Lawyers today more likely to 'meet' criminal division of the IRS

By Robert W. Wood

Not too many years ago, any type of interaction with the Internal Revenue Service's Criminal Investigation Division was rare. Today, though, lawyers and non-lawyers alike are far more likely than ever before to face criminal tax issues. Many people are surprised to learn that the vast majority of IRS criminal tax cases arise because of referrals from the civil division of the IRS. It can start quite innocuously.

If during the course of an audit a civil IRS auditor discovers something that seems untoward, he or she can refer it to the Criminal Division of the IRS for investigation. You may never know you are being investigated. If the referral does not merit action, you may *never* know.

Many investigations do not lead to prosecutions. But if you are contacted by the IRS Criminal Investigation Division as a target or even as a witness you should politely decline to be interviewed. Refer them to your lawyer.

The biggest reason for the increasing presence of the criminal wing of the IRS today is the IRS' continuing focus on undeclared income and offshore accounts. The IRS voluntary disclosure program is a good solution for taxpayers who have still not come forward. It offers manageable penalties, protection from prosecution, and a predictable and low-key procedural path.

Besides, the IRS has multiple avenues for finding even past account holders. Moreover, the stakes are growing higher. One especially frightening development involves grand jury subpoenas to produce your *own* offshore bank records. Most lawyers have a knee-jerk reaction to this.

"Just take the Fifth," lawyers tend to say, since the Fifth Amendment says you cannot be forced to incriminate yourself. Suppose the IRS and Department of Justice are investigating to determine if you used offshore bank accounts to evade taxes. The grand jury issues a subpoena demanding bank records under the Bank Secrecy Act of 1970—that's the law requiring the annual foreign bank account statements known as FBARs.

You might well try to quash the subpoena based on your constitutional privilege against self-incrimination, since handing over the records clearly would incriminate you. However, the courts have said that the Required Records Doctrine trumps your Fifth Amendment privilege. Thus, you have to hand over the documents no matter how incriminating they are.

In *In re Grand Jury Investigation M.H.*, 648 F.3d 1067 (9th Cir. 2011), the Ninth Circuit Court of Appeals allowed prosecutors to compel someone to produce offshore account data even if it was self-incriminating. The Seventh Circuit recently agreed with this approach in *In re Special February 2011-1 Grand Jury Subpoena Dated September 12, 2011,* 2012 U.S. App. LEXIS 18354 (7th Cir. 2012).

Under the Required Records Doctrine, these courts have held that there is no violation of the Fifth Amendment if:

- The government's inquiry is essentially regulatory;
- The information is a preserved record of a kind customarily retained; and
- The records have taken on public aspects making them analogous to a public document.

Many citizens and many lawyers are surprised to learn that foreign bank records can be viewed in this way. But two appellate courts have said so. This kind of development should make the IRS voluntary disclosure program even more attractive. But there is another related respect in which tax lawyers are watching this unfolding situation with a cautious eye.

Tax charges and FBAR charges can be separate and the FBAR filings carry even higher criminal penalties. The cases are also easier to prosecute. In *United States v. Williams*, No. 10-2230, slip. op. (4th Cir. 2012), the Fourth Circuit recently reversed a district court which had held that a taxpayer did not act willfully when he failed to file FBARs.

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Until it was reversed on appeal, *Williams* was a ray of hope for those considering FBARs to be obscure forms the IRS must prove you *knew* about. With the reversal, the threat of FBAR penalties seems more serious. Williams had checked the "no" box on his tax return to indicate that he did not have a foreign account and he failed to file FBARs. Although Williams pled guilty to tax evasion, he denied that his FBAR violation *itself* was willful.

The district court suggested the IRS would have a hard time proving willfulness. Most people simply do not know about FBARs. Moreover, some tax cases imply that you might not be willful if you have a genuine misunderstanding of the tax law, even if it is unreasonable. See *Cheek v. United States*, 498 U.S. 192 (1991).

Although the district court said the government did not separately prove willfulness, the appeals court was willing to connect the dots. The appeals court said that Williams made a *conscious effort to avoid learning* about FBARs. That itself was willful, the court suggested.

How much the *Williams* case will impact future FBAR penalties and prosecutions is unclear. The court suggests that one can be willful *without* a specific bad intent: willful blindness. Whether the issues are related to foreign accounts or any other kind of tax issue, dealings with the IRS should be given an appropriate level of caution.

Robert W. Wood *is a tax lawyer with a nationwide practice (www.WoodLLP.com). The author of more than 30 books including "Taxation of Damage Awards & Settlement Payments" (4th Ed. 2009 With 2012 Supplement www.taxinstitute.com), he can be reached at Wood@WoodLLP.com. This discussion is not intended as legal advice, and cannot be relied upon for any purpose without the services of a qualified professional.*