

**No. 08-10831**

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IN THE UNITED STATES COURT OF APPEALS  
FOR THE FIFTH CIRCUIT

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UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

JAMES RAY PHIPPS,

Defendant-Appellant.

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

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**BRIEF OF APPELLANT JAMES RAY PHIPPS**

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## **CERTIFICATE OF INTERESTED PERSONS**

*United States of America v. James Ray Phipps*, No. 08-10831

The undersigned counsel of record certifies that the following listed persons and entities as described in the fourth sentence of 5th Cir. Rule 28.2.1 have an interest in the outcome of this case. These representations are made in order that the judges of this Court may evaluate possible disqualification or recusal.

1. James Ray Phipps, Defendant-Appellant.
2. Weston C. Loegering, Richard C. Rosalez, and David L. Horan, Jones Day, appointed counsel on appeal and at sentencing for Defendant-Appellant.
3. Carlton C. McLarty and Sam Ogan, Federal Public Defender's Office, Northern District of Texas, former appointed trial counsel for Defendant-Appellant.
4. United States of America, Plaintiff-Appellee.
5. Richard B. Roper, James T. Jacks, Susan B. Cowger, Stephen Booker, Robert A. Kemins, United States Attorney's Office, Northern District of Texas, counsel for Plaintiff-Appellee.

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David L. Horan

## **STATEMENT REGARDING ORAL ARGUMENT**

Appellant requests oral argument. This appeal presents issues regarding sufficiency of the evidence on several counts of conviction following a jury trial. Argument from counsel will likely assist the Court in resolving these issues.

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## **JURISDICTIONAL STATEMENT**

This is a direct appeal from a final judgment of the District Court in a criminal case. The District Court had jurisdiction over the action under 18 U.S.C. § 3231. This Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 1291.

Appellant James Ray Phipps filed a timely notice of appeal on August 18, 2008, R. 1096 [RE 2], from the District Court's August 20, 2008 final judgment of conviction and sentence, which judgment was amended on November 10, 2008, RE 6.<sup>1</sup> *See* FED. R. APP. P. 4(b).

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<sup>1</sup> Citations to the record on appeal that is consecutively paginated as "USCA5" will be denoted herein as "R." Citations to the Transcript of the Jury Trial will be denoted herein as "Trial Tr. Volume:Page" Citations to the Transcript of the Sentencing Hearing on August 12, 2008 will be denoted herein as "8/12/08 Tr." Citations to the probations officer's Presentence Report will be denoted herein as "PSR." References to the Record Excerpts will be denoted as "RE."

## **STATEMENT OF THE ISSUES**

1. Whether Phipps's conviction of mail and wire fraud should be reversed where the evidence at trial was legally insufficient to support a finding that Phipps acted with the specific intent to commit fraud.

2. Whether Phipps's conviction of wire fraud should be reversed where the evidence at trial was legally insufficient to connect the "wire" to any alleged fraud.

3. Whether Phipps's conviction of corrupt impediment of due administration of the internal revenue laws should be reversed where the evidence at trial was legally insufficient and was partially composed of Phipps's protected speech.

4. Whether Phipps's conviction of tax evasion should be reversed where the evidence at trial was legally insufficient to support a finding that Phipps acted willfully to evade federal income tax.

5. Whether the District Court's within-Guidelines sentence should be vacated and remanded for resentencing where the District Court improperly calculated the sentence by failing to reduce Phipps's loss amount by the value of the materials received by participants in his programs.

## **STATEMENT OF THE CASE**

This is a direct appeal from a final judgment in a criminal case.

Appellant James Ray Phipps (“Phipps”) was named in a 21-count indictment filed in the Northern District of Texas, Dallas Division, on April 12, 2006. R. 153 [RE 3]. Counts 1 through 3 charged Phipps with mail fraud and aiding and abetting, in violation of 18 U.S.C. §§ 1341 and 2. R. 161 [RE 3]. Count 4 charged Phipps with wire fraud and aiding and abetting, in violation of 18 U.S.C. §§ 1343 and 2. R. 162 [RE 3]. Counts 5 through 17 charged Phipps with money laundering and aiding and abetting, in violation of 18 U.S.C. §§ 1956(a)(1)(A)(i) and 2. R. 163-167 [RE 3]. Count 18 charged Phipps with corruptly endeavoring to obstruct and impede the due administration of the internal revenue laws, in violation of 26 U.S.C. § 7212(a). R. 168 [RE 3]. Counts 19 through 21 charged Phipps with income tax evasion, in violation of 26 U.S.C. § 7201. R. 174-176 [RE 3].

Phipps was subsequently named in a superseding indictment filed on July 12, 2006. R. 153 [RE 3]. The superseding indictment included the original 21 counts and added Count 22—forfeiture—in accordance with 18 U.S.C. §§ 981(a)(1)(C) and 982 (a)(1) and 28 U.S.C. § 2461. R. 177 [RE 3].

Phipps’s jury trial began on April 23, 2007. R. 14 [RE 1]. Counts 5 and 6 (alleging money laundering) were dismissed by the government’s oral motion during trial. Trial Tr. VII:51 [RE 8]. On May 4, 2007, the jury found Phipps

guilty of Counts 1 through 4 and 7 through 21 of the superseding indictment. R. 652-53 [RE 4].

The District Court subsequently granted a motion for judgment of acquittal as to counts 7 through 17 alleging money laundering, based on the Supreme Court's decision in *United States v. Santos*, 128 S. Ct. 2020 (2008), which was issued after the jury's verdict. R. 1117 [RE 5]. The District Court denied Phipps's motion for acquittal on the remaining counts and entered a final amended judgment on November 10, 2008. Final Amended Judgment 1 [RE 6].

The District Court sentenced Phipps to a within-Guidelines sentence of 210-months imprisonment (210 months on each of Counts 1 through 4 and 22 months on each of Counts 18-21, to be served concurrently), to be followed by a three-year term of supervised release. Final Amended Judgment 3-4 [RE 6]. The court also ordered Phipps to pay \$1,402,446.00 in restitution. Final Amended Judgment 6 [RE 6].

## **STATEMENT OF THE FACTS**

For over twenty years, Phipps has operated various educational programs dedicated to teaching others how to eliminate their debt and live within their means. Trial Tr. III:55 [RE 8]. While Phipps generally refrained from giving explicit, specific financial direction, he encouraged participants to study the educational materials that he provided them, apply his general financial teachings, and share their newfound knowledge with others. Trial Tr. VII:64-65 [RE 8].

In 1996, Phipps established Life Without Debt (the “Program”). Trial Tr. III:34 [RE 8]. Under the Program, participants paid an enrollment fee and received various financial education materials. Trial Tr. VII:62-63 [RE 8]. These materials espoused Phipps’s beliefs on staying out of debt by avoiding bank accounts, credit cards, and loans for cars and real property. Trial Tr. VII:82-84 [RE 8]. As a means of encouraging his students to share Phipps’s teachings, participants in the Program received a monetary incentive for each new person they introduced to the Program. VII:65-66 [RE 8]. Participants also received an incentive when those they introduced to it, in turn, introduced it to others who also enrolled. Trial Tr. VII:97 [RE 8]. These incentives were referred to as the “downline” and, as might be expected, resulted in the active recruitment of new participants. Trial Tr. VII:99 [RE 8]. Although the costs of enrollment ranged from a \$200 per month program

up to a \$100,000 per year program, the entry level program cost \$2,000 per year. PSR 4; Trial Tr. II:207 [RE 8].

After two decades of efforts to challenge Phipps' practices, the Internal Revenue Service (the "IRS") arrested Phipps in April of 2006. PSR 1-2. Phipps was subsequently indicted and, after a two-week jury trial, convicted in May of 2007. PSR 2. In August of 2008, the District Court granted a judgment of acquittal on the money laundering counts, which composed 11 of the 19 total counts. R. 1117 [RE 5]. District Judge Lynn subsequently sentenced Phipps to a total of 210 months imprisonment, followed by three years of supervised release. Final Amended Judgment 3-4 [RE 6].

The District Court entered judgment on the sentence. Final Amended Judgment 1 [RE 6]. This appeal followed.

## SUMMARY OF THE ARGUMENT

The government failed to present evidence of specific intent sufficient to support guilty verdicts on the mail and wire fraud counts. All of the representations that Phipps made to participants regarding the Program were true. Each representation was accompanied by disclosures of the work necessary to profit from the program and accurately described the method of payment used in the program. This included the representations that Phipps made regarding the prospects of financial gain under the Program, all of which Phipps couched in appropriate disclaimers and disclosures regarding the work required to realize the potential profit.

The government also did not present sufficient evidence of wire fraud within the meaning of 18 U.S.C. § 1343. The only “wire” that the government attempted to prove for the purposes of establishing wire fraud was a single fax sent *from* a program participant. That fax is not adequately connected to any alleged fraud by Phipps and is not sufficient evidence to support a wire fraud conviction.

The government also failed to present legally sufficient evidence to support a conviction on the corrupt impediment of due administration of the internal revenue laws count. The government presented three categories of evidence to support this charge: (1) Phipps encouraged other people not to pay their taxes; (2) Phipps operated on a cash-only basis, without bank accounts or credit cards;

and (3) Phipps sent complaint letters to the IRS and other government offices. The first category of evidence consists of protected speech under the First Amendment, and the remaining evidence is insufficient to support Phipps's conviction.

The government likewise failed to present sufficient evidence of tax evasion. Phipps had a good-faith belief that he did not owe income tax on the funds he received from program participants. He understood that the funds were contributions to a political and educational organization and thereby tax exempt. The evidence at trial supported the existence and sincerity of Phipps's good-faith beliefs, and the government did not rebut it. Phipps's good-faith belief negated the willfulness element of the tax evasion count.

Finally, even if the Court were to determine that there is sufficient evidence to support Phipps's convictions, the District Court improperly calculated the amount of loss used for sentencing Phipps by not accounting for the value of the materials and services that the Program participants received. Because the incorrect loss amount was a plain error and indisputably affected the selection of Phipps's sentence, the sentence must be vacated and remanded for resentencing.

## **ARGUMENT**

### **I. Standard of Review**

The standard of review for a challenge to the sufficiency of the evidence is “*de novo* without deference to the district court.” *United States v. Sterling*, \_\_\_F.3d

\_\_\_, 2009 WL 89639, \*3 (5th Cir. Jan 15, 2009). In reviewing the sufficiency of the evidence, this Court will reverse a conviction unless it determines that “a rational trier of fact could have found that the evidence established the essential elements of the offense beyond a reasonable doubt.” *United States v. Westbrook*, 119 F.3d 1176, 1189 (5th Cir. 1997) (citations omitted). In reaching that determination, the Court considers “all the evidence and reasonable inferences drawn therefrom in a light most favorable to the verdict.” *United States v. Harris*, 420 F.3d 467, 470 (5th Cir. 2005) (internal quotation marks omitted).

This Court reviews an improperly calculated guidelines sentence not objected to at trial or during sentencing for plain error. A showing of plain error requires (1) an error, (2) that is clear or obvious, and (3) that affected Phipps’s substantial rights (*i.e.* “affected the outcome of the district court proceedings”). *United States v. Cotton*, 535 U.S. 625, 631-32 (2002). If those conditions are met, this Court may reverse the error to preserve the “fairness, integrity, or public reputation of judicial proceedings.” *Id.* at 631 (internal quotations and citations omitted); *see also United States v. Baker*, 538 F.3d 324, 333 (5th Cir. 2008).

## **II. The Government Failed To Present Sufficient Evidence That Phipps Acted With The Specific Intent To Commit Fraud Under 18 U.S.C. §§ 1341 and 1343.**

Phipps was convicted of mail and wire fraud pursuant to 18 U.S.C. §§ 1341 and 1343. The elements of the statutes are parallel except that wire fraud requires

use of an interstate telephone call or electronic communication. *United States v. Mills*, 199 F.3d 184, 188 (5th Cir. 1999) (noting that “[t]he Supreme Court has said that because the mail and wire fraud statutes share the same language in relevant part, the same analysis applies to each”) (citing *Carpenter v. United States*, 484 U.S. 19, 25 n.6 (1987)); *see also United States v. Keller*, 14 F.3d 1051, 1056 (5th Cir. 1994) (describing elements). Mail and wire fraud are both specific-intent crimes that require the government to prove that a defendant knew the scheme involved false representations. *See United States v. Brown*, 459 F.3d 509, 518-19 (5th Cir. 2006) (wire fraud); *United States v. Rochester*, 898 F.2d 971, 976 (5th Cir. 1990) (mail fraud); *see also United States v. Bieganowski*, 313 F.3d 264, 275 (5th Cir. 2002) (mail fraud requires “the specific intent to defraud”); *United States v. Mann*, 493 F.3d 484, 493 (5th Cir. 2007) (“Violation of the wire-fraud statute requires the specific intent to defraud, i.e., a conscious knowing intent to defraud.”). In this context, “specific intent” has been defined as “a conscious knowing intent to defraud.” *Brown*, 459 F.3d at 519; *see also United States v. Blocker*, 104 F.3d 720, 732 (5th Cir. 1997) (a defendant acts with the intent to defraud when he “acts knowingly with the specific intent to deceive for the purpose of causing pecuniary ‘loss to another or bringing about some financial gain to himself.’”) (quoting *United States v. Jimenez*, 77 F.3d 95, 97 (5th Cir. 1996)).

The evidence presented at trial was insufficient to show that Phipps had a conscious, knowing intent to defraud. Rather than proving Phipps intended to defraud anyone, the evidence presented at trial instead overwhelmingly demonstrated the transparency of Phipps's educational endeavors and the sincerity of his efforts to educate participants about his financial philosophies. Trial Tr. VII:85 [RE 8]. Whenever Phipps made any representations regarding the Program and the financial incentives that it contained, he made sure that the information he communicated was accurate and clearly disclosed the work necessary in order to profit from the Program. Trial Tr. VII:116-17 [RE 8]. Moreover, Phipps accurately described the method of incentive payout used in the Program: The information sent to potential participants contained a graphical representation of the Program upline and downline payout structure. Trial Tr. VII:66 [RE 8]. These representations were true and accurate, and the government presented no evidence otherwise. When Phipps alluded to the potential for financial gain by participation in the Program, he took care to spell about all steps and criteria necessary to realize that potential profit. Trial Tr. VII:198 [R 8]. And indeed, while the hallmark of fraud is pecuniary loss, *Blocker*, 104 F.3d 720, 732, the government presented no evidence that Phipps failed to pay the promised incentives to anyone (or intended or planned to fail to do so) until the IRS seized the money and computers from him and disabled his operations. Trial Tr. VII:31-32 [RE 8]. In short, the government

failed to supply legally sufficient evidence that Phipps acted with the specific intent to defraud the Program participants.

### **III. The Government Failed To Present Sufficient Evidence That Phipps Committed Wire Fraud Under 18 U.S.C. § 1343.**

The wire fraud conviction also must be reversed because the wire was only tangentially related to the alleged fraud. “Wire fraud is (1) the formation of a scheme or artifice to defraud, and (2) use of the wires *in furtherance* of the scheme.” *Mann*, 493 F.3d at 493 (internal quotation marks omitted) (emphasis added). To sustain a conviction for wire fraud, “the government must present evidence that shows a link between the fraudulent activity and the [wire] at issue which demonstrates that the [wire] either ‘advanced or [was] integral to the fraud.’” *United States v. Strong*, 371 F.3d 225, 230 (5th Cir. 2004) (affirming judgment of acquittal for insufficiency of evidence) (quoting *United States v. Vontsteen*, 872 F.2d 626, 629 (5th Cir. 1989)). A wire is an “integral” part of a scheme to defraud if the completion of the scheme is dependant on the information contained in the wire. *United States v. Blankenship*, 746 F.2d 233, 241-42 (5th Cir. 1984) (information passed by wire must be “an integral part of execution of the scheme”). In other words, a wire that was not essential to the fraud cannot be the basis for a wire fraud conviction.

The lone “wire” upon which the government rested this count was a single fax sent by a Program participant to Phipps, informing him about her new address.

Trial Tr. III:130 [RE 8]. This single fax sent by a Program participant in no way advanced or was integral to the alleged fraud. Trial Tr. III:129 [RE 8]. In fact, the District Court requested additional briefing on this issue at the end of trial because the fax presented as the sole evidence of this charge was not fraudulent. Trial Tr. VII:54-55 [RE 8]. This evidence failed, as a matter of law, to establish the requisite connection between the wire and the fraud for three reasons.

First, the single wire at issue did nothing to advance Phipps's alleged fraudulent scheme because the wire did not lead to additional fraud. The government offered no evidence at trial that the fax induced additional individuals to join the Program or that it encouraged the participant who sent it to remain a member for longer than she otherwise would have. After all, the fax was sent *by* the participant *to* Phipps. Trial Tr. III:130 [RE 8]. Instead, the government only speculated in its response to Phipps's motion for new trial that the listed fax number on the Program materials that the participant received created the illusion of satisfactory customer service that induced the participant into a higher-level Program. R. 753 [RE 7]. Although the participant who sent the fax later joined another program, she never testified that the fax played any role in that decision. Trial Tr. III:151 [RE 8]. There simply was no connection between the fax and alleged fraud in evidence. The government did not offer any evidence whatsoever to support its conclusion that the fax led to additional fraud.

The fax that was the sole basis for the wire fraud charge was also not an integral part of the Program insofar as that term is understood by this Circuit. *Blankenship*, 746 F.2d at 241-42. If the participant at issue had not sent her fax to Phipps, but instead withdrew from the Program, there is no evidence that that would have had any effect on the Program. Therefore, this fax cannot support the wire fraud conviction.

The government's evidence is also insufficient because the wire fraud statute does not apply to the use of wires after a fraud has been fully consummated. *See United States v. Henderson*, 425 F.2d 134, 141 (5th Cir. 1970). Here, the participant who sent the fax was already an enrolled member of the Program. Trial Tr. III:129 [RE 8]. Thus, under the government's theory of the case, she had already been defrauded by the time she sent the fax. *United States v. Evans*, 148 F.3d 477, 483 (5th Cir. 1998) (holding mailing requirement of mail fraud was not satisfied because fraud was complete each time supervisor approved vouchers which were later mailed). The use of a fax by a participant of the Program after she has already joined cannot support a guilty verdict for wire fraud.

Finally, the government offered no evidence that Phipps intended this medium of communication to be used in the execution of his allegedly fraudulent scheme. As the United States Supreme Court has recognized in the related mail fraud context, "the relevant question at all times is whether the mailing is part of

the execution of the scheme to defraud as conceived by the perpetrator at the time.” *Schmuck v. United States*, 489 U.S. 705, 715 (1989). Phipps did not intend for the wires to serve a primary or significant role in the Program’s communications with members. He relied almost entirely upon traditional mail to operate the Program. Trial Tr. III:258-60 [RE 8].

#### **IV. The Government Failed To Present Sufficient Evidence of Corrupt Impediment Under 26 U.S.C. § 7212.**

Phipps was convicted under 26 U.S.C. § 7212(a)’s “omnibus” provision, which punishes a wide variety of conduct that impedes government operations. *United States v. Popkin*, 943 F.2d 1535, 1540 (11th Cir. 1991). In order to prove this charge, the government needed to show that Phipps: (1) engaged in some act; (2) intending to make it more difficult to administer the Internal Revenue laws; and (3) acted with the intent to unlawfully benefit himself, or cause someone else to unlawfully benefit. *United States v. Reeves*, 752 F.2d 995, 1001-02 (5th Cir. 1985). The evidence presented at trial was not sufficient to prove elements (2) and (3). The judgment on the guilty verdict on the corruptly impeding due administration of the internal revenue laws count must be reversed because most of the supporting evidence consists of protected speech, and the remaining evidence is insufficient to support a guilty verdict.

**A. *Phipps's Communications With Current And Potential Program Participants About The Tax Laws Are Protected Speech Under The First Amendment.***

The first category of evidence that the government presented to support the charge was that Phipps encouraged other people not to pay their income taxes. He shared with his students, in conference calls, at seminars, and in the Program materials that are sent out to participants, his own personal beliefs regarding the illegality of income taxes. Trial Tr. II:204-05 [RE 8]. In the absence of imminent illegal conduct, however, even outright advocacy of lawless activity—which Phipps did not engage in—is protected speech, *see Brandenburg v. Ohio*, 395 U.S. 444 (1969), and Phipps's advocacy of tax evasion was protected by the First Amendment.

The advocacy of illegal behavior regarding tax laws is only punishable if it is accompanied by *imminent* lawless activity. *Id.* at 447. Cases finding such activity invariably involve *specific* instructions on tax avoidance, directly followed by someone following those instructions. *See, e.g., United States v. Moss*, 604 F.2d 569 (8th Cir. 1979) (anti-tax advocate gave specific instructions on avoiding withholding that directly led to the filing of false W-2 forms); *United States v. Kelley*, 864 F.2d 569 (7th Cir. 1989) (promoter of illegal tax shelter directly caused filing of false tax returns); *United States v. Buttorff*, 572 F.2d 619 (8th Cir. 1978)

(tax protestor meeting where defendants gave specific instructions on filling out false W-2 forms and provided forms at the meeting).

While Phipps advocated against the federal income tax and sincerely believed it was invalid, he never instructed anyone on how to avoid their taxes, and the government offered no evidence showing that anyone avoided taxes due to Phipps's advocacy. Trial Tr. VII:119 [RE 8]. To the contrary, Phipps repeatedly advised students and others to consult a CPA or a lawyer about their tax liability and reminded them that he was not a tax advisor. *See, e.g.*, Trial Tr. III:187 [RE 8]; VII:123-24. [RE 8]. In the absence of imminent illegal activity, therefore, it would be unconstitutional to use the advocacy evidence to convict Phipps.

**B. *Phipps's "Cash-Only Lifestyle" And Letters To The Government Are Not Sufficient To Support A Conviction Under 26 U.S.C. § 7212.***

Phipps's First-Amendment-protected speech was the cornerstone of the 26 U.S.C § 7212 charge, as confirmed by the complete irrelevance of the government's other evidence. In short, the remaining evidence supporting the section 7212 count is wholly insufficient by any standard. Phipps's use of cash instead of bank accounts and credits cards and his habit of writing letters to government agencies do not support a guilty verdict on the section 7212 count.

There is no support for government's theory that operating without credit cards and bank accounts is enough—without evidence of intent—to convict Phipps

under section 7212. In fact, given the current credit crisis gripping the country, such practices are increasingly common. *See, e.g.* Kathryn Glass, *Banking on Cash: A Life Without Credit*, Fox Business, October 13, 2008, <http://www.foxbusiness.com/story/personal-finance/on-topic/debt/banking-cash-life-credit>. Congress enacted 26 U.S.C. § 7212 to punish “threats or threatening acts against agents of the IRS ... or members of the families of such persons, on account of the performance by such agents ... of their official duties,” House Report No. 1337 (1954), *reprinted in* 1954 U.S.C.C.A.N. 4574, not to target legitimate, but financially cautious, lifestyles. Indeed, cases involving this statute describe behavior drastically different from that exhibited by Phipps. *See, e.g., United States v. Saldana*, 427 F.3d 298 (5th Cir. 2005) (filing false form 8300s against IRS agents); *United States v. Allison*, 264 Fed. Appx. 450 (5th Cir. 2008) (same); *United States v. Reeves*, 752 F.2d 995 (5th Cir. 1985) (filing false liens against IRS agents); *United States v. Yagow*, 953 F.2d 423 (8th Cir. 1992) (sending false bills to individual IRS agents and filing false IRS forms against those agents); *United States v. Rosnow, et al.*, 977 F.2d 399 (8th Cir. 1992) (bringing false tort claims against IRS agents). No case has shown that someone may be punished under section 7212 for merely operating without credit cards or bank accounts or for writing protest letters to government agencies. Indeed, such a scenario is a far cry from the purpose of the statute.

The government presented no evidence at trial showing that Phipps's resistance to bank accounts and credit cards was borne out of a desire to interfere with an IRS agent's investigation. Instead Phipps's behavior is wholly consistent with the financial practices he advocated for more than 10 years. Trial Tr. VII:111-12 [RE 8]. He openly advocated a cash-based lifestyle in his Program materials as a way to avoid debt. Trial Tr. VII:123 [RE 8]. His cash flow was painstakingly documented by the computer program Phipps used to run the Program, and there was no evidence that he hid this information from the IRS. Trial Tr. IV:72 [RE 8]. There never has been and likely never will be any law requiring people to use credit cards or hold bank accounts. Similarly, there is no law that prohibits a person from running an all-cash business, so long as it complies with other relevant laws. Evidence that Phipps's personal and business finances were run on a cash-only basis is insufficient, without more, to show that Phipps endeavored to impede the tax code.

There was also no evidence that the letters Phipps sent to the IRS delayed the IRS's investigation of Phipps or were intended to do so. To the contrary, a review of the letters themselves suggests that Phipps's intent was to evaluate the tax consequences of the Program and to persuade members of government that he was not a United States citizen. *See, e.g.* Trial Tr. III:48-49, 238-40 [RE 8]. Phipps frequently sent letters to government offices and participants of the

Program; the IRS was not the only recipient. Trial Tr. III:47-49 [RE 8].

Additionally, one of the IRS agents who testified at trial stated that letters of the type sent by Phipps were very common at the IRS and were routinely thrown away. Trial Tr. VII:19 [RE 8]. This falls far short of the standard of “intending to impede an IRS investigation” that the government was required to prove.

**V. The Government Failed To Present Sufficient Evidence To Rebut Phipps’s Sincere, Good-Faith Belief That He Did Not Owe Income Tax, Thereby Negating The “Willfulness” Element of 26 U.S.C. § 7201.**

Congress specifically added the “willfulness” element to certain federal criminal tax offenses because it is difficult for the average citizen, like Phipps, to understand the extent of his duties under the complex and wide-ranging tax laws. *See Cheek v. United States*, 498 U.S. 192, 199-200 (1991). As a result, a person should not “become a criminal by his mere failure to measure up to the prescribed standard of conduct.” *United States v. Murdock*, 290 U.S. 389, 396 (1933). Phipps did not intend for his conduct to be illegal, and any violation of the tax laws by him was due to an innocent mistake that does not fulfill the specific intent required under the law.

Phipps lacked the willfulness required for conviction for tax evasion because he honestly believed that the cash receipts from the Program did not constitute income that needed to be reported to the IRS. As used in the Internal Revenue Code, the term “willful” means a voluntary, intentional violation of a known legal

duty. *Cheek*, 498 U.S. at 201. A good-faith misunderstanding of the law or a good-faith belief that one is not violating the law negates willfulness, whether or not the claimed belief or misunderstanding is objectively reasonable. *Id.* at 202. The evidence presented at Phipps's trial can only support the conclusion that he did not pay his income taxes because he believed that his income from the Program was not taxable.

Participants of the Program who personally knew Phipps testified at trial that he appeared sincere in all his beliefs about income tax. *See, e.g.*, Trial Tr. VII:71, 85, 115 [RE 8]. Their testimony was supported by Phipps's statements in conference calls played at trial and in literature sent to participants that the Program payments were non-taxable. Trial Tr. V:97 [RE 8]. He also misunderstood important aspects of the tax code and sent letters to the IRS stating these misunderstandings and seeking guidance. Trial Tr. III:236-37 [RE 8]. These letters about the non-taxability of his income, which were described in trial testimony, went unanswered. Trial Tr. VII:19-20 [RE 8].

The only evidence the government offered at trial to rebut the good-faith defense was that Phipps had been advised that he could obtain free tax advice at the Southern Methodist University Law School and that he structured his assets in a trust. Trial Tr. VII:38 [RE 8]. His refusal to seek out advice, however, does not make any tax violation willful, so long as he did not voluntarily and intentionally

violate a *known duty* to pay his taxes. *See United States v. Bishop*, 412 U.S. 346, 360 (1973) (“willfully” in tax statutes “connotes a voluntary, intentional violation of a known legal duty”). Although he secured his assets in a trust, he was not charged with structuring, and there was no evidence presented that he intended this trust to serve a tax evasion purpose. Trial Tr. VI:135 [RE 8]. He did not have a legal duty to structure his assets in a different way, and therefore he could not have been intentionally violating a known legal duty.

**VI. The District Court Improperly Calculated Its Guidelines Sentence By Incorrectly Determining Phipps’s Loss Amount.**

**A. *The Trial Court Did Not Reduce Phipps’s Loss Amount By The Value Of The Materials Received By the Program Participants.***

Finally, even if the Court were to determine that there is sufficient evidence to support Phipps’s convictions, the District Court erred by not reducing the amount of loss used for Phipps’s sentencing by the value of the educational materials and services the Program participants received. The Sentencing Guidelines unambiguously state that the amount of “loss *shall* be reduced by ... the fair market value of the ... services rendered, by the defendant ... to the victim before the offense was detected.” U.S. SENTENCING GUIDELINES MANUAL (“U.S.S.G.”) § 2B1.1 cmt. 3(E)(i) (2006) (emphasis added). The failure to do so is an improper application of the Guidelines. *United States v. Klein*, 543 F.3d 206, 215 (5th Cir. 2008).

Several of the program participants testified at trial that the books, audiotapes, and other educational materials they received as Program participants were valuable to them. Trial Tr. VII: 64, 84, 112-13 [RE 8]. The actual loss used to calculate the Guidelines sentence must be discounted by the value of these educational materials. *Klein*, 543 F.3d at 214. There is nothing in the Presentence Report or the record to suggest that the District Court made any attempt to estimate the fair market value of these materials and use it to reduce the loss amount Phipps was sentenced under. This was a miscalculation of Phipps's sentence that was clearly in violation of the requirements shown under both the Guidelines and *Klein*.

**B. *The District Court's Sentence Was Based On An Improper Guidelines Calculation And Must Be Vacated.***

Phipps's sentence was based on a \$16 million amount of loss, which resulted in a 20-level increase in his offense level and a Guidelines sentence range of 188 to 235 months. 8/12/08 Tr. 33-34, 55 [RE 9]; U.S.S.G. § 2B1.1(b). The District Court erred by calculating this loss amount without discounting for the value of Phipps's educational materials, as the District Court was required to do as the sole finder of fact during sentencing. The error substantially affected Phipps's rights if it was prejudicial, *United States v. Olano*, 507 U.S. 725, 732-33 (1993), and the error was prejudicial if there is a reasonable probability that, but for the error, Phipps would have received a lesser sentence, *United States v. Villegas*, 404 F.3d 355, 364 (5th Cir. 2005).

The District Court's sentence is prejudicial because it is clearly a Guidelines sentence resulting from an incorrect calculation of Phipps's amount of loss. The next-lowest loss amount under the guidelines results in an 18-level increase in offense level and a sentencing range of 151 to 188 months. U.S.S.G. §§ 2B1.1(b) (2006); SENTENCING TABLE (2006). Because the District Court did not discount Phipps's loss amount by the value of the materials sent to the Program participants, there is a reasonable probability that a correct calculation of his sentence would have resulted in a shorter sentence. If the court correctly calculated the loss amount and it resulted in this lower sentencing range, Phipps's sentence of 210 months would have exceeded the Guidelines. *Id.* at SENTENCING TABLE. This Court cannot make the factual determinations necessary to calculate the correct loss amount. *See Sabah Shipyards Sdn. Bhd. v. M/V Harbel Tapper*, 178 F.3d 400, 410 n.12 (5th Cir. 1999) (appellate court cannot make factual calculations); *Silberblatt, Inc. v. United States*, 353 F.2d 545, 550 (5th Cir. 1965) (“[i]t is not the province of this court to determine the essential facts on which the judgment is based”); *Bay Sound Trans. Co. v. United States*, 410 F.2d 505, 512 (5th Cir. 1969) (appellate court cannot make findings of fact when District Court fails to do so). That duty fell solely to the District Court, and its failure to do so creates a reasonable probability that Phipps received a longer sentence, substantially interfering with his rights.

Additionally, this Court has repeatedly held that “sentencing error ‘seriously affects the fairness, integrity, or public reputation of judicial proceedings’” if it “‘clearly affected [the] defendant’s sentence.’” See *United States v. Price*, 516 F.3d 285, 290 (5th Cir. 2008) (quoting *United States v. Perez*, 484 F.3d 735, 744 (5th Cir. 2007)); *Villegas*, 404 F.3d at 365 (an erroneously imposed sentence enhancement under the Guidelines affects a defendant’s sentence and therefore affects the fairness and integrity of the judicial proceeding); *United States v. Garza-Lopez*, 410 F.3d 268, 275 (5th Cir. 2005); *United States v. Aderholt*, 87 F.3d 740, 744 (5th Cir. 1996) (sentencing calculation errors affect the fairness and integrity of the proceedings). The District Court’s calculation error in sentencing Phipps here did so and therefore affected the fairness and integrity of the proceedings, and his sentence must be remanded for resentencing by the District Court.

### **CONCLUSION**

The Court should reverse Phipps’s conviction on each count, vacate his sentence, and remand for entry of a judgment of acquittal or resentencing. Even if the Court were to determine that there is sufficient evidence to support Phipps’s convictions, Phipps’s sentence must be vacated and remanded for resentencing.

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**CERTIFICATE OF SERVICE**

I hereby certify that on February 19, 2009, an original and six true and correct copies of the foregoing Brief of Appellant and a computer diskette with a copy of the foregoing Brief of Appellant in Portable Document File (PDF) format were filed via Federal Express with the Clerk of Court, and two true and correct copies and a diskette with a copy in PDF format were served via Federal Express upon:

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## CERTIFICATE OF COMPLIANCE

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 5,689 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).
  
2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft<sup>®</sup> Office Word 2003 in 14-point font Times New Roman type (with the exception of footnotes, which pursuant to Local Rule 32.1, are in a proportionally spaced typeface in 12 point Times Roman).

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Dated: February 19, 2009

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