

# **FAILURE TO MAINTAIN BUSINESS RECORDS CAN LEAD TO PROSECUTION**

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## **Failure to Maintain Business Records Can Lead to Prosecution**

*Written by Sanford Millar of MillarLaw A Professional Corporation – 10/17/16*

A recent appellate court case out of New York (U.S. vs. Marinello) affirmed the conviction for tax evasion of a taxpayer for failing to maintain business records and timely file income tax returns. The facts of the case are as follows:

“In 1990, Marinello incorporated Express Courier Group/Buffalo, Inc. (“Express Courier”), a New York corporation. Express Courier maintained a freight service that couriered documents and packages between the United States and Canada. Despite owning and managing the company, Marinello maintained little documentation of his business income or expenses. He shredded or discarded most of the business’s records, including bank account statements, employee work statements, gas receipts, and bills. Marinello paid his employees in cash and did not issue them (or himself) tax documents such as familiar Form 1099s or Form W2s. He often used Express Courier’s funds for personal purposes, including mortgage payments on his residence (made indirectly through weekly cash contributions to his wife) and monthly payments to his mother’s senior living center.

In each of the years 2005 through 2008, Express Courier had generated annual total gross receipts of between \$200,718.88 and \$445,184. During each of those years, Marinello took approximately \$26,000 to \$50,000 from Express Courier’s business account and spent it in payment of his personal expenses.

In 2005, Marinello sought the advice of counsel, whom he informed of his failure to file his tax returns. Counsel told Marinello that this failure to file was improper and referred him to an accounting firm for a consultation. Allan Wiegley, a certified public accountant at that firm, told Marinello that he needed to provide records of business receipts and expenses in order to pay corporate taxes with respect to Express Courier and its business. Marinello was unable to do so: **He had destroyed or failed to keep the documents."**

**The taxpayer was charged with** "corruptly endeavoring to obstruct and impede the due administration of the Internal Revenue laws, in violation of 26 U.S.C. § 7212(a) (Count One), and willfully failing to file individual and corporate tax returns for calendar years 2005 through 2008, in violation of 26 U.S.C. § 7203 (Counts Two through Nine). Count One alleged that Marinello had violated section 7212(a) by, "among other thing[s]":

- (1) failing to maintain corporate books and records for [Express Courier] of which the defendant was an employee, officer, owner and operator;
- (2) failing to provide the defendant's accountant with complete and accurate information related to the defendant's personal income and the income of Express Courier;
- (3) destroying, shredding and discarding business records of Express Courier;
- (4) cashing business checks received by Express Courier for services rendered;
- (5) hiding income earned by Express Courier in personal and other nonbusiness bank accounts;

- (6) transferring assets to a nominee;
- (7) paying employees of Express Courier with cash; and
- (8) using business receipts and money from business accounts to pay personal expenses, including the mortgage for the residence in which the defendant resided and expenses related to the defendant's mother's care at a senior living center.

The key to understanding the court's affirmation of the conviction is found in the following part of the court's discussion of the law"

Section 7212(a) criminalizes certain "[attempts to interfere with [the] administration of internal revenue laws." Under section 7212(a),[w]hoever [1] corruptly or by force or threats of force (including any threatening letter or communication) endeavors to intimidate or impede any officer or employee of the United States acting in an official capacity under this title, **or [2] in any other way corruptly or by force or threats of force (including any threatening letter or communication) obstructs or impedes, or endeavors to obstruct or impede, the due administration of this title**, shall, upon conviction thereof, be [fined or imprisoned, or both]. 26 U.S.C. § 7212(a) (emphases added). The first clause addresses conduct specifically directed toward federal officers or employees in the discharge of their duties under Title 26 of the United States Code the Internal Revenue Code. The second clause, the "omnibus clause," is a catchall provision that criminalizes "any other way" of corruptly obstructing or impeding the due administration of the Internal Revenue Code. The term "corruptly" within the meaning of this section encompasses conduct that has "the intent to secure an unlawful advantage or benefit either for one's self or for another." *United States*



*v. Parse*, 789 F.3d 83, 121 (2d Cir. 2015) (quoting *United States v. Kelly*, 147 F.3d 172, 177 (2d Cir. 1998)).

Marinello asks that we conclude, as the Sixth Circuit did in *Kassouf*, that the statutory phrase “the due administration of this title” under the omnibus clause refers exclusively to pending IRS investigations or proceedings, of which a defendant must have knowledge in order to corruptly obstruct or impede them. For the reasons that follow, we decline to adopt this construction.”

It is the holding under 7212(a)(2) that forms the basis for the crime and the conviction. The taxpayer knowingly failed to maintain business records and/or destroyed those records, thereby violating the provisions of section 7212(a)(2). This case is important to all business owner’s but in particular those who operate cash businesses and who may be lax in record keeping. It also demonstrates that a mere consultation with tax professionals will not be a sufficient defense to charges under section 7212(a)(2) absent affirmative acts to properly estimate and report income and expenses.

The taxpayer in this case should have retained counsel and provided bank records and all other records available or accessible to counsel for review and analysis. Counsel could then hire a certified public account to prepare estimates of tax scenarios as privileged “work product” and once a proper reporting scenario is determined prepare the late returns. The taxpayer would most likely face Failure to File and Failure to Pay penalties, but the alternative just hoping not to get caught is hardly a rational approach.

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