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White Collar Roundup - May 2013

Tainted Funds

The U.S. Court of Appeals for the Second Circuit in United States v. Walsh ruled that the defendant could not use the proceeds from the sale of his house to fund his criminal defense because he used tainted funds to obtain the home. The defendant, who faced criminal charges for his role in a purported Ponzi scheme, sought to fund his criminal defense with assets frozen in a parallel civil forfeiture action. Walsh's former wife had bought a house with untainted funds. As part of a divorce, Walsh paid his wife $12.5 million and received title to the house. In the civil forfeiture action, the court restrained the house as an asset traceable to the fraud. Walsh asked the court in his criminal case to release the funds to allow him to pay for criminal defense counsel. The trial court refused, finding that the house was "traceable" to the fraud because Walsh had paid his former wife with tainted funds. On appeal, the Second Circuit affirmed the trial court's ruling.

Winding Up as Wire Fraud

In United States v. Jinian, the Ninth Circuit held that interbank transfers suffice to bring a fraud within the wire-fraud statute. Jinian, the chief executive officer of a software company, falsely told the company's finance manager that he was authorized to receive advances on his compensation. As a result, the finance manager wrote checks on the company's California bank account, which Jinian deposited into his California bank. At trial, the government elicited testimony from an internal auditor at the Federal Reserve Bank about the process by which banks transmit electronic images of checks through a server in Texas to process check payments through the Federal Reserve system. At trial, Jinian unsuccessfully argued that the government failed to prove that he knew that interstate wires would be used in the scheme, thus failing to prove the use-of-wire element of wire fraud. After his conviction, Jinian appealed. The Ninth Circuit affirmed, holding that even though Jinian might not have foreseen the interstate wire transfers, they were necessary to complete and conceal each fraud.

Hiding the Ball

The Seventh Circuit in United States v. Peterson recommended that courts refrain from keeping the confidential sentencing recommendations of the probation department from the parties. As in all federal criminal cases, a probation officer in Peterson's case prepared a Presentence Investigation Report (PSR) detailing Peterson's history, personal characteristics, and criminal offense. Peterson received the PSR and had the opportunity to make sentencing arguments. The probation officer also provided a confidential report to the court, which the court reviewed on imposing sentence. Peterson appealed his sentence, contending that the sentencing court's reliance on the confidential report violated his Fifth and Sixth Amendment rights because he did not have an opportunity to address the report's claims. The Seventh Circuit affirmed the sentence, noting that he had access to the facts in the PSR from which he argued his position. The court also wrote, "[t]o the extent confidential sentencing recommendations create the appearance of hidden information or a secret tilt in the government's favor, we offer the view that our federal sentencing procedures might be better served by allowing the parties to evaluate any analysis that might form the basis of a judicial determination."

Easing the Path of the Whistleblower

The Third Circuit analyzed the whistleblower protection provisions of Section 806 of the Sarbanes-Oxley Act (SOX), 18

U.S.C. ? 1514A, in Wiest v. Lynch. The issue was whether a whistleblower plaintiff had adequately alleged that he engaged in "protected activity" under 29 C.F.R. ? 1980.104(e)(2)(i) when he raised concerns about the accounting treatment of certain lavish corporate events as a business expense. The Third Circuit rejected the defendants' argument that in order for a whistleblower to have had a "reasonable belief" that his employer violated a SOX-protected law, rule or regulation, his communication of that belief must have "definitively and specifically" pointed to such a violation. Rather, the Third Circuit held that a plaintiff's communication need only reflect a subjective and objectively reasonable belief that his employer's conduct constituted a violation of an enumerated provision in Section 806.

Warrant + Plea + Learning the Warrant Was Based on a Lie = Vacatur

The Fourth Circuit held in United States v. Fisher that a police officer's false statement in a search warrant invalidates a subsequent guilty plea. In the case, an officer swore to an affidavit underlying the search of the defendant's residence and vehicle, which yielded the discovery of the "evidence forming the basis of the charge to which the defendant pled guilty." More than a year after the guilty plea, Fisher learned that the officer had himself pleaded guilty to making false statements on numerous affidavits, including the one in Fisher's case. Fisher petitioned the court under 28 U.S.C. ? 2255 to vacate his plea. The trial court denied the petition, ruling that while knowledge of the misconduct may have prompted Fisher to file a suppression motion, he still admitted to his crime at his voluntary guilty plea. On appeal, the Fourth Circuit reversed, holding that the officer's misconduct so tainted the prosecution that his conviction could not stand.

Flipping Houses for Fraud

In United States v. Morrison, the Fifth Circuit ruled that the sentencing court did not err by calculating the loss in a mortgage-fraud case without including an offset for the value of the real estate collateralizing the loans. The defendants in the case engaged in a complex house-flipping scheme whereby they defrauded owners, buyers, and lenders. At sentencing, the defendants sought to deduct from the loss amount calculated under U.S.S.G. ? 2B1.1 the residual value of the properties. The district court refused to do so. On appeal, the Fifth Circuit said, "we cannot say that the district court erred by employing an intended loss calculation and declining to account for the collateral's value, especially given the district court's factual findings that the defendants did not intend to repay the mortgage loans here." But the Fifth Circuit was explicit that its holding does not prohibit a sentencing court in another case from considering the collateral's value.

Defining Complexity

The Ninth Circuit held in United States v. Jennings that using a false name on a bank account constituted "sophisticated means" under U.S.S.G. ? 2T1.1(b)(2). The defendants owned Environmental Soil Sciences, Inc. (ESS), which hired Eco-Logic Environmental Engineering (Eco-Logic) as a vendor to develop machinery for ESS. They also opened a bank account, using the fake name "Ecologic." They had ESS write checks and make deposits to their Ecologic account pretending on ESS's books that the deposits were for Eco-Logic's services. In the words of the Ninth Circuit, "ESS generated no substantial revenues. But the Ecologic account funded Defendants' new homes, cars, and cash payments to family members. Defendants did not report that money to the IRS as income." After being convicted for conspiracy and tax evasion, the district court applied the two-point enhancement of ? 2T1.1(b)(2) for the crime's having "involved sophisticated means." The defendants appealed, claiming their means were not very sophisticated when compared to the conduct listed in the application note to
? 2T1.1(b)(2). The Ninth Circuit disagreed, explaining that "the enhancement properly applies to conduct less sophisticated than the list articulated in the application note." The Ninth Circuit further noted that "[t]he method employed by Defendants here reflected a sophisticated effort to conceal income" and held that the district court did not err in applying the enhancement.