2.B.1.1., by excluding anything of economic benefit *transferred* by Mr. Foley to Global VR before September 22, 2006.

Even though the mandatory nature of the Guidelines has been eliminated and they are now "advisory" only, *see Booker*, 543 U.S. at 245-46, they must be given "respectful consideration" by the sentencing court, *Kimbrough*, 552 U.S. at 101.

Clearly Amendment 617 to the guidelines contemplates an exclusion of economic benefit *transferred* to the victim in the use of the loss table, and even more clearly, the spirit and intent of the guideline contemplates a calculation is "net loss."

The definition of "net," in this sense is:

> **Net**. That which remains after all allowable deductions, such as charges, expenses, discounts, commissions, taxes, etc. are made. *Black's Law Dictionary*, 1040 (6th ed. 1990).

The "time of detection" of the alleged mail/wire fraud offense of Count One of Indictment No. CR 09000670-EJD is Friday, September 22, 2006. That is the day that Mr. DeRose had a long telephone conversation with Mr. Dadonna about the activities of

Mr. Foley regarding "game packs," and the day before Mr. DeRose terminated Mr. Foley's employment with Global VR.

Now most, if not all, of the evidence adduced at the loss hearing sessions of December 6, 2012, and December 11, 2012, was directed at establishing what Mr. Foley had held back from Global VR, i.e., what he did *not* transfer to Global VR per the ABC, in the period "… beginning on a date unknown, but no later than on or about June, 2006, and continuing on to on or about February, 2008," in the language of the superseding indictment.

However, in the course of introducing evidence at the loss hearing sessions of what Mr. Foley did *not* transfer to Global VR, the Government, in particular, introduced ample documentation as to what he *did* transfer of economic benefit to Global VR before September 22, 2006. The testimony taken at the hearings as well as the MOU documentation and the ABC documentation clearly establish that Mr. Foley transferred economic benefit of *very great value* to Global VR. He transferred his company, UltraCade, and everything that went with it, lock, stock and barrel, to Global VR—with the exceptions so painstakingly highlighted by the Government in its prosecution.

The purchase price that Global VR agreed to pay for the acquisition of UltraCade was $6,343,315, broken down as follows [ABC, §§ 3.1, and 9.2]:

1) $2,724,314—assumed liabilities of NanoTech (Exhibit H);
2) $225,000—payment;
3) $1,460,000—promissory note;
4) $750,000—Peter Feuer;
5) $1,184,000—in Global VR notes:
    a) $550,000;
    b) $350,000;
    c) $250,000;
    d) $34,000.

Arguably the most valuable items of economic benefit that Mr. Foley transferred to Global VR by way of the ABC were the tangible and intangible assets related to casino gaming. In the loss hearing conducted by the court, Mr. DeRose and Chief Financial Officer Giavanittone gave testimony as to the economic benefit that Mr. Foley did transfer to Global VR.[4]

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[4] MR. SINGER: I APOLOGIZE. SIR, DO YOU RECALL A FEBRUARY 7TH, 2006, E-MAIL THAT YOU SENT TO DAVID FOLEY AND BOB GIOVANNETTONE SAYING YOU GOT YOUR HANDS SLAPPED BY LEGAL COUNSEL FOR ENTERING A LICENSE FOR ULTRACADE'S GAMING, CASINO GAMING PROPERTIES IN GLOBAL VR'S NAME? [12-06-12 LHTX; 80:4-25]

MR. SINGER: DO YOU RECALL AUTHORING AN E-MAIL DATED FEBRUARY 7TH, 2006, TO DAVID FOLEY AND BOB GIOVANNETTONE, THE SUBSTANCE OF WHICH IS I'VE GOT MY HANDS SLAPPED BY COUNSEL TODAY FOR LICENSING ULTRACADE'S PROPERTIES TO A THIRD PARTY? [12-06-12 LHTX; 80:4-25]

MR. SINGER: IT REFRESHES YOUR RECOLLECTION, SIR. [LHTX; 81:1]

(PAUSE IN PROCEEDINGS) [LHTX 81:4]

MR. DEROSE: I SEE THE E-MAIL. I UNDERSTAND THE E-MAIL. I'M A LITTLE CONFUSED BY THE HEADING AT THE TOP OF THE PAGE THAT SAYS DAVID@HYPERWARE.COM AND HAVE NO UNDERSTANDING AS TO WHY AN E-MAIL THAT WAS SENT IN FEBRUARY OF 2006 HAS A DAVID@HYPERWARE.COM HEADING AT THE TOP OF IT.

MR. SINGER: PROBABLY OF HOW I PRINTED IT OUT FOR THIS CASE, BUT ARE YOU SUGGESTING, SIR, THAT THE E-MAIL IS NOT ACCURATE AND YOU DID NOT SEND IT?

MR. DEROSE: I'M SIMPLY SAYING, SIR, THAT I WAS CONFUSED ABOUT WHAT WAS AT THE TOP OF THIS AND WHY, IN FACT, IF IT WAS AN E-MAIL FROM ME IT HAS ANYTHING BUT MY HEADING AT THE TOP OF IT.

NONETHELESS, IN READING THIS E-MAIL, IT CLEARLY STATES THAT I WAS GIVING INSTRUCTIONS TO MY PEOPLE NOT TO EXECUTE ANY AGREEMENTS UNDER THE NAME OF GLOBAL VR UNTIL THE DEAL CLOSED. [LHTX 12-06-12; 81:19]

MR. SINGER: AND, IN FACT, IT SAYS—COULD YOU READ FOR THIS THE SUBSTANCE OF THE FIRST FULL PARAGRAPH?

THE COURT: THIS WAS USED TO REFRESH THIS WITNESS'S RECOLLECTION. IF YOU ARE GOING TO SOMEHOW READ IT INTO EVIDENCE, WE NEED TO HAVE IT MARKED.

MR. SINGER: YES, YOUR HONOR. COULD I MARK IT AS [LHTX 12-06-12; 81:25] DEFENDANT'S EXHIBIT 1?

THE COURT: ALL RIGHT. MARK IT AS SUCH. DO YOU HAVE A COPY OF THIS?

MS. KNIGHT: YES, YOUR HONOR, THANK YOU.

[DEFENDANT'S EXHIBIT 1 WAS MARKED FOR IDENTIFICATION.]

MR. SINGER: SORRY, YOUR HONOR, I'M STILL LEARNING.

THE COURT: THAT'S OKAY. THANK YOU.

MR. SINGER: I'M DOING MY BEST HERE.

THE COURT: AND YOU'D LIKE THIS TO BE RECEIVED INTO EVIDENCE?

MR. SINGER: YES. WE OFFER DEFENDANT'S EXHIBIT 1 INTO EVIDENCE.

THE COURT: ANY OBJECTION?

MS. KNIGHT: NO, YOUR HONOR.

This is evidenced in the loss hearing testimony and exhibits. For example, consider the email (Defense Exhibit 1), dated February 7, 2006, from James DeRose to David Foley that was admitted into evidence by the court at the hearing on December 6, 2012. The email proves that Global VR was selling UltraCade's casino gaming property interests before Global VR even owned and with great "zeal" [excitement for a profit].[5]

There is much more evidence of Global VR's interest in UltraCade's gaming product line, as expressed by Global VR's Financial Officer, Mr. Giovannettone.

THE COURT: ALL RIGHT. IT'S RECEIVED WITHOUT OBJECTION.

(DEFENDANT'S EXHIBIT 1 WAS ADMITTED) [LHTX 12-06-12; 82:17]

MR. SINGER: AND THEN MR. DEROSE—

MR. DEROSE: DEROSE.

MR. SINGER: I WAS THINKING. I DIDN'T FORGET, I PROMISE. COULD YOU READ THE FIRST FULL PARAGRAPH?

MR. DEROSE: THIS IS DAVID FOLEY AND BOBBY G. I'M ADDRESSING.

"I GOT MY HANDS SEVERELY TRAPPED BY LEGAL COUNSEL TODAY. UNTIL THE DEAL CLOSES, WE SHOULD NOT BE SIGNING ANY OF THE [LHTX 12-06-12; 82:25] ULTRACADE LICENSES, CONTRACTS OR AGREEMENTS IN THE NAME OF OR ON BEHALF OF ULTRACADE. WHERE POSSIBLE, THE CONTRACTS SHOULD BE MADE ASSIGNABLE AT THE TIME OF THE ACQUISTION.

"I APOLOGIZE THAT MY ZEAL FOR COMPLETING THE DEAL HAS LEAD TO ANY CONFUSION OR EXTRA WORK. THE LEGAL RAMIFICATIONS OF 'ASSUMING' OWNERSHIP PRIOR TO CLOSE ARE SUBSTANTIAL. PLEASE ADDRESS THIS ON ALL FUTURE AGREEMENTS, AND WHERE NECESSARY, CORRECT ANY OF THE CONTRACTS WHER WE HAVE ALREADY SIGNED IN ERROR. I WILL BE HAPPY TO EXPLAIN THIS TO ANY INDIVIDUALS YOU NEED ME TO SPEAK WITH DIRECTLY. THANKS, JIM."

MR. SINGER: THANK YOU.

MR. DEROSE: SIR?

THE COURT: YOU CAN KEEP IT THERE. [LHTX 12-06-12; 83:14]

MR. SINGER: NOW, THE REFERENCE IN THE BOTTOM THAT SAYS, PLEASE ADDRESS THIS ON ALL FUTURE AGREEMENTS AND WHERE NECESSARY PLEASE CORRECT ALL OF THE CONTRACTS WE HAVE SIGNED IN ERROR.

ARE YOU AWARE SITTING HERE TODAY OF ANY OTHER ABSCESS [SIC] OF ULTRACADE THAT YOU SOLD AND SIGNED ON BEHALF OF GLOBAL VR?

MR. DEROSE: NO, SIR, I'M NOT. [LHTX 83:1 TO 21]

[6]

The forecast placed the value of that line of products at $10, 531,000. [citation needed] The actual numbers that they received in value, are not in the record, however, in January of 2006, they licensed the casino properties to Bally Technologies, that they were scheduled to receive at least $75,000 in the first quarter of 2006 [Specific amounts were not evidenced at the loss hearing.], and at least $60,000 in the second quarter [Specific amounts were not evidenced at the loss hearing.], based upon the submission that is known.

In addition to the items of economic benefit that Mr. Foley transferred to Global VR by way of the ABC agreement include:

1) All of the unpaid wages;
2) Services as an unpaid employee;
3) Global VR collections.

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[6] MS. KNIGHT: AND DO YOU RECALL A POTENTIAL ACQUISITION OPPORTUNITY THAT CAME UP FOR GLOBAL VR IN APPROXIMATELY THE FALL OF 2005? [LHTX 12-06-12; 126-5]

MR. GIOVANNETTONE: YES.

MS. KNIGHT: AND WHAT WAS THAT?

MR. GIOVANNETTONE: ULTRACADE.

MS. KNIGHT: AND WHAT WAS ULTRACADE?

MR. GIOVANNETTONE: ULTRACADE WAS A BUSINESS THAT WAS IN A SIMILAR INDUSTRY AS US. THEY MAKE COIN-OP GAMES.

MS. KNIGHT: UH-HUH.

MR. GIOVANNETTONE: AT THE TIME WE GOT INVOLVED, THEY HAD A HORSE RACING GAME CALLED BREEDERS CUP, AND WE ACTUALLY GOT INVOLVED AND SO THAT THERE WAS POTENTIAL IN THE GAMING INDUSTRY AND IT BECAME OF INTEREST TO US. [LHTX 12-06-12; 126-17]

MS. KNIGHT: AFTER THE MOU, WERE YOU INVOLVED IN THE DUE DILIGENCE? [LHTX 127:12]

MR. GIOVANNETTONE: YES.

MS. KNIGHT: AND CAN YOU DESCRIBE SOME OF THE THINGS THAT YOU DID REGARDING THAT DUE DILIGENCE?

MR. GIOVANNETTONE: SURE. WE LOOKED AT THE LIABILITIES, WE LOOKED AT THE FORECASTS, WE LOOKED AT THE REVENUE COMING IN, WE LOOKED AT THE LICENSES, WE INTERVIEWED PEOPLE. [LHTX 12-06-12; 127:16]

MS. KNIGHT: UH-HUH.

MR. GIOVANNETTONE: WE TALKED TO SOME OF THE DEBT HOLDERS AND PROBABLY A FEW MORE THINGS THAT I CAN'T THINK OF RIGHT NOW, BUT THAT'S BASICALLY WHAT WE DID. [LHTX 127:12-22]

If the Court finds Mr. Foley to be not entitled to any exclusions ("credits") within the meaning of sentencing guideline 2.B.1.1. punitive loss enhancement calculation table, then Mr. Foley requests a <u>downward departure</u> of 14 levels for being a much less serious offender.

There is no question that the evidence admitted at the loss hearing shows that Mr. Foley transferred items and provided services of considerable, and eagerly-desired, economic benefit to Global VR in the period from December of 2005 to September of 2006. Accordingly, his offense by official definition of the guidelines is therefore far "less serious" than if he had not transferred such benefit—it's an express statement of guideline policy.

> … because the seriousness of the offense and the culpability of a defendant is better determined by using a net approach …. The offender who *transfers* something of value to the victim(s) generally is committing *a less serious offense* than an offender who does not." U.S.S.G. App. C, amend. 617 (reason for amendment).

Mr. Foley's offense being less serious than the enhancement loss table would have it, then, prescinding from any actual application of credits per 2.B.1.1. cmt. n. 3(E)(i), the facts developed at the loss hearing still call for mitigation by utilizing the application of another guideline:

> There may be cases in which the offense level determined under this guideline substantially overstates the seriousness of the offense. In such cases, a downward departure may be warranted. U.S.S.G. 2.B.1.1—Application note 19(C).

In other words, the court determined a loss figure of $450,000 without making allowance for anything of economic benefit that Mr. Foley transferred to Global VR. One way for the court to produce a just outcome would be to recognize this transfer as a mitigating element anticipated by the guidelines and still very clearly within the purview of the guideline architecture. This would appropriately justify a downward departure.

Given the magnitude of the economic benefit transferred, far exceeding the loss

calculation of $450,000, a downward departure of 14 levels is justified. Mr. Foley lost most, if not everything he owned in the financial disaster. Furthermore, he has been burdened with millions of dollars of liabilities that were supposed to have been taken over by Global VR as part of the transaction. His financial statements and other documents submitted to the probation department bear this out, and his ongoing personal bankruptcy obligations are corroborative of this.

If the Court finds that Mr. Foley is not entitled to any exclusions ("credits") within the meaning of Amendment 617 to the sentencing guideline 2.B.1.1. punitive loss enhancement calculation table, and if the Court also chooses to not grant a downward departure, then Mr. Foley requests a variance on the grounds of the over-arching intent of 18 U.S.C. 3553 for the same reasons stated, and for the additional reasons stated in support of a variance per 18 U.S.C. 3553.

If, for some reason, the court concludes that the mitigating effect Mr. Foley's transfer of economic benefit does not meet the criteria of either a credit, within the meaning and intent of guideline 2.B.1.1 cmt. n. 3(E)(i), or a downward departure within the meaning and intent of guideline 2.B.1.1 cmt. n. 19(C), then Mr. Foley requests a variance per 18 U.S. 3553 based upon the same facts and others set out in this memorandum.

Since this is purely an economic offense case, the defense requests that Court consider, per § 3553, all the rehabilitation efforts, especially financial ones, that Mr. Foley has made in the months since his plea of guilty. Doing so would be consistent with sound social policy and with the holding in *Pepper v. U.S.*, quoted below:

> We hold that when a defendant's sentence has been set aside on appeal, a district court at resentencing may consider evidence of the defendant's post-sentencing rehabilitation and that such evidence may, in appropriate cases, support a downward variance from the now-advisory Federal Sentencing Guidelines range. Separately, we affirm the Court of Appeals' ruling that the law of the case doctrine did not require the District Court in this case to apply the same percentage departure from the Guidelines range for substantial assistance that had been applied at

petitioner's prior sentencing. *Pepper v. U.S.* (2011) 131 S.Ct. 1229.

"A camel is a horse designed by a committee" —*Kimbrough* comes to California.

If there was any doubt that the 2007 holding of the U.S. Supreme Court in *Kimbrough* was applied to a sentencing in California, that doubt was most certainly resolved in the *Henderson* case, which arose out of the Central District, and was decided in April of 2011.[7]

On direct appeal, Mr. Henderson challenged the district court's failure to exercise the discretion accorded it in *Kimbrough* to vary from the Sentencing Guidelines based on policy disagreements with them, and not simply based on an individualized determination that they yield an excessive sentence in a particular case. The Circuit Court remanded the case to the trial court, "Because it is unclear whether the district judge recognized and exercised his Kimbrough discretion, we reverse and remand for resentencing."

In *Henderson*, the court held, at pages 963 and 964:

> During oral argument, the government recognized that district courts have authority to disagree with the child pornography Guidelines. As the history and the Commission's own reports and assessments of these Guidelines demonstrate, the child pornography Guidelines are, to a large extent, not the result of the Commission's "exercise of its characteristic institutional role," which requires that it base its determinations on "empirical data and national experience," but of frequent mandatory minimum legislation and specific congressional directives to the Commission to amend the Guidelines. *Kimbrough,* 552 U.S. at 109, 128 S.Ct. 558. *We therefore hold that, similar to the crack cocaine Guidelines, district courts may vary from the child pornography Guidelines, § 2G2.2, based on policy disagreement with them* [emphasis added], and not simply based on an individualized determination that they yield an excessive sentence in a particular case. *See Spears,* 129 S.Ct. at 843; *Kimbrough,* 552 U.S. at 109-10, 128 S.Ct. 558.

[7] *United States v. Henderson* (9th Cir. 2011) 649 F.3d 955

In the majority opinion the Court included a lengthy footnote (4), stating, "In so holding, we join several of our sister circuits," citing with approval, *United States v. Pape*, 601 F.3d 743, 749 (7th Cir. 2010) (district courts "are at liberty to reject *any* Guideline on policy grounds—though they must act reasonably when using that power.") (internal quotations omitted).

Justice Berzon, Circuit Judge, *concurring* in *Henderson*, wrote, at page 966:

> For better or worse, we must live with § 2G2.2: it is on the books and so must be the "`starting point and initial benchmark'" for district judges sentencing those convicted of child pornography offenses. *Kimbrough v. United States,* 552 U.S. 85, 108, 128 S.Ct. 558, 169 L.Ed.2d 481 (2007) (quoting *Gall,* 552 U.S. at 49, 128 S.Ct. 586). But, like any Guideline, § 2G2.2 is merely advisory. District judges who, after having considered § 2G2.2, conclude that it constitutes bad advice should be encouraged to reject it as such. *See Kimbrough,* 552 U.S. at 113, 128 S.Ct. 558 (Scalia J., concurring) (*emphasizing that "the district court is free to make its own reasonable application of the § 3553(a) factors, and to reject (after due consideration) the advice of the Guidelines*") [emphasis added]. *United States v. Henderson* (9th Cir. 2011) 649 F.3d 955, at 966.

The "loss calculation" guideline, ranking behind perhaps the crack cocaine and pornography guidelines is a highly criticized guideline.[8]

The court is invited to abandon this guideline completely if it so chooses, particularly if the court decides that the guideline 2.B.1 is not based upon empirical research such as the first offender research.

Section 3553 offender characteristics: USSC research.

The most obvious factor for consideration by the court pursuant to 18 U.S.C. 3553, and the one, which, in all fairness, most certainly should be given great weight in

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[8] Bowman, Frank O. *Sentencing High-Loss Corporate Insider Frauds Post-Booker*. 20 Fed. Sent. Rrptr. 167 (2008); Bowman, Frank O. The *Failure of the Federal Sentencing Guidelines: A Structural Analysis*. 100:2 Columbia Law Review 101 (2005); Bowman, Frank O. *Testimony Before the U.S. Sentencing Commission*, February 16, 2012; Berry, William W. III. *Discretion Without Guidance: The Need to Give Meaning to § 3553 after Booker and its Progeny*, 40 Conn. L.Rev. 631 (2008); Volrath, Derick R. *Losing the Loss Calculation: Toward a More Just Sentencing Regime in White-Collar Criminal Cases*, 59 Duke L.J. 1001 (2010).

sentencing, is the fact that Mr. Foley is not only a first offender [Criminal History Column One], but apparently he has never had any prior contact with the criminal justice system whatsoever. More importantly, in this Post-*Booker* era of federal sentencing, first offender status is a factor that has been subject to empirical study by the U.S. Sentencing Commission and produced some valuable statistics on recidivism.

Mr. Foley presents an exceptionally low risk [perhaps one of the very lowest risks] of re-offending. Mr. Foley is now 48 years old. He is a college-educated, brilliant computer technologist who has been productively employed [usually self-employed] in the demanding field of computer science for all of his adult life. He is married with one child, and has no personal history of substance abuse whatsoever.

According to research conducted by the U.S. Sentencing Commission itself, for all male offenders in Criminal History Category I, the recidivism rate is 15.2%. For those over age 40 at the time of sentencing, however, the rate in Category I is only 6.9%. For those who are college-educated, the rate in Catagory I is just 13.9%; for those who have been employed, the rate is 12.7%; and for those who were ever married, the rate is 9.8%. For those with no history of illicit drug use, the recidivism rate is less than half that of those who do have a drug history. For those like Mr. Foley who are educated, have been employed, have been married, are drug free and over 40, the recidivism rate is certainly much lower. *See* U.S. Sent'g Comm'n, *Measuring Recidivism: The Criminal History Computation of the Federal Sentencing Guidelines,* at Exh. 9, at 28; Exh. 10, at 29 (May 2004) [hereinafter *Measuring Recidivism*]. For all Category I persons convicted of fraud, the recidivism rate is just 9.3%, compared to 16.9% for all fraud offenders. *Id*., Exh. 11, at 30. Finally, persons like Mr. Foley with zero criminal history points have a rate of recidivism half that of offenders with one criminal history point. *See* Sent'g Comm'n, *Recidivism and the "First Offender,"* at 13-14 (May 2004) [hereinafter *First Offender*].

The Commission has recognized the advisability of revising the guidelines to take

age and first offender status into account. *See First Offender* at 1-2 (identifying goal of "refin[ing] a workable 'first-offender' concept within the guideline criminal history structure"); *Measuring Recidivism* at 16 (noting that "[o]ffender age is a pertinent characteristic" that would "improve [the] predictive power of the guidelines "if incorporated into the criminal history computation"). The Commission has not implemented any such revisions to the criminal history guidelines, but has recently stated that age "may be relevant" in granting a departure. USSG § 5H1.1, p.s.

In imposing the least sentence sufficient to account for the need to protect the public from further crimes of Mr. Foley, the Court should consider the statistically low risk of recidivism presented by Mr. Foley's history and characteristics. *See, e.g.*, *United States v. Darway,* 255 Fed. Appx. 68, 73 (6th Cir. 2007) (upholding downward variance on basis of defendant's first-offender status); *United States v. Hamilton*, 323 Fed. Appx. 27, 31 (2d Cir. 2009) ("the district court abused its discretion in not taking into account policy considerations with regard to age recidivism not included in the Guidelines"); *United States v. Holt*, 486 F.3d 997, 1004 (7th Cir. 2007) (affirming below-guideline sentence based on defendant's age, which made it unlikely that he would again be involved in a violent crime); *United States v. Urbina*, slip op., 2009 WL 565485, *3 (E.D. Wis. Mar. 5, 2009) (considering low risk of recidivism indicated by defendant's lack of criminal record, positive work history, and strong family ties); *United States v. Cabrera*, 567 F. Supp. 2d 271, 279 (D. Mass. 2008) (granting variance because defendants "with zero criminal history points are less likely to recidivate than all other offenders"); *Simon v. United States*, 361 F. Supp. 2d 35, 48 (E.D.N.Y. 2005) (basing variance in part on defendant's age of 50 upon release because recidivism drops substantially with age); *United States v. Nellum*, 2005 WL 300073 at *3 (N.D. Ind. Feb. 3, 2005) (granting variance to 57-year-old defendant because recidivism drops with age); *United States v. Ward,* 814 F. Supp. 23, 24 (E.D. Va. 1993) (granting departure based on defendant's age as first-time offender since guidelines do not "account for the length of time a particular

defendant refrains from criminal conduct" before committing his first offense).

The employment history of Mr. Foley is impeccable.

In *U.S. v. Munoz-Nava*, 524 F.3d 1137 (10th Cir. 2008) the court affirmed a below-guideline sentence of one year and a day in a possession with intent to distribute heroin case because *defendant had a long and consistent work history*; had a great deal of community support; did not have a felony record; was the primary caretaker and sole supporter of an 8-year-old son and elderly parents; and the judge had received letters from family, friends, and community members.

Obviously the 3553 factors, including employment history, in Mr. Foley's case are very similar.

Conclusion.

For the reasons stated above, Mr. Foley requests:

1. That the court order the presentence report of the Probation Department be stricken from the record and that an amended report be prepared consistent with a completed calculation of net loss per guideline 2.B.1.1 cmt. n. 3(E)(i), and consistent with such other guidelines as have been presented to the court by Mr. Foley;

2. In the alternative, that the court impose a sentence that does not include a 14-level enhancement, either casting this term of final judgment as a downward departure fully within the spirit and letter of the guidelines, or that the court declare a variance, per 18 U.S.C. 3553, based upon the equities in the case.

Dated: December 10, 2013
at Palo Alto, California

/s/ Jerome P. Mullins
Jerome P. Mullins
Attorney for Defendant
DAVID RUSSELL FOLEY