Tax Evasion

Background

The law does not require taxpayers to arrange their finances in order to maximize their taxes. All taxpayers are entitled to take all lawful steps that apply to their individual situations in order to minimize their tax liabilities. For example, it is lawful to take tax deductions that are available, and a taxpayer may avoid taxes on a certain amount of income by making charitable contributions.

Contrasted with legal efforts to minimize tax liabilities, TAX EVASION is a crime. Tax evasion typically involves failing to report income, or improperly claiming deductions that are not authorized. Some of the most common forms of tax evasion include the following:

- Failing to report the cash income
- Taking unauthorized deductions for personal expenses on a business's TAX RETURN
- Falsely claiming charitable deductions—or inflating the amount of charitable deductions—when there have in fact been none or there have been significantly less than claimed
- Overestimating the value of property donated to charity
- Filing a false tax return, improperly omitting property and knowingly and significantly underreporting the value of an estate

According to section 7201 of the Internal Revenue Code (IRC), it is a federal crime for anyone to willfully attempt to evade or defeat the payment of federal income taxes. A taxpayer can be found guilty of that offense when all of the following facts are proved beyond a reasonable doubt:

1. The DEFENDANT owed substantial INCOME TAX in addition to that declared in the defendant's tax return
2. The defendant knowingly and willfully attempted to evade or defeat the tax

The prosecution need not show the exact amount of the taxes due, but it must prove that the defendant knowingly and willfully attempted to evade or defeat a substantial portion of the additional tax charged in the INDICTMENT.

In this context, the word "attempt" means that the defendant knew or understood that he had TAXABLE INCOME which he was required by law to report to the Internal Revenue Service (**IRS**) during the particular tax year or years involved. Nevertheless, the defendant attempted to evade or defeat the tax, or a significant part of the tax on that income, by willfully failing to report all of the income the defendant earned during that year.

The Criminal Investigation Division

During an AUDIT, if an IRS revenue agent suspects FRAUD, he can impose penalties himself, or he can refer the case to the Criminal Investigation Division (CID). The CID is part of the enforcement mechanism for the IRS. It is divided into two parts— General Enforcement (for ordinary taxpayers) and Special Enforcement (for unions, organized crime, and cases involving drugs).

The CID has broad powers. In fact, a taxpayer may not even know the CID is investigating him until the taxpayer is formally charged. The CID takes its job very seriously and conducts extremely thorough investigations. In pursuit of EVIDENCE, CID agents may contact a taxpayer's friends, employer, co-workers, neighbors, and bankers, and spouse. There are CID offices throughout the United States. CID agents are federal investigators who have been trained in law enforcement techniques. Most CID agents are also accountants, and many have earned their **CPA**.

The CID may monitor mail and may apply for a court order for a phone tap. For example, In October, 2000, prompted by the IRS, the U. S. District Court ordered American Express and MasterCard to provide credit and DEBIT card information pertaining to U. S. taxpayers involving banks in Antigua, the Bahamas, and the Cayman Islands for the 1998 and 1999 tax years. The IRS has estimated that some $70 million in annual taxes is lost through offshore tax evasion activities. The banks of Antigua, the Bahamas, and the Cayman Islands are favorite locations in which to conceal revenue from the IRS.

If taxpayers fail to report transactions and pay taxes on those transactions, they could be guilty of tax fraud, tax evasion, and MONEY LAUNDERING under U. S. law. U. S. citizens must inform the IRS whether they have earned interest on an account deposited in a foreign bank on Form 1040, Schedule B. If they do, then they must complete TD F90-221 if the aggregate amount held in all foreign accounts exceeds $10,000 at any time during the tax year. Additionally, currency transactions involving more than $10,000 must be reported on Form 4789, and international transportation of currency or monetary instruments (such as bearer BONDS) must be reported on Form 4790. By focusing on the records of U. S. credit card companies, the IRS has found an effective means to investigate offshore tax havens. Thus, many U. S. tax evaders have cause to be uneasy about their offshore activities.

Because of the many resources it takes to conduct a CID investigation, only a very small percentage of taxpayers or tax evaders are investigated by the CID. The IRS will use the CID only when it has strong implications of serious wrongdoing. Even in these cases, the CID will recommend prosecution only if it has built an airtight case against the suspect.

The CID will usually PROSECUTE cases it determines are very strong. On the other hand, if the case may generate a lot of publicity, the CID may decide to prosecute anyway. The CID and IRS view high publicity prosecutions against high profile people as being a major deterrent for others contemplating committing a tax crime. The CID also considers the amount of money involved in a tax crime when deciding whether to prosecute a case. The average amount of money owed in most criminal tax cases exceeds $70,000. Once the decision to prosecute has been made by officials in the CID, and the **J**USTICE **D**EPARTMENT accepts the case, the chances of obtaining a CONVICTION are about 80 percent. About half of those convicted will be incarcerated, irrespective of any prior criminal record in their past.

Tax Evasion, Tax Fraud, And Other Tax Crimes

When the CID completes an investigation and recommends that a taxpayer be prosecuted for a tax crime, IRS lawyers will conduct at least two stages of before there is final approval to proceed with a prosecution:

1. After the IRS decides to prosecute, it forwards the case to the United States Department of Justice Tax Division in Washington, D. C. Federal prosecutors with special training in prosecuting criminal tax violations review the case and determine whether or not to authorize prosecution.
2. If the Department of Justice Tax Division in Washington approves prosecution, the case is sent to U. S. attorney's office located near the suspect. It is instructed to prepare indictments and to prosecute the individual or individuals for the alleged offenses.

The Tax Division's principal function is to provide legal advice for its main client, the IRS. The Division handles almost all civil LITIGATION arising under the internal revenue laws except for those cases that are docketed in the U. S. Tax Court. The Division also enforces the criminal tax laws by supervising or directly handling all criminal tax cases.

In tax crime cases, the prosecution approval process can work to a suspected taxpayer's advantage. The process allows several opportunities to derail a federal criminal case before it ever gets presented to a GRAND JURY. Assuming a taxpayer is aware that a case is being prepared against him, his lawyer will have the opportunity to confer with the government's lawyers and try to convince them not to prosecute his client. If the government has a strong case against the suspected taxpayer, it is unlikely that the IRS can be dissuaded from pursuing the case. However, if the case involves mere misunderstandings that can be explained and the IRS can be convinced that there really was no criminal conduct, the taxpayer may be able to convince the government to decline prosecution prior to grand jury.

In a tax crime case, a defendant is well advised to hire a lawyer who is experienced in federal criminal matters and who also has significant experience in federal criminal tax cases. If a defendant in a tax crime case cannot find a lawyer with this combination of training and experience, the defendant may want to consider hiring a former CID agent to help with the defense. In short, it is sound policy to have both federal criminal defense and tax crime experience on the defense team.

Tax Fraud Prosecution

After the (CID) has conducted an investigation and has recommended prosecution to the Justice Department, there are three crimes with which an individual may be charged:

- Tax evasion: This is an intentional violation of tax laws. It is a broad category, encompassing any cheating of the government in taxes. Tax evasion is a FELONY and a very serious crime. A conviction for tax evasion can carry with it up to a five-year prison sentence and/or fines up to $100,000.
- Filing a false return: Prosecution for this crime is appropriate when a taxpayer has provided the government with false or misleading information on the taxpayer's tax return. In such cases, the government does not have to prove the taxpayer intended to evade tax laws. Rather, it merely must prove that the taxpayer filed a false return. Filing a false return is a felony. Punishment for this crime can consist of up to three years in prison and/or up to $100,000 in fines.
- Not filing a tax return at all: Failing to file a tax return is the least serious of the three tax crimes. It is a MISDEMEANOR. The consequences for being found guilty is a maximum of 1 year in prison and/or fines totaling up to $25,000 for each year a taxpayer failed to file.

A taxpayer may be arrested once the taxpayer has been charged with one of these three crimes. If so, the taxpayer may be required to post BAIL or may be released on his or her own recognizance. Once charged, it is imperative that the ACCUSED taxpayer retain a tax attorney as soon as possible. The lawyer will need time to study the client's case and formulate a defense. Taxpayers need to keep in mind that the IRS has already completed their investigation and has most likely built a strong case against the accused taxpayer.

Failing to File Returns

The vast majority of taxpayers do file their tax returns with the IRS every year. However, according to some estimates, about three percent of taxpayers do not file tax returns at all. If a taxpayer does not owe any taxes, the penalties are not severe. But failing to file a tax return in years where one does owe taxes is a crime. The penalties can be quite severe. For example, for each year a taxpayer fails to file a return, the IRS can fine that taxpayer up to $25,000, or the taxpayer can be sentenced to one year in prison. And this is just for being negligent. If a taxpayer does not file a return in an effort to evade taxes, the IRS can pursue felony charges, including a fine up to $100,000 or a maximum of 5 years in jail. While INCARCERATION is rare, the threat is real and should deter those considering evading taxes.

It is wise to file a return even in cases where a taxpayer may not have enough resources to pay the entire tax bill. The IRS will work out a payment plan with taxpayers in these cases. There is a six-year STATUTE OF LIMITATIONS for filing criminal charges based on failing to file a tax return, but there is no STATUTE of limitations on how long the IRS can seek taxpayers and demand payment or taxes owed on non-filed returns.

The IRS may penalize taxpayers for filing tax returns late. Depending on the circumstances, there can be criminal or civil trials. At the very least, the IRS may withhold refunds to the taxpayer. If the taxpayer actually owes taxes from a late return, the IRS can levy a late filing PENALTY of 5 percent per late month to a maximum of 25 percent. Additionally, the IRS may impose a = percent to 1 percent late payment penalty to the late filing penalty. In the meantime, interest is accumulating on the debt to the IRS. Thus, it is in taxpayers' best interests to file late returns before they are contacted by the IRS.

The IRS usually does not pursue criminal charges against taxpayers who file of their own volition before the IRS has contacted them. The IRS also tends to be more sympathetic in collecting taxes from taxpayers who volunteer their late returns than taxpayers the IRS had to investigate and "catch." If the IRS identifies an errant taxpayer before the taxpayer has a chance to file a late return, the manner in which they contact the taxpayer is an indication of how seriously they may treat the particular case. The IRS uses four ways to notify taxpayers of fraud or other criminal tax behavior:

1. Most non-filers receive a non-threatening written request from the IRS Service Center.
2. A letter or personal call from a Taxpayer Service Representative gives taxpayer a deadline for filing (usually 30 days).
3. A call or personal visit from a Revenue Agent or Officer gives the taxpayer a deadline by which to file returns directly to the agent. The agent may even offer to assist in preparing the missing returns. Note that if a taxpayer refuses to file, the IRS can legally prepare a return, which is never in a taxpayer's best interest.
4. The worst way to be notified is by a visit by a Special Agent in which the taxpayer is informed that he or she has become the subject of a criminal investigation.

Considering all the above, it appears crucial to file one's tax returns within the deadlines. If a taxpayer needs more time to file, the IRS has a fairly simple method to request an extension for time to file. But do not fail to file at all. If one has failed to file returns in the past, it is best to go ahead and file late returns before coming to the attention of the IRS. If one owes taxes from late returns, it is advisable to go ahead and pay the debt as soon as possible, even if one must borrow the amount. It costs more to owe the IRS than it does almost anybody else. If a taxpayer has not filed returns in many years, the taxpayer should not worry about being caught if the taxpayer resumes filing. The IRS computers do not search for such taxpayer information. Besides, the IRS wants to encourage non-filers to start filing again.

Additional Resources

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