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Heisenberg's Uncertainty: An Analysis of Criminal Tax Pretextual Prosecutions in the Context of Breaking Bad's Notorious Anti-Hero

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HEISENBERG'S UNCERTAINTY: AN ANALYSIS OF CRIMINAL TAX PRETEXTUAL PROSECUTIONS IN THE CONTEXT OF *BREAKING BAD*'S NOTORIOUS ANTI-HERO

Scott D. Shimick*

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In Breaking Bad, AMC's "Mr. Chips to Scarface" story,¹ Walter White, who produces and sells narcotics, is the protagonist and anti-hero. Throughout the show, Walter is very careful to conceal or destroy any evidence that will link him to violence and drug

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1. Genetta M. Adams, "Breaking Bad: From Mr. Chips to Scarface in 10 Easy Steps, CNN ENT. (July 12, 2012), <http://www.cnn.com/2012/07/12/showbiz/tv/breaking-bad-chips-scarface/index.html>; Paul MacInnes, *Breaking Bad Creator Vince Gilligan: The Man Who Turned Walter White from Mr. Chips into Scarface*, THE GUARDIAN (May 19, 2012), <http://www.theguardian.com/tv-and-radio/2012/may/19/vince-gilligan-breaking-bad>.

trafficking activities. However, as the bootleggers and gangsters of the Prohibition era learned, the government holds the trump card; criminal tax prosecution. By charging drug traffickers with criminal tax fraud, the government can imprison dangerous criminals without having to prove beyond a reasonable doubt that the drug traffickers actually produced and sold narcotics. This article will examine criminal tax fraud as a pretextual prosecution tool. Under the assumption that Walter White could not have been prosecuted for drug trafficking or murder, this article will analyze whether Walter White should have fled from the potential prosecution for criminal tax fraud. This article addresses the arguments against pretextual prosecution, discusses a brief history of prosecuting notorious criminals for tax fraud, outlines the applicable felonies provided for in the Internal Revenue Code and methods of proving criminal tax fraud, and analyzes whether, at the time he decided to flee New Mexico, Walter would have been prosecuted for a potential criminal tax fraud felony. In so doing, this article demonstrates the value of pretextual criminal tax fraud prosecutions.

I. INTRODUCTION

“My name is Walter Hartwell White. I live at 308 Negra Arroyo Lane, Albuquerque, New Mexico, 87104. To all law-enforcement entities, this is not an admission of guilt.”²

Walter White takes the first steps toward a criminal enterprise while working as a high school chemistry teacher in Albuquerque, New Mexico. Walter has just been diagnosed with terminal lung cancer. His wife, Skyler, is pregnant. His son, Walt Jr., has cerebral palsy. He lives a modest existence in a suburban home. To make ends meet, Walter holds a second job as a cashier at a car wash. Walter bears the burden of his illness alone and does not share his terminal diagnosis with his family right away. He realizes, however, that he needs to provide for his family after he is gone.³

Walter’s brother-in-law, Hank Schrader, is an agent for the United States Drug Enforcement Agency (DEA). Walter goes on a ride-along with Agent Schrader to a DEA bust of a methamphetamine laboratory. At the bust, Walter sees a former student, Jesse Pinkman, climb out a window and scurry away undetected by everyone but Walter. This is the “eureka!” moment when Walter conceives the plan for providing for his family—partnering with Pinkman to cook methamphetamine hydrochloride (“crystal meth”).⁴

Walter is a trained chemist.⁵ He loves the process of “cooking” crystal meth, and he excels at the precision of the chemistry. Walter and Pinkman pair up to make an extraordinarily pure—and eventually blue—crystal meth.⁶ Throughout the course of the series, Walter “cooks” thousands of pounds of crystal meth. Partly to hide his identity, but, more importantly, to create a persona to deal with the dangers of making and selling crystal meth, Walter White takes the *nom-de-guerre* Heisenberg.⁷

2. *Breaking Bad: Pilot* (AMC television broadcast Jan. 20, 2008). These are the opening lines of AMC’s hit series *Breaking Bad*. *Id.*

3. *Id.*

4. *Id.*

5. Walter White studied at the California Institute of Technology. He is an expert in X-ray crystallography and co-founder of Gray Matter Technologies. *Breaking Bad: Gray Matter* (AMC television broadcast Feb. 24, 2008). Walter’s research led to a Nobel Prize in Chemistry, awarded to Herbert A. Hauptman and Jerome Karle, for outstanding achievements in the development of crystal structures. *Breaking Bad: Pilot*, *supra* note 2.

6. *Breaking Bad: Cancer Man* (AMC television broadcast Feb. 17, 2008).

7. *Breaking Bad: Crazy Handful of Nothin’* (AMC television broadcast Mar. 2, 2008). Heisenberg is a clear

Donning a black pork-pie hat, shaved head, and goatee, Walter White—as Heisenberg—becomes increasingly more violent. Over the course of the next year,⁸ Walter commits seven murders by his own hand,⁹ orders the murder of eleven more,¹⁰ conspires to two additional murders,¹¹ and poisons a young boy.¹² In addition to these violent acts, Walter steals large quantities of chemicals,¹³ obstructs a federal investigation,¹⁴ and wiretaps Agent Schrader's office phone.¹⁵ Despite this long list of criminal activity, Agent Schrader and the Drug Enforcement Agency do not know the identity of the mastermind behind the blue crystal meth, except that he is known as “Heisenberg”.

Through serendipity, Agent Schrader discovers that Walter is Heisenberg.¹⁶ Given the circumstances of a family member being the largest producer of crystal meth in the Southwest, Agent Schrader shares nothing with the DEA or his fellow agents. Agent Schrader remains dogged in his investigation but cannot produce evidence against Walter,

reference to Werner Heisenberg, the famed quantum physicist. Heisenberg's most important contribution to quantum physics is his Uncertainty Principle. The Uncertainty Principle states in lay terms that the more precisely an observer measures the location of something, the less the observer knows about where it is going, and the more precisely an observer measures the direction and speed of something, the less the observer knows about where it is. From this, one can extrapolate the theory to mean that the act of observing changes the thing being observed. DAVID LINDLEY, UNCERTAINTY: EINSTEIN, HEISENBERG, BOHR, AND THE STRUGGLE FOR THE SOUL OF SCIENCE 4 (2007). The Nobel physics committee awarded the 1932 Nobel Prize for Physics to Werner Heisenberg. *Id.* at 171.

8. The series begins on Walter's 50th birthday. *Breaking Bad: Pilot*, *supra* note 2. Walter's 51st birthday is a few weeks before he “retires.” *Breaking Bad: Fifty-One* (AMC television broadcast Aug. 5, 2012).

9. Walter kills Emilio Koyama by poison gas—arguably in self-defense—after a drug deal goes wrong. *Breaking Bad: Pilot*, *supra* note 2. Walter strangles Domingo “Krazy 8” Molina with a bike lock in Pinkman's basement after realizing that Molina will kill Walter if he lets Molina live. *Breaking Bad: . . . and the Bag's in the River* (AMC television broadcast, Feb. 10, 2008). Walter kills two rival drug dealers by running them over in his Pontiac Aztek and shooting the survivor in the head. *Breaking Bad: Half Measures* (AMC television broadcast June 6, 2010). Walter shoots two of Gustavo Fring's henchmen who are guarding the Superlab. *Breaking Bad: Face Off* (AMC television broadcast Oct. 9, 2011). Walter fatally shoots his co-conspirator, Mike Ehrmentraut, in the stomach. *Breaking Bad: Say My Name* (AMC television broadcast Aug. 26, 2012).

10. Walter orders Pinkman to murder Gale Boetticher, a fellow chemist, who Walter believes is being groomed by the drug kingpin Fring as his replacement. *Breaking Bad: Full Measure* (AMC television broadcast June 13, 2010). Walter orders the murders of nine of Ehrmentraut's former workers who have been taken into custody, along with their attorney. The potential witnesses murdered simultaneously in prison are Dan Wachsberger, Jack McGann, Andrew Holt, Anthony Perez, Isaac Conley, William Moniz, Harris Bolvin, Raymond Martinez, Ron Forenall, and Dennis Markowski. *Breaking Bad: Gliding over All* (AMC television broadcast Sept. 2, 2012). Note that Walter orders Pinkman to kill Fring and later orders Welker to kill Pinkman, but these orders are not followed. *Breaking Bad: To 'hajiilee* (AMC television broadcast Sept. 8, 2013).

11. Walter conspires with Hector “Tio” Salamanca to murder Fring and his henchman, Tyrus Kitt. The method of murder is a suicide bomb built by Walter and detonated by Salamanca. *Breaking Bad: Face Off*, *supra* note 9. (Although Walter protests, his co-conspirators also murder two DEA Agents, Schrader and Gomez. *Breaking Bad: Ozymandias* (AMC television broadcast Sept. 15, 2013).

12. As part of a scheme to ensure Pinkman does not conspire with Fring against him, Walter poisons the son of Pinkman's girlfriend, Brock Antillo. *Breaking Bad: End Times* (AMC television broadcast Oct. 2, 2011).

13. Walter and Pinkman steal a barrel of methylamine—a replacement for the pseudoephedrine necessary to “cook” crystal meth. *Breaking Bad: A No-Rough-Stuff-Type Deal* (AMC television broadcast Mar. 9, 2008). Walter and Pinkman, with the assistance of Ehrmentraut, Todd Alquist, and Patrick Kubly, rob a freight train tanker and steal approximately 24,000 gallons of methylamine. During the robbery, Alquist shoots and kills a young boy—Drew Sharp—who happens upon the scene. *Breaking Bad: Dead Freight* (AMC television broadcast Aug. 12, 2012).

14. Agent Schrader spends much of the series investigating the newest drug kingpin—Heisenberg—and his blue crystal meth. Of the many instances of Walter's obstruction, the most damaging to the investigation is when Walter, Pinkman, and Ehrmentraut use a giant magnet to erase the hard drives in the Albuquerque Police Department's evidence room. This erases any evidence linking Walter to the deceased Fring. *Breaking Bad: Live Free or Die* (AMC television broadcast July 15, 2012).

15. *Breaking Bad: Dead Freight*, *supra* note 13.

16. Agent Schrader discovers a gift from the murder victim Boetticher in Walter's house, connecting him to the murder and the production of the blue crystal meth. *Breaking Bad: Gliding over All*, *supra* note 10.

except the recorded confession of Walter's alienated business partner, Jesse Pinkman.¹⁷

Walter knows Agent Schrader suspects he is Heisenberg and tries to cover his tracks. Walter buries his barrels full of money in the New Mexico desert.¹⁸ The site of the buried money becomes the site of a showdown among Walter, his current co-conspirators, Pinkman, Agent Schrader, and his partner, Agent Steven Gomez. Agent Schrader arrests Walter and calls his wife to tell her he has arrested Walter as Heisenberg.¹⁹ However, before leaving the scene, Walter's current co-conspirators, Jack Welker and his white supremacist gang, shoot and kill Agents Schrader and Gomez. They bury the bodies in the desert—in the hole that had been secreting seven barrels of cash. At this point, Walter decides it is in his best interests to flee New Mexico and assume a new identity.²⁰

With little evidence of the drug trafficking, violence, and racketeering crimes, the Department of Justice would likely turn to a felony conviction under the Internal Revenue Code.

II. PRETEXTUAL PROSECUTIONS

A. *Prosecution of Walter White on Drug Trafficking and Murder Charges*

As of the time Walter White decides to flee New Mexico, prosecutors would probably not have enough evidence to prosecute Walter White for drug trafficking, murder, conspiracy, or racketeering. Marie Schrader tells the DEA of Agent Schrader's suspicions about Walter. A DEA investigation into Walter White would surely follow, especially with the disappearance of two DEA agents. However, no substantive evidence remains to present to a jury.

Walter sees to the concealment or destruction of all material evidence tying him to the production of crystal meth. The first "cook" site is a Fleetwood Bounder recreational vehicle, which Walter purchases through proceeds of his teacher's retirement account. Walter and Jesse Pinkman drive the RV to the desert to produce the crystal meth in private.²¹ However, Walter sends the RV to the scrapyard for destruction before any evidence can be gathered.²²

Walter then begins a production relationship with Gustavo Fring—a regional distributor of crystal meth and owner of several fried chicken franchises. Fring builds a "Superlab" where Walter and Pinkman produce hundreds, if not thousands, of pounds of crystal meth. Following the murder of Fring, the Superlab is compromised. So, Walter and Pinkman destroy the Superlab and all the evidence therein.²³ Within the Superlab, Fring maintains digital surveillance equipment stored to his personal computer. However, Walter destroys the digital video captured by the Superlab's security cameras, along with all other ties to Fring, by using a large magnet to erase all the hard drives in the Albuquerque Police Department's evidence room.²⁴

17. *Breaking Bad: Confessions* (AMC television broadcast Aug. 25, 2013).

18. *Breaking Bad: Buried* (AMC television broadcast Aug. 18, 2013).

19. *Breaking Bad: To 'hajiilee*, *supra* note 10.

20. *Breaking Bad: Ozymandias*, *supra* note 11.

21. *Breaking Bad: Pilot*, *supra* note 2.

22. *Breaking Bad: Sunset* (AMC television broadcast Apr. 25, 2010).

23. *Breaking Bad: Face Off*, *supra* note 9.

24. *Breaking Bad: Live Free or Die*, *supra* note 14.

Walter continues to produce crystal meth by using the cover of Vamanos Pest Control. Under the guise of whole-home fumigation, Walter “cooks” crystal meth in a mobile laboratory in residences throughout Albuquerque.²⁵ At the time Walter decides to flee, Vamanos Pest Control and the equipment are under the control of Todd Alquist, Jack Welker, and the white supremacist gang. The federal prosecutors have no way to connect Walter to the white supremacist gang, which is not under suspicion for the continuing crystal meth production. Furthermore, the white supremacist gang destroys all evidence tying Walter and the gang to crystal meth production, including stealing the recording of Pinkman’s confession and ensuring the silence of Skyler White through threats against her and her children. Although Welker does not kill Pinkman, as Walter ordered him to do, the gang imprisons Pinkman for the purpose of continuing to “cook” until the store of methylamine is depleted.²⁶

Walter kills, orders to be killed, or conspires to kill twenty people.²⁷ Only a handful of others are aware of Walter’s involvement in these crimes. Pinkman was directly involved in most of these acts. However, at the time Walter decides to flee, he presumes Pinkman is dead. Welker and Alquist are also aware of the crystal meth production and many of the murders, but are not under suspicion. The seasoned criminals are unlikely to cooperate in any investigation regarding the drug trafficking and murders. Furthermore, Alquist ensures the destruction of all links to Walter and his criminal activity.²⁸ Finally, the last person to know about any of these murders is Saul Goodman, Esq. Goodman provides criminal legal representation to Walter. Despite the fact that conversations with Goodman regarding the commission of prospective crimes would not be protected by the attorney-client privilege,²⁹ Goodman has also fled and taken a new identity.³⁰ The prosecutors have no physical evidence tying Walter to the murders and are unlikely to develop any witnesses with knowledge of the crimes. Therefore, Walter White would not be prosecuted for drug trafficking, murder, conspiracy, or racketeering.

The Department of Justice and the DEA are aware Walter White is Heisenberg, but are unable to convict him for his drug trafficking and murders. Thus, the government would likely turn to a pretextual prosecution: a prosecution of Walter White for tax crimes in place of a prosecution for the much more serious, but likely unprovable, crimes.

B. *Pretextual Criminal Tax Prosecutions*

A pretextual prosecution is a prosecution for a putatively lesser crime of a defendant who has been targeted for a more serious crime that is too difficult to prove. A pretextual prosecution is not a baseless prosecution; the accused has allegedly committed the lesser

25. *Breaking Bad: Gliding over All*, *supra* note 10.

26. *Breaking Bad: Granite State* (AMC television broadcast Sept. 22, 2013).

27. *See supra* notes 9-11 and accompanying text.

28. *Breaking Bad: Granite State*, *supra* note 26.

29. *United States v. Zolin*, 491 U.S. 554, 556 (1989).

30. *Breaking Bad: Granite State*, *supra* note 26. Note that Walter’s wife, Skyler White, has some knowledge of the violent acts and drug trafficking and has intimate knowledge of the money-laundering. The crime-fraud exception to spousal privilege would prevent Skyler White from invoking spousal privilege. *United States v. Neal*, 743 F.2d 1441, 1446 (10th Cir. 1984), *cert. denied*, 105 S. Ct. 1848 (1985). However, Skyler would be unlikely to testify because of her fear of Walter and Alquist’s white supremacist gang. *Breaking Bad: Granite State*, *supra* note 26. Skyler also becomes integral to the criminal enterprise and demonstrates her support for Walter. *Breaking Bad: Buried*, *supra* note 18. Walter is aware that Skyler is unlikely to testify against him in any criminal proceeding.

crime.³¹ Commentators, and defendants, have roundly criticized the use of pretextual prosecutions.³²

Defendants argue that a pretextual prosecution is an arbitrary prosecution, targeting a specific person and treating that person differently than similarly situated individuals.³³ One commentator even labels pretextual prosecutions as “sideshow[s]” and “end-run around[s].”³⁴ Another commentator argues that Prohibition failed because of the inconsistent application of the laws through, in part, pretextual prosecutions. Using this same logic, pretextual prosecutions could lead to a failure in the War on Drugs.³⁵ One commentator notes that state budget crises have led to increased prosecutions and fines, expressing concern that pretextual prosecutions could be used to generate funds for the state’s coffers.³⁶

Many commentators have raised legitimate concerns about the use of pretextual prosecutions. In arguing that the government should minimize the use of pretextual prosecutions, one commentator posits that reducing pretextual prosecutions will increase transparency and governmental accountability.³⁷ Another commentator argues that pretextual prosecutions, generally the realm of federal prosecutions and crimes, increase federalism and reduce state legitimacy.³⁸

In noting the potential for abuse, one commentator condemns pretextual prosecutions against suspected terrorists as an avenue of stifling dissent.³⁹ Just as federal prosecutors have used tax crimes to imprison bootleggers, the government has used the federal material witness statute to detain suspected terrorists.⁴⁰ These detentions without prosecution under the pretext of being material witnesses raise concerns about abuses under the Fourth Amendment with respect to suspected terrorists.⁴¹ Whether using the material witness statute, money-laundering, or criminal tax fraud, federal prosecutors may become heavy-handed in the use of pretextual prosecutions given the heightened concerns over terrorism.⁴²

Commentators have even argued against pretextual prosecutions from both sides of

31. See Erin Murphy, *Manufacturing Crime: Process, Pretext, and Criminal Justice*, 97 GEO. L.J. 1435, 1442-43 (2009).

32. See, e.g., Sahar F. Aziz, *Policing Terrorists in the Community*, 5 HARV. NAT’L SECURITY J. 147 (2014); Beau D. Barnes, Note, *Confronting the One-Man Wolf Pack: Adapting Law Enforcement and Prosecution Responses to the Threat of Lone Wolf Terrorism*, 92 B.U. L. REV. 1613 (2012); Hallie T. Damon, Note, *A Reasonable Detention? Rethinking the Material Witness Statute’s Probable Cause Standard After al-Kid*, 44 COLUM. HUM. RTS. L. REV. 537 (2013); Murphy, *supra* note 31; Daniel C. Richman & William J. Stuntz, *Al Capone’s Revenge: An Essay on the Political Economy of Pretextual Prosecution*, 105 COLUM. L. REV. 583 (2005). But see Harry Litman, *Pretextual Prosecution*, 92 GEO. L.J. 1135 (2004).

33. See Richman & Stuntz, *supra* note 32, at 584 (citing, as an example, *Wayte v. United States*, 470 U.S. 598 (1985)).

34. Dale A. Oesterle, *Early Observations on the Prosecutions of the Business Scandals of 2002-03: On Sideshow Prosecutions, Spitzer’s Clash with Donaldson over Turf, the Choice of Civil or Criminal Actions, and the Tough Tactic of Coerced Cooperation*, 1 OHIO ST. J. CRIM. L. 443, 456 (2004).

35. Hadar Aviram & Daniel L. Portman, *Inequitable Enforcement: Introducing the Concept of Equity into Constitutional Review of Law Enforcement*, 61 HASTINGS L.J. 413, 429-30 (2009).

36. Murphy, *supra* note 31, at 1502.

37. See Richman & Stuntz, *supra* note 32, at 583.

38. Murphy, *supra* note 31, at 1500-02; Richman & Stuntz, *supra* note 32, at 599-600.

39. Aziz, *supra* note 32, at 161-62.

40. See, e.g., *Ashcroft v. al-Kidd*, 131 S. Ct. 2074 (2011).

41. See Damon, *supra* note 32, at 552-53.

42. Richman & Stuntz, *supra* note 32, at 623-24.

an issue. Because the federal prosecutors are not answerable to the public in the way that local law enforcement may be, federal prosecutors are at greater risk to abuse the use of pretextual prosecutions.⁴³ Another commentator has argued that local law enforcement is prone to greater abuse because, while local authorities have apparent accountability to the public, they are not subject to the restrictions of reasonable application that are inherent in the federal system.⁴⁴

Another argument is that pretextual prosecutions and prosecutions for criminal process can create a cycle of self-aggrandizement and self-promotion, spiraling to dangerous proportions.⁴⁵ Also, pretextual prosecutions reduce the credibility of the justice system.⁴⁶ The basis for this argument is that criminal charges are both a means of identifying and punishing criminal conduct and a means for prosecutors to send a signal to the public and other criminals. By pursuing pretextual prosecutions, the government sends mixed signals that can erode trust in the criminal justice system.⁴⁷

Despite these concerns, the Department of Justice has a history of success in pretextual prosecutions, prosecuting notorious criminals for tax crimes. After ratification of the 16th Amendment, Congress defined income as “gains, profits, and income derived from . . . the transaction of any *lawful* business carried on for gain or profit, or . . . income derived from any source whatever.”⁴⁸ By 1916, the definition of income changed but only by omitting the word “lawful.”⁴⁹ This one word forever changed the landscape of federal prosecutions. In *United States v. Sullivan*, Justice Holmes delivered an opinion that created the basis for pretextual prosecutions.⁵⁰ The Supreme Court held that income from illegal sources is subject to the internal revenue laws and that reporting illegal income is not a violation of the right against self-incrimination.⁵¹ Using this as a starting point, the government began prosecuting bootleggers and gangsters for tax evasion.⁵² The seminal case for pretextual tax prosecution is the prosecution of Al Capone.

Alphonse Capone, Public Enemy No. 1, was known for bootlegging, racketeering, and murder.⁵³ Halting Capone's criminal enterprise was not only a concern for local authorities, the Treasury Department, and the Federal Bureau of Investigation, but was daily on the mind of the President of the United States.⁵⁴ However, Capone was careful to not leave any connections to his primary criminal activity.

43. *Id.* at 615-17.

44. Murphy, *supra* note 31, at 1498-1500.

45. *Id.* at 1506.

46. Richman & Stuntz, *supra* note 32, at 624. After Al Capone's conviction, the public attitude toward Capone changed from disdain to sympathy. While the public had no taste for a cold-blooded murderer, most could relate to an individual cheating on his taxes. The public confidence in the judicial system did wane in the aftermath of the Capone conviction. Many thought that Capone should have been prosecuted for the serious crimes he committed, rather than relying on the “technicality” of tax evasion. JOHNATHAN EIG, GET CAPONE: THE SECRET PLOT THAT CAPTURED AMERICA'S MOST WANTED GANGSTER 369-70 (2010).

47. Richman & Stuntz, *supra* note 32, at 585-87.

48. Income Tax Law of 1913, Pub. L. No. 16, ch. 16, 38 Stat. 114, 167 (1913) (emphasis added).

49. The Revenue Act of 1921, Pub. L. No. 67-98, ch. 136, 42 Stat. 238 (1921).

50. *United States v. Sullivan*, 274 U.S. 259 (1927).

51. *Id.* at 263-64.

52. LUCIANO IORIZZO, AL CAPONE: A BIOGRAPHY 74 (2003). Among the first gangsters to serve time for tax evasion included Ralph Capone, Terry Druggan, Frankie Lake, Jack Guzik, and Frank Nitti. *Id.*

53. Richman & Stuntz, *supra* note 32, at 583; JOHN KOBLE, CAPONE: THE LIFE AND WORLD OF AL CAPONE 14, 285-305 (2003).

54. EIG, *supra* note 46, at 219; IORIZZO, *supra* note 52, at 75-76.

Capone never owned property, never endorsed checks, never signed receipts, and never kept a bank account.⁵⁵ Without this type of tangible evidence, the government set about investigating a case based on Capone's net worth and net expenditures, thereby deriving proof of income. Although the government suspected income of up to \$100 million, the investigators felt certain that they would be able to prove income of approximately \$165,000 for years 1926 to 1929.⁵⁶ Capone's own attorney, Lawrence P. Mattingly, Esq., met with the investigators and produced his own statement of Capone's approximate income of \$266,000 under the guise of settling the tax debt.⁵⁷ However, this miscalculation by Mattingly led to the final evidence against Capone and the United States Attorney secured indictments on twenty-two felony counts of income tax evasion and two misdemeanor counts of failure to file returns.⁵⁸ At trial, the government produced a stream of witnesses that testified to expenditures made by Capone, proving its allegations of unreported income through Capone's own expenditures.⁵⁹ After eight hours of deliberation, the jury returned guilty verdicts on three felony counts of evasion and two misdemeanor counts for failure to file. The judge sentenced Capone to eleven years in prison, and the government had finally prevailed.⁶⁰

The government used this effective new tool to convict other bootleggers and gangsters. Anthony Accardo was a reputed Chicago gangster and Capone hitman.⁶¹ He was allegedly the leader of a multi-million dollar crime syndicate. Accardo was the frequent target of murder investigations over a 30-year period and remains a suspect in the notorious 1929 St. Valentine's Day Massacre. In 1960, Accardo was convicted of income tax evasion. He made the fatal error of falsely deducting his red sports car as a business expense.⁶²

Meyer Harris "Mickey" Cohen was a Prohibition-era gangster and "notorious law-violator."⁶³ The government secured conviction against Cohen on eight felony counts, but none for violent crimes or racketeering. The convictions were for willful filing of a false and fraudulent return, willfully attempting to defeat and evade payment of tax, concealment of property on which levy is authorized, and making a false statement to the Internal Revenue Service.⁶⁴ Cohen was sentenced to fifteen years for these tax crimes.⁶⁵

Meyer Lansky is another notorious Prohibition-era gangster who evaded prosecution for his crimes.⁶⁶ Lansky was not the violent thug personified by Capone; he was the brains of the organized crime operation.⁶⁷ Well-known for his statement that organized crime is

55. IORIZZO, *supra* note 52, at 74.

56. *Id.* at 76.

57. *Id.* at 76-77.

58. *Id.* at 77.

59. *Id.* at 81.

60. *Capone v. United States*, 56 F.2d 927 (7th Cir.), *cert. denied*, 286 U.S. 553 (1932); IORIZZO, *supra* note 52, at 83.

61. IORIZZO, *supra* note 52, at 42.

62. *Gangster is Convicted of Tax Evasion*, GETTYSBURG TIMES, Nov. 12, 1960, at 3.

63. *Cohen v. United States*, 82 S. Ct. 8, 9 (1961).

64. *Cohen v. United States*, 297 F.2d 760, 762 (9th Cir.), *cert. denied*, 369 U.S. 865 (1962).

65. *Id.* at 762. See also Sam Nunn, *The Impact of the Senate Permanent Subcommittee on Investigations on Federal Policy*, 21 GA. L. REV. 17, 31-32 (1986) (discussing the impact of Attorney General Kennedy's successful use of pretextual prosecutions against notorious gangsters).

66. ROBERT LACEY, *LITTLE MAN: MEYER LANSKY AND THE GANGSTER LIFE* 50 (1991).

67. *Id.* at 6.

bigger than U.S. Steel, Lansky took lessons from the conviction of Capone and reported enough income to demonstrate his lifestyle.⁶⁸ However, the \$40,000 per year of income Lansky reported was not nearly enough to account for the hundreds of millions of dollars he was reputed to control.⁶⁹ As the government closed in on an indictment, Lansky fled to Israel to avoid prosecution for tax evasion.⁷⁰

In addition to prosecuting bootleggers and gangsters, the Department of Justice has used the tax laws to convict suspected terrorists and financiers of terrorism. The government prosecuted Muhamed Mubayyid for conspiracy to defraud the United States, making false statements to a federal agent, and making false statements on tax returns. In support of terrorist activities, Mubayyid was soliciting funds through—and distributing funds from—a tax-exempt organization: Care International, Inc.⁷¹ The pretextual prosecution for these tax crimes closed a pipeline supporting terrorist activities.

The government continues to use tax crimes to prosecute suspected gangsters. In a recent case of pretextual prosecution, Vincent Faraci pled guilty to tax evasion. Vincent “Vinny Green” Faraci is a reputed Bonanno crime family soldier and one of the last known mobsters to be working in Las Vegas.⁷² Faraci pled guilty to failing to report approximately \$134,000 of income and received a sentence of fifteen months in prison.⁷³ The Organized Crime Task Force, not the Internal Revenue Service, led the investigation that resulted in Faraci’s plea.⁷⁴

The prosecution of Al Capone, as with the prosecutions of these other notorious criminals, was a pretextual prosecution because the federal government did not charge Capone for tax evasion with the purpose of achieving his ongoing compliance with the Internal Revenue Code. The government prosecuted Capone because he was a murderer, bootlegger, and racketeer.⁷⁵ Likewise, the government would not seek to charge Walter White with tax evasion to ensure his future compliance, but because it has no other recourse to prosecute the known drug kingpin.

III. TAX CRIMES

The Internal Revenue Code provides for two types of felonies that could apply to Walter White’s criminal enterprise: attempting to evade or defeat tax⁷⁶ and engaging in

68. *Id.* at 284, 286.

69. *Id.* at 312.

70. *Id.* at 323.

71. The defendants were convicted of all charges. *United States v. Mubayyid*, 567 F. Supp. 2d 223, 225-26 (D. Mass. 2008), *aff’d in part and rev’d in part*, 658 F.3d 35 (1st Cir. 2011). However, the trial judge entered an acquittal on the conspiracy charges. *Mubayyid*, 567 F. Supp. 2d at 251. This acquittal was overturned and the jury verdict reinstated. *Mubayyid*, 658 F.3d at 74.

72. Nathan Baca, *I-Team: Accused Mobster Pleads Guilty to Tax Evasion*, KLAS-TV (July 17, 2013), <http://www.8newsnow.com/story/22867315/i-team-accused-mobster-pleads-guilty-of-tax-evasion>; *see also* Mitchel Maddux, *Alliance Between Mafia, Bikers and Cartel Fueled NYC’s Marijuana Trade: DEA Probe*, N.Y. POST (Jan. 14, 2013), <http://nypost.com/2013/01/14/alliance-between-mafia-bikers-and-cartel-fueled-nycs-marijuana-trade-dea-probe/>.

73. Jeff German, *Former Strip Club Manager Sentenced to Federal Prison on Tax Conviction*, LAS VEGAS REV.-J. (Dec. 16, 2013), <http://www.reviewjournal.com/news/former-strip-club-manager-sentenced-federal-prison-tax-conviction>.

74. Baca, *supra* note 72.

75. *See* Murphy, *supra* note 31, at 1442-43.

76. I.R.C. § 7201 (West 2013).

fraud and making false statements.⁷⁷

A. *Section 7201 – Attempt to Evade or Defeat Tax*

Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title 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 not more than \$100,000 (\$500,000 in the case of a corporation), or imprisoned not more than 5 years, or both, together with the costs of prosecution.⁷⁸

An attempt to evade or defeat a tax can be either the willful attempt to evade the assessment of a tax or the willful attempt to evade the payment of a tax.⁷⁹ Evasion includes an attempt to prevent the determination of the true tax liability.⁸⁰ An attempt to evade the payment of the proper tax liability by hiding assets is an attempt to evade the payment of a tax.⁸¹ The real character of evasion lies in the attempt to defraud the government by evading the tax, not in the success of the fraud.⁸² In prosecuting a taxpayer for attempting to evade or defeat a tax, the government must prove willfulness, the existence of a tax deficiency, and an affirmative act that constitutes an evasion or attempted evasion of the tax.⁸³

Willfulness requires proof that the law imposed a duty on the taxpayer, that the taxpayer knew of this duty, and that the taxpayer voluntarily and intentionally violated such duty.⁸⁴ The government need not prove any other motive than this standard as set forth by

77. I.R.C. § 7206 (West 2013). The analysis in this article is limited to discussion of these two felonies. In addition to these Title 26 crimes, Title 18 provides additional potentially applicable criminal prohibitions, which include: 18 U.S.C. § 2 (West 2013) (aiding and abetting); 18 U.S.C. § 371 (West 2013) (conspiracy); 18 U.S.C. § 1001 (West 2013) (making a false statement to a government official); and 18 U.S.C. § 1956(a)(1)(A) (West 2013) (tax money laundering). Even convictions for misdemeanor criminal tax conduct, such as failure to file under Section 7203, can lead to several years' imprisonment when the taxpayer receives consecutive sentences. *See, e.g.*, *United States v. Snipes*, 2008 WL 6124556 (M.D. Fla. May 1, 2008) (sentencing the movie actor Wesley Snipes to three consecutive one-year terms of imprisonment for conviction of failure to file), *aff'd*, 611 F.3d 855 (11th Cir.), *reh'g and reh'g en banc denied*, 409 Fed. Appx. 314 (11th Cir. 2010), *cert. denied*, 131 S. Ct. 2962 (2011).

78. I.R.C. § 7201 (West 2013).

79. *United States v. Mal*, 942 F.2d 682, 686-88 (9th Cir. 1991). Some taxpayers, citing *Sansone v. United States*, 380 U.S. 343, 354 (1965), have argued that these are two distinct elements of one crime, *e.g.*, *United States v. Hogan*, 861 F.2d 312, 315 (1st Cir. 1988). However, courts have consistently held that the statute provides for two distinct crimes, either one alone amounting to tax evasion under I.R.C. § 7201. *See United States v. Huguenin*, 950 F.2d 23, 26 (1st Cir. 1991); *Hogan*, 861 F.2d at 315; *United States v. Masat*, 896 F.2d 88, 91 (5th Cir. 1990), *appeal after remand*, 948 F.2d 923 (5th Cir. 1991); *Mal*, 942 F.2d at 686; *United States v. Dunkel*, 900 F.2d 105, 107 (7th Cir. 1990). An attempt to evade tax materially differs from the common law crime of attempt, which is generally considered a lesser offense. At common law, attempt involves conduct designed to result in the commission of the completed offense. Whereas, a willful attempt to evade tax constitutes the complete and independent crime in its most serious form once the attempt itself is complete. *Spies v. United States*, 317 U.S. 492, 498-99 (1943).

80. *Mal*, 942 F.2d at 687.

81. *Hogan*, 861 F.2d at 315.

82. *Garipey v. United States*, 220 F.2d 252, 259 (6th Cir.), *cert. denied*, 350 U.S. 825 (1955) (quoting *Emmich v. United States*, 298 F. 5, 9 (6th Cir.), *cert. denied*, 266 U.S. 608 (1924)).

83. *Sansone*, 380 U.S. at 351; *United States v. Thompson*, 518 F.3d 832, 850 (10th Cir. 2008).

84. *Cheek v. United States*, 498 U.S. 192, 201 (1991); *United States v. Pomponio*, 429 U.S. 10, 12 (1976). The standard of willfulness has not always been so clear. Prior Supreme Court opinions interpreted the standard of willfulness with respect to tax crimes by suggesting that motive is an element of willfulness. *Spies v. United States*, 317 U.S. 492, 498 (1943) (requiring that "evil motive and want of justification in view of all the financial

the Supreme Court in *Cheek v. United States*.⁸⁵ Once the government establishes that a tax evasion motive played any role in the conduct of the taxpayer, a jury can infer willfulness from the taxpayer's conduct, even if the conduct served a purpose other than willful evasion of tax.⁸⁶ However, the government cannot provide expert witness testimony regarding the willfulness of the taxpayer.⁸⁷

A taxpayer's good faith misunderstanding of the law or good faith belief that the taxpayer is not violating the law negates willfulness. This good faith exception applies whether or not the belief or misunderstanding asserted by the taxpayer is objectively reasonable.⁸⁸ Willful blindness of the requirements of the law is not a good faith misunderstanding of the law. Deliberate ignorance and positive knowledge are equally culpable.⁸⁹

A trier of fact can infer willfulness from actions such as keeping double sets of books, making false entries or alterations in books, making false invoices or documents, destroying books or records, concealing assets or covering up sources of income, handling affairs so as to avoid recording transactions in the usual manner, and engaging in any conduct having the likely effect of misleading or concealing income.⁹⁰ Additionally, a jury can infer willfulness from the taxpayer's consistently underreporting large amounts of income,⁹¹ providing the return preparer with inaccurate and incomplete information,⁹² making false statements or presenting false documents to an Agent,⁹³ making false documents, entries, and invoices,⁹⁴ spending large amounts of cash that cannot be reconciled with reported income,⁹⁵ having a profoundly unfavorable view of the taxing authority,⁹⁶ and having illegal sources of income.⁹⁷

The second element in proving tax evasion is a tax deficiency. Because the purpose of Section 7201 is criminal prosecution and not tax collection, the government need not prove a precise amount of tax evaded by the taxpayer.⁹⁸

circumstances of the taxpayer" be present for a finding of willfulness); *United States v. Murdock*, 290 U.S. 389, 398 (1933) (requiring "bad faith or evil intent" be present for a finding of willfulness).

85. *Cheek*, 498 U.S. at 192. See *United States v. Jerde*, 841 F.2d 818, 821 (8th Cir. 1988) (citing *Pomponio*, 429 U.S. at 12).

86. *United States v. Guidry*, 199 F.3d 1150, 1157 (10th Cir. 1999).

87. *United States v. Windfelder*, 790 F.2d 576, 580-81 (7th Cir. 1986).

88. *Cheek*, 498 U.S. at 203.

89. *United States v. Jewell*, 532 F.2d 697, 700 (9th Cir.) (en banc), *cert. denied*, 426 U.S. 951 (1976). Disallowing willful blindness as a defense is not contradictory to *Cheek* because an intentional avoidance of the law is contrary to a good faith exercise of reasonable care. *United States v. Stadtmayer*, 620 F.3d 238 (3d Cir. 2010). To prove the good faith exception, a taxpayer does not need to testify at trial and waive his privilege against self-incrimination. Although a taxpayer's own testimony may be the best evidence of good faith, the taxpayer can offer evidence of good faith through circumstantial evidence and hearsay statements. *United States v. Kokenis*, 662 F.3d 919, 929 (7th Cir. 2011), *cert. denied*, 132 S. Ct. 2713 (2012).

90. *Spies v. United States*, 317 U.S. 492, 499 (1943).

91. *United States v. Bishop*, 264 F.3d 535, 550 (5th Cir. 2001).

92. *Id.* at 552; *United States v. Samara*, 643 F.2d 701, 703 (10th Cir. 1981); see also *United States v. Chesson*, 933 F.2d 298, 305 (5th Cir. 1991).

93. *Chesson*, 933 F.2d at 304; *United States v. Thompson*, 518 F.3d 832, 852-53 (10th Cir. 2008).

94. *United States v. Wilson*, 118 F.3d 228, 236 (4th Cir. 1997); *United States v. Walker*, 896 F.2d 295, 298 (8th Cir. 1990).

95. *United States v. Simonelli*, 237 F.3d 19, 30 (1st Cir. 2001); *United States v. Olbres*, 61 F.3d 967, 971 (1st Cir. 1995).

96. *United States v. Stein*, 437 F.2d 775, 777, 780 (7th Cir. 1971).

97. *United States v. Palmer*, 809 F.2d 1504, 1505-06 (11th Cir. 1987).

98. *United States v. Johnson*, 319 U.S. 503, 517 (1943). Requiring proof of the exact amount of tax due would reward the skillful concealment of income. *Id.* at 517-18. The amount of evaded tax proven by the government

A deficiency is the amount by which the tax imposed by statute exceeds the sum of the tax due shown on the return and the amount of any previously assessed deficiency, minus any rebate previously received.⁹⁹ This element does not require the government to charge or prove the exact amount of the tax that is due and owing.¹⁰⁰ An assessment is *prima facie* evidence of an asserted tax due, which, if unchallenged, may suffice to prove the tax due and owing.¹⁰¹ However, an assessment is not necessary to prove evasion of payment. The tax obligation arises by operation of law, and the government need not assess the taxpayer and provide notice of the deficiency for this element to be met.¹⁰² Correction of the tax due and owing does not defeat the existence of a tax deficiency when the offense was committed and is not a defense.¹⁰³

The Supreme Court has noted that circuits are split on whether the tax liability must be a substantial unpaid tax liability,¹⁰⁴ but it failed to address the issue of substantiality in its opinion.¹⁰⁵ Assuming a substantiality requirement, courts have not agreed on a formula to calculate substantiality, settling on a facts and circumstances test.¹⁰⁶ Any amount a taxpayer attempts to evade or defeat is a substantial amount if such amount exceeds an amount that would be deemed relatively small under the circumstances.¹⁰⁷

The third element of tax evasion is an affirmative act that constitutes an evasion or attempted evasion of the tax. The affirmative act of evasion can be an attempt to evade tax “in any manner.”¹⁰⁸ Although an omission cannot be an affirmative act,¹⁰⁹ virtually any conduct that is likely to mislead or conceal constitutes an affirmative attempt to evade tax.¹¹⁰ Even if an act is legal on its own, such an act can be an affirmative act to evade tax.¹¹¹ The government needs to prove only one such affirmative act, even if it has alleged multiple affirmative acts of evasion in the indictment.¹¹²

may be more or less than the amount alleged in the indictment unless the variance is material and unfairly prejudicial to the taxpayer. *United States v. Costello*, 221 F.2d 668, 675 (2d Cir. 1955), *aff'd*, 350 U.S. 359 (1956). Furthermore, the tax deficiency need not be for taxes due and owing by the taxpayer charged with evasion, but taxes due and owing by another taxpayer. *See Wilson*, 118 F.3d at 231, 236; *United States v. Townsend*, 31 F.3d 262, 264, 266-67 (5th Cir. 1994).

99. I.R.C. § 6211; *United States v. Bishop*, 264 F.3d 535 (5th Cir. 2001).

100. *Bishop*, 264 F.3d at 550-52; *United States v. Harrold*, 796 F.2d 1275, 1278 (10th Cir. 1986).

101. *United States v. Silkman*, 220 F.3d 935, 937 (8th Cir. 2000); *United States v. Voorhies*, 658 F.2d 710, 715 (9th Cir. 1981).

102. *Voorhies*, 658 F.2d at 714-15.

103. *United States v. Jewell*, 614 F.3d 911, 923-24 (8th Cir. 2010).

104. *Boulware v. United States*, 552 U.S. 421, 424 n.2 (2008) (citing *United States v. Daniels*, 387 F.3d 636, 640-41 & n.2 (7th Cir. 2004)). The Sixth Circuit Court of Appeals noted that nothing in the statute requires proof of a “substantial” tax due and owing. However, it held that the “substantial” requirement is properly applied in prosecutions relying on the net worth of proof because of the inherent imprecision in the net worth method. *United States v. Heath*, 525 F.3d 451, 456-57 (6th Cir. 2008).

105. *Boulware*, 552 U.S. at 424.

106. *Canaday v. United States*, 354 F.2d 849, 851-52 (8th Cir. 1966). Substantiality is a question of fact for the jury. *United States v. Cunningham*, 723 F.2d 217, 230-31 (2d Cir. 1983), *cert. denied*, 466 U.S. 951 (1984).

107. *See United States v. Siragusa*, 450 F.2d 592, 594-96 (2d Cir. 1971), *cert. denied*, 405 U.S. 974 (1972); *United States v. Gross*, 286 F.2d 59, 61 (2d Cir.), *cert. denied*, 366 U.S. 935 (1961); *Marks v. United States*, 391 F.2d 210, 211-12 (9th Cir.), *cert. denied*, 393 U.S. 839 (1968).

108. I.R.C. § 7201; *Imholte v. United States*, 226 F.2d 585, 588 (8th Cir. 1955).

109. *United States v. Meek*, 998 F.2d 776, 779 (10th Cir. 1993); *See United States v. Hoskins*, 654 F.3d 1086, 1091 (10th Cir. 2011).

110. *Spies v. United States*, 317 U.S. 492, 499 (1943).

111. *See United States v. Voigt*, 89 F.3d 1050, 1090 (3d Cir. 1996); *See, e.g., United States v. Jungles*, 903 F.2d 468, 474 (7th Cir. 1990); *United States v. Conley*, 826 F.2d 551, 556-57 (7th Cir. 1987).

112. *United States v. Mackey*, 571 F.2d 376, 387 (7th Cir. 1978); *United States v. Conley*, 826 F.2d 551, 558-

The taxpayer must commit the affirmative act with the intent to evade tax. The government must prove that the taxpayer committed an affirmative act with the specific intent to evade tax. Mere nonpayment or understatement of taxes is insufficient to establish intent.¹¹³

Examples of an affirmative act to evade tax include keeping a double set of books,¹¹⁴ making a false entry, altering an entry,¹¹⁵ making a false invoice or document,¹¹⁶ destroying a book or record,¹¹⁷ concealing an asset or covering up a source of income,¹¹⁸ handling affairs so as to avoid recording a transaction in the usual manner,¹¹⁹ and engaging in any conduct having the likely effect of misleading or concealing income.¹²⁰

False statements to Internal Revenue Service agents frequently amount to affirmative acts of evasion.¹²¹ Even a false statement, to the effect that no tax is due on an application for an extension to file a tax return is sufficient to meet the affirmative act requirement.¹²² Likewise, a false Form W-4, claiming a false number of exemptions for withholding purposes, is an affirmative act of evasion.¹²³

B. Section 7206 – Fraud and False Statements

Any person who—

(1) Declaration under penalties of perjury.—Willfully makes and subscribes any return, statement, or other document, which contains or is verified by a written declaration that it is made under the penalties of perjury, and which he does not believe to be true and correct as to every material matter;

...

shall be guilty of a felony and, upon conviction thereof, shall be fined not more than \$100,000 (\$500,000 in the case of a corporation), or imprisoned not more than 3 years, or both, together with the costs of

59 (7th Cir. 1987).

113. See *United States v. Slutsky*, 487 F.2d 832, 844 (2d Cir. 1973); *United States v. Coblenz*, 453 F.2d 503, 505 (2d Cir. 1972).

114. *United States v. Daniels*, 617 F.2d 146, 148-50 (5th Cir. 1980); *Shinyu Noro v. United States* 148 F.2d 696, 699 (5th Cir.), *cert. denied*, 326 U.S. 720 (1945).

115. *Spinney v. United States*, 385 F.2d 908, 911 (1st Cir. 1967), *cert. denied*, 390 U.S. 921 (1968); *United States v. Stone*, 431 F.2d 1286, 1288 (5th Cir. 1970), *cert. denied*, 401 U.S. 912 (1971).

116. *United States v. Walker*, 896 F.2d 295, 298 (8th Cir. 1990); *United States v. Lewis*, 235 F.3d 215, 216 (4th Cir. 2000).

117. *Stone*, 431 F.2d at 1288; *United States v. Garavaglia*, 566 F.2d 1056, 1059 (6th Cir. 1977).

118. *Burke v. United States*, 293 F.2d 398, 399 (1st Cir.), *cert. denied*, 368 U.S. 930 (1961).

119. *Garipey v. United States*, 220 F.2d 252, 256-59 (6th Cir. 1955).

120. *Spies v. United States*, 317 U.S. 492, 499 (1943).

121. See, e.g., *United States v. Higgins*, 2 F.3d 1094, 1097 (10th Cir. 1993); *United States v. Frederickson*, 846 F.2d 517, 520-21 (8th Cir. 1988); *United States v. Ferris*, 807 F.2d 269, 270-71 (1st Cir. 1986); *United States v. Neel*, 547 F.2d 95, 96 (9th Cir. 1976); *United States v. Calles*, 482 F.2d 1155, 1160 (5th Cir. 1973).

122. *United States v. Klausner*, 80 F.3d 55, 62 (2d Cir. 1996).

123. *United States v. DiPetto*, 936 F.2d 96, 97 (2d Cir. 1991); *United States v. Williams*, 928 F.2d 145, 148-49 (5th Cir. 1991); *United States v. Waldeck*, 909 F.2d 555, 560 (1st Cir. 1990); *United States v. Connor*, 898 F.2d 942, 944-45 (3d Cir. 1990); *United States v. King*, 126 F.3d 987, 990 (7th Cir. 1997). For example, a false Form W-4 filed before the years at issue may constitute an affirmative act in each year that the taxpayer maintains the false W-4 because the taxpayer is under a continuing obligation to correct intentional misrepresentations. See, e.g., *Williams*, 928 F.2d at 149 (ruling that false Form W-4, claiming 50 exemptions, filed in a year prior to the prosecution was an affirmative act for the years of the indictment).

prosecution.¹²⁴

Willfully making and subscribing a false document, if the document was signed under penalties of perjury, is a felony.¹²⁵ The primary purpose of this crime is to impose the penalties of perjury upon taxpayers who willfully falsify tax returns, regardless of the tax consequences.¹²⁶ The elements for willfully making and subscribing a false document are: making and subscribing a return, statement, or other document that is false as to a material matter; such return, statement, or other document contains a written declaration that it is made under the penalties of perjury; the taxpayer did not believe the return, statement, or other document to be true and correct as to every material matter when it was subscribed; and the taxpayer falsely subscribes to the return, statement, or other document willfully, with the specific intent to violate the law.¹²⁷

Section 7206(1) applies to any filed personal tax returns, as well as to amended returns,¹²⁸ schedules attached to the return, and any other attachments that relate to the determination or collection of tax.¹²⁹ Statements submitted for purposes of financial disclosures and Offers in Compromise are also documents subject to Section 7206(1).¹³⁰

“Making” a return, statement, or other document is the preparing and filing of the return, statement, or other document.¹³¹ The statute does not require that the taxpayer physically prepare the return, statement, or document. If an accountant prepared the return on the basis of information provided by the taxpayer, who later signed and filed the return or document, then the taxpayer has “made” the return.¹³² The plain language of Section 7206(1) does not require that the return, statement, or document be filed. However, courts have held that a completed Form 1040 does not become a return, and a taxpayer does not “make” a return, until the form is filed with the Internal Revenue Service.¹³³

124. I.R.C. § 7206.

125. I.R.C. § 7206(1). Willfulness has the same meaning for all crimes under the Internal Revenue Code for which willfulness is an element. *United States v. Pomponio*, 429 U.S. 10, 12 (1976). *See supra* notes 84-97 and accompanying text.

126. *United States v. Romanow*, 509 F.2d 26, 28 (1st Cir. 1975) (quoting *Gaunt v. United States*, 184 F.2d 284, 288 (1st Cir. 1950)).

127. *United States v. Bishop*, 412 U.S. 346, 350 (1973); *United States v. Hills*, 618 F.3d 619, 634 (7th Cir. 2010); *United States v. Griffin*, 524 F.3d 71, 75-76 (1st Cir. 2008); *United States v. Clayton*, 506 F.3d 405, 410, 413 (5th Cir. 2007) (per curiam); *United States v. Pirro*, 212 F.3d 86, 89 (2d Cir. 2000); *United States v. Owen*, 15 F.3d 1528, 1532 (10th Cir. 1994).

128. *See Clayton*, 506 F.3d at 412-13. The amendment of a false return does not allow for the sole basis of an inference of willfulness. *United States v. Dyer*, 922 F.2d 105, 108 (2d Cir. 1990). The filing of an amended return with correct information does not negate the prior false statement. *United States v. Tishberg*, 854 F.2d 1070, 1073 (7th Cir. 1988).

129. *See, e.g., United States v. Taylor*, 574 F.2d 232, 237 (5th Cir.), *cert. denied*, 439 U.S. 893 (1978) (holding that I.R.C. § 7206(1) applies to Schedule E and Schedule F of Form 1040); *United States v. Edwards*, 777 F.2d 644, 652 (11th Cir. 1985), *cert. denied*, 475 U.S. 1123 (1986) (holding that I.R.C. § 7206(1) applies to Schedule C of Form 1040); *United States v. Gurtunca*, 638 F. Supp. 296 (E.D. Wis. 1986), *aff'd*, 836 F.2d 283 (7th Cir. 1987) (holding that I.R.C. § 7206(1) applies to Schedule C of Form 1040); *United States v. Mauser*, 723 F. Supp. 995, 999 n.8 (S.D.N.Y. 1989) (holding that I.R.C. § 7206(1) applies to attachment to return of appraisal of donated real estate); *United States v. Sun Myung Moon*, 532 F. Supp. 1360, 1365-66 (S.D.N.Y. 1982) (holding that I.R.C. § 7206(1) applies to explanatory note attached to Form 1040 that contained false information).

130. *United States v. Hunerlach*, 197 F.3d 1059, 1068-69 (11th Cir. 1999), *appeal after remand*, 258 F.3d 1282 (11th Cir. 2001); *United States v. Cohen*, 544 F.2d 781 (5th Cir.), *cert. denied*, 431 U.S. 914 (1977).

131. *United States v. Gilkey*, 362 F. Supp. 1069, 1071 (E.D. Pa. 1973).

132. *United States v. Badwan*, 624 F.2d 1228, 1232 (4th Cir. 1980), *cert. denied*, 449 U.S. 1124 (1981).

133. *United States v. Harvey*, 869 F.2d 1439, 1448 (11th Cir. 1989) (en banc); *United States v. Dahlstrom*, 713 F.2d 1423, 1429 (9th Cir. 1983), *cert. denied*, 466 U.S. 980 (1984); *Gilkey*, 362 F. Supp. at 1071. The

“Subscribing” a return, statement, or other document means signing the return.¹³⁴ Authorizing a subscription by a return preparer is a subscription of the return under Section 7206(1).¹³⁵ Additionally, a joint return signed by one spouse can be deemed subscribed by either spouse if evidence shows that the couple intended to file a joint return.¹³⁶ As an element of the crime, the burden of proving the signature beyond a reasonable doubt lies with the prosecution. However, the fact that an individual’s name is signed to a return, statement, or other document is *prima facie* evidence that the return, statement, or other document was actually signed by the taxpayer.¹³⁷ A signature on a return creates a permissible inference that allows the jury to infer the existence of an elemental fact.¹³⁸

The return, statement, or other document must be made “under the penalties of perjury.” This element is self-evident as the return, statement, or other document either does or does not contain a declaration that it is signed under the penalties of perjury.¹³⁹ Adding the phrase “without prejudice” near the taxpayer’s signature on the jurat does not affect the jurat.¹⁴⁰ A stricken jurat will not meet the “under penalties of perjury” requirement and the taxpayer cannot be prosecuted under Section 7206(1).¹⁴¹

The return, statement, or other document must be false with respect to a material matter. If any item on a return must be reported for a correct computation of tax, then it is a material matter.¹⁴² Additionally, if the item has the effect of influencing the accuracy of the return, or is of a nature capable of influencing or affecting the ability of the Internal Revenue Service to audit or verify the accuracy of the return, then the matter is material.¹⁴³ The false statement need not actually affect the processing of the return for the false statement to be material.¹⁴⁴

Falsely reported gross income is material, regardless of amount.¹⁴⁵ A misstatement of the source of income is also a materially false statement, even if the amount is accurate.¹⁴⁶ Omitting gross receipts is a materially false statement.¹⁴⁷ Furthermore, failing to

rationale is that taxpayers should have an opportunity for self-correction. *Id.*

134. Without a signature, the taxpayer has not violated I.R.C. 7206(1), but, by submitting a false unsigned return, the taxpayer may have committed an evasion under Section 7201. *United States v. Robinson*, 974 F.2d 575, 577-78 (5th Cir. 1992).

135. *United States v. Ponder*, 444 F.2d 816, 822 (5th Cir. 1971).

136. *United States v. McKee*, 506 F.3d 225, 233 (3d Cir. 2007).

137. I.R.C. § 6064.

138. *United States v. Gaines*, 690 F.2d 849, 853 (11th Cir. 1982).

139. Without a subscription “under penalties of perjury,” the government can only prosecute the taxpayer for the act of submitting a false statement as a misdemeanor. I.R.C. § 7207; *See United States v. Bishop*, 412 U.S. 346, 357-58 (1973).

140. *United States v. Davis*, 603 F.3d 303, 307 (5th Cir. 2010).

141. TAX DIVISION, U.S. DEP’T OF JUSTICE, CRIMINAL TAX MANUAL ¶ 12.09[1] (2012). Note that this does not preclude a prosecution under I.R.C. § 7201.

142. *United States v. Boulterice*, 325 F.3d 75, 82 (1st Cir. 2003); *United States v. Clifton*, 127 F.3d 969, 970 (10th Cir. 1997).

143. *United States v. Strand*, 617 F.2d 571, 574 (10th Cir.), *cert. denied*, 449 U.S. 841 (1980).

144. *Genstil v. United States*, 326 F.2d 243, 245 (1st Cir.), *cert. denied*, 377 U.S. 916 (1964); *accord*, *United States v. Romanow*, 509 F.2d 26, 28 (1st Cir. 1975) (stating that materiality must be “measured objectively by a statement’s potential rather than by its actual impact.”).

145. *United States v. Hedman*, 630 F.2d 1184, 1196 (7th Cir. 1980).

146. *United States v. DiVarco*, 484 F.2d 670, 672-73 (7th Cir. 1973); *United States v. Jacobson*, 547 F.2d 21 (2d Cir. 1976), *cert. denied*, 430 U.S. 946 (1977).

147. *United States v. Holladay*, 566 F.2d 1018 (5th Cir.), *cert. denied*, 439 U.S. 831 (1978).

report gross revenues from the sale of narcotics¹⁴⁸ and winnings from gambling¹⁴⁹ are materially false statements.

Neither evasion nor tax deficiency is an element of making a false return under Section 7206(1).¹⁵⁰ Technically, a taxpayer can be convicted of making a false return even if the tax was overpaid if the taxpayer made a materially false statement.¹⁵¹

IV. PROVING CRIMINAL TAX FRAUD

The Internal Revenue Service's Criminal Investigation Division investigates the top echelon members of high-level drug trafficking organizations, including the orchestration of financial activities directing the transportation, distribution, and laundering of drug trafficking proceeds. Investigations within the narcotics program may be undertaken through the Organized Crime Drug Enforcement Task Force (OCDETF).¹⁵² The Service established the OCDETF to identify, investigate, and prosecute drug dealers and to dismantle the operations of their enterprises.¹⁵³

In proving a criminal tax fraud case, the government can use direct or indirect methods of proof. Using specific items to show unreported income or overstated deductions is a direct method. The government can use an indirect method to prove its case by employing the net worth method, the cash expenditures method, or the bank deposits method. These methods are not exclusive and one method can be used to corroborate another.¹⁵⁴ In proving a criminal tax fraud case, the government need not prove a precise deficiency,¹⁵⁵ and the government is free to use any legal evidence available.¹⁵⁶

A. *Direct Method – Specific Items*

The specific items method is a direct method of proof to demonstrate unreported income and overstated deductions. The Department of Justice has identified four general categories of specific items cases: (1) understating income from reported sources; (2) failing to report a particular item of income; (3) failing to report a business; and (4) reporting

148. *United States v. Garcilaso De La Vega*, 489 F.2d 761 (2d Cir. 1974).

149. *United States v. Scholl*, 166 F.3d 964, 980 (9th Cir. 1999).

150. *United States v. Perez*, 612 F.3d 879, 886 (7th Cir. 2010). Some courts, however, have allowed the argument that no tax was due to be a question of materiality for the jury. *See United States v. Clifton*, 127 F.3d 969 (10th Cir. 1997).

151. *United States v. Johnson*, 558 F.2d 744, 745-46 (5th Cir. 1977), *cert. denied*, 434 U.S. 1065 (1978).

152. INTERNAL REVENUE MANUAL ¶ 9.5.3.4 (2005).

153. *Id.* ¶ 9.5.7.2.

154. The government can use the net worth method to corroborate the direct method. *See, e.g., Holland v. United States*, 348 U.S. 121, 126 (1954); *United States v. Cramer*, 447 F.2d 210, 217-18 (2d Cir. 1971). The government can use the expenditures method to corroborate the direct method. *See, e.g., United States v. McGuire*, 347 F.2d 99, 101 (6th Cir. 1965). The government can use the bank deposits method to corroborate the direct method. *See, e.g., United States v. Tafoya*, 757 F.2d 1522, 1528 (5th Cir. 1985); *Canton v. United States*, 226 F.2d 313, 322-23 (8th Cir. 1955). The government can use an indirect method to corroborate another indirect method. *See, e.g., United States v. Abodeely*, 801 F.2d 1020, 1023 (8th Cir. 1986). Additionally, the government can rely on a direct method for one charge and an indirect method for a different charge. *United States v. Dawson*, 400 F.2d 194, 203 (2d Cir. 1968). When using an indirect method to corroborate the direct method, the jury should be instructed to limit its consideration of the indirect analysis to corroboration. *See United States v. Horton*, 526 F.2d 884, 887-88 (5th Cir. 1976).

155. *Johnson*, 319 U.S. at 503.

156. *Holland*, 348 U.S. at 121. *See also Ray A. Knight & Lee G. Knight, Criminal Tax Fraud: An Analytical Review*, 57 MO. L. REV. 175, 191-92 (1992).

a false source of income.¹⁵⁷ This method of proof differs from the indirect methods of proof, focusing on specific financial transactions and not attempting to reconstruct the taxpayer's overall financial situation.¹⁵⁸ This simple method of proving tax evasion may consist of only the return and the testimony or records of a third party showing the payment of an unreported item of income. The specific items method is advantageous because it is easy for the prosecutor to present and easy for the jury to understand.¹⁵⁹

The Department of Justice has identified four basic proofs to establish a specific items case: (1) the relevant amounts are taxable income to the taxpayer; (2) receipt of income by the taxpayer; (3) the taxpayer's failure to report the income; and (4) the taxpayer's personal involvement in the failure to report the income and in the disposition of the unreported income.¹⁶⁰

In proving its claims for understating income from reported sources, the government must establish that the total income received is greater than the total reported, but need not prove which particular items were not reported.¹⁶¹ The simple proof required to overcome reported income can be fairly simple and include calling witnesses to testify as to the amount of money paid to the taxpayer, adding the amounts, and comparing the total to that shown on the return. However, this method requires an itemization of, and witnesses to testify to, enough income to exceed the income reported on the return.

In proving its claims for failing to report income from a business enterprise, the government must establish that the taxpayer operated the business by using the testimony of insiders and customers who witnessed the operation. The government must also prove the existence of unreported income through the use of witness testimony, bank records, and business records. Finally, the government may have to prove, if appropriate, that the taxpayer did not inform his or her return preparer.¹⁶²

B. *Indirect Method – Net Worth*

If a taxpayer purposely fails to maintain books and records, or does not use bank accounts to deposit receipts or to pay business expenses, the government must use other evidence to prove an individual had taxable income.¹⁶³ The net worth method relies on the premise that if a taxpayer has more wealth at the end of a given year than at the beginning of that year, the taxpayer has income unless the increase comes from nontaxable sources. The measure of such increase is the taxpayer's income for the year.¹⁶⁴ A net worth method analysis reveals not only the taxpayer's income, but how that income was spent, thereby describing the financial life of the taxpayer.¹⁶⁵

In a net worth method prosecution, the government must: (1) prove an opening net

157. TAX DIVISION, U.S. DEP'T OF JUSTICE, CRIMINAL TAX MANUAL ¶ 30.01 (2012).

158. *United States v. Black*, 843 F.2d 1456, 1458 (D.C. Cir. 1988).

159. TAX DIVISION, U.S. DEP'T OF JUSTICE, CRIMINAL TAX MANUAL ¶ 30.01 (2012).

160. *Id.* The government must show that the taxpayer received unreported taxable income, but it need not show how the taxpayer spent the money. *United States v. Martin*, 525 F.2d 703, 707 (2d Cir. 1975).

161. *See, e.g., United States v. Marabelles*, 724 F.2d 1374, 1378 & n.2 (9th Cir. 1984); *United States v. Horton*, 526 F.2d 884, 886 (5th Cir. 1976).

162. *See, e.g., Siravo v. United States*, 377 F.2d 469 (1st Cir. 1967).

163. *See, e.g., United States v. Terrell*, 754 F.2d 1139 (5th Cir.), *cert. denied*, 472 U.S. 1029 (1985).

164. *Holland v. United States*, 348 U.S. 121, 125 (1954); *United States v. Giacalone*, 574 F.2d 328, 331-32 (6th Cir. 1978).

165. *See Holland*, 348 U.S. at 125, 132-33; *United States v. Mastropieri*, 685 F.2d 776, 778 (2d Cir. 1982).

worth, (2) demonstrate that it investigated all relevant leads furnished by the taxpayer to establish innocence, and (3) either demonstrate a likely source of the illegally unreported income or demonstrate that all possible sources of nontaxable income must be negated.¹⁶⁶

Under the net worth method, the government's first step is to establish the taxpayer's total value of assets at the beginning of the period and compare that value to the value of the taxpayer's assets at the end of the period.¹⁶⁷ A *prima facie* case is made if the government establishes the taxpayer's opening net worth with reasonable certainty, then shows increases in net worth for each year in question that, when added to the nondeductible expenditures and excluding known nontaxable receipts for the year, exceed the reported taxable income by a substantial amount.¹⁶⁸ Sloppy recordkeeping is not criminal, but it can lead to legal increases in net worth that can be difficult to explain. Thus, to avoid the inherent problems of the net worth system, which might subject sloppiness to criminal sanctions, the government must conduct a meticulous investigation, which is subject to close scrutiny.¹⁶⁹

The government must establish with reasonable certainty the opening net worth. The accuracy of the net worth method depends entirely upon the inclusion in the opening net worth of all assets on hand at the outset.¹⁷⁰ If the charges cover a period of consecutive years, the government need not prove the reasonably certain net worth prior to each taxable year. However, any increases must be allocated to the appropriate taxable year.¹⁷¹ The government must make every effort to obtain all the assets and liabilities of the taxpayer at the starting point. However, this standard does not obligate the government to establish the opening net worth to a mathematical certainty, only to a reasonable certainty.¹⁷²

Generally, in establishing the net worth of a taxpayer, assets are reflected at cost, not at fair market value, because the net worth method relies on actual expenditures.¹⁷³ This does not apply when cost is not used as a basis, such as inheritances and gifts.¹⁷⁴ Likewise, if the taxpayer receives services in exchange for property, the net worth method requires the use of the fair market value of the property.¹⁷⁵

Once the government establishes the opening net worth and ending net worth, the opening net worth is subtracted from the ending net worth, resulting in the net worth increase. To obtain income, the taxpayer's nondeductible expenditures during the period, including living expenses, are added to the net worth increase to obtain the income.¹⁷⁶ If

166. *United States v. Blandina*, 895 F.2d 293 (7th Cir. 1989); see *Holland*, 348 U.S. at 132.

167. *Terrell*, 754 F.2d at 1139.

168. *United States v. Sorrentino*, 726 F.2d 876 (1st Cir. 1984).

169. *Terrell*, 754 F.2d at 1145. The government must undertake an extremely thorough investigation because the net worth method creates in the government a special responsibility of thoroughness and particularity in its investigation and presentation. *United States v. Hall*, 650 F.2d 994, 999 (9th Cir. 1981); *Terrell*, 754 F.2d at 1145. If the government fails to complete a thorough investigation, a conviction can be overturned. See *United States v. Smith*, 890 F.2d 711, 713 (5th Cir. 1989).

170. *Holland*, 348 U.S. at 132.

171. *United States v. Mastropieri*, 685 F.2d 776 (2d Cir. 1982).

172. *Holland*, 348 U.S. at 138; *United States v. Gardner*, 611 F.2d 770, 775 (9th Cir. 1980); *Terrell*, 754 F.2d at 1145; *Sorrentino*, 726 F.2d at 879.

173. *United States v. O'Connor*, 237 F.2d 466, 473 n.6 (2d Cir. 1956).

174. See I.R.C. §§ 1014(a)(1), 1015.

175. Treas. Reg. § 1.61-2(d).

176. *Holland*, 348 U.S. at 125; *Terrell*, 754 F.2d at 1144; *United States v. Hamilton*, 620 F.2d 712, 714 n.1 (9th Cir. 1980); *United States v. Skalicky*, 615 F.2d 1117, 1119 (5th Cir. 1980). The government has the burden of establishing that the expenditures added to the net worth increase are nondeductible expenditures, rather than

the income so determined exceeds the income reported, the taxpayer has unreported income.

The net worth method requires evidence supporting the inference that the net worth increases are income.¹⁷⁷ The government has two ways of supporting such an inference:¹⁷⁸ proof of a likely source of taxable income¹⁷⁹ and negation of nontaxable sources of income.¹⁸⁰ The government can establish a likely source of taxable income through either direct or circumstantial evidence from which a jury could reasonably find that the net worth increases arose.¹⁸¹ Additionally, the government has no limitation on the number of likely sources of taxable income, but can introduce evidence of as many possible sources of taxable income as the investigators have developed.¹⁸² Furthermore, the government need not prove that the identified likely source is the source of the entire amount of unreported income.¹⁸³

The likely source can be a legal or illegal source of income.¹⁸⁴ Without a charge of the crime underlying the illegal source of income, the court should limit the evidence to prove the illegal source of income because of the possibility of undue prejudice.¹⁸⁵ The government must clearly establish that the purpose of introducing evidence of illegal activities is the establishment of a likely source of income, and the government may not introduce or allude to the evidence in a manner calculated to inflame the jury.¹⁸⁶

C. Indirect Method – Expenditures

Another indirect method of proving income is the expenditures method.¹⁸⁷ In proving an expenditures method deficiency, the government must start with an appraisal of the taxpayer's net worth at the beginning of a period. If, during that period, the taxpayer's expenditures have exceeded the amount reported as income and the taxpayer's net worth at the end of the applicable period is not reduced accordingly, the jury may conclude that the taxpayer has underreported income.¹⁸⁸ As with the net worth method, use of the expenditures method requires a measurement in comparison to reported income. Because the

deductible expenditures, such as business expenses. *Fowler v. United States*, 352 F.2d 100, 103 (8th Cir. 1965).

177. *Holland*, 348 U.S. at 137; *United States v. Dvoskin*, 644 F.2d 418, 422 (5th Cir. 1981).

178. *See* *United States v. Sorrentino*, 726 F.2d 876, 879-80 (1st Cir. 1984).

179. *Holland*, 348 U.S. at 137-38. The government need not prove a specific source, but only a likely source. *United States v. Hom Ming Dong*, 436 F.2d 1237, 1241-42 (9th Cir. 1971).

180. *United States v. Massei*, 355 U.S. 595, 595-96 (1958) (per curiam). The government need not negate every possible source, as this would prove impossible. *United States v. Hiatt*, 581 F.2d 1199, 1202 (5th Cir. 1978).

181. *Holland*, 348 U.S. at 138.

182. *See, e.g.*, *Feichtmeir v. United States*, 389 F.2d 498, 502 (9th Cir. 1968).

183. *United States v. Costanzo*, 581 F.2d 28, 33 (2d Cir. 1978).

184. *James v. United States*, 366 U.S. 213 (1961).

185. *See, e.g.*, *United States v. Tunnell*, 481 F.2d 149, 151 (5th Cir. 1973).

186. *See* *United States v. Abodeely*, 801 F.2d 1020, 1022 (8th Cir. 1986). Testimony of "customers" can establish the source of income for narcotics traffickers. *See* *United States v. Scrima*, 819 F.2d 996, 999 (11th Cir. 1987); *United States v. Palmer*, 809 F.2d 1504, 1505 (11th Cir. 1987); *United States v. Lewis*, 759 F.2d 1316, 1328, 1336 (8th Cir. 1985); *United States v. Horvath*, 731 F.2d 557, 563 (8th Cir. 1984); *United States v. Heyward*, 729 F.2d 297, 301 (4th Cir. 1984); *United States v. Enstam*, 622 F.2d 857, 860 (5th Cir. 1980); *United States v. Browning*, 723 F.2d 1544, 1547 (11th Cir. 1984).

187. *United States v. Johnson*, 319 U.S. 503, 517-18 (1943).

188. *United States v. Caserta*, 199 F.2d 905, 907 (3d Cir. 1952).

method is so similar to the net worth method, the same general requirements and safeguards apply.¹⁸⁹

In attempting to prove income under the expenditures method, the government must: (1) establish an opening net worth with reasonable certainty and demonstrate that the taxpayer's expenditures did not result from the reduction of assets on hand at the beginning of the period; (2) establish through independent evidence that the expenditures charged to the taxpayer are nondeductible; (3) establish a likely source of income from which the expenditures sprang or, alternatively, negate nontaxable sources of income; and (4) investigate all relevant, reasonable leads that are reasonably susceptible of being checked.¹⁹⁰

D. Indirect Method – Bank Deposits

The final indirect method of proving income is the bank deposits method. Under this method, the government first aggregates all deposits to the taxpayer's bank and similar accounts in a single year to determine the gross deposits. The government must then identify all deposits that are nontaxable, such as gifts, transfers, loan repayments, and cash on hand prior to that year, resulting in net taxable bank deposits. The government must then demonstrate the amount of expenditures from undeposited cash. The net taxable bank deposits plus the undeposited cash expenditures equals actual gross income, which the government then compares to the reported income. The excess is the unreported income.¹⁹¹

Underlying the bank deposits method is the assumption that if a taxpayer engages in an income-producing activity and regularly makes deposits to bank accounts, then those deposits, after adjustments, constitute taxable income.¹⁹²

The government must conduct an adequate and full investigation of the taxpayer's accounts to distinguish between income and non-income deposits in support of the inference that the unexplained excess in deposits is taxable income.¹⁹³ However, the government is not under an obligation to negate every possible non-income source of each deposit.¹⁹⁴ The adequacy of the government's investigation depends on the circumstances of each case based on the practicality of completing a certain degree of investigation. The investigator's burden is to do the best possible work to discover and exclude all non-income items.¹⁹⁵

V. UNITED STATES V. WALTER WHITE

Walter White is a chemistry teacher who has just turned fifty. He collapses while

189. *United States v. Breger*, 616 F.2d 634, 635 (2d Cir. 1980).

190. The reasonable certainty, likely source, and investigation requirement are the same burdens required under the net worth method. *See Taglianetti v. United States*, 398 F.2d 558, 564-65 (1st Cir. 1968), *aff'd*, 394 U.S. 316 (1969); *accord United States v. Marrinson*, 832 F.2d 1465, 1472 (7th Cir. 1987). *See supra* text accompanying notes 170-86. Although a formal statement of net worth is not required in an expenditures method case, the government must still establish the taxpayer's opening financial position. *See United States v. Conaway*, 11 F.3d 40, 43 (5th Cir. 1993); *United States v. Citron*, 783 F.2d 307, 316 (2d Cir. 1986). Demonstrating the opening financial position of the taxpayer is the most difficult component of proof in such tax prosecutions. *See, e.g., id.* at 316-17 (reversing the taxpayer's convictions because the district court admitted into evidence a summary chart containing figures not demonstrably supported by the evidence).

191. *United States v. Boulet*, 577 F.2d 1165, 1167 (5th Cir. 1978).

192. *United States v. Morse*, 491 F.2d 149, 152 (1st Cir. 1974).

193. *United States v. Lawhon*, 499 F.2d 352, 356 (5th Cir. 1974); *Morse*, 491 F.2d at 152.

194. *Boulet*, 577 F.2d at 1171.

195. *United States v. Slutsky*, 487 F.2d 832, 841 (2d Cir. 1973).

working his second job. Later that day, the doctor gives Walter the diagnosis; Walter has terminal lung cancer. He bears this burden alone while he plots a way to leave a nest egg for his family. Walter and his former student, Jesse Pinkman, begin “cooking” and selling crystal meth.¹⁹⁶ Walter and Pinkman come into their first illicit revenues from a deal with two low level drug dealers that goes wrong. The meth is not sold and the dealers end up dead. However, Walter and Pinkman keep the money brought by the dealers.¹⁹⁷

Once Walter finally divulges the secret of his terminal lung cancer diagnosis, his family is distraught.¹⁹⁸ Skyler, Walter’s wife, pressures Walter to get the best possible treatment and makes an appointment with a top oncologist—one who will not take the teachers’ union insurance. The cost of the treatments requires a \$5,000 deposit, which Walter begrudgingly pays. For the series of treatments, Walter commits to \$90,000 in fees.¹⁹⁹ Walter’s former business partners at Gray Matter, Elliot and Gretchen Schwartz, learn of Walter’s cancer and offer him a job. After his refusal, they offer to pay for his cancer treatment. Walter declines out of pride, but tells Skyler he accepted their offer so she will not be suspicious about the source of his funds.²⁰⁰

Walter and Pinkman continue “cooking” and seeking a method of distribution. The pair finds a willing, but unstable, distributor in Tuco Salamanca. The first sale to Salamanca produces \$50,000 for a batch of crystal meth.²⁰¹ Salamanca agrees to a weekly purchase of crystal meth for approximately \$140,000.²⁰² However, Salamanca meets an untimely demise after a showdown in the desert, causing Walter and Pinkman to find a new method of distribution.²⁰³

Walter calculates that, to save for college tuition, pay off the mortgage, and provide for a modest monthly income, he needs to save \$737,000 before he succumbs to the cancer.²⁰⁴ To expedite the distribution and increase profits, Walter and Pinkman decide to begin distributing their product directly by enlisting street-level dealers.²⁰⁵ The distribution is slow and not profitable. Still, Walter has netted another \$16,000.²⁰⁶ Walter and Pinkman share their difficulties with their attorney, Saul Goodman, who puts them in touch with Gustavo Fring.²⁰⁷ Fring buys thirty-eight pounds of crystal meth for over \$1,000,000.²⁰⁸ Subsequently, Walter enters into a contractual relationship with Fring. Fring builds a Superlab and Walter produces crystal meth in exchange for \$1,000,000 per month.²⁰⁹ After Fring’s demise, Walter continues to produce crystal meth under the cover of Vamanos Pest Control and provides shipments to the Czech Republic. The Vamanos operation produces approximately \$80 million over the next few months.²¹⁰ After accumulating this much

196. *Breaking Bad: Pilot*, *supra* note 2.

197. *Id.*

198. *Breaking Bad: Cancer Man*, *supra* note 6.

199. *Id.*

200. *Breaking Bad: Gray Matter*, *supra* note 5.

201. *Breaking Bad: Crazy Handful of Nothin'*, *supra* note 7.

202. *Breaking Bad: Seven Thirty-Seven* (AMC television broadcast Mar. 8, 2009).

203. *Breaking Bad: Breakage* (AMC television broadcast Apr. 5, 2009).

204. *Breaking Bad: Seven Thirty-Seven*, *supra* note 202.

205. *Breaking Bad: Peekaboo* (AMC television broadcast Apr. 12, 2009).

206. *Breaking Bad: 4 Days Out* (AMC television broadcast May 3, 2009).

207. *Breaking Bad: Mandala* (AMC television broadcast May 17, 2009).

208. *Breaking Bad: Phoenix* (AMC television broadcast May 24, 2009).

209. *Id.*

210. *Breaking Bad: Gliding over All*, *supra* note 10.

cash, Walter decides to “retire.”²¹¹

Although Walter has the funds to pay for his surgery, his family is unaware and continues raising money. Agent Schrader solicits donations from co-workers and Walter’s son, Walt Jr., creates a website seeking donations to pay for his father’s cancer treatment.²¹² This website provides Walter with his first laundering scheme. Walter’s attorney, Saul Goodman, Esq., hatches the scheme to use the website to bring in thousands of small donations. A computer expert in Belarus hacks computers around the world that log donations, providing an explanation of the source of Walter’s new-found revenue.²¹³ After the website is shut down, Walter explores other options for laundering money, which leads to the purchase of the car wash at which Walter used to work. Walter pays \$800,000 for the car wash, much of which is paid for by a loan.²¹⁴

Walter begins spending money in a manner inconsistent with his means. As a high school chemistry teacher, his income is insufficient to support his wife, teenage son, and himself, which is why he holds the second job at the car wash.²¹⁵ With a baby on the way, Walter has additional expenses, such as the nursery and diapers. However, Walter begins spending cash freely. He buys an expensive water heater with cash.²¹⁶ He pays oncologist fees and schedules a surgery related to his cancer treatment, which costs approximately \$200,000.²¹⁷ After a rift develops between Walter and his wife, he gets a separate apartment.²¹⁸ Walter upgrades and purchases a condominium shortly thereafter.²¹⁹ After two hitmen shoot him, Agent Schrader suffers spinal damage and needs therapy. Walter pays over \$177,000 in medical bills for Agent Schrader’s recovery.²²⁰ Additionally, Walter buys an expensive leather jacket and leases flashy new cars for himself and Walt Jr.²²¹

A. *Walter White Committed Tax Fraud*

Walter White committed a felony by attempting to evade or defeat a tax by willfully attempting to evade the assessment of a tax.²²² In prosecuting Walter for attempting to evade or defeat a tax, the government must prove (1) willfulness, (2) the existence of a tax deficiency, and (3) an affirmative act that constitutes an evasion or attempted evasion of the tax.²²³

Walter was willful in his attempt to evade or defeat the tax. Willfulness requires

211. *Breaking Bad: Rabid Dog* (AMC television broadcast Sept. 1, 2013).

212. *Breaking Bad: No Mas* (AMC television broadcast Mar. 21, 2010).

213. *Breaking Bad: Phoenix*, *supra* note 208. Walter White, Jr.’s website is available at <http://www.savewalterwhite.com/>. SAVE WALTER WHITE, <http://www.savewalterwhite.com> (last visited Feb. 1, 2014).

214. *Breaking Bad: Shotgun* (AMC television broadcast Aug. 14, 2011).

215. *Breaking Bad: Pilot*, *supra* note 2.

216. *Breaking Bad: Over* (AMC television broadcast May 10, 2009).

217. *Breaking Bad: Phoenix*, *supra* note 208.

218. *Breaking Bad: No Mas*, *supra* note 212.

219. *Breaking Bad: Sunset*, *supra* note 22.

220. *Breaking Bad: Kafkaesque* (AMC television broadcast May 16, 2010).

221. *Breaking Bad: Fifty-One*, *supra* note 8. Walter leases a Chrysler 300 for himself and a Dodge Challenger for Walt, Jr. *Id.*

222. I.R.C. § 7201.

223. *Sansone v. United States*, 380 U.S. 343, 351 (1965); *United States v. Thompson*, 518 F.3d 832, 850 (10th Cir. 2008).

proof that the law imposed a duty on Walter, that he knew of this duty, and that he voluntarily and intentionally violated such duty.²²⁴ Willfulness can be inferred from such actions as making false invoices or documents and concealing assets or covering up sources of income.²²⁵ Walter used the charitable website created by his son to convert income to non-taxable gifts by creating false logs of the donations. Walter hid cash in ducts, crawl spaces, storage units, and barrels buried in the desert, each a concealment of assets. Willfulness can also be inferred from a consistent pattern of underreporting large amounts of income,²²⁶ spending large amounts of cash that cannot be reconciled with reported income,²²⁷ and having illegal sources of income.²²⁸ Walter never reported his vast proceeds from his manufacture of crystal meth. He spent large amounts of cash on medical treatments, cars, an extra apartment, and a car wash. These are items he could not afford on his reported income—that of a public school teacher. He also had significant sources of illegal income. Each action of consistently underreporting income, overspending, and collecting illegal income demonstrates willfulness. Walter knew the law imposed upon him a duty to abide by the internal revenue laws, and he voluntarily and intentionally violated such duty.

Walter's unreported income would lead to additional tax due. A tax deficiency equals the amount by which the lawful tax due exceeds the sum of the tax due shown on the return and any previously assessed deficiency minus any rebate previously received.²²⁹ Income from illegal sources is taxable income.²³⁰ Walter had significant income from the illegal production and sale of crystal meth. These proceeds are taxable income that Walter failed to report. The substantiality requirement for the tax deficiency is a facts and circumstances test,²³¹ but if a deficiency exceeds an amount that would be deemed relatively small under the circumstances it is a substantial deficiency.²³² The government can prove that Walter had at least hundreds of thousands of dollars of unreported income—several times his reported wages. If a substantiality threshold applies, the unreported income would create a substantial tax deficiency because the unreported income was many multiples of the reported income. Therefore, Walter had a substantial tax deficiency.

Walter committed affirmative acts that constitute an evasion or attempted evasion of the tax. The government must prove that the taxpayer committed an affirmative act with the specific intent to evade tax. The acts of making false entries and altering entries and concealing assets or covering up sources of income are affirmative acts that constitute evasion.²³³ Walter created false logs by using his son's website to convert income to non-taxable gifts. Additionally, Walter hid cash and assets and did not disclose his narcotics

224. *Cheek v. United States*, 498 U.S. 192, 201 (1991); *United States v. Pomponio*, 429 U.S. 10, 12 (1976).

225. *Spies v. United States*, 317 U.S. 492, 499 (1943).

226. *United States v. Bishop*, 264 F.3d 535, 550 (5th Cir. 2001).

227. *United States v. Simonelli*, 237 F.3d 19, 30 (1st Cir. 2001); *United States v. Olbres*, 61 F.3d 967, 971 (1st Cir. 1995).

228. *United States v. Palmer*, 809 F.2d 1504, 1505-06 (11th Cir. 1987).

229. I.R.C. § 6211(a); *Bishop*, 264 F.3d at 535. Rebates are abatements, credits, refunds, or other repayments from income tax due. I.R.C. § 6211(b)(2).

230. *James v. United States*, 366 U.S. 213 (1961).

231. *Canaday v. United States*, 354 F.2d 849, 851-52 (8th Cir. 1966). *See also*, *United States v. Cunningham*, 723 F.2d 217, 230-31 (2d Cir. 1983).

232. *See United States v. Siragusa*, 450 F.2d 592, 594-96 (2d Cir. 1971); *United States v. Gross*, 286 F.2d 59, 61 (2d Cir. 1961).

233. *See Spinney v. United States*, 385 F.2d 908, 911 (1st Cir. 1967); *United States v. Stone*, 431 F.2d 1286, 1288 (5th Cir. 1970); *Burke v. United States*, 293 F.2d 398, 399 (1st Cir. 1961).

business, thereby concealing his sources of income. These acts prove not only willfulness, but also constitute affirmative acts to evade tax. Because he willfully attempted to evade tax, had a substantial tax deficiency in 2009, and committed affirmative acts of evasion, Walter White violated Section 7201 by attempting to evade a tax.

Walter White committed a felony by making and subscribing to a false document.²³⁴ This crime is willfully making, and subscribing to, a materially false return, signed under the penalties of perjury, for which the taxpayer did not believe it to be true and correct as to every material matter.²³⁵

Walter was willful in making and subscribing to the false document.²³⁶ His willful acts include using the charitable website created by his son to convert income to nontaxable gifts, hiding cash, providing his return preparer with inaccurate and incomplete information,²³⁷ spending large amounts of cash that cannot be reconciled with reported income,²³⁸ and having illegal sources of income.²³⁹

Walter made and subscribed income tax returns. "Making" a return, statement, or other document is the preparing and filing a return.²⁴⁰ "Subscribing" a return means signing the return. By filing annual income tax returns, whether by mail or electronically, Walter made and subscribed to a return. Authorizing a subscription by a return preparer is a subscription of the return under Section 7206(1).²⁴¹ Therefore, even if Walter had hired a return preparer to file the tax return, he still made and subscribed to the return.²⁴²

Walter's returns contained materially false information. If any item on a return must be reported for a correct computation of tax, then it is a material matter.²⁴³ Walter failed to report significant amounts of income, which, of course, would be an item required to correctly compute income. Falsely reported gross income is material, regardless of amount.²⁴⁴ Because Walter did not report the income from the sale of crystal meth, the return is materially false. A misstatement of the source of income is a materially false statement even if the amount is accurate.²⁴⁵ Failing to report gross revenues from the sale of narcotics is a materially false statement.²⁴⁶ Walter had millions of dollars in revenue from the sale of

234. I.R.C. § 7206(1). Walter and Skyler White filed, and would have continued to file, income tax returns. Although the show does not provide the viewers with such details, it must be inferred from their money-laundering actions that the intent remains to hide the criminal activities by acting as if they are still law-abiding taxpayers. *See, e.g., supra* text accompanying notes 212-14.

235. *United States v. Bishop*, 264 F.3d 535, 550 (5th Cir. 2001); *United States v. Hills*, 618 F.3d 619, 634 (7th Cir. 2010); *United States v. Griffin*, 524 F.3d 71, 75-76 (1st Cir. 2008).

236. The willfulness requirement has the same components as for the attempt to evade or defeat tax. *See supra* text accompanying notes 84-97.

237. *Bishop*, 264 F.3d at 552; *United States v. Samara*, 643 F.2d 701, 703 (10th Cir. 1981). *See also* *United States v. Chesson*, 933 F.2d 298, 305 (5th Cir. 1991).

238. *United States v. Simonelli*, 237 F.3d 19, 30 (1st Cir. 2001); *United States v. Olbres*, 61 F.3d 967, 971 (1st Cir. 1995).

239. *United States v. Palmer*, 809 F.2d 1504, 1505-06 (11th Cir. 1987).

240. *United States v. Gilkey*, 362 F. Supp. 1069, 1071 (E.D. Pa. 1973).

241. *United States v. Ponder*, 444 F.2d 816, 822 (5th Cir. 1971).

242. A return preparer must obtain a signed Form 8879, which provides authorization for e-filing signature authority. *See* I.R.S., Form 8879, IRS e-File Signature Authorization (2013).

243. *United States v. Boulterice*, 325 F.3d 75, 82 (1st Cir. 2003); *United States v. Clifton*, 127 F.3d 969, 970 (10th Cir. 1997).

244. *United States v. Hedman*, 630 F.2d 1184, 1196 (7th Cir. 1980).

245. *United States v. DiVarco*, 484 F.2d 670, 672-73 (7th Cir. 1973); *United States v. Jacobson*, 547 F.2d 21 (2d Cir. 1976).

246. *United States v. Garcilaso De La Vega*, 489 F.2d 761 (2d Cir. 1974).

narcotics, which was not reported on his return. Therefore, he made materially false statements. The Internal Revenue Service requires disclosure of the source of proceeds from illegal activity.²⁴⁷ Walter did not accurately disclose the source of his income and, therefore, filed a materially false return.

The return must be made “under the penalties of perjury.” All income tax returns have a jurat subjecting the filer to the penalties of perjury for false statements thereon.²⁴⁸ Hence, the act of filing an income tax return by Walter is making a statement “under the penalties of perjury.”

Walter knew that the information on the return was not true and correct as to all material statements. A taxpayer’s signature on an income tax return indicates that the taxpayer attests to the accuracy of the reported data.²⁴⁹ Furthermore, once it has been shown that the return was false, a taxpayer’s signature is sufficient to establish knowledge.²⁵⁰ Walter signed the return, and the return is materially false. Therefore, he is presumed to have knowledge that the return was not true and correct.

Without doubt, Walter White attempted to evade or defeat a tax, and filed false statements. However, the government will not be able to discover all of the acts that constitute Walter’s criminal tax fraud.

B. *The Government Can Prove Walter White’s Tax Fraud*

The government has four different methods of proving the monetary elements of criminal tax fraud: the specific items method, the net worth method, the expenditures method, and the bank deposit method. These four methods are not mutually exclusive and can be used in conjunction to prove criminal tax acts.²⁵¹ Therefore, in its case against Walter White, the government would likely employ more than one of these methods to prove criminal tax fraud.

The specific items method is useful for prosecuting cases of understatement, failing to report a business income, and reporting false sources of income. Walter White understated his income by not reporting his millions of dollars of income, failed to report a business income by failing to report income from his crystal meth production, and reported a false source of his illegal narcotics sales.

To prove a case under the specific items method, the government must show: (1) the relevant amounts are taxable income to the taxpayer; (2) receipt of income by the taxpayer; (3) the taxpayer’s failure to report the income; and (4) the taxpayer’s personal involvement in the failure to report the income and in the disposition of the unreported income.²⁵²

The government must prove these specific items through direct evidence, such as witness testimony. This means that, to prove its case against Walter, the government must call witnesses with direct knowledge of Walter’s receipt of unreported income. Those with

247. See I.R.S., Form 1040, U.S. Individual Income Tax Return 1 (2013) (requiring the taxpayer to list the amount and source of any “Other Income” on Line 21); I.R.S. Publication 17, Your Federal Income Tax at 96 (Nov. 26, 2013) (requiring reporting of illegal sources of income, including “money from dealing illegal drugs”).

248. See, e.g., I.R.S., Form 1040, U.S. Individual Income Tax Return 2 (2013).

249. *United States v. Davis*, 603 F.3d 303, 306 (5th Cir. 2010).

250. *United States v. Drape*, 668 F.2d 22, 26 (1st Cir. 1982).

251. See, e.g., *Holland v. United States*, 348 U.S. 121, 126 (1954); *United States v. McGuire*, 347 F.2d 99, 101 (6th Cir. 1965); *United States v. Tafoya*, 757 F.2d 1522, 1528 (5th Cir. 1985); *United States v. Abodeely*, 801 F.2d 1020, 1023 (8th Cir. 1986).

252. TAX DIVISION, U.S. DEP’T OF JUSTICE, CRIMINAL TAX MANUAL ¶ 30.01 (2012).

direct knowledge of Walter's illicit income include Jesse Pinkman, Skyler White, Saul Goodman, Tuco Salamanca, Gustavo Fring, Mike Ehrmentraut, Lydia Rodarte-Quayle, Todd Alquist, and Jack Welker. At the time Walter decides to run, Walter presumes the white supremacist gang has killed Pinkman. Even though he is not dead, Pinkman's life expectancy is only as long as the store of methylamine will last. Therefore, Walter has no reason to fear the testimony of Pinkman. Skyler White demonstrates to Walter that she is completely on board with the enterprise. Her actions make her just as culpable as Walter with respect to the tax fraud. Also, Alquist ensures her silence through threats to her children. Walter has no reason to believe Skyler will testify against him. Saul Goodman is also complicit in the tax fraud schemes. Walter knows that Goodman is fleeing and taking a new identity. Hence, Walter has no reason to believe Goodman will testify against him. The testimony of narcotics purchasers can establish the source of income for drug trafficking.²⁵³ Walter sells crystal meth only through Ehrmentraut and Rodarte-Quayle, and sells crystal meth directly only to Salamanca and Fring. Except for Rodarte-Quayle, Walter knows that these potential witnesses are each dead and cannot testify against him. Finally, Rodarte-Quayle, Alquist, and Welker are unknown to the authorities. Rodarte-Quayle continues to operate the enterprise as the head of the drug-trafficking operation.²⁵⁴ As with Skyler, Rodarte-Quayle is more afraid of repercussions from criminals than prosecution by the government. The two seasoned criminals, Alquist and Welker, have been accomplices in many of the murders and much of the narcotics production. Walter can reasonably believe that these three will not testify against him. Without the testimony of at least one of these individuals, the government will not be able to prove the tax fraud of Walter using the specific items method.

Without any witnesses to prosecute a direct method case, the government must turn to an indirect method. The net worth method measures the net worth of a taxpayer at the beginning of a period and compares it to the net worth at the end of the period. If the net worth increases by more than the reported sources of income, minus expenditures, then the excess increase is unreported income. In a net worth method prosecution, the government must prove an opening net worth, demonstrate that it investigated all relevant leads furnished by the taxpayer to establish innocence, and either demonstrate a likely source of the illegally unreported income or demonstrate that all possible sources of nontaxable income have been negated.²⁵⁵

Walter's opening net worth should be fairly easy to establish. He owns a home (presumably with a mortgage), he has no investments, no substantial assets of value, and less than \$10,000 in his retirement account. At the end of the period, Walter owns a condominium, has leased two new fairly expensive cars, has spent hundreds of thousands of dollars in medical bills, and owns a car wash. Therefore, his closing net worth plus cash expenditures is significantly higher than his opening net worth plus reported income.

Walter may furnish investigators with sources that include gifts through Walt Jr.'s website and proceeds from gambling. If Walter demonstrates enough gifts through the website and reports enough income from the gambling to account for these expenses, the net worth increase will not exceed the reported income. The government would follow

253. See *United States v. Scrima*, 819 F.2d 996, 999 (11th Cir. 1987).

254. *Breaking Bad: Blood Money* (AMC television broadcast Aug. 11, 2013).

255. *United States v. Blandina*, 895 F.2d 293 (7th Cir. 1989); See *Holland*, 348 U.S. at 132.

these leads. Not only would they not prove helpful to Walter, but this information, if provided, would likely produce damaging evidence under the scrutiny of federal investigators. The website was funded through a “zombie” computer scheme run by a Belarussian cohort of Goodman. A detailed forensic investigation and witness testimony of the purported donors would easily discredit this scheme, thereby providing a source of unreported income. Also, any gambling gains sufficient to match these expenditures would have generated significant disclosures from the casino as well as surveillance footage of a significant presence on the casino floor.²⁵⁶

The government can establish a likely source of taxable income through either direct or circumstantial evidence from which a jury could reasonably find that the net worth increases arose.²⁵⁷ The government need not prove a specific source, but only a likely source.²⁵⁸ The government could provide evidence of the likely source of the illegal income, which is the production of crystal meth, without having the burden of proving the underlying crime.²⁵⁹ This means that the government can introduce evidence of the more serious crime of producing and selling narcotics for the purpose meeting its burden of establishing a likely source of income. Alternatively, without disclosure of the website and gambling income, the government could demonstrate that Walter had no possible sources of nontaxable income. Either way, the government would likely carry its burden of proving at least several hundred thousand dollars of unreported income using the net worth method.

Another indirect method of proving Walter's unreported income is the expenditures method. In attempting to prove income under the expenditures method, the government must: (1) establish an opening net worth and demonstrate that the taxpayer's expenditures did not result from the reduction of assets on hand at the beginning of the period; (2) establish through independent evidence that the expenditures charged to the taxpayer are nondeductible; (3) establish a likely source of income from which the expenditures sprang or negate nontaxable sources of income; and (4) investigate all relevant, reasonable leads that are reasonably susceptible of being checked.

As with the net worth method, the government could easily establish the opening net worth of Walter. He expended hundreds of thousands of dollars over the course of the year: purchasing a condo, leasing two new cars, paying substantial medical bills, and making a down payment on a car wash. Because his assets on hand at the beginning of the period were minimal, the government could demonstrate that the expenditures were not from the assets on hand at the beginning of the period. Although portions of the medical bills may be deductible,²⁶⁰ the capital investments of purchasing a condo and a car wash are not deductible. Likewise, the personal expenditure of a car lease, which is not a business expense, is not deductible. Therefore, the government could establish that most of these expenditures are nondeductible. As with the net worth method, the government could provide evidence of the likely source of the illegal income, which is the production of crystal meth, without having the burden of proving the underlying crime. Alternatively,

256. See I.R.S., Instructions for Forms W-2G and 5754 (2014).

257. *Holland*, 348 U.S. at 138.

258. *United States v. Hom Ming Dong*, 436 F.2d 1237, 1241-42 (9th Cir. 1971).

259. See *United States v. Tafoya*, 757 F.2d 1522, 1526 (5th Cir. 1985) (ruling that trial court judge did not err in allowing evidence of assassinations as likely source of income).

260. I.R.C. § 213(a). The \$177,000 paid for Agent Schrader's treatment would not be deductible because Agent Schrader is not a dependent of Walter. See *id.*

the government could demonstrate that Walter had insufficient sources of nontaxable income. Finally, the government could demonstrate that it has followed all leads in its investigation, which, incidentally, would also uncover many of the expenditures and illegal sources of income. Therefore, the government would likely carry its burden of proving at least several hundred thousand dollars of unreported income using the expenditures method.

The final indirect method of proving income is the bank deposits method. Under this method, the government first aggregates all deposits to the taxpayer's bank and similar accounts in a single year to determine the gross deposits, then subtracts all reported income and nontaxable sources. The remainder is unreported income. Because Walter did not deposit any funds into a bank account without first laundering the cash through the website or the car wash, the bank deposits method is not likely to demonstrate unreported income.

The government would use the net worth method and the expenditures method in conjunction to prove that Walter had unreported income. Walter has a significant increase in net worth, as evidenced by his nearly zero net worth at the beginning of the period and his significant holdings at the end of the period, even without discovery of his barrels of currency buried in the desert. Furthermore, Walter expended significantly more money than he could afford on his salary.

The government could convict Walter for evasion by proving Walter willfully evaded tax, had a tax deficiency, and committed an affirmative act that constitutes an evasion or attempted evasion of the tax. The government can prove willfulness by proving Walter's actions of consistently underreporting income, overspending cash, and collecting illegal income. The government can prove a deficiency through a combination of the net worth method and the expenditures method. Also, the government can prove Walter committed an affirmative act by showing the creation of false logs regarding the website donations and the concealment of his cash hoard that paid for his significant expenditures. Therefore, the government can convict Walter of the felony of tax evasion.

The government could convict Walter for making and subscribing a false document by proving Walter willfully made, and subscribed to, a materially false return, signed under the penalties of perjury, that he did not believe to be true and correct. The government can prove willfulness by proving Walter's actions of consistently underreporting income, overspending cash, and collecting illegal income. The government can prove a return was made and subscribed by proving Walter filed annual income tax returns, whether by mail or electronically. Through the net worth method and expenditures method, the government can prove Walter had unreported income, which proves that his return was materially false. Because the filed tax return contains a jurat, Walter signed under the penalties of perjury. The government can prove that Walter knew the return was not true and correct because he signed the return, which is a presumption of belief of accuracy. Therefore, the government could convict Walter of the felony of making and subscribing a false document. Walter would suffer serious consequences upon conviction, facing years in a federal prison.²⁶¹

261. The penalty for each of these felonies under the Federal Sentencing Guidelines starts by determining the tax loss. U.S. SENTENCING GUIDELINES MANUAL § 2T1.1(a) (2013). Assuming a tax loss of between \$80,000 and \$200,000, Walter would have a starting offense level of 16. *Id.* at §2T4.1. Two-point increases each for criminal source unreported income and sophisticated means increase his offense level to 20. *Id.* at §2T1.1(b). For a defendant with no prior criminal history, the sentencing guidelines range is 33-40 months. *Id.* at Sentencing Table. The judge may apply an upward variance up to the statutory maximum. *See* United States v. Booker, 543

VI. CONCLUSION

Just like Al Capone, Walter White deliberately avoids any record of his activities, eliminates any potential witnesses, and erases any evidence that would connect him to his criminal enterprise. However, the criminal enterprise does not encompass all of his criminal activity. Both Al Capone and Walter White committed tax crimes by failing to report their illegal source income, leading to pretextual criminal tax prosecution.

Walter White committed a felony by attempting to evade or defeat a tax by willfully attempting to evade the assessment of a tax. Walter willfully evaded tax, had a tax deficiency, and committed an affirmative act that constitutes an evasion or attempted evasion of the tax. The government can prove each of these elements. Additionally, Walter White committed a felony by filing a false return. Walter willfully made, and subscribed to, a materially false return, signed under the penalties of perjury, that he did not believe to be true and correct. The government can prove each of these elements. Therefore, Walter would be facing several years in federal prison.

Generally, the most successful drug traffickers are the most careful. The most careful drug traffickers are the most difficult to prosecute. Unfortunately, these high-level drug traffickers are also the highest value criminals for the government to prosecute. As demonstrated in the case of Walter White, the most careful drug trafficker can leave significant evidence for a criminal tax prosecution.

Commentators have roundly criticized pretextual prosecutions, arguing that the government should minimize the use of pretextual prosecutions. Some have raised legitimate concerns about the use, and potential abuse, of pretextual prosecutions. Federal prosecutors have exercised reasonable restraint in the use of criminal tax pretextual prosecutions since their inception in 1920. However valid the argument for potential abuse may be, over eighty years have passed since the first such prosecutions without any significant claims of prosecutorial abuse. Commentators condemn pretextual prosecutions as an avenue of stifling dissent, a reduction of state legitimacy, and an erosion in the credibility of the justice system. Criminal tax defendants, unlike material witness detainees, are not subject to pretextual prosecutions for any constitutionally protected activity. This should eliminate concerns of using criminal tax pretextual prosecutions to deprive individuals of constitutionally protected rights. Arguments of federalism and state legitimacy are also valid, but better suited to more pressing and impactful areas of the law.²⁶² Criminal tax prosecutions have morphed from the “technicality” that caught Capone into a tool used to ensure compliance.²⁶³ Eighty years of pretextual prosecutions have yet to erode public confidence in the judicial system sufficient to warrant a reconsideration of the use of criminal tax pretextual prosecutions. These prosecutions serve a valuable dual purpose, providing a

U.S. 220 (2005).

262. See, e.g., John Dinan, *Contemporary Assertions of State Sovereignty and the Safeguards of American Federalism*, 74 ALB. L. REV. 1637 (2011); Gillian E. Metzger, *Federalism under Obama*, 53 WM. & MARY L. REV. 567 (2011); Rachael Rawlins & Robert Paterson, *Sustainable Buildings and Communities: Climate Change and the Case for Federal Standards*, 19 CORNELL J. L. & PUB. POL'Y 335 (2010); Erin Ryan, *Negotiating Federalism*, 52 B.C. L. REV. 1 (2011); Mila Sohoni, *The Idea of “Too Much Law”*, 80 FORDHAM L. REV. 1585 (2012); Amy Widman, *Advancing Federalism Concerns in Administrative Law Through a Revitalization of State Enforcement Powers: A Case Study of the Consumer Product Safety and Improvement Act of 2008*, 29 YALE L. & POL'Y REV. 165 (2010).

263. See Elizabeth Branham, *Closing the Tax Gap: Encouraging Voluntary Compliance Through Mass-Media Publication of High-Profile Tax Issues*, 60 HASTINGS L.J. 1507 (2009).

method of prosecuting dangerous criminals and promoting compliance with tax laws.

Despite all the arguments against pretextual prosecutions, no one can argue that criminals such as Walter White, Al Capone, and Muhamed Mubayyid should be free to continue producing narcotics, bootlegging, racketeering, and fundraising for terrorists. Although these criminals have merely committed, as one commentator states, the “lowly offense of income tax evasion,”²⁶⁴ each has committed a felony. Society deserves to be free from the crimes perpetrated by these individuals and the public demands accountability. Pretextual prosecutions, so long as not baseless prosecutions, are a valuable tool for prosecutors, which should be employed in a regular and reasonable manner.

264. Barnes, *supra* note 32, at 1646.