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PAY DAY: TAX CASH HOARD DEFENSE HIDDEN INSIDE THE COUCH

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Abstract: A defendant's claim of cash on hand is commonly referred to as a cash hoard defense[1]. A typical cash hoard defense asserts that the defendant in earlier years received money from such sources as gifts from family members or friends, or an inheritance, which he or she then spent during the prosecution period[2]. George Kleinman's trial hinged on a cash hoard. In *U.S. v. Kleinman*, the trial proceeded as to Count Two which charges that in 1950 Kleinman filed a false and fraudulent joint income tax return on behalf of himself and his wife for the calendar year 1949, wherein it was stated that their net income for that calendar year was $6,141.69, and that the amount of tax due thereon was $621.12, whereas the defendant knew that their net income for that calendar year was $20,225.46, upon which there was owing to the United States an income tax of $3,955.78[3].

Keywords: cash, money, taxes, case law

I. PIGGY BANK: NEVER SPENT A NICKEL COINING THE CASH HOARD DEFENSE

The United States District Court noted:

The defendant's father, Bernard Kleinman, died in 1954. Beginning in 1944, and throughout the years from 1944 through 1949, savings bank accounts were opened in the father's name. Approximately $55,000 was deposited in these accounts during these years, and from these accounts approximately $50,000 was subsequently,

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[1] The United States Department of Justice, Criminal Tax Manual 12.

[2] *Id*.

[3] 167 F.Supp. 870, 871 (E.D.N.Y. 1958).

and within the years mentioned, transferred to the defendant or to members of his family. This was accomplished in part by the transfer of cash by check from Bernard Kleinman to the defendant and members of his family, and in part by the transfer of assets from Bernard Kleinman to the defendant, which assets had been purchased with funds deposited in these savings bank accounts[1].

The court indicated:

The Special agent who investigated this case testified that he examined taxpayer's returns which had been audited by the defendant; that he spoke to some three hundred of such taxpayers, and investigated taxpayers who prepared returns audited by the defendant. No one was brought forward to testify that the defendant had taken a bribe or had offered to take a bribe. The Government in the late hours of the case candidly advised that it does not ask the Court to assume that the unreported income of the defendant was received through bribes. The net result is that there is a void as to a showing of a possible source of unreported income, and the persuasive value which such as showing might have is replaced only by speculation of no probative value whatever[2].

The court suggested:

From the middle of 1946 until the latter part of 1947 the defendant was assigned in connection with the performance of his duties to posts in Phoenix, Arizona and Los Angeles, California. During this period approximately forty-eight deposits totalling some $13,700 were made in the Bernard Kleinman accounts in Brooklyn and in New York City. Assuming, arguendo, that these were deposits of the defendant's funds in the continued pursuit of a conspiracy in his behalf, in the absence of evidence indicating the actual state of facts, it is as reasonable to conclude that this was the systematic disposition by the father of a hoard accrued by the defendant in some prior period, as it is to conclude that the funds were the current unreported earnings of the defendant transmitted to his father in some unknown manner. If such were the case, it may have been the case in the year 1949, with which we are primarily concerned, and in such event it would be clearly erroneous to assimilate deposits in the Bernard Kleinman accounts with current unreported income of the defendant[3].

Kleinman should not be read for the proposition that the cash hoard defense can replace federal tax accounting. The entire structure of the income tax depends on an annual accounting system that assigns income, deductions and other tax incidents to specific accounting periods[4]. It is not enough for a taxpayer to know that she has

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[1] *Id.* at 873.

[2] *Id.* at 874.

[3] *Id.*

[4] *Michael B. Lang, Elliot Manning & Mona L. Hymel*. Federal Tax Accountnig iv (2nd ed. 2011).

an item of income, loss, deduction, or credit to report on her federal income tax return[1]. The taxpayer must also know when the item should be reported on a return[2]. Tax accounting rules determine when the tax incidents of tax-recognized events must be taken into account for federal income tax purposes[3]. Tax accounting issues permeate all areas of the federal income tax[4]. One of the most important facets of the annual accounting system is that it requires a method for deciding which tax-recognized events are reported in which year[5]. By a method, we mean a series of rules for determining when to recognize items of income, expense, credit and other tax incidents[6]. The cash method basically focuses on when the taxpayer receives income items or pays expenses, while any accrual method generally focuses instead on when the taxpayer has earned the income items and when all events have occurred fixing the taxpayer's liability to pay for expenses[7]. However, *Kleinman* reinforces the reality that it is as reasonable to conclude funds were a relative's cash hoard as current unreported income.

Put Me On Your Calendar: Shuffling Money Through Taxable Years With The Cash Hoard Defense

Under the federal income tax, tax returns are prepared on an annual basis, each return covering a period of one year or occasionally a fraction of a year (a "short year")[8]. At this point, the important point is that the when question is really: for which year[9]? Use of an annual accounting system for the income tax has a number of consequences and offers planning opportunities that go far beyond merely shifting income from December of one year until January of the following year, or shifting a deduction from one year to another[10].

An annual accounting system requires that taxpayers file returns on an annual basis[11]. For individuals, generally, annual filing would ordinarily refer to a calendar year basis, but many businesses use some other fiscal year for financial accoun-

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1 *Id.* at 1.

2 *Id.*

3 *Id.*

4 *Id.*

5 *Id.* at 14.

6 *Id.*

7 *Id.* at 15.

8 Lang, Manning, & Hymel, supra note 7, at p. 3.

9 *Id.*

10 *Id.* at 7.

11 *Id.* at 10.

ting purposes, often for business reasons[1]. Thus, a business which must keep track of physical inventory will often end its fiscal year at a time of year when its actual inventory is low, thus reducing the burden of doing the annual inventory[2]. 20 For example, many retail stores use a January fiscal year, before which they reduce their physical inventory through post-Christmas sales[3].

Section 7701(a)(23) defines a "taxable year" as the calendar year or the fiscal year upon the basis of which taxable income is computed for the income tax[4]. The term "fiscal year" is defined as "an accounting period of 12 months ending on the last day of any month other than December"[5]. So there are basically 12 different possible taxable years[6]. In addition, the Code permits use of a 52–53 week year, a type of fiscal year which always ends on the same day of the week and is favored by some cyclical businesses, but the 52–53 week year is essentially a variation on the fiscal year[7]. Section 441(b) generally defines which of these possible years is the taxpayer's possible year, unless another provision of the Code provides otherwise[8]. If the taxpayer regularly keeps her books on the basis of an annual accounting period that is either a calendar year or a fiscal year, that year is the taxpayer's taxable year[9]. Otherwise, the taxpayer must use the calendar year as her taxable under section 441(b)(2) and(g), unless the return is made for a period of less than 12 months, in which case that period — referred to as a "short period" — is the taxable year[10].

Most individuals really have no choice about what taxable year they use since section 441(g) requires the calendar year for taxpayers who either keep no books or who otherwise lack an annual accounting period[11]. Treas. Reg. § 1.441-1(b)(7) explains that "books" must be sufficient to reflect income adequately and clearly", but merely having a checkbook — the extent of most individuals' books — is probably not adequate[12]. While there are often advantages to an individual using a fiscal

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1 *Id.*

2 *Id.*

3 *Id.*

4 *Id.*

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.*

9 *Id.*

10 *Id.*

11 *Id.*

12 *Id.*

year, to do so an individual would have to keep books with respect to her income on a fiscal year basis for the first year in which she had income, a most unlikely occurrence[1].

In *U.S. v. Uccellini*, Emil Uccellini was convicted of income tax evasion for the years 1950 and 1951[2]. Other than a check book, Uccellini kept no personal books or records of his income[3]. The United States District Court observed:

Mindful that expenditures in excess of reported income, standing alone, might not of themselves support a conviction of tax evasion without evidence indicating a lack of available funds from which these expenditures might have come, the revenue agents, prior tot [sic] trial, undertook an elaborate investigation in order that the government might prove, insofar as it was possible, that defendant did not have any substantial available cash, and that his 1951 expenditures, after deductions, were paid out of taxable income earned in 1951[4].

The court found:

The agents interviewed the defendant concerning inheritances, gifts and loans. Court records were searched for inheritances and none were found.

They attempted to negative a claimed cash hoard of $15,000, allegedly saved by defendant from earnings up to 1944, by investigating his financial history back to 1926.

At the trial, December 31, 1941 was selected as a starting point. At that date defendant was credited with the alleged hoard of $15,000. During the succeeding years he was credited with depreciation and loans from his partner and certain financial institutions which were revealed by the investigation[5].

The court determined:

Consequently, it is argued that the jury could conclude that defendant had not only exhausted the alleged hoard, but in addition had expended approximately $24,000 in excess of the income reported in his tax returns filed for the preindictment years, and thus there was no available cash at the beginning of the indictment years. But the government's evidence tends to prove just the contrary, i.e., that defendant either had considerable cash available at the beginning of 1951, or he acquired it during the first four months of 1951 from an undisclosed source other than his partnership business and real estate rents[6].

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1 *Id.*

2 159 F. Supp. 491 (W.D. Pa. 1957).

3 *Id.* at 492.

4 *Id.* at 493.

5 *Id.*

6 *Id.*

The court reversed, concluding:

Even if we assume defendant's available cash was taxable income, it cannot be allocated reasonably to taxable income received from defendant's business and rents from January to May 3, 1951. The government's evidence conclusively proved that the partnership was not capable of producing income remotely approaching $24,000 for defendant's share even annually. Thus the fund was either accumulated from receipts in prior years, or it was acquired in 1951 up to May 3 from an undisclosed source, and was not shown to have been taxable income. In either event, as shown, the conviction on the second count cannot be sustained[1].

Cash Is King: Problem Of Not Calculating Starting Cash On Hand

Since the subject may contend that the unexplained deposits into the bank accounts came from a cash hoard, it crucial to thoroughly establish and document any increase in the subject's cash on hand[2]. The special agent must begin by documenting the cash on hand at the starting point and then document cash on hand at the end of each year under investigation[3]. The cash on hand increase (or decrease) is then determined for the first year of the investigation by subtracting the cash on hand at the starting point from the cash on hand at the end of the first investigation year[4].

In *U.S. v. Birozy*, The Honorable Mark Costantino presided over Hyman Birozy's trial[5]. The only problem with the government's offer of proof was its failure to establish a cash on hand figure to start the analysis, as stated in *U.S. v. Slutsky*"[6]. An exchange addressed cash hoards:

MS. O'BRIEN: Your Honor, if I may make a brief response to that? THE COURT: Surely.

MS. O'BRIEN: The government has no proof at the present time as to the defendant's available cash on hand; however, in the *Slutsky* case, that is far different from this particular case, because there is only two relatively small cash deposits in the business checking account; an amount of $2300 from which the defendant has not been given credit.

There was another deposit of $5,000. We consider that to be the proceeds of the loans and we have already given him credit for that $5,000 in that 1967 figure. Ac-

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[1] *Id.* at 495.

[2] Internal Revenue Manual 9.5.9.7.4.3.

[3] *Id.*

[4] *Id.*

[5] 1974 WL 605, 1 (E.D.N.Y. 1974).

[6] *Id.*

tually, all we're talking about as the possible cash re-deposits in that $2300 figure in May, '65.

THE COURT: It does stand for the fact you must start with some monies at the beginning of the year. What was the cash on hand when they started for that period?

If he started with zero, then you can assume all the money placed in there was income, but if he started with, let's say $100,000 left over from the year before, and that's been reported at prior income tax period, then you must deduct that from the following year. That hasn't been done here.

MS. O'BRIEN: What your Honor says is absolutely true, if the deposits were cash re-deposits.

If that were a fact, then the cash deposits could be attributable to prior cash on hand. In this case, your Honor, there's only one small $2300 cash deposit. Every other deposit in that account, your Honor, is a check.

THE COURT: That doesn't mean — you see, it doesn't only mean the cash itself. It means any other resources that may be available at the beginning of the year. It could be merchandise or anything else. That would all be inclusive as to whether or not that was part of the incomeproducing monies that were deposited in the bank.

MS. O'BRIEN: Your Honor, it's not reasonable to suppose that if a man has a cash hoard, he would transfer this into some sort of a money order or some sort of other check, and thereafter re-deposit it by check. If a man has a prior cash hoard, he would indeed deposit as cash to the business banking account.

The *Slutsky* case is different because there was substantial question there of having an accumulation of cash, which he defendant claim were to be cash for advanced reservations and, therefore, should not figure into the present income figure[1].

An exchange addressed cash on hand:

THE COURT: You're not answering the question. What did he start off the taxable year?

MS. O'BRIEN: We do not know.

THE COURT: You have to find this out. That's what this paragraph says. This paragraph says, you must start with a figure, that you say is income. You can't say if a man has a going business, you can't say that's income, any more than if I just started my business yesterday. You couldn't say it's income because I put $200,000 in the bank. I may have paid taxes on that for years. The question is, where did all that money come from, and must be deducted from the taxable income. If it is, then you don't have $200,000. Then you may have $20,000. You can see that.

MS. O'BRIEN: Then there is, in effect, what your Honor is saying, not what your Honor is saying, no real distinction a net worth case and bank deposit.

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[1] *Id.* at 2.

THE COURT: Just because I make a salary every year, you can't add on the salary for the past 19 years. Assume I never spent a nickel. You can't tax that money[1].

Birozy suggests it was a problem for the government to have no proof as to the defendant's available cash on hand. Cash was king, because it was a problem to not calculate the starting cash on hand amount:

Verdict

The indictment herein having regularly come on trial before the Honorable MARK

A. COSTANTINO, United States District Judge, and a Jury, and the defendant having moved for a Judgment of Acquittal, and the said motion having been granted, and the Jury having been discharged

IT IS ADJUDGED that the defendant HYMAN BIROZY is NOT GUILTY of the charge in said indictment.

Dated: Brooklyn, New York[2].

II. QUIET ON THE SET: LEARNING THE VALUE OF A DOLLAR THRU THE FIFTH AMENDMENT PRIVILEGE AGAINST SELF-INCRIMINATION

Open The Safe: Spilling Cash Hoard Beans To IRS

The Internal Revenue Service has a publication addressing minimum income probes and cash hoards. It provides:

Always ask about a cash hoard. In a cash business this is critical. Find out if one existed and where the money came from. In a cash business this is critical. Find out if one existed and where the money came from. If it was skimmed from the business in prior years, it is taxable. If it came from other sources it can be traced and the examiner must follow up[3].

A publication provides:

With a cash intensive business, it is important to get complete information about nontaxable income as soon as possible in the examination. Question the taxpayer about any Cash T imbalances during the initial interview. If there is a cash hoard, or other nontaxable income, the examiner will want to consider this information early in the examination. It will be necessary in every indirect method case.

Cash-on-hand should be established for the beginning of each year under audit. Also, the taxpayer's practice of keeping cash on hand should be determined for present and prior periods to establish any accumulation of cash over the years.

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[1] *Id.* at 5.

[2] *Id.* at 8.

[3] Cash Intensive Businesses Audit Techniques Guide — Chapter 4, Internal Revenue Service.

Cash-on-hand is defined as including all cash not in a financial institution, such as: at home, in pocket, in a safe deposit box or a safe.

A taxpayer's explanation about a cash hoard may change during an examination. The examiner should document the information as it is received. The documentation should include when and where the information was received, who was present, what was said, and when the documentation was prepared.

The credibility of a cash hoard explanation should be examined. The examiner should ask to see the cash hoard and where it is kept to determine if the space is adequate. The examiner should examine the taxpayer's bill paying and borrowing habits; an individual which a cash hoard will not incur insufficient fund charges for checks written or require loans[1].

A Criminal Tax Manual provides:

If the defendant claims during the investigation to have had a cash hoard, the IRS agent will ask very detailed questions to attempt to learn the amount of this cash hoard, its source, when it was received, and where it was kept, who else was aware of its existence, the denomination of the bills, and whether it was always kept in the same place. The defendant should be asked to identify which particular assets were purchased with the funds from this cash hoard so the government can contact the seller-witness to verify that currency was in fact exchanged during the sale[2].

Can't Tell You That: Disclosing Cash Hoard Danger

The Fifth Amendment privilege against self-incrimination states that "[n]o person…shall be compelled in any criminal case to be a witness against himself…."[3] An individual might seek to raise this privilege in response to interrogation by a police officer or in response to a request for evidence[4]. In what circumstances can an individual validly invoke the privilege[5]? This was the question addressed by the Supreme Court in *Hoffman v. United States*[6]*2*

As *Hoffman* makes clear, an individual can invoke the privilege against self-incrimination in two circumstances[7]. The first circumstance is when the individual is asked a question and an answer in itself would support a conviction under

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1 Cash Intensive Businesses Audit Techniques Guide — Chapter 6 14, Internal Revenue Service.

2 Criminal Tax Manual 14, The Department of Justice.

3 Colin Miller, Criminal Adjudication 239.

4 *Id.*

5 *Id.*

6 *Id.*

7 *Id.* at 246.

a federal [or state] criminal statute…"[1]. For instance, if a defendant is charged with robbery and the prosecutor calls the defendant's alleged co-conspirator and asks him, "Did you rob the bank with the defendant", the witness could invoke the Fifth Amendment privilege because an affirmative answer would itself support a robbery conviction[2].

Second, an individual can invoke the Fifth Amendment privilege if an answer would furnish a link in the chain of evidence needed to prosecute the claimant for a federal [or state] crime"[3]. Assume that a defendant is charged with murder and that the prosecutor calls his alleged co-conspirator as a witness[4]. If the prosecutor asks the witness, "Where is the victim's body", the witness could invoke the Fifth Amendment privilege because an answer pointing the State to the body could be the first link on the chain of evidence needed to prosecute the witness for murder[5]. Can an individual, however, who claims that he is innocent of any criminal wrongdoing,

invoke the privilege[6]? This was the question addressed by the Supreme Court in *Ohio v. Reiner*[7]. As *Reiner* makes clear, even an individual who protests his innocence can invoke the Fifth Amendment privilege against self-incrimination[8]. Assume that a defendant is charged with murder and the prosecution calls his alleged co-conspirator[9]. On the witness stand, the alleged co-conspirator repeatedly answers questions by stating that he had no role in the murder of the victim[10]. Then, when the prosecutor asks him if he knows the location of the victim's body, the witness pleads the Fifth[11]. At a sidebar conference, the judge might ask the witness why he is pleading the Fifth, and the witness could legitimately respond that he played no role in the killing but that an answer identifying the location of the body could lead the prosecutor to think that he was involved in the murder and thus bring charges against him[12].

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1 *Id.*

2 *Id.*

3 *Id.* at 247.

4 *Id.*

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.* at 250.

9 *Id.*

10 *Id.*

11 *Id.*

12 *Id.*

While Ohio v. Reiner stands for the proposition that even an individual protesting his innocence pleads the Fifth, it also states that an individual cannot plead the Fifth if the danger that answering a question could lead to his prosecution is of "imaginary and unsubstantial character…"[1]. Instead, the individual must have "reasonable cause to apprehend danger from a direct answer…"[2].

Assume that a husband is accused of tax fraud based upon misstatements in a joint tax return, and the prosecutor calls his wife as a witness at the husband's trial and asks her questions about statements that her husband made about taxes during tax season[3]. Even though these questions are directed toward the husband's wrongdoing, the wife could likely plead the Fifth on the ground that the prosecutor could easily assume that the statements might have given her constructive knowledge of the tax fraud, making her guilty of some tax-related crime[4].

The court in *Uccellini* noted there is danger in a taxpayer disclosing a cash hoard. The court acknowledged:

Were the taxpayer compelled to come forward with evidence, he might risk lending support to the Government's case by showing loose business methods or losing the jury through his apparent evasiveness... The courts must minimize this danger.' (Emphasis supplied.)

Seemingly appropriate is this admonishment to this case if the taxpayer here were compelled to state when or from where he accumulated the $24,000 which he had available from March to May 3, 1951, to say nothing of his expenditures in excess of declared income during the preindictment years[5].

Birozy indicates the government expects the taxpayer to disclose the cash hoard:

MS. O'BRIEN: Your Honor, it's not reasonable to suppose that if a man has a cash hoard, he would transfer this into some sort of a money order or some sort of other check, and thereafter re-deposit it by check. If a man has a prior cash hoard, he would indeed deposit as cash to the business banking account[6].

Birozy provides:

Secondly, I would state that, again, these are all cash deposits, and it is highly unlikely that any individual who did have a cash hoard would somehow translate the cash into checks and, therefore, deposit it in the checking account. It's much more likely an individual would take cash, deposit it directly to his checking account as cash, and, therefore, since this is not the situation in this case, since we only have

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1 *Id.* at 251.

2 *Id.*

3 *Id.*

4 *Id.*

5 159 F.Supp. at 495.

6 Birozy, 1974 WL 605, 2.

one small $2300 cash deposit, the rest of the deposits were either verified customers' receipts or had the inherent appearance of customers' receipts[1].

Keeping Quiet: Ethics In Tax Practice, Fifth Amendment, And Questions

State ethics rules and opinions, rules of court, and state judicial opinions are as significant in the regulation of tax practice as provisions of the Code (*e.g.*, return preparer penalties in Section 6694) and Regulations[2]. In addition, ethics rules governing accountants who provide tax services are relevant to those who concurrently maintain professional licenses as lawyers and accountants, and also serve as nonbinding guidance to non-accountant lawyers who practice in the tax area[3]. ABA Formal Op. 85-352, however, regards the filing of a tax return as a possible first step in an adversary proceeding"[4]. Therefore, the lawyer has an ethical duty not to mislead the IRS by misstatement, silence, or through her client, but has no ethical duty to disclose the weaknesses of her client's case[5]. She may advise the statement of positions most favorable to the client, even if she believes that the positions probably will not prevail, so long as she has a good faith belief that those positions are warranted in existing law or can be supported by a good faith argument for an extension, modification, or reversal of existing law[6]. On the other hand, where an audit or litigation is underway, the IRS is on notice that the lawyer is an adversary and her primary duty is to the client[7]. Thus, the lawyer's obligations to the IRS in this context are those of one litigator to another[8]. She may make any nonfrivolous argument that could win for the client and need not act in the government's interest[9].

Bar associations at all levels issue advisory opinions on discrete ethical questions[10]. While these are never binding, they are both helpful and instructive[11]. In the area of tax practice, two ABA opinions, ABA Formal Op. 65-314 and ABA Formal Op. 85-352, are and have been particularly influential[12]. ABA Formal Opinion 314 provides:

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1 *Id.* at 3.

2 Linda Galler & *Michael B.* Lang, Regulation Of Tax Practice iv (2nd ed. 2016).

3 *Id.*

4 *Id. at 5.*

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.*

9 *Id.*

10 *Id.* at 7.

11 *Id.*

12 *Id.*

Similarly, a lawyer who is asked to advise his client in the course of the preparation of the client's tax returns may freely urge the statement of positions most favorable to the client just as long as there is reasonable basis for those positions. Thus where the lawyer believes there is a reasonable basis for a position that a particular transaction does not result in taxable income, or that certain expenditures are properly deductible as expenses, the lawyer has no duty to advise that riders be attached to the client's tax return explaining the circumstances surrounding the transaction or the expenditures[1].

It indicates "But as an advocate before a service which itself represents the adversary point of view, where his client's case is fairly arguable, a lawyer is under no duty to disclose its weaknesses, any more than he would be to make such a disclosure to a brother lawyer"[2].

Opinion 65-314 has been superseded as to the "reasonable basis" reporting standard but otherwise accurately describes the guiding principles[3]. ABA Formal Op. 85-352 superseded ABA Formal Op. 65-314 with respect to the "reasonable basis" standard for advising on tax return positions"[4]. Under ABA Formal Op. 85-352:

A lawyer may advise reporting a position on a tax return so long as the lawyer believes in good faith that the position is warranted in existing law or can be supported by a good faith argument for an extension, modification or reversal of existing law and there is some realistic possibility of success if the matter is litigated[5].

ABA Formal Op. 85-352 provides "In many cases a lawyer must realistically anticipate that the filing of the tax return may be the first step in a process that may result in an adversary relationship between the client and the IRS"[6]. No efforts have ever been undertaken to revise ABA Formal Op. 85-352[7]. As an advocate ethics, rules permit a lawyer to advise her client not to volunteer information to the IRS, and the lawyer herself is not obligated to disclose weaknesses in her client's position[8].

The Fifth Amendment privilege precludes compelling a witness to give testimony that is incriminating[9]. Thus, in a summons proceeding and in an ensuing

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[1] Ethical Relationship Between the Internal Revenue Service and Lawyers Practicing Before It, ABA Opinion 314 (1965).

[2] *Id.*

[3] *Id.* at 9.

[4] *Id.* at 9 n. 2.

[5] *Id.*

[6] Tax Return Advice; Reconsideration of Formal Opinion 314, ABA Formal Opinion 85-352 (1985).

[7] Galler & Lang, supra note 73, at p. 137 n. 12.

[8] *Id.* at 13.

[9] *John A. Townsend.* Federal Tax Procedure 847 (2020 Practitioner Ed.).

summons enforcement proceeding, a taxpayer having substantial fear of incrimination from answering the questions posed can assert the Fifth Amendment[1]. In *U.S. v. Matthews*, in response to the summonses, the defendants appeared at the local IRS office separately and refused to answer questions regarding their assets and sources of income, asserting their Fifth Amendment privilege against self-incrimination[2]. The court refused to enforce the summonses[3]. The United States District court determined that invocation of the Fifth Amendment privilege against self-incrimination was appropriate in case finding that:

The defendants had and still have a real apprehension of danger that by answering the IRS's questions and providing documents could lead to evidence necessary to prosecute them for criminal violations. The IRS had conducted a criminal investigation of the defendants for nine years, the last being 2001. Although no charges have been filed, the IRS is unwilling to represent that none will be filed. Transcript ("Tr.") at 23–24, 27 (Jan. 6, 2004). Furthermore, it refuses to grant immunity from criminal prosecution, even though its own counsel has requested it[4].

Matthews provides illustrations of questions to consider not answering "In response to the summonses, the defendants appeared at the local IRS office separately and refused to answer questions regarding their assets and sources of income, asserting their Fifth Amendment privilege against self-incrimination"[5].

Down To Last Penny: Fifth Amendment And Documents

Under current jurisprudence, while the person compelled to produce documents may not assert a Fifth Amendment privilege as to the contents of the documents, the person may have and assert a Fifth Amendment privilege as to any testimonial characteristics inherent in the compulsory act of producing the documents[6]. In *City of Cincinnati v. Bawtenheimer*, the basis of the charge against Ralph Bawtenheimer was his refusal to comply with a subpoena duces tecum from the tax commissioner requiring him to produce certain documents for inspection[7]. The stated ground for his refusal was the Fifth Amendment's protection against self-incrimination[8]. The Court of Appeals of Ohio affirmed dismissal of the charge,

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1 *Id.*

2 327 F. Supp.2d 527, 528 (E.D.Pa. 2004).

3 *Id.*

4 *Id.* at 530.

5 *Id.* at 528.

6 Townsend, supra note 92, at 849.

7 1990 WL 138914, 1 (Ohio Ct. App. 1990).

8 *Id.*

concluding that "As we find *Cates* persuasive on this issue, we adopt its reasoning in the instant case and conclude that the documents subpoenaed herein "fell into the categories of documents for which the act of production may be privileged" by the Fifth Amendment[1].

Secret Stash: Penny Saved Is Penny Earned With Cash Hoard Defense

As noted, an individual can plead the Fifth in response to interrogation or in response to interrogation or in response to a request for evidence[2]. The Supreme Court has stated that the Fifth Amendment only covers "testimonial" evidence that results from compelled communicative acts, i.e., acts which disclose the content of one's mind[3]. But while the prior voluntary creation of evidence is not testimonial, the Supreme Court has recognized the act of producing such evidence might in some cases be testimonial and trigger the Fifth Amendment privilege[4]. This is known as the act of production doctrine[5]. Under this doctrine, the act of producing such evidence in response to a subpoena can be "testimonial" if the act of production involves compelled admissions that the documents exist, are authentic, and are in the witness' possession or control[6].

Assume that Dan is charged with murdering his wife, and the prosecution gets the court to issue a subpoena that compels Dan to produce all diaries or journals that he has created in which he discusses the murder of his wife[7]. If there are in fact such diaries, Dan did not create them under government compulsion[8]. But, if Dan were to produce such diaries, he would be admitting that the diaries exist, that he wrote them, i.e., that they are authentic, and that they are in his possession or control[9]. Therefore, the act of production would be testimonial, and Dan can move to quash the subpoena[10].

Birozy indicates a defendant who is found not guilty in tax case is quiet about the cash hoard initially:

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1 *Id.* at 2.

2 Miller, supra note 49, at p. 255.

3 *Id.*

4 *Id.* at 256.

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.*

9 *Id.*

10 *Id.*

THE COURT: Paragraph 14, "As in a net worth case, *Holland v. United States, supra,* 348 U.S. at 132-35, an essential element of the government's burden of proof in a bank deposits case is to establish an accurate cash on hand figure for the beginning of the taxable year. If the taxpayer's deposits or other expenditures during the relevant year 'came from a safety deposit box in a bank or from a hoard at home, obviously they are not 'income' when taken from their storage place and deposited in a checking account nor when spent.' *United States v. Frank* [57-1 USTC P 9675], 245 F. 2d, 287 (3 Cir), cert. denied, 335 U.S. 819 (1957). Thus,

the government must prove with reasonable certainty the amount of undeposited cash at the beginning of the year so that an appointment amount may be subtracted from the total of deposits made during the taxable year."

This what they're talking about.

MS. O'BRIEN: Yes, your Honor. I would request, then, that for that particular fact, under those cases, when they were dealing with a substantial amount of cash deposited to the business checking accounts, that the requirement under the Second Circuit be applied to a bank deposits case where you do have these cash deposits.

In this case, your Honor, basically, it is irrelevant to the case what his cash on hand was, with the exception of that small $2300 figure. We can delete from the calculations; that's a small amount compared.

I think the rationale that they're applying had particular application to the Nevele situation when there was a substantial amount of cash items deposited to that account and in that particular kind of bank deposit case, where there's cash deposited, then the cash on hand figure must be established. Otherwise, you would have — if that were true for all cases, we would have a net worth case in every single situation which is not again the method of proof the government is using here.

I would state, your Honor, that if – first of all, the defendant has not made any allegations in the opening statement there was any defense that there was a prior cash hoard or money in safe deposit boxes, or anything in that nature[1].

Birozy notes the government claimed the cash on hand amount could not be calculated: THE COURT: Is there any way at all the agents can, in this case, come up with cash on hand?

I'll give you an opportunity to review them. Take a recess for half an hour. See what you can do with them.

MS. O'BRIEN: He claims if it's provided by the defendant. That's the only way at this point that we can get a statement as to the net worth, income, or the cash on hand figure at the beginning[2].

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[1] 1974 WL 605, 3.

[2] *Id.* at 6.

III. KEEP THE CHANGE: FOLLOWING MONEY INSIDE MATTRESS TO THE CASH HOARD DEFENSE

Some Things Money Can't Buy: Cash Hoard Defense Is Worth A Try

Tax controversy enthusiasts will recall that one of the traditional defenses to the net worth method of proof often used in both civil and criminal cases is the cash hoard defense[1]. The net worth method may be stated simply, although the concept may be difficult in application because it takes a lot of work: The method is a simple comparison of the net worth at the beginning of the period and at the end of the period, with the assumption that increases in net worth from the beginning to the end coupled with expenditures in the period are taxable income unless otherwise explained (such as by gifts, unrealized appreciation in value, etc.). The cash hoard defenses argues that the agent incorrectly used the method because the agent understated beginning net worth by leaving out a "cash hoard" or other assets acquired before the beginning that contributed to the ending net worth or expenditures in the period[2]. Since cash is the usual claimed "hoard", this is referred to as the cash hoard defense[3]. A Federal Tax Crimes blog provides:

Apparently, ISIS has some form of income tax and will, perhaps arbitrarily, determine the amount of income and the tax that should be paid. If the ISIS tax police find assets in your home (say cash or some valuable asset such as gold items), they would claim that is part of the income subject to tax. The hapless "taxpayer" — if that is the right word to use — might, with valuable assets like gold at least, claim that those assets were from long ago, such as wedding gifts an therefore should not be considered for that particular genre of income tax. I am not sure how often that would work in the ISIS controlled regions (wonder if ISIS keeps database entries on that), but I guess it is worth a try[4].

William Bethea's trial hinged on a cash hoard. Bethea filed no income tax return for the years 1971 and 1972 and paid no income tax in either year[5]. He testified at trial that increases in his net worth established by the government were derived from an inheritance of between $53,000 and $54,000 which was left him by his brother, Vernon Bethea, who was knifed to death in July 1970 in New York City[6]. According to the defendant, his brother often left him sealed envelopes containing

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1 *Jack Townsend.* The Cash Hoard Defense and ISIS Taxes, Federal Tax Crimes (2015).

2 *Id.*

3 *Id.*

4 *Id.*

5 U.S. v. Bethea, 537 F.2d 1187, 1188 (4th Cir. 1976).

6 *Id.* at 1189

money to be put in his safe deposit box and told him the contents of those envelopes were his if Vernon were to die[1].

The United States Court of Appeals, Fourth Circuit noted "The typical "cash hoard" defense which the government disparges rests upon the totally uncorroborated testimony of a defendant that years ago he buried money in his backyard"[2]. The court indicated:

He says his brother made a lot of money in the narcotic traffic in New York. Vernon's criminal record confirms that he was in the business. Lawyer Moss' testimony confirms that Vernon at times carried very large sums on his person. And finally the bank's record show the rental of a safety deposit box by a defendant living at a poverty level. The government, in short offers no evidence to refute the probability of a cash hoard, and instead, relies solely upon a natural disinclination to believe that large sums of money are ever cached away.

It is not necessary that we believe Bethea's story to reverse his conviction. He is not required, even under the net-worth theory, to prove his innocence; the government must establish his guilt beyond a reasonable doubt[3].

The court concluded "Because of failure to offer evidence sufficient to establish Bethea's guilt beyond a reasonable doubt, the conviction will be REVERSED"[4].

Money In Hand: Net-Worth Expenditures

The net worth method is used often when there is a reason to believe that such records as the taxpayer maintains do not accurately reflect his or her taxable income (and components thereof)[5]. Basically, the net worth method develops taxable by identifying the taxpayer's increase in net worth and nondeductible expenses during the period that can, by inference, indicate that the increase in net worth and nondeductible expenses are from taxable income[6]. In brief, the methodology is:

Taxpayer's net worth at the beginning of the period (one or more years) Less: Taxpayer's net worth at the end of the period.

Plus: Taxpayer's nondeductible expenditures during the period

Less: Income (or asset receipts) from nontaxable sources (such as gifts) Yields: Taxpayer's income during the period[7].

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[1] *Id.*

[2] *Id.* at 1190.

[3] *Id.*

[4] *Id.* at 1192.

[5] Townsend, supra note 92, at p. 435.

[6] *Id.* at 435–36.

[7] *Id.* at 436.

There are variations on this formula[1]. According to the court in *Bethea*:

On the net-worth theory, the government must first establish the total net value of the defendant's assets at the beginning of the tax year in question. That figure is subtracted from the net value of his assets at the close of the tax year, and to it is added all his non-deductible expenditures during the year. The final figure is the defendant's "taxable income" if the government's proof either (1) negates all non-taxable sources of income or (2) demonstrates a likely taxable source which generated the income[2].

Money On The Table: Bank Deposits And Expenditures Methods

This method uses bank deposits on the opening premise that all unexplained bank deposits are taxable income[3]. Depending upon the facts involved, the method then proceeds to reconstruct income[4]. An example of a formula that might be used is:

All of the deposits to the taxpayer's bank accounts(s) during the period Less: Deposits shown to be nontaxable income (such as gifts)

Plus: All known expenditures which were not from the bank account(s)

Less: All expenditures which are deductible

Yields: Taxpayers' taxable income during the period.

A related method is the expenditures method[5]. If the IRS had done a sloppy job in performing the indirect method analysis or used a methodology that does not fit under the taxpayer's circumstances, a court may throw it out altogether or give the taxpayer all benefit of the doubt despite the supposed burden of proof being on the taxpayer[6].

Cash on hand is one of the most common and troublesome areas in any indirect method computation[7]. Because a cash hoard defense is so difficult to refuse, subjects frequently claim their cash hoard was of a sufficient amount to account for any understatement of income[8]. In *Bryan v. U.S.*, Bryan did not take the stand, but his wife did, and testified that when she married the Defendant in 1926 he was a bootlegger possessed of approximately $180,000, the residue of which was kept in a safe in a closet in their home until November 4, 1940, when she rented a lock

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1 *Id.*

2 537 F.2d. at 1188–89.

3 Townsend, supra note 92, at p. 436.

4 *Id.*

5 *Id.*

6 *Id.* at 437.

7 Internal Revenue Manual 9.5.9.7.4.9.

8 *Id.*

box at the Florida National Bank in Jacksonville wherein she put between $150,000 and $160,000 in cash[1]. An exchange addressed cash money:

'By the Court:

'Q. If you overlooked any assets that this defendant had, in your calculations, then your calculations would be in error, or subject to revision? A. Yes, sir.' (R. 289.)

'Q. And you don't mean to say that he had no money whatsoever other than what is shown on that bank account, shown on January 1, 1941? A. I didn't say that.

'Q. Doesn't your audit assume that? A. That is all the money we could account for.' (R. 296.)

'Q. And you took into consideration only recorded purchases that you could find?

A. That was all I could.

'Q. That was all you could? A. Yes.

'Q. During the course of examining Mr. Bryan, did you inquire into the cash sales that he made prior to that time? A. No.

'Q. Did the Department, or someone in your presence in one of the Government Departments, make inquiry into that? A. I would not know. (R. 300.)

'Q. Yet up until that time you had never found a bank account, up unitl 1940, that Mr. Bryan had? A. No.

'Q. And yet you assume that the only monies he had were in the bank on the first day of January, 1941? A. That is all we took into account.

'Q. You don't know whether he had a lot of other money, or not? A. No, sir.' (R. 302–303.)[2].

The United States Court of Appeals reversed finding that:

The jury no doubt disbelieved, and had the right to disbelieve, Mrs. Bryan's testimony, but in view of the auditor's admissions that he was not able to say that his computation included all of the assets of the Defendant at the beginning of the period, together with the absence of any admissions, records, financial statements, bookkeeping entries, or other findings, or evidence, tending to bind the defendant as to the lack of additional assets at the beginning of the tax period, the evidence, in the light of the bill of particulars, was insufficient to make out a prima facie case against the defendant on the net worth-expenditure basis, and the case should not have been submitted to the jury since it did not exclude the hypothesis that the funds used in making some of the expenditures might have been from sources other than current business income[3].

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[1] 175 F.2d 223, 226 (5th Cir. 1949).

[2] *Id.*

[3] *Id.* at 227.

The Internal Revenue Manual addresses the option to hoard money and bank deposits method of proving income:

The theory behind the bank deposits method of proof is simple: There are only three things a subject can do with money once it is received, i.e., he/she can spend it, deposit it, or hoard it. Accounting for these three areas considers all funds available to the subject. If non-income sources are eliminated, the remaining currency expenditures, deposits, and increases in cash on hand will equal corrected gross income[1].

It indicates:

An increase in the subject's cash on hand is treated as a currency expenditure. Since the subject may contend that the unexplained deposits into the bank accounts came from a cash hoard, it is crucial to thoroughly establish and document any increase in the subject's cash on hand.

The special agent must begin by documenting the cash on hand at the starting point and then document cash on hand at the end of each year under investigation. The cash on hand increase (or decrease) is then determined for the first year of the investigation by subtracting the cash on hand at the starting point from the cash on hand at the end of the first investigative year[2].

Savings Jar: Living Frugally To Cash In On Cash Hoard Defense

Evidence developed during the course of a thorough financial investigation may be used to prove actions inconsistent with a cash hoard[3]. The Criminal Tax Manual provides:

For example, an individual with a cash hoard would not

— withdraw money at ATMs in $20-$40-$60 increments;
— obtain high interest rate loans;
— borrow relatively small amounts of money from friends/relatives to buy assets or pay bills;
— pay high fees to cash checks;
— be charged NSF fees for bounced checks in his or her bank account;
— pay over time for appliances, furniture, carpeting, etc.; or
— engage in other spending, or manifest a lack of spending, inconsistent with a person who had access to significant sums of currency[4].

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[1] IRM 9.5.9.7.1.

[2] IRM 9.5.9.7.4.3.

[3] The United States Department of Justice, Criminal Tax Manual 17.

[4] *Id.*

Living frugally has a relationship with the cash hoard defense. *Kleiman* indicates about the defendant who had a father with a large hoard of money that "He lived frugally with his unmarried daughter who had her own income"[1]. While it is often difficult to disprove the existence of a cash hoard, the government can often prove acts that are inconsistent with a person's having had a substantial amount of currency available to spend[2]. Such proof might include evidence that the defendant took out a high interest rate loan to purchase a vehicle or home furnishings or that the defendant made frequent ATM withdrawals in small increments[3].

One's Man's Trash Is Another's Man Treasure: The Power Of The Dollar That Builds A Cash Hoard

There are various ways to build a cash hoard. In *U.S. v. Melillo*, Nicholas Melillo was charged with willfully attempting to evade the payment of income taxes[4]. Melillo a laborer, began a garbage and rubbish collection service[5]. His first four Brooklyn customers, referred to by him as 'stops', were 'donated' by a relative, one Gallo[6]. His married sister kept the books[7]. Central to the success of the business was defendant's mother, a matriarch of the old school[8]. In addressing the issue, the United States District Court noted:

Trucks and new stops were purchased from money advanced by the mother. She used some dozen substantial bank accounts in her name, individually and as co-owner. These assets were said by her to have come from cash received from her father and other relatives.

The mother also hired an 'accountant' to help with the books. He was without formal training in this country and his main vocation was as a customer's man in a brokerage office. Experts for both the government and the defense agreed that the accounting techniques used were not satisfactory. For example, tens of thousands of dollars in income each year from major customers, including Fort Totten Army Base in Brooklyn, were deposited directly in the mother's many bank accounts, bypassing the business records completely. This income was not reflected in the tax returns prepared by the accountant. Cash, claimed to have amounted to more

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1 167 F.Supp. at 875.

2 Criminal Tax Manual, supra note 1, at p. 13.

3 *Id.*

4 275 F.Supp. 314 (E.D. N.Y. 1967).

5 *Id.*

6 *Id.*

7 *Id.*

8 *Id.*

than twenty thousand dollars each year, was used to 'purchase stops'. The recipients of these disbursements were not shown on the books and defendant refused on and off the witness stand to tell them who any of them were.

Whether the mother followed the accountant's directions — as she testified — or he hers — as appears possible from her forceful personality — is impossible to determine. He died a natural death after the government began its tax investigation. Some of the papers relating to the business perished with him[1].

The court acknowledged:

The problem of jury control at the trial level is particularly important in a case like the present one where prejudice lurks. The trial judge, observing the jury, sensed a distinct danger that it, would rely upon rumor current in the local process to conclude that defendant was linked with organized crime and weigh this conclusion against him in determining guilt[2].

The court indicated:

The defendant was closely associated — as owner of his own business and as a trade association official — with the garbage collecting industry, believed to be influenced by criminals; he received assistance from a cousin named Gallo — a named associated in the public's mind with organized crime; and there were large payments for 'purchasing stops' to unnamed persons — who might have been used to channel cash into the underworld[3].

The court concluded "The motion for judgment of acquittal is granted"[4].

Badge Of Honor: Cash Hoard Money Machine

In making the determination, as with criminal cases, courts will often look to certain common patterns indicating fraud-referred to as badges of fraud, such as unreported income, failure to keep adequate books, dealing in cash, etc[5].

However, in *Kleinman* a defendant employed by the IRS who was dealing in cash used the cash hoard defense to explain receipts during his IRS employment:

In the instant case the defendant was employed as an agent of the Internal Revenue Service from 1935 until 1951. It should be stated preliminarily that this is a case involving no specific items of allegedly unreported income. It appears that the defendant filed returns for and paid income taxes upon his salary as an

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1 *Id.* at 315.

2 *Id.* at 319.

3 *Id.*

4 *Id.* at 320.

5 Townsend, supra note 92, at p. 321.

agent and upon capital gains, interest and dividends earned by him during these years[1].

In *Kleinman*, the defendant employed as an agent of the Internal Revenue Service from 1935 until 1951 had a father who built a cash hoard:

The defendant testified that during the 1940's his father earned about $50 per week, and that prior to that period he earned more. The defendant's mother worked for fifteen years prior to her death in 1929, and earned about $35 per week which she gave to her husband. The defendant and his two sisters starting working at a young age and turned money over to their father[2].

In *Uccellini*, the court indicated that:

Preliminarily, it is to be observed that defendant might have acquired and set aside more money that is represented by his expenditures during the preindictment years and in 1950. Of course, this statement is mere speculation, but a look at the government's evidence demonstrates that defendant had a substantial amount of available cash in March and April, 1951[3].

In *Birozy*, the court suggested the cash hoard might have just as easily come from pay day money in the taxpayer's piggy bank:

THE COURT: It does stand for the fact you must start with some monies at the beginning of the year. What was the cash on hand when they started for that period?

If he started with zero, then you can assume all the money placed in there was income, but if he started with, let's say $100,000 left over from the year before, and that's been reported at prior income tax period, then you must deduct that from the following year. That hasn't been done here[4].

IV. WALKING RIGHT INTO A TRAP: TAX AGENT ENTRAPMENT

Prior to utilizing a CI/CW, the controlling special agent, in the presence of the back up agent or other law enforcement office will review the applicable information on Form 9834 with the CI/CW which covers "The CI/CW will not tamper, intimidate, or entrap any witnesses, nor will they fabricate, alter, or destroy evidence"[5]. In *U.S. v. Campbell*, Alphonso Campbell is charged with engaging in the business of accepting wagers on horse races without registering or paying the tax[6]. The only evidence of such a continuity of activity as could amount to being 'engaged'

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1 167 F.Supp. at 873.

2 *Id.* at 875.

3 159 F.Supp. at 494.

4 1974 WL 605, at 2.

5 Internal Revenue Manual 9.4.2.5.4.11.

6 235 F.Supp. 190 (E.D.N.Y. 1964).

either 'in the business of accepting wagers' or 'in receiving wagers' was evidence of the receipt of a series of wagers from Agents of the Internal Revenue Service at their solicitation effected through a man defendant had known for forty years; there was no evidence that defendant had theretofore been suspected, reasonably or otherwise, of being engaged in receiving wagers and there was only one episode, somewhat ambiguous, of the receipt of a wager from any other person and that was coincident with the last of the series of wagers placed by the Internal Revenue Agents[1]. In determining there must be an acquittal on both counts the United States District Court finds that:

The great difference is that the Agents' activities must serve to throw light on independently existing criminality and must not themselves be the constitutive elements of all the offense that is made to appear. The test of criminality is not the embittered and disdainful standard of Mark Twain's The Man that Corrupted Hadleyburg, the ability to withstand calculated temptation by the Government, but the more useful standard of actual engagement in the criminality at the solicitation of others than the Government; where that exists, the evidence of Agents' activities is useful, but useful only as it proves criminality beyond that which consists solely in the immediate reciprocals of the Agents' acts.

It follows that in this case there must be an acquittal on both counts[2].

In *Zwak v. U.S.*, an undercover operation, conducted by agents of the Alcohol, Tobacco & Firearms Division of the Treasury Department, resulted in criminal charges against Jerald Swak for crimes of making and transferring firearms without pay the tax and possession of firearms which did not have serial numbers[3]. At his criminal trial, Zwak raised the defense of entrapment[4]. The jury returned a verdict of acquittal[5]. Zwak sought a claim for tax refund incorporating into the complaint the allegations of entrapment previously made in his claim to the IRS[6]. According to the United States Court of Appeals "In conclusion, the district court's grant of summary judgment in favor of the United States of America is REVERSED and the case is REMANDED"[7].

When requesting the use of Federal prisoners the Federal Prisoner Application and Appendices must include "Acknowledgement that the Federal prosecutor has

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[1] *Id.*

[2] *Id.* at 191.

[3] 848 F.2d 1179, 1180 (11th Cir. 1988).

[4] *Id.*

[5] *Id.* at 1181.

[6] *Id.* at 1181.

[7] *Id.* at 1185.

considered entrapment issues and foresees no problems"[1]. The Internal Revenue Manual provides:

While controlling a CI/CW, special agents will not:

Make any promises of immunity or give the impression that the special agent has the authority to do.

Authorize the CI/CW to participate in an act that would be unlawful if conducted by a law enforcement officer.

Let a CI/CW determine the procedure to be used in the investigation or otherwise control the investigation.

Condone any violation of law in order for a CI/CW to obtain information. If a defendant can show that that the CI/CW was acting under some arrangement with Federal agents, he/she will have a viable defense. Whenever there appears to be a possibility of entrapment or some other unlawful act by a CI/CW, he/she should be guided in a manner that will prevent the occurrence of such acts[2].

According to the Internal Revenue Manual "Undercover agents will avoid acts of entrapment and must observe the Constitutional rights of persons they come in contact with during assignments"[3].

V. POT OF GOLD: TAX EVASION MESSAGE OF INNOCENCE AT END OF RAINBOW

The Solicitor General of the United States ("SG") has two key roles in tax litigation[4]. The SG's lawyers are the crème de la crème and usually beyond political influence[5]. Federal Tax Procedure information provides:

In any event, as I said, there did appear to be a conflict among the circuits and, at the time, a conflict was almost guaranteed certiorari material. I therefore recommended that the United States seek certiorari in the case. The SG (Dean Griswold whom I mentioned in two paragraphs up) himself nixed the recommendation, noting in handwriting on my recommendation that (and this is a paraphrase but pretty close to the actual quote) "We can't take a mitigation case to the Supreme Court, for they will never understand it"[6].

Dean Griswold's quote should not be read for the proposition that the Supreme Court of the United States is over qualified to resolve any case. The District Judge

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[1] Internal Revenue Manual 9.4.2.5.13.1.

[2] Internal Revenue Manual 9.4.2.5.8.

[3] Internal Revenue Manual 9.4.8.8.

[4] Townsend, supra note 92, at p. 99.

[5] *Id.* at 100.

[6] *Id.*

in *Birozy* understood it is simple that the cash hoard defense is king. *Birozy* provides:

THE COURT: That's not the argument. It's the argument, it's the question of what was deposited of any resources whatsoever, including the cash on hand. That's the argument. That must be deducted. That must be deducted.

In other words, you can't say the man has a going business for prior years and he's paid taxes on the amount of money that have been in that account and he starts off with an account for 1965 with $150,000, he's already paid taxes on. You can't tax him to say he made $150,000. You have to start off with cash on hand. That, to me, is simple. That's business[1].

The court indicates:

THE COURT: Madame Forelady, ladies and gentlemen of the jury:

I advised you on Friday that a serious problem, a question of law, had been propounded to the court and that the Court was going to give it complete research as to the question of proof that would be permitted in this trial, the admissibility of that proof.

There is one case that the Court had to follow with a line of the essentials of the elements in the trial of this type must be proven by the government and lacking any one of those essentials, then the case must fail

It has nothing to do with yourselves or myself. It's a Court of Appeals case.

We can make determination, decisions on the cases, of cases recited prior to the ones we're trying.

I had given the opportunity to the government and Ms. O'Brien to see whether or not she could obtain the necessary proof to go forward with the case and meet the required essential which has been set forth in the United States versus Slutsky, which is the case I was following, and I've been advised the evidence they have is the only evidence they can produce before the jury.

On the basis of that, the Court accepted the motion to acquit the defendant for failure of proof. On that basis, the indictment is dismissed and I dismiss you with the thanks of the Court, and I do hope you don't think I've taken the facts away from you, but I must go according to the law.

Sometimes, I know that people get a little disturbed by the fact the judge takes the law in his own hands and does what he thinks is right, and they want to know how come they haven't a right to make a determination. Just remember one thing: as I told you when I selected you, that I will continue to be the judge of the law, contrary to what anybody else may say. I will do what I think is right in my own good conscience, as I interpret the law.

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[1] 1974 WL 605, 4.

I've been on the bench for 19 years. I'm not a newcomer to the judiciary in any sense of the word. I've been doing that all my entire tenure on the bench as a judge.

I've made my own decisions. This one, I feel I'm absolutely right in. Thank you. Have a good day. It's a nice day outside[1].

The IRS understands the cash defense is king. The Internal Revenue Manual indicates:

1. When a subject offers leads or information during a net worth investigation that, if true, would establish his/her innocence, such leaders must be pursued. This also applies if the subject offers leaders or information after the completion of an investigation but within sufficient time before trial.
2. During the trial, if the government fails to show an investigation into the validity of the leads provided by the subject, the trial judge may consider the defendant's information as true and the government's investigation insufficient to go to the jury.
3. Most leads refer to cash hoards, gifts, inheritances, and loans. These leads should be checked as routine steps taken during the investigation[2].

However, if a case has certain problems taxpayers following the money may be the most invested in the cash hoard defense paying off.

In making the determination, as with criminal cases, courts will often look to certain common patterns indicating fraud-referred to as badges of fraud, such as unreported income, failure to keep adequate books, dealing in cash, etc.[3]

However, in *Kleinman* a defendant employed by the IRS who was dealing in cash used the cash hoard defense to explain receipts during his IRS employment:

In the instant case the defendant was employed as an agent of the Internal Revenue Service from 1935 until 1951. It appears that the defendant filed returns for and paid income taxes upon his salary as an agent and upon capital gains, interest and dividends earned by him during these years[4].

Additionally, *Uccellini* reinforces the reality why taxpayers should write down as little as possible.

The defendant was engaged in the restaurant business in Pittsburgh. Since about 1942 he operated restaurants as an equal partner with Gilbert Kinderman who individually conducted a restaurant supply business. On March 31, 1951, defendant bought Kinderman's interest and thereafter operated the restaurant known as 'Emil's' as an individual enterprise.

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[1] *Id.* at 7–8.

[2] Internal Revenue Manual 9.5.9.5.8.

[3] Townsend, supra note 92, at p. 321.

[4] 167 F.Supp. at 873.

In 1944 the partnership purchased the building in which 'Emil's' was located, and in 1943 and 1946 defendant, or defendant and his wife, bought four properties in or near Pittsburgh. One of the latter was sold prior to 1950, but the defendant continued to own the others through 1951.

Defendant derived income from the restaurant and rentals from some of the real estate.

Other than a check book, he kept no personal books or records of his income[1].

The court acknowledged "The efforts to show that the partnership understated its actual income failed when the partnership bookkeeper did not testify as expected, but said she entered the daily receipts in the partnership books as shown by the cash register tapes which she destroyed"[2]. In *Birozy*, the court notes "The fact that the years following 1965 at here turned up increasing proportions of identifiable deposits indicates that the problem here was not the investigatory methods of the prosecution, but rather the fact that the businesses which paid defendant simply did not keep their old records"[3].

One issue is will never they understand cases are just a § 441 situation where the taxpayer keeps no books. Most individuals really have no choice about what taxable year they use since section 441(g) requires the calendar year for taxpayers who either keep no books or who otherwise lack an annual accounting period"[4]. It is not expected taxpayers will keep adequate books:

Treas. Reg. § 1.441-1(b)(7) explains that "books" must be sufficient to reflect income adequately and clearly", but merely having a checkbook — the extent of most individuals' books — is probably not adequate. While there are often advantages to an individual using a fiscal year, to do so an individual would have to keep books with respect to her income on a fiscal year basis for the first year in which she had income, a most unlikely occurrence[5].

In *Melillo* experts for both the government and the defense agreed that accounting techniques used were not satisfactory:

The mother also hired an 'accountant' to help with the books. He was without formal training in this country and his main vocation was as a customer's man in a brokerage office. Experts for both the government and the defense agreed that the accounting techniques used were not satisfactory. For example, tens of thousands of dollars in income each year from major customers, including Fort Totten Army

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1 159 F.Supp. at 491–92.

2 *Id.* at 494.

3 1974 WL 605, 1.

4 Lang, Manning, & Hymel, supra note 7, at p. 10.

5 *Id.*

Base in Brooklyn, were deposited directly in the mother's many bank accounts, bypassing the business records completely. This income was not reflected in the tax returns prepared by the accountant. Cash, claimed to have amounted to more than twenty thousand dollars each year, was used to 'purchase stops'. The recipients of these disbursements were not shown on the books and defendant refused on and off the witness stand to tell them who any of them were.

Whether the mother followed the accountant's directions — as she testified — or he hers — as appears possible from her forceful personality — is impossible to determine. He died a natural death after the government began its tax investigation. Some of the papers relating to the business perished with him[1].

The court finds:

Both mother and son testified that he had not dealt at all with the accountant and had not seen or had any notion of the books or of the tax returns. The mother testified that only she and her daughter talked to the accountant. This testimony was partially confirmed by that of the government investigators who had to obtain details from the accountant rather than from the defendant.

Whatever uncertainty may have existed as to whether there could be a reasonable doubt about defendant's knowledge was dispelled by the government. It rigorously cross-examined the business's recently retained Certified Public Accountant — a man of conceded reputation and skill, whose direct testimony tracked that of government experts. He had been called by the defense to show the inadequacy of the books previously kept by the business in an effort to demonstrate that the deceased accountant's advice had been bad. Pressed by the Assistant United States Attorney, he testified that the prior accountant had declared that all of his dealings were with the mother and sister[2].

The record reads as follows:

Q You didn't ask Mr. Melillo (the defendant) during the entire indictment years, which he is being tried for right now, '57, '58, '59, if he discussed these books and records with Mr. Lo Castro (the dead accountant)? Is that your testimony?

A The only thing Mr. Lo Castro told me was that he had all his dealings with Mrs. Melillo and Mrs. Vivian Magliano (defendant's sister).

Q I am asking you now in the preparation of the defense of this case. Did you ask Mr. Melillo, the defendant, whether he ever discussed during the indictment years the books and records of Melillo Carting with Mr. Lo Castro?

A. No, sir[3]. The court observed:

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[1] 275 F.Supp. at 315.

[2] *Id.* at 315–16.

[3] *Id.* at 316.

The declaration of the former, now deceased, accountant was, of course, hearsay. But it had considerable probative force. There was no obvious reason for the former accountant — the hearsay declarant — to lie about the matter in dealing with his successor. The witness, a Certified Public Accountant had no substantial reason to falsify[1].

Matthews indicates:

The summonses sought testimonial and documentary evidence. The defendants did not, as the IRS suggests, refuse to produce documents. They informed the IRS that they did not have any documents responsive to the requests. In re: Richard L. Matthews, Hearing, at 14–15 (May 29, 2003). Consequently, it was not necessary to consider the application of the act-of-production doctrine[2].

Campbell considers whether the IRS is walking taxpayers right into a trap:

The great difference is that the Agents' activities must serve to throw light on independently existing criminality and must not themselves be the constitutive elements of all the offense that is made to appear. The test of criminality is not the embittered and disdainful standard of Mark Twain's The Man that Corrupted Hadleyburg, the ability to withstand calculated temptation by the Government, but the more useful standard of actual engagement in the criminality at the solicitation of others than the Government, where that exists, the evidence of Agents' activities is useful, but useful only as it proves criminality beyond that which consists solely in the immediate reciprocals of the Agents' acts.

It follows that in this case there must be an acquittal on both counts[3].

Zwak indicates the Treasury Department is involved with undercover operations:

An undercover operation, conducted in 1979 by agents of the Alcohol, Tobacco, & Firearms Division of the Treasury Department, resulted in criminal charges against the taxpayer, Jerald D. Swak for crimes of making and transferring firearms without paying the tax and possession of firearms which did not have serial numbers[4].

Kleinman indicates the cash hoard of a taxpayer's relative is a defense:

Assuming, arguendo, that these were deposits of the defendant's funds in the continued pursuit of a conspiracy in his behalf, in the absence of evidence indicating the actual state of facts, it is as reasonable to conclude that this was the systematic disposition by the father of a hoard accrued by the defendant in some prior

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[1] *Id.*

[2] 327 F.Supp.2d at 528–29.

[3] 235 F.Supp. 190.

[4] 848 F.2d 1179, 1180.

period, as it is to conclude that the funds were the current unreported earnings of the defendant transmitted to his father in some unknown manner"[1].

Bethea suggests a taxpayers have a lot to gain from a personal cash hoard defense:

The typical "cash hoard" defense which the government disparges rests upon the totally uncorroborated testimony of a defendant that years ago he buried money in his backyard. Bethea's story is atypical. He says his brother made a lot of money in the narcotic traffic in New York. Vernon's criminal record confirms that he was in the business. Lawyer Moss' testimony confirms that Vernon at times carried very large sums on his person. And finally the bank's records show the rental of a safety deposit box by a defendant living at a poverty level. The government, in short offers no evidence to refute the probability of a cash hoard, and instead, relies solely upon a natural disinclination to believe that large sums of money are ever cached away[2].

Use of an annual accounting system for the income tax has a number of consequences and offers planning opportunities that go far beyond merely shifting income from December of one year until January of the following year, or shifting a deduction from one year to another[3]. The lawyer's personal integrity is particularly significant in tax planning, where the lawyer assists her client in making or creating facts, rather than in characterizing events that have already occurred[4]. A taxpayer needs to create five things given planning opportunities. First, a relative with a cash hoard. Second, a personal cash hoard. Third, willingness to exercise the Fifth Amendment privilege against self incrimination. Fourth, a lawyer. Fifth, the least method of accounting regularly used allowable. There is a pot of gold at the end of the tax case message of innocence rainbow. It is pay day, because of the tax cash hoard defense hidden inside the couch.

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[1] 187 F.Supp. at 874.

[2] 537 F.2d at 1190.

[3] Lang, Manning, & Hymel, supra note 7, at p. 7.

[4] Galler & Lang, supra note 73, at p. 3.

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