

## [Headlines - IRS, DOJ must rethink strategy on felony tax obstruction charges post-Marinello](#)

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### **Body**

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The Supreme Court's March 21 decision in *Marinello v. United States* put substantial limits on the government's ability to pursue felony tax obstruction charges, but it left an opening for the Internal Revenue Service and the Justice Department's Tax Division to potentially bring such charges. The agencies must show they gave a taxpayer fair warning that engaging in certain behavior is unlawful and could result in a tax proceeding.

The high court's decision to adopt a narrow interpretation of the so-called omnibus clause in [Internal Revenue Code Section 7212\(a\)](#), the criminal tax obstruction statute, was roundly praised by the defense bar, which had argued that a broad interpretation could lead to prosecutors adding a tax obstruction charge to any tax misdemeanor charges and could even criminalize otherwise legal tax planning.

The omnibus clause in [IRC Section 7212\(a\)](#) imposes criminal liability on anyone who "in any ... way corruptly ... obstructs or impedes, or endeavors to obstruct or impede, the due administration of [the Internal Revenue Code]." The government used the provision sparingly in the first few decades following its enactment in 1954, but began using it more often starting in the 1990s.

As tax obstruction indictments grew, defense attorneys expressed concerns that the government was, in some cases, using the omnibus clause as a catch-all charge when it didn't have sufficient proof to support more traditional felony charges, such as tax evasion or aiding or assisting a false return, or was overcharging misdemeanor conduct as felonies. Practitioners also argued that the omnibus clause gave the IRS too much power in negotiating with taxpayers who wouldn't acquiesce to the IRS's interpretation of the IRC.

The question the Supreme Court had to decide was whether the scope of the omnibus clause should be limited to cases in which the defendant deliberately acted to obstruct or impede some pending proceeding before the IRS. Carlo Marinello, the New York business owner at the center of the case, had not filed a personal or corporate income tax return since at least 1992 and didn't maintain business records. Unbeknownst to Marinello, the IRS Criminal Investigation unit intermittently probed his tax activities between 2004 and 2009.

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In 2012, Marinello was charged with one felony count of violating the omnibus clause and eight misdemeanor counts of willful failure to file individual and corporate returns. The omnibus clause count alleged that Marinello had violated the statute by failing to maintain corporate books and records, failing to provide his accountant with all of his and his company's income information, destroying company records, cashing business checks, hiding company income in personal accounts, transferring assets to a nominee, paying employees with cash and using company money to pay personal expenses.

A jury convicted Marinello on all nine counts. The judge had instructed the jury that, to convict him of an omnibus clause violation, it must find that he "corruptly" engaged in at least one of the eight specified activities, but the jury was not told that it needed to find that Marinello knew he was under investigation and intended corruptly to interfere with that investigation.

Marinello appealed to the US Court of Appeals for the Second Circuit, arguing that an omnibus clause violation requires that the defendant be aware of a pending IRS action, and that the government provided no evidence that he knew of a pending IRS investigation against him. The Second Circuit rejected his argument, holding that [IRC Section 7212\(a\)](#) does not require the government to prove the defendant acted with knowledge of a pending IRS action.

In a 7-2 decision, the Supreme Court reversed the Second Circuit's ruling, holding that to convict a defendant under the omnibus clause, the government must prove the defendant was aware of a pending "particular administrative proceeding" or could reasonably foresee that such a proceeding would commence.

The court did not, however, provide an exhaustive list of what constitutes a particular administrative proceeding. Other than citing three examples (an investigation, an audit, or other targeted administrative action), the court defined it in the negative, explaining that it "does not include routine, day-to-day work carried out in the ordinary course by the IRS, such as the review of tax returns."

Likewise, the court did not define the term "reasonably foresee," saying only that "it is not enough for the Government to claim that the defendant knew the IRS may catch on to his unlawful scheme eventually. To use a maritime analogy, the proceeding must at least be in the offing."

- How can tax obstruction charges be used post-*Marinello*? -

The decision was undoubtedly a big loss for the IRS and DOJ, but the fuzziness around what constitutes a pending, particular administrative proceeding gives the government some room to continue using the omnibus clause as a tool in its enforcement arsenal.

When evaluating the decision's impact on charging decisions, the IRS and DOJ will need to decide where they want to draw the line on which activities within the universe of the IRS's tax administration responsibilities fall under the scope of the "particular administrative proceeding" language used by the court.

"People looking at this decision need to understand how the IRS works to appreciate how vague this line is that the court tried to draw," said Jenny Johnson Ware, a tax litigator with Johnson Moore in Chicago. "There are so many things the IRS does in terms of processing and reviewing tax returns, assessing tax liabilities and collecting taxes that trying to figure out which of these activities fall on which side of the line here is going to be very challenging."

Johnson Ware, who authored an *amicus curiae* brief in the *Marinello* case on behalf of the American College of Tax Counsel, said it will be interesting to see how the IRS and DOJ approach this question.

"Are they going to restrict tax obstruction charges to things that are obvious - like audits - or will they try to stretch the boundaries to include things like correspondence audits or collection activities?"

Caroline Rule, a partner with Kostelanetz & Fink in New York, said the court's repeated use of the words "particular" and "targeted" seem to mean that an IRS proceeding must be directed or aimed at a specific taxpayer or small group of taxpayers, such as partners in an organization, to fall within the scope of the omnibus clause.

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"It's not clear whether publicized IRS investigations into a broad category of taxpayers, such as the IRS's Return Review Program, would count as sufficiently 'targeted' administrative action under Section 7212(a)," said Rule. "Along the same lines, would an IRS John Doe summons proceeding be sufficiently targeted for a Section 7212(a) prosecution? I would think not, as the very idea of a John Doe proceeding is that the IRS is targeting a broad group of unknown taxpayers, not targeting a particular taxpayer."

- Putting taxpayers on notice -

To satisfy the requirement that a defendant be aware of a pending tax-related proceeding, the IRS and DOJ might look at how they can build their case files in a way that addresses the court's "fair warning" concerns.

"I wonder whether IRS-CI and DOJ will modify or expand their areas of interest during the investigative stage in order to prove knowledge of a pending tax-related proceeding, or gather facts to prove the taxpayer could reasonably foresee that such a proceeding would commence," said Michael A. Villa, Jr., a partner with Meadows Collier in Dallas. "The 'reasonably foresee' language appears to provide an opportunity for the IRS and DOJ to put a taxpayer on notice somehow and then gather the facts to demonstrate obstruction."

Villa noted that most criminal tax investigations can take months or even years to complete. "It's possible the IRS could try to institute some type of notice or fair warning opportunity as a matter of course during an investigation," he said. "Especially if they have a Marinello situation, where there are several issues creeping up, it's snowballing and the taxpayer is not cooperating. Is there a way to give that taxpayer notice that a proceeding will commence and he better stop failing to maintain records, or paying in cash, etc.?"

Villa said the IRS sometimes uses a warning process in the context of the Bank Secrecy Act, which requires trades and businesses to report cash payments of more than \$10,000 to the federal government by filing IRS/FinCen Form 8300. A person required to file Form 8300 who willfully fails to file, fails to file timely or fails to include complete and correct information is subject to criminal sanctions as a felony under [IRC Section 7203](#). To establish a willful failure to file, the government must prove the defendant knew of the reporting requirement.

"Sometimes an IRS agent will appear on the scene to do an educational-type meet and greet or a civil examination of the BSA requirements," said Villa, adding that these types of exams or educational visits can result in a warning letter or a list of corrective actions that must be taken.

"The agent might go to a car dealer, for example, to explain the requirements for Form 8300 and document the visit," Villa said. "Then the agent will come back in 18 months and check to see if the dealer is doing it correctly. Now the IRS has evidence in the file that the dealer has knowledge of the reporting requirement because the IRS informed the dealer, in writing, of the requirements during the original visit."

Rule wondered whether the IRS and DOJ might try to insert a "willful blindness" standard into an omnibus clause argument. However, she noted that in the Supreme Court's 2005 decision in *Arthur Andersen LLP v. United States* - which was cited by the majority in the *Marinello* decision for its "reasonably foreseeable" language - the court held that jury instructions concerning criminal liability under [18 USC Section 1512](#) (a witness tampering statute that applies to the obstruction of federal proceedings) were improper because they failed to convey that conviction requires proof of nexus between the document destruction and a particular official proceeding.

"It seems that the court in *Marinello* meant that the government must at least prove that a defendant charged under Section 7212(a) must be contemplating a particular IRS proceeding when he or she engages in obstructive conduct," said Rule.

She added that there was no mention of "willful blindness" in either the *Arthur Andersen* decision or in *United States v. Aguilar*, a 1995 Supreme Court decision on which the *Marinello* court strongly relied.

"Is it possible to be willfully blind to the contemplation of a particular proceeding?" Rule said. "Maybe 'reasonably foreseeable' is a kind of equivalent of willful blindness? We will have to wait and see if the government tries to rely

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on the concept of willful blindness, which it does more and more often, and how courts will rule on that issue in connection with Section 7212(a) as articulated in *Marinello*."

- A bargaining chip?-

The IRS and DOJ will also need to reevaluate how they can still use the omnibus clause as a leveraging tool during the investigative process and in plea negotiations. Prior to the *Marinello* decision, the statute's broad language and vagueness gave the government substantial leverage to force settlements or admissions from recalcitrant taxpayers.

The *Marinello* decision will change that dynamic and give taxpayers some power to push back during behind-the-scenes negotiations. However, if the IRS takes the time to educate field agents on how they can build their case files to later support an argument that a taxpayer was put on notice about the consequences of inappropriate or unlawful activity, the government could potentially use the omnibus clause as a leveraging tool.

"If a taxpayer points out why an obstruction charge would be difficult because of the *Marinello* decision, the IRS could turn its back on them and say, 'Well, that decision also said we have to show that you could reasonably foresee that such a proceeding would commence. Here's what we have in our file to show that you should've reasonably foreseen this,'" said Villa.

"There's still an opportunity for the government to use the omnibus clause," Villa continued. "But they're going to have to do a good job, especially the first few times they try to continue using it in court or as a leveraging tool, of making sure their strategy aligns with what the court has outlined in *Marinello*."

REFERENCE:

[https://www.supremecourt.gov/opinions/17pdf/16-1144\\_p8k0.pdf](https://www.supremecourt.gov/opinions/17pdf/16-1144_p8k0.pdf)

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