

**CIVIL AND CRIMINAL TAX PENALTIES**  
**IMPORTANT DEVELOPMENTS - CRIMINAL**

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## THE KPMG CASES

### *United States v. Jeffrey Stein, et al.* 05 Crim. 0888 (S.D.N.Y.) (KPMG)

On October 17, 2005, the government filed a 46-count superseding indictment in *United States v. Jeffrey Stein, et al.*, adding 10 additional defendants to what has been billed as “the largest criminal tax case ever filed.” Press Release (October 17, 2005), United States Attorney, Southern District of New York. The 19 defendants included the former Deputy Chairman of KPMG, several former heads of KPMG’s Tax Practice, the former CFO of KPMG, the former head of KPMG’s Department of Professional Practice, a former KPMG Associate General Counsel, a former tax partner of a prominent national law firm, and numerous other KPMG tax partners. Count One charged all defendants with conspiracy to defraud (18 U.S.C. § 371) for allegedly devising, marketing, and implementing fraudulent tax shelter schemes, which generated at least \$11.2 billion in phony tax losses. Counts Two through Forty charged all defendants with tax evasion (26 U.S.C. § 7201) based on their own tax returns and those of tax shelter clients. In Counts Forty-one through Forty-four, certain defendants were charged with evasion based on payments made in exchange for opinion letters provided to tax shelter investors. Counts Forty-five and Forty-six charged certain defendants with obstructing the investigations into the tax shelters (26 U.S.C. § 7212). KPMG is not a defendant in the *Stein* indictment, having executed a deferred prosecution agreement.

As noted, in furtherance of this fraud, the defendants allegedly issued opinion letters containing false representations that the tax shelter losses would “more likely than not” survive an IRS challenge, as well as other false documentation regarding the tax shelter transactions. The superseding indictment alleged that the defendants fraudulently concealed the tax shelters from the Service by failing to register the tax shelters and by preparing tax returns that fraudulently concealed phony losses. The government contended that the defendants obstructed the IRS and United States Senate investigations into their tax shelter scheme by: (1) attempting to conceal documents and information with sham attorney-client privilege claims; (2) failing to turn over requested documents; and (3) falsely testifying before both the IRS and Senate.

In *United States v. Stein, et al.*, 435 F. Supp. 2d 330 (S.D.N.Y. 2006) (June 26, 2006) (“*Stein I*”), Judge Lewis Kaplan ruled that the government unconstitutionally pressured KPMG not to pay legal fees for the defendants. “Those who commit crimes – regardless of whether they wear white or blue collars – must be brought to justice. The government, however, has let its zeal get in the way of its judgment. It has violated the Constitution it is sworn to defend.” *Id.* at 336. Judge Kaplan noted that while the government did not literally request or direct that KPMG do anything with respect to the legal fees, it was clear that “KPMG refused to pay because the government held the proverbial gun to its head.” *Id.*

In the earlier stages of the investigation, and in an attempt to demonstrate cooperation and avoid prosecution, KPMG put significant pressure on its employees, using legal fees as leverage. According to a form letter KPMG sent to counsel for its employees and to the government, the firm authorized \$400,000 in fees for employees willing to cooperate. If an employee failed to cooperate or was charged with a crime, KPMG would pay nothing. Judge Kaplan also pointed to the Memorandum from then-Deputy Attorney General Larry D. Thompson to Heads of Department Components and United States Attorneys, entitled: Principles of Federal Prosecution of Business Organizations (Jan. 20, 2003), which advised prosecutors to

grant more lenient treatment to firms under criminal investigation if they stop paying legal fees on behalf of potentially culpable employees.

At that time, Judge Kaplan stopped short of dismissing the charges or ordering the government to pay the legal fees, which would literally require an act of Congress, but said the defendants could proceed against KPMG in an ancillary civil action, over which he would preside and move expeditiously. He suggested that KPMG pay the fees to avoid “more unpalatable relief” being granted to the defendants.

In *United States v. Stein, et al.*, 252 F. Supp. 2d 230 (S.D.N.Y. 2006) (September 6, 2006), some of the defendants filed suit against KPMG seeking advancement of legal defense costs, and KPMG filed a motion to dismiss for lack of subject matter jurisdiction and on the merits. In particular, KPMG argued that the defendants are obliged, by the terms of their employment contracts, to arbitrate these claims. KPMG further argued that the claims by some of the defendants were foreclosed by the partnership agreement or released.

Judge Kaplan held that the district court had ancillary jurisdiction over the advancement claim. He further held that, assuming the existence of a valid arbitration agreement regarding the claim, the enforcement of any such agreement would violate public policy by compromising the court’s ability to ensure a speedy trial, protect the public interest by avoiding possible dismissal of the criminal charges, safeguard the defendants’ rights to a fundamentally fair trial, and seek to avoid imposing defense costs on the taxpayers if any of the defendants are required to seek appointed counsel. Finally, Judge Kaplan held that the allegations stated a claim for contract implied in fact and, with the possible exception of one defendant whose claim may be subject to dismissal on summary judgment, the claims would proceed to trial. KPMG appealed the ruling.

On January 8, 2007, by invitation from the Second Circuit, Judge Kaplan filed a 47-page brief urging the court to treat KPMG’s appeal as a petition for writ of mandamus. Judge Kaplan argued that the petition should be denied, as there was “little likelihood that the issue” would recur, and described the entire case as “the perfect storm.”

Having declined to dismiss the charges in June of 2006, one year later, on July 16, 2007, Judge Kaplan dismissed the indictments as to thirteen of the remaining defendants (all of whom had been employed by KPMG) after (a) the Second Circuit overruled his decision that the U.S. District Court for the Southern District of New York had ancillary jurisdiction over the claims of certain defendants against KPMG for advancement of defense costs and after (b) the government filed a Memorandum of Law essentially conceding (as a predicate to an appeal) that, based on Judge Kaplan’s holding in *Stein I*, the indictments as against thirteen of the defendants must necessarily be dismissed. *United States v. Stein, et al.*, 495 F. Supp. 2d 390 (S.D.N.Y. 2007) (July 16, 2007) (“*Stein II*”).

Judge Kaplan began that Opinion by stating “The government threatened to indict, and thus to destroy, the giant accounting firm [KPMG]. It coerced KPMG to limit and then cut off its payment of the legal fees of KPMG employees. KPMG avoided indictment by yielding to government pressure. Many of its personnel did not. They now await trial, four of them deprived of counsel of their choice and most of the others unable to afford the defenses that they would have presented absent the government’s interference.” *Id.* at 393.

In his Opinion, Judge Kaplan reviewed much of the factual history and legal considerations, including the deprivation of defendants' substantive due process rights, that had led to his Opinion in *Stein I* and also analyzed whether the actions of the U.S. Attorney's Office "shocks the conscience in the constitutional sense." Judge Kaplan determined that, "[t]heir actions were not justified by any legitimate governmental interest. Their deliberate interference with the defendants' rights was outrageous and shocking in the constitutional sense because it was fundamentally at odds with two of our most basic constitutional values -- the right to counsel and the right to fair criminal proceedings." The Court went on to note that even a "deliberate indifference" to constitutional rights would be sufficient to conclude that a constitutional violation, in addition to the deprivation of substantive due process rights, had occurred.

After examining the circumstances surrounding each of the individual defendants, Judge Kaplan concluded that three defendants who could not afford their counsel of choice after KPMG ceased paying their legal bills were denied their Sixth Amendment rights. With regard to ten of the other defendants, the Court found that the government's conduct, interfering "with the payment of defense costs that KPMG would otherwise have paid" left them unable to "defend this case as he or she would have defended it had KPMG been paying the cost." With regard to each of those defendants, Judge Kaplan found that without dismissing the case, it would be impossible to restore them to the position they would have been but for the misconduct.

With regard to three other defendants, Judge Kaplan declined to dismiss the indictments because he found that the government's conduct had not deprived them of their right to counsel. Two of the defendants left KPMG many years earlier and much of the conduct with which they were charged occurred after they left so that KPMG likely would not have paid their legal fees. The third defendant left KPMG under "strained circumstances" and signed a release of claims, so that KPMG likely would not have paid his legal fees.

Judge Kaplan's decision left five defendants. On August 3, 2007, Judge Kaplan rejected the Motion of those defendants for a continuance of the October 16, 2007 trial date as well as the government's motion to sever the case of David Greenberg so that his case could be tried first.

On September 10, 2007, David Amir Makov, one of the remaining five defendants, pled guilty to "participating in a conspiracy to defraud the United States Treasury, evade taxes and file false tax returns" in connection with "Bond Linked Issue Premium Structures" ("BLIPS").

## **RECENT DEVELOPMENTS**

Although the case was calendared for trial on October 16, 2007, two days after that, the Court issued an Order discharging the already qualified jury panel. This was necessary because the government had belatedly brought to the Court's attention a conflict between counsel for John Larson and Mr. Larson himself which required (in the absence of a waiver by Mr. Larson) that new counsel be appointed. The conflict apparently arose because Mr. Larson's counsel may have represented Mr. Makov at an earlier stage of the investigation and therefore might have been barred from cross-examining him on behalf of Mr. Larson during the trial.

The trial is now scheduled to commence in September 2008, with *voire dire* to begin on or about September 25, 2008.

As recently as November 4, 2007, despite the Court's August 3, 2007 rejection of the government's motion seeking to sever the trial of Mr. Greenberg, the government sought a fourth superseding indictment with regard to Mr. Greenberg. According to a Memorandum in Law in Support of David Greenberg's Motion to Dismiss the Fourth Superseding Indictment, on November 4, 2007, "the same date that the superseding indictment was returned, the government sent a copy to the Court with a letter expressing the view that " a prompt trial of [Mr.] Greenberg [alone] is in the interest of justice as it would permit the Government and the Court to try this discrete, pared down case without additional delay." There has been no ruling on Mr. Greenberg's Motion.

The government filed its Brief on Appeal of *Stein II* on October 10, 2007 and on January 8, 2008, a Brief ("Defendant's Brief") was filed on behalf of those defendants against whom charges were dismissed in *Stein II*. As described in the introduction to Defendant's Brief, "This appeal presents a single, straightforward question: may prosecutors, without justification, deprive a criminal defendant of funds that otherwise would lawfully be available for his defense." The government's brief (page 106) concludes by noting that the "District Court's conclusion that the USAO's conduct 'shocked the conscience' unfairly tarnishes the reputations of devoted public servants whose only objective was, and is, to protect society from the predations of criminals, whether they wield a gun or a pen...The District Court's conclusion that the investigation 'shocks the conscience' should be reversed."

## OTHER NEWS

In *United States v. Snipes*, 2007 WL 2572198 (M.D. Fla.) (Sept. 5, 2007), Wesley Snipes has been charged with conspiring with Eddie Ray Kahn and Douglas P. Rosile to defraud the government in violation of 18 U.S.C. § 371 by frustrating the Service's attempt to collect income tax owed by Snipes for tax years 1999 through 2005, filing false claims in violation of 18 U.S.C. § 287, based on Snipes' amended return for 1997 claiming a refund in excess of \$7.3 million, and six counts of failing to file tax returns for years 2000 through 2005 in violation of 26 U.S.C. § 7203. In addressing Snipes' pretrial motions, the court quickly dispensed with his motion to dismiss for failure to state an offense and his argument that the insertion of the word "no" before "penalties of perjury" on the Form 1040X dispensed with the charge under § 287. *Id.* at \*2. The court also rejected Snipes' argument that he was the victim of selective prosecution based on racial prejudice. The court noted that Snipes is not being prosecuted because of his race, but he may have been selected for the purpose of general deterrence based on his apparent wealth and famous status. The court also rejected Snipes' request to move the trial to the Southern District of New York, finding that the travel burdens on his family and legal counsel were insufficient to transfer venue when the other defendants and the majority of witnesses were located in Florida. Jury selection began on January 14, 2008.

**"Operation Dialing for Dollars"** – On December 6, 2007, Treasury Inspector General for Tax Administration J. Russell George announced the indictment of 10 employees of BNT Investigations by a federal grand jury in Seattle on charges of conspiracy and wire fraud. The indictments are the result of a year-long investigation called "Operation Dialing for Dollars." Under the scheme, the BNT employees would pose as another individual (for example, a representative from a doctor's office) to illegally obtain confidential information from the Internal Revenue Service, the Social Security Administration and assorted state employment security offices.

## 26 U.S.C. § 7201 (intent to evade or defeat tax)

In *United States v. Vaughn*, 2007 WL 4014457 (4th Cir.) (Nov. 15, 2007), Vaughn was convicted of evasion of payment in violation of 26 U.S.C. § 7201, stemming from false information provided with an Offer in Compromise. He was sentenced to 51 months. On appeal, Vaughn argued that the district court did not allow him to present a “good faith” defense, improperly disallowed a challenge to the underlying deficiency, and incorrectly ruled that a formal assessment is not an element of tax evasion. Vaughn further contends that the government impermissibly indicted or threatened to indict two defense witnesses.

The Fourth Circuit quickly rejected the good faith and deficiency arguments. It went on to find that the district court was correct in stating that the prosecution did not need to prove a valid assessment because § 7201 is not limited to assessed liabilities. *Vaughn*, at \*2 (citing *United States v. Silkman*, 156 F.3d 833, 835 (8th Cir. 1998)). Finally, the court rejected Vaughn’s contention that his witness should have been given immunity, noting that the decision to grant immunity is within the sole discretion of the prosecution unless the defendant demonstrates prosecutorial misconduct or overreaching and proves that the expected testimony will be material, exculpatory and unavailable from all other sources. Vaughn failed to meet this burden and his conviction was affirmed.

In *United States v. Thomas*, 2007 WL 4104390 (W.D. La.) (Nov. 14, 2007), Thomas was indicted on August 24, 2006, of, among other charges, evasion of payment in violation of 26 U.S.C. § 7201. The overt acts of evasion began in November, 1997 and continued through April, 2006. Thomas moved for judgment of acquittal at the close of the government’s case, arguing that the only acts occurring within the 6-year statute of limitations (26 U.S.C. § 6531) were not false or misleading statements. Alternatively, he argued that whether the acts were false or misleading was for the jury and required an instruction on the statute of limitations and acts which may interrupt the statute of limitations. The court noted that each circuit that has addressed the issue of what constitutes an affirmative act of evasion agrees that it is the “willful attempt to evade taxes *in any manner*.” *Thomas*, at \*2 (emphasis in original). Thus, the court held that the indictment was timely having alleged an overt act within the 6-year period, but agreed that whether Thomas was entitled to the requested jury instructions.

In *United States v. Chisum*, 502 F.3d 1237 (10th Cir.) (Sept. 25, 2007), Chisum was a business and estate planner and a tax protestor. He was convicted on four counts of aiding and abetting the evasion of income tax owed by two former clients in violation of 26 U.S.C. § 7201. On appeal, Chisum raised time worn protestor arguments, including the lack of subject matter jurisdiction, the federal Paperwork Reduction Act, and the Speedy Trial Act. On a more substantive note, Chisum argued that the district court erred in admitting evidence of his suits against Tax Court judges, filed in response to the judges’ rulings that Chisum’s trusts were shams. Chisum claimed that evidence of the lawsuits painted him in a poor light and added nothing relevant because the actual Tax Court opinions were already admitted.

The Tenth Circuit noted that “[t]he intent requirement in criminal tax cases is particularly strict.” *Chisum*, 502 F.3d at 1241 (citation omitted). The government must show not only that the defendant had a duty and knew of it, but that the defendant also voluntarily and intentionally violated the duty. This heavy burden cannot be met by merely proving that the defendant had actual knowledge; there is an intent component which can be defeated by a showing of good-

faith belief. For that reason, the court found that evidence of the prior lawsuits were extremely relevant and, since the Tax Court decisions were already admitted as evidence without objection, there was little danger of unfair prejudice.

Chisum further argued that the district court erred in applying a role enhancement under U.S.S.G. § 3B1.1, because it did not specifically find that he organized, led, managed or supervised someone who was criminally responsible. The Tenth Circuit agreed that this finding was not made and declined the government's invitation to hold that it was "obvious" that Chisum's former client was criminally responsible. The court remanded for specific factual findings on this matter. *Id.* at 1243.

In *United States v. Miller*, 2007 WL 2746703 (W.D. La.) (Sept. 18, 2007), Miller was indicted on two counts of tax evasion in violation of 26 U.S.C. § 7201. He moved to strike for prejudice language in the indictment referring to his alleged failure to file. Miller claimed that failure to file by itself does not constitute tax evasion, but it could be interpreted as an act of evasion by a jury. The court disagreed, holding that even if information in an indictment is prejudicial, it should not be stricken if it is sufficiently relevant to the charged offense. Because Miller's failure to file or pay income tax was a necessary element of his evasion, the court found that the indictment was proper and any prejudice could be eliminated through jury instruction.

### **26 U.S.C. § 7203 (failure to file)**

In *United States v. McKee*, 506 F.3d 225 (3d Cir.) (Oct. 29, 2007), McKee and his co-defendants, Joseph and Inge Donato, were "members of the Reformed Israel of Yaweh ("RIY"), a small religious sect founded by Leo Volpe that opposes payment of taxes based upon the members' religious opposition to war and the taxes that fund it." *McKee*, at 228. McKee and Joseph were partners in a construction company and Inge, Joseph's wife, assisted with the bookkeeping. For their employees who were also RIY members, the defendants did not withhold income taxes or report wages on employment tax returns. For non-RIY employees, the defendants reported and withheld payroll taxes as required.

The defendants were charged and convicted of conspiring to defraud the United States in violation of 18 U.S.C. § 371, and employment tax evasion in violation of 26 U.S.C. § 7201. McKee and Joseph were also convicted of failure to file for 1997 through 2000 in violation of 26 U.S.C. § 7203. Inge was charged with the same four counts of failure to file as Joseph. The court dismissed two of those counts (1998 and 2000) because the government failed to establish that Inge had income during those years. She was convicted on the remaining counts for 1997 and 1999. On appeal, the defendants' arguments included a collective challenge to the jury instruction on affirmative acts of evasion and sufficiency of the evidence.

On appeal, the defendants challenged the jury instruction regarding affirmative acts of evasion. Because the argument was not raised below, the Third Circuit reviewed for plain error. Under Third Circuit precedent, *see United States v. Syme*, 276 F.3d 131, 154 (3d Cir. 2002), a constructive amendment is not a *per se* reversible error, but gives rise to a rebuttable presumption of prejudice. *Id.*, n.3. The instruction included the following language:

Affirmative attempts to evade federal employment taxes include, for example, filing false Employers Quarterly Federal Tax Returns (Forms 941), *falsifying*

*books and records so as to conceal the payment of wages and the employment taxes due thereon, or failing to report to your accountant all of the wages paid to employees.*

506 F.3d at 229-30 (emphasis in original). While evidence of each example was admitted at trial, the indictment only charged the defendants with filing false quarterly returns. The Third Circuit held that the instruction constructively amended the indictment because it allowed the jury to convict for uncharged conduct. The court vacated the convictions and, after determining that sufficient evidence had been introduced to support all but two charges against Inge, remanded for further proceedings. *Id.* at 232.

With respect to the failure to file convictions against Inge, the district court instructed the jury that, “the married couple files no returns, the law presumes that the tax status of the husband and wife is married filing separately.” *Id.* at 244. The government conceded that Inge did not earn a paycheck for services rendered. It claimed, however, that Inge was compensated because company checks were used in 1997 to purchase a Honda Accord titled in her name and to pay for a paint job on the Donato residence, and in 1999 to purchase an Acura titled in her name. The government argued that 50% of these payments constituted taxable income to Inge.

The Third Circuit disagreed based on the government’s failure to prove that the payments were intended as compensation to Inge or, if they were so intended, that Inge knew of that intention and therefore, knew she had a duty to file returns for those years.” *Id.* at 245. The court specifically noted Inge’s history of providing services without compensation and the lack of connection between the payments and any specific amount of time she worked. It further noted that the payments could simply represent a gift from Joseph or household support. The Court held that “benefit alone can not establish income,” *Id.* at 247. The court vacated the failure to file convictions against Inge and directed an order of acquittal.

## **26 U.S.C. § 7206 (false statement)**

In *United States v. Clayton*, 506 F.3d 405 (5th Cir.) (Oct. 29, 2007), Clayton was a tax protestor who claimed that under 26 U.S.C. § 861, U.S. citizens may not be taxed on domestically earned income. He was convicted of two counts of making and subscribing a false amended tax return for 1997 and 1998 in violation of 26 U.S.C. § 7206(1), and six counts of willful failure to file a tax return for 1999 through 2004 in violation of 26 U.S.C. § 7203. Clayton was sentenced to sixty months imprisonment after his post-trial motion for judgment of acquittal on the 1997 and 1998 counts was denied.

Clayton appealed his convictions for failure to file on the grounds that the district court erred in determining that Clayton was required to file a tax return because “in establishing the exemption amount in 26 U.S.C. § 6012, the government failed to comply with the procedural requirements of the Administrative Procedure Act (“APA”)” when it relied on the Consumer Price Index (“CPI”). *Clayton*, at 408-09.

In rejecting this argument, the Fifth Circuit noted that the obligation to file a tax return is derived from a congressionally-enacted statute, not an agency and, thus is not subject to the APA. Additionally, the Court held that the CPI is an “ascertainable numerical standard” which does not need to be an enforceable rule of law to be incorporated into a statute. *Id.* at 409-10.

Clayton next argued that the district court erred in denying his request for a jury instruction based on his theory that the Forms 1040X, the basis of the false return charges, were not false returns but rather, proper claims for refund. The Fifth Circuit again disagreed, holding that “filing a false claim for the refund of taxes gives rise to legal liability for filing a false tax return.... Moreover, use of a legal procedure to challenge tax liability does not preclude criminal liability.” *Id.* at 411 (citations omitted).

In *United States v. Contreras*, 2007 WL 2718660 (2d Cir.) (Sept. 18, 2007), Contreras was a tax return preparer charged and convicted of conspiring to defraud the government in violation of 18 U.S.C. § 286 and 17 counts of aiding and abetting the filing of fraudulent income tax returns in violation of 26 U.S.C. § 7206(2). He was sentenced to 60 months and appealed, arguing insufficient evidence and unreasonable sentence. The court considered and rejected Contreras’ classic tax preparer defenses, including that: (1) he did not prepare the returns at issue (his employees did); and (2) he had an absolute good faith right to rely on information provided by his clients (the government found two clients that disavowed the information on their returns).

In *United States v. Cerullo*, 2007 WL 2683799 (S.D. Cal.) (Sept. 7, 2007), the government obtained an indictment against Cerullo, a religious minister, for filing a false tax return in violation of 26 U.S.C. § 7206(1). Cerullo moved to dismiss the indictment, alleging that prosecutorial error created sufficient prejudice to undermine the independence of the grand jury and warrant dismissal. In making his case to the grand jury, the prosecutor alleged that all money received by Cerullo as a result of his sermons constituted taxable income. He presented testimony of a revenue agent who failed to advise the jurors of the importance of donor intent and, despite specific questions, failed to acknowledge the possibility that the funds could be nontaxable gifts. The court noted that the Supreme Court found that donor intent was a critical factor in making such a determination in *Commissioner v. Duberstein*, 363 U.S. 278 (1960). In dismissing the indictment, the court held that the refusal to so inform the grand jury constituted prosecutorial error that substantially prejudiced Cerullo.

### **26 U.S.C. § 7212 (obstruction)**

In *United States v. Willner*, 2007 WL 2963711 (S.D.N.Y.) (Oct. 11, 2007), Willner was indicted for obstructing the administration of the IRS in violation of 26 U.S.C. § 7212(a), and filing false corporate returns in violation of 26 U.S.C. § 7206(2). The government alleged that while he was employed as an IRS agent, Willner failed to report income earned from other activities and took steps to hide his income and income of third parties by diverting the payment of funds to an entity he owned. Specifically, Willner directed one of his employers to issue checks for services rendered to his corporation (NIA) and those funds were reported as corporate income, but were offset by a net operating loss such that no tax was paid. Likewise, Willner enlisted others to pay their income to NIA and thereby avoid tax, in exchange for payment of 20% of the funds diverted. Willner moved to dismiss the obstruction count, arguing that it failed to allege that he interfered with an on-going proceeding or investigation of the Internal Revenue Service. The court disagreed and in denying Willner’s motion, rejected the holding of *United States v. Kassouf*, 144 F.3d 952 (6th Cir. 1998), that § 7212(a) requires that the defendant be aware of a pending IRS investigation while committing the charged conduct.

## **18 U.S.C. § 1956 (money laundering)**

In *United States v. Khanani*, 502 F.3d 1281 (11th Cir.) (Oct. 2, 2007), the defendants appealed their convictions for knowingly encouraging or inducing aliens to reside in the United States unlawfully in violation of 8 U.S.C. § 1324(a)(1)(A)(iv); conspiring to conceal, harbor, or shield from detection, or encouraging or inducing aliens to illegally enter or reside in the United States in violation of 8 U.S.C. § 1324(a)(1)(A)(v)(I); and committing wire and mail fraud in violation of 18 U.S.C. §§ 1341 and 1343. *United States v. Maali*, 358 F. Supp. 2d 1154, 1156 (M.D. Fla. 2005). The government cross appealed the court's grant of defendants' motion for acquittal on the charge of conspiring to engage in money laundering or in monetary transactions in property derived from a specified unlawful activity in violation of 18 U.S.C. § 1956(h).

Khanani owned several retail stores that employed individuals who were not authorized to work in the United States. Khanani and his co-defendant Portluck paid these workers with money skimmed from the retail stores. The income paid to the workers was not reported, and no employment taxes were paid on the wages.

Under §§ 1956 and 1957, the government was required to establish that the “defendants conspired to launder or to engage in a monetary transaction involving the proceeds of specified unlawful activity.” *Maali*, 358 F. Supp. 2d at 1156-57 (internal quotations and footnote omitted). The government argued that the tax and cost savings from hiring undocumented workers constituted “proceeds” and that the defendants channeled these funds into shell companies to conceal their unlawfully derived income and promote their illegal employment scheme. The district court disagreed with the government’s “cost savings” theory of “proceeds,” finding that the “plain and ordinary meaning” of the term was “something which is obtained in exchange for the sale of something else as in, most typically, when one sells a good in exchange for money.” *Id.* at 1158. The district court further held that the “the term does not contemplate profits or revenue indirectly derived from labor or from the failure to remit taxes.” *Id.* at 1160.

The Eleventh Circuit sustained defendants' convictions and affirmed the acquittal of the money laundering charge. It held that sales revenue indirectly derived from owner's employment practices, through tax and labor cost savings, did not constitute “proceeds” of a specified unlawful activity within the meaning of § 1956(h).

## **18 U.S.C. § 2342 (Contraband Cigarettes Trafficking Act)**

In *United States v. Morrison*, -- F. Supp. 2d --, 2007 WL 3315887 (E.D.N.Y.) (Nov. 9, 2007), Morrison, a Native American cigarette retailer, was charged with 77 counts of violating the Contraband Cigarettes Trafficking Act (“CCTA”) by knowingly and intentionally selling and distributing contraband cigarettes lacking valid New York State tax stamps in violation of 18 U.S.C. §§ 2342(a) and 2. The government alleged that Morrison aided and abetted the sale of contraband (untaxed) cigarettes on Native American reservations to non-tribal members. Sales to tribal members are exempt from tax. Morrison moved to dismiss on substantive due process grounds. He argued that the CCTA is vague as applied because the State of New York fails to enforce the statute. While the court acknowledged the void-for-vagueness doctrine, it noted that “the failure of the executive branch to enforce the law is not the same as saying that the legislative branch has repealed it.” *Morrison*, at \*6. In rejecting Morrison's argument, the court noted that the requirement that the government prove that Morrison acted with specific intent to

aid and abet the sale of the contraband cigarettes alleviates some of the concern raised by potentially vague or indefinite statutes. The court also rejected Morrison's contention that the CCTA authorizes arbitrary and discriminatory enforcement. The court held that the statute clearly defined the unlawful conduct – the aiding and abetting of the sale of unstamped cigarettes off-reservation. Finally, the court rejected the argument that the federal government had no place enforcing the CCTA where New York State has failed to prosecute such violations under its statute.

In *United States v. Kaid*, 2007 WL 2705574 (2d Cir.) (Sept. 12, 2007), Kaid and his co-defendants were convicted of conspiring to commit money laundering in violation of 18 U.S.C. § 1956(h) and conspiring to traffic in contraband cigarettes in violation of the Contraband Cigarettes Trafficking Act ("CCTA"), 18 U.S.C. § 2342(a). Defendants appealed, arguing that the charges should have been dismissed based on New York State's policy of not imposing its cigarette tax on non-Native Americans who purchase cigarettes on Indian reservations, and that the court erred in its calculation of tax loss. The Second Circuit held that while New York did not enforce its tax on cigarettes purchased on reservation for personal use by non-Native Americans, such forbearance does not bar prosecution of the sale of massive quantities of untaxed cigarettes to non-Native Americans for resale.

With respect to the tax loss, the court agreed that government's calculations were based on directives by the prosecutor to the government's forensic auditor that were not supported by credible evidence in the record. Because the tax loss figures impacted restitution in one case, and the Guidelines base offense level in another, the sentences were vacated and remanded.

### **31 U.S.C. § 5324 (structuring)**

In *United States v. Catherman*, 2007 WL 2790384 (S.D. Iowa) (Sept. 24, 2007), Catherman was charged with four counts of structuring financial transactions in violation of 31 U.S.C. § 5324 and one count for forfeiture of assets pursuant to 21 U.S.C. § 853(p). In each structuring count, the government alleged a series of cash deposits totaling \$275,500 over a period of approximately 2 years. The government did not allege, and concedes it can not prove, the source of these funds. Catherman moved to dismiss or alternatively, to consolidate the substantive counts, arguing that structuring can only be charged as separate counts where there are separate sources of funds. Since his funds are all from one source – a long time cash hoard – Catherman contends that the counts are multiplicitous. After reviewing authority from other circuits, the court agreed and directed the government to either elect between the four counts or consolidate.

### **SENTENCING ISSUES**

In *United States v. Delfino*, -- F.3d --, 2007 WL 4394412 (4th Cir.) (Dec. 18, 2007), the Delfinos appealed their convictions and sentences for conspiracy to defraud the United States in violation of 18 U.S.C. § 371, attempted evasion of payment of income tax in violation of 26 U.S.C. § 7201 and 18 U.S.C. § 2, and mail fraud in violation of 18 U.S.C. § 1341. Among their arguments on appeal, the Delfinos claimed that the district court incorrectly calculated their tax loss by refusing to consider reasonable, unclaimed deductions. The Delfinos relied heavily upon *United States v. Schmidt*, where the court determined that tax loss should be the actual loss in tax revenue to the IRS. 935 F.2d 1440, 1451 (4th Cir. 1991).

The Fourth Circuit noted that the definition of tax loss in U.S.S.G. § 2T1.3 was changed after the *Schmidt* opinion. Tax loss is now defined as the “total amount of the loss that was the object of the offense (*i.e.*, the loss that would have resulted had the offense been successfully completed).” *Delfino*, at \*4. As a result, the court held that *Schmidt* was no longer binding on this point of law and that the tax loss should be calculated as “the *attempted*, or *intended* loss, rather than the *actual* loss to the [G]overnment.” *Id.* (quoting *United States v. Chavin*, 316 F.3d 666, 677 (7th Cir. 2002) (emphasis in original)). The court found that the intended loss is the unpaid tax on the gross unreported income. *Id.*

The Delfinos then argued that U.S.S.G. § 2T1.1(c)(2)(A) mandates consideration of unclaimed deductions because it states that the tax loss is equal to a percentage of gross income “unless a more accurate determination of the tax loss can be made.” *Id.* at \*5. The Fourth Circuit considered the conflict in the circuits. It rejected the minority view that supported the Delfinos’ approach, set forth in *United States v. Gordon*, 291 F.3d 181, 187 (2d Cir. 2002), and instead adopted the reasoning of *United States v. Spencer*, 178 F.3d 1365, 1368 (10th Cir. 1999) (U.S.S.G. § 2T1.1(c)(2)(A) merely *allows* a court to reject the presumptive percentage if it is able to calculate a more accurate tax loss), and *Chavin*, 316 F.3d at 678 (rejecting the consideration of unclaimed deductions).

**[Author’s Note]** The facts and analysis in *Spencer* are distinguishable. *Spencer* paid employees under the table (conspiring with them to understate their tax liability) and diverted checks payable to his company to secret bank accounts under his control. *Spencer* filed returns, but failed to report the diverted checks as corporate or personal income. He was charged with filing false returns in violation of 26 U.S.C. § 7206 and conspiracy in violation of 18 U.S.C. § 371. In response to *Spencer*’s argument against a presumptive percentage, the court noted that *Spencer* had *no specific records* from which a more accurate tax loss could be determined, and to prove a more accurate figure would impose an extreme burden on the government (reviewing each employee’s returns to determine actual tax evaded). 178 F.3d at 1367-68.

The Fourth Circuit did not qualify its holding with respect to the amount or type of evidence the Delfinos attempted to submit at sentencing. It noted their lack of cooperation during the civil audit, but did not say that such cooperation would have resulted in a different holding. Instead, it stated, “nor does [the law] entitle the Delfinos to the benefit of deductions they might have claimed now that they stand convicted of tax evasion.” *Delfino*, at \*5. In reaching this decision, the court appears to eviscerate the language of § 2T1.1(c)(2)(A): “...unless a more accurate determination of the tax loss can be made.”

In *United States v. Carter*, -- F.3d --, 2007 WL 4372879 (6th Cir.) (Dec. 17, 2007), *Carter* was convicted of filing false returns in violation of 18 U.S.C. § 287 and § 2. On appeal, *Carter* objected to the sentencing enhancement imposed for obstruction pursuant to U.S.S.G. § 3C1.1. The enhancement was based on *Carter*’s false denials during the government’s investigation and his failure to appear in response to summons for fingerprints and handwriting exemplars, issued after he denied signing or filing the returns at issue. The Sixth Circuit recognized that simply making false statements to a law enforcement officer while not under oath is not obstruction (Application Note 5(b)) unless the statement is material and significantly obstructs or impedes an official investigation of the offense at issue (Application Note 4(g)). Because the government was forced to spend significant time and effort to obtain fingerprints and handwriting exemplars from another source, and because this delay played some role in the

expiration of the statute of limitations as to the 1999 tax year, the Sixth Circuit held that district court properly found that Carter's conduct warranted an obstruction enhancement.

In *United States v. Hirsch*, 2007 WL 2914214 (2d Cir.) (Oct. 5, 2007), Hirsch pled guilty to wire fraud in violation of 18 U.S.C. § 1343, and tax evasion in violation of 26 U.S.C. § 7201, and was sentenced to 37 months. The court imposed enhancements for abusing a position of trust under U.S.S.G. § 3B1.3, and for failing "to report or correctly identify the source of income exceeding \$10,000 in any year from criminal activity" under U.S.S.G. § 2T1.1(b)(1).

On appeal, Hirsch argued that the court erred in applying the enhancements. The Second Circuit rejected the contention that a position of trust requires a legally defined duty, finding that a discretionary authority entrusted to the defendant by the victim is sufficient. *Hirsch*, at \*1 (citation omitted). The victim in this case entrusted Hirsch with discretion over the victim's money, which provided Hirsch with the opportunity to commit the crime. The court further noted that Hirsch's preparation of payroll tax forms demonstrated a special skill by the use of his "knowledge of IRS procedures and tax forms to carry out a scheme of tax fraud." *Id.* (citing *United States v. Fritzon*, 979 F.2d 21, 23 (2d Cir. 1992)).

The court also rejected Hirsch's argument that the § 2T1.1(b)(1) enhancement does not apply because he did not plead guilty to failing to pay taxes on *criminal* activities. The court noted that uncharged relevant conduct may be considered for purposes of enhancements if the conduct was part of the same course of conduct, common scheme or plan as offense of conviction. *Hirsch*, at \*2. The Second Circuit held that the enhancement was warranted because Hirsch failed to report the embezzled income obtained from the fraudulent scheme.

In *United States v. Lukasik*, 2007 WL 2913876 (6th Cir.) (Oct. 3, 2007), Lukasik was involved in a fraudulent real estate investment scheme that resulted in his indictment on 86 counts, including seven counts of tax evasion in violation of 26 U.S.C. § 7201 and 18 U.S.C. § 2, and two counts of failure to pay, collect or pay over tax under 26 U.S.C. § 7202. Pursuant to his guilty plea to a single count of evasion, Lukasik agreed that the court could consider the dismissed charges as relevant conduct. He was sentenced to 46 months and appealed on numerous grounds, including that the district court miscalculated his tax loss and improperly engaged in fact-finding.

Lukasik claimed that the court erred when it included in unreported income a loan from his business partner and payments to third parties for business expenses. The court rejected this argument because Lukasik failed to produce any evidence of the loans, and while the payments to third parties may have been related to Lukasik's enterprise, the court noted that business expenses incurred in furtherance of illegal activities are not deductible.

Lukasik also argued that the amount of tax loss was a factual finding affecting the severity of his sentence and, in light of recent Supreme Court decisions in *United States v. Booker*, 543 U.S. 220 (2005), and *Blakely v. Washington*, 542 U.S. 296 (2004), should have been submitted to a jury. The Sixth Circuit disagreed, holding that as long as the district court understands that the Guidelines are merely advisory, it may find facts that determine the appropriate sentencing range.

In *United States v. Villella*, 2007 WL 2845290 (S.D.N.Y.) (Sept. 25, 2007), Villella pled guilty to one count of tax evasion in violation of 26 U.S.C. § 7201, stemming from his failure to

file returns and his conduct while associated with Save a Patriot, a tax protestor group. At sentencing, the Court noted that Villella was a family man and the primary wage-earner for his family. He had no criminal record or drug history, was formerly involved in charitable organizations, was convicted of a non-violent crime and accepted responsibility for his actions. The court noted that if Villella were able to continue working, he would be better able to pay restitution. Based on the foregoing, the court rejected the advisory Guideline range (10 to 16 months) and sentenced Villella to 60 months of probation, restitution and a \$5,000 fine.

In *United States v. Roudakov*, 239 Fed. Appx. 776, 2007 WL 2660068 (3d Cir.) (Sept. 12, 2007), Roudakov filed his 1996 and 1997 income tax returns without reporting \$541,504 and \$34,050 respectively in computer sales. A jury convicted Roudakov of two counts of willfully filing false returns in violation of 26 U.S.C. § 7206(1). The court determined the tax loss by adding the unreported income to the gross receipts reported on his tax returns, and recalculating the tax due. The resulting loss exceeded \$200,000 and supported a sentence of 24 months.

On appeal, Roudakov argued that the district court erred by not reducing his unreported income by a reasonable cost of goods sold. He argued that, using the returns he filed, the court should have applied a profit margin of 10% (not 100%). The Third Circuit disagreed. It did not hold that Roudakov was prohibited from presenting evidence of unclaimed deductions, but that he failed to present any such evidence. The Third Circuit also recognized that while Roudakov could have argued for a tax loss based on 28% of the unreported income, pursuant to U.S.S.G. § 2T1.1(c)(1)(A), which would have resulted in a lower loss, counsel did not argue that point.

## RESTITUTION

In *United States v. Rodriguez*, 2007 WL 4201353 (2d Cir.) (Nov. 29, 2007), Rodriguez pled guilty to filing a false tax return in violation of 18 U.S.C. § 287. The district court ordered restitution based on 53 related counts that were dismissed pursuant to the plea agreement. Rodriguez appealed, arguing that under *Hughey v. United States*, 495 U.S. 411 (1990), restitution was limited by the loss caused by the conduct supporting the offense of conviction. The Second Circuit agreed, but noted that Rodriguez allowed the government to go beyond the offense of conviction by the language in his plea agreement.

Rodriguez further argued that restitution should be limited to the amount of each refund that Rodriguez retained, and should not include the portion of the refund received by his clients and to which they were legally entitled. At sentencing, the district court found that the IRS had “unfiled” the returns submitted by Rodriguez “because the individuals never filed the tax returns for the tax figures in which [Rodriguez] prepared and submitted the claims.” *Id.* at \*1. The Second Circuit vacated the restitution order and remanded to determine if credit should be given for amounts received by Rodriguez’s clients. The Second Circuit noted that, “[t]he restitution amount must not provide the IRS with a double recovery from both Rodriguez and his taxpayer clients. The district court may wish to consider whether Rodriguez’s clients have subsequently filed for a refund for the tax years in question and, if they have not, whether they can still file for a refund at this late date.” *Id.* at \*2.

## FORFEITURES

In *United States v. Fleet*, 498 F.3d 1225 (11th Cir.) (Sept. 5, 2007), Fleet was convicted of numerous counts, including money laundering in violation of 18 U.S.C. § 1957, stemming from his participation in a fraudulent land swap deal. The government sought forfeiture under § 982(a)(1) and § 982(b)(1), which incorporates 21 U.S.C. § 853, the criminal forfeiture statute, and noted in the indictment that it would seek forfeiture of substitute property if necessary. When Fleet's cash was insufficient to satisfy the preliminary order of forfeiture, the government asked the district court to order forfeiture of Fleet's interest in property subject to Florida's homestead exemption and property held as tenancy by the entirety. Fleet argued that the substitute property provision of § 853(p) did not preempt state law.

The Eleventh Circuit acknowledged that § 853(p) conspicuously omits the express preemption clause found in the § 853(a). However, the court recognized that preemption could be implied, and noted the broad scope of the statute, which provides that "the court shall order the forfeiture of any other property of the defendant." 498 F.3d at 1229 (quoting § 853(p)(2)). The court considered and rejected the reasoning of the Seventh Circuit in *United States v. Lee*, 232 F.3d 556 (7th Cir. 2000), where the court held that tenancy by the entirety property was not subject to forfeiture under § 853(p). Finally, the Eleventh Circuit noted the difference between civil forfeitures, which are *in rem* and recognize an innocent owner defense, and a criminal forfeiture, which does not provide for an innocent owner defense and acts *in personam* against only the property interests of the person who commits the criminal conduct. The court held that with respect to the forfeiture of substitute property, § 853(p) preempts the Florida homestead exemption and tenancy by the entirety laws and therefore, the government could seek forfeiture of Fleet's interest in such properties.

## MISCELLANEOUS

**(trial time limits)** In *United States v. Cousar*, 2007 WL 4456798 (W.D. Pa.) (Dec. 16, 2007), the defendants were indicted on 39 counts of mail fraud in violation of 18 U.S.C. § 1341 and § 2, fraud against the government in violation of 18 U.S.C. § 1031 and § 2, and conspiracy to defraud in connection with three construction projects in violation of 18 U.S.C. § 371. During a pre-trial conference, the government claimed that it required five weeks to present its case-in-chief. After an *in camera* review of an *ex parte* memorandum outlining the Government's expected testimony, the Court determined that the majority of the testimony was cumulative. Citing various policy concerns, authority in other circuits and Fed.R.Evid. 611(a), the court extended to criminal trials the Third Circuit's precedent of permitting time limits in civil trials. The court limited the government's case to 40 hours, commencing with opening statement, including direct and cross examinations, requests for side bar conference and closing arguments. The defendants' were allowed 12 hours each, using the same parameters.

**(limitations)** In *United States v. Bordewick*, 2007 WL 4287333 (N.D. Cal.) (Dec. 5, 2007), Bordewick was indicted on nine counts of mail fraud in violation of 18 U.S.C. § 1341 and one count of corruptly interfering with the administration of tax laws in violation of 26 U.S.C. § 7212(a). The initial indictment read as follows:

[Bordewick] knowingly and intentionally devised and intended to devise a scheme and artifice to defraud the IRS and to obtain at least \$44,000 by means of

false and fraudulent pretenses, representations, and promises, well knowing that the pretenses, representations and promises were false and fraudulent when made.

*Bordewick*, at \*1. Almost 20 months later, a superseding indictment was returned that consolidated the mail fraud charges into a single count (because there were nine checks but a single mailing) and modified the language of the indictment to read:

[*Bordewick*] knowingly and intentionally devised and intended to devise a scheme and artifice to defraud the IRS and to obtain at least \$44,000 by means of *material* false and fraudulent pretenses, representations, and promises, well knowing that the pretenses, representations and promises were false and fraudulent when made, *and well knowing that the false and fraudulent pretenses, representations and promises were material in that they would reasonably influence Orange Coast Title Company to not pay the IRS demand for taxes in the amount of \$87,251.30, but instead to pay the balance of the proceeds from the sale of the condominium, approximately \$44,000, to his friend, Robert Morrison.* (Italics added to indicate text not found in original indictment.)

*Id.* at \*2. *Bordewick* challenged the superseding indictment by claiming that it was time barred or, in the alternative, that it was duplicitous.

The district court noted that, “a fraud indictment’s failure to recite an essential element of the charged offense, namely the materiality of the scheme or artifice to defraud, is a fatal flaw requiring dismissal of the indictment.” *Id.* at \*3 (citing *United States v. Omer*, 395 F.3d 1087, 1089 (9th Cir. 2005)). *Bordewick* claimed that such a fatal flaw in the original indictment meant that the statute of limitations for mail fraud was not tolled and the superseding indictment was time barred. The court distinguished *Omer*, noting that it involved a dismissal of a flawed indictment, not the relation-back of charges in a subsequent indictment. *Id.* It held that since “materiality is a necessary component” of a mail fraud charge, *Bordewick* had notice of materiality and the superseding indictment related back for purposes of limitations. *Id.*

**(joinder)** In *United States v. Nicolo*, -- F. Supp. 2d --, 2007 WL 4191722 (W.D.N.Y.) (Nov. 27, 2007), four defendants, including Constance Roeder, were charged with multiple offenses all related to an alleged scheme to defraud various companies, including Eastman Kodak Company (“Kodak”), and the Town of Greece, New York (“Greece”). Roeder moved for severance, arguing that her tax charges were not properly joined with the non-tax counts against the other defendants under Rule 8 of the Federal Rules of Criminal Procedure.

For a tax count to be joined with a non-tax count, the tax offense must be directly linked to the non-tax crime. *Nicolo*, at \*17. Here, the court found that the tax conspiracy count against Roeder was directly related to the fraud counts against the other defendants because the government alleged that Roeder conspired to evade tax on proceeds from the fraudulent schemes. The court further found that the charges of filing false returns in violation of 26 U.S.C. § 7206(1) were directly related to the tax conspiracy count, and therefore “all the tax charges against Roeder ‘arose directly from the other offenses charged’ in the indictment.” *Id.* at \*18 (quoting *United States v. Turoff*, 853 F.2d 1037, 1043 (2d Cir. 1988)). Finally, the court rejected Roeder’s argument of prejudicial joinder under Rule 14(a), finding that any such prejudice could be overcome with appropriate instructions. The motion to sever was denied.

**(joinder)** In *United States v. Shellef*, 507 F.3d 82 (2d Cir.) (Nov. 8, 2007), Shellef and Rubenstein were in the business of buying and selling industrial, ozone-depleting chemicals (CFC-113) that were subject to an excise tax under 26 U.S.C. § 4681(a)(1) and § 4682(a)(2). An exception to the excise tax applies if the CFC-113 is diverted or recovered as part of a recycling process, or if the sale is ultimately for export. To be eligible for the exception, purchasers must satisfy certain procedural requirements. The government alleged that Shellef and Rubenstein conspired to evade the payment of excise taxes by misrepresenting to CFC-113 sellers that their purchases were for export, and for misrepresenting to buyers that the CFC-113 was recycled. The government further alleged that Shellef failed to report proceeds from CFC-113 sales on his corporate return for 1996, failed to report income on his personal return for 1996, and failed to report income from CFC-113 sales on his corporate return for 1999.

Shellef and Rubenstein were charged with conspiring to impede the collection of excise tax in violation of 18 U.S.C. § 371 and 46 counts of wire fraud in violation of 18 U.S.C. § 1343 based on their false promises to CFC-113 manufacturers. Shellef was also charged with false statement in violation of 26 U.S.C. § 7206(1) for his 1996 corporate return, tax evasion in violation of 26 U.S.C. § 7201 for his 1996 personal return, and false statement (again, § 7206(1)) for his 1999 corporate return. Finally, Shellef was charged with 41 counts of money laundering and wire fraud in violation of 18 U.S.C. § 1956.

Prior to trial, Shellef and Rubenstein moved to sever all tax counts from the other counts pursuant to Fed. R. Crim. P. 8. The district court denied the motion, and the defendants were convicted on all counts. Various arguments were raised on appeal, including misjoinder of the tax counts with the non-tax counts and misjoinder of the defendants.

The Second Circuit noted that Rule 8(a) allows joinder of offenses that are of the same or similar character, while Rule 8(b) requires that, to join defendants, the government must allege that they participated in the same act(s) or transaction(s). The government argued that the 1996 tax charge was based on the same acts or transactions as the other charges, and that all of the charges are related to the sales of CFC-113. In applying what it called the “commonsense rule,” 507 F.3d at 98, the court found that the 1996 tax count could be properly jointed with the 1999 tax count based on Shellef’s continuing relationship with the same accounting firm, and that the 1999 tax count was connected to the non-tax counts because it arose out of the funds generated by the wire fraud, money laundering, and conspiracy schemes. However, since the 1996 tax count involved unreported income earned prior to the commencement of the conspiracy and in light of the numerous elements related to the 1999 tax count and non-tax charges that are *unrelated* to the 1996 tax count, the Second Circuit held that joinder of the 1996 tax count was improper. *Id.* at 100. The court further held that the misjoinder was not harmless error and therefore, vacated the convictions on all counts for both defendants. Despite this finding, the Second Circuit addressed other issues raised on appeal to provide guidance to the district court on remand. In the interest of brevity, we simply commend that portion of the opinion for your review.

**(jeopardy levy on legal defense funds)** *United States v. Thomas*, -- F. Supp. 2d --, 2007 WL 4180827 (D. Me.) (Nov. 21, 2007), Thomas was indicted on six counts of tax evasion under 26 U.S.C. § 7201. Prior to trial, the IRS issued a jeopardy levy against a trust fund from which Thomas was paying living expenses and legal fees. Thomas moved to dismiss the indictment, claiming that the levy was a “deliberate and outrageous” violation of his Sixth Amendment right to counsel because it eliminated his ability to retain chosen counsel, which in turn violated his

Fifth Amendment due process rights. The court noted that a dismissal based on prosecutorial misconduct required a finding that the defendant was prejudiced by such misconduct. *Id.* at \*3 (citing *Bank of Nova Scotia v. United States*, 487 U.S. 250, 263 (1988)). The court found no prejudice against Thomas because his counsel had not yet asked to withdraw, the court had granted prior requests for funds to aid in Thomas' defense, and the court was unable to assume future problems or issue advisory rulings.

**(tax protestors)** In *United States v. Patridge*, 507 F.3d 1092 (7th Cir.) (Nov. 14, 2007), Patridge was a tax protestor who used offshore trusts to conceal income. He either failed to file returns or filed false returns, which were later audited. When he failed to pay the assessments, the IRS issued a Final Notice of Intent to Levy and Patridge appealed to dispute liability. While the civil proceedings developed, Patridge was indicted and convicted for tax evasion, money laundering and wire fraud. Patridge appealed the conviction and raised classic protestor arguments. The Seventh Circuit addressed and rejected each argument as frivolous. In response to Patridge's argument regarding the Paperwork Reduction Act of 1980, Judge Easterbrook took the opportunity to analyze the argument and reiterate the Circuit's holding in *Salberg v. United States*, 969 F.2d 379 (7th Cir. 1992), that "the obligation to file a tax return stems from 26 U.S.C. § 7203, not from any agency's demand". *Patridge*, at \*3. The court also severely chastised Patridge's counsel, Jerold W. Barringer, calling into question his ability to practice law and condemning his disdain for the norms of legal practice and rules of procedure. The Court concluded with an order giving Barringer fourteen days to show cause why he shouldn't be fined \$10,000 and suspended from practice.

**(removal proceedings)** In *Kawashima v. Gonzales*, 503 F.3d 997 (9th Cir.) (Sept. 18, 2007), Mr. and Mrs. Kawashima, Japanese citizens and legal residents of the United States, were convicted in 1997 of filing a false return in violation of 26 U.S.C. § 7206(1), and aiding and assisting in the preparation of a false tax return in violation of 26 U.S.C. § 7206(2), respectively. In 2001, the Immigration and Naturalization Service (INS) successfully sought removal of the Kawashimas on the grounds that their convictions were aggravated felonies under 8 U.S.C. § 1101(a)(43)(M)(i)-(ii) ("subsection M"). On appeal, the Kawashimas argued that their convictions did not meet the statutory definition of aggravated felony.

As a preliminary matter, the Ninth Circuit addressed the issue of whether any tax offenses may qualify as an aggravated felony under subsection (M)(i), or if subsection (M)(ii)'s specific reference to 26 U.S.C. § 7201 implies that other tax offenses are not considered aggravated felonies. In *Ki Se Lee v. Ashcroft*, 368 F.3d 218, 223 (3d Cir. 2004), the Third Circuit concluded that if tax offenses were included under subsection (M)(i), then subsection (M)(ii) would become superfluous. Then-Judge (now Justice) Alito wrote in dissent and concluded that the plain language of the statute did not preclude the inclusion of other tax offenses under subsection (M)(i). The Ninth Circuit agreed with Judge Alito's dissent and held that Mr. Kawashima's conviction under 26 U.S.C. § 7206 could be a removable offense.

The Court next applied the two-step test set forth in *Taylor v. United States*, 495 U.S. 575 (1990), to determine if the Kawashimas' convictions met the aggravated felony definition under subsection (M)(i). First, the court compared the elements of the statute of conviction to the definition of aggravated felony in 8 U.S.C. § 1101(a)(43) to determine if the full range of conduct included in the relevant statute is covered. If the statute of conviction is broader than the definition of an aggravated felony, then the court must look to the record of conviction to determine if the defendant was convicted of the elements of the generically defined crime under

subsection (M)(i). Using this framework, the court determined that the conduct included within § 7206(1) and (2) was broader than the definition in 8 U.S.C. § 1101(a)(43) and therefore, looked to the Kawashimas' records of conviction.

Subsection (M)(i) requires that the offense at issue involve fraud or deceit and that the loss to the victim exceed \$10,000. The Court found that both convictions necessarily involved "fraud or deceit," and that Mr. Kawashima's record of conviction established a loss to the victim (the government) of more than \$10,000. Thus, his order of removal was affirmed. On the other hand, Mrs. Kawashima's record of conviction failed to allege a tax loss in excess of \$10,000 and therefore, her order of removal was vacated.