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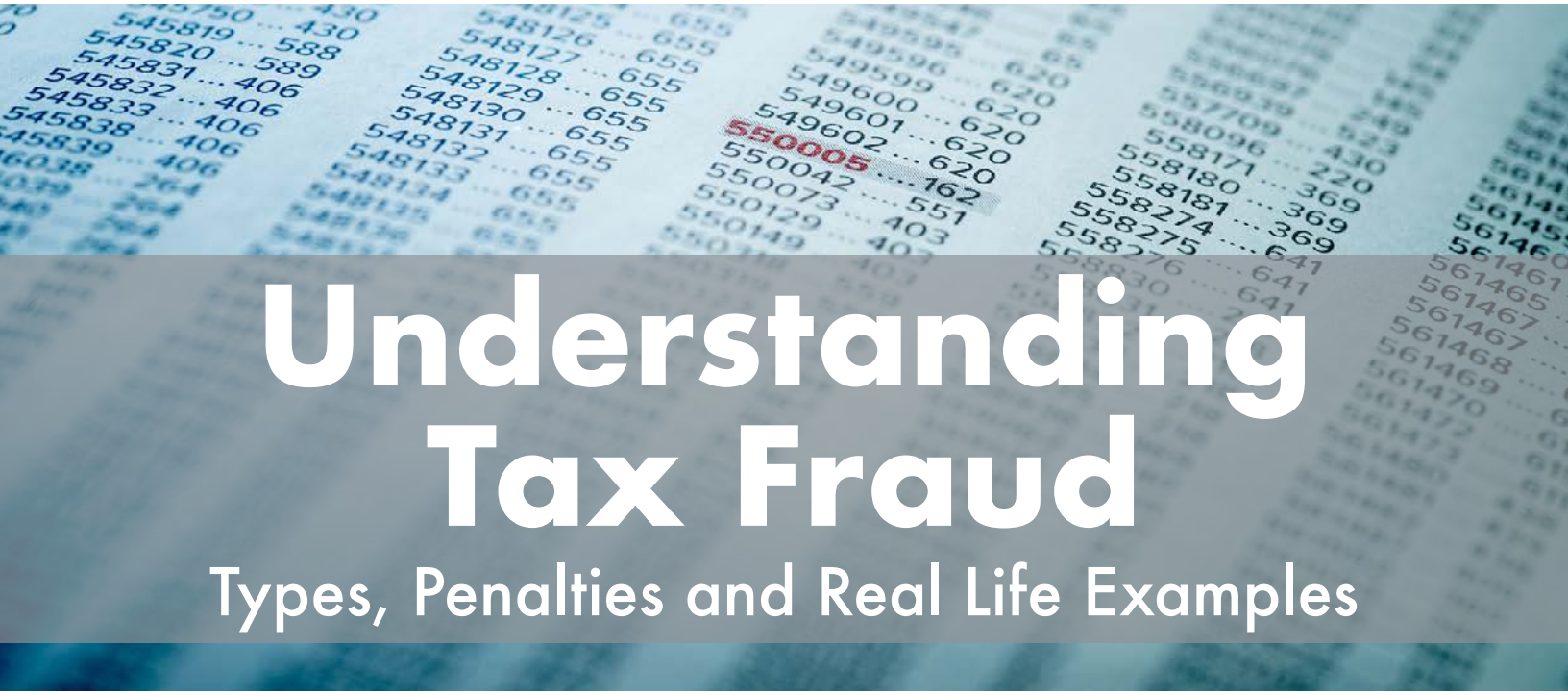

Understanding Tax Fraud

Types, Penalties and Real Life Examples

Tax Fraud. It is more than just a simple error in judgment. There are many kinds, all with penalties, and without proper advice and guidance, it's easy for a small matter to spiral out of control. Filing a false tax return or other document is treated seriously by the Internal Revenue Service. If its investigation turns up substantive information, civil cases can be referred for criminal tax investigation. Arrests and tax-related criminal charges could follow.

So it's important to not take a tax fraud charge lightly, and hopefully this document can help you understand it better. However, the attorneys at Robert J. Fedor, Esq., L.L.C. are knowledgeable when it comes to providing representation for those facing life changing criminal charges involving tax fraud. An experienced tax attorney with knowledge of IRS investigations and tax law is vital in cases involving fraud charges. For immediate representation, contact Robert J. Fedor, Esq., L.L.C. at 800-579-0997.

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1 PART 1: **Defining Tax Fraud**

What Exactly IS Tax Fraud?

Tax fraud is more than just a mistake; it is a willful attempt to get out of tax obligations. The key to a tax fraud claim is that the person accused of the crime willfully or intentionally committed acts to avoid paying taxes. Examples include failing to file an income tax return or preparing a false return.

Although the penalty for a simple mistake may seem severe, those that apply in cases of a tax fraud conviction are even more severe. A failure to file can come with up to one-year imprisonment and a monetary penalty of $100,000, while an attempt to evade taxes can come with up to five-years imprisonment and a $250,000 fine.

How Does the IRS Determine Tax Fraud?

The IRS defines tax fraud as "the willful and material submission of false statements or false documents in connection with an application and/or return." To make this determination, investigators will look for any indicators of fraud such as, but not limited to:

- Underreporting income
- Using a false Social Security number
- Falsifying documents
- Intentionally failing to pay taxes

If these common indicators are absent, the IRS typically assumes that an unintentional mistake has occurred due to negligence. Though this typically does not lead to criminal charges for tax fraud, mistakes with your taxes can lead to an accuracy-related penalty that equates to 20 percent of the underpayment.

Anyone could be caught off guard when they are assessed this penalty, which is why it's important to make sure all tax information is accurate and truthful before submitting it to the IRS. It's also important to remember your right to an attorney as well, especially if you believe a tax fraud charge has been levied against you in error.

Understanding the Difference Between Tax Evasion and Tax Avoidance

Few people enjoy paying taxes, but some taxpayers avoid taxes, while others evade them—what's the real difference?

The Internal Revenue Service (IRS) notes the income tax system in the U.S. is based on voluntary compliance. It is a volunteer action right up to the point that you do not volunteer to pay the taxes that are required of you. Failure to file your income tax return or filing a fraudulent tax return could earn you a criminal tax charge at some point.

We talk a lot about types of tax fraud, how it occurs, and the consequences of conviction in a criminal tax matter brought by the IRS. As noted, tax fraud is one way that people evade their taxes. Before they took a criminal turn, the idea was to avoid paying taxes altogether.

Avoiding your tax burden is perfectly legal. In the U.S., there are a number of ways that assets can be held, taxes can be paid, and deductions can be used to reduce the amount of tax you pay on a quarterly or annual basis. Deferred tax plans are often used around retirement planning to shield savings and maximize wealth.

Tax Evasion is Big Business

On a global scale, tax evasion is big business. The use of offshore tax havens and other secrecy jurisdictions can skirt dangerously close to tax evasion. In recent years, the IRS has offered programs to prompt taxpayers into compliance who were on the wrong side of the tax evasion/tax avoidance question.

While it is legal to hold money in foreign bank accounts, taxpayers and institutions must file reports like the FBAR and FATCA to ensure their wealth is reported and appropriate taxes paid.

The bottom line is that the U.S. requires qualified citizens to pay appropriate taxes. That doesn't mean you should pay more than you owe—or more than you might owe if you took advantage of appropriate tax avoidance strategies. When you are concerned about what you may pay in taxes—talk to an experienced tax attorney to learn how you can avoid taxes, without being guilty of evading them.

2 PART 2: **Types of Tax Fraud**

Willful Failure to Pay Income Taxes

The Internal Revenue Service claims that about 1 out of every 6 taxpayers fails in one way or another to comply with the tax code. If the federal agency's estimate is accurate, you might reasonably expect the numbers of tax-related arrests to be significantly higher than they are now.

The reason why not every sixth person you know is facing criminal charges is because the IRS distinguishes between income tax fraud and negligence.

Tax fraud is a deliberate attempt to evade taxes or to defraud the IRS. Tax fraud takes place when a person or company willfully does one of the following:

- Intentionally fails to pay taxes owed
- Willfully fails to file a federal income tax return
- Fails to report all income
- Makes false or fraudulent claims

People Make Mistakes

It goes without saying that the tax codes are long and dense and sometimes nearly indecipherable—even for accountants paid to make sense of them. In that regard, the IRS acknowledges that sometimes mistakes happen and people will assume A about the code when B actually applies.

Without evidence of fraud or other criminal activity, the IRS will typically assume you have made an honest mistake on your returns. That's about the extent of the agency's willingness to forgive, however, as even unintentional mistakes can result in a 20 percent penalty to the taxpayer.

There are certainly circumstances in which the IRS assumes an unintentional error is actually a deliberate attempt to defraud. In these situations, the taxpayer can face serious consequences, including prison time. Many will turn then to experienced tax law attorneys to help them resolve disputes with the IRS. In some cases, negotiations can lead to resolution of the issue without any criminal charges; in other cases, vigorous representation in court is required.

Making a Frivolous Tax Claim

One of the many things that makes the U.S. a great nation is that we have the freedom to express our opinions, even when those opinions run counter to official government policy. For instance, people are free to argue that the federal income tax is illegal and that it violates several amendments of the Constitution.

People are free to make the argument, but they are not free to refuse to pay the income tax they owe. Because some of those who argue that the income tax is illegal, immoral and unconstitutional are articulate and persuasive, sometimes people give in to temptation and file returns making "unreasonable and outlandish claims," the IRS says, "to avoid paying the taxes they owe."

When you file that return, trouble can begin. No matter how reasonable the argument sounded in the book you read or website you visited, the IRS has very likely heard the argument before, taken it to court and prevailed. In fact, penalties levied against those who take up the court's time with "frivolous arguments" are getting harsher.

You can argue that only employees of the federal government are subject to the income tax, or that filing a return is voluntary or that Federal Reserve notes are not income–the anti-tax arguments go on and on–but at the end of the day, you must send in an accurate income tax return.

Other Common Tax Fraud Crimes

Within the IRS, the Criminal Investigation (CI) unit takes a hard look at tax fraud, tax-associated money laundering, and illegal proceeds earned by legitimate companies through a variety of fraudulent methods. Some of the crimes pursued by CI include:

- **Employment and payroll tax fraud:** Payroll tax issues are common. Underreporting workforce numbers, collecting payroll taxes (federal unemployment, social security, and withholding taxes) and failing to pay them over to the IRS, or paying employees in cash under the table are just a few of the schemes pursued by the IRS.
- **Refund fraud:** Most people know that filing a false income tax return could turn into tax litigation. Individuals and tax preparers engage in refund fraud and sometimes identity theft in order to obtain an unearned tax refund. This is also the realm where fake deductions, exemptions, and business expenses come into play.
- **Abusive tax schemes:** U.S. taxpayers who avoid filing regulatory reports like FBAR and FATCA could find themselves facing an IRS criminal tax investigation. With the proliferation of secrecy jurisdictions, individuals with significant wealth may seek the greater privacy available through offshore tax havens. There is often a fine line between an abusive tax scheme and a tax option used by an unwitting taxpayer trying to make legitimate use of offshore tax resources.

Committing tax fraud or tax evasion could provoke the interest of the IRS. But remember, the IRS is both underfunded and short-staffed these days. An important aspect of any tax crime is intent. It takes less time and money to work out a civil arrangement with a delinquent taxpayer, then it does to try and convict that same taxpayer of a criminal offense.

Employee Tax Fraud Explained

Criminal tax investigations are often aimed at business owners or C-suite executives. Just as often, it is the rank-and-file who perpetrate tax fraud. Monies gained from tax crime often go to pay debt or pay for personal comforts.

When an employee embezzles, it is important for an employer to obtain experienced legal advice about reporting the loss to the IRS, and properly classifying repayments on those embezzled funds should they occur. At the outset of discovery of the theft, employers can provide the IRS with information about the loss. That said, the report and steps to deal with the embezzlement should be reviewed with general counsel or a qualified tax attorney before contacting the IRS.

Common Employment Tax Fraud Scams

While failure to properly remit or pay over employment taxes may not seem the most serious crime, it is a hardball issue for the IRS. Conviction on one count of employment tax fraud can earn five years in prison. The IRS routinely identifies and investigates employment tax scams that take a number of forms, including:

- **Employment leasing:** When an employer outsources their personnel and payroll responsibilities it is called "employment leasing." While an employer contracts help from the outsourcing company, the outsourcer is responsible for collecting and paying over employment taxes. Sometimes these middleman organizations pocket employment taxes, close up shop, and disappear when notified of an impending IRS civil audit—leaving a significant tax liability.

- **Pyramiding:** A common employment tax scam is the practice of "pyramiding," which is the IRS term for business owners who withhold payroll taxes and pocket the money with no intention of turning it over to the IRS.

- **Cashing out:** When employers or outsource employment agencies pay employees in cash, the opportunity for tax crime rises across the board. In addition to skirting Workers' Compensation laws, employers can falsify payroll records, underreport the number of employees on the books, or underreport the amount of payroll taxes owed.

Tax Preparer Fraud

The IRS routinely brings criminal tax charges against preparers. Tax fraud is serious for the accused and for their clients, especially if the client had knowledge, or should have known that a false tax return was filed on their behalf. Here are a couple of recent IRS prosecutions:

- A Charlotte, North Carolina woman pled guilty to "aiding and assisting the preparation of a false tax return." The woman admitted to the most common forms of tax preparer fraud, enhancing expenses, creating fake deductions, and claiming education credits that were non-existent. The amount of tax lost to the IRS from her conduct amount to approximately $500,000 and she faces up the three years in prison, probation, restitution, and penalties.

- Facing similar consequences, a Rhode Island man also faced the long arm of the law for his habit of filing fraudulent tax returns between the years of 2011 and 2015. Like the North Carolina tax preparer, the accused sought to boost refund checks for his client by creating false deductions, and inflating expenses. He also amplified charitable donations and falsified home mortgage and home energy improvement deductions.

- On a larger scale, a pair of Southern Florida tax preparers were shut down by the IRS and face injunctions and the permanent loss of the livelihoods for their part in scamming the IRS and their clients. Using the same sorts of tactics described above, a tax preparation business inflated deductions and expenses on the tax returns of their client to increase the amount of the refund their client would receive. When the refund returned, the tax preparers pocketed the excess without the knowledge of their victims.

3 PART 3: **Tax Fraud—Precautions and Preparations**

Avoid Tax Fraud: Know Who is Preparing Your Return

The non-profit consumer watchdog, Consumer Reports, and the IRS offer straightforward advice for choosing a reputable tax preparer. Tips include:

- **Check the credentials of your preparer:** The IRS provides a Directory of Federal Tax Return Preparers as a tool for finding qualified tax assistance. There are also search tools for CPAs and tax experts from association resources. Conduct an online search, ask for references—and check them.
- **Look for a preparer familiar with your background:** If you have complicated tax filings, including FBAR or FATCA filings, it is critical for you to work with an accountant or attorney capable of preparing a tax return that responds to all of your financial needs. Read carefully through your return and ask questions before signing on the bottom line.
- **Speak up if there are problems with your return:** If you are alerted by the IRS to problems with your return, speak with your tax preparer immediately.

You can file a complaint with the IRS if you have financial exposure due to a tax preparer.

Questions to Ask to Avoid Tax Preparer Fraud

The IRS cautions individuals and businesses to scrutinize their tax preparer on an ongoing basis. If you can answer "yes," to any of the following questions, proceed with caution:

- Does your tax preparer ask you to sign a blank return or are you expected to file your return or other regulatory filings without careful review?
- Are the fees you pay your accountant or tax preparer based on how much of a refund they claim to be able to provide for you?
- Do you have concerns that your accountant or preparer may not have credentials or contemporary knowledge of recent legislative and tax changes?

Good to Know: Penalties for Criminal Tax Fraud and Civil Tax Fraud

Civil tax fraud penalties are limited to monetary consequences and do not result in a criminal prosecution. Common civil infractions and their associated penalties include:

- **Fraudulent failure to file a tax return:** 15% of the net tax due for each month up to five months with a maximum penalty of 75% of the unpaid tax
- **Filing a fraudulent tax return:** 75% of the underpayment amount

Criminal tax fraud can result in a significant period of imprisonment, among other penalties. For criminal tax fraud, the potential penalty is directly tied to the specific criminal charge you face. For example, some common crimes and punishments related to criminal tax fraud include:

- **Tax evasion:** This crime carries a maximum sentence of five years imprisonment and a fine up to $100,000 for individuals or $500,000 for corporations.
- **Willful failure to pay tax, failure to file or failure to keep sufficient records:** This crime carries a maximum term of imprisonment of one year, accompanied with a potential fine up to $25,000 for individuals or $100,000 for corporations.

Tips to Protect Yourself Against Employment Tax Fraud

Diverting employment taxes is easy—but how do you protect your business and prevent an employment tax dispute with the Internal Revenue Service (IRS)?

In a business of any size, employment tax collection and pay over to the IRS is an important responsibility. Depending on your business or corporate structure, responsibility for payment of employment taxes may land in the finance department, a sole accountant, or an outsourced vendor. Regardless of your business operation, you are responsible for the money owed to the IRS.

Some business owners are deep into deliverables, growth strategies, and staying afloat amid competition. Backroom operations like payroll are easy to delegate. In Ohio and elsewhere, the IRS expects employers to accurately report on income and taxes withheld. Turning over employment taxes to the IRS is part of that. Consider these tips for keeping your books and payments to the IRS above board:

1. **Clarity:** Classify and onboard employees properly. Misclassification of employees as contractors who are operating as employees is a quick tip-off that there are systemic business problems. Employee misclassification is a form of tax evasion. Whether you onboard your employees or use a service, be sure you can defend your classification.

2. **Maintain process:** Payroll accounting can be complicated. Employees without adequate training may not have the expertise and current understanding of regulations to handle the job. The individual, team, or vendor you put in place to manage your company finances and withholdings have direct impact on the viability of your company and your ability to respond without fear to an IRS audit. In short—be sure you can trust the people handling your money.

3. **Checks and balances:** Put checks and bounds in place to avoid payroll tax fraud. Appropriately restrict access to your accounting function and spread responsibility for different payroll functions between personnel. Choose your payroll accounting system software carefully and use alerts to track inconsistent or suspicious activity. Digital time-keeping should be part of the system to avoid payroll errors and collusion between employees and finance personnel in padding hours. Overall, ensure your process is being routinely reviewed and you are signing off on at least monthly reports that your operations are clean.

There is little to no defense for a business owner who claims they delegated their employment tax function to an employee or vendor. The IRS can apply a trust fund recovery penalty (TFRP) against the business owner and anyone in the organization who is responsible for paying withholdings but willfully fails to do so. With a TFRP, your personal income and assets are not protected if the IRS chooses to go after you.

Collection and remittance of payroll taxes is an important function for any business. Failure to account for employee withholdings has long-term consequences for the business owner, the business, and the employees whose social security benefits depend upon those payments.

You're Charged with Tax Fraud. Now What?

Here are straightforward tips to avoid headlines and resolve the charges of tax fraud:

- **Respond immediately:** Take quick action if you receive notice or become aware of interest by the Internal Revenue Service (IRS). When significant wealth, complicated tax avenues, or criminal charges could be involved, contact a tax attorney experienced with IRS investigations. Connecting with knowledgeable legal counsel straight away could be your strongest move for avoiding tax litigation.

- **Preserve your records:** Locate and preserve all records that you feel could be of interest to the IRS. Do not tamper with evidence, destroy records, or make phone calls to potential witnesses about what they should or should not say. If you destroy evidence or try to tamper with witnesses, it could make things worse.

- **Engage the process:** Your tax lawyer will spearhead and guide you through interactions and meetings with the IRS. Be honest and cooperate. Although it is a stressful process, little is gained by defensive posturing. Work with your attorney to ensure that your explanations are consistent across venues and align with the overall situation.

- **Work toward a solution—not litigation:** Even if it is found you have significant tax liability, your attorney can work toward options that may not involve trial, but allow you to repay monies you are found to owe. Prosecution takes time and resources for the IRS, and you may be able to avoid a criminal charge, or face a lesser charge depending on the seriousness of the allegations.

Of course, the best way to avoid a tax controversy is to ensure that you meet FBAR and foreign bank account reporting guidelines, pay your taxes, and work with best-in-class accountants and tax preparers. When there are issues or a tax crime allegation is pending—contact a tax attorney with the defense experience you need to keep you from career or reputational damage, financial loss, or prison.

Will I Be Charged with Criminal Tax Fraud?

Statistically speaking, the chances of any given taxpayer being charged with criminal tax fraud or evasion by the IRS are minimal. The IRS initiates criminal investigations against fewer than 2 percent of all American taxpayers. Of that number, only about 20 percent face criminal tax charges or fines. In a recent year, only less than 2,500 Americans were convicted of tax crimes – approximately .0022% of all taxpayers. Additionally, the "unofficial" minimum amount of taxes owed before the IRS will choose to file criminal charges is around $70,000, in cases involving multiple years of fraud.

The term tax fraud is a general one which can refer to a number of different laws found in Title 26 (the Internal Revenue Code) and Title 18 of the United States Code (or "U.S.C"). The main distinguishing feature of tax fraud is the taxpayer's intent to defraud the government by not paying taxes that he knows are lawfully due. Tax fraud can be punishable by civil (i.e. money), criminal (i.e. jail time and money) penalties, or both. For example, a taxpayer can commit tax fraud and be punished under 26 U.S.C § 6663 with civil penalties, without actually being charged with criminal tax evasion under Title 26 U.S.C § 7201.

If you have concerns or fear you may be facing criminal tax charges, this eBook will help to educate you on the basics criminal tax fraud and your personal rights. We invite you to download our eBook and as always, please contact the experience tax attorneys at Robert J. Fedor, Esq., L.L.C. with any questions.

Download Our IRS Criminal Tax Fraud eBook

4 PART 4: **Recent Stories of Tax Fraud**

Tax Evasion

A New York family decided to do more with their dough than just make pastries to sell at their three donut shops.

In October 2020, a federal grand jury returned an indictment against John and Helen Zourdos and their son Dimitrios. The family lives in Rome, New York and were charged following an IRS criminal tax investigation that raised allegations of felony tax evasion, conspiracy to defraud the IRS, and filing false tax returns. The charges arise from their management of their three donut shops, two in Rome and one in New Hartford.

While the indictment was bad, the jury verdict was worse. Despite a considerable amount of evidence against them, the defendants took the matter to trial. The prosecution produced several former employees who provided testimony on business practices that included:

- Employees were advised to clock in for 40 hours only, while they were routinely working overtime. Employees were paid cash for their overtime and not advised that employment taxes were owed on cash paid under the table.
- Employees were instructed to direct regular deposits of unaccounted business proceeds into the personal bank accounts of family members.
- The family maintained a notated set of books from which unaccounted proceeds could be calculated. Overall, the IRS determined the family evaded more than $650,000 in taxes and siphoned $2.8 million into their personal accounts from 2013 to 2017.

The donut business was good and the money the family kept off the books paid for lifestyle enhancements including travel and luxury vehicles.

The defendants were convicted of conspiracy to defraud, tax evasion, and filing fraudulent tax returns. John and Helen Zourdos provided incomplete and false information to their accountant, leading him to file inaccurate individual and corporate tax returns on their behalf.

In this instance, tax evasion was an established pattern for these small business owners, not a one-time deal. Cooked books, cash under the table, false tax returns, and eventually, allegations of criminal tax fraud and conviction.

For any individual or business owner engaged in a tax scheme, or who knows they are walking a line with their employment taxes or falsified corporate or individual tax returns, talk to a trusted criminal tax defense attorney now. If you are caught, the consequences are more difficult to mitigate than if the matter is approached before the IRS is involved.

Spending Employee Withholding

Sometimes an employment tax dispute is more than that. For a New York businessman, stashing the payroll taxes became a habit, and then a tax crime.

It is the responsibility of business owners in the U.S. to withhold certain wage taxes and pay those taxes over to the Internal Revenue Service (IRS) along with payment of their own withholding taxes. Seems pretty simple. Unfortunately, employment tax fraud is common. That pot of cash withheld from employee taxes can sing a siren song to business owners short of cash, trying to improve their bottom line, or just dreaming of a new car or other fancy trimming.

As we have discussed before, the efforts of the IRS to pursue business owners for their tax obligations is just as common as the crime itself. In the case of Mr. Dean Whittles, an IRS criminal tax investigation found Mr. Whittles failed to pay $617,843 in payroll taxes. An experienced entrepreneur, Mr. Whittle formerly owned several businesses in the Syracuse area, including the popular collegiate watering hole DJ's on The Hill, Dejon's Hair Designs, and several other salons.

Between the years of 2016 and 2019, Mr. Whittles collected employee withholding taxes but never quite got them to the IRS. Instead, Mr. Whittles paid other business and personal expenses. While the story is not new, there are underlying points to be made here. As a criminal tax matter, spending employee withholding is fairly likely to be identified by the IRS. Failing to pay over withholding is not a victimless crime. Employees expect the benefits of paying into the American social safety net.

Disputes over employment taxes that have been embezzled never end well for business owners who are held personally and professionally responsible for the lost funds. In this case, it was the business owner who took the funds—and pled guilty to the charge. As a result, he will be repaying $617,843 of those taxes to the IRS. In other cases, an employee siphons off the funds, which still leaves the business owner on the line through Trust Fund Recovery. Business owners are responsible for payment of withholding taxes regardless of their delegation of the role.

The last point of payroll tax theft and other business-related tax crime—speak with a criminal tax defense attorney as soon as possible if you want to avoid incarceration. Mr. Whittles has divested himself of his New York businesses and moved to sunny Arizona. At least for now. With sentencing scheduled for later in 2022, Mr. Whittles faces a potential five years in prison and another $250,000 in fines.

Employee Embezzlement

Criminal tax investigations are often aimed at business owners or C-suite executives. Just as often, it is the rank-and-file who perpetrate tax fraud.

In March 2019, Alabama resident Alita Edeker was sentenced to almost four years in prison for stealing from her employer and filing false income tax returns. According to the Department of Justice, Ms. Edeker was an accounts manager at a science technologies company based in Auburn, Alabama, between 2005 and 2014.

Like many individuals who embezzle from their employer, Ms. Edeker was in a position that enabled her to route and reroute monies coming into the company for the payment of goods and services. Ms. Edeker processed credit and debit card product purchases for the company. Between 2007 and 2014, Ms. Edeker transferred more than $700,000 into accounts that she controlled.

Monies gained from tax crime often go to pay debt or pay for personal comforts. Ms. Edeker used the illicit funds to pay for her car, home utilities, and mortgage. As with many types of criminal endeavors, Ms. Edeker was pursued for filing fraudulent tax returns. In addition to the embezzlement and making false statements about the money she diverted, the IRS found she filed inaccurate income tax returns between 2011 and 2013.

Ultimately, Ms. Edeker will serve her prison time, plus three years of probation. She is required to repay her employer $819,497.29 and owes the IRS another $101,604. As an accounts manager and felon, Ms. Edeker will be hard-pressed to repay her debts in her lifetime.

Payroll Tax Fraud

A Paradise Valley, Arizona man took a familiar tax scam and made it his. His story is a cautionary tale on a couple of levels. John Propstra is going to prison for almost two years. After that, the 47-year old man will be on probation for another three years and he will be paying restitution to the tune of $700,000 to the IRS for a lot longer than that.

How did a man who owned several small businesses and provided outsourced payroll services get in this position? There is a clue in the previous sentence, and it is "payroll services." Mr. Propstra was in the business of collecting federal employment taxes for other companies and paid them to the IRS—until he didn't. In the process of his business dealings, Mr. Propstra slid down the slippery slope of withholding taxes he was being paid to withhold for the IRS.

Failing to pay over employment taxes is not uncommon. Business owners facing red ink may claw back employment taxes collected from their employees. Other owners may collect and spend employment tax money on personal expenses.

While it seems a straightforward scam, this tax crime usually involves multiple charges. As the subject of an IRS criminal tax investigation, Mr. Propstra faced numerous allegations. In addition to failing to pay over the monies he collected from his client companies, Mr. Propstra filed false income tax returns stating he paid more taxes than he had. Then he quit filing employment tax returns altogether and disposed of filing accurate wage reports to the Social Security Administration (SSA). For his own group of small businesses, Mr. Propstra failed to pay over $710,819.05.

Business owners who make a habit of dipping into withholding taxes are taking a risk. Owners who are in the business of collecting employment taxes and fail to pay over the money to the IRS are making a blatant misjudgment.

Despite the similarity of charges faced by defendants, no two tax crimes are ever truly the same. Had Mr. Propstra consulted with a tax attorney with experience in defense of criminal tax matters prior to his arrest, some of the consequences of this crime might have been mitigated. We'll never know.

Willful Evasion or Simple Mistake?

Can claiming you made an innocent mistake on your tax return get you out of hot water with the Internal Revenue Service (IRS)? Maybe so, maybe not.

Simple errors on tax returns are common. Individual taxpayers and business owners may forget a schedule, file a return with miscalculations, or misinterpret what is being asked. It happens. The IRS may catch it or may not. If you receive a letter from the IRS or become the focus of an IRS civil audit, it behooves you to speak with a tax attorney to review your tax profile and reporting. In some cases, there may be an opportunity to prove the miscalculation, while in other situations, it may be tough to prove it is not tax evasion.

Let's look at the case of Mr. Jonathon Michael, a mechanic in Springfield, who worked with port operations in New Jersey. Like the rest of the working world, Mr. Michael was asked to designate his withholding allowance on an IRS W-4 form. The form allows an employer to calculate the amount of wages to withhold and pay the IRS on behalf of the employee. In 2014, Mr. Michael completed and submitted the W-4 form verifying he was exempt from federal income tax withholding.

Mr. Michael earned more than $260,000 per year and had no recognized exemption from paying employment taxes. At this point in the story, Mr. Michael appears to have made a serious mistake with regard to designating his withholding allowance. Signing on the bottom line of the form acknowledges that information is accurate and subject to charges of perjury if it is not. As a result of the W-4, his employer withheld no taxes for Mr. Michael.

Employers annually provide the IRS with a W-2 form for each employee. The W-2 alerts the IRS to the actual wages, compensation, and withheld taxes paid by each employee. It is pretty easy math for an algorithm to compare incoming W-2s and W-4's. The difference can mean an IRS tax investigation. In this case, that is just what happened.

In 2016, the IRS stepped in and advised the employer of Mr. Michael to disregard the W-4 he provided and to begin withholding appropriate wages on his behalf. At this point, Mr. Michael was alerted to the intervention of the IRS and their focus on his tax situation. The story might have ended here had Mr. Michael acknowledged the "mistake," and paid and filed his taxes accordingly along with arrears and penalties for the years 2014, 2015, and 2016. To this point, Mr. Michael could have argued, if pressed, he made an unintentional mistake and intended to make good on it.

But—that is not what happened. Instead, Mr. Michael wrote a letter to his employer attesting to the correctness of the prior W-4 he had provided. As a result, his employer withheld no payroll taxes on his behalf for the year 2014 through 2018. Given fair warning that the IRS could consider his choices as a tax crime, he chose to stick to his story, pretty much foreclosing the opportunity to claim he made an unintentional error.

In April 2021, Mr. Michael was indicted by a federal grand jury for tax evasion and willful failure to file individual income tax returns. Overall, he failed to pay withholding and federal income taxes on $1.6 million in income earned over the five-year period in question.

The devil is in the details between an unintended error and willful tax evasion. Mr. Michael faces approximately ten years in prison for not responding to the IRS when he had a chance. While his sentence will likely fall well short of ten years, he owes significant money to the IRS.

Employment Tax Fraud

Tax crime pays—for a while. A North Carolina couple recently learned how expensive tax fraud can really be.

In the past, we discussed the interesting matter of Dr. James Rice and his wife. An orthopedic surgeon, Dr. Rice and his wife ran a private practice in Pinehurst. The pair decided to stop paying over their employment tax obligations to the IRS in 2007. The taxes, collected from the wages of their employees, eventually totaled $580,000 by 2016 when agents conducting an IRS criminal investigation came knocking. As well, the couple dispensed with income taxes altogether between 2014 and 2016—failing to declare and pay their own tax liabilities.

The ill-gotten gains were used for country-club dues, expenses related to their home and their dog, as well as the truffle business of Mrs. Rice. After an almost week-long trial in September 2021, the jury took 41 minutes to convict the couple. They were convicted of one count of conspiracy to defraud, one count of tax evasion, two counts of

failure to pay over employment taxes and three counts of failure to file tax returns. Dr. Rice was also convicted on three counts of failure to file corporate tax returns.

In late January 2022, Dr. and Mrs. Rice were sentenced to five years in prison. They must also pay $2.4 million in restitution.

Special Agent Donald Eakins with the Charlotte Field Office said, *"Failure to pay over withheld taxes is a serious offense. Employment tax evasion results in the loss of tax revenue to the U.S. government and the loss of future Social Security and Medicare benefits for those employees. The investigation of employment tax fraud is a priority for IRS Criminal Investigation, and our special agents will vigorously pursue anyone who collects these taxes and then uses the funds for their own personal gain."*

It is the job of the IRS to pursue those seeking illegal profit by bending and breaking laws around employment tax, offshore taxes, money laundering, or foreign bank accounts. For those who would never dream of being involved in a criminal tax matter, a prison sentence sounds fitting. For individuals who are currently involved in a criminal tax enterprise, a prison sentence of five years is chilling.

Dr. and Mrs. Rice took their best shot and lost big time. We do not know what measures were taken to try and avoid a jury trial involving overwhelming evidence against the defendants. If you find yourself the target of a criminal tax investigation, the advice is unequivocal—speak with an experienced criminal tax defense attorney as quickly as possible.

15 Years of Criminal Tax Fraud

Taking advantage of company perks and fringe benefits is no new thing. For a New York CFO, the practice has plunged him and the company he works for into a media circus that could send him to prison.

Allen Weisselberg is the former Chief Financial Officer of the Trump Organization. Mr. Weisselberg, 73 years old, was charged with an array of tax crimes including tax fraud, falsifying records, and scheming to defraud tax agencies. Overall, the government accuses Mr. Weisselberg of attempting to evade more than $900,000 in taxes, while at the same time collecting $133,000 in tax refunds based on fraudulent tax returns.

At the top of the Trump Organization for decades, Mr. Weisselberg is being systematically removed as a named officer in Trump subsidiaries. Although the Trump Organization has stopped short of terminating his employment, Mr. Weisselberg is no longer a prominent name in the organization.

Although investigation into the tax profile of the Trump Organization has moved slowly forward over the years, the turning point in the arrest of Mr. Weisselberg appears to have been the divorce of his son Barry Weisselberg.

When Jennifer Weisselberg, now divorced from Mr. Weisselberg, began digging through documents for her impending divorce, she could not reconcile the lifestyle she enjoyed with her two children with the actual reported income of her husband. Mr. Weisselberg is employed by the Trump Organization to run the Wollman Rink in Central Park for which he reported income of $211,000 in 2016. Both Mr. and Mrs. Weisselberg confirmed Barry has not received a raise in years.

A respectable sum, for sure, however, both children of the couple attend the Columbia Grammar and Preparatory School in Manhattan at a cost of approximately $100,000 per year for both students. The Weisselbergs enjoyed a high-end lifestyle, and also lived in an apartment overlooking Central Park.

While trying to reconcile the perks with the hard income, Ms. Weisselberg shared documents with Bloomberg News, and later the New York Attorney General and the Manhattan District Attorney. Although the couple is not facing charges, the ensuing deep-dive into the documents revealed the breadth of money and perks accruing from the potentially illegal practices of the Trump Organization in chronically underreporting income and taking high return deductions.

For many, the prosecution of Mr. Weisselberg on criminal tax charges is seen as a gambit to pressure the executive to provide evidence in the long-running investigation of the Trump Organization and its namesake, Donald Trump.

Like Michael Cohen, the disgraced former foot soldier of Mr. Trump, Mr. Weisselberg may eventually find turning informant may save him from spending his twilight years in a prison cell. Unlike another Trump ally, Paul Manafort, Mr. Weisselberg will not be able to count on a pardon from the President of the United States at the end of the day.

A Nationwide Tax Fraud Seminar Scheme

Though most of them today have gone virtual for the time being, seminars are a great way to experience interactive learning on a topic, hosted by a dynamic speaker. Unfortunately, there's always that little nugget of uncertainty going into one—you never know if it's being run by scammers just look getting to rich while committing fraud at the expense of trusting people.

Recently, one such seminar came to an end. Several individuals plead guilty to conspiring to defraud the U.S. by promoting a nationwide tax fraud scheme through seminars they hosted across the country. They also

plead guilty to preparing and filing false tax returns for the individuals they recruited into the scheme. The most recent to plead guilty in this case is Mehef Bey.

From the Department of Justice Release:

> According to court documents, Mehef Bey, also known as Arthur Daniels, of Charlotte, promoted a scheme that involved recruiting clients and preparing false tax returns on their behalf by convincing them that their mortgages and other debts entitled them to tax refunds. Between 2014 and 2016, Bey and his co-conspirators held seminars across the country to publicize the scheme. As part of the scheme, Bey and his co-conspirators helped prepare and file tax returns for the participants, which collectively sought more than $64 million in refunds from the IRS. These tax returns falsely claimed that banks and other financial institutions had withheld large amounts of income tax from the participants, thereby entitling the clients to a refund. In reality, the financial institutions had not paid any income to or withheld any taxes from these individuals. To make the refund claims appear legitimate, however, Bey and his co-conspirators filed tax documents with the IRS that matched the withholding information listed on the tax returns, making it seem as if they had been issued by the banks.
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> As part of his plea, Bey admitted he and his co-conspirators charged their clients approximately $10,000 to $15,000 in preparation fees for each tax return. Although Bey personally received more than $1 million for his role in the scheme, he did not file tax returns for the years 2015 and 2016 to report this income. For 2014, Bey filed a false income tax return on which he claimed a tax refund that he was not entitled to receive. On this return, he also did not report his income from promoting the scheme.
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> Bey also admitted he and his co-conspirators concealed their roles in the scheme by, among other things, indicating the false tax returns had been "self-prepared" and coaching the participants how to conceal the scheme from the IRS.
>
> Bey's sentencing will be scheduled for a later date. He faces a maximum penalty of five years in prison for conspiring to defraud the United States and three years in prison for each of the two counts of aiding and assisting in the preparation and filing of a false tax return. He also faces a period of supervised release, restitution, and monetary penalties. A federal district court judge will determine any sentence after considering the U.S. Sentencing Guidelines and other statutory factors.

Tax fraud is more than just a mistake; it is a willful attempt to get out of tax obligations. There are many kinds, all with penalties, and without proper advice and guidance, it's easy for a small matter to spiral out of control. So it's important to not take a tax fraud charge lightly and get professional help quickly.