The Danger of Being Under Oath

What the Bankruptcy Attorney Needs to Know About Financial Crimes

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INTRODUCTION

Two federal criminal statutes apply specifically to bankruptcy fraud, but the government has at its disposal several other criminal statutes that are less restrictive, more powerful, or easier to prove.

Thus, while the bankruptcy practitioner must be familiar with the bankruptcy fraud statutes, he or she should also be aware of these other statutes, and make sure the client understands that when the certification is made under oath, there is no turning back.

BANKRUPTCY CRIME STATUTES

The crimes specifically connected to actions or conduct in relation to a bankruptcy filing or proceeding can be found at 18 U.S.C. § 152. They include:

- knowingly and fraudulently concealing any property belonging to the estate of a debtor;
- knowingly and fraudulently making a false oath or account;
- knowingly and fraudulently presenting any false claim for proof against the estate of the debtor;
- knowingly and fraudulently receiving any property from a debtor with intent to

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defeat the provisions of the bankruptcy laws.

- after the filing of a bankruptcy petition, knowingly and fraudulently concealing, destroying, withholding or falsifying any records relating to the property or financial affairs of the debtor.

Convictions under this statute carry a maximum penalty of 5 years' imprisonment. In 1994, Congress added the Bankruptcy Fraud statute, 18 U.S.C. § 157. This statute mirrors the robust mail fraud, wire fraud and bank fraud statutes found at 18 U.S.C. 1341, 1343 and 1344 respectively. Arguably, it added little to the federal criminal code, since the underlying offense conduct could already have been charged under one of the aforementioned statutes.

In fact, § 157 has a limiting clause that prosecutors don't like: it requires that the defendant has filed for bankruptcy, filed a document in the bankruptcy proceeding, or made a false representation *"for the purpose of executing or concealing"* the scheme or artifice to defraud. This additional essential element to prove the offense has driven prosecutors away: the annotations to the statute show that there have been very few appellate cases in the 20-year history of the statute.[1]

In January of 2000, a federal District Court in Pennsylvania dismissed a charge of bankruptcy fraud under § 157, narrowly construing the statute's scope. *United States v. Lee*, 82 F.Supp.2d 384 (E.D. Pa. 2000). The Court, after noting its surprise that there were no reported cases construing § 157, found that a filing made during the bankruptcy proceedings by the defendant was made *subsequent* to allegedly fraudulent payments made to defendant's wife, and could not therefore have "executed" the already completed scheme. *Id.* at 388. The Court further

[1] 18 U.S.C. § 157 carries a maximum penalty of five years' imprisonment, while the mail and wire fraud statutes carry 20-year maximums, and bank fraud carries a 30-year maximum term of imprisonment.

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found that the lack of disclosure in the filing of the payments to defendant's wife leads to civil liability, not criminal. *Id.* At 388-89. In other words, the Court refused to criminalize an omission.

With this type of precedent, and with the more powerful general fraud statutes available, it is not surprising that prosecutors have not often relied on § 157. And most reported cases of bankruptcy fraud convictions include a combination of other crimes, such as tax evasion or filing false tax returns, mail and wire fraud, etc. When the government can prove more serious crimes more easily, it does not need to prove the more complicated crime. In addition, the government has trended toward using the defendant's own statements against him, or his attempts at a cover-up, to prove even more simple crimes.

FALSE STATEMENTS AND OBSTRUCTION

While federal prosecutors still mainly use the three aforementioned mail, wire and bank fraud statutes to prosecute financial crimes, in recent years there seems to be increasing use of other "process crime" statutes, such as Making False Statement under 18 U.S.C. § 1001, Perjury under 18 U.S.C. § 1621 *et seq*, and Obstruction of Criminal Investigations under 18 U.S.C. § 1510.

The False Statement statute is the most sweeping. It reads as follows:

> a) Except as otherwise provided in this section, whoever, in any matter within the jurisdiction of the executive, legislative, or judicial branch of the Government of the United States, knowingly and willfully--(1) falsifies, conceals, or covers up by any trick, scheme, or device a material fact;
>
> (2) makes any materially false, fictitious, or fraudulent statement or representation; or
>
> (3) makes or uses any false writing or document knowing the same to contain any materially false, fictitious, or fraudulent statement or entry;
>
> shall be fined under this title, imprisoned not more than 5 years . . . . .

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THE PROBLEM OF INCONSISTENT STATEMENTS

When a client comes into a criminal defense lawyer's office because there is an investigation (or an indictment) of him for conduct somehow related to a bankruptcy case, the client is usually in one of three situations:

(1) he is stone-cold innocent;

(2) the alleged fraud is already completed, and the client filed bankruptcy protection because he still went broke; or

(3) the client filed for the bankruptcy thinking that it might help hide the fraud, or end the episode.

Under either of the latter two scenarios, the filing of the bankruptcy case entails the great risk that the client has now created two inherently conflicting statements that cannot both be true.

Although we tend to think the only time a citizen speaks under oath is in a courtroom, there are a surprising number of instances in which people must sign documents under penalty of perjury. Some examples are:

- Insurance claim, such as theft of jewelry
- Standard FHA Home Loan Application
- HUD-1 Real Estate Closing Statement
- Student Loan Application
- Credit Card Application
- Financial Statement, especially in divorce or child custody litigation

In some cases, the false statement has already been made in a prior event, such as listing assets not actually owned, or over-valuing assets on a home-loan application. When the person

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filing bankruptcy states the truth on his petition, he is exposing himself to investigation for bank fraud concerning obtaining the home loan, for example. Federal law enforcement agents and prosecutors love this type of evidence: two statements under oath by the defendant, both of which cannot be true.

Furthermore, if there is a prior inconsistent statement somewhere, it is highly likely that federal investigators will find it and find it quickly. The combination of aggressive administrative or grand jury subpoenas and increasing electronic storage of financial records by businesses and agencies means that what used to take weeks or months is now being found by investigators in days or hours.

This situation presents a real quandary for the client, and a difficult task for his bankruptcy lawyer, if the problem is divulged to or discovered by the lawyer. The lawyer of course can only recommend the client tell the truth, or decline to file the bankruptcy petition. The client needs to understand that the consequence of being convicted of such a crime is often imprisonment.

INCARCERATION IS LIKELY UNDER THE FEDERAL SENTENCING GUIDELINES

The Internal Revenue Service recently published data showing that in 2015, 63% of the bankruptcy fraud cases that its Criminal Investigation Division prosecuted (and resolved) ended up in a sentence of imprisonment, with the average of those sentences being 16 months.[2]

[2] See https://www.irs.gov/uac/statistical-data-bankruptcy-fraud .

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Three reasons make it likely that a person convicted of a federal financial crime (whether related to bankruptcy or not) is likely to get a significant sentence of imprisonment. First, the federal sentencing guidelines are tough. Second, federal prosecutors and law enforcement agents usually only focus on frauds involving hundreds of thousands of dollars, so if they go after your client, he will surely be in an incarceration range under the guidelines. Third, financial crimes are the "new drug crimes," in that the momentum is toward more and more punishment.

The federal sentencing guidelines use a table under which the suggested term of imprisonment is governed by the combination of a person's prior criminal history, and the severity of the offense.

The guideline calculation has essentially three parts: (1) a Base Offense Level, which is a minimum starting point indicating the severity of the basic criminal conduct at issue; (2) an adjustment for monetary amount, which increases the offense level the more money is involved; and (3) Specific Offense Characteristics, which further increase the offense level for various dastardly methods used to achieve the crime.

A guideline calculation might look like this:

6 Base offense level for bankruptcy fraud, § 2B1.1(a)(1)

+ 10 Intended monetary loss amount > $150,000 but less than $250,000. § 2B1.1(b)(1)(F)

+ 2 Specific offense characteristic: if the offense involved a misrepresentation or other fraudulent action during the course of a bankruptcy proceeding. § 2B1.1(b)(8)(B)

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+2 Obstruction Adjustment: if the defendant willfully obstructed or impeded the investigation, prosecution or sentencing.[3] § 3C1.1

20 Adjusted Offense Level Subtotal

- 3 Acceptance of responsibility and full disclosure to government, § 3E1.1.

17 Final Offense Level

If a person has no prior record, then the Sentencing Guideline Range of offense level 17 and criminal history category I is 24 - 30 months' imprisonment. While the sentencing guidelines are now just advisory, after the Supreme Court case of *United States v. Booker*, 543 U.S. 220 (2005), the judges in our district still tend to follow relatively closely to the ranges.

One important concept to understand about the sentenced guidelines in federal financial crimes is "intended loss". The guideline calculations made are not limited to using the *actual* loss incurred, but rather the loss that was *intended* by the defendant or his actions.[4] For example, if a person filing for bankruptcy intentionally withholds from his bankruptcy petition an asset worth $151,100, even if the bankruptcy trustee finds the asset before resolution of the case, under the federal sentencing guidelines, the damage has been done. Because the defendant intended to hide the asset, that figure is used in calculating his guideline range even though no actual loss has been incurred by the creditors. *See* § 2B1.1, Application Note 3.

[3] Under Application Note 7(E)(ii) of the Sentencing Guidelines, the obstruction of justice enhancement will not apply "if the conduct that forms the basis for the [+2 bankruptcy proceeding] enhancement is the only conduct that forms the basis for the [obstruction] enhancement."

[4] Furthermore, in the unusual case where the actual loss is greater than the intended loss, the actual loss is used. *See* § 2B1.1, Application Note 3(A).

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CONCLUSION

The various statements that are required to be made under oath by the debtor during a bankruptcy proceeding can serve as either the predicate false statement, or an inconsistent statement that makes a prior statement appear false. Given the serious potential for a sentence of imprisonment in any federal fraud case, clients who are considering filing for bankruptcy should be clearly advised that false statements during the proceedings could result in criminal charges, and truthful statements could expose prior false statements or fraudulent activity.

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