How to Obtain the Holy Grail in the Criminal Tax World:

A Prosecutorial Declination of a Federal Tax Case

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In the pantheon of achievements for a criminal tax defense attorney, few merit badges are more difficult to garner than obtaining a declination of tax charges from a federal prosecutor. By the time a criminal tax case reaches a prosecutor, whether stationed in the United States Department of Justice's Tax Division and/or in a United States Attorney's Office, that case has already survived multiple layers of scrutiny at the IRS, had scores or even hundreds of hours of investigative time committed to it, and resulted in a finding of a tax loss in the $10,000s, $100,000s, or millions of dollars. To derail that steaming prosecutorial locomotive before it reaches the indictment station, a defense attorney must not dwell on the initial decision to prosecute his client. Instead, the defense counsel must be fully versed in the mechanics of the process, the motivations of the key players, and the relevant facts and applicable law of the case if he/she has any hope to succeed.

1. "Why Me?": An Irrelevant Starting Point for a Prosecutorial Declination

Almost every client who finds herself facing an IRS criminal investigation asks her attorney at some point: "Why me?" Why not my competitor down the road who was doing the same thing I was doing or worse? My crooked neighbor? My cheating boss?, My unethical banker? My tax evading gardener? My "wink wink, nod nod" accountant? My (fill in the blank) whose tax manipulations make me look like a piker in comparison?

The most honest answer to this question is to tell the client that this question is the wrong one to be asking. How the client arrived on the government's radar screen might be useful in trying to determine what the government has learned about the client's conduct but virtually useless in trying to get a prosecutorial declination. Building a case for unconstitutional selective prosecution based on an impermissible criteria is extraordinarily hard and rarely found by the courts. A prosecutor's stock answer to the "Why me" question is that they will certainly try to go after every criminal they can but they have to start somewhere and you (the client) are the "somewhere." In

actuality, however, the prosecutor's stock bravado masks the stark reality that the federal government has virtually no chance to prosecute its way into tax compliance if simply locking up tax cheats is the measure for success. If one looks at the chances of being criminally prosecuted for tax violations, one would have to conclude that the odds are overwhelmingly in the crooked taxpayer's favor. A simple review of the numbers tells the story:

- Over 130,000,000 taxpayers file over 240,000,000 returns each year.
- IRS estimates 3% of taxpayers (or approximately 4,000,000 taxpayers) intentionally file fraudulent tax returns every year.
- IRS has approximately 2,800 Special Agents to investigate criminal tax violations.
- Approximately 4,000 IRS criminal investigations are initiated every year, with approximately 2800 of those resulting in prosecution recommendations to the Department of Justice.
- Over 90% of IRS prosecution recommendations are accepted by the Department of Justice.
- Approximately 2500 indictments/informations are filed each year.
- Approximately 2100 criminal convictions are obtained each year.

Based on the numbers alone, an average taxpayer has about a .003% chance of being criminally investigated and a .002% of being convicted. Phrased differently, an average taxpayer has a 99.997% chance of not being criminally investigated and a 99.998% chance of not being criminally convicted. Even the crooked taxpayer has an over 99% chance of not being investigated, prosecuted or convicted.

2. Top Three Prosecutorial Motivations for Tax Crimes: Deterrence, Deterrence, Deterrence

Given the staggering odds against anyone being criminally prosecuted and convicted, the very few cases the federal government prosecutes have to achieve the greatest deterrence possible for the country's voluntary self-assessment system to work. Prosecutors have to make each of the approximately 2500 charged criminal tax cases count in order to convince the

tens of millions of taxpayers that there really are dire consequences for committing tax offenses. Sending tax scofflaws to prison, seizing their assets, and exacting huge fines and penalties -- and doing so in the most public manner possible to achieve maximum deterrence with each case -- is the main agenda for tax prosecutions. Leveraging each case so that not only the defendant, his family, and his friends are specifically deterred, but the overall taxpaying community "gets the message" is among the prime missions of every tax prosecution. This directive reverberates in the Tax Division's Criminal Tax Manual, the United States Attorney's Manual, the IRS Manual, and the U.S. Sentencing Guidelines. For instance, the Introductory Commentary to Part T – Offenses Involving Taxation of the Sentencing Guidelines states in pertinent part: "Because of the limited number of criminal tax prosecutions relative to the estimated incidence of such violations, deterring others from violating the tax laws is a primary consideration underlying theses guidelines." As shown below, knowing that deterrence lays at the heart of a prosecutor's decision-making matrix provides a defense attorney with key ammunition in framing a declination argument.

3. How Did My Client's Case Land End Up on the Prosecutorial Radar Screen?

From the over 4,000,000 annual potential criminal cases, only approximately 4,000 investigations are initiated by the IRS each year. How does the IRS choose which ones to pursue? The leads for these investigations span the gamut from whistleblowers and "ex's" (e.g., ex-spouse, ex-partner, ex-employee, ex-computer programmer) to Revenue Agents conducting audits, Revenue Officers involved in collections, Fraud Referral Specialists, the Lead Development Centers, other federal or state agencies or even referrals coming out of family and bankruptcy courts. More recently, many referrals have emanated from international sources like the Joint International Tax Shelter Information Center (JITSIC), tax information sharing agreements, and foreign financial institutions.

Once the IRS determines it has a valid lead, the IRS can choose to open (or "number") its investigation administratively or through a grand jury. If the IRS

elects the administrative path, then its strict disclosure provisions prevent it from sharing information during that stage with the Department of Justice. Only once a referral is made for prosecution or a grand jury investigation does the Department of Justice have decision-making authority over the criminal tax case.

Over 25% of the criminal investigations initiated by the IRS on an annual basis do not result in prosecution recommendations by the IRS to the Tax Division. For the approximately 2800 out of 4,000 cases that are referred, these cases are the products of a tremendous amount of time and resources by the lead IRS Special Agent assigned the case, that agent's Supervisory Special Agent, the Assistant Special Agent in Charge, the Special Agent in Charge, and IRS Criminal Tax Counsel, who all review the investigation. A detailed Special Agent Report will have been prepared, reviewed, edited, and approved by multiple levels at the IRS before it reaches the Tax Division. Once the referral is made to the Tax Division, the case will either be kept by a Tax Division attorney who will run the prosecution from that point or the case will be sent out to the local United States Attorney's Office for prosecution or grand jury investigation. It is important to note that with very few exceptions, all criminal tax charges must ultimately be approved by the Tax Division.

Thus, a local United States Attorney's Office does not have unilateral discretion to decline a case, change a charge from a felony to a misdemeanor, or enter into a disposition for other than the "major count" (i.e., usually the tax year with the greatest tax loss) without running that decision by the Tax Division first. If a United States Attorney's Office chooses to decline a case and the Tax Division disagrees, the Tax Division has the ability to take over the prosecution of the case. On the other hand, if the Tax Division elects to decline a case, then that case cannot be prosecuted regardless of the position taken by the United States Attorney's Office.

The impact of a prosecutorial declination on the various stakeholders cannot be understated. A declination effectively nullifies the scores or hundreds of hours of IRS time (and prosecutorial time) devoted to the criminal case, even if a civil case can be salvaged to recover the tax, interest and civil penalties. If the case was the only or primary case being investigated by the lead

Special Agent and occupied one to three years of that agent's time, a declination will presumably not have positive consequences for that agent's career. While a prosecutor will rarely, if ever, admit that his declination decision weighed these collateral consequences, a defense counsel must be conscious of such consequences, particularly in a lengthy investigation.

4. How to Convince the Prosecutor to Decline the Case

With so much momentum generated toward filing charges once the charges have cleared the IRS' multi-layered review and landed on a prosecutor's desk, how can a defense counsel possibly convince the prosecutor to forego an indictment?

In order to be assured that a defense counsel will have the opportunity to meet with the Tax Division lawyer or Assistant United States Attorney, defense counsel must make a written request for a pre-indictment conference well prior to any charging decision being made. That request should be directed to the Criminal Enforcement Section Chief for the region in which the case has been investigated or the taxpayer resides (Western, Southern or Northern) and should include the taxpayer's name and identification number (e.g., Social Security Number). If the case has already been sent to a United States Attorney's Office, then a copy of the request should be sent to the Assistant United States Attorney assigned to the case and the Chief of the Criminal Division as well.

While there is no legal right to have a pre-indictment conference with the prosecutor, such conferences are routinely given and sanctioned by the Tax Division's Criminal Tax Manual and United States Attorney's Manual. The conference will be more a monologue by the defense counsel than a dialogue with the government attorney. During the conference, the Tax Division attorney will normally advise defense counsel of the proposed charges, the method of proof (e.g., bank deposits, indirect method), and the income and tax computations the IRS has recommended. The conference will not be a vehicle to discover or explore the government's evidence. Instead, defense counsel has the opportunity to present whatever arguments she wishes to convince the prosecutor to decline the case. The attorney's statements on

her client's behalf are not to be used by the government in general court proceedings as vicarious admissions of the client.

The arguments that resonate best with a prosecutor are ones that demonstrate how the prosecutor will lose in court if he brings the proposed charges. Framing one's attack in terms of "litigation risk" is crucial because the prosecutor's central mission of deterrence will fail miserably if the case is dismissed by a judge or the taxpayer receives a verdict of acquittal. Indeed, such a failure, if anything, may embolden the tax evading community who view the government's inability to convict an alleged tax violator as a sign that even in the unlikely event they get caught, they may prevail at trial. Moreover, such a failure will have wasted enormous amounts of prosecutorial and investigative time and resources that could have been devoted to other more meritorious cases.

To demonstrate "litigation risk," a defense counsel must appreciate the fairly unique and very difficult burdens a prosecutor faces in bringing criminal tax charges. Unlike in a civil case where the burden of proof is preponderance of the evidence or clear and convincing evidence, the burden of proof in a criminal tax case is the highest in our courts -- beyond a reasonable doubt. The fact finder in almost all cases is not a judge, but a jury. In contrast to a civil jury which may be composed of six members, a criminal jury is composed of 12 members and their verdict must be unanimous. With respect to the mens rea or mental state required for a criminal tax charge, the prosecutor faces the highest standard in the law – willfulness -- the intentional violation of a known legal duty. In addition, the prosecutor must prove a negative, namely, that the taxpayer did not have a subjective good faith belief in the legitimacy of her tax position (the *Cheek* defense), in order to obtain a conviction.

While a defense counsel can present "litigation risk" arguments to the IRS during the investigation, these arguments may receive a more favorable audience with a prosecutor. In many ways, a prosecutor will be more sensitive to "litigation risk" because the prosecutor will be the one in charge of the trial, figuring out how to admit evidence, examining and cross-examining witnesses, dealing with the judge's rulings, and assessing how

the case will play with a jury. For instance, while the IRS may use information from a "dirty" informant with a criminal record to build its case, the prosecutor may be more sensitized as to how a judge and a jury will consider the evidence, particularly in light of the jury instructions that will be given to question it more carefully. Similarly, if the prosecutor will not be able to properly authenticate foreign records and such records are necessary to prove the taxpayer's guilty mental state, then the mere fact that the IRS obtained the documents during its investigation is of little solace to the prosecutor.

In fashioning "litigation risk" arguments, a savvy defense counsel will have performed essentially a mirror investigation of the IRS' investigation, interviewing as many of the witnesses the IRS has interviewed as possible, accumulating all the documentary evidence gathered by the IRS, and trying to stay one step ahead of the IRS on the information curve about the case. If the investigation started administratively, defense counsel will try to keep track of the investigation through the IRS summonses issued and witnesses interviewed. If the investigation is in the "secret" grand jury phase, defense counsel can attempt to monitor the investigation by trying to interview any witnesses called to testify before the grand jury and discovering not only the testimony given but the questions asked. In many respects, the questions asked are as important as the answers given because they will alert defense counsel to the focus of the criminal tax investigation.

There is no substitute for knowing the facts and applicable law of the case as well or better than the prosecutor in trying to convince the prosecutor to decline the case based on "litigation risk." For instance, if the IRS operated under the assumption that the cash found in a client's safety deposit box came from his business when the defense counsel has ironclad proof it came from a nontaxable source like an inheritance, then a prosecutor may perceive the problems with his case as insurmountable and decline to proceed. Other examples of "litigation risk" might include establishing unreported deductions that fully offset unreported income in a tax evasion case; providing legal or accounting opinions that the client relied on to justify her good faith position taken on her returns; highlighting Fourth Amendment

problems embedded in the search warrants used to obtain key evidence; or demonstrating the lack of credibility of crucial government witnesses (e.g. financial incentives, personal vendettas, past acts of dishonesty). "Litigation risk" factors can also encompass potential government intrusions into privileged material, difficulties in bringing witnesses to court, particularly overseas ones, and significant impediments in bringing the client to court, particularly if the client is not a U.S. citizen and is living abroad.

In addition to demonstrating as much "litigation risk" as possible, a defense counsel should be prepared to argue in the right case how similarly situated taxpayers were not prosecuted criminally, but resolved their matters civilly. The Tax Division's mantra is "broad, balanced and uniform criminal tax enforcement." If similarly situated taxpayers in the same or other jurisdictions did not get indicted, then uniformity demands an equal result in the client's case. Obtaining this information is easier said than done since there is no publicly available database showing what cases have received criminal declinations. In large-scale, multi-defendant cases, one can attempt to track which defendants have and have not been offered civil-only resolutions. For other types of cases, obtaining this information on a district or circuit basis will require significant networking with other defense counsel and research on the Internet.

To the extent that a client paid off the outstanding tax liability at issue during the investigation or is in a position to do so along with significant civil penalties, a defense counsel should trumpet these "lack of loss" and "making the government whole" arguments as additional factors militating in favor of a civil disposition.

Defense counsel should also be prepared to humanize their client as much as possible. If a prosecutor is on the fence as to how to proceed, establishing that one's client is a good person or a good corporate citizen who made a mistake rather than a bad person or company who got caught may tip the balance toward a declination. In this regard, defense counsel must be able to effectively present the positive highlights from the client's life story including charitable and communal commitment, the lack of any significant criminal record, a high degree of tax compliance and taxes paid outside the years at

issue, any serious medical conditions, and any extraordinary family responsibilities. In addition, defense counsel in the proper case need to be able to detail the draconian collateral consequences of a criminal charge ranging from loss of employment and deportation for a non-United States citizen to revocation and debarment for clients with professional licenses. For a corporate client, a defense counsel should focus on many of the same criteria emphasized by the Sentencing Guidelines including prior civil or criminal history, effective compliance and ethics programs, self-reporting, cooperation, and collateral consequences to the organization.

5. When Should A Defense Counsel Go For The Holy Grail Of A Declination?

The decision of whether to lay out some or all of one's cards to a prosecutor to try to obtain a declination is one of the hardest and most important decisions a defense counsel will make. A defense counsel must factor into the decision the strength of the arguments and evidence to be presented, the level of trust in the prosecutor's judgment and ability to view the presentation objectively, and the repercussions to the client of getting indicted at all versus prevailing at trial at a much later stage. The stronger the arguments and evidence, the greater the trust, and the more significant the repercussions of an indictment, the more likely a defense counsel will come out in favor of full disclosure to obtain a declination. If a defense counsel has a legal or factual defense that is irrefutable and effectively decimates the prosecutor's case, then playing all the cards of such a defense with a reasonable prosecutor may make tactical sense. If the ramifications of the mere filing of an indictment are too profound, e.g., irreversible reputational or financial damage, then a defense counsel may have no choice other than to lay out the complete defense to stave off an indictment.

On the other hand, if a client can survive an indictment but wants to best position themselves for a victory at trial and if the problems pointed out in the prosecutor's case can be fixed prior to indictment or trial or do not completely eviscerate the case, then the wisest course of action may be to lay down no cards or only a few cards.

If a complete declination is not in the cards, then a defense counsel must consider whether to go for "Plan B." Plan B in this case constitutes a full disclosure of the defense with the lesser objectives in mind of getting a different type of charge (i.e., a misdemeanor instead of a felony), a lower tax loss, a fewer number of counts, a declination against proceeding against others potentially involved in the case (e.g., relatives), and/or the most favorable sentencing recommendation possible. If the client cannot suffer any conviction at all, understands the harsh sentencing consequences if found guilty after trial, and will not authorize Plan B, then the best course of action may be no action at all.

Legend has it that only those worthy of the Holy Grail had any chance to obtain it. While a prosecutorial declination may seem as remote and idyllic a goal as the Holy Grail, if a defense counsel's case is legally and factually worthy of the challenge, then that elusive prize should be pursued with commensurate fervor.