LAW360

Portfolio Media. Inc. | 230 Park Avenue, 7th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

5th Circ. Ruling May Beget Fraud Jury Instruction Appeals

By **Charles Fowler** (November 6, 2023, 2:55 PM EST)


Charles Fowler

Drawing on a line of U.S. Supreme Court cases, the U.S. Court of Appeals for the Fifth Circuit recently provided a reminder that federal fraud crime statutes protect traditional property rights.

In U.S. v. Greenlaw,[1] the court explained that the object of the crime must be to take the victim's property. So, the court held, the model jury instruction defining "intent to defraud" as intent to deceive or cheat misstates the law.

Even so, the court held that the error was harmless.

The Greenlaw defendants ran investment funds that financed real estate development.[2] The funds solicited capital and loaned it to developers to buy and develop property.[3]

One fund, called UDF III, boasted an almost 10% rate of return.[4] When UDF III did not collect enough in loan repayments to maintain its high payouts, the defendants paid UDF III's investors with cash from other funds to "ensure that UDF III continued to appear lucrative to the investing public."[5]

The defendants allegedly hid the nature of these interfund cash transfers and lied about them in U.S. Securities and Exchange Commission filings.[6]

The government called this arrangement a Ponzi scheme: The defendants paid UDF III's investors with new cash from the other funds' investors.[7] The defendants called the cash transfers routine transactions by which the other funds made fully collateralized, interest-bearing loans to UDF III, effectively just refinancing the developers' debt through the other funds.[8]

A jury in the U.S. District Court for the Northern District of Texas bought the government's version and convicted the defendants of wire fraud, securities fraud, conspiracy, and aiding and abetting.[9] The four defendants received prison sentences of 36 to 84 months.[10]

On July 31, the Fifth Circuit affirmed the jury verdict, and on Oct. 11, it denied the defendants' request for a rehearing en banc.

The Fifth Circuit held that its model instruction on "intent to defraud" misstates the law. The model instruction for wire fraud defines "intent to defraud" as "a conscious, knowing intent to deceive or cheat someone."[11] But, the "fraud statutes are limited in scope to the protection of property rights,"[12] so

intent to defraud requires not just deception, but also intent to deprive a victim of property.[13]

The Fifth Circuit agreed with the defendants that the model instruction's "disjunctive 'or'" — implying that deceptive intent alone is enough — "makes it a misstatement of law."[14]

It joined the U.S. Courts of Appeals for the Ninth and Eleventh Circuits in disapproving disjunctive fraudulent-intent instructions.[15]

The Fifth Circuit's holding will likely spawn more appeals challenging fraudulent-intent instructions.

The Ninth Circuit has decided at least 14 such appeals since it disapproved its disjunctive model instruction in 2020 in U.S. v. Miller.[16]

Appeals may arise in mail, wire or securities fraud cases because district courts used the disapproved instruction in trials held before Greenlaw was decided. Or they may arise because no one brought Greenlaw's holding to the district court's attention, in which case the Fifth Circuit will review only for plain error.

Still other appeals will urge the Fifth Circuit to extend Greenlaw's holding to other crimes requiring fraudulent or similar intent.

The disapproved phrase "deceive or cheat" appears 10 times in the 2019 edition of the Fifth Circuit's pattern jury instructions. It is used to define not just elements requiring intent to defraud,[17] but also those requiring the defendant to "act ... fraudulently,"[18] to "obtain [property] by fraud,"[19] and to "[take property] by fraud."[20]

The outcome for each crime will depend on whether the whole instruction accurately states the statutory elements. Disjunctive language may not misstate the elements when the instruction otherwise contemplates taking the victim's property.

The government may also argue that disjunctive language correctly defines some crimes — that some statutes are meant to criminalize merely deceptive intent.[21]

In Greenlaw, the Fifth Circuit held that the jury-instruction error was harmless.[22] That result squares with the results reached in most other cases identifying the same error.

The Ninth Circuit, for instance, has repeatedly held that using the disjunctive instruction was harmless or, when reviewing for plain error, that the error affected no substantial rights.[23]

How can courts so readily brush aside misstating a central element of wire fraud, and — more to the point — how can defendants fend off that result? The Fifth Circuit gave little guidance on how to assess harmlessness.[24]

The court applied the harmlessness standard in three sentences focusing mainly on how voluminous the record was — not on any particular facts or evidence.[25] The court was "convinced that a rational jury would have found the defendants guilty absent the erroneous instruction."[26]

The real problem, though, was that the evidence and arguments apparently put the jury to an all-or-nothing choice. Either the defendants did nothing wrong at all — i.e., they intended to neither deceive

nor cheat, but merely carried out routine transactions — or they ran a Ponzi scheme with no purpose other than to cheat investors.

Harmlessness should usually turn on whether the record gave the jury a plausible explanation of the facts consistent with an intent to deceive but not necessarily take the victim's property.

So what kind of facts would suggest intent to deceive but not cheat the victim? Thirty years ago, in U.S. v. Walters, U.S. Circuit Judge Frank Easterbrook offered an example.

Norby Walters, a sports agent, contracted to represent college football players for a cut of their future NFL salaries.[27] But since professional representation would disqualify the players for collegiate sports, and thus dash their NFL hopes, Walters postdated the contracts to after the players graduated.[28]

Walters no doubt intended to deceive the schools about the players' eligibility, causing the schools to lose scholarship money to ineligible players.[29] But Walters did not commit mail fraud, the U.S. Court of Appeals for the Seventh Circuit held, because he did not take the schools' money. Walters meant to obtain no part of the scholarship money, but to profit off the players' NFL salaries.[30]

The Eleventh Circuit reasoned similarly in 2016 in U.S. v. Takhalov.[31] The defendants were bar owners who had women pose as tourists, find businessmen and lure the men into the defendants' bars.[32]

The government claimed that, inside the bars, the defendants swindled the men by getting them drunk and overcharging them.[33]

The defendants admitted luring the men into the bars but testified that, once there, "these men got what they paid for — nothing more, nothing less."[34] In other words, the defendants deceptively induced the men to transact, but did not mislead them about any essential element of the bargain.

The court held that the jury-instruction error was not harmless because the jury could have credited the defendants' testimony that they deceived but did not cheat.[35]

Other facts and charges will be conducive to still other theories of intent to deceive but not cheat. The Ninth Circuit has held that, like wire fraud, access-device fraud — fraud related to payment cards and identifying information — requires intent to both deceive and cheat.[36]

Suppose agents catch a defendant with a cache of stolen account and identifying information.[37] Consider whether the defendant can show that he meant not to steal the account holders' money but only to ruin their credit scores. Or consider whether he can show that he simply meant to disguise his identity to transact — i.e., deception — but without misleading anyone as to the essential elements of the bargain, which was essentially the fraudulent-inducement theory the defendants successfully urged in Takhalov.

In short, a defendant who admittedly lied can defend against federal fraud charges by contending that their deception furthered ends other than taking the victim's property.

The defendant may have profited only indirectly, as in Walters; induced transactions not themselves tainted by deception, as in Takhalov; or acted out of a vindictive desire to do harm without gaining anything for himself, as in the hypothetical credit score example. Other variations surely exist.

Defendants who present themes like these at trial can urge acquittal but, if convicted, should at least defeat the argument that an erroneous intent-to-defraud instruction was harmless.

Charles Fowler is a principal at McKool Smith. He previously served as an assistant U.S. attorney in the Central District of California and in the Western District of Texas.

[1] United States v. Greenlaw, --- F.4th ----, 2023 WL 6617934 (5th Cir. Oct. 11, 2023).

[2] Id. at *1.

[3] Id.

[4] Id. at *2.

[5] Id.

[6] Id.

[7] Id. at *1–2.

[8] Id. at *2.

[9] Id. at *1, *3.

[10] Id. at *3.

[11] 5th Cir. Pattern Jury Instr. (Criminal Cases) §2.57 (2019 ed.).

[12] Greenlaw, 2023 WL 6617934, at *7 (quoting Kelly v. United States, 140 S. Ct. 1565, 1571 (2020)).

[13] Id. at *7–8 (citing Kelly, 140 S. Ct. at 1571; Shaw v. United States, 580 U.S. 63, 72 (2016)).

[14] Id. at *13.

[15] See United States v. Miller, 953 F.3d 1095, 1103 (9th Cir. 2020); United States v. Takhalov, 827 F.3d 1307, 1319 (11th Cir.), as revised, opinion modified on denial of reh'g, 838 F.3d 1168 (11th Cir. 2016).

[16] See, e.g., United States v. Shih, 73 F.4th 1077, 1099 (9th Cir. 2023); United States v. Saini, 23 F.4th 1155, 1163 (9th Cir. 2022); United States v. Minasyan, 4 F.4th 770, 780 (9th Cir. 2021).

[17] 18 U.S.C. §545 (smuggling); 18 U.S.C. §656 (theft or embezzlement by a bank employee); 18 U.S.C. §657 (theft from lending, credit, and insurance institutions); 18 U.S.C. §1341 (mail fraud); 18 U.S.C. §1343 (wire fraud); 18 U.S.C. §1344(1) (bank fraud).

[18] 18 U.S.C. §152 (concealing assets and presenting false claims in bankruptcy).

[19] 18 U.S.C. §666(a)(1)(A) (theft from programs receiving federal funds).

[20] 18 U.S.C. §2314 (interstate transport of stolen property).

[21] See, e.g., Saini, 23 F.4th at 1163 (considering such an argument for access-device fraud under 18 U.S.C. §1029(a) but holding that the statute's unambiguous text requires intent to take property).

[22] Greenlaw, 2023 WL 6617934, at *15.

[23] Shih, 73 F.4th at 1100 (harmless); Saini, 23 F.4th at 1164 (harmless); Minasyan, 4 F.4th at 780 (no effect on substantial rights); Miller, 953 F.3d at 1103 (harmless); United States v. Canada, No. 20-50188, 2021 WL 3630230, at *2 (9th Cir. Aug. 17, 2021) (no effect on substantial rights).

[24] Greenlaw, 2023 WL 6617934, at *15. The Fifth Circuit's original opinion said the error was harmless if a rational jury could find that the defendants had the required intent; the court referred back to its sufficiency-of-the-evidence discussion to conclude that the record cleared that bar. Greenlaw, 76 F.4th at 331. The defendants' rehearing petition pointed out that the court appeared to apply the wrong harmlessness standard: the question is not whether the evidence was sufficient to convict but whether it was clear beyond a reasonable doubt that the jury would have convicted absent the error. The substitute opinion revises the court's harmlessness discussion to state the right standard. But it gives, if anything, even less indication of how the record shows harmlessness.

[25] Id.

[26] Id.

[27] United States v. Walters, 997 F.2d 1219, 1221 (7th Cir. 1993).

[28] Id.

[29] Id. at 1224.

[30] Id.

[31] 827 F.3d 1307.

[32] Id. at 1310.

[33] Id.

[34] Id. at 1311.

[35] Id. at 1319.

[36] Saini, 23 F.4th at 1163.

[37] See 18 U.S.C. §1029(a)(3), (4).