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EXPERT ANALYSIS

Clarifying the Bank Fraud Statute: 'Because That's Where the Money Is'

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Sixty-five years ago Slick Willie Sutton, a career criminal who spent half his life incarcerated despite three successful escapes, reportedly told a newspaperman that the reason he robbed banks was, "Because that's where the money is." The U.S. Supreme Court heard oral argument Oct. 4 in *Shaw v. United States* (No. 15-5991) to resolve the elements of the first clause of the bank fraud statute, 18 U.S.C.A. § 1344, concerning intent.

Under clause (1), the government must prove that a defendant defrauded a financial institution, but to do so is it also required to prove the defendant intended to obtain the bank's own property, as opposed to the property of a customer? In other words, does a clause (1) violation require evidence of a defendant's intent to harm a financial institution?

There is no doubt Lawrence Shaw committed bank fraud. Like Slick Willie Sutton, he admitted it. Shaw was charged and convicted under 18 U.S.C.A. § 1344(1) of the bank fraud statute. However, he argued that clause (1) does not apply to his conduct. Instead, he said he should have been charged pursuant to 18 U.S.C.A. § 1344(2).

THE CONDUCT OF LAWRENCE SHAW

Shaw devised and implemented a scheme to obtain Stanley Hsu's money. Hsu lived in Taiwan, and he had his Bank of America account statements mailed to a home, where Shaw resided, in the United States.

Shaw intercepted Hsu's bank statements and opened a PayPal account in Hsu's name. Shaw linked the PayPal account to Hsu's BofA account. He also opened accounts in his father's name at another bank and linked some of those accounts to the PayPal account. PayPal flagged this as suspicious activity, but Shaw convinced PayPal that he was Hsu by providing falsified documents.

Shaw siphoned money from Hsu's BofA account through outgoing transfers to the PayPal account and then used the PayPal account to make purchases. Shaw also moved money from the PayPal account into the accounts in Shaw's father's name. Ultimately, Shaw used the money for his own benefit. By the time the scheme was discovered, Shaw had transferred more than $300,000 from Hsu's BofA account to the PayPal account.

Once the fraud was reported, the compromised BofA account was closed. BofA then reversed 16 of the 39 unauthorized transfers, which totaled $132,503 based on a 60-day window within which certain unauthorized transfers could be reversed. PayPal was required to reimburse BofA for the reversed transfers.

Importantly, BofA suffered no financial loss. PayPal suffered a net loss of $107,836 (the $132,503 reimbursed to BofA minus the $24,667 remaining in the PayPal account), and Hsu suffered a loss of nearly $175,000.

ENACTMENT OF THE BANK FRAUD STATUTE

The federal bank fraud statute, 18 U.S.C.A. § 1344, criminalizes two kinds of schemes. It provides:

Whoever knowingly executes, or attempts to execute, a scheme or artifice—

> (1) to defraud a financial institution; or
>
> (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises; shall be fined not more than $1,000,000 or imprisoned not more than 30 years, or both.

The statute was signed into law Oct. 12, 1984. Congress enacted it in the wake of three U.S. Supreme Court decisions that exposed significant gaps in the statutes used to prosecute bank fraud.[1] These three cases are:

- *United States v. Maze,* 414 U.S. 395 (1974), affirmed the reversal of a conviction for mail fraud. *Maze* concerned a defendant who stole a third party's credit card, which was then used to make purchases. To satisfy the mailing requirement, the government relied on post-purchase mailings between the merchants and the bank that issued the credit card. *Maze* held that the merchants, the bank that issued the credit card, and the credit card owner were all victims, but that the mailing element of the statute was not satisfied because the mailings were made after the fraud was completed and were "directed to the end of adjusting accounts between the [victims]."[2]

Lawrence Shaw admitted he was involved in a scheme, but he said it was not bank fraud because the bank was not his intended victim.

- *Williams v. United States,* 458 U.S. 279 (1982), concerned false statements made for the purpose of defrauding a bank. The defendant initiated a check-kiting scheme (utilizing the period of time it takes to process checks to make use of non-existent funds in a bank account). While check kiting is directed at misleading banks, *Williams* held that a check is not a factual assertion and therefore cannot be considered a false statement.[3]

- *Bell v. United States,* 462 U.S. 356 (1983), affirmed a conviction for bank larceny based on a scheme where the defendant opened an account with false identification, deposited a stolen and altered check, and then withdrew the deposited funds. The conviction was upheld because the conduct involved "a taking and carrying away" of the property. Thus, it also held attempts would not satisfy the statute.[4]

These decisions made clear that there were criminal schemes that targeted banks and yet were not covered by any existing federal statute. Congress responded by enacting 18 U.S.C.A. § 1344.

The two clauses of Section 1344 are distinct but overlapping. Clause (1) covers schemes to defraud financial institutions, such as the check-kiting scheme in *Williams,* while clause (2) concerns the use of false statements to induce a bank to part with money in its control, such as the schemes utilized in *Maze* and *Bell.*

FALSE STATEMENTS UNDER CLAUSE (2)

In 2014 the U.S. Supreme Court analyzed clause (2) of the bank fraud statute in *Loughrin v. United States,* 134 S. Ct. 2384 (2014). The defendant in that case, Kevin Loughrin, executed a scheme to convert altered checks into cash by presenting them to the retail merchant Target. The trial court held that appellate court precedent precluded a conviction under clause (1) of the bank fraud statute, but it permitted the case to proceed to the jury under clause (2).

The jury instructions provided that Loughrin could be found guilty "if, in offering the fraudulent checks to Target, he had 'knowingly executed or attempted to execute a scheme or artifice to obtain money or property from the [banks on which the checks were drawn] by means of false or fraudulent pretenses, representations, or promises.'"[5]

Loughrin requested an instruction that would require the jury to find that he intended "to defraud a financial institution."[6] The requested instruction was denied, and Loughrin was convicted.

The conviction was upheld on appeal since clause (2) of the bank fraud statute requires that the defendant intend to obtain property "owned by, or under the custody or control of, a financial institution" and that the intended result occur "by means of false or fraudulent pretenses, representations, or promises."[7]

The case reached the U.S. Supreme Court, which determined that clause (2) of the bank fraud statute focuses "on the scheme's goal (obtaining bank property) and, second, on the scheme's means (a false representation)." Accordingly, it said, "nothing in the clause additionally demands that a defendant have a specific intent to deceive a bank."

Loughrin also noted that the suggested construction of clause (2) was "more untenable in light of the rest of the bank fraud statute. That is because the *first* clause of Section 1344, as all agree, includes the requirement that a defendant intend to 'defraud a financial institution'; indeed, that is Section 1344(1)'s whole sum and substance."

Loughrin held under clause (2) there was no requirement of an intent to defraud a financial institution because that was the crime covered by clause (1).

ELEMENTS OF CLAUSE (1)

Shaw was convicted on multiple counts of bank fraud under clause (1) of the statute and sentenced to 57 months' imprisonment. Through his counsel, Shaw admitted he was involved in a scheme. But he said the scheme did not constitute bank fraud as Hsu, not BofA, was the intended victim.

Both the trial court and the 9th U.S. Circuit Court of Appeals concluded that the government was not required to prove that a defendant intended for a financial institution to lose money or property as a result of the Section 1344(1) bank fraud scheme, and that proof of an intent to deceive or cheat the financial institution alone was sufficient for conviction. Several federal appellate courts have held that an intent to obtain something of value from the financial institution (i.e., the bank is the victim in that it was subject to a risk of financial loss) is an element of a Section 1344(1) violation.

The oral argument in Shaw sharpened the parties' arguments and the potential trail the Supreme Court may blaze as to the elements of a Section 1344(1) bank fraud violation.

SHAW'S SUPREME COURT ARGUMENT

Shaw argued to the U.S. Supreme Court that "to defraud a financial institution" under clause (1) of the bank fraud statute requires proof of an intent to deceive and cheat a financial institution, and that the defendant's objective in devising the scheme must be the intent to obtain property owned by the financial institution.[8]

Shaw relied upon precedent establishing that "defraud" means wronging a victim in his property rights by deceit. Since the term "defraud" is immediately followed by "a financial institution," the clear text of clause (1) requires an intent to wrong the victim financial institution in its property right by deceiving it. Thus, Shaw asserted, the financial institution, not its customer, must be the intended victim.

To further support this argument, Shaw relied on the existence of the separate clause (2) of the bank fraud statute. Clause (2) distinguishes schemes that target a financial institution from those that target customer, bank-held property by containing explicit language that the clause applies to both schemes to obtain property "owned by" a financial institution and property "in the custody or control of" a financial institution. Only when a scheme to obtain bank-owned property through false statements exists can that scheme be prosecuted under both clauses (1) and (2).

Shaw also took issue with the jury instructions explaining that "'scheme to defraud' means any deliberate plan of action or course of conduct by which someone intends to deceive, cheat *or* deprive a financial institution of something of value" and "intent to defraud" was defined as "intent to deceive *or* cheat." Therefore, he argued, because the instruction was phrased in the disjunctive, a jury could convict based merely on an intent to deceive or cheat a financial institution even if the goal of the scheme was not to obtain something of value.[9]

THE GOVERNMENT'S ARGUMENT

The government argued that Section 1344(1) prohibits the knowing execution of a scheme to defraud a financial institution of a property interest by deceiving the entity. Therefore, the government argued prosecution for a clause (1) violation is not limited to schemes that deprive a financial institution of an ownership interest or monetary loss.

The government contended that Shaw's interpretation of clause (1) schemes to those whose objective is to deprive the financial institution of its own property was too limited. Accordingly, the government argued a scheme to defraud a financial institution is a scheme to deprive a victim financial institution of a property interest, including both ownership and possessory interests. Thus, according to the government, clause (1) covers schemes to defraud a financial institution that target property held by the financial institution, through ownership or on behalf of a customer.

Financial institutions hold a property interest in their customer's funds. A property interest includes a possessory interest in something of value. When a customer's funds are stolen, the financial institution is deprived of its possessory interest in those funds. Shaw's taking of Hsu's property deprived the bank of something of value; its possessory interest in Hsu's funds. Despite the language differences between clauses (1) and (2), there is no language to suggest that clause (1) only concerns property owned by the financial institution.

A defendant's belief as to who the scheme will harm does not control whether clause (1) applies. The government argued that the textual language "to defraud a financial institution" clearly does not include an intent-to-harm requirement. The required mental state is to deceive, not to harm.

Furthermore, the government pointed out that language proposed during the enactment of Section 1344(1) that would have required a plan to obtain bank property or to cause economic loss to the bank by fraudulent means was rejected.[10] An intent-to-harm requirement would be difficult to establish because it would rest heavily on a defendant's knowledge of banking laws.

The government also addressed the "scheme to defraud" jury instruction, contending that the instruction correctly conveyed the elements of a Section 1334(1) violation. The instruction on "scheme to defraud" was defined as any deliberate plan of action or course of conduct "by which someone intends to deceive, cheat *or* deprive a financial institution of something of value."

The government argued that the phrase uses a "financial institution" as the direct object of all three verbs — deceive, cheat and deprive — and therefore the prepositional phrase "of something of value" applied to each verb independently. Thus, the jury instruction required a finding the scheme intended to "deceive" the bank out of "something of value," "cheat" the bank out of "something of value," or "deprive" the bank of "something of value."

ORAL ARGUMENT BEFORE THE SUPREME COURT

The oral argument in *Shaw* sharpened the parties' arguments and the potential trail the Supreme Court may blaze as to the elements of a Section 1344(1) bank fraud violation. Multiple justices questioned the type of property interest the financial institution must be deprived of to establish a clause (1) violation.

The questions suggest that the harm to the financial institution was not to the bank itself, but rather to the bank's property interest. That interest was much broader than the classic ownership interest. It included possessory interests or even a bailment interest.

Importantly, the justices' questions suggested the harm or deprivation did not have to equate to an actual loss or risk of loss to the financial institution itself.

Justice Elena Kagan illustrated this point when she posed the following question to the government's counsel:

> If somebody went in (a financial institution) and said, I'd like to see the security deposit boxes, and made a false statement to the bank about his entitlement to see the security deposit boxes and took the money out? .... Doesn't — you know, the bank still have a possessory interest in that, even though it doesn't use that money in the same way; is that correct?[11]

So long as there was evidence of an intent to deceive a financial institution and the financial institution was deprived of a possessory interest, regardless of who actually owned the property, that may be sufficient for purposes of Section 1344(1).

The oral argument also considered the propriety of the jury instructions. The instructions defined a "scheme to defraud" as "any deliberate plan of action or course of conduct by which someone intends *to deceive, cheat, or deprive a financial institution of something of value*."[12]

Chief Justice John G. Roberts explained the issue is whether "deceive" and "cheat" stand alone, or whether they were modified by "of something of value." He noted that the government's brief argued that "of something of value" modified "deceive" and "cheat," but added in language that did not appear in the actual jury instructions. He concluded that deceive of something of value, and cheat of something of value makes no sense, so the brief supplied the words "out of."[13]

Accordingly, Justice Kagan read the instruction such that "deceive a bank" was operating as a disjunctive clause without the "of something of value." The instruction on scheme to defraud suggested that it would be sufficient to convict if there was evidence that the financial institution was simply deceived.

This interpretation of the instruction was further supported, according to Chief Justice Roberts, by the appellate court's statement that the defendant "was guilty of bank fraud because he intended to deceive the bank."

The questions during oral argument suggest that the court is likely to conclude that the elements of a clause (1) bank fraud offense require an intent to obtain something of value from the financial institution by deception, but that the something of value need only be a property right, such as a limited, temporary right of possession. The jury instruction at issue should have required that "scheme to defraud" be defined as any deliberate plan of action or course of conduct by which someone intends to deceive a bank out of something of value, cheat a bank out of something of value or deprive it of something of value.

Such an instruction would make clear that the intent required is more than just an intent to deceive a financial institution. Instead, it is also an intent to obtain something of value from the financial institution as a result of that deceit.

LIKELY OUTCOME IN *SHAW*

The high court's decision in *Shaw* will likely conclude that the elements of a Section 1334(1) violation require proof of the knowing execution of a scheme to defraud a financial institution out of a property interest through deceit. Whether the financial institution suffers a loss or even a risk of loss will be immaterial so long as a property interest of the bank, ownership or possessory, is impacted.

While the decision in *Shaw* may prove most significant to the individual defendant, there will be little if any impact on future bank fraud schemes subject to federal prosecution. Even Shaw's counsel conceded that Shaw's conduct met the elements of a Section 1334(2) violation. *Shaw* and *Loughrin* will stand as the essential cases setting forth the elements of the bank fraud offense — an offense that carries stiffer penalties and a longer limitations period than those applicable to federal mail and wire fraud offenses.

NOTES

1 S. Rep. No. 98-225, at 377-378 & n.3 (1983).

2 *United States v. Maze,* 414 U.S. 395, 402 (1974).

3 *Williams v. United States,* 458 U.S. 279, 284-285 (1982).

4 *Bell v. United States,* 462 U.S. 356, 361 (1983).

5 *Loughrin v. United States,* 134 S. Ct. 2384, 2388 (2014) (quoting App. 7).

6 Petition for Writ of Certiorari at 4, *Loughrin v. United States,* 134 S. Ct. 2384 (2013) (No. 13-316), 2013 WL 4855971 at *5.

7 *Loughrin*, 134 S. Ct. at 2389.

8 Brief for Petitioner at 9, *Shaw v. United States* (No. 15-5991), 2016 WL 3548945 at *9.

9 *Id.* at 22

10 Brief of United States at 41, *Shaw v. United States* (No. 15-5991), 2016 WL 4375377 at 25.

11 Transcript of Oral Argument at 51, *Shaw v. United States* (No. 15-5991), 2016 WL 5852131 at *51.

12 Brief for Petitioner at 6, *Shaw v. United States* (No. 15-5991), 2016 WL 3548945 at *6 (emphasis added).

13 Transcript of Oral Argument at 37, *Shaw v. United States* (No. 15-5991), 2016 WL 5852131 at *37.

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