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TITLE 26

Fifth Circuit Affirms Convictions for Tax Evasion

In *United States v. O'Kane*, 2004 WL 1681295, 94 A.F.T.R.2d 2004-5274 (5th Cir. (Tex.) June 18, 2004), the Fifth Circuit affirmed O'Kane's jury convictions for four counts of tax evasion in violation of 26 U.S.C. § 7201.

On appeal, O'Kane initially argued the evidence presented during trial was insufficient to support his convictions for tax evasion for tax years 1994 through 1997, the government did not prove that the Internal Revenue Service made a tax assessment or demand for the years 1994 through 1997, and the government failed to prove the willfulness requirement of 26 U.S.C. § 7201. After reviewing the evidence in question, the Fifth Circuit was satisfied the district court's finding that O'Kane was guilty of four counts of tax evasion for the years 1994 through 1997 was indeed supported by "substantial evidence" and that "any rational trier of fact could have found that the evidence established guilt beyond a reasonable doubt." *Id.* (citing *United States v. Ceballos-Torres*, 218 F.3d 409, 411 (5th Cir. 2000)).

Specifically, the Fifth Circuit found the evidence established there were tax deficiencies for tax years 1994 through 1997, that O'Kane took numerous affirmative steps to evade or attempt to evade taxes, and that he did so willfully. *Id.* (citing *United States v. Townsend*, 31 F.3d 262, 266 (5th Cir. 1994)).

O'Kane also argued that the district court erred in denying his motion to quash the indictment wherein he alleged the government withheld "notices of deficiency issued for tax periods 1994 and 1995." After finding that O'Kane had not established a violation of *Brady v. Maryland*, 373 U.S. 83, 87 (1963), to the extent that he had not shown the government withheld any deficiency notices or that such notices would have been favorable to his defense, the Fifth Circuit held the district court did not err in denying his motion to quash the indictment.

Lastly, O'Kane argued the district court erred when it

denied his motion to require the government to show its authority to act. Since O'Kane filed this motion in the district court, but argued for the first time on appeal that it was based on his claim that the federal income tax laws are unconstitutional, the Fifth Circuit limited its review to plain error. *Id.* (citing *United States v. Olano*, 507 U.S. 725, 732-34 (1993)). The Fifth Circuit then recognized that it had "rejected on numerous occasions attacks on the constitutionality of the federal income tax laws," and ultimately opined that O'Kane failed to show that the district court's denial of this motion was error, plain or otherwise. *Id.* (citing *Stelly v. Comm'r*, 761 F.2d 1113, 1115 (5th Cir.1985) and *Olano*, *supra* at 732-34).

State Court Judgment Relevant and Admissible in Tax Evasion Case

In *United States v. Boulware*, 384 F.3d 794 (9th Cir. 2004), the Ninth Circuit held that a state court judgment determining the property rights over money transferred from the defendant to his girlfriend was relevant and admissible into evidence at defendant's trial on tax fraud charges. In this case, Boulware was convicted of five counts of filing false tax returns, four counts of tax evasion, and one count of conspiracy. On appeal, Boulware argued the district court erred in excluding evidence of a state court judgment that supported Boulware's criminal defense on tax charges. The state court judgment in the lawsuit between Boulware and his girlfriend to determine whether money was transferred as a gift or to be held in constructive trust for his corporation, contradicted the government's theory that Boulware stole the money from the corporation and gifted it to his girlfriend. Boulware was granted a new trial.

At trial, the government sought to prove Boulware diverted funds from his company, Hawaiian Isles Enterprises (HIE) by writing checks to employees and friends, and having them return cash to him. Boulware allegedly submitted fraudulent invoices to cover the payments, and then laundered the proceeds through other companies he owned. Boulware's defense was that he never relinquished ownership of the transferred funds. In support of his defense, Boulware sought to introduce the state court judgment, which determined that money he transferred to

her was not a gift, but rather held by her in constructive trust for his company. The district court excluded the evidence of the state court judgment, and Boulware was convicted.

The Ninth Circuit looked at two main issues regarding the state court judgment. First, whether the judgment had the preclusive effect of preventing the government from relitigating the issue of ownership of the transferred funds. Since property rights are determined under state law, Boulware, citing several tax cases requiring federal courts to treat state court determinations as binding on questions of state law, argued the government was collaterally estopped from arguing that Boulware had gifted the funds at issue. The Ninth Circuit disagreed the state court judgment would have preclusive effect because “[e]ven assuming that the state court judgment is binding as to the ownership of funds . . . [t]he money could still be income to Boulware . . . if he gave it to Lee to hold for him in an effort to hide it from the IRS.”

Next, the court addressed whether the state court judgment was relevant, and thus admissible evidence at trial. The district court excluded the judgment under Federal Rules of Evidence 401 and 402 stating the issue of whether the transfer of money was gifts was not relevant. Rule 401 provides that evidence is relevant if it has “any tendency to make the existence of a fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence.” The Ninth Circuit explained that Boulware’s successful litigation to force his girlfriend to return the money was relevant because it tended to make it more likely that he transferred the funds to her to hold in trust for HIE. The Ninth Circuit reversed Boulware’s conviction on the tax fraud counts, and remanded for a new trial.

Willful Failure to Collect or Pay Over Employment Tax

In *United States v. Pflum*, 2004 WL 1505383, 94 A.F.T.R.2d 2004-5239 (D.Kan. June 18, 2004), the U.S. District Court for the District of Kansas denied Pflum’s efforts to have the government’s second superseding indictment dismissed by way of its denial of his Motion to Dismiss for Duplicity and Motion to Dismiss for Retaliatory, Selective, and Vindictive Prosecution.

In this case, David G. Pflum was the sole defendant named in an eleven-count second superseding indictment which charged him with various tax offenses. Counts one through eight charged that Pflum, as the sole proprietor of a business with several employees, violated 26 U.S.C. § 7202 by failing to collect, account for, and pay over federal employment taxes related to those employees for the four quarters of tax years 1998 and 1999. Each count corresponds to Pflum’s duty to collect and truthfully account for the employment taxes due each quarter of the two calendar years. Counts nine, ten, and eleven charged that Pflum violated 26 U.S.C. § 7203 by failing to file his

individual income tax returns for tax years 1997, 1998, and 1999.

By way of his Motion to Dismiss for Duplicity, Pflum argued that counts one through eight defectively charged him with committing an offense that 26 U.S.C. § 7202 criminalizes as two separate offenses. Put another way, Pflum contends the indictment was flawed because it charged him in the conjunctive with having willfully failed “to collect and truthfully account for and pay over . . . said employment taxes” when § 7202 reads in the disjunctive by creating an offense that can be committed in two different ways, *i.e.*, by one “who willfully fails to collect or truthfully account for and pay over such tax shall, . . . , be guilty of a felony....” In dismissing this Motion, the district court recognized that, in the Tenth Circuit, “it is a matter of hornbook law that ‘a crime denounced in the statute disjunctively may be alleged in an indictment in the conjunctive, and thereafter proven in the disjunctive.’” *Id.* (citing *United States v. Powell*, 226 F.3d 1181, 1192 n. 4 (10th Cir.2000), *cert. denied*, 531 U.S. 1166 (2001)). Put even more simply, the district court stated that “an indictment may use the word ‘and’ although the statute employs the word ‘or.’” *Id.* (citing *United States v. Daily*, 921 F.2d 994, 1001 (10th Cir.1990), *cert. denied*, 502 U.S. 952 (1991)).

As for his Motion to Dismiss for Retaliatory, Selective, and Vindictive Prosecution, Pflum argued that the criminal investigation that resulted in the indictment against him was initiated because he had exercised his First Amendment right to the redress of grievances by filing several civil complaints against the United States in opposition to, and in connection with, the Services’ efforts to collect a trust fund recovery penalty from him which dated back to 1989. In dismissing this Motion as well, the district court found that Pflum simply failed to satisfy his threshold burden of proving actual vindictiveness or a realistic likelihood of vindictiveness.

Specifically, the court opined that “[t]he evidence attached to the defendant’s motion do [sic] not establish circumstances from which one could reasonably infer a realistic likelihood of vindictiveness” and ultimately held there was “ample evidence that the decision to prosecute here was motivated by reasons other than a vindictive desire to punish the defendant for his civil litigation.” *Id.* The court also found persuasive the fact IRS agents were already suspicious of Pflum’s other tax-related activities before he even initiated any of his civil litigation.

Jury May Consider Reasonableness as a Factor in Deciding Whether Defendant

Satisfied Good Faith Defense to Tax Evasion

In *United States v. Pensyl*, 387 F.3d 456 (6th Cir. 2004), the Sixth Circuit held the district court did not err by allowing the jury to consider the reasonableness of Pensyl's beliefs in deciding the willfulness element of a tax evasion charge. The jury instructions indicated Pensyl did not act willfully if he held a good faith belief that his actions complied with the law, but said reasonableness is a factor to consider in determining if Pensyl actually held the belief.

Despite having taxable income in excess of \$100,000 in each of the years 1995 through 1997, Pensyl failed to file his personal federal income tax returns, as well as failed to withhold payroll taxes for the employees of his dental practice. At trial, Pensyl argued he did not know he was liable for income taxes, and thus, his failure to pay income tax was not willful. Pensyl was convicted on three counts of attempted tax evasion in violation of 26 U.S.C. § 7201. The district court sentenced him to thirty months in prison and three years of supervised release. Pensyl appealed his conviction on the grounds the jury instructions contaminated his right to a fair trial under the Sixth Amendment.

Pensyl argued that by allowing the jury to consider the reasonableness of his belief, the jury instructions were contrary to the Supreme Court's holding in *United States v. Cheek*, 498 U.S. 192 (1991). In *Cheek*, the Supreme Court held that an honest but unreasonable belief could negate willfulness. Therefore, the jury instructions in that case, which precluded the jury from considering unreasonable beliefs when deciding if Cheek acted willfully, were impermissible.

The Sixth Circuit distinguished the jury instructions in *Cheek*. In this case, the district court judge instructed the jury they could consider reasonableness of Pensyl's belief as a factor in determining whether Pensyl actually held and acted on that belief. The court found the instructions in this case did not misstate the law, nor were they confusing, misleading or prejudicial.

§7212 Properly Joined with §7206(2) in Superseding Indictment under FRCP 8(a)

In *United States v. Triumph*, 94 AFTR.2d 2004-5750 (D.C. Cir. 2004), the D.C. Circuit denied the defendant's motion to sever the 26 U.S.C. §7212 charge of corrupt interference with the administration of internal revenue laws from the 38 count indictment of aiding and abetting the filing of false tax returns in violation of 26 U.S.C. §7206(2). The court held the corrupt interference charge was properly joined as part of the "common scheme or plan" of Triumph's efforts to obstruct the IRS through the preparation of false income tax returns. The court did sever a charge of failing to appear in violation of 18 U.S.C. §3146(a)(1).

Triumph argued that joinder of the 26 U.S.C. §7212 and 18

U.S.C. §3146(a)(1) counts with the 38 counts of 26 U.S.C. §7206(2) would be prejudicial to him. The court disagreed finding there was no indication the jury would use evidence cumulatively or as propensity evidence. In addition, the court found it unlikely that trying both charges would confuse the jury.

The court did grant Triumph's motion to sever the failure to appear count from the Superseding Indictment. The court labeled it prejudicial joinder, but acknowledged the primary reason for severance of this count was to give Triumph time to develop his insanity defense to that charge. The court determined the government would still be able to use evidence of Triumph's flight from custody as evidence of consciousness of guilt.

Amounts Forfeited to State Not Deductible As Business Loss

In *Hackworth v. Commissioner of Internal Revenue*, 2004 WL 1632734 (T.C.M. July 22, 2004), the Tax Court held Hackworth was not entitled to a loss deduction for cash he forfeited to the State of South Carolina as a result of his violation of state gambling laws. During 1998 and 1999, Hackworth owned and operated a bar in which he operated an illegal gambling business. The local Sheriff's office (GCSO) began an investigation based on information Hackworth was operating an illegal gambling business out of his home and business. Following the execution of several search warrants, trash runs and an undercover operation, certain monies were seized. Prior to Hackworth's guilty plea, he consented to the forfeiture of seized monies which were derived from illegal gambling. On Hackworth's 1999 schedule C, he deducted the forfeited monies under the caption "legal and professional services." The IRS disallowed the deduction.

Hackworth petitioned the tax court arguing he should be allowed the deduction as a loss, or in the alternative, he argued the forfeiture was invalid, that the damage done to the state's policy against illegal gambling was outweighed by congressional intent that "business losses" be allowed as a deduction, that the income tax be imposed upon his net income, or that imposing a liability for Federal income taxes on the forfeited monies without allowing a deduction violated the Double Jeopardy Clause of the Fifth Amendment.

Finding for the IRS, the tax court noted that courts have consistently found "that a loss deduction will be denied, [] where the deduction would frustrate a sharply defined Federal or state policy." In this case, the court found that "to allow [Hackworth] a deduction for a loss arising out of [his] illegal activities would undermine South Carolina's policy by permitting a portion of the forfeiture to be borne by the Federal government, thus taking the 'sting' out of the forfeiture." In accordance with controlling precedents, the court held Hackworth was not entitled to a loss

deduction for the monies forfeited to the state.

With respect to Hackworth's alternative arguments, the Tax Court stated it lacked jurisdiction over Hackworth's collateral attack on the forfeiture and distinguished authorities Hackworth cited in support of his loss argument.

Finally, the court held a federal income tax deficiency was remedial in nature and not a criminal punishment for double jeopardy purposes.

TITLE 18

Proceeds Defined As Gross Receipts Rather Than Net Profits

In *United States v. Grasso*, 379 F.3d 496 (3d Cir. 2004), the Third Circuit held the term "proceeds," as used in the money laundering statute, means gross receipts, rather than net profits, from illegal activity. In this case, Grasso was convicted of money laundering stemming from his use of proceeds from his illegal activity, a fraudulent work-at-home schemes, to pay advertising, printing, and mailing expenses.

Grasso relied on a Seventh Circuit case, *United States v. Scialabba*, 282 F.3d 475 (7th Cir. 2002) to argue the term "proceeds," which is not defined in the statute, must be interpreted to mean "net profits."

The *Scialabba* court reasoned the crime of money laundering was about concealment and only net profits need to be concealed; accordingly, convictions for reinvesting revenue in the illegal activity may be based only on reinvested net profits.

The Third Circuit disagreed with *Scialabba's* reasoning. The court looked to the two main purposes of the money laundering statute, prohibiting the concealment of proceeds of illegal activity and outlawing the "promotion of illegal activity." The court found that Grasso promoted an illegal activity within the meaning of the statute, regardless of whether the funds were profits or gross receipts. Further, the Third Circuit had routinely upheld money laundering convictions based on the reinvestment of proceeds, without requiring the proceeds be "net profits." Accordingly, the court held the statutory term "proceeds" in 18 U.S.C. § 1956 "means simply gross receipts from illegal activity."

SENTENCING GUIDELINES

Seventh Circuit Follows *Blakely*

In *United States v. Booker*, 2004 WL 1535858 (7th Cir. July 9, 2004), Booker appealed his sentence arguing the imposition of a sentence which was calculated based on a judge determined quantity of cocaine and enhanced for obstruction of justice violated Booker's Sixth Amendment right to have the jury make these determinations. A jury found Booker guilty of possessing with intent to distribute at least 50 grams of cocaine base, which has a sentence of 10 years to life imprisonment. At sentencing, the judge found, by a preponderance of the evidence, that Booker 1) distributed 566 grams over and above the 92.5 grams found by the jury and 2) obstructed justice. Under the Sentencing Guidelines, Booker's base offense level increased from 32 to 36 to account for the increase cocaine quantity, and another 3 levels for the obstruction enhancement, which placed Booker in a sentencing range of 360 months to life.

Reversing Booker's sentence, the court took guidance from *Apprendi v. New Jersey* and *Blakely v. Washington*. Specifically, the court found the "'statutory maximum' for *Apprendi* purposes, is the maximum sentence a judge may impose solely on the basis of the facts reflected in the jury verdict or admitted by the defendant," citing *Blakely*. In other words, the court stated "the relevant 'statutory maximum' is not the maximum sentence a judge may impose after finding additional facts, but the maximum he may impose without any additional findings." Thus, the court concluded Booker had a right to have the jury determine the quantity of drugs he possessed and the facts underlying the obstruction determination by proof beyond a reasonable doubt.

Sentencing Guidelines Factors Included in Superseding Indictment Constitute *post-Blakely* Surplusage

In *United States v. Mutchler*, 333 F.Supp.2d 828 (S.D.Iowa 2004), Mutchler and his co-defendants were charged with a narcotics trafficking conspiracy. Prior to trial, the defendants moved to strike the government's superseding Indictment which contained four factual allegations modeled after several "aggravating factors" set forth in the Federal Sentencing Guidelines. Specifically, they argued the government's inclusion of the aggravating factors was nothing more than surplusage under Fed. R. Crim. P. 7(d) and violated their rights under the Federal Constitution.

In response to the Joint Motion, the government argued the inclusion of the aggravating factors in its Superseding Indictment was necessary in the event the Sentencing Guidelines are ultimately deemed unconstitutional under the principles set forth *Blakely v. Washington*, --- U.S. ---, 124 S.Ct. 2531 (2004). In the alternative, assuming the factors were indeed surplusage, the government argued they were not so prejudicial or inflammatory as to justify striking them from the Superseding Indictment.

The district court was ultimately persuaded by the defendants' argument and held the aggravating factors in question did indeed constitute prejudicial surplusage. In doing so, the district court recognized that:

The test for a sufficient indictment is whether it contains the elements of the offense intended to be charged and sufficiently apprise[s] the defendant what he must be prepared to meet and, in case any other proceedings are taken against him for a similar offense, whether the record shows with accuracy to what extent he may plead a former acquittal or conviction. (Internal quotation marks omitted).

The district court then found the aggravating factors set forth in the Superseding Indictment did not constitute criminal conduct specifically defined by Congress and, as such, had no place within the government's charging documents. Specifically, the district court stated that:

...the factors themselves are based in sentencing guidelines with the power to do nothing more than fetter the discretion of sentencing judges to do what they have done for generations – impose sentences within the broad limits established by Congress. (Internal quotations and citations omitted). As a part of guidelines meant to act as procedural rules for the court, the aggravating factors do not provide sufficient authority to bring the allegations contained within them properly before a trier of fact in a United States Courtroom.

In regard to the government's alternate argument, *i.e.*, that the included aggravating factors were not prejudicial, the district court reiterated that none of those factors were based upon statutory language, that the factors should only have been included in the Superseding Indictment if they constituted actual crimes defined by Congress, and that there was no good reason to burden a jury with unnecessary complexity by alleging separate drug amounts in the charging documents.

In sum, the district court held that, "short of an act of Congress that establishes a particular drug amount, or for that matter, any of the aggravating factors, as a necessary element of an offense under the United States law," it would only permit the jury to consider those factual allegations which were necessary to apply the appropriate federal statutory penalties.

Application of Two-Level Sentencing Enhancement for Obstruction of Justice

In *United States v. Fiore*, 381 F.3d 89 (2nd Cir. (S.D.N.Y.) August 23, 2004), the U.S. Court of Appeals for the Second Circuit held, *inter alia*, the district court did not err when it

enhanced the base offense level of DeSimone's fraud offense in light of the perjury that he committed during an earlier SEC civil investigation into his fraud scheme, and that said enhancement did not constitute impermissible double counting.

In this case, DeSimone was charged with participating in a stock manipulation scheme in which the trading price of certain securities was inflated by fraud. The scheme involved a cornucopia of securities laws violations.

On December 17, 2001, pursuant to a plea agreement, DeSimone entered a guilty plea three counts of a superseding indictment charging him with conspiracy to commit securities fraud, wire fraud and commercial bribery (Count One); securities fraud (Count Two); and perjury (Count Three). The probation office's presentence report suggested a two-level enhancement, not in the plea agreement, for obstruction of justice based upon DeSimone's perjury during a related SEC civil investigation. The presentence report also detailed DeSimone's financial condition and recommended restitution but no fine. DeSimone's sentencing took place during two proceedings. At the first proceeding, the district court deferred its restitution determination and found that the obstruction enhancement was indeed applicable to DeSimone's sentencing calculation. At the subsequent proceeding, the district court sentenced DeSimone to a 21-month term of imprisonment to be followed by three years of supervised release. The district court also ordered restitution to the victims of the fraud in the amount of \$742,060.63 and imposed a \$250 special assessment.

On appeal, DeSimone argued, in pertinent part, that the district court erred during his sentencing proceedings when it applied a two-level obstruction of justice enhancement pursuant to Section 3C1.1 of the Sentencing Guidelines. Specifically, he argued that his perjury did not constitute an obstruction of the investigation into the underlying fraud offense because it was committed during an SEC civil investigation that took place prior to the initiation of the criminal investigation. He further argued that the enhancement results in double counting, improperly punishing him for conduct which had already been taken into consideration at the time of his perjury conviction.

In dealing with Appellant's first argument, the Second Circuit stated "[i]t is undisputed that DeSimone perjured himself in an SEC investigation involving the precise conduct for which he was criminally convicted: conspiracy to commit securities fraud and securities fraud." Further, it noted that his admitted perjury was directly related to the substance of the underlying fraudulent scheme to which he pleaded guilty. Thus, the court opined that, "[w]here federal administrative and prosecutorial jurisdiction overlap, subsequent criminal investigations are often inseparable from prior civil investigations, and perjury in the prior proceeding necessarily obstructs--if successful, by

preventing--the subsequent investigation.”

As for the second prong of DeSimone’s argument, the Second Circuit found it to be as lacking in merit as the first. Specifically, the court found that DeSimone’s sentence was calculated using the underlying fraud count as the base and, “[a]bsent the two-level obstruction enhancement, the sentence would not have reflected DeSimone’s perjury.”

The Second Circuit ultimately held that the district court “properly grouped the underlying (fraud) and obstruction (perjury) offenses under Section 3D1.2(c), applied the appropriate offense level for fraud, and adjusted upward by two levels for the perjury.”

Application of Two-Level Sentencing Enhancement for Obstruction of Justice

In *United States v. DeGeorge*, 380 F.3d 1203 (9th Cir. (C.D.Cal) August 30, 2004), the U.S. Court of Appeals for the Ninth Circuit held, *inter alia*, that the district court’s application of a two-level upward enhancement for obstruction of justice was improper despite the fact that DeGeorge’s perjury conviction was supported by the evidence.

In this case, DeGeorge is alleged to have engaged in a scheme to purchase a 76-foot yacht valued at \$1.9 million dollars, inflate its value, and then collect insurance proceeds after scuttling it. It was also alleged that DeGeorge proffered false testimony during his deposition in the underlying civil matter which involved a dispute over the insurance policy which covered the yacht. DeGeorge was eventually convicted on all 16 counts with which he had been charged and sentenced to 90 months imprisonment, three years supervised release, and was ordered to pay restitution of \$2,872,643.89 along with a special assessment of \$850.00.

On appeal, DeGeorge challenged several aspects of his sentence, including the district court’s application of a two-level obstruction of justice enhancement which was based upon his conviction on the perjury charges. The Ninth Circuit ultimately held that DeGeorge’s perjury did not constitute an obstruction of justice because the statements at issue were made during the underlying civil trial and in furtherance of his scheme to defraud the insurance carrier, rather than during the criminal investigation as part of an attempt to obstruct justice. *Id.* at 1222.

In reaching its decision, the Ninth Circuit opined that the district erred when it relied upon U.S.S.G. § 3C1.1, cmt. n. 8 (2000), which provides for the grouping of “the count for the obstruction offense...with the count for the underlying offense,” and adjusted the base offense level of the underlying offense upwards by two-levels. Specifically, the court stated as follows:

The district court erred in relying on Note 8

because DeGeorge’s perjury occurred during the *civil* trial as part of his scheme to defraud and not during the *criminal* investigation as part of an attempt to obstruct justice. Thus, the perjury was not an “obstruction offense” at all and should not have been grouped with the other offenses under § 3D1.2(c). In fact, because the civil trial occurred before the criminal investigation of DeGeorge began, the district court’s characterization of the perjury as an “obstruction offense” served only to make Note 8 inconsistent with the text of § 3C1.1 itself, which requires the perjury to occur “*during* the course of the [criminal] investigation.”

Id.

The Ninth Circuit also took issue with the government’s reliance upon *United States v. Briscoe*, 65 F.3d 576 (7th Cir. 1995), specifically noting that the Seventh Circuit affirmed Briscoe’s sentence only after specifically concluding that the obstruction at issue occurred *during* the criminal investigation. *Id.* at 1223 (emphasis added). Lastly, because the government actively portrayed DeGeorge’s perjury as part of his fraudulent scheme in order to avoid any potential statute of limitations problems, the Ninth Circuit was unwilling to allow it to subsequently “abandon this approach simply to obtain a higher sentence.” *Id.*

FORFEITURE

Pre-CAFRA Probable Cause Standard of Proof applied to Forfeit Seized Cash

In *United States v. \$242,484*, No. 01-16485 (11th Cir. 2004), the Eleventh Circuit, sitting en banc, reversed a previous Eleventh Circuit panel’s ruling that the government failed to establish probable cause to believe \$242,484 in seized cash was the proceeds of illegal drug transactions. The court defined probable cause as a “reasonable ground for belief of guilt, supported by less than prima facie proof but more than mere suspicion.” (citations omitted). The court affirmed the district court’s finding of probable cause.

The Eleventh Circuit used the totality of the circumstances to determine whether the government met its burden of proof. The circumstances include a courier with a large quantity of cash in small denominations, sealed in cellophane and wrapped in Christmas paper. The courier told DEA agents two conflicting stories about the reason for her travel, and she completely lacked documentation to support either version. She claimed not to know the identities of the people who gave her the money, and offered no explanation as to why the money was not wired or transferred by a safer method. Finally, a highly experienced narcotics dog alerted to the money

immediately, which tends to suggest the money was in recent contact with narcotics.

The Circuit Court added in its review of the totality of the circumstances that no one has come forward to claim ownership of the money in the two and a half years between the seizure and the probable cause hearing. The court agreed with the district court's finding of probable cause to believe the money was proceeds of, or traceable to illegal drug transactions.

Forfeited Drug Proceeds Traceable to Drug Trafficking

In *United States v. Bronstein*, 379 F.3d 496 (8th Cir. 2004), the Eighth Circuit affirmed the district court's finding the government had established, by a preponderance of the evidence, the money seized from Bronstein was connected to drug trafficking. During a routine traffic stop, after the officer noticed a strong odor of marijuana, Bronstein admitted to smoking marijuana and handed the officer the remaining drugs. During a consensual search of Bronstein's vehicle, the officer discovered another small amount of marijuana and cash. A total of \$64,115 was uncovered in seven air-tight bundles sealed in a padded UPS package. Another three bundles containing \$20,500 were uncovered concealed in a bag. The funds were seized and forfeited pursuant to 21 U.S.C. § 881(a)(6), as funds connected to drug trafficking. Bronstein appealed arguing the government failed to demonstrate a "substantial connection" between his possession of marijuana and the currency in his vehicle.

Upholding the district court's finding the government met its burden, the court concluded there existed sufficient evidence to establish a substantial connection between Bronstein's property and drug trafficking. The court considered significant the fact that possession of a large amount of cash was strong evidence the cash was connected to drug activity. Further, Bronstein undisputedly possessed illegal drugs, marijuana, at the time the money was discovered, and the dog's alert to Bronstein's currency provided a slight indication that Bronstein's cash was connected to drug trafficking. Finally, the court affirmed the district court's finding Bronstein's behavior undermined the credibility of his assertions of legitimate reasons for possessing the money (the manner in which the presence of the cash was disclosed and the manner in which it was stored).

FIFTH AMENDMENT

Foregone Conclusion – Reasonable Particularity Needed Prior to Issuance of the Subpoena

In the case of *In Re Grand Jury Subpoena*, 383 F.3d 905 (9th Cir. 2004), the Ninth Circuit held the government could

not show the Fifth Amendment privilege against self-incrimination was inapplicable where the existence, location, and authenticity of documents under subpoena were not a foregone conclusion. The appellant, John Doe, was held in contempt by the district court for not producing the documents sought under the government's subpoena. John Doe argued production of the documents would be testimonial and therefore, protected by the Fifth Amendment.

Doe was an employee of a company that manufactured Dynamic Random Access Memory (DRAM). The government was investigating possible antitrust violations by the semiconductor industry. During an interview with Doe, he admitted to sharing pricing information with competitors and memorializing the discussions in emails. However, he no longer possessed any of the emails, notes or documents still presumably held by his former employer. The government agents served Doe with a subpoena ordering him to appear and produce before the grand jury all documents relating to the investigation including but not limited to "handwritten notes, appointment calendars, or notepads or similar documents." A nearly identical subpoena was issued to Doe's former employer to produce the documents Doe had created.

Doe refused to comply with the subpoena, claiming the Fifth Amendment privilege against self-incrimination, and moved to quash the subpoena. The district court denied the motion, stating the documents were a "foregone conclusion," and thus, not testimonial. Doe appealed.

The Ninth Circuit disagreed with the district court's reasoning, distinguishing between the contents of the documents, which are not protected by the Fifth Amendment, and the act of producing the documents. By producing the documents, the court found Doe would be implicitly admitting to the existence, possession, and authenticity of the documents. "When the 'existence and location' of the documents under subpoena are a 'foregone conclusion' and the witness 'adds little or nothing to the sum total of the Government's information by conceding that he in fact has the [documents],' then no Fifth Amendment right is touched because the 'question is not of testimony but of surrender.'" *Fisher v. United States*, 425 U.S. 391 (1976)(quoting *In re Harris*, 221 U.S. 274 (1911)). In order to use the foregone conclusion doctrine however, the government has the burden of production and proof, which must be met by assessing the information possessed before the subpoena was issued. The court found the government lacked sufficient information when the subpoena was issued to make the existence or location of "handwritten notes, calendars, diaries, daybooks... 'a foregone conclusion.'" The government was required to establish with "reasonable particularity" the existence and possession of the documents. Although Doe made substantial admissions regarding the contents of documents and emails he created during his employment, the government failed to identify those documents with

reasonable particularity in the subpoena. Thus, the breadth of the subpoena exceeded the knowledge the government possessed when it served the subpoena.

The second prong of the foregone conclusion doctrine requires the government to show that it can independently verify the authenticity of the compelled documents. If the witness were compelled to use his discretion to select and assemble the documents, he would in fact be authenticating the documents through identification. Production would therefore be testimonial in nature, thus implicating the Fifth Amendment. The court remanded for the district court to determine whether the testimonial production would be incriminating.

BRADY

Multiple *Brady* Violations Requires New Trial

In *United States v. Sipe*, No. 03-40657, 2004 WL 2325496 (5th Cir. Oct. 15, 2004), the Fifth Circuit held Sipe was entitled to a new trial as the cumulative effect of numerous failures by the prosecution to disclose material exculpatory evidence was sufficient to undermine confidence in the jury's verdict despite "significant evidence" of Sipe's guilt. Sipe, a border patrol agent, was charged with violating 18 U.S.C. § 242 by using excessive force while arresting a foreign national attempting an illegal entry. Sipe filed pretrial motions seeking discovery of any criminal records of government witnesses, information relating to the benefits given the aliens the government would call as witnesses, and all other *Brady* material. The government responded that it had no knowledge of any criminal records of its witnesses, and the three aliens had only been granted the benefit of permission to remain and work in the country pending trial.

Sipe later learned that all of the alien witnesses had been granted numerous other benefits, including social security cards, witness and travel fees, and permission to travel around the country and to cross U.S. borders. Additionally, the government failed to produce evidence that a border patrol agent testifying for the government told the prosecutor that he personally disliked Sipe, and evidence that another government witness had a criminal history of filing a false police report.

The Fifth Circuit held that although none of the nondisclosures standing alone could have affected the outcome of the trial, when viewed in the aggregate, they undermined the confidence in the verdict. Although the record "unquestionably contained significant evidence" of Sipe's guilt, the court concluded "the prosecution's withholdings prevented Sipe from exposing significant weaknesses in the government's case at every turn." The court explained that, in assessing the significance of the *Brady* violations, it was necessary to place the facts in the context of the charged offense, which required proof that

Sipe's conduct was willful and taken with "a bad and evil purpose." Here, Sipe struck the alien on the back of the head with his flashlight, the only non-lethal weapon Sipe could wield effectively. While the facts were sufficient to support a conviction, they were also consistent with a finding that the use of excessive force was a "spontaneous act of poor judgment," the court concluded. Consequently, the court affirmed the district court's order of a new trial.

FEDERAL RULES OF CRIMINAL PROCEDURES

Motion for a New Trial

In *United States v. Barbera*, 93 A.F.T.R.2d 2004-25467 (S.D.N.Y. 2004), Barbera motioned for a new trial pursuant to Fed. R. Crim. P. 33(a) on the ground the district court improperly instructed the jury on IRS regulations concerning "employee" compensation. Barbera was convicted on 11 counts, including one count of conspiracy to defraud the United States and commit federal tax offenses and five counts of aiding in the preparation of false returns. The charges stem from Barbera's provision of a "no show" job in his medical practice for a mob member, which included health insurance. In his motion, Barbera argued the court's "jury charge failed to properly instruct the jury that they had to find that Barbera acted knowingly with respect to the tax fraud charges in Counts Two through Six, in that the court's instructions about IRS regulations 'took this fact-finding away from the jury.'" Instead, the court instructed the jury "as a matter of law when it was appropriate to treat someone as an 'employee' under the IRS laws, rather than instructing them that they had to decide whether Barbera treated Gelardo as an employee knowing that it was improper to do so."

In denying Barbera's motion, the court found the jury had been instructed on numerous occasions they had to find that Barbera acted knowingly and willfully in order to find him guilty on the tax fraud counts. Further, when viewed in light of the entire jury instructions on the tax fraud charges, the descriptions of IRS regulations pertaining to "employee" and "independent contractor" designations did not serve to remove the fact-finding function from the jury or otherwise mislead the jury. Thus, they found, the instruction to the jury regarding the IRS regulations in this case was relevant to the jury's determination whether each tax return was materially false and, when viewed in the context of the repeated explicit instructions to the jury that they had to decide whether Barbera acted knowingly and willfully, did not mislead them as to the correct legal standard. Accordingly, the court found the jury was properly instructed on the IRS regulations pertaining to "employee" and "independent contractor" designations.

Investigators of the Massachusetts Insurance Fraud Bureau Found to be

“Government Personnel” Excepted from Grand Jury Secrecy Rule

In *United States v. Pimental*, 380 F.3d 575 (1st Cir. 2004), the First Circuit, addressing an issue of first impression, found that the employees of the Massachusetts Insurance Fraud Bureau (“IFB”) were government personnel excepted from grand jury secrecy rule pursuant to Fed.R.Crim.P. 6(e)(3)(a)(ii).

This workers' compensation insurance fraud criminal case produced an appeal from both sides. The government appealed the district court's dismissal of two counts on which the jury had convicted, while Pimental cross-appealed on the ground that the entire case should have been dismissed because of an alleged violation of the grand jury secrecy rule found in Fed.R.Crim.P. 6(e). The First Circuit held that: (1) the district court erred in dismissing the two counts and reinstated the jury convictions; and concluded that (2) there was no violation by the prosecution of Rule 6(e). This second point was a matter of first impression.

After a jury convicted Pimental of two counts of mail fraud, the district court dismissed the convictions because it found that the two underlying mailings were not "in furtherance" of Pimental's fraudulent scheme. Pimental's scheme involved lying to various workers' compensation insurance company representatives about the nature and scope of his company's work. His false statements tended to reduce the premium payments he owed for workers' compensation insurance. The government appealed the district court's decision, arguing that the two mailings furthered Pimental's scheme by helping to ensure that the insurance company did not discover his earlier misrepresentations.

Pimental cross-appealed, arguing that his indictment should have been dismissed because the prosecuting attorney disclosed secret grand jury materials to an investigator for the Massachusetts Insurance Fraud Bureau (IFB). Pimental argued that the rule allowing disclosure of grand jury materials to "government personnel" in certain circumstances, Fed.R.Crim.P. 6(e)(3)(a)(ii), was inapplicable because the IFB investigator was a private actor. The IFB, which investigates potential cases of insurance fraud, is authorized and structured by Massachusetts statute, but partially run and entirely funded by insurers.

The First Circuit ultimately reversed the district court's dismissal of Pimental's convictions, finding that the mailings by insurance company representatives which formed the basis of the two counts of conviction were indeed in furtherance of Pimental's fraudulent scheme. Additionally, the appellate court rejected Pimental's cross-appeal after finding that the first district court (not the trial court) did not err when it opined that the IFB investigators in question were indeed "government personnel" within the meaning of Fed. R. Crim. P. 6(e)(3)(A)(ii) (“Rule 6(e)(3)(A)(ii)”) which authorized the prosecutor to reveal grand jury materials to

them.

In reaching its decision as to the status of the IFB investigators, the First Circuit initially noted that “[t]he IFB straddles the line between a government and a private entity, having attributes of each.” It then reviewed the legislative history and purpose of the exception to grand jury secrecy set forth in Rule 6(e)(3)(A)(ii) and concluded that the exception does indeed cover the unique quasi-governmental investigators of the IFB who were involved in the investigation of Pimental’s fraud scheme. The First Circuit’s holding was based, in large part, upon the fact that the IFB investigators in question had “access to non-public information that is not normally available to private investigators,” and that, in the event that IFB investigation leads to a referral to the Attorney General’s Office, “the IFB investigator assigned to the case provides significant support to the prosecuting attorney.”

It is important to note, however, that the First Circuit explicitly recognized that its holding was limited to the specific facts of this case and that “[t]he mere fact that a person works for the IFB does not mean that he or she fits the definition for government personnel within Rule 6(e)(3)(A)(ii).”

FEDERAL RULES OF EVIDENCE

Rule 901

In *United States v. Chin*, 371 F.3d 31 (2d Cir. 2004), the Second Circuit vacated and remanded for a new trial Chin’s conviction on one count of impersonating a federal employee and three counts of tax evasion. Chin was believed to be the swindler who, while simultaneously impersonating both an immigration lawyer and an officer of the INS, promised Chinese immigrants work visas for their foreign relatives in exchange for cash payments. Between 1997 and 1999, the swindler rented two different locations using multiple pseudonyms and traveled to China in furtherance of the scam. The swindler never produced any visas for his victims and absconded with the cash collected. Chin, believed to be the swindler, was convicted on all four counts and sentenced to 120 months imprisonment. The district court declined to group the four counts and enhanced Chin’s sentence for “sophisticated concealment” on the tax evasion counts.

On appeal, Chin argued the district court improperly excluded credit card receipts to prove his alibi defense as the receipts were authenticated and should have been admissible. Further, Chin argued the district court abused its discretion in limiting his language expert’s testimony. Chin also alleged the district court should have grouped the impersonation and tax evasion counts and improperly enhanced his sentence for sophisticated concealment. As the court vacated Chin’s conviction based on a review of the evidentiary issues, the court only cursorily discussed

the sentencing issues.

The court held the copies of the credit card receipts satisfied the authentication requirement of Fed. R. Evid. 901, and are admissible as non-hearsay evidence. The court found that doubts of the receipts ultimate reliability was within the jury's purview. The court found this required vacating Chin's conviction as the error was not harmless. Specifically, the court determined Chin's interpretation of the receipts, if credited by the jury, would have established is misidentification defense and could have resulted in Chin's acquittal. The court found the district court's exclusion of the expert's testimony was not manifest error requiring reversal, however, on remand, Chin may submit a revised proffer to satisfy the requirements of Fed. R. Evid. 702.

With respect to the sentencing issues, although the court did not make binding findings, it noted its inclination would have been to vacate the sentence and remand for grouping and for omission of the enhancement. The court determined grouping was proper as the Sentencing Guidelines measured both the impersonation and tax counts in monetary terms. Further, while the impersonation offense may have involved "sophisticated means," the court found no "intricate or complex steps to evade taxes." Accordingly, the sophisticated means enhancement relative to the tax counts was improper.

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