

### PROFESSIONAL RESPONSIBILITY

# Criminal Considerations For Fiduciaries



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Fiduciaries—both individual and corporate—run the risk of being charged with numerous crimes. Some crimes are intentionally committed, while some arise unintentionally but nevertheless create criminal liability. While not exhaustive, this article provides insight into some of the criminal charges fiduciaries may face.

### Tax Fraud

Any person, including a corporation, who willfully attempts to evade the payment of taxes owed to the United States, may violate Internal Revenue Code (IRC) §7201, which states in part:

Any person who willfully attempts in any manner to evade or defeat any tax imposed ... or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined or imprisoned or both ...

Thus, elements of an offense under IRC §7201 are: an attempt to evade or defeat a tax or the payment of a tax; an additional tax is due and owing; and willfulness. Each element is required to be proven beyond a reasonable doubt. This

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is a federal felony, and penalties may be \$250,000 for individuals and \$500,000 for corporations. For individuals, significant incarceration may also be imposed.

Note that the statute is inclusive. It includes evading or defeating the assessment of tax or the willful attempt to evade or defeat payment of a tax. The term “person” is also inclusive. It may include a person or a corporation. Employees and officers, as well as partners in a partnership or members in a Limited Liability Company, may be criminally liable if they had a duty to perform tax responsibilities and did not, or someone else also having a duty failed to act properly and the fiduciary did not correct him or her. The term person also includes guardians and executors.

IRC §7201 may result in prosecution for someone else’s tax liability. For example, it is possible that someone assisting a taxpayer in committing tax fraud may also be committing fraud himself. This class of persons may include bookkeepers, controllers, accountants and others working with or on behalf of a taxpayer. Examples of potential criminal tax acts noted by federal officials include: keeping double sets of books; making false or altered entries; falsifying invoices; destroying records; concealing income sources; and behaving so as to avoid discovery

While there is much to be said about the proof of each element of an offense under IRC §7201, one serious aspect must be noted: Making false written or oral statements to federal officers is a crime. Government agents and judges take the making of false statements very seriously. These acts go to the very integrity of our criminal justice system. Do not make any statements before seeking the advice of counsel.

### Privilege Concerns

Keep in mind that, as a general rule, accountants do not have the status of privilege when dealing with a client. Attorneys for retained clients have attorney/client privilege. This attorney/client privilege prevents an attorney from divulging information or documents provided by the client. Clients do not have that protection when speaking or providing documents to accountants. That accountant can be made to testify against the client and disgorge documents provided by the client. Thus, an important rule of thumb is: Do not speak to the accountant or provide any documents once the client becomes a possible suspect or target of a criminal investigation. Clients should never speak or provide documents to a government agent or attorney but rather should tell them to contact the client’s attorney. This will ensure that the client does not

divulge damaging information or documents without advice from and protection of counsel. For those readers who remember the TV show *Perry Mason*, whenever a prospective client visited the titular attorney, he asked that person for one dollar. When he got that dollar, he was then retained and the attorney/client privilege became effective. Make sure you are retained before obtaining information and documents from the prospective client. If not retained, the privilege does not become effective.

### Other Considerations

**Funds.** There have been trustees and executors who have “borrowed” funds from the assets entrusted to them. This is illegal under state law, with grand larceny being just one of the possible charges.

**Referral payments.** Another fiduciary “mistake” is hiring a financial advisor who makes “referral” payments to the fiduciary. This may be illegal under state law, as it is a violation of a fiduciary’s responsibility of undivided loyalty to the fund it manages and its beneficiaries. At the same time, it may create a tax crime if the fiduciary does not include the value of what was received on its personal or corporate income tax return.

**More tax issues.** Some items to be included in income for tax purposes are gambling proceeds; campaign contributions used for personal gain; embezzlement (even if repaid); and extortion proceeds, fraud income, loans received with no intent to repay, and kickbacks.

Other crimes include failure to file tax returns, failure to collect a tax, submitting fraudulent withholding certificates and more.

### What’s a Fiduciary to Do?

How do all of these issues affect fiduciaries? It’s simple: Many fiduciaries deal with income, expenses, and less than honest individuals, and must protect

themselves from getting caught in the crosshairs of a federal agent.

A fiduciary must keep and retain full and complete books and records. This includes all bank and brokerage statements, including all transactions that have taken place. One author not long ago represented a trust beneficiary who believed that the trustee invaded the trust for his own benefit. A meeting was called and the trustee arrived. When asked to see his records, he unfolded a wall of papers that were taped together, representing his trust accounting records. Needless to say, that trustee had a serious problem.

Fiduciaries need to be extra careful since they deal with other peoples’ assets, may deal with persons (corporations) unknown to them, and are held to a high standard of care. International transactions and assets are many times dealt with by financial

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advisors. The fiduciary must understand what assets the funds are being invested in. After all, the buck stops with the fiduciary.

Given all of the above considerations, the fiduciary needs to be careful when a beneficiary is the person being investigated. It is possible the government agents may contact the fiduciary for information or documents. Even though the fiduciary is not the target of the investigation, it is recommended that the fiduciary seek advice of an attorney before speaking to the agent or providing documents. It is always possible that the fiduciary may have acted inappropriately and needs advice and attorney/client privilege protection.

New York tax statutes in many cases mirror the federal ones. The New York Attorney General’s Criminal Enforcement and Financial Crimes Bureau as well as the local district attorney offices deal with tax crimes. A fiduciary may find itself being contacted or investigated by both federal and state agents at the same time. All of the above discussion is applicable when dealing with state agents, the attorney general or district attorney offices or their agents.

Fiduciaries, as well as all taxpayers, should be careful in the choice and employment of tax advisors, including accountants, financial advisors, attorneys and others. Ultimately, the fiduciary is held liable under the laws discussed above.

All taxpayers and information providers (issuers of 1099s, W-2s, and other tax information statements), including fiduciaries who issue K-1s, must issue correct ones. The discussion above applies to these filings and issuance.

There are numerous other crimes that apply to fiduciaries, but those are left for a future discussion. The best advice of all is always to use caution when contacted by government agents and/or attorneys, and make sure that the advice you get from an attorney is protected under the attorney/client privilege. To put it another way: Remember the *Perry Mason* rule.

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