

08-10831

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

UNITED STATES OF AMERICA,
Plaintiff - Appellee,

v.

JAMES RAY PHIPPS,
Defendant - Appellant.

On Appeal from the United States District Court
for the Northern District of Texas
Dallas Division
District Court No. 3:06-CR-114-M

BRIEF FOR THE UNITED STATES

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STATEMENT REGARDING ORAL ARGUMENT

_____ Oral argument is not necessary in this case. The issues and positions of the parties, as presented in the record and briefs, are sufficient to permit the Court to reach a just determination.

TABLE OF CONTENTS

STATEMENT REGARDING ORAL ARGUMENT..... i

TABLE OF AUTHORITIES..... iii

STATEMENT OF JURISDICTION..... 1

STATEMENT OF THE ISSUES. 2

STATEMENT OF THE CASE..... 2

STATEMENT OF FACTS. 4

SUMMARY OF THE ARGUMENT. 20

ARGUMENT AND AUTHORITIES..... 23

 1. There was sufficient evidence in regard to Phipps’s specific
 intent to defraud to support the jury’s guilty verdict on mail
 and wire fraud..... 25

 2. There was sufficient evidence in regard to the connection of
 the wire communication to Phipps’s fraud to support the
 jury’s guilty verdict on wire fraud. 31

 3. There was sufficient evidence to support the jury’s guilty
 verdict of corrupt impediment of the due administration of the
 internal revenue laws. 36

 4. There was sufficient evidence to support the jury’s verdict of
 guilty of tax evasion. 41

 5. The district court did not err in calculating Phipps’s loss amount.. . 44

CONCLUSION..... 49

CERTIFICATE OF SERVICE. 49
CERTIFICATE OF COMPLIANCE. 50

TABLE OF AUTHORITIES

FEDERAL CASES	Page(s)
<i>Brandenburg v. Ohio</i> , 395 U.S. 444 (1969).	38-40
<i>Masses Publishing Co. V. Patten</i> , 244 F. 535 (S.D.N.Y. 1917).	40
<i>Schmuck v. United States</i> , 489 U.S. 705 (1989).	33
<i>United States v. Aubin</i> , 87 F.3d 141 (5th Cir 1996).	31
<i>United States v. Ayala</i> , 887 F.2d 62 (5th Cir. 1989).	24
<i>United States v. Brewer</i> , 807 F.2d 895 (11th Cir. 1987).	17, 35
<i>United States v. Bullard</i> , 13 F.3d 154 (5th Cir. 1994).	25, 36, 45
<i>United States v. Buttorff</i> , 572 F.2d 619 (8th Cir. 1978).	40, 41
<i>United States v. Cabrera</i> , 288 F.3d at 168 (5th Cir. 2002)..	46
<i>United States v. Cooper</i> , 274 F.3d 230 (5th Cir. 2001).	46
<i>United States v. Creech</i> , 408 F.3d 264 (5thCir. 2005).	46
<i>United States v. Duhon</i> , 440 F.3d 711 (5th Cir. 2006).	45, 46
<i>United States v. Evans</i> , 473 F.3d 1115 (11th Cir. 2006).	17, 35
<i>United States v. Georgalis</i> , 631 F.2d 1199 (5th Cir. 1980).	17, 35
<i>United States v. Green</i> , 324 F.3d 375 (5th Cir. 2003).	44
<i>United States v. Hammond</i> , 201 F.3d 346 (5th Cir. 1999).	46, 47
<i>United States v. Hewes</i> , 729 F.2d 1302 (11th Cir. 1984).	17, 35

FEDERAL CASES, cont'd

United States v. Holmes, 406 F.3d 337 (5th Cir. 2005). 24

United States v. Jimenez, 256 F.3d 330 (5th Cir. 2001). 44

United States v. Kelly, 864 F.2d 569 (7th Cir. 1989). 39

United States v. Lane, 474 U.S. 438 (1986). 17, 35

United States v. Moss, 604 F.2d 569 (8th Cir. 1979). 41

United States v. Mulderig, 120 F.3d 534 (5th Cir. 1997). 24

United States v. Olano, 507 U.S. 725 (1993). 25, 26, 37, 45

United States v. Plache, 913 F.2d 1375 (9th Cir. 1990). 30

United States v. Powers, 168 F.3d 741 (5th Cir. 1999). 46

United States v. Rivera, 295 F.3d 461 (5th Cir. 2002). 23

United States v. Santos, ___ U.S. ___, 128 S. Ct. 2020 (2008). 3, 19

United States v. Smith, 440 F.3d 704 (5th Cir. 2006). 45

United States v. Sotelo, 97 F.3d 782 (5th Cir. 1996). 44

United States v. Sowels, 998 F.2d 249 (5th Cir. 1993). 47

United States v. Strong, 371 F.3d 225 (5th Cir. 2004). 16, 31-34

United States v. Sutton, 77 F.3d 91 (5th Cir. 1996). 46

United States v. Toney, 598 F.2d 1349 (5th Cir. 1979). 16, 34

United States v. Williams, 264 F.3d 561 (5th Cir. 2001). 24

FEDERAL STATUTES AND RULES

18 U.S.C. § 2. 2

18 U.S.C. § 1341. 2

18 U.S.C. § 1343. 2, 16, 32, 34

18 U.S.C. § 1956(a)(1)(A)(I).. 2

18 U.S.C. § 3742. 1

18 U.S.C. § 3742(e).. 46

26 U.S.C. § 7201. 3

26 U.S.C. § 7212(a).. 3, 37

28 U.S.C. § 1291. 1

FED. R. APP. P. 4(b). 1

UNITED STATES SENTENCING GUIDELINES

§ 2B1.1. 46, 47

§ 2B1.1(a)(1). 19

§ 2B1.1(b)(1)(J).. 19

§ 2B1.1(b)(1)(K). 48

§ 2B1.1(b)(2)(C). 19

§ 2B1.1(b)(8)(C). 19

UNITED STATES SENTENCING GUIDELINES, cont'd

§ 2B1.1(b)(9)(A). 19

§ 2B1.1, comment. (n.3(C)).. . . . 47

§ 2B1.1, comment. (n.3(E)(1)). 47

§ 2S1.1(b)(2)(B). 19

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BRIEF FOR THE UNITED STATES

STATEMENT OF JURISDICTION

This is an appeal from a final judgment and sentence in a criminal case. This Court has jurisdiction under 28 U.S.C. § 1291 and 18 U.S.C. § 3742. Timely notice of appeal was filed pursuant to Rule 4(b), Fed. R. App. P. (R5/1096-1097.)

STATEMENT OF THE ISSUES

1. Was there sufficient evidence in regard to Phipps's specific intent to defraud to support the jury's guilty verdict on mail and wire fraud?
2. Was there sufficient evidence in regard to the connection of the wire communication to Phipp's fraud to support the jury's guilty verdict on wire fraud?
3. Was there sufficient evidence to support the jury's guilty verdict of corrupt impediment of the due administration of the internal revenue laws?
4. Was there sufficient evidence to support the jury's verdict of guilty of tax evasion?
5. Did the district court err in calculating Phipps's loss amount?

STATEMENT OF THE CASE

On July 12, 2006, a grand jury in the Northern District of Texas, Dallas Division, returned a 22 count indictment against Appellant James Ray Phipps. (R1/153-180.) Counts 1 to 3 charged Phipps with mail fraud and aiding and abetting, in violation of 18 U.S.C. §§ 1341 and 2. (R1/161.) Count 4 charged Phipps with wire fraud and aiding and abetting, in violation of 18 U.S.C. § 1343 and 2. (R1/162.) Counts 5 to 17 charged Phipps with money laundering and aiding and abetting, in violation of 18 U.S.C. §§ 1956(a)(1)(A)(I) and 2. (R1/163-167.) Count 18 charged Phipps with a corrupt endeavor to obstruct and impede

the due administration of the internal revenue laws, in violation of 26 U.S.C. § 7212(a). (R1/168-173.) Counts 19 to 21 charged Phipps with income tax evasion, in violation of 26 U.S.C. § 7201. (R1/174-176.) Count 22 contained a forfeiture allegation. (R1/177-178.)

Phipps was tried before a jury, starting on April 23, 2007. (R1/Docket entry dated 4/23/2007.) On May 2, 2007, on the government’s motion during trial, the district court dismissed money laundering counts 5 and 6. (R1/docket entry dated 5/2/2007.) On May 4, 2007, the jury found Phipps “guilty” on all the remaining substantive counts of the indictment.¹ (R6/652-653.)

On August 21, 2008, the district court entered a judgment of acquittal on all the money laundering counts based on its reading of the Supreme Court’s decision in *United States v. Santos*, ___ U.S. ___, 128 S.Ct. 2020 (2008).² (R5/1117.)

In its written amended judgment entered on November 10, 2008, the district court sentenced Phipps to 210 months’ imprisonment,³ to be followed by a three-

¹These were counts 1 through 4 and counts 7 through 21. (R3/652-653.)

²This judgment of acquittal encompassed counts 7 through 17. (R5/1117.)

³The district court explained this sentence as follows:

This consists of an imprisonment term of two-hundred and ten (210) months on each of Counts 1, 2, 3, and 4, and twenty-two (22) months on each of counts 18, 19, 20, and 21, to run concurrently with Counts 1, 2, 3, and 4, for a total imprisonment term of TWO-HUNDRED and TEN (210) MONTHS.

(continued...)

year term of supervised release. (SUPP/39-71.) The court also ordered Phipps to pay \$1,402,446.00 in restitution. (SUPP/44.)

Phipps filed his timely notice of appeal on August 18, 2008. (R5/1096-1097.)

STATEMENT OF FACTS

The Offense Conduct

The Presentence Report described Phipps' offense conduct as follows:

For over twenty years, James Ray Phipps, operated pyramid schemes and changed business names to avoid legal warnings by state and federal officials. Some of the known names he operated under included Fast Cash Financial Services, Inc., (Fast Cash), Creative Advertising Concepts, Marathon Marketing, and Life Without Debt (LWD).

Prior to 1988, Phipps operated Fast Cash, a pyramid, multi-level marketing scheme identical to LWD, in which participants sent to Phipps payments of \$67.50, through the mail, to 603 Field Street in Colleyville, Texas, the same address later used for LWD between 1996 to 2006. The product provided by Fast Cash to paying investors was a list of names which was referred to as a "down-line" list of those who were already involved in Phipps' scheme. According to [United States Postal Inspector] Ewing, Phipps did not offer a product other than the list of names. The \$67.50 payment was then divided as follows: \$7.50 to Phipps and \$10.00 each to six other individuals. Participants

³(...continued)
(RSupp/41.)

received \$10.00 for every member they recruited. Participants did not receive any payment until they recruited three individuals who invested \$67.50 each.

On January 15, 1988, Phipps, individually, on behalf of Fast Cash, signed an "Agreement Containing Consent Order to Cease and Desist" with the [United States Postal Service]. By doing so, Phipps agreed to permanently discontinue operating a multi-level marketing program and lottery, Fast Cash Financial Services, Inc.

After Phipps signed the "Agreement Containing Consent Order to Cease and Desist," he began operating Marathon Marketing, another pyramid marketing scheme similar to Fast Cash and to LWD. With Marathon Marketing, Phipps continued to solicit money to be sent to his address at 603 Field Street in Colleyville. Participants in Marathon Marketing were directed to join by mail and send to Phipps, \$20, \$65, or \$150 in money orders. According to USPI Ewing, after participants sent in their payments, Phipps sent to them cassette tapes and literature in which Phipps discussed and wrote about making money by compound leveraging, and included anti-government information, some of which was directed against the IRS. New members were encouraged to pay \$150 and were required to recruit two persons to join Marathon Marketing. Of the \$150 payment, Phipps kept \$30 and the remaining funds were distributed "up-line" to existing members in the program.

In a Notice of Intended Action and Opportunity to Cease and Desist dated October 20, 1993, the state of Michigan, Department of the Attorney General, informed Phipps that he had 10 days to cease and desist conducting business in the state of Michigan. The notice stated that Phipps was in violation of Section 28 of the Michigan Franchise Investment Law, which declared pyramid or chain promotions to be illegal and against public policy of the state.

In a letter dated November 15, 1993, authorities in Contra Costa County in Martinez, California, ordered Phipps, and all people associated with Marathon Marketing, to cease and desist all operations within Contra Costa County and elsewhere in the state of California.

In a letter dated May 12, 1994, the County of Fresno in Fresno, California, informed Phipps that Marathon Marketing was the subject of a criminal investigation of the Fresno Police Department. The investigation focused on Marathon Marketing's possible violation of California Penal Code Section 327, "Endless Chain Schemes".

On February 7, 1994, the USPS filed a complaint against Phipps in which it contended he was in breach of the Order to Cease and Desist, which he signed January 15, 1988, by operating Marathon Marketing. On March 24, 1994, an administrative judge with the USPS found that Phipps had breached the terms of the agreement he signed in 1988.

Despite receiving notice from the USPS that his prior businesses, Fast Cash and Marathon Marketing, were considered pyramid schemes, Phipps established and operated Life Without Debt (LWD), a business similar in structure to his prior businesses, Fast Cash and Marathon Marketing.

From June 1996 to June 1, 2006, Phipps operated LWD, a ponzi scheme in the Northern District of Texas and elsewhere. During the scheme, Phipps received in excess of \$25,000,000 from LWD members. Phipps executed the scheme by and through unsolicited facsimile transmissions, unsolicited mailings, and weekly conference telephone calls that encouraged others to become members and contribute money to LWD and receive money in return for recruiting other members. Members were encouraged to contribute between \$2,000 to \$100,000. The larger the contribution

to LWD, the larger the return of money to the contributors from the plan. Contributions were restricted to cash and money orders. After August 20, 2001, Phipps began to require payment in cash only and no longer accepted money orders. Between 2001 and 2006, Phipps modified the LWD program to include a \$400 level, a program Phipps called, "The \$2500 Master Networker Plan," and, finally, a \$200 per month plan which he marketed as a retirement plan.

LWD was a ponzi scheme marketed as a multi-level marketing program which claimed to use compound leveraging to generate large sums of money to its members. Phipps assured members that LWD was legal and was not a pyramid scheme.

Phipps required members to mail their contributions to LWD, 603 Field Street in Colleyville. In order to avoid law enforcement authorities, he relocated his scheme and required members to mail their payments to P.O. Box 980 in Alexandria, Alabama; and to 1414 Golden Springs Road PMB 350, Anniston, Alabama, a United Parcel Service Store. Members were required to recruit two new members within 90 days of their enrollment. The two new members were then required to recruit an additional two new members. The classic pyramid was created with the new members being positioned below the earlier established members. The established contributors were positioned near the top of the pyramid. Phipps represented to members that he collected a 4 percent fee for the administration of the matrix. Phipps also represented that he distributed the remainder of contributor's monies in eight equal payments to the people above them in the pyramid matrix. These members' positions or stages in the pyramid were referred to as "up-line" from new recruits. Phipps instructed members who contributed by money order to send nine money orders and leave the payee lines blank for processing by LWD. Phipps explained

that one money order was for his 4 percent processing fee and the other eight money orders were payments for up-line members in the LWD matrix. In addition to his 4 percent processing fee of each new member's investment, Phipps also received payments as a LWD up-line position founding member.

In an attempt to conceal the illegality of LWD, Phipps provided purported educational materials to new members. The materials included literature and audio cassette tapes, which were anti-government/anti-income tax in nature. New members received a document that indicated their up-line positions or stages in the LWD matrix.

Phipps offered members seven different entry-level plans which ranged from \$2,000 to \$100,000. The \$2,000 plan involved a 2 x 8 matrix which required each member to recruit new members, repeating this cycle until there was an eight-level matrix with 510 members. Phipps' literature represented, "The end result is that \$2,000 is compound leveraged into \$122,400 with minimum effort and absolutely no risk." However, Phipps encouraged members to invest with LWD's \$2,500 plan. The \$2,500 plan required each new member to recruit two more members until 1,024 members were "down-line" in the matrix. A \$2,500 contributor received \$491,040 once the matrix enrollment totaled 1,024 members in the down-line position.

To promote LWD, Phipps held weekly teleconferences and mailed postcards through the U.S. Postal Service which explained the program and the ease with which members accumulated their wealth. Phipps recruited new members through mass mailings, teleconference calls, and seminars held in places which included North Carolina, Alabama, Las Vegas, Nevada, and Chicago, Illinois. The government showed that, after Phipps was indicted, he continued to conduct

weekly conference telephone calls to recruit new members and, in this case, keep existing members informed of his plan. While monitoring these calls, it was discovered that from September 26, 2006, Phipps designed a new plan for the members to use until the charges against him were settled. Members were invited to email Phipps to request an instruction book titled "The Easy Wealth Book," and, in turn send Phipps \$10 for the plan that advised participants that they could "compound" \$110 into more than \$200,000 "without a lot of work," by following Phipps' instructions. In defiance of the court's orders, on October 3 and 10, 2006, Phipps participated in two LWD conference telephone calls in which he discussed the new plan and solicited funds for the publication and his dislike for the "moron jack booted thugs in government," who charged him with the offenses. The email used by Phipps, who ran as an independent for governor in the state of Alabama, was phippsforgov@sbc.net. In another publication forwarded along with "The Easy Wealth Book," Phipps stated he believed the powerful forces in Alabama had caused his Indictment and incarceration in order to keep his name from the ballot. Phipps also purchased mailing lists of individuals to whom he sent his solicitations for LWD.

Phipps' sources of income from LWD were, until August 20, 2001, "net retainage" and "participation proceeds." Net retainage was the 4 percent administrative fee charged and collected by Phipps for each \$1 contributed by a member to LWD. Participation proceeds were monies received and retained by Phipps as an initial established member of LWD. After August 20, 2001, Phipps' earnings came from three combined sources or categories in the LWD which included "Base Level Number," "Vacant," and "In-House Earnings." In-House Earnings equated to net retainage.

In addition to the net retainage and participation proceeds income earned by Phipps, and in furtherance of the scheme, he used false member identities found in the LWD pyramid to surreptitiously siphon a larger portion of member funds.

As part of the scheme, Phipps mailed false materials and fraudulent representations to potential investors in order to entice them to join LWD. Phipps also sent "lulling" cash payments to LWD member participants, the purposes of which were to further the scheme by keeping current participants in the scheme and entice them to recruit additional participants. In addition, on occasion, Phipps sent payments to LWD members even though they had not recruited any new members. These latter payments were designed to encourage the LWD members receiving the payment to continue in the program or, more importantly, to reinvest in larger payment plans.

Phipps also defrauded individuals and obtained money and property by means of false material and fraudulent statements which were transmitted by wire communications.

As a result of this investigation, the numerous complaints, and the prior USPS investigation into Phipps' business activities, in 2001, the IRS executed a search warrant at 603 Field Street in Colleyville, Texas, Phipps' home and business address where he operated LWD.

During the execution of the search warrant, the IRS and USPS seized several computers and LWD materials. On the computers, the IRS found a database that stored the names and addresses of all past and present LWD participants. Phipps used his computer program to determine who had sent in their initial payment (i.e. the new members of LWD) and who should receive a portion of that initial payment (i.e. the existing LWD members).

After the IRS executed the search warrant in 2001, Phipps continued to conduct weekly conference calls to customers, disseminate LWD information, and solicit members and their money. Afterwards, Phipps relocated to Alexandria, Alabama, where he continued to operate LWD.

In a letter dated May 8, 2001, the state of Georgia informed Phipps that "the operation of or participation in a pyramid scheme operation is illegal in Georgia." The letter continued to read, "Please be aware that continued operation in Georgia may result in civil and/or criminal enforcement actions against your company."

In a letter dated June 13, 2001, the State of Oklahoma Department of Securities informed Phipps that it "has received information that Life Without Debt Educational Systems may have engaged, and may continue to be engaged, in activities involving the offer and/or sale of securities in/or from the state of Oklahoma. These securities involve participation in the "Life Without Debt" program." The letter also put Phipps on notice that offers and/or sales of securities are regulated by the Oklahoma Securities Act and that violations of the Act were subject to administrative, civil, and/or criminal sanctions and penalties.

On August 13, 2001, as part of a joint investigation with the Florida State Attorney's Office, the Escambia County Sheriff's Office (Pensacola, FL) executed a search warrant at a location used by Phipps to conduct a series of meetings promoting LWD. During the execution of the search warrant, six LWD members were arrested; five were charged with felony promotion of an illegal lottery, and two were charged with the misdemeanor offense of participating in a lottery.

On April 10, 2006, the Office of the Attorney General of Maryland informed Phipps in writing that establishing, operating, advertising, or promoting a pyramid promotional scheme was prohibited in Maryland

by the Pyramid Promotional Schemes Law. Furthermore, convicted violations are subject to a fine of not more than \$10,000 or imprisonment for not more than one year, or both. The state of Maryland also informed Phipps that, based on its review of LWD, the program was a classic pyramid promotional scheme.

Despite receiving notices from various state agencies that LWD was or may have been an illegal enterprise, Phipps continued to operate LWD.

Phipps also promoted LWD by taking money received in cash from the initial payments of new members and converting the cash into money orders. Phipps then used the money orders to pay Federal Express bills that had been incurred by sending out advertisements, "educational materials," and payments in connection with operating LWD.

Phipps interfered with the due administration of the revenue laws by providing and advertising to prospective LWD participants a source of income that he said need not be reported to the IRS. Phipps operated LWD as a cash business; he used no bank accounts; and he kept no accounting records, which demonstrated that he never intended to report his income to the IRS. Phipps made it clear to participants in LWD that he did not report the payments to the IRS and that reporting the income was not required. LWD was an illegal activity that defrauded numerous investors and allowed those who made money to evade income taxes. The very nature of those activities interfered with the due administration of the IRS.

From 1988 to 2006, Phipps did not report any of his earned income to the IRS. Phipps knew that he was required to report his income and chose not to do so. Counts 19, 20, and 21 of the superseding Indictment include tax years 1999, 2000, and 2001, respectively. Phipps' earned income was \$551,715, \$1,832,389, and \$1,210,407 for these years, respectively. Therefore, the

taxable income for these three years totaled \$3,594,511. This resulted in a tax loss of \$188,599 for 1999, \$694,786 for 2000, and \$430,279 for 2001, which resulted in a total tax loss for these years of \$1,313,664. According to Agent Lagos, these figures were derived by reviewing the data system of LWD and determining the total amount of monies received by Phipps for these years. In her analysis, Agent Lagos allowed for particular business expenses and other deductions, and determined the income and tax loss for these three years. However, according to Agent Lagos, this does not include the tax losses for calendar year 1998, or calendar years 2002 through 2005, for which Phipps failed to file income tax returns and report his income. Agent Lagos reported an analysis was conducted by using the database of LWD and determining an approximate income for the defendant during this time period. Based on the money that was recorded as being received in the LWD system, the total tax loss for 1998 through 2006, which includes the \$1,313,664 for the three counts of conviction, was \$1,533,500.

Phipps demonstrated his intent to evade income taxes by planning a reliance defense that he promoted through LWD. The reliance defense was described in Phipps' literature as "a defense system whereby you rely upon the advice of competent (income tax) professionals and information from creditable sources that could be used to convince a jury of your peers that you sincerely believe that you are not a person that is liable or required to pay or file State or Federal Income Taxes." He began to implement this defense when he told the IRS that he relied on others who told him he did not have to file income taxes.

An analysis of Phipps' computer data revealed that from July 3, 1998, to June 1, 2006, LWD received \$24,900,681 in proceeds from approximately 31,000 participants. Analysis further revealed that less than 9

percent of these participants made a net profit above their initial investment. Approximately 91 percent of participants lost money. From 1998 through 2006, Phipps laundered \$23,518,998 through lulling payments to entice participants to continue recruiting and to join higher level plans. This resulted in a net gain to Phipps in the amount of \$4,606,396, \$1,381,683 [of] which was "participation income," and \$3,224,712 he paid to himself in the pyramid under aliases. Therefore, \$4,606,396 will be used in the computation of the guidelines as the intended loss amount. There is no record of the defendant's expenditures of the money he received, other than making the "lulling" payments to the victims in furtherance of the scheme and paying Federal Express for its services in his correspondence. ***

After he was arrested in Alabama, in April 2006, for the instant offense, Phipps continued to direct the operations of LWD from federal custody until the IRS and USPS conducted a second search warrant of his premises in Anniston, Alabama on June 1, 2006. After the second search warrant, LWD ceased to operate while Phipps was in federal custody. After being transported from Alabama to Texas, Phipps was released from custody subject to certain conditions of his pretrial release. Despite being ordered by the court that he not operate any activity similar to LWD or any other network marketing business, nor associate with LWD members, Phipps violated his conditions of release by starting a new pyramid scheme while he was on house arrest at his mother's home in Arlington, Texas. He also participated in a LWD telephone conference call to entice LWD members to join his new pyramid scheme. This resulted in the revocation of his pretrial bond and current custody status pending sentencing in his case.

The government's investigation discovered a total of 35,416 entries of victims in LWD's data base who invested monies with LWD. However, further

investigation found that numerous entries in LWD's data base included multiple entries of the same victims. Following this analysis, approximately 31,000 participants have been identified as victims. The government's analysis revealed that less than 9 percent of these participants received a net profit beyond their initial investment. Approximately 91 percent of the participants incurred a loss.

Although approximately 9 percent of the participants recovered their initial investment, they are considered victims because they were enticed to join under false pretenses. They would not have invested their money had they known it was an illegal business which made false claims as to the potential earnings they could receive.

(PSR ¶¶ 8-42.)

The Motion for New Trial

On May 11, 2007, Phipps filed a motion for new trial. (R3/658-661.)

Relevant to the issues in this appeal, Phipps alleged that there was insufficient evidence to support his conviction on count four (mail fraud) because the fax at issue there “was not adequately connected with the alleged fraud.” (R3/659.) He also alleged, generally, that the jury’s overall verdicts were “against the great weight of the evidence introduced at trial.” *Id.*

On May 15, 2007, the district court denied Phipps’s motion for a new trial. (R3/664.) The court did request additional briefing on two issues, including the

mail fraud issue.⁴ *Id.* After briefing by the parties the district court found there was sufficient evidence to support the mail fraud conviction, stating:

As to the fax issue, Defendant asserts that he did not rely heavily on fax communications and the specific fax forming the basis of the wire fraud count was tangential, a matter of fortuity, not sent by Defendant, and not a part of Defendant's scheme. A defendant need not personally generate a wire transmission, but must merely "cause the wire communication facilities to be used." 18 U.S.C. § 1343. As the Fifth Circuit noted in *United States v. Strong*, although the federal fraud statute requires more than a tangential relationship between the mailing (or wiring) and the fraud, "[i]t is sufficient for the mailing to be incident to an essential part of the scheme or a step in [the] plot." 371 F.3d 225, 228 (5th Cir. 2004) (internal quotations and citations omitted). "[T]he use of the mails need not be an essential element of the scheme." *Id.* Defendant had instructed individuals with questions about Life Without Debt to contact him by fax, thereby providing customer service to participants in the program. The fax which is the basis for the wire fraud count was sent by a Life Without Debt participant to the Defendant, asking Defendant to correct an error. There is a "well-established rule that mailings from the victims can be mailed in execution of the fraud." *United States v. Toney*, 598 F.2d 1349, 1353 (5th Cir. 1979). Likewise, "post-purchase mailings which are designed to lull the victim into a false sense of security, postpone inquiries or complaints, or make the transaction less suspect are mailings in furtherance of the scheme." *Id.* The "lulling doctrine" has been applied by courts when mailings, even if sent by victims, were "designed

⁴The other issue involved the money laundering counts on which the district court later ordered Phipps' acquittal, and are thus not now part of this appeal.

to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Evans*, 473 F.3d 1115, 1120 (11th Cir. 2006); see also, e.g., *United States v. Lane*, 474 U.S. 438, 452, (1986); *United States v. Hewes*, 729 F.2d 1302, 1321 (11th Cir. 1984).

In *Evans*, the Eleventh Circuit noted that the lulling doctrine was particularly appropriate in cases involving Ponzi schemes, where victims are constantly recruited and solicited for further funds. 473 F.3d at 1121 (citing *United States v. Brewer*, 807 F.2d 895, 898 (11th Cir. 1987); *United States v. Georgalis*, 631 F.2d 1199, 1205 (5th Cir. 1980)). The *Evans* court also noted that "when the scheme includes not only obtaining the benefit of the fraud but also delaying detection of the fraud by lulling the victim after the benefit has been obtained, the scheme is not fully consummated, and does not reach fruition, until the lulling portion of the scheme concludes." *Id.* at 1120. The Court concludes that Life Without Debt was such an ongoing scheme, as it included receiving the benefit of the fraud and also lulling participants into a false sense of security so as to avoid apprehension.

The author of the fax at issue was a victim who invested twice in Life Without Debt, starting at the \$2,500 level and later moving into the \$5,000 plan. The Court finds that the fax was not tangential to Phipps's scheme. By providing the fax number to participants in Life Without Debt, it was reasonably foreseeable to the Defendant that participants would send faxes to him. The Defendant intended to provide customer service to program participants by allowing them to contact him about their accounts. The accessibility of the Defendant to participants was an important part of the scheme—it lulled current participants into a false sense of security as to present and future investments, and thus was essential

to the execution of the scheme. By avoiding apprehension, the Defendant was able to solicit further donations by program participants, and also to recruit new participants.

(R4/965-967.)

The Presentence Report

The PSR fixed Phipps's loss amount for sentencing purposes, and explained its computation as follows:

An analysis of Phipps' computer data revealed that from July 3, 1998, to June 1, 2006, LWD received \$24,900,681 in proceeds from approximately 31,000 participants. Analysis further revealed that less than 9 percent of these participants made a net profit above their initial investment. Approximately 91 percent of participants lost money. From 1998 through 2006, Phipps laundered \$23,518,998 through lulling payments to entice participants to continue recruiting and to join higher level plans. This resulted in a net gain to Phipps in the amount of \$4,606,396, \$1,381,683 [of] which was "participation income," and \$3,224,712 he paid to himself in the pyramid under aliases. Therefore, \$4,606,396 will be used in the computation of the guidelines as the intended loss amount. There is no record of the defendant's expenditures of the money he received, other than making the "lulling" payments to the victims in furtherance of the scheme and paying Federal Express for its services in his correspondence.

(PSR ¶ 39.)

The PSR noted that under USSG § 2B1.1(a)(1) sets a base offense level of 7. (PSR ¶ 52.) This was increased by 18 levels because of the \$4,606,396 loss amount pursuant to USSG § 2B1.1(b)(1)(J). *Id.* Another 6 levels were added, pursuant to USSG § 2B1.1(b)(2)(C), because the offense involved more than 250 victims. *Id.* Two more levels were added, pursuant to USSG § 2B1.1(b)(8)(C), because Phipps violated a prior specific judicial or administrative order. *Id.* Two more levels were added, pursuant to USSG § 2B1.1(b)(9)(A), because Phipps relocated his scheme from Texas to Alabama. *Id.* When combined, these calculations resulted in a base offense level of 35. *Id.*

The PSR then added two levels, pursuant to USSG § 2S1.1(b)(2)(B) because Phipps was convicted of a money laundering offense. (PSR ¶ 53.)

The PSR calculated Phipps's Criminal History Category at III. (PSR ¶ 64.) Based on its calculations, the PSR fixed Phipps's advisory guideline range at 262 to 327 months. (PSR ¶ 91.)

The Sentencing Hearing

At the sentencing hearing, the district court dismissed all of the money laundering counts on which Phipps was convicted, based on its reading of *United States v. Santos*, 128 S.Ct. 2020 (2008). (Supp. Sentencing Tr at 7-8.) Based on this holding, the district court removed the two-level enhancement imposed by the

PSR based on the money laundering convictions, which reduced Phipps's total offense level to 35. *Id.* at 8-9. The court then held that Phipps's advisory guideline range was thus reduced to 210 to 262 months. *Id.*

The district court then sustained Phipps's objection to the PSR's addition of two levels based on his relocation from Texas to Alabama. *Id.* at 21. Next, the district court reduced Phipps's Criminal History Category from III to II. *Id.* at 24. These two adjustments by the district court reduced the advisory guideline range to 151 to 181 months. *Id.*

The district court then partially sustained the government's objection to the PSR's calculation of the loss amount and added two offense levels on that basis. *Id.* at 55-56. This brought the advisory guideline range to 188 to 235 months. *Id.* at 56.

The district court then sentenced Phipps to 210 months' imprisonment. *Id.* at 80-81. This is to be followed by a three-year term of supervised release. *Id.* at 90.

SUMMARY OF THE ARGUMENT

Phipps first contends there was insufficient evidence to permit a reasonable jury to find that he had the specific intent to defraud, as required for his mail and wire fraud convictions. The record contains extensive evidence that shows that at

least since 1988, Phipps has operated schemes, under various names, that were for all practical purposes, identical to the LWD scheme involved in this case. The record also indicates that Phipps had voluntarily entered into cease and desist orders involving those plans, and had then been found in violation of those orders for continuing to operate his scheme. He was also put on notice by officials from various states that his plans violated their laws. Finally, there was evidence that on at least six occasions, a Postal Inspector met personally with Phipps and explained why his basic scheme of operation was fraudulent and illegal. In the face of this evidence, there was clearly a sufficient basis to permit a rational jury to find Phipps had a specific intent to defraud.

Next, Phipps argues there was insufficient evidence to connect a fax transmission to him to sustain his wire fraud conviction. This issue was carefully considered by the district court, which wrote a comprehensive opinion explaining its finding that the evidence was sufficient. That opinion is correct both legally and factually. There was no error.

Next, Phipps asserts that there was insufficient evidence to support his conviction for corrupt impediment of the internal revenue laws. The record demonstrates that Phipps had a long and consistent record of telling followers that their income from his programs was not taxable and that they should not report it

to the IRS. In support of such claims, he told followers that he did not report such income himself. Phipps argues that using these statements as a basis for conviction violates his First Amendment rights. The Supreme Court has made clear that speech advocating illegal action is not protected so long as it is directed to inciting imminent lawless action. A review of the law, including cases cited by Phipps, makes clear that his speech here falls outside the protection of the First Amendment. The consideration of the speech was proper and there was thus sufficient evidence to sustain the conviction.

Next, Phipps argues that there was insufficient evidence to support his tax evasion conviction. Phipps bases this allegation on his assertion that the jury was required to accede to his assertions that he genuinely believed that he did have an obligation to pay taxes for the years at issue. The record shows that Phipps completely failed to file tax returns since 1988. During many of those years, the IRS filed substituted returns assessing Phipps taxes based on the evidence of income that was available to them. These assessments clearly put Phipps on notice that he did in fact have tax obligations, yet in each of the years in question, he wholly failed to file a tax return as required by law. There is clearly sufficient evidence to sustain the conviction.

Finally, Phipps asserts that the district court did not properly give him credit for the value of tapes and educational materials he supplied to followers in calculating his loss amount for sentencing purposes. Since he did not raise this argument in the district court, it is reviewed for plain error. Phipps never offered any evidence as to the reasonable value of the tapes and educational materials, and thus the district court lacked any basis on which to give him the credit he now seeks. Even more importantly, Phipps would have to show the district court erred by more than \$9,000,000.00 in fixing his loss amount before he would be entitled to a lower offense level on that basis. Needless to say, nothing in the record supports such an allegation. There was no error – and certainly no plain error.

ARGUMENT AND AUTHORITIES

The Sufficiency of Evidence Standard of Review

When a proper objection is made, “the standard for evaluating the sufficiency of the evidence is whether a rational jury, viewing the evidence in the light most favorable to the prosecution, could have found the essential elements of the offense beyond a reasonable doubt. When viewing the evidence, we draw all reasonable inferences in favor of the jury’s verdict.” *United States v. Rivera*, 295 F.3d 461, 466 (5th Cir. 2002) (internal citations omitted). In *United States v.*

Williams, 264 F.3d 561, 576 (5th Cir. 2001), this Court further described the standard:

We have recognized that the jury is free to choose among all reasonable constructions of the evidence, and it is not necessary that the evidence exclude every reasonable hypothesis of innocence or be wholly inconsistent with every conclusion except that of guilt. Our review is thus limited to whether the jury's verdict was reasonable, not whether we believe it to be correct. Finally, this standard of review applies whether the evidence is direct or circumstantial.

(Internal quotation marks and citations omitted). This Court has also explained that in making this determination:

[W]e apply a "rule of reason," knowing that the jury may properly rely on their "common sense" and "evaluate the facts in light of their knowledge and the natural tendencies and inclinations of human beings."

United States v. Holmes, 406 F.3d 337, 351 (5th Cir. 2005), quoting *United States v. Mulderig*, 120 F.3d 534, 547 (5th Cir. 1997), and *United States v. Ayala*, 887 F.2d 62, 67 (5th Cir. 1989).

- 1. There was sufficient evidence in regard to Phipps's specific intent to defraud to support the jury's guilty verdict on mail and wire fraud.**

Standard of Review

Phipps cites to no place in the record where he raised this specific sufficiency objection before the district court. With no objection on this ground having been made, this ground of error must be reviewed for plain error. In *United States v. Bullard*, 13 F.3d 154, 156 (5th Cir. 1994), this Court said:

We will allow sentences to be attacked on grounds raised for the first time on appeal in only the most exceptional cases. A party must raise a claim of error with the district court in such a manner so that the district court may correct itself and thus, obviate the need for our review. This court will not reverse a district court on an issue raised for the first time on appeal unless a gross miscarriage of justice would otherwise result.

(Internal footnotes omitted).

Under the plain error standard, error is reversible only if it is clear or obvious and affects the defendant's substantial rights. Phipps bears the burden of showing prejudice under the plain error standard. *United States v. Olano*, 507 U.S. 725, 734 (1993) (“[I]t is the defendant rather than the Government who bears the burden of persuasion with respect to prejudice.”). Furthermore, even if plain error is established, the Court may decline to reverse if the error had no serious

effect on the fairness, integrity, or public reputation of judicial proceedings.

Olano, 507 U.S. at 732.

Discussion

Phipps argues that there was insufficient evidence of his specific intent to defraud, which is necessary to violate the mail and wire fraud statutes. (Phipps’s Brief at 9-12.) To support this assertion, Phipps relies on self-serving statements he made about his purposes and beliefs concerning the LWD program. *Id.* This totally ignores the extensive evidence before the jury concerning Phipps’s long history of operating ponzi-type schemes and the large numbers of ways in which he had been told that such schemes were fraudulent and illegal. In light of this evidence, there was no question that there was sufficient evidence to support a jury finding of specific intent.

For both the mail and wire fraud counts, the district court clearly charged the jury that the government was required to prove that Phipps acted with “a specific intent to defraud.” (Mail fraud:R3/632; Wire fraud:R3/633.)

The jury heard testimony from Steven Caver, a retired United States Postal Inspector who had been involved with investigations involving Phipps from 1987 until his retirement in 2004. (Tr. Tran. 1/204-205.) During this time Phipps operated using six or seven different names. *Id.* at 206. Among these names were

Fast Cash (*Id.* at 204), Marathon Marketing, (*Id.* at 212), and Life Without Debt, (Tr. Tran. 2/42-43). All of these programs, whatever name they went by, were pyramid schemes and were essentially identical in their operation.⁵ (Tr. Tran 2/206-208.)

The record also contains a great deal of information about Phipps's encounters over the years with various state and federal law enforcement authorities all of whom, in one way or another, made Phipps aware that his basic scheme was fraudulent and illegal. Despite this vast array of notice, Phipps continued to operate his basic scheme, changing the name to try to avoid detection.

The PSR provided a good summary of the evidence the jury heard about the various ways Phipps unquestionably learned that his scheme was fraudulent and illegal:⁶

⁵Postal Inspector Caver specifically told the jury:

“The common thread was that they all required a certain amount of money to purchase or get involved in the promotion. Then it also – they had several levels involved. It was not just you get involved, you sell something, you make a commission. It always involved recruiting other people and filling in levels. There was always a large sum of cash that you could make as a result of participating in the promotion.”

(Tr. Tran 1/206-207.)

⁶In addition to the items described in the PSR, the jury also had documentary and testimonial evidence about a judgement against Phipps and a business called Paymaster (an
(continued...)

On January 15, 1988, Phipps, individually, on behalf of Fast Cash, signed an "Agreement Containing Consent Order to Cease and Desist" with the [United States Postal Service].⁷ By doing so, Phipps agreed to permanently discontinue operating a multi-level marketing program and lottery, Fast Cash Financial Services, Inc.

After Phipps signed the "Agreement Containing Consent Order to Cease and Desist," he began operating Marathon Marketing, another pyramid marketing scheme similar to Fast Cash and to LWD. With Marathon Marketing, Phipps continued to solicit money to be sent to his address at 603 Field Street in Colleyville.⁸ ***

In a Notice of Intended Action and Opportunity to Cease and Desist dated October 20, 1993, the state of Michigan, Department of the Attorney General, informed Phipps that he had 10 days to cease and desist conducting business in the state of Michigan.⁹ The notice stated that Phipps was in violation of Section 28 of the Michigan Franchise Investment Law, which declared pyramid or chain promotions to be illegal and against public policy of the state.

⁶(...continued)

interim between Fast Cash and Marathon (Tr. Tran 1/212)). *See* Government Exhibit 2 and (Tr. Tran 1/219.) The jury also had documentary and testimonial evidence about a letter received from the State of North Carolina by Phipps. *See* Government Exhibit 5 and (Tr. Tran 1/220.; Tr. Tran 2/ 29.)

⁷This evidence was presented to the jury by way of Government Exhibit 1 and the testimony of Postal Inspector Caver. (Tr. Tran 1/209-210; Tr. Tran 2/17-22.)

⁸This evidence was presented to the jury by way of the testimony of Postal Inspector Caver. (Tr. Tran 1/211-212.) The jury also had before it Government Exhibit 9 which was a book containing Marathon's promotional materials. (Tr. Tran 2/222.)

⁹This evidence was presented to the jury by way of Government Exhibit 6 and the testimony of Postal Inspector Caver. (Tr. Tran 1/220; Tr. Tran 2/32.)

In a letter dated November 15, 1993, authorities in Contra Costa County in Martinez, California, ordered Phipps, and all people associated with Marathon Marketing, to cease and desist all operations within Contra Costa County and elsewhere in the state of California.¹⁰

In a letter dated May 12, 1994, the County of Fresno in Fresno, California, informed Phipps that Marathon Marketing was the subject of a criminal investigation of the Fresno Police Department.¹¹ The investigation focused on Marathon Marketing's possible violation of California Penal Code Section 327, "Endless Chain Schemes".

On February 7, 1994, the USPS filed a complaint against Phipps in which it contended he was in breach of the Order to Cease and Desist, which he signed January 15, 1988, by operating Marathon Marketing. On March 24, 1994, an administrative judge with the USPS found that Phipps had breached the terms of the agreement he signed in 1988.¹²

Despite receiving notice from the USPS that his prior businesses, Fast Cash and Marathon Marketing, were considered pyramid schemes, Phipps established and operated Life Without Debt (LWD), a business similar in structure to his prior businesses, Fast Cash and Marathon Marketing.¹³

¹⁰This evidence was presented to the jury by way of Government Exhibit 4 and the testimony of Postal Inspector Caver. (Tr. Tran 1/220.)

¹¹This evidence was presented to the jury by way of Government Exhibit 7 and the testimony of Postal Inspector Caver. (Tr. Tran 1/221; Tr. Tran 2/32-33.)

¹²This evidence was presented to the jury by way of Government Exhibit 10 and the testimony of Postal Inspector Caver. (Tr. Tran 1/214-215; Tr. Tran 2/17-22; Tr. Tran 2/26.)

¹³This evidence was presented to the jury by way of the testimony of Postal Inspector Caver. (Tr. Tran 1/206-208; Tr. Tran 2/17-22.)

(PSR ¶¶ 10-16.)

In addition to this large array of legal notices that his schemes were fraudulent and illegal, Postal Inspector Caver also testified that he had at least six different conversations with Phipps over the years in which he explained why Phipps's schemes were illegal. (Tr. Tran 1/226-227.) Phipps was thus well aware that his LWD scheme was fraudulent and illegal, but nevertheless proceeded with the plan. There was thus clearly sufficient evidence from which a jury could reasonably conclude that Phipps had the specific intent to defraud.

This case is very similar to *United States v. Plache*, 913 F.2d 1375 (9th Cir. 1990). There the defendant, who sold a commodity trading program called the "ELMAS Trading Program," was convicted of, among other offenses, numerous counts of mail fraud. *Id.* at 1376-1377. Rejecting a challenge to the sufficiency of the evidence to support a finding of specific intent to defraud, that court held:

Plache had been served with a preliminary injunction by the California Department of Corporations, enjoining codefendants Attarain and Smith, *inter alia*, "and persons acting in concert or participating with them" from promoting the ELMAS. The Department then brought a contempt action against Plache for violating the injunction by continuing to offer the ELMAS Program. Plache and others were found in contempt, following a trial. This circumstantial evidence was more than sufficient to establish the specific intent element.

913 F.2d at 1382. *See also United States v. Aubin*, 87 F.3d 141, 147 (5th Cir 1996) (cease and desist order served on another party was factor considered in finding sufficient evidence of specific intent).

This is very similar to Phipps's situation where, after agreeing to the cease and desist order involving Fast Cash, he was found to have violated the order by operating Marathon – plans that were essentially identical in their critical aspects to LWD. There was sufficient evidence to support the jury's specific intent findings, and there is no reason for this Court to set those findings aside.

2. There was sufficient evidence in regard to the connection of the wire communication to Phipps's fraud to support the jury's guilty verdict on wire fraud.

Discussion

Phipps argues that there was insufficient evidence to sustain the wire fraud count of conviction because the fax that formed its basis was not an integral part of the scheme to defraud. (Phipps's Brief at 12.) There is no merit to this contention.

Specifically, Phipps relies on *United States v. Strong*, 371 F.3d 225, 231 (5th Cir. 2004), for the proposition that the statute requires more than a tangential relationship between the wire and the fraud. He contends that because he did not generate the fax, it did not constitute a part of his scheme, and he did not rely

heavily on such communications, that the fax is tangential to the scheme and therefore cannot support his conviction. The defendant's argument fails.

First, there is not and has never been, a requirement that a defendant generate a wire transmission or mailing. All that is required is that the defendant "cause the wire communication facilities ... to be used." 18 U.S.C. § 1343. The Fifth Circuit Pattern Jury instructions (which the court used in the instant case) state:

It is not necessary that the government prove all of the details alleged in the indictment concerning the precise nature and purpose of the scheme, or that the material transmitted by wire was itself false or fraudulent, or that the alleged scheme actually succeeded in defrauding anyone, or that the use of interstate wire communications facilities was intended as the specific or exclusive means of accomplishing the alleged fraud.

What must be proved beyond a reasonable doubt is that the defendant knowingly devised ... a scheme to defraud that was substantially the same as the one alleged in the indictment, and that the use of the interstate wire communications facilities was closely related to the scheme because the defendant either wired something or caused it to be wired in interstate commerce in an attempt to execute or carry out the scheme. To "cause" interstate wire communications facilities to be used is to do an act with knowledge that the use of the wire facilities will follow in the ordinary course of business or where such use can reasonably be foreseen.

In *Strong*, the Fifth Circuit was concerned with a mailing that had no connection to the scheme to defraud, and, in fact, was not contemplated by the

defendant in operating his scheme. Neither the defendant, nor any victim or co-conspirator caused the mailing, and the mailing occurred after the fraud was complete. Here, none of those considerations exist. The fax at issue is a downline report that was sent from a Life Without Debt participant to the defendant to notify him of errors in the participant's downline that needed to be corrected. Contrary to the defendant's assertion that he did not plan for the fax to occur, on a similar form (the upline report) the defendant instructed individuals to do exactly what the participant in this case did: notify him of any problems so that the necessary corrections could be made.

Even though Phipps claims not to rely heavily on these types of communications, the defendant's business partly depended on them so that a proper matrix was created for the distribution of incoming payments. The Court in *Strong* explained "that for a mailing to be part of the execution of a fraudulent scheme, 'the use of the mails need not be an essential element of the scheme.'" 371 F.3d at 228 (quoting *Schmuck v. United States*, 489 U.S. 705, 710 (1989)). They continued by saying that "[i]t is sufficient for the mailing to be 'incident to an essential part of the scheme' or 'a step in [the] plot.'" *Id.* Rather than a tangential wire as the defendant suggests, the fax he complains of was essential to the fraud

being perpetrated by the defendant, or at the very least, incident to an essential part of the scheme or a step in the plot, making any reliance on *Strong* misplaced.

The district court carefully considered this issue and wrote a long and thoughtful opinion addressing it. The court described its reasons for rejecting this argument as follows:

As to the fax issue, Defendant asserts that he did not rely heavily on fax communications and the specific fax forming the basis of the wire fraud count was tangential, a matter of fortuity, not sent by Defendant, and not a part of Defendant's scheme. A defendant need not personally generate a wire transmission, but must merely "cause the wire communication facilities to be used." 18 U.S.C. § 1343. As the Fifth Circuit noted in *United States v. Strong*, although the federal fraud statute requires more than a tangential relationship between the mailing (or wiring) and the fraud, "[i]t is sufficient for the mailing to be incident to an essential part of the scheme or a step in [the] plot." 371 F.3d 225, 228 (5th Cir. 2004) (internal quotations and citations omitted). "[T]he use of the mails need not be an essential element of the scheme." *Id.* Defendant had instructed individuals with questions about Life Without Debt to contact him by fax, thereby providing customer service to participants in the program. The fax which is the basis for the wire fraud count was sent by a Life Without Debt participant to the Defendant, asking Defendant to correct an error. There is a "well-established rule that mailings from the victims can be mailed in execution of the fraud." *United States v. Toney*, 598 F.2d 1349, 1353 (5th Cir. 1979). Likewise, "post-purchase mailings which are designed to lull the victim into a false sense of security, postpone inquiries or complaints, or make the transaction

less suspect are mailings in furtherance of the scheme." *Id.* The "lulling doctrine" has been applied by courts when mailings, even if sent by victims, were "designed to lull the victims into a false sense of security, postpone their ultimate complaint to the authorities, and therefore make the apprehension of the defendants less likely than if no mailings had taken place." *United States v. Evans*, 473 F.3d 1115, 1120 (11th Cir. 2006); see also, e.g., *United States v. Lane*, 474 U.S. 438, 452, (1986); *United States v. Hewes*, 729 F.2d 1302, 1321 (11th Cir. 1984).

In *Evans*, the Eleventh Circuit noted that the lulling doctrine was particularly appropriate in cases involving Ponzi schemes, where victims are constantly recruited and solicited for further funds. 473 F.3d at 1121 (citing *United States v. Brewer*, 807 F.2d 895, 898 (11th Cir. 1987); *United States v. Georgalis*, 631 F.2d 1199, 1205 (5th Cir. 1980)). The *Evans* court also noted that "when the scheme includes not only obtaining the benefit of the fraud but also delaying detection of the fraud by lulling the victim after the benefit has been obtained, the scheme is not fully consummated, and does not reach fruition, until the lulling portion of the scheme concludes." *Id.* at 1120. The Court concludes that Life Without Debt was such an ongoing scheme, as it included receiving the benefit of the fraud and also lulling participants into a false sense of security so as to avoid apprehension.

The author of the fax at issue was a victim who invested twice in Life Without Debt, starting at the \$2,500 level and later moving into the \$5,000 plan. The Court finds that the fax was not tangential to Phipps's scheme. By providing the fax number to participants in Life Without Debt, it was reasonably foreseeable to the Defendant that participants would send faxes to him. The Defendant intended to provide customer service to program participants by allowing them to contact him about their accounts. The accessibility of the Defendant

to participants was an important part of the scheme—it lulled current participants into a false sense of security as to present and future investments, and thus was essential to the execution of the scheme. By avoiding apprehension, the Defendant was able to solicit further donations by program participants, and also to recruit new participants.

(R4/965-967.)

The district court heard all of the evidence in the case and very carefully considered the relevant law. The court is clearly correct in its conclusion that there was sufficient evidence to support the wire fraud conviction. There was no error in the jury’s verdict, and there is no reason for this Court to set that proper jury verdict aside.

- 3. There was sufficient evidence to support the jury’s guilty verdict of corrupt impediment of the due administration of the internal revenue laws.**

Standard of Review

Phipps does not cite any objection he made raising the arguments he now raises in the district court, and research has not located such an objection. This claim is therefore reviewable under the plain error standard. In *United States v. Bullard*, 13 F.3d 154, 156 (5th Cir. 1994), this Court said:

We will allow sentences to be attacked on grounds raised for the first time on appeal in only the most exceptional cases. A party must raise a claim of error with the district

court in such a manner so that the district court may correct itself and thus, obviate the need for our review. This court will not reverse a district court on an issue raised for the first time on appeal unless a gross miscarriage of justice would otherwise result.

(Internal footnotes omitted).

Under the plain error standard, error is reversible only if it is clear or obvious and affects the defendant's substantial rights. Phipps bears the burden of showing prejudice under the plain error standard. *United States v. Olano*, 507 U.S. 725, 734 (1993) (“[I]t is the defendant rather than the Government who bears the burden of persuasion with respect to prejudice”). Furthermore, even if plain error is established, the Court may decline to reverse if the error had no serious effect on the fairness, integrity, or public reputation of judicial proceedings. *Olano*, 507 U.S. at 732.

Discussion

Phipps asserts that there was insufficient evidence to support his conviction under 26 U.S.C. § 7212(a). There is no factual or legal merit to this assertion.

The PSR summed up the government's case against Phipps as follows:

Phipps interfered with the due administration of the revenue laws by providing and advertising to prospective LWD participants a source of income that he said need not be reported to the IRS. Phipps operated LWD as a cash business; he used no bank accounts; and

he kept no accounting records, which demonstrated that he never intended to report his income to the IRS. Phipps made it clear to participants in LWD that he did not report the payments to the IRS and that reporting the income was not required. LWD was an illegal activity that defrauded numerous investors and allowed those who made money to evade income taxes. The very nature of those activities interfered with the due administration of the IRS.

(PSR ¶ 36.)

The district court charged the jury that to “obstruct or impede” means “to hinder or prevent or delay, or make more difficult, the administration of the Internal Revenue laws.” (R3/639.) That is clearly what Phipps did in this case.

The First Amendment

For the first time on appeal, Phipps asserts that his free speech rights under the First Amendment protect him from a conviction based on his extensive advocacy that his followers do as he did and not file federal income tax returns. In particular, he relies on the Supreme Court’s holding in *Brandenburg v. Ohio*, 395 U.S. 444 (1969). There, the Court held:

[T]he constitutional guarantee of free speech and free press do not permit a State to forbid or proscribe advocacy of the use of force or of law violation *except where such advocacy is directed to inciting or producing imminent lawless action and is likely to incite or produce such action.*

Id. at 447. (Emphasis added.) Telling his followers that he did not report his LWD income to the IRS and that they were not required to do so clearly comes within the requirements of *Brandenburg*.

The very cases that Phipps cites make this clear. In *United States v. Kelly*, 864 F.2d 569 (7th Cir. 1989), the court addressed a case involving a defendant's advice about tax shelters. The court held:

Kelley did more than merely advocate a tax shelter at a seminar. The evidence showed that he sold the shelter to his clients, advised his clients about the "recourse" portion of the notes, told his clients to keep the side letter agreement secret from the IRS, attended and participated in the closings, and received a commission for each sale. The district court properly rejected the first amendment protection of advocacy instruction.

Id. at 577. That behavior closely parallels what Phipps did here. Phipps told his followers that they did not need to report any of their LWD income to the IRS and bolstered that claim by telling them that he did not report his LWD income. Just as the defendant in *Kelly* advised his clients to keep certain matters secret from the IRS, Phipps similarly advised his followers to keep all of their LWD income secret from the IRS. In both cases, it is easy to determine that those statements gave rise to the imminent likelihood of lawless action as those hearing this very specific and

targeted advice followed it, and thus impeded the IRS's ability to collect the tax revenue it was due.

In *United States v. Buttorff*, 572 F.2d 619, 624 (8th Cir. 1978), another case relied on by Phipps, that court quoted with approval from an earlier writing of Judge Learned Hand: "One may not counsel or advise others to violate the law as it stands. Words are not only the keys of persuasion, but the triggers of action..." Quoting *Masses Publishing Co. V. Patten*, 244 F. 535, 540 (S.D.N.Y. 1917). The court also noted *Brandenburg's* teachings about the need to incite imminent lawless activity. 572 F.2d at 624.

In *Buttorff*, the defendant counseled about how to avoid income withholding just as Phipps counseled about how to avoid taxes by not reporting LWD income to the IRS. On those facts, the Eighth Circuit held:

Although the speeches here do not incite the type of imminent lawless activity referred to in criminal syndicalism cases, the defendants did go beyond mere advocacy of tax reform. They explained how to avoid withholding and their speeches and explanations incited several individuals to activity that violated federal law and had the potential of substantially hindering the administration of the revenue. This speech is not entitled to first amendment protection and, as discussed above, was sufficient action to constitute aiding and abetting the filing of false or fraudulent withholding forms.

572 F.2d at 624. Just as was true for *Buttorff*, Phipps's speech directly advocating illegal action by his followers is not entitled to First Amendment protection. See also *United States v. Moss*, 604 F.2d 569 (8th Cir. 1979) (following *Buttorff*).

There was clearly a sufficient evidentiary basis to permit a reasonable jury to find Phipps guilty on this count. There is no reason for this Court to set that jury verdict aside.

4. There was sufficient evidence to support the jury's verdict of guilty of tax evasion.

Discussion

Phipps's only challenge to the sufficiency of the evidence to support his tax evasion conviction is based on the tenuous assertion that he was genuine in his belief that he did not owe any taxes. (Phipps's Brief at 21.) Even a cursory examination of the record belies this assertion.

The PSR summed up the evidence on this issue as follows:

From 1988 to 2006, Phipps did not report any of his earned income to the IRS. Phipps knew that he was required to report his income and chose not to do so. Counts 19, 20, and 21 of the superseding Indictment include tax years 1999, 2000, and 2001, respectively. Phipps' earned income was \$551,715, \$1,832,389, and \$1,210,407 for these years, respectively. Therefore, the taxable income for these three years totaled \$3,594,511. This resulted in a tax loss of \$188,599 for 1999, \$694,786 for 2000, and \$430,279 for 2001, which

resulted in a total tax loss for these years of \$1,313,664.

Phipps demonstrated his intent to evade income taxes by planning a reliance defense that he promoted through LWD. The reliance defense was described in Phipps' literature as "a defense system whereby you rely upon the advice of competent (income tax) professionals and information from creditable sources that could be used to convince a jury of your peers that you sincerely believe that you are not a person that is liable or required to pay or file State or Federal Income Taxes." He began to implement this defense when he told the IRS that he relied on others who told him he did not have to file income taxes.

(PSR ¶¶ 37-38.)

The record makes clear that Phipps did not file any tax return for the years from 1988 through 2004. (Tr. Tran3/226-236.) During several of these years, based on income reported by banks and other institutions for Phipps, the IRS prepared and filed substitute tax returns and gave Phipps notice of such returns and the taxes that he thus owed. *Id.* It is thus impossible for Phipps to assert that a jury could not determine that he lacked the intent to evade taxes – he was clearly on notice that he did in fact owe taxes. There is no evidence that Phipps ever tried to resolve his tax issues with the government or make any attempt to vindicate whatever beliefs he may have claimed to hold.

His assertion here is nothing more than a continuation of the scheme he pushed on the people who participated in his fraudulent schemes. Recall that Phipps advised his followers that: "a defense system whereby you rely upon the advice of competent (income tax) professionals and information from creditable sources that could be used to convince a jury of your peers that you sincerely believe that you are not a person that is liable or required to pay or file State or Federal Income Taxes." (PSR ¶ 38.)

Based on the evidence before the jury, there is no way to conclude that a reasonable jury could not have determined that Phipps had the specific intent to evade his income taxes when he completely failed to file tax returns for the years at issue. Phipps clearly had taxable income for the years in question, and thus had an obligation to file tax returns. The fact that Phipps thought he could evade his obligation by simply not filing any return proves rather than refutes his intent in this case. The jury had the opportunity to consider this issue, and, based on the evidence, rejected it. There is no valid reason for this Court to set that jury verdict aside.

5. The district court did not err in calculating Phipps's loss amount.

Standard of Review

Phipps raises a narrow complaint based on the fact that the district court did not offset his loss amount with the “value” of the “audiotapes and other educational materials” they received from Phipps. (Phipps’s Brief at 22-23.) Phipps does not cite to any place in the record where he raised this objection in the district court, and a review of the record has revealed none. When the objection raised in the district court differs from the objection raised on appeal, this Court applies the plain error standard. *United States v. Green*, 324 F.3d 375, 381 (5th Cir. 2003) (“Because the basis for Green’s objection during trial is different from the theory he now raises on appeal, ‘plain error’ is the standard of review.”), *citing United States v. Jimenez*, 256 F.3d 330, 340 (5th Cir. 2001) (holding that “where the theory underlying the basis for an appeal is different from the one raised in the lower court, ‘plain error’ should be the standard of review.”). *See also United States v. Sotelo*, 97 F.3d 782, 793 (5th Cir. 1996) (“Because [the defendant’s] objection to the remark at trial was based on a different theory than that presented on appeal, this Court applies the plain error standard of review.”).

In *United States v. Bullard*, 13 F.3d 154, 156 (5th Cir.1994), this Court said:

We will allow sentences to be attacked on grounds raised for the first time on appeal in only the most exceptional cases. A party must raise a claim of error with the district court in such a manner so that the district court may correct itself and thus, obviate the need for our review. This court will not reverse a district court on an issue raised for the first time on appeal unless a gross miscarriage of justice would otherwise result.

(Internal footnotes omitted).

Under the plain error standard, error is reversible only if it is clear or obvious and affects the defendant's substantial rights. Phipps bears the burden of showing prejudice under the plain error standard. *United States v. Olano*, 507 U.S. 725, 734 (1993) (“[I]t is the defendant rather than the Government who bears the burden of persuasion with respect to prejudice”). Furthermore, even if plain error is established, the Court may decline to reverse if the error had no serious effect on the fairness, integrity, or public reputation of judicial proceedings. *Olano*, 507 U.S. at 732.

If a proper objection had been made, “the district court’s interpretation of the Guidelines, even after *Booker*, is reviewed *de novo*.” *United States v. Duhon*, 440 F.3d 711, 714 (5th Cir. 2006), citing *United States v. Smith*, 440 F.3d 704 at n.2 (5th Cir. 2006). “We accept the district court’s findings of fact unless clearly

erroneous.” *Duhon*, 440 F.3d at 714, *citing United States v. Creech*, 408 F.3d 264, 270 n. 2 (5th Cir. 2005). “This court reviews a district court’s loss determination for clear error.” *United States v. Hammond*, 201 F.3d 346, 350 (5th Cir. 1999), *citing United States v. Sutton*, 77 F.3d 91, 95 (5th Cir. 1996). “Giving due regard to the opportunity of the district court to judge the credibility of the witnesses, 18 U.S.C. § 3742(e), we will deem the district court’s factual findings clearly erroneous only if based on the entire evidence, we are left with the definite and firm conviction that a mistake has been committed.” *Cabrera*, 288 F.3d at 168 quoting *United States v. Cooper*, 274 F.3d 230, 238 (5th Cir. 2001). “A factual finding is not clearly erroneous as long as it is plausible in the light of the record as a whole.” *United States v. Powers*, 168 F.3d 741, 752 (5th Cir. 1999).

Discussion

An Application Note to § 2B1.1, the guideline provision under which Phipps’s offense level was determined, states:

Estimation of Loss. – The court need only make a reasonable estimate of the loss. The sentencing judge is in a unique position to assess the evidence and estimate the loss based upon that evidence. For this reason, the court’s loss determination is entitled to appropriate deference.

§ 2B1.1, comment. (n.3(C)). This Court follows the teaching of the Application Note that loss amounts need not be determined precisely. *Hammond*, 201 F.3d at 350 (“For the purpose of subsection (b)(1) of USSG § 2B1.1, the loss need not be determined with precision.”); *United States v. Sowels*, 998 F.2d 249, 251 (5th Cir. 1993) (“The district court need not determine the loss with precision.”).

The PSR originally fixed the loss amount at \$4,606,396. (PSR ¶ 39.) After hearing evidence at the sentencing hearing, the district court ruled that the proper loss amount was \$16,000,000. (Supp. Sent. Tr. at 56.)

Phipps centers his entire argument around application note 3(E)(1). (Phipps’s Brief at 22.) That application note directs that the loss shall be reduced by:

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.

USSG § 2B1.1, comment. (n.3(E)(1)).

At the sentencing hearing, the government presented the testimony of Special Agent Arceli Lagos, the case agent in charge of the Phipps investigation. (Supp. Sent. Tr. at 37-51.) Agent Lagos told the court that all of the information she was presenting came directly from a computer database kept by Phipps where

he recorded the activities of his fraudulent schemes. *Id.* at 38. Based on those records, Lagos told the district court she was able to determine that of the approximately 30,689 people who participated in Phipps's various programs, approximately 27,048 lost a total of \$16,215,882. (*Id.* at 42-43.) After hearing the testimony, the district court adopted that amount as its final loss determination and used it to fix Phipps's final offense level. (*Id.* at 55.)

Phipps neither objected on the grounds that he raises here nor offered any evidence as to the value of the tapes and educational materials he now suggests the court should have considered. Without such evidence, the district court not only had no reason to consider such a reduction, but even if it did consider it, had absolutely no basis on which to determine its amount.

Of even more direct consequence is the fact that the district court invoked the provisions of USSG § 2B1.1(b)(1)(K) which covers the broad range of losses from \$7,000,000 to \$20,000,000. Phipps would thus need to demonstrate that he was entitled to a reduction of \$9,215,882 before his loss amount would change his offense level.¹⁴ The record contains absolutely no evidence which would support any such conclusion. There was no error – and certainly no plain error – in the

¹⁴\$16,215,882 - \$7,000,000 = \$9,215,882.

calculation of Phipps's loss amount. There is no reason for this court to set aside the district court's sentence.

CONCLUSION

The judgment of the district court should be affirmed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that paper and electronic copies of this Brief were mailed to Weston C. Loegering and David Horan, Jones Day, 2727 N. Harwood Street, Dallas, Texas 75201, this 5th day of June, 2009.

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CERTIFICATE OF COMPLIANCE

Pursuant to FED. R. APP. P. 32(a)(7)(C), I certify that this brief complies with the type-volume limitations of FED. R. APP. P. 32(a)(7)(B).

1. Exclusive of the exempted portions in FED. R. APP. P. 32(a)(7)(B)(iii), the brief contains 12,002 words of text in proportionally spaced typeface.
2. The brief has been prepared in the Times New Roman typeface using WordPerfect X3. Text is in 14 point type and footnotes are in 12 point type.
3. I provided an electronic version of the brief to the court as well as to appellants' counsel.
4. I understand a material misrepresentation in completing this certification, or circumvention of the type-volume limits in FED. R. APP. P. 32(a)(7)(b), may result in the court's striking the brief and imposing sanctions against me.

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