

It is 8:35 a.m., and you are the first person to arrive at the office. The first pot of coffee has been brewed. You are ready to take your first sip when the phone rings. On the line is the president of your firm's best corporate client. In the most anxious of voices, he blurts out, "the IRS is at my house and wants to ask me questions. What should I do?" Your heart flutters. You think to yourself, "I am a general practitioner, not a criminal tax lawyer." But, the Internal Revenue Service (IRS) is at your client's home rather than his office (a bit unusual to say the least), it is early, and no other lawyers have arrived at your office yet. There's no avoiding it . . . you must say something to your

client, and you must say it now.

First, determine why the agents are standing on your client's doorstep. You must ask: "How many of them are there?" If your client's answer is "Two," he has real problems, and you may have a juicy case. Special Agents of the Criminal Investigation Division (CID) of the IRS are law enforcement officers who always work in pairs. Thus, if there are two of them, the great likelihood is that the agents at your client's house are conducting a criminal tax investigation.

Next, you must instruct your client to say *absolutely nothing* to the agents beyond requesting their business cards and advising them that his lawyer will call them. If your client takes these steps, you — not the agents — can control the nature and extent of any information your client provides the government.

IRS WANTS YOU



TAX MAN COMETH

By Lawrence S. Horn

Often, however, you (and your client) will not be so fortunate. Instead of receiving a phone call at the outset of the government contact, your client will call you after the agents have already left his home. The following dialogue then takes place:

Lawyer: "Did you tell them anything?"

Client: "Of course not."

Lawyer: "How long were they at your house?"

Client: "Two hours."

Regrettably, the above scenario occurs hundreds of times each year. But, whether you learn of the government's

visit after the agents have left or before they've stepped through your client's front door, you must know how the IRS is organized, and how each division functions, if you are to provide your client with the effective assistance of counsel.

The nature and severity of your client's problem with the IRS may be determined in part by identifying which IRS division has dispatched its agent(s) to his home. For purposes of this article, the IRS consists of three divisions: the Criminal Investigation Division, the Examination Division and the Collection Division. Each of these divisions has a distinct role in the IRS structure

and the ramifications of the inquiry will vary widely depending upon which division is conducting the inquiry. I will discuss each in turn.

Criminal Investigation Division

The Criminal Investigation Division (formerly known as the Intelligence Division) investigates suspected violations of the criminal tax laws — including attempted tax evasion, the filing of false or fraudulent returns, the willful failure to file returns, currency reporting violations and money laundering. CID's investigations can take the form of either administrative or grand jury inquiries. For purposes of this discussion, assume that the IRS is conducting an administrative investigation into the accuracy of your client's tax returns rather than working with an Assistant

U.S. Attorney (AUSA) as part of a Title 26 tax grand jury investigation.

Unlike agents from other division of the IRS, special agents from the Criminal Investigation Division have no interest in assessing or collecting tax deficiencies. CID special agents are law enforcement officers who always work in pairs. They are interested only in developing evidence that will sustain a criminal prosecution. Consequently, the filing of amended or delinquent returns will not deter an investigation by this division. Indeed, such returns will often be used in the subsequent prosecution of your client as affirmative admissions of false filing or non-filing.

In keeping with the division's goal of building criminal cases, often your client's first contact with CID will be an unannounced visit by its special agents. The agents' primary intent during this initial visit will be to extract damaging statements from your client. And, if history is any guide, the agents will likely be successful. Though special agents typically advise taxpayers of their constitutional rights (*i.e.*, give *Miranda-type* warnings), experience demonstrates that taxpayers are often so flustered or cavalier that they try — usually unsuccessfully — to talk themselves out of any problem. These efforts often cause the taxpayers to make incriminating statements or false exculpatory statements. Both are damaging.

The government has the burden of proving crimes beyond a reasonable doubt. Why help them in any way? Why give uncounseled responses about events which took place years ago, without the opportunity of reviewing documents and refreshing recollections? Unfortunately, that's often the situation with which you will be dealing if your client calls you after-the-fact.

Examination Division

The Examination Division (formerly known as the Audit Division) audits filed returns to determine whether additional tax, interest, or civil penalties should be assessed. The Examination Division also reviews returns to determine whether an overpayment has been made.

Officers of the Examination Division are known as revenue agents. Revenue agents typically begin an audit by sending the taxpayer a letter that (1) advises him or her that a forthcoming audit has been scheduled, (2) identifies which years and returns will be under examination, and (3) identifies particu-

lar items on those returns that require substantiation or documentation. It is important to note that barring unusual circumstances, a revenue agent conducting a routine audit will usually *not* begin his examination with an unannounced visit to your client's home. Rather, the audit notification letter is, by and large, the exclusive method of announcing Examination Division investigations. Contrasting the notification practices of the Examination Division with those of CID, it is clear that the method of contact used by the IRS will often give you some indication of whether a routine audit or a more serious inquiry is contemplated. However, one important footnote to this rule, which arises in the context of the third branch of the IRS — the Collection Division — is discussed below.

Collection Division

The Collection Division has three primary purposes: (1) the collection of delinquent income and payroll taxes, (2) the collection of delinquent tax returns, and (3) the collection of tax deficiencies previously assessed by the Examination Division. The agents of the Collection Division that undertake these tasks are known as revenue officers.

Your client's first indication that the Collection Division is working a case against him (or her) may be when a revenue officer shows up at the front door. Like CID special agents, revenue officers often begin cases with unannounced visits. However, unlike special agents, revenue officers normally do not travel in pairs. Thus, while the *fact* of a visit may distinguish between investigations by CID and the Examination Division, it is the *number* of agents making a visit that will help clarify whether your client faces a collection problem or a criminal inquiry.

Revenue officers can appear at your client's doorstep armed with considerable authority. They can seize assets and levy against bank accounts. Revenue officers also can assess a one hundred percent penalty on individuals because of an employer's payroll tax delinquencies. The unbridled authority and discretion that many revenue officers possess requires that they must be dealt with properly and (on occasion) gingerly.

Prudence and discretion

At the outset, whether your client faces a criminal investigation, an audit or collection activity, you must convince your client to keep his distance from the IRS agent(s). Prudence and discretion

are your only guarantees against intentional or unintentionally false or inaccurate statements. Consequently, you should not permit your client to engage in conversation or offer explanations to the agent(s). Remember: you and your client are on the agent's playing field, not yours. The agent knows what information is needed to build the government's case. Thus, a seemingly innocuous statement may actually be a damning admission, depending upon the method of proof employed by the agent to reconstruct your client's income.

Early caution provides you with extra time to prepare your strategy for dealing with the IRS. Only after conferring with your client, and then the agent, can a decision be made as to the nature and sensitivity of the problem, and only then can a decision be made as to the strategy that should be employed.

It is now 10:30 a.m., and your client has followed your advice. He obtained the business cards of the two special agents (indicating a criminal investigation) and declined to answer any questions. He is now in your office. Once again, you must decide what to do.

First, if your client arrives with his accountant, instruct the accountant to remain in the waiting room. While the attorney/client privilege is widely recognized, there is *no* federal accountant/client privilege if the IRS is conducting a criminal investigation. This is not to say, however, that an accountant's work product can never be subject to privilege. The interviews and work papers of an accountant prepared by him *after retention by an attorney* to assist in the defense of a criminal tax case (*Kovel* accountants) are protected by the attorney/client privilege.¹ But, the accountant retained for these purposes should *not* be the same accountant who prepared the returns in question, for this individual will likely be a fact witness subject to interview by the agents. In fact, the IRS often sends pairs of agents to interview both your client and your client's accountant simultaneously.

Next, you must ensure that the special agents do not make another attempt to meet or speak with your client. Remember, this is a criminal investigation that just happens to focus on tax returns or tax-related issues. It should be handled like any other criminal case. Hence, the Fifth Amendment may be your client's best and only ally.

One foolproof way to prevent the special agents from communicating

directly with your client is to have your client complete an IRS Power of Attorney (Form 2848), which names you as the legal representative. This form serves two important purposes. First, it authorizes the agents to speak to you about your client without violating IRS disclosure provisions. Second, it forces the IRS to communicate with you, the legal representative, rather than your client. Absent a valid Form 2848, the special agents conducting the administrative investigation (as distinguished from a Title 26 tax grand jury investigation) cannot divulge any information to you regarding your client's case. It also bears mention that caution should be exercised once the special agent is given the Power of Attorney Form 2848 appointing you spokesperson. As your client's representative, you speak for your client and thus should be wary of making any vicarious admissions. See Fed. R. Evid. 801(d)(2)(C).

When you submit the Form 2848, you should include a letter to the special agent. This letter should contain specific requests regarding future contacts and the service of summonses. In addition, the letter should request a final conference with CID prior to any referral being made to the Tax Division of the U.S. Department of Justice.²

The special agent's goal is to develop sufficient evidence to author a Special Agent's Report (SAR) recommending prosecution. The agent develops the evidence by interviewing witnesses and reviewing documents. The administrative summons is the vehicle by which the special agent compels testimony and document production. It is the functional equivalent of a personal grand jury subpoena. The statutory language authorizing administrative summonses states, in relevant part,

For the purpose of ascertaining the correctness of any return, . . . [or] determining the liability of any person for any internal revenue tax . . . the Secretary [of the Treasury or his designee] is authorized –

(1) To examine any books, papers, records . . . which may be relevant or material to such inquiry;

(2) To summon . . . any . . . person the Secretary may deem proper . . . and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.³

Issued in good faith

If a person or entity does not comply with an authorized summons, the IRS can seek enforcement in the United States District Court. See 26 U.S.C. § 7604. Indeed, judges routinely grant applications to enforce IRS summonses, for the standards of enforcement are easily met by the government. To justify enforcement, the government need only demonstrate that the summons was issued in good faith. This means simply that the IRS must show that (1) the investigation will be conducted for a legitimate purpose; (2) the inquiry may be relevant to this purpose;⁴ (3) the information sought is not already in the Commissioner's possession; (4) the administrative steps required by the Internal Revenue Code have been followed; and (5) no referral to the Department of Justice has yet been made recommending the initiation of a grand jury investigation or prosecution. If these five elements are established, the summons will be enforced.⁵

One other issue with regard to the issuance of summonses concerns those served upon your client's return preparer or accountant. More often than not, the accountant who prepared the returns in question will be a critical government witness in a tax evasion or false filing investigation. When the special agent issues a summons to compel the appearance of the return preparer and the production of his file, including work papers and retained copies of returns, the summons must be issued in accordance with the requirements of 26 U.S.C. § 7609. This Section governs summonses issued to "third-party record keepers," including banks, consumer reporting agencies, credit card companies, brokers, lawyers and accountants. Section 7609 requires that a copy of any summons issued to a third-party record keeper be mailed to the person whose records are being summoned (usually your client). This person then has the right to initiate an action in U.S. District Court to quash the summons within 20 days of receipt. Unfortunately for taxpayers, motions to quash are rarely, if ever, granted.

Best witness

The special agent hopes that the return preparer will be his best witness by furnishing testimony that questionable information contained on the return is strictly the result of items and amounts provided by the taxpayer. The special agent further hopes to garner testimony from the return preparer that any

omissions or understatements on the return are the result of information that the taxpayer withheld. For a variety of reasons, the special agent's hopes are often realized. For example, the return preparer is typically frightened or intimidated by the presence of the special agents.

In addition, return preparers are commonly concerned that their conduct in preparing the returns may come under scrutiny. For these reasons, consideration should be given to retaining an attorney to represent the return preparer. This will help ensure that truthful testimony is obtained. Moreover, it will help to safeguard against the return preparer becoming subject to implied threats or coercion as to the consequences of providing the special agent with less than "cooperative" testimony, *i.e.*, exculpatory statements or confessions of negligence or mistake.

The special agent always asks the attorney for the target-taxpayer if he is going to cooperate. However, cooperation means different things to different people. Cooperation, according to the special agent, likely means submitting to a recorded interview under oath. Unless the case is a "slam dunk" and the taxpayer wants heavenly absolution for his sins, cooperation (as defined by the special agent) is anathema to experienced defense counsel.

The special agent usually issues a summons to the taxpayer for the production of his business records. If the taxpayer-target conducts his business as a sole proprietorship, the invocation of the Fifth Amendment may shield him from producing those critical documents. However, if he conducts his business affairs as a partnership or corporation, the Fifth Amendment will offer protection from the production of business records only in very limited circumstances.⁶

At the conclusion of the special agent's investigation, he or she will prepare the SAR. If the agent concludes that there is insufficient evidence for prosecution, a "d.i." (discontinued investigation) report will be prepared. If the special agent recommends that the case be prosecuted, the attorney for the target-taxpayer should attend a formal conference with the special agent and his group manager. As stated earlier, no conference will be granted unless one is requested. That conference can be a valuable learning experience. You will learn, at the very least, the years for which prosecution will be recommended, the statutes alleged to be violated,

the method of proof and the amount of the alleged civil tax deficiencies. However, counsel must exercise caution and not make specific factual assertions on behalf of his client because of the vicarious admission problem associated with the IRS Power of Attorney Form 2848.

The review procedure for administratively investigated tax crimes distinguishes them from other federal criminal cases. Prior to the year 2000 restructuring, every criminal tax case moved along a three-tiered review track. After the Chief of CID approved the SAR, the case file moved to the local IRS District Counsel's office. The District Counsel is the legal advisor to the IRS in the local area. A docket attorney from District Counsel reviewed the case file for legal sufficiency, but conducted no independent investigation. The attorney then determined whether there was (1) a *prima facie* case and (2) a reasonable likelihood of a conviction. If the answer to both these determinations was yes, District Counsel sent a Criminal Reference Letter (CRL) to the Tax Division of the Department of Justice (DOJ-Tax). If District Counsel concluded on legal or factual grounds that either of the two criteria was not present, a Criminal Action Memorandum (CAM) was prepared and forwarded to DOJ-Tax.

Prior to the year 2000 restructuring, counsel for the taxpayer was also offered a conference with District Counsel as a matter of course. The information available and scope of the conference were, however, limited. For example, the conference was not the place to discuss plea bargaining or to address disputed factual or evidentiary issues unless they were glaring. Similarly, the IRS typically said very little about the facts of its case and usually took a 'sit back and listen' posture. Likewise, civil resolution of the case was never discussed. In fact, civil resolution is *never* a bargaining point at any level in the criminal review process. Once again, the vicarious admission rule applied. However, if your defense to a case was technical (e.g., errors in calculating the tax impact of a transaction or lack of a proper starting point for an IRS net worth reconstruction of your client's income) or based on IRS policy grounds, the best place to raise it was at the District Counsel level.

Since restructuring, the review process has been somewhat streamlined. The most significant change is District Counsel's earlier involvement in

the process. Now, instead of receiving the case after CID has completed its investigation, an attorney from District Counsel's office is assigned to each case *along with* the special agent-in-charge (SAIC). District Counsel is, thus, closely involved in a concurrent review and investigation of the case. The referral of the case to the Tax Division is then made directly by the SAIC, and District Counsel's assessment of the case is memorialized in a letter that becomes part of the package forwarded to the Tax Division. The conversion to this new review process is effective immediately. Thus, referrals to the Tax Division are now made exclusively by CID.

The next level of review for an administratively-investigated criminal tax case is by the Criminal Enforcement Section of the DOJ Tax Division in Washington, D.C. When cases arrive in the Criminal Enforcement Section, a determination is quickly made to classify each case as complex or non-complex. Any case for which a conference is requested is classified as complex. Because the classification is made quickly and because simple cases are reviewed in approximately two weeks, it is important to request a conference while the case is still being reviewed by

the IRS.⁷ The importance of drafting the letter before the case even arrives in DOJ-Tax is that unless a "when and if" letter is written, the case may already have been reviewed by the time your letter is received, and you will have missed your opportunity to confer with the attorneys reviewing the case.

Tax Division

The vicarious admission rule does not apply at the Tax Division. Tax Division attorneys are trial lawyers as well as reviewers. They are generally far more sensitive to trial problems and credibility issues than lawyers in the District Counsel office (who generally do not practice in U.S. District Courts). Tax Division attorneys apply the same standards of review as District Counsel — *prima facie* case? Reasonable likelihood of a conviction? If the Tax Division concludes that these criteria are present, it will forward the case to the United States Attorney's office in the appropriate district with an instruction to initiate prosecution. It will also provide the United States Attorney with instructions on what count or counts guilty pleas should be tendered if plea negotiations take place. The Tax Division has a "major count" policy

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which governs plea negotiations in all criminal tax cases.

In the event the Tax Division is uncertain that the two criteria are present, it can authorize the United States Attorney to conduct a grand jury investigation in order to determine whether the case is worthy of prosecution. Oftentimes, the direction to conduct a grand jury investigation is prompted by defense counsel's comments during the Tax Division conference which highlight infirmities that may exist with the credibility of a witness or other aspects of the case.

Once the case has been sent to the United States Attorney's Office by the Tax Division for the initiation of prosecution, prosecution cannot be unilaterally declined by the United States Attorney. A memorandum must be sent back to the Tax Division setting forth reasons why the case should be declined. If the Tax Division disagrees and does not change its recommendation, it can send its staff attorneys to the district to prosecute the case on their own.

Finally, the local AUSA handling your client's case typically does not handle tax prosecutions full time or have a complete knowledge of the IRS or its procedures unless the district in which

you practice is a very large one. Also, typically the AUSA will not be a technical tax expert and will rely heavily on what the IRS agents who investigated the case tell him or her about technical matters. But remember, the AUSA who will ultimately represent the government at trial is the person most sensitive to factual or evidentiary problems which may impair a successful prosecution.

Notes

1. United States v. Kovel, 296 F.2d 918 (2d Cir. 1961).

2. Internal Revenue Service
Criminal Investigation Division
Post Office Box 741
Springfield, New Jersey 07081-0741

ATTENTION: Special Agent Skip Cashdollar

RE: Tom Taxpayer

Dear Mr. Cashdollar:

The above named law firm represents Tom Taxpayer. I enclose a copy of a Power of Attorney (Form 2848) evidencing same.

All contacts relating to this taxpayer should be made through me at this office. Please send copies of all summonses required to be served on the taxpayer pursuant to § 7609 of the Internal Revenue Code to me at the above address, as well as all other summonses issued in this case.

Please provide me with a copy of the memoranda of interview prepared by you or other agents after your meeting with Mr. Taxpayer on or about June 1, 2002.

Please telephone me at your earliest convenience so we may arrange for a mutually convenient time and place to meet in order to discuss your investigation.

Pursuant to the provisions of § 9356.1(1) of the Internal Revenue Manual, the undersigned hereby respectfully requests an opportunity for a final conference in the Criminal Investigation Division prior to any recommendation for consideration of criminal prosecution.

Very truly yours,

LAWRENCE S. HORN

3. See 26 U.S.C. § 7602.

4. Courts construe the term "relevant" very broadly.

5. See 26 U.S.C. §§ 7602, 7604 and United States v. LaSalle National Bank, 437

U.S. 298, 313 (1978).

6. *Braswell v. United States*, 487 U.S. 99 (1988); *United States v. Doe*, 465 U.S. 605 (1984).

7. Rosemary Paguni, Chief
Northern Criminal Enforcement Section
Tax Division
United States Department of Justice
Washington, D.C. 20530

Re: Tom Taxpayer

Dear Ms. Paguni:

I represent the above named taxpayer who is the subject of an investigation being conducted by the Criminal Investigation Division of the Internal Revenue Service in Springfield, New Jersey. In the event a case concerning Mr. Taxpayer is forwarded to you with a recommendation for prosecution, I request an opportunity to have a conference with a member of your section prior to your taking any action.

Please acknowledge receipt of this letter.

Thank you for your courtesies.

Very truly yours,

LAWRENCE S. HORN ■

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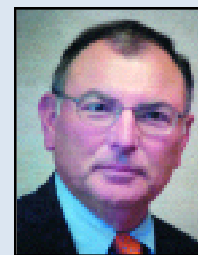
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About the Author

Lawrence S. Horn received his B.A. from



Princeton University and his J.D. from New York University. From 1971 to 1978 he was an Assistant United States Attorney (AUSA) for the District of New Jersey where he specialized in tax fraud prosecutions. He is with the firm of Sills Cummis Radin Tischman Epstein & Gross, PC Certified as a criminal defense attorney of the State of New Jersey, and a member of the American College of Tax Counsel, his practice places a special emphasis on criminal tax investigations and trials. He is an NACDL Life Member.

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