RECOGNIZING "DELIBERATE IGNORANCE"

AS A FORM OF KNOWLEDGE IN

CUSTOMS FRAUD CASES

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by

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I. Introduction

On April 5, 2006, the Court of International Trade issued a final judgment against an importer of tracksuits from China, Thomas Man Chung Tao, awarding the United States $1,844,284.78, as well as interest in the amount of $1,791,115.37, to compensate for losses in revenue stemming from Mr. Tao's illegal importation of merchandise by means of falsified entry documents prepared by Mr. Tao's broker. See United States v. Pan Pacific Textile Group, Inc., Slip. op. 06-18 (CIT Jan. 31, 2006) (accepting the Government's calculation and fixing defendants' liability for unpaid duties, plus interest as provided by law).

This judgment established the amounts owing to the Government based upon a previous decision, United States v. Pan Pacific Textile Group, Inc., 395 F. Supp. 2d 1244, 1254-55 (CIT 2005) ("Pan Pacific"), in which the Court held that, among other things, the agency principle of imputation may be applied in actions brought pursuant to 19 U.S.C. § 1592 to establish an importer's liability for actions of a customs broker making entries on behalf of the importer. The Court reasoned that the purpose underlying imputation is "to protect innocent third parties or . . . to prevent principals from benefiting at the expense of innocent third parties." Id. (citing Bankers Life Ins. Co. of Neb. v. Scurlock Oil Co., 447 F.2d 997, 1005 (5th Cir. 1971)). The Court further noted that "the United States Court of Appeals for the Federal Circuit has previously indicated that, rather than force the government (as third party) to bear the loss resulting from unpaid duties, it is preferable to extend liability for unpaid duties to an innocent party who is nonetheless 'traditionally liable' for such payment. Id. (citing United States v. Blum, 858 F.2d 1566, 1570 (Fed. Cir. 1988) (footnote omitted). The Court concluded that "extending liability to defendants in this case achieves the public policy goals underlying both

traditional agency principles and the Blum court's reasoning." Id.

The Court also explained that the applicability of agency imputation principles is particularly appropriate in the context of Customs penalty cases:

> [T]he Court's holding in this case serves an additional public policy interest by creating proper incentives for importers in the future. If the Court were to allow defendants to immunize themselves from liability for customs violations by hiring a customs broker and transferring importer of record status, the Court would effectively create an incentive for bad behavior. Allowing such protection for importers would discourage care on their part in selecting their agents, and would thus provide more opportunity for dishonest middlemen such as [Tao's broker] Juang. Moreover, if importers could lower their costs through unlawful customs transactions without incurring any liability, they would be encouraged to seek brokers willing to commit fraud on their behalf (this case demonstrates that it is possible for both parties to benefit from such an arrangement). In the Court's view, the likely effect of denying liability in this case would be an increase in fraudulent customs transactions. Therefore, the Court concludes that extending liability to defendants for duties unpaid as a result of Juang's fraud is not only well supported by law, but also sound public policy. See TIE Communications, Inc. v. United States, 1994 WL 176918, 18 CIT 358, 366 (1994) (weighing public policy concerns to arrive at disposition in customs case).

Id.

As explained in greater detail below, the Government had also argued that the incontrovertible evidence demonstrated that Mr. Tao was apprised of highly suspicious irregularities in the manner in which his broker, Mr. Juang, entered the goods upon his behalf, the amounts he was paying, and the documentation that he was receiving. The Government further argued that, nevertheless, Mr. Tao chose not to inquire into the details or the mechanics of how Mr. Juang was in fact entering the goods, and that such admittedly deliberate ignorance is tantamount to knowledge as a matter of law. However, because the Court held that Mr. Juang's fraudulent acts, statements and omissions could be imputed to Mr. Tao as principal, the Court in

Pan Pacific did not reach the issue of whether Mr. Tao's admittedly deliberate ignorance regarding material facts surrounding the entry of his merchandise by his broker on his behalf would constitute "knowledge" of fraud as a matter of law. Id. at 1249 n.11.

This article summarizes the theory of deliberate ignorance as applied in the context of criminal and civil fraud cases and recommends its application to Customs fraud cases pursuant to section 1592, either through judicial recognition in a future case or amendment to the relevant regulation promulgated by the United States Customs and Border Protection ("Customs").

II. Relevant Statutory Scheme

A. Section 1592

To establish a violation of 19 U.S.C. § 1592, the Government must demonstrate that: (1) "'no person"; (2) "by fraud, gross negligence, or negligence"; (3) "may enter, introduce, or attempt to enter or introduce any merchandise into the commerce of the United States" (4) "by means of any document or electronically transmitted data or information, written or oral statement, or act which is material and false" or "any omission which is material." 19 U.S.C. § 1592(a)(1). Pursuant to the regulation, a violation of 19 U.S.C. § 1592 is fraudulent when "a material false statement, omission, or act in connection with the transaction was committed (or omitted) knowingly, i.e., was done voluntarily and intentionally, as established by clear and convincing evidence." 19 C.F.R. pt. 171 app. B(C)(3) (emphasis added). Thus, the regulation does not specifically require that the Government establish "actual knowledge" for purposes of penalty actions alleging fraud.

B. Standard Of Review

For claims alleging fraud, "the United States shall have the burden of proof to establish

the alleged violation by clear and convincing evidence." 19 U.S.C. § 1592(e)(2). "Although not susceptible to precise definition, 'clear and convincing' evidence has been described as evidence which produces in the mind of the trier of fact 'an abiding conviction that the truth of [the] factual contentions are "highly probable.'" Buildex Inc. v. Kason Industries, Inc., 849 F.2d 1461, 1463 (Fed. Cir. 1988) (quoting Colorado v. New Mexico, 467 U.S. 310, 316 (1984)).

The Government may establish deliberate ignorance by offering circumstantial evidence. "The record need not contain direct evidence . . . that the defendant deliberately avoided knowledge of wrongdoing; all that is necessary is evidence from which the jury could infer deliberate avoidance of knowledge." United States v. Whittington, 26 F.3d 456, 463 (4th Cir. 1994). In determining whether the evidence supports the charge, the evidence and all reasonable inferences that may be drawn from it are viewed in the light most favorable to the government. See United States v. Sharpe, 193 F.3d 852, 871 (5th Cir. 1999). "It is not required that the evidence supporting such an instruction be introduced by the government rather than by the defense." United States v. Bautista, 252 F.3d 141, 147 (2d Cir.2001).

III. The Application Of "Deliberate Ignorance" Theory To Establish Fraudulent Knowledge

A. The Theory Of "Deliberate Ignorance" Is Widely Accepted In Cases Involving Fraud In Other Contexts

1. Judicial Acceptance Of "Deliberate Ignorance" Theory Of Knowledge

The concept of deliberate ignorance (also referred to as "willful blindness" or "conscious avoidance") generally provides that "if [a defendant] has his suspicions aroused but then deliberately omits to make further enquiries, because he wishes to remain in ignorance, he is deemed to have knowledge." See, e.g., United States v. Prather, 205 F.3d 1265, 1270 (11th Cir.

2000) (quoting United States v. Rivera, 944 F.2d 1563, 1570 (11th Cir. 1991)).

Many circuit courts of appeal have generally recognized and applied the theory that, under certain circumstances, the knowledge element of a fraud statute may be proved by demonstrating deliberate ignorance. See, e.g., United States v. Epstein, 426 F.3d 431, 440-41 (1st Cir. 2005) (money laundering and mail fraud under 18 U.S.C. § 1341, in connection with scheme to defraud timeshare owners.); United States v. Wasserson, 418 F.3d 225, 237-39 (3d Cir. 2005) (improper disposal of hazardous waste, 42 U.S.C. § 6928(d)); United States v. Zedner, 401 F.3d 36, 50-51 (2d Cir. 2005) (bank fraud, 18 U.S.C. § 1344); United States v. Freeman, 434 F.3d 369, 377-78 (5th Cir. 2005) (wire fraud under 18 U.S.C. § 1343, travel fraud under 18 U.S.C. § 2314, and money laundering under 18 U.S.C. § 1957, in connection with defendant's operation of Ponzi scheme that involved telling investors that he would invest their funds in high yield programs or "private placement secured trading programs" involving overseas trades of financial instruments); United States v. Patient Transfer Service, Inc., 413 F.3d 734 (8th Cir. 2005) (false or fraudulent claims involving Medicare, in violation of 18 U.S.C. §§ 2 and 287, and false statements involving Medicaid, in violation of 42 U.S.C. § 1320a-7b.); United States v. Arias, 431 F.3d 1327, 1335 (11th Cir. 2005) (conspiracy to defraud Medicare, 18 U.S.C. § 371); United States v. Collins, 372 F.3d 629, 634 (4th Cir. 2004) (money laundering, 18 U.S.C. § 1956); United States v. Carney, 387 F.3d 436, 448-49 (6th Cir. 2004) (aiding and abetting the felonious utterance of knowingly false statements by customers in the defendants' firearms transfer records, 18 U.S.C. § 924, and felonious creation or maintenance of willful omissions and/or falsehoods in their firearms transaction records regarding the name, age, and place of residence of firearms purchasers, 18 U.S.C. § 922(b)(5)); United States v. Jaffe, 387 F.3d 677,

681 (7th Cir. 2004) (real estate attorney convicted for wire fraud under 18 U.S.C. § 1343 for financing purchase of a Chicago property with a fraudulently obtained mortgage loan of more than $60,000 for a property worth just $25,000); United States v. King, 351 F.3d 859, 866 (8th Cir. 2003) (conspiracy to violate the Foreign Corrupt Practices Act, 15 U.S.C. § 78dd-1(a), in connection with scheme to bribe Costa Rican officials to obtain valuable land concessions to aid land development project); United States v. Bieganowski, 313 F.3d 264 (5th Cir. 2002) (scheme to defraud medical-insurance companies in violation of, 18 U.S.C. § 1341 and 18 U.S.C. § 1956); United States v. Draves, 103 F.3d 1328 (7th Cir. 1997) (conviction for knowingly using or attempting to use a fraudulently obtained credit card in violation of 15 U.S.C. § 1644(a) and 18 U.S.C. § 2.); United States v. Bussey, 942 F.2d 1241, 1246 (8th Cir. 1991) (conviction for filing false tax returns in violation of 26 U.S.C. § 7206(1); failing to file tax return in violation of 26 U.S.C. § 7203; and filing false statement with Department of Housing and Urban Development in violation of 18 U.S.C. § 1001).

2. Codification Of Deliberate Ignorance Theory Under The False Claims Act

The definition of "knowledge" in fraud statutes may specifically include deliberate ignorance.

The False Claims Act ("FCA"), 31 U.S.C. § 3729(a), applies to false statements that are made knowingly. To establish fraud under the FCA, the Government must establish that: (1) a person presented a claim for payment or approval or to decrease an obligation owed to the Government; (2) at that time, the claim was false or fraudulent; and (3) the person acted knowingly. United States ex rel. A + Homecare, Inc. v. Medshares Mgmt. Group, Inc., 400 F.3d 428, 451 (6th Cir. 2005); see also 31 U.S.C. § 3729(a) (providing for liability under the FCA

where a defendant, among other things, "(1) knowingly presents, or causes to be presented, to an officer or employee of the United States Government or a member of the Armed Forces of the United States a false or fraudulent claim for payment or approval; (2) knowingly makes, uses, or causes to be made or used, a false record or statement to get a false or fraudulent claim paid or approved by the Government; . . . or (7) knowingly makes, uses, or causes to be made or used, a false record or statement to conceal, avoid, or decrease an obligation to pay or transmit money or property to the Government").

Pursuant to the 1986 amendments to the FCA, a "specific intent to defraud" would no longer be required to satisfy the *scienter* element. United States ex rel. Taylor v. Gabelli, 345 F. Supp. 2d 313 (S.D.N.Y 2004). "[I]n amending the Act in 1986, Congress explained that . . . its purpose in lowering the threshold was to impose upon individuals and contractors receiving public funds 'some duty to make a limited inquiry so as to be reasonably certain they are entitled to the money they seek,' and to 'preclude 'ostrich' type situations where an individual has 'buried his head in the sand' and failed to make any inquiry that would have revealed the false claim.'" Id. (quoting S.Rep. No. 99-345 at 20-21, reprinted in 1986 U.S.C.C.A.N. 5266, 5285)); see also U.S. v. Hercules, Inc., 929 F. Supp. 1418 (D. Utah 1996) (recognizing that 1986 amendments broadened liability under FCA). "The drafters were especially concerned about "corporate officers who insulate themselves from knowledge of false claims submitted by lower-level subordinates' and as such, drafted the new mens rea requirements to make it more difficult for these officers to avoid liability." Pamela H. Bucy, CIVIL PROSECUTION OF HEALTH CARE FRAUD, 30 Wake Forest L. Rev. 693 (1995) (citing S. Rep. No. 345, 99th Cong., 2d Sess. 7 (1986), reprinted in 1986 U.S.C.C.A.N. 5266, 5272).

Consequently, under the current version of the FCA, "knowingly" is defined as "actual knowledge of the information, or with deliberate ignorance or reckless disregard of the truth or falsity of the information." Medshares, 400 F.3d at 451. Specifically, the Government need only establish one of the following: "(1) [the defendant] has actual knowledge of the information; (2) [the defendant] acts in deliberate ignorance of the truth or falsity of the information; or (3) [the defendant] acts in reckless disregard of the truth or falsity of the information . . . ." 31 U.S.C. § 3729(b). Thus, for purposes of the FCA, "what constitutes the offense is not intent to deceive but knowing presentation of a claim that is either 'fraudulent' or simply 'false.'" United States ex rel. Hagood v. Sonoma County Water Agency, 929 F.2d 1416, 1421 (9th Cir.1991); see also Lamb Eng'g & Const. Co. v. United States, 58 Fed. Cl. 106 (2003) (holding government contractor liable under FCA where contractor acted knowingly, or in deliberate ignorance with reckless disregard of falsehoods, when it certified contrary to fact that all subcontractors had been paid).

B. Criteria Used In Determining The Applicability Of "Deliberate Ignorance" Theory

Courts have considered several criteria in determining whether the deliberate ignorance theory may be applied to establish knowledge for purposes of fraud. Courts have held that there is a proper factual basis for a "deliberate ignorance" jury instruction where the evidence supports inferences that: "(1) the defendant was subjectively aware of a high probability of the existence of illegal conduct; and (2) the defendant purposely contrived to avoid learning of the illegal conduct." United States v. Scott, 159 F.3d 916, 922 (5th Cir. 1998). Courts also consider whether the defendant derived a benefit from the fraudulent scheme.

1. The Government Must Typically Establish That The Defendant Was, At A Minimum, On Notice Of Facts Underlying Alleged Fraud

Several courts have found that fraud is proved where a principal is "on notice" of facts surrounding false statements. See, e.g., Stone v. Lawyers Title Ins. Corp., 554 S.W. 2d 183, 188 (Tex. 1977) (even though president of company had no actual knowledge of an easement, existence of memorandum disclosing easement put president of title agency "on notice;" misstatement was knowing and fraudulent). The deliberate ignorance instructions has been held appropriate where an employer contends that he the responsibility for the fraud rested solely with his employees and that he knew nothing of their wrong doing. For example, in United States v. Walker, 191 F.3d 326, 337 (2nd Cir. 1999), the Court of Appeals for the Second Circuit held that the instruction was proper where the employer-defendant, charged with making false statements to Immigration and Naturalization Service (INS), had "supervised his employees and occasionally reviewed their completed applications," he was "confronted . . . about a false story on [an] application," and he "instructed [an employee] to sign blank forms that later contained a false account of persecution." The Court concluded that "[t]his and other evidence easily supported the inference that even if Walker did not have direct knowledge of the crimes occurring in his office, he deliberately remained ignorant of them." Id.

Similarly, the court in Roadmaster Indus., Inc. v. Columbia Manufacturing Co., 892 F. Supp. 1162, 1176-78 (D. Mass. 1995), granted summary judgment despite defendant's offer to present evidence concerning subjective intent. The court reasoned that defendant had "knowledge" of false statement even though he lacked actual knowledge that a remediation of the property at issue would be needed. Id. The court reasoned that the defendant was "on notice" that remediation might be needed in light of old monitoring results and the fact that

defendant had knowledge of a pending inspection. Id.

Other courts have held that a plaintiff must present specific evidence that the defendant actually suspected possible criminal activity. See, e.g., United States v. Heredia, 429 F.3d 820, 824 (9th Cir.2005) ("[T]he instruction is 'rarely appropriate,' and should be given only when the government presents 'specific evidence' that the defendant '(1) actually suspected that he or she might be involved in criminal activity, (2) deliberately avoided taking steps to confirm or deny those suspicions, and (3) did so in order to provide himself or herself with a defense in the event of prosecution.'") (quoting United States v. Baron, 94 F.3d 1312, 1318 n.3 (9th Cir. 1996)). Similarly, the Court of Appeals for the Second Circuit has limited the use of the instruction to circumstances where the defendant was aware of a "high probability" of the fraudulent acts and "consciously avoided confirming that fact." United States v. Ferrarini, 219 F.3d 145, 154 (2d Cir. 2000) (quoting United States v. Rodriguez, 983 F.2d 455, 458 (2d Cir. 1993)).

The defendant's sophistication, experience, and education are relevant to determining whether the defendant was, or should have been, on notice of illegal activity. For example, the court in Campbell, 977 F.2d at 857, applied the deliberate ignorance in a money laundering case where the defendant was a licensed realtor who had conveyed to the sellers of real property a buyer's proposal to pay a substantial amount of cash under the table and lower the contract price accordingly. The amount of money and the nature of payment should have been a red flag to an experienced realtor of a possible illegality in the transaction. Id.

The defendant's proximity to the fraudulent actions are also relevant to determining whether a deliberate ignorance jury instruction is warranted. For example, the Court of Appeals for the Fifth Circuit in Freeman, 434 F.3d at 378, sustained a conviction for conspiracy, wire

fraud, travel fraud, and money laundering in connection with a Ponzi scheme. The appellate court held that trial court's deliberate indifference instruction was proper because, among other things, there was ample evidence that the defendant was subjectively aware of a high probability of the existence of illegal conduct, given his involvement in typing and witnessing bogus agreements with investor-victims. Id. See also Draves, 103 F.3d at 1333-34 (relying upon evidence of defendants close proximity to wrongdoing, close relationship with primary perpetrator, and a strange pattern of activity).

2. The Government Must Typically Establish That The Defendant Took Affirmative Steps To Avoid Learning The Truth Or Failed To Conduct An Investigation Notwithstanding Suspicious Circumstances

To warrant application of the "deliberate ignorance" theory, the evidence must indicate that the defendant took affirmative steps to avoid learning the truth. "A deliberate ignorance instruction is appropriate only when there is evidence in the record showing the defendant purposely contrived to avoid learning the truth." United States v. Stone, 9 F.3d 934, 937 (11th Cir.1993) (emphasis added); see also United States v. Espinoza, 244 F.3d 1234, 1242 (10th Cir.2001) (allowing "deliberate ignorance" instruction "'only when the prosecution presents evidence that the Defendant purposely contrived to avoid learning all the facts in order to have a defense in the event of a subsequent prosecution' ") (quoting United States v. Hanzlicek, 187 F.3d 1228, 1233 (10th Cir.1999)).

However, the signs of fraud may be so glaring that courts have held that it is sufficient that a defendant failed to conduct an adequate investigation. See, e.g., United States v. Faulkner, 17 F.3d 745, 766 (5th Cir.1994) ("We have held that in some cases the likelihood of criminal wrongdoing is so high, and the circumstance surrounding a defendant's activities and cohorts are

so suspicious, that a failure to conduct further inquiry or inspection can justify the inclusion of the deliberate ignorance instruction.") (citations omitted). See also United States v. Stouffer, 986 F.2d 916, 925 (5th Cir.1993) (holding that the deliberate indifference instruction was appropriate where corporate officer used investment company funds for personal purposes, "blindly accept[ing]" co-defendant's representation that the company's charter authorized the expenditures); United States v. Del Aguila-Reyes, 722 F.2d 155, 157 (5th Cir. 1983) ("From these suspicious facts, it was reasonable for the jury to infer that [the defendant] should have known that his trip to Miami was prompted for some additional, probably illegal, reason.").

The failure to conduct an adequate investigation is particularly relevant where a principal claims ignorance of an agent's fraudulent actions. In United States v. Leahy, 445 F.3d 634, 652 (3d Cir. 2006), a president of an auction company and his employee, a manager, were accused of selling repossessed vehicles at prices greater than amounts reported to the banks. The court allowed a deliberate ignorance instruction where the president had claimed ignorance of the employee's double billing scheme. Id. See also United States v. Gray, 105 F.3d 956, 967 (5th Cir.1997) (holding that the deliberate indifference instruction was warranted because defendant had first-hand information that loan applicants received no money, but failed to make an adequate inquiry as to any possible wrongdoing).

Accordingly, a deliberate ignorance instruction is warranted if: (1) the defendant denies knowledge of a specific fact required for conviction, and (2) there is evidence that the defendant was aware of a high probability of the disputed fact and deliberately avoided confirming that fact, for example, where his involvement may have been so *overwhelmingly suspicious* that his failure to question the suspicious circumstances establishes his purposeful contrivance to avoid

guilty knowledge. United States v. Svoboda, 347 F.3d 471, 480 (2d Cir. 2003) (quoting United States v. Lara-Velasquez, 919 F.2d 946, 952 (5th Cir. 1990) (internal quotations and citations omitted) (emphasis in original)), cert. denied, 541 U.S. 1044 (2004).

3. Courts Also Consider Whether The Defendant Derived Any Benefit From The Fraudulent Acts

To establish the applicability of deliberate ignorance theory, the Government may introduce evidence that the defendant had benefitted from the fraudulent acts. See Lowry v. SEC, 340 F.3d 501, 506 (8th Cir. 2003) (holding that defendant's spending investor funds on personal expenses establishes the requisite state of mind for committing securities fraud); SEC v. Infinity Group Co., 212 F.3d 180, 192 (3d Cir. 2000) (same). For example, the Court of Appeals for the Seventh Circuit applied the theory of deliberate ignorance in finding a bankruptcy attorney liable for securities fraud, in part because he benefitted from the illegal transactions. SEC v. Jakubowski, 150 F.3d 675, 678 (7th Cir. 1998). In Jakubowski, the Securities and Exchange Commission ("SEC") claimed that a bankruptcy attorney had made false statements of material fact in connection with the sale of securities in violation of Rule 10b-5, which has a scienter requirement of "knowledge." Specifically, the SEC alleged that the defendant had participated in violation of a regulation that: (1) prevents an individual from transferring ownership of conversion rights and (2) prevents the sale of any securities in excess of the maximum amount provided. Id. Mr. Jakubowski claimed that, while he may have been "careless," he was unaware of the regulations precluding such sales. Id. at 681. Mr. Jakubowski contended that he failed to read thoroughly the purchase forms, which stated that the stocks could not be resold. Id. Mr. Jakubowski also asserted that he performed a quick search on Lexis and was unable to find any cases prohibiting his actions. Id.

The court rejected Mr. Jakubowski's defense upon the grounds that: (1) he had failed to conduct an adequate investigation regarding or to inquire into the legality of the transactions; (2) he had been sufficiently aware that something was wrong with these transactions; and (3) he had derived a financial benefit from the transactions. Id. at 682. The court held that Mr. Jakubowksi was at the very least "deliberately ignorant" and that deliberate ignorance is a form of knowledge. Id. Accordingly, the court affirmed the lower court's decision to grant the SEC's motion for summary judgment. Id.

C. The Courts Have Cautioned Against Use Of The Deliberate Ignorance Instruction In Certain Circumstances

Many courts have expressed that "[c]aution is necessary in giving a willful blindness instruction." United States v. Cassiere, 4 F.3d 1006, 1023 (1st Cir. 1993); see also United States v. Mancuso, 42 F.3d 836, 846 (4th Cir. 1994) (indicating a "war[iness] of giving a willful blindness instruction"); United States v. Inv. Enters., Inc., 10 F.3d 263, 269 (5th Cir. 1993) (cautioning that instruction be given only "sparingly"). Other courts have cautioned that such an instruction is "rarely appropriate" or is only proper in "rare circumstances." Heredia, 429 F.3d at 824; United States v. de Francisco-Lopez, 939 F.2d 1405, 1409 (10th Cir.1991); United States v. Ruhe, 191 F.3d 376, 385 (4th Cir.1999); United States v. Mendoza-Medina, 346 F.3d 121, 132 (5th Cir.2003); United States v. Concha, 233 F.3d 1249, 1252 (10th Cir. 2000); Prather, 205 F.3d at 1270; United States v. Sanchez-Robles, 927 F.2d 1070, 1073 (9th Cir. 1991). Several circumstances are of particular concern: (1) where the defendant has not asserted a lack of knowledge; (2) where the Government alleges deliberate ignorance as well as actual knowledge; (3) where the instructions do not clearly distinguish deliberate ignorance from recklessness or negligence; and (4) where the statute requires that the plaintiff establish knowledge as to specific

facts.

1. Courts Typically Require That The Defendant Have Asserted A Lack Of Fraudulent Knowledge Before Allowing Application Of "Deliberate Ignorance" Theory

A willful blindness jury instruction is appropriate when the defendant asserts a lack of guilty knowledge, but the evidence supports an inference of deliberate ignorance. A plaintiff may rely upon "deliberate ignorance" theory where a defendant asserts that he was unaware of the allegedly fraudulent acts, statements or omissions despite the appearance that he possessed such knowledge. United States v. Hildebrand, 152 F.3d 756, 764 (8th Cir. 1998)). For example, the Court of Appeals for the Second Circuit recently held that a "conscious avoidance" charge was proper where, because the defendant "did not dispute that he took certain actions but denied having knowledge of their criminal nature, the defendant has put in issue whether the circumstances would have alerted him of the high probability that his actions were criminal and what steps he took to learn of the extent of that danger." United States v. Chu, Slip op., 2006 WL 1526922 (2nd Cir. 2006) (conspiracy to commit bank fraud, mail fraud, wire fraud, and money laundering, 18 U.S.C. §§ 371, 1341, 1343, 1344, 1956(h)). See also Ruhe, 191 F.3d at 384 ("A willful blindness instruction is proper when the defendant asserts a lack of guilty knowledge but the evidence supports an inference of 'deliberate ignorance' on defendant's part."); Sdoulam, 398 F.3d at 993.

Other courts have required that the defendant have asserted a lack of specific aspect of knowledge that is necessary to conviction. See Walker, 191 F.3d at 337 (holding that a deliberate ignorance jury instruction was warranted where a "defendant claims to lack some specific aspect of knowledge necessary to conviction" where the "evidence may be construed as

deliberate ignorance") (emphasis added).

2. Some Courts Have Cautioned Against Allowing A "Deliberate Ignorance" Instruction When The Government Also Alleges Actual Knowledge

Some courts have held have cautioned against the use of the "deliberate ignorance" instruction where the Government claims that the defendant had actual knowledge of the circumstances forming the basis of fraud. For example, the Court of Appeals for the Seventh Circuit has cautioned district courts "against instructing juries on deliberate ignorance when the evidence only points to either actual knowledge or no knowledge on the part of the defendant." United States v. Ndiaye, 434 F.3d 1270 (11th Cir. 2006) (quoting Stone, 9 F.3d at 937).

However, a court's decision to give an instruction regarding deliberate ignorance is subject to "harmless-error" review. Id. Thus, because juries are presumed to follow the judge's instructions, the error is harmless as a matter of law where (1) "the jury was clearly instructed that a precondition to its application of the deliberate ignorance instruction was proof beyond a reasonable doubt that [the defendant] deliberately kept himself ignorant," and (2) the evidence was sufficient to support a conviction based on actual knowledge, but not necessarily overwhelming. Id. at 937-39. See also United States v. Wells, 262 F.3d 455, 466 (5th Cir. 2001) ("[E]rror in giving the deliberate ignorance instruction is ··· harmless where there is substantial evidence of actual knowledge."); United States v. Whittington, 26 F.3d 456, 464 (4th Cir. 1994).

However, other courts have rejected the proposition that a "deliberate ignorance" jury instruction is not necessarily improper merely because the Government has also claimed that the defendant actually knew of the fraudulent acts, statements or omissions. See, e.g., United States v. Saucedo-Munoz, 307 F.3d 344, 349 (5th Cir. 2002) (noting that relevant cases do not

"suggest[ ] that a deliberate ignorance instruction is improper where evidence may be construed as showing either actual knowledge or contrivance to avoid learning the truth. Instead, [the] precedent suggests that a deliberate ignorance instruction may be given alongside evidence of actual knowledge."). In Patient Transfer Service, 413 F.3d at 742, the court held that, to establish that the defendant knowingly violated Medicare and Medicaid regulations by a double billing scheme, the Government could prove that the defendant either actually knew that the billing practice was improper or that the defendant deliberately avoided investigating whether it was improper. The court considered that "[t]he evidence indicates [that the defendant] had at least some knowledge of Medicare and Medicaid regulations," and that "[i]t could be inferred from the evidence that Wise had actual knowledge of what activity was reimbursable and how the claim forms should have been submitted or that he avoided learning more about proper billing." Id. (emphasis added). Thus, the Government should be able to plead "deliberate ignorance" in the alternative to actual knowledge provided that the evidence may support either inference and that the jury instructions are clear in this regard.

3. Some Courts Have Cautioned Against Allowing A "Deliberate Ignorance" Instruction When There May Be Possible Confusion With Recklessness Or Negligence

One of the dangers in applying the "deliberate ignorance" theory to fraud cases requiring a "knowing violation" is that the line between intentional violations and reckless or negligent violations may be blurred. Courts have held that a defendant acts with extreme recklessness if he "encountered 'red flags,' or 'suspicious events creating reasons for doubt' that should have alerted him to the improper conduct." Howard v. SEC, 376 F.3d 1136, 1143 (D.C. Cir. 2004) (quoting Graham v. SEC, 222 F.3d 994, 1006 (D.C. Cir. 2000)). However, the concept of "red

flags" that put a defendant upon notice of fraudulent activity has been used in the context of applying the "deliberate ignorance" theory to fraud cases. Epstein, 426 F.3d at 440 (applying the theory where "record evidence reveals 'flags' of suspicion that, uninvestigated, suggest willful blindness") (quoting United States v. Coviello, 225 F.3d 54, 70 (1st Cir.2000)). See also United States v. Craig, 178 F.3d 891, 898 (7th Cir. 1999) (affirming conviction based on willful blindness because defendant "saw and experienced enough suspicious activities to raise several red flags," which "supports an inference that she consciously chose not to pursue the truth"). This concern has engendered much criticism by commentators. See Charlow, R., WILFUL IGNORANCE AND CRIMINAL CULPABILITY, 70 Tex. L. Rev. 1351, 1382-90 (1992) (expressing concern that "most definitions of wilful ignorance delineate a mens rea that is the equivalent neither of knowledge nor recklessness"); Robbins, I.P., THE OSTRICH INSTRUCTION: DELIBERATE IGNORANCE AS A CRIMINAL MENS REA, 81 J. Crim. L. & Criminology 191, 220-27 (1990) (contending that the Model Penal Code "has merely renamed recklessness with respect to existing facts in order to reach the deliberately ignorant defendant").

This concern is heightened when courts recognize "reckless disregard" to satisfy the knowledge element in the context of securities fraud. See, e.g., In re Kidder Peabody Sec. Litig., 10 F. Supp. 2d 398, 415 (S.D.N.Y. 1998) ("[R]eckless disregard of the truth satisfies the scienter requirements of [the anti-fraud provisions] when the defendant deliberately failed to acquire the information that would have indicated to her that her statements were false or misleading.").

Courts are also "cognizant of the risk . . . that a deliberate ignorance instruction might lead the jury to employ a negligence standard and convict a defendant on the impermissible ground that he should have known an illegal act was taking place." King, 351 F.3d at 866

(citing United States v. Barnhart, 979 F.2d 647 651 (8th Cir. 1992)). Accordingly, courts of cautioned that, in evaluating the propriety of a deliberate ignorance instruction, "'[t]he evidence must establish that the defendant had subjective knowledge of the criminal behavior," and, thus, "[s]uch knowledge may not be evaluated under an objective, reasonable person test.'" United States v. Lee, 54 F.3d 1534, 1538-39 (10th Cir. 1995) (emphasis added).

Nevertheless, jury instructions may be carefully constructed to avoid any confusion in this regard. Pursuant to typical jury instructions regarding "deliberate ignorance," the word "knowingly" or the phrase "the defendant knew" signifies "that the defendant realized what she was doing and was aware of the nature of her conduct and did not act through ignorance, mistake or accident." Typical jury instructions read as follows:

> When the word "knowingly" or the phrase "the defendant knew" is used in these instructions, it means that the defendant realized what she was doing and was aware of the nature of her conduct and did not act through ignorance, mistake or accident.
>
> The government may prove that the defendant acted "knowingly" by proving, beyond a reasonable doubt, that this defendant deliberately closed her eyes to what would otherwise have been obvious to her. No one can avoid responsibility for a crime by deliberately ignoring what is obvious. A finding beyond a reasonable doubt of an intent of defendant to avoid knowledge or enlightenment would permit the jury to find knowledge. Stated another way, a person's knowledge of a particular fact may be shown from a deliberate or intentional ignorance or deliberate or intentional blindness to the existence of that fact.
>
> It is, of course, entirely up to you as to whether you find any deliberate ignorance or deliberate closing of the eyes and any inferences to be drawn from any such evidence. You may not conclude that defendant had knowledge, however, from proof of a mistake, negligence, carelessness, or a belief in an inaccurate proposition.

See United States v. Alston-Graves, 435 F.3d 331 (D.C. Cir. 2006) (emphasis added). Thus, jury

instructions should include cautionary language to avoid conflation with negligence.

4. Some Courts Have Cautioned That Deliberate Ignorance May Serve Only As A Mechanism For Inference, Rather Than A Substitute For Knowledge

Other commentators have expressed skepticism regarding deliberate ignorance theory because of the conceptual distinction with actual knowledge. "[I]t is hard to see how ignorance, from whatever cause, can be knowledge. A particular explanation of why a defendant remains ignorant might justify treating him as though he had knowledge, but it cannot, through some mysterious alchemy, convert ignorance into knowledge." Douglas N. Husak & Craig A. Callender, WILFUL IGNORANCE, KNOWLEDGE, AND THE "EQUAL CULPABILITY" THESIS: A STUDY OF THE DEEPER SIGNIFICANCE OF THE PRINCIPLE OF LEGALITY, 1994 Wis. L. Rev. 29, 52.

The Court of Appeals for the Eighth Circuit in Mattingly v. United States, 924 F.2d 785, 791 (8th Cir. 1991), considered whether a the trial court, in a proceeding to assess a civil penalty for aiding and abetting an understatement of tax liability, erred in giving a deliberate ignorance instruction. The Court held that the trial court erred because "actual knowledge, as opposed to the less stringent willful blindness, is required" where the statute at issue requires that the actor perform certain specified acts and know certain specified facts. Specifically, the Court found that "the statute requires that appellant assist in the creation of a tax document, know the use of the tax document, and know such document will understate another's tax liability." Id. at 791 (contrasting United States v. Massa, 740 F.2d 629 (8th Cir.1984), a brokerage fraud case requiring proof of specific intent, in which the court held that a willful blindness instruction was appropriate).

The court contrasted the "knows" requirement of 26 U.S.C. § 6701 to the "willful"

requirement in other civil tax preparer penalty provisions, and reasoned that "[s]ections 6694(b) and 7206(2) require willful understatement or willful assistance, respectively, before imposing liability." Id. The Court explained that "[t]he fact Congress chose to use 'knows' as opposed to a lesser form of mental state commonly used in other provisions leads us to believe a distinction was intended." The Court further noted that "[t]he legislative history indicates Congress intended that the actor be directly involved in aiding or abetting an understatement before liability is imposed." Id. (citing S. Rep. at 276, reprinted 1982 U.S.C.C.A.N. at 1022). The Court concluded that "the direct involvement requirement, in combination with Congress' choice of language, suggests an actual knowledge jury instruction is most appropriate." Id.[2]

Notwithstanding the Court's holding that the trial court erred in giving the deliberate ignorance instruction where the statute required knowledge of specific facts, the Court specifically recognized that "the willful blindness instruction still plays a role when knowledge is required, but as a mechanism for inference, not as a substitute for knowledge." Id. at 791. Therefore, jury instructions should be clear that deliberate ignorance is a means of drawing inferences.

IV. The Theory Of "Deliberate Ignorance" Should Apply To Customs Fraud Cases

The facts underlying Pan Pacific present a classic case of an importer's attempt to shield himself from liability for Customs fraud by deliberately seeking to avoid learning about the fraudulent scheme conducted upon his behalf and to his benefit.

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[2] Nevertheless, the Court held that the trial court's error was harmless where: (1) the trial court had also instructed the jury that the Government must prove a tax preparer knew he was aiding and abetting the understatement; (2) the instruction did not authorize substitution of willful blindness for the element of knowledge; and (3) there was evidence of actual knowledge on the part of the alleged aider and abettor. Id. at 792.

1. The Policies Underlying "Deliberate Ignorance" Apply Equally To Customs Fraud Cases

Key aspects of many Customs fraud cases fall in line with the policies underlying cases involving other types of fraud where the deliberate ignorance instruction was allowed. There are several rationales supporting the application of the deliberate ignorance theory that apply with equal force in the context of Customs fraud.

For example, the deliberate ignorance theory is often justified on the premise that a defendant who deliberately remains ignorant is just as culpable as a defendant who is fully informed. See, e.g., Jewell, 532 F.2d at 700. As in Walker, 191 F.3d at 337, and Leahy, 445 F.3d at 652, Customs cases often involve individuals who claim not to be aware of the specific mechanics of how goods are entered fraudulently by agents acting on their behalf. The arrangements for entering goods fraudulently often involve highly suspicious circumstances, such as the unusually low fees charged by a broker that may be well below the duty rates that would have been charged otherwise in many instances.

Deliberate ignorance theory recognizes that individuals should not be able to shield themselves from liability merely because they had the foresight not to conduct a reasonable inquiry about the suspicious actions taken on their behalf. Similarly, courts have reasoned that conscious avoidance of material facts does not necessarily negate an ability to perform fraudulent acts. See, e.g., United States v. Adeniji, 31 F.3d 58, 62 (2d Cir. 1994). Customs cases may involve defendants who, as in Jaffe, 387 F.3d at 681 and Jakubowski, 150 F.3d 678, have a high degree of understanding with respect to their legal obligations. Just as evidence of personal benefit supported use of the deliberate ignorance instruction in Lowry, 340 F.3d at 506 and other cases, the benefits from the fraudulent acts by a broker often redound to the importer.

Courts have reasoned that the concept of "knowledge" necessarily encompasses more than positive knowledge. United States v. Graham, 739 F.2d 351, 353 (8th Cir. 1984) ("one 'knows' facts of which he is less than absolutely certain. To act 'knowingly,' therefore, is not necessarily to act only with positive knowledge, but also to act with an awareness of the high probability of the existence of the fact in question."). Similarly, the theory recognizes that person's knowledge or a state of mind can rarely be proven directly, and that plaintiffs typically must rely upon circumstantial evidence to establish mens rea. The Customs penalty statute does not require that a defendant have knowledge of certain facts that are specified by statute, unlike in Mattingly, 924 F.2d at 791-92, and many Customs cases rely upon circumstantial evidence to prove the requisite level of scienter. In the absence of any legislative intent that "knowingly" was intended to be limited to actual knowledge, the statute allows for knowledge to be established by means of an inference that can be drawn from circumstantial evidence of deliberate ignorance.

2. The Facts In Pan Pacific Demonstrate The Applicability Of The Deliberate Ignorance Theory

Defendant Thomas Man Chung Tao was the sole owner and president of Pan Pacific Textile Group, Inc. ("Pan Pacific"), and Aviat Sportif, Inc. ("Aviat"). Mr. Tao and his companies were almost exclusively engaged in the importation and distribution of men's and women's track suits manufactured in the People's Republic of China. At issue in the case were 68 entries of track suits entered into the United States at the Ports of Los Angeles and Long Beach, California, between September 21, 1995 and January 20, 1997. Mr. Juang was the owner, president, and chairman of defendant Prime International Agency ("Prime") and Budget Transport, Inc. ("Budget"), (collectively "Prime/Budget"). Mr. Juang provided freight

forwarding services and cleared shipments through customs on behalf of Mr. Tao, even though Mr. Juang did not have a valid broker's license.

Mr. Tao's business arrangement with Mr. Juang for the importation of track suits occurred in two main phases. Initially, without Mr. Tao's knowledge Mr. Juang filed with Customs falsified invoices and other falsified entry documents that falsely described the goods, understated their value, and, thus, arrived at a lesser amount of duty owed. The documents falsely described the track suits as non-restricted (that is, not subject to quota), low-duty, and inexpensive "plastic sacks and bags" or "wooden patio tables." Compare HTSUS 3923.21.0090 (1996) (setting 3% tariff for plastic bags) and HTSUS 9401.79.0025 (1996) (setting 2.4% tariff for outdoor household furniture sets with metal frames) with HTSUS 6211.33.30 (1996) (setting 16.8% tariff for sets of men and boys' tracksuits of man-made fibers). Mr. Juang paid Customs the lower amount of duty and pocketed the difference between what was charged to Mr. Tao and what was paid to Customs. Id. Mr. Juang attached to his invoices to Mr. Tao entry documents that he had created which accurately described the goods, the value, and the applicable duty rate, but were never in fact filed with Customs.

Approximately one year and a half later, however, Mr. Juang proposed a change in the business relationship. Mr. Juang offered Mr. Tao a "flat fee" that was necessarily lower than the actual amount of duties that Mr. Tao would have had to pay to Customs. Mr. Juang also told Mr. Tao that he no longer needed to purchase quota visas. For the duration of Mr. Tao's business relationship with Juang, Chinese textiles were subject to quotas and required quota visas for entry into the United States. See, e.g., Agreement Between the United States and China Concerning Trade in Textile and Apparel Products, U.S.-China, June 8, 1995, Temp. State Dep't

No. 95-148, 1995 WL 539718.

Mr. Tao accepted Mr. Juang's proposal. Messrs. Juang and Tao negotiated the flat fee, which varied depending on the size of the container. Mr. Tao knew that he would be benefitting from it by paying an amount lower than the duties he had been paying previously. Mr. Tao agreed that he would no longer be identified as the "importer of record," and he stopped keeping copies of his entry records.

Mr. Tao told his supplier in China, Singmay, to continue submitting invoices properly identifying the merchandise as track suits, but that it no longer needed purchase the quota visas. Mr. Juang began submitting to Mr. Tao invoices that did not indicate the amount actually paid for customs duties, and stopped providing Mr. Tao with copies of entry documents. Mr. Tao instructed his employees to pay the invoices from Mr. Juang automatically.

On or about November 26, 1996, Customs Special Agents began investigating Mr. Juang's involvement in an operation of suspected smuggling of Chinese medicine into the United States. On February 26, 1997, a Federal search warrant was issued to conduct a search of the premises of Mr. Juang's companies, Prime/Budget. Upon analyzing the seized records, investigators discovered that, from late 1993 to early 1997, Prime/Budget entered track suits for numerous importers, including Mr. Tao and his companies, Pan Pacific and Aviat. Based upon the evidence seized, investigators searched the premises of Pan Pacific and Aviat, Mr. Tao's companies in City of Industry, California, in early 1997.

On June 19, 1997, Customs conducted another search of Pan Pacific's premises, and recovered documents establishing that payments by Pan Pacific to Prime/Budget's shell companies, Ever Power and/or Billion Sales, were generally less than one-third of the duties that

would have been owed based upon the value represented on the actual commercial invoices. The search also revealed that quota visa charges had not been paid for entries of track suits.

Before the Court of International Trade, the Government argued, among other things, that the application of "deliberate ignorance" theory was warranted based upon the Mr. Tao's admissions as well as uncontroverted facts surrounding his business arrangment with Mr. Juang. Mr. Tao specifically chose not to ascertain basic facts to ensure that the goods were entered properly. Mr. Tao was aware of Customs filing requirements. Mr. Tao testified that he did not know how Mr. Juang was able to enter the goods for a lower duty, but that he deliberately did not inquire as to the nature of Mr. Juang's activities. Lastly, Mr. Tao derived a personal benefit from his agent's activities where he paid amounts substantially below the amount he would have had to pay had the goods been entered properly.

As in Stone, 554 S.W. 2d at 188, Walker, 191 F.3d at 337, and Roadmaster, 892 F. Supp. at 1176-78, Mr. Tao was also aware of highly suspicious facts that put him "on notice" of false statements being made upon his behalf. Mr. Tao admitted that he knew that the "flat fee" that Mr. Juang was charging him for complete package of entry services represented an amount that was necessarily less than the duties that he would have had to pay otherwise. Mr. Tao admitted that he knew that the amounts that he actually paid under this scheme were below the amount of duties he would have to pay based upon the value of the merchandise indicated on the commercial invoices. As in Jakubowski, 150 F.3d 675, 678, this arrangement resulted in a benefit to Mr. Tao.

As in Faulkner, 17 F.3d at 766; Stouffer, 986 F.2d at 925; and Del Aguila-Reyes, 722 F.2d at 157, Mr. Tao failed to conduct a reasonable inquiry notwithstanding the highly

suspicious activities of his broker. Mr. Tao never asked Mr. Juang how it was possible to pay an amount below the duties that would be owing. Mr. Tao assumed Mr. Juang was basing the duties upon the cost of production, but never verified with Mr. Juang that such was the case. Mr. Tao knew of irregularities in the way Mr. Juang billed him for his “import services,” but nonetheless accepted the way Mr. Juang implemented the "flat fee" agreement without question. Mr. Tao stated that once the "flat fee" arrangement went into effect, he stopped paying attention to the information in the invoices sent by Mr. Juang. Mr. Tao did not request supporting documentation, and instructed his employees to pay the invoices from Mr. Juang “automatically.” Mr. Tao's employee brought to his attention the fact that the charges on Mr. Juang's invoices varied for no apparent reason, but Mr. Tao instructed her to pay the charge without receiving any explanation from Mr. Juang, even though the previous broker's charges had always been consistent. Mr. Tao’s intimate involvement with the facts surrounding the entry documents supports application of the deliberate ignorance instruction. Draves, 103 F.3d at 1333-34.

Mr. Tao was an experienced importer who was familiar with his legal obligations, as in Jaffe, 387 F.3d at 681. Mr. Tao knew that a quota visa was necessary for each shipment, yet took no steps to ensure that one was in fact being purchased during the "flat fee" period. Mr. Tao agreed that Mr. Juang would "handle" the visa, and instructed Singmay not to purchase the visa, but never inquired of Mr. Juang how he obtained a visa or asked to see proof that one was in fact being purchased. Mr. Tao instructed his employee not to ask questions with respect to Mr. Juang's "handling" of the quota visa. Mr. Tao's admission that he had instructed Singmay to continue submitting invoices properly identifying the merchandise as track suits indicates that he

was aware that Mr. Juang's "flat fee" scheme was, at best, not the normal course of business.

Therefore, the factual circumstances underlying the Pan Pacific case demonstrate that Customs fraud cases can bear all the hallmarks of "deliberate ignorance" as applied in other fraud cases.

V. Conclusion

In recognition of the applicability of these principles, Customs regulations should be amended to specify that the Government may satisfy the "knowledge" requirement for purposes of establishing fraudulent intent under 19 U.S.C. § 1592 by establishing that: (1) the defendant was subjectively aware of a high probability of the existence of illegal conduct; and (2) the defendant purposely contrived to avoid learning of the illegal conduct. Scott, 159 F.3d at 922. Such an amendment would clarify the applicability of deliberate ignorance theory and provide practical guidance for the standards for making the determination. In the meantime, the Courts are well within their discretion to apply the "deliberate ignorance" theory as applied in other fraud contexts to Customs penalty actions in which the Government claims that the defendant acted with fraudulent intent.