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From:
Sent: Friday, March 27, 2009 4:00 PM
To:
Cc:
Subject: RE: Question for you

Per my voicemail…

In *Cheek*, the Supreme Court clarified prior decisions in *United States v. Bishop*, 412 U.S. 246 (1973) and *United States v. Pomponio* 429 U.S. 10 (1976), stating that willfulness is the "voluntary, intentional violation of a known legal duty."

Willfulness Article.doc (43 KB...

Attachment:

Proof of Willfulness

Often, a criminal tax case turns on the taxpayer's "mens rea," intent, or motive. In the criminal tax world, a taxpayer's criminal intent is referred to as "willfulness." Willfulness must be proven beyond a reasonable doubt in each criminal tax case and may make prosecution of criminal tax cases more difficult than other types of criminal prosecution. Generally, ignorance of criminal laws is not a defense to prosecution. *Reynolds v. United States*, 98 U.S. 145, 167 (1879). However, in 1933 the Supreme Court set criminal tax laws apart from other criminal statutes by providing that ignorance of the law is a defense to a criminal tax prosecution. *See United States v. Murdock*, 290 U.S.

389, 396 (1933). Allowing ignorance of the law as a defense to criminal tax prosecution is due in large part to the complexity of the tax laws. *Cheek v. United States,* 498 U.S. 192, 200 (1991). Since then courts have required the prosecution to demonstrate that the defendant was aware of the tax laws. Until 1991, courts stated the standard for willfulness in a variety of ways, generally including a "bad faith" or "evil motive" element. In *Cheek*, the Supreme Court clarified prior decisions in *United States v. Bishop*, 412 U.S. 246 (1973) and *United States v. Pomponio* 429 U.S. 10 (1976), stating that willfulness is the "voluntary, intentional violation of a known legal duty."

Cheek

Cheek, an airline pilot, who had repeatedly failed to file income tax returns and progressively lowered the amount of money withheld from his wages, argued at trial that the Sixteenth Amendment does not authorize a tax on wages. The Supreme Court recognized that the argument was frivolous. *Cheek* at 205-206. However, Cheek also argued that a good-faith misunderstanding of the law or a good-faith belief that one is not violating the law is a defense to willfulness. In the end, along with setting the willfulness standard as a "voluntary, intentional violation of a known legal duty," the Supreme Court also made it clear that whether the defendant has a good faith belief that he is not violating tax statutes is subjective and a question for the jury. In other words, even if the defendant puts forth patently frivolous arguments, as Cheek did, the jury is required to determine whether the defendant has a good faith belief that he was not violating the tax laws. The Supreme Court noted though, the more unreasonable the misunderstandings or arguments are, the more likely a jury will find them to be simple disagreements with a known legal duty. *Cheek* at 204-205. Therefore, since *Cheek*, the prosecution has been required to show proof that the defendant was aware of the Internal Revenue Code ("IRC") requirements and voluntarily and intentionally violated the requirements; and the jury must evaluate any good faith belief argument asserted by the defendant.

Cryer* and *Kuglin

In the *Cheek* dissenting opinion, Justices Blackmun and Marshall stated that the "Court's opinion… will encourage taxpayers to cling to frivolous views of the law in the hope of convincing a jury of their sincerity." *Cheek* at 210. The dissent's view that *Cheek* may cause criminal tax violators "to cling" to frivolous views may have, in part, come true. Recently a jury acquitted Tommy Cyrer, a practicing attorney, of two counts of tax evasion charges. Mr. Cryer argued that he was unable to find where the IRC holds him liable for income taxes. The jury acquitted, apparently finding that he had a good-faith belief that he was not liable for income taxes and therefore he did not willfully violate the income tax laws. In 2003, Vernice Kuglin, a FedEx airline pilot, was indicted on six counts of tax evasion. At trial, Kuglin stated that she had written letters to the IRS requesting information on why she had to pay income taxes and that the IRS did not respond. She also argued that she did not know where the IRC holds her liable for income taxes. The jury also acquitted Kuglin, apparently finding that she had a good-faith belief that she was not required to pay income taxes and therefore she did not willfully violate the tax laws.

Cheek, Cryer, and Kuglin each asserted frivolous "legal arguments" which are made by individuals and groups who oppose compliance with the federal tax laws (The IRS Restructuring and Reform Act of 1998 prohibits the IRS from classifying taxpayers who assert frivolous arguments as "tax protesters"). Other common frivolous arguments are: the filing of a tax return and payment of tax is voluntary; a "zero return" will reduce your federal income tax liability; a taxpayer is not a citizen of the United States; wages are not income; a taxpayer is not a "person" as defined by the IRC and thus not subject to the federal income tax laws; and the 16th Amendment was not properly ratified. *See IRS Publication The Truth About Frivolous Tax Arguments, November 30, 2006.* These arguments have repeatedly been recognized by the courts as frivolous and as such are rarely successful.

While Cheek, Cryer and Kuglin were successful, the IRS wins 92% of its criminal tax cases. Indeed, on remand and retrial Cheek was convicted and the conviction was upheld by the Seventh Circuit. *See United States v. Cheek,* 3 F.3d 1057 (7th Cir.

1993). It should be noted that Kuglin, after being acquitted of criminal charges, entered into an agreement with the IRS to pay more than half a million in back taxes and penalties. *Kuglin v. Commissioner,* Docket No. 21743-03; *see* 2004 TNT 177-6 (Sept. 13, 2004). The IRS website lists several other recent victories including:

- On May 30, 2006, in Honolulu, HI, John David Van Hove, also known as Johnny Liberty, was sentenced to 27 months in prison, followed by three years of supervised release for his role in a tax and wire fraud scheme. Van Hove previously pleaded guilty to one count of obstructing and impeding the administration of the tax laws and one count of wire fraud. As part of the sentence, Van Hove was ordered to pay $400,000 restitution to defrauded investors. Van Hove was also ordered to pay restitution to the IRS based on income he received as a result of producing promotional materials for the Institute of Global Prosperity. According to court documents, Van Hove offered clients schemes for hiding income and assets from the IRS, including the use of "common law trusts" to conceal ownership and control of assets and income; and the use of offshore trusts with related bank accounts in which assets would be repatriated through the use of a debit card.
- On May 18, 2006, in Tacoma, WA, David Carroll Stephenson was sentenced to 96 months in prison and ordered to pay $8.5 million in restitution to the IRS. In February 2006, Stephenson was convicted of conspiring to defraud the United States and three counts of failing to file income tax returns for three tax years. According to the indictment and evidence introduced during trial, Stephenson helped hundreds of people create and operate "pure equity trusts." Stephenson advised his clients that they could avoid paying income taxes if they placed their income and assets into the trusts, even though they continued to control the use of the income and property placed in the trusts.
- On February 24, 2006, in Las Vegas, NV, Irwin Schiff was sentenced to a total of 163 months in prison—151 months for tax fraud and an additional 12 months for contempt of court. In addition, Schiff was ordered to pay more than $4.2 million in restitution and to serve three years of supervised release. In October 2005, Schiff was convicted of conspiring to defraud the United States, aiding and

assisting in the preparation of false income tax returns, filing his own false tax returns, and evading the payment of millions of dollars in back taxes owed. This marks the third time Schiff has been convicted for committing federal tax offenses. Schiff previously has spent more than four years in jail for his tax crimes. Two associates of Schiff, Cynthia Neun and Lawrence Cohen, were also convicted of aiding and assisting other taxpayers in the filing of false tax returns. On February 3, 2006, Cohen was sentenced to 33 months in prison. Neun was sentenced to 68 months in prison and ordered to pay $1.1 million in restitution. According to the indictment and the evidence introduced at trial, beginning in 1995, Schiff aided thousands of taxpayers in the filing of false federal income tax returns with the IRS that reported zero taxable income in spite of the taxpayers earning reportable income. Schiff owned and operated Freedom Books, a business that sold books, tapes, and informational packages encouraging customers not to pay income tax.

Proof of Willfulness

Generally willfulness is proven using circumstantial evidence. "Direct proof of a taxpayer's intent to evade taxes is rarely available. Willfulness may be inferred, however, by the trier of fact from all the facts and circumstances of the attempted understatement of tax." *United States v. Conforte*, 642 F.2d 869, 875 (9th Cir. 1980). Circumstantial evidence is indirect evidence, meaning the prosecutor presents facts that will allow the jury to infer willfulness. For example, if the defendant is charged with failing to file a tax return, the prosecutor may show that the defendant has filed tax returns in the past. This demonstrates that the defendant was aware of the requirement to file and allows the jury to infer that the defendant voluntarily, intentionally violated a known legal duty. *See United States v. Shrivers*, 788 F.2d 1046, 1048 (5th Cir. 1986). Practical considerations cited in the Internal Revenue and the Department of Justice's Criminal Tax Manuals include:

- A reminder from an accountant, to the defendant, that a tax return is due.
- Letters from a Service Center reminding the defendant of an Internal Revenue Code requirement; disregarding warning letters from the IRS

- Demonstrating a pattern of failing to file.
- Showing that a taxpayer has mailed frivolous arguments to the IRS
- Filing contradictory forms, such as W-4
- Demonstrating that the defendant has lied to a revenue agent or criminal investigator
- Education and background
- Evidence showing the defendant earned a large gross income

As you can see, when considering any criminal tax matter, the issue of willfulness is crucial. It is imperative that evidence, usually circumstantial, be developed to overcome a taxpayer's defense that they lacked willfulness.