American Bar Association Taxation Section
Criminal and Civil Tax Penalties Committee
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Important Developments: Criminal

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1. Interesting new cases.

Multiagency investigation, including IRS-CI, results in Bitcoin ATM operator agreeing to plead guilty to running unlicensed money remitting business.

The IRS, FINCEN, SEC, and CFTC, among others, have long been warning that cryptocurrency enforcement actions, including prosecutions, are in the pipeline. One case has come through the pipe, with more promised.

In what the Department of Justice billed as the first-of-its-kind prosecution, a Los Angeles man pled guilty to having operated a virtual currency exchange business that services, among others, criminals who were laundering criminal proceeds.

Although the case in many ways fits a standard profile for a defendant having laundered funds for drug dealers, what made defendant Kunal Kalra unique was his use of an anonymous ATM that permitted his customers to exchange a minimum of $5,000 per transaction to and from Bitcoin. Kalra, whose nicknames included “coinman” and “skecklemayne,” ensured anonymity by using a kiosk that permitted transactions without the user inputting any identifying information or having their images recorded on a video camera. Kalra earned a commission on each transaction, but his luck ran out when he exchanged $400,000 of self-reported “drug proceeds” from an undercover federal agent.

There are many questions unanswered, including whether the manufacturer or distributor of the anonymizing kiosk could face any repercussions. There are parallels with the “tax zapper” cases discussed below.


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Owner of restaurant that purchased “tax zapper” software pleads guilty to tax conspiracy.

Back in December 2016, a point-of-sale-system salesman named John Yin pled guilty to selling a “tax zapper” add-on to the POS systems to dozens of restaurants, including eight in the Seattle area.  https://www.justice.gov/usao-wdwa/pr/everett-software-salesman-pleads-guilty-selling-tax-zapper-software-enable-cheating

The POS systems were made by a Canadian company that had offices in China, which company had defeated an earlier prosecution by Canadian authorities by successfully claiming that selling such software, which deletes transactions in a hard-to-spot way, is not itself a crime.  https://www.bccourts.ca/jdb-txt/CA/13/03/2013BCCA0333.htm

Although one of the eight restaurant owners was prosecuted by the State of Washington, it took nearly three years to prosecute what appears to be one of the remaining restaurant owners.

On August 25, 2019, the US Attorney for the Western District of Washington announced that two owners of a Seattle-area Thai restaurant chain used a zapper program for two of their restaurants, resulting in more than $1 million of underreported cash income.

As is characteristic of many of these cases, the restaurants used the unreported cash to pay its employees under the table.  Less common in zapper cases is the fact that the owners diverted funds to unreported Thai bank accounts.  This could be the reason that they were prosecuted where other restaurant owners in the scheme have not yet been charged.

Both state and federal taxing authorities care deeply about such cases, because they impact state sales and income taxes and federal income and employment taxes.  The State of Washington coordinated with the IRS on this prosecution, and other states including Wyoming and California are doing the same.  This has included training of agents to recognize issues; if the POS system is downloaded, a skilled investigator can see shadows of the deleted entries, even if the business owner was careful to avoid keeping a second set of books (as many do).

Another purported first – charging defendant with filing a false “streamlined” submission.

DOJ has been saying for the past few years that it has started scrutinizing closely streamlined filings, and we’ve just seen proof.  DOJ issued a press release announcing the first indictment stemming from a false streamlined filing.

In particular, on August 22, 2019, DOJ obtain a superseding indictment in the Southern District of Florida that included a 26 U.S.C. Sec. 7206(1) count for the defendant (Brian Nelson Booker) allegedly having filed a false streamlined submission that stated the defendant had only learned about the FBAR filing requirement in 2008 and believed only personal accounts needed to be reported.  The government alleged that the statement was false in that the defendant claimed his conduct was non-willful.
However, these were not the only charges. Mr. Booker was charged with failing to file FBAR forms and filing false tax returns, and the indictment lays out a series of actions including using an “insurance wrapper” that made it appear as if his foreign accounts were owned by a foreign insurance company instead of himself.

And, another former IRS employee, an attorney, was convicted of tax evasion and lost his motion for new trial.

Craig Orrock is a former attorney who worked for the IRS for several years. He spent the bulk of his legal career, however, as a sole practitioner with a tax law focus. After a week-long jury trial, Orrock was found guilty of two counts of evasion of payment and assessment of tax and one count of attempt to interfere with the administration of internal revenue laws.

Apparently, Orrock had a long history of concealing income by providing the IRS false information, using a web of bank accounts and fake businesses. When enforcement efforts were made by the IRS, Orrock maneuvered funds through his accounts, submitted a false Offer in Compromise, and filed several frivolous bankruptcy petitions to stay the IRS’s collection efforts. *U.S. v. Orrock*, 123 AFTR 2d 2019-2242 (DC NV) 06/13/2019.

2. **Monthly Tax Prosecution Numbers Leveling Out?**

Although the IRS has been touting its recent hiring spree, it can take years before new employees are finishing cases. In early 2019, the IRS reported an uptick in its prosecution numbers with an implication that the upward trend would continue. The reality is, the numbers went up and are now back down again.

The July numbers, published on August 24, 2019, reflect an 11.8% decline from last year – which was already one of the worst years on record – and a 5.2% decline from the prior month. Consistent with recent years, prosecutions were down more than 50% compared with five years ago, which period had the benefit of many smaller cases as well as a much larger group of special agents. As with any statistics, it will take more time to know whether the trend is generally upward, sideways, or down.

https://trac.syr.edu/trareports/bulletins/tirs/monthlyjul19/fil/

3. **The Tax Division Continues to Focus on Employment Tax Enforcement.**

Since the last meeting, there are have been several reported guilty pleas to employment tax-related charges and at least one reported sentencing. The list of injunctions obtained by the Tax Division also continues to grow.

https://www.justice.gov/tax/recent-criminal-employment-enforcement-news
4. **Chief Counsel Updated Guidance on Assessing Interest and Penalties on Criminal Restitution.**

In July, the IRS issued Chief Counsel Notice 2019-004 (the “Notice”) which updates guidance on the assessment and collection of interest and penalties on criminal restitution. The Notice follows the Tax Court’s decision in *Klein v. Commissioner*, 149 TC 341 (2017).

The IRS may assess and collect criminal restitution ordered under 18 U.S.C. section 3556 for failure to pay any tax imposed under Title 26 just as if the restitution were a tax. Under Section 6601(a), interest accrues on any amount of tax imposed under Title 26 if not timely paid.

On August 26, 2011, IRS Chief Counsel issued Notice 2011-018, which stated that interest under Section 6601(a) would accrue on restitution assessed under Section 6201(a)(4)(A) until fully paid. On October 3, 2017, in *Klein*, the Tax Court held that the IRS was not actually authorized under Section 6201(a)(4) to assess and collect underpayment interest under Section 6601, or failure to pay penalties under Section 6651(a)(3) and that restitution clearly is not a tax imposed by Title 26 as required by Section 6601.

The Notice, consistent with *Klein*, provides that interest on restitution should be abated if the taxpayer challenges the accrual of interest on restitution assessed under Section 6201(a)(4)(A) in litigation, or otherwise seeks to abate the interest. The Notice also adds that interest should not be abated if it is specifically ordered.

The Notice also explains that the Section 6651 failure to pay penalty does not apply to criminal restitution assessed under Section 6201(a)(4)(A), but that if ordered by the Court, the taxpayer will be liable. This could happen if the taxpayer has agreed to be liable for the penalty as part of a plea agreement, or if the restitution is based on a previously assessed tax liability that included a failure to pay penalty.