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Eleventh Circuit Affirms Promoters' Convictions for Abusive Transactions Lacking Economic Substance

In ***United States v. Donaldson***, 767 F. App'x 903 (11th Cir. 2019) (unpublished), the Eleventh Circuit affirmed the convictions of two tax shelter promoters, upholding the district court's conclusion that the transactions were a sham and lacked economic substance.

The promoters, Duane Crithfield ("Crithfield") and Stephen Donaldson, Sr. ("Donaldson"), established a network of mostly offshore limited liability companies ("LLCs") and trusts to promote and sell to closely-held businesses the Business Protection Plan ("BPP"), a purportedly lawful, insurance–based tax shelter. As part of the scheme, the closely-held business paid a lump-sum premium in exchange for an insurance policy issued by one of two insurance entities within the promoters' commercial enterprise. The business then deducted the premium as an "ordinary and necessary" business expense—thereby reducing taxable income. After collecting the premium, the insurance entity charged the business 15% or 17% of the premium, a rate ostensibly lower than the business' nominal marginal tax rate, and then allocated the remaining 85% or 83% to a segregated trust or LLC set up solely for that business. The business then assumed control of the trust or LLC, which contained the remaining portion of its premium, without paying any tax or interest on the premium. After a bench trial, the district court found Crithfield and Donaldson guilty of conspiracy to defraud the U.S. (18 U.S.C. § 371) and wilfully aiding the submission of a false return (26 U.S.C. § 7206(2)), and sentenced them to 54 and 76 months' imprisonment, respectively.

On appeal, the Eleventh Circuit affirmed the defendants' convictions, holding the evidence supported the district court's finding that the BPP had no economic substance independent of a taxpayer's federal income tax considerations, and was thus a substantive sham. Specifically, the appellate court noted, the district court did not err in concluding that the purchase of BPP policies did not shift any risk to defendants' commercial enterprise and was therefore non–deductible. The Eleventh Circuit also affirmed the district court's denial of a new trial and the denial of defendants' motion to suppress.

***Note*:** This is an unpublished opinion.

FOURTH AMENDMENT

Supreme Court Holds Unauthorized Driver of Rental Vehicle Otherwise in Lawful Possession and Control of Vehicle Has Reasonable Expectation of Privacy

In ***Byrd v. United States***, 138 S. Ct. 1518 (2018), the Supreme Court held a person otherwise in lawful possession and control of a rental vehicle has a reasonable expectation of privacy, even if not listed as an authorized driver in the rental agreement.

During a traffic stop of Terrence Byrd ("Byrd"), Pennsylvania State Troopers learned the vehicle was rented and Byrd was not an authorized driver on the rental agreement. For this reason, the troopers told Byrd

they did not need his consent to search the vehicle, including the trunk. In the trunk, the troopers found body armor and 49 bricks of heroin. Byrd was charged with federal drug and other offenses. The district court denied Byrd's motion to suppress the evidence as the fruit of an unlawful search, and Byrd entered a conditional plea reserving the right to appeal the denial of his motion. The Third Circuit summarily affirmed, acknowledging an inter-Circuit split, but indicating it was bound by intra-Circuit precedent.

On certiorari, the Supreme Court resolved the inter-Circuit conflict, holding that an unauthorized driver of a rented vehicle, otherwise in lawful possession and control of the vehicle, has a reasonable expectation of privacy protected by the Fourth Amendment. The Court's rationale was that the expectation of privacy that comes from lawful possession and control of property, and the attendant right to exclude others from it, should not differ depending on whether a car is rented or privately owned by someone other than the person in possession.

Third Circuit Holds Good-Faith Exception Applied to Void Warrant for Electronic Information

In ***United States v. Werdene***, 883 F.3d 204 (3d Cir 2018), *cert. denied*, 139 S. Ct. 260 (2018), the Third Circuit affirmed the district court's denial of the defendant's motion to suppress evidence obtained from a void electronic warrant based on the exclusionary rule's good-faith exception.

The Federal Bureau of Investigation ("FBI") obtained a single search warrant, issued in the Eastern District of Virginia ("EDVA"), to search the computers of persons who accessed the "Playpen" dark-web site, used internationally by child pornographers. The warrant allowed the FBI to obtain user identifying information using the "Network Investigative Technique" ("NIT"), a government-created malware. After the FBI was able to identify Gabriel Werdene ("Werdene"), a Pennsylvania resident, it obtained a search warrant from the Eastern District of Pennsylvania ("EDPA") to search Werdene's home, where agents seized one USB drive and one DVD containing child pornography. Werdene filed a pretrial motion to suppress evidence seized pursuant to the NIT warrant and any fruits therefrom, claiming that the EDVA magistrate had no authority to issue a warrant for a search of Werdene's computer in Pennsylvania, and, therefore, the warrant was invalid and the search was conducted in violation of the Fourth Amendment. The EDPA district court denied the motion, holding that while the NIT warrant was invalid for lack of jurisdiction, the use of the NIT did not constitute a Fourth Amendment search. Ultimately, Werdene was convicted and sentenced to 24 months' imprisonment.

On appeal, the Third Circuit upheld the denial of the motion to suppress, holding that the good-faith exception to the exclusionary rule applied, even though the NIT warrant was void *ab initio* because it violated 28 U.S.C. § 636(a)'s jurisdictional limitations and Fed. R. Crim. P. 41(b). The appellate court explained that the good-faith exception applied because "the issuing magistrate's lack of authority has no impact on police misconduct, if the officers mistakenly, but inadvertently, presented the warrant to an innocent magistrate."

Eighth Circuit Holds No Clear Error in Finding that Encounter with Law Enforcement was Consensual and Consent to Search was Voluntary

In ***United States v. Garcia***, 888 F.3d 1004 (8th Cir. 2018), the Eighth Circuit held the district court did not clearly err in finding defendant's encounter with investigator was consensual and that his consent to a search of his luggage was voluntary.

A state patrol investigator boarded a train to question Jesus L. Garcia ("Garcia"), based on a tip that a male passenger might be carrying illegal items. After telling Garcia there was no problem and he was not under arrest, Garcia agreed to talk with the investigator. After answering questions, Garcia agreed to "a quick search," retrieved his luggage from the overhead compartment, opened it, and moved the clothes as requested by the investigator. When the investigator asked if he could touch the inside of the bag, Garcia did not respond but reached into his bag and pulled his clothes back, revealing a yellow bundle, which contained methamphetamine. After the district court denied Garcia's motion to suppress the evidence seized from his bag, Garcia conditionally pled guilty and was sentenced to 120 months' imprisonment.

Based on a totality of the circumstances, the Eighth Circuit held the district court did not clearly err in finding the encounter between the investigator and Garcia was consensual. The appellate court reasoned the investigator's close positioning to Garcia was not unreasonable or unreasonably limited Garcia's movement under the circumstances; only two officers were present, both in plain clothes, and the other officer was several seats away; no weapon was displayed, nor did the investigators physically touch Garcia until he was arrested; the investigator's tone and language did not indicate Garcia had to comply; the investigator asked Garcia if he could search his bag, but did not touch or exercise control over it; and upon approaching Garcia, the investigator explicitly stated he was not in trouble and there was no problem, which indicated Garcia was not the focus of a particular investigation.

The Eighth Circuit further concluded there was no plain error in the district court's finding that Garcia voluntarily consented to the physical search of his bag. The appellate court reasoned Garcia was 26; his answers to the officer's questions were appropriate, there was no evidence his intelligence was below average; Garcia was sober during the search; the entire encounter took place in less than four minutes; and the encounter between the investigator and Garcia was consensual.

Ninth Circuit Holds IRS Special Agent Not Entitled to Qualified Immunity on Summary Judgment Because Bodily Intrusion Violated Fourth Amendment

In ***Ioane v. Hodges***, 903 F.3d 929 (9th Cir. 2018), the Ninth Circuit affirmed the district court's denial of summary judgment on a qualified immunity claim in a civil rights lawsuit under 42 U.S.C. § 1983 against an IRS, Criminal Investigation ("IRS-CI") special agent.

IRS-CI executed a search warrant at the residence of Michael and Shelly Ioane. IRS-CI was investigating Michael for tax fraud and conspiracy, but Shelly was not under investigation. Upon arrival at the residence, IRS-CI special agents gave the Ioanes the option to remain or leave the premises during execution of the warrant. The Ioanes chose to remain in the kitchen. When Michael asked to use the bathroom, an agent escorted him, quickly searched the bathroom, and waited outside until Michael came out. Later, Shelly asked to use the bathroom, a female IRS-CI agent escorted her, search the bathroom, but insisted she stay inside the bathroom with Shelly. Despite Shelly's objections, the female agent required Shelly to remove her dress, stating it was standard procedure to ensure Shelly was not hiding anything, and to prevent Shelly from destroying evidence. The female agent directed Shelly how to hold her clothing while she relieved herself and faced Shelly the entire time. Shelly filed a § 1983 civil rights lawsuit against the agent, claiming her actions violated her Fourth Amendment right to bodily privacy. The district court denied the agent's motion for summary judgment on qualified immunity grounds.

The Ninth Circuit affirmed the district court's decision. Following case law analyzing the right to bodily privacy, the appellate court held a reasonable jury could conclude the actions of the IRS-CI agent in accompanying the suspect's wife to the bathroom and standing in the room facing her while she used the toilet were unreasonable and violated Shelly's Fourth Amendment rights. The appellate court further held that the personal privacy interests the IRS-CI agent intruded on were clearly established under Ninth Circuit case law at the time, such that the agent was not entitled to qualified immunity from suit. After weighing the search scope, manner, justification, and place, the Ninth Circuit panel concluded the agent's general interests in preventing destruction of evidence and promoting officer safety were not justified.

Fifth Circuit Upholds Admission of Evidence Based on Attenuation Factors

In ***United States v. Mendez***, 885 F. 3d 899 (5th Cir. 2018), the Fifth Circuit affirmed the district court's suppression ruling, holding that the evidence obtained from an unlawful traffic stop was sufficiently attenuated.

Officers secured a warrant to search the residence of Eligio San Miguel Mendez ("Mendez"). After he left his residence, officers stopped his vehicle and detained him while the search took place. In the car, officers found a revolver, and in the residence they found an empty Glock pistol case and ammunition. Mendez was arrested and interrogated at the police station. He told the officers where the pistol was and confessed he owned the ammunition and firearms. Finding that the traffic stop was

unlawful, the district court suppressed the revolver, but not the pistol or Mendez's statements. Mendez was convicted of being a felon in possession of a firearm and sentenced to 84 months' imprisonment.

On appeal, the Fifth Circuit first noted that the district court erred by not analyzing each of the attenuation factors in *Brown v. Illinois*, 422 U.S. 590, 599 (1975) (temporal proximity, waiver of *Miranda* rights, intervening events, and flagrancy of police misconduct). Nonetheless, the appellate court affirmed the district court's decision to admit Mendez's statements based on its analysis of the *Brown* factors. The Fifth Circuit concluded that Mendez was informed of, understood, and waived his *Miranda* rights; his lawful arrest for being a felon in possession of ammunition was a critical intervening circumstance; and the misconduct at issue was not purposeful and flagrant, but instead motivated by legitimate safety concerns.

Tenth Circuit Holds Evidence is Material to Probable Cause Determination If It Negates Other Evidence

In ***United States v. Gerhmann***, 731 F. App'x. 792 (10th Cir.) (unpublished), *cert. denied*, 139 S. Ct. 462 (2018), the Tenth Circuit held a probable cause affidavit's exclusion of a state agency's admonition letter was *not* material because its inclusion would not have negated other evidence of fraud in the affidavit.

Thomas F. Gerhmann, Jr. ("Gerhmann") and Eric William Carlson ("Carlson") were under criminal investigation for tax and healthcare fraud offenses. In support of a warrant for the search of their businesses and storage facility, the 43-page affidavit detailed existing evidence, referenced other entities' independent investigations, including the Colorado Department of Regulatory Agencies ("DORA"), and concluded there was probable cause to believe that the defendants committed the alleged offenses, evidence of which would be found at the described locations. The affidavit did not reference DORA's admonition letter that declined to pursue any "formal action" following DORA's investigation into healthcare fraud allegations. Execution of the warrants led to seizure of evidence, which resulted in defendants being charged with only criminal tax offenses. Defendants moved to suppress the seized evidence based on the omission of the admonition letter. Following a *Franks* hearing, the district court found DORA's admonition letter material to the probable-cause determination for the alleged healthcare offenses, but not the tax offenses. It further concluded that the invalid healthcare portions of the warrants were not severable from the valid tax portions, and suppressed all evidence seized under the warrants.

The Tenth Circuit reversed, holding the admonition letter was not material because inclusion of the letter in the (corrected) affidavit would not have negated probable cause with respect to healthcare fraud. The appellate court reasoned that the district court had: (i) erroneously imparted a meaning to the admonition letter that was not evident (*i.e.*, describing the letter as a finding that Carlson "was not guilty" of healthcare fraud); and (ii) wrongly focused exclusively on the admonition letter, rather than the totality of the information contained in the affidavit that there was at least a "substantial basis" to conclude that there was a "fair probability" of finding evidence of healthcare fraud.

***Note*:** This is an unpublished opinion.

TITLE 18 – MONEY LAUNDERING

Fifth Circuit Holds Conspiracy to Commit Promotion Money Laundering Does Not Merge with Conspiracy to Commit Health Care Fraud

In ***United States v. Gibson***, 875 F.3d 179 (5th Cir. 2017), *cert. denied*, 139 S. Ct. 1241 (2019), the Fifth Circuit held, *inter alia*, that a conviction for conspiracy to commit promotion money laundering did not merge with a conviction for conspiracy to commit health care fraud.

Earnest Gibson III and Earnest Gibson IV devised a scheme to defraud Medicare by falsely claiming to operate a qualifying Partial Hospitalization Program (PHP). Gibson III, Chief Executive Officer, president, and administrator of Houston's Riverside General Hospital, was convicted, *inter alia,* of conspiracy to commit health care fraud and conspiracy to commit promotion money laundering. Gibson IV operated an affiliated offsite PHP and was convicted of the same conspiracy charges. Gibson III was sentenced to 540 months' imprisonment and ordered to pay $46,753,180.04 in restitution. Gibson IV was sentenced to 240 months' imprisonment and ordered to pay $7,518,480.11 in restitution.

On appeal, the Gibsons argued, *inter alia*, that the conspiracy to commit promotion money laundering merged with the conspiracy to commit health care fraud. The Fifth Circuit rejected this argument, concluding these were two distinct conspiracies, and therefore, there was no merger. The appellate court explained that the health care fraud conspiracy was a pact to perpetrate Medicare fraud while the promotion money laundering conspiracy was a pact to conduct a financial transaction with the proceeds of the health care fraud, intending to promote or further unlawful activity. Put another way, stated the appellate court, the healthcare conspiracy count targeted a conspiracy to submit false bills to Medicare, while the promotion money laundering scheme alleged a conspiracy to use fraudulently obtained money with the goal of submitting subsequent false bills. Thus, the Fifth Circuit affirmed the Gibsons' convictions, holding there was no merger because each conspiracy involved different facts and agreements, and neither one had, as an element, any overt act that could have overlapped to create a merger problem.

FORFEITURE

Fifth Circuit Holds Defendant Commingled Funds to Facilitate Money Laundering Scheme

In ***United States v. Cessa***, 872 F.3d 267 (5th Cir 2017), the Fifth Circuit affirmed the defendant's conviction and sentence, holding, *inter alia,* that sufficient evidence supported the forfeiture order.

Around 2004, Francisco Antonio Colorado-Cessa ("Colorado") became associated with the Zetas, an organization that imports drugs from Colombia and exports them to the United States. The Zetas engaged in a money-laundering operation involving the purchase of racehorses in the U.S. The scheme was designed to conceal illegal drug money by repeatedly buying and reselling horses to "straw purchasers and shell companies" to generate "clean" money, the origin of which was difficult to trace. Colorado was indicted as part the scheme and convicted of conspiracy to launder money. He was sentenced to 200 months' imprisonment, followed by three years' supervised release, forfeiture of two aircrafts and a $60 million money judgment.

After a series of appeals and remands, the Fifth Circuit affirmed Colorado's conviction and sentence. First, the appellate court noted that pursuant to 18 U.S.C. § 982(a)(1), a person convicted of money laundering under 18 U.S.C. § 1956 must "forfeit to the United States any property, real or personal, involved in such offense, or any property traceable to such property." Next, the Fifth Circuit noted that the standard for a § 982 forfeiture is preponderance of the evidence, and that property "involved in" an offense "includes the money or other property being laundered (the corpus), any commissions or fees paid to the launderer, and any property used to facilitate the laundering offense." "Facilitation occurs, the appellate court noted, when the property makes the prohibited conduct 'less difficult or more or less free from obstruction or hindrance.'"

In this case, the Fifth Circuit concluded that the government had introduced sufficient evidence to establish that the forfeited bank accounts were used to facilitate money laundering. The evidence showed that Colorado comingled Zeta drug money in his otherwise legitimate accounts in order to facilitate the money laundering offense. The evidence also showed that both the forfeited aircrafts were used to facilitate the money laundering scheme. Accordingly, the Fifth Circuit affirmed Colorado's conviction and sentence.

SENTENCING

First Circuit Holds Sentence at High End of Guidelines Substantively Reasonable

In ***United States v. Delima***, 886 F.3d 64 (1st Cir. 2018), the First Circuit affirmed a sentence at the high end of the United States Sentencing Guidelines ("USSG or Guidelines") range as substantively reasonable.

While investigating a drug trafficking organization, law enforcement discovered that Malik Delima ("Delima") and others were also engaged in a scheme to manufacture and use fraudulent credit cards. During execution of a search warrant at Delima's associate's apartment, law enforcement discovered equipment used to manufacture fraudulent credit cards, a laptop containing text files of stolen credit card numbers, as well as credit, debit, and gift cards.

Delima pleaded guilty to one count of conspiracy to commit access-device fraud (18 U.S.C. § 1029). According to the presentence investigation report, Delima was responsible for $1,163,000 in intended losses, pursuant to USSG § 2B1.1. At sentencing, the district court determined that Delima's offense level was 24, with a criminal history category of III, resulting in a sentencing range of 63-78 months. The court sentenced Delima to 75 months' imprisonment.

Delima appealed his sentence, arguing that it was substantively unreasonable. He claimed the district court should have granted a downward variance because the actual loss caused by the conspiracy was lower than the intended loss attributed to him. The First Circuit disagreed, noting that the actual loss was lower than the intended loss because law enforcement fortuitously discovered the scheme and seized the equipment and inventory of the conspirators, thus preventing them from profiting further. The First Circuit also noted several aggravating factors that warranted a sentence at the high end of the Guidelines, including: (1) the scheme was "broad-ranging" and crossed state lines; (2) Delima had several prior convictions and began participating in the credit card scheme shortly after serving a term of supervised release; (3) the conspiracy caused significant harm to Maine residents, including banks, credit card holders, and merchants; and (4) the conspiracy stopped only after execution of a search warrant.

TABLE OF CASES