

# Criminal Tax Bulletin

Department of Treasury  
Internal Revenue Service

Office of Chief Counsel  
Criminal Tax Division

March - September

This bulletin is for informational purposes. It is not a directive.

2009

## SIXTH AMENDMENT

### **Supreme Court Holds Forensic Analysts Are Witnesses Subject to Defendant's Right to Confrontation**

In *Melendez-Diaz v. Massachusetts*, 129 S. Ct. 2527 (2009), the Supreme Court held that “certificates of analysis” prepared by forensic analysts for use in criminal trials are testimonial statements and that the analysts are witnesses subject to the defendant’s right to confrontation under the Sixth Amendment.

Following police surveillance of his activities in a parking lot, Luis Melendez-Diaz (“Melendez-Diaz”) was arrested along with three other men. The police submitted plastic bags seized from the suspects to a state laboratory for forensic testing. The laboratory provided three notarized “certificates of analysis” reporting that the bags contained cocaine. Based on this evidence, Melendez-Diaz was charged with drug trafficking.

At trial, Melendez-Diaz objected to the admission of the certificates into evidence on the grounds that the Sixth Amendment and the Supreme Court’s decision in *Crawford v. Washington*, 541 U.S. 36 (2004) required the forensic analysts to testify in person. The trial court overruled the objection, and the certificates were admitted as *prima facie* evidence of the composition of the seized substance. The jury found Melendez-Diaz guilty. On appeal, the Massachusetts Appeals Court affirmed, and the Massachusetts Supreme Judicial Court denied review.

The U.S. Supreme Court granted certiorari and reversed the Massachusetts Appeals Court’s decision. The Supreme Court concluded that the certificates were testimonial statements because they were written declarations of fact made under oath for the purpose of establishing a fact and were therefore the functional equivalent of witnesses providing live testimony. Accordingly, the Court held that Melendez-Diaz had the right to be confronted with the forensic analysts who prepared the certificates, absent a showing that the

analysts were unavailable to testify at trial and that Melendez-Diaz had a prior opportunity to cross-examine them.

In reaching this conclusion, the Court rejected the argument that the certificates were not subject to the right to confrontation because they resulted from neutral, scientific testing. The Court attributed this argument to the notion that evidence with “particularized guarantees of trustworthiness” was admissible without confrontation – a theory rejected in *Crawford*. The Court also discussed whether the certificates were admissible without confrontation under the hearsay exception for official or business records, and concluded that they were not. The Court explained that the certificates were not official or business records because they were created for use at trial.

Because the state did not establish that the forensic analysts were unavailable and Melendez-Diaz did not have the opportunity for prior cross-examination, the Court concluded that he was entitled to be confronted with the analysts at trial.

## IDENTITY THEFT

### **Supreme Court Holds Aggravated Identity Theft Statute Requires Proof Defendant Knew Means of Identification Belonged to Another Person**

In *Flores-Figueroa v. United States*, 129 S. Ct. 1886 (2009), the Supreme Court held that 18 U.S.C. § 1028A(a)(1), the “aggravated identity theft” statute, requires the government to show the defendant knew the means of identification he or she unlawfully transferred, possessed, or used belonged to another person.

Ignacio Carlos Flores-Figueroa (“Flores-Figueroa”), was a Mexican citizen who used false identification to secure employment in the United States. In 2000, he gave his employer a false name, birth date, and Social Security number, along with a counterfeit alien registration card. The identifying information he provided was not that of a

real person. Subsequently, in 2006, Flores-Figueroa presented his employer with new counterfeit Social Security and alien registration cards that used his real name but had numbers that were assigned to other people.

The government charged Flores-Figueroa with entering the U.S. without inspection and misusing immigration documents, along with aggravated identity theft under 18 U.S.C. § 1028A(a)(1). Flores-Figueroa moved for a judgment of acquittal on the aggravated identity theft counts, claiming that the government could not prove he knew the numbers on the counterfeit documents were assigned to other people. The district court accepted the government's argument that it need not prove such knowledge and found Flores-Figueroa guilty of the predicate crimes and aggravated identity theft. The Eighth Circuit affirmed.

The Supreme Court granted certiorari to consider the "knowledge" issue. Finding the legislative history of the statute inconclusive, the Court rejected the government's position on textual grounds, noting that the statute's word "knowingly" appeared to apply to all elements of the crime. Further, the Court stated that the clarity of the statute was not outweighed by the practical difficulties of proving knowledge in this context.

Concluding that § 1028A(a)(1) required the government to show the defendant knew the means of identification belonged to another person, the Court reversed and remanded to the Eighth Circuit for reconsideration.

## **SEARCH AND SEIZURE**

### **Supreme Court Narrows Application of Search-Incident-to-Arrest Exception to Warrant Requirement**

In *Arizona v. Gant*, 129 S.Ct. 1710 (2009), the Supreme Court held that the search-incident-to-arrest exception to the Fourth Amendment's warrant requirement applies to a vehicle search only if the officers executing the search reasonably believe that either (1) the target could access the vehicle during the search; or (2) the vehicle contains evidence of the crime of arrest.

Rodney Gant ("Gant") was arrested for driving with a suspended license. After he had been handcuffed and locked in a patrol car, police officers searched his car and discovered a bag of cocaine. Gant was charged with drug possession.

At trial, Gant moved to suppress the bag of cocaine on

the ground that the search-incident-to-arrest exception did not apply to his situation. The trial court denied his motion to suppress, and the jury found him guilty. On appeal, the Arizona Supreme Court reversed, holding that the search-incident-to-arrest exception did not justify the warrantless search. The United States Supreme Court granted certiorari and affirmed the appellate court's decision.

Clarifying its prior holding in *New York v. Belton*, 453 U.S. 454 (1981), the Court noted that the search-incident-to-arrest exception "derives from interests in officer safety and evidence preservation that are typically implicated in arrest situations." 129 S.Ct. at 1716. Accordingly, the Court held that police may search a vehicle incident to arrest only when the arrestee is unsecured and within reach of the vehicle, or if it is reasonable to believe the vehicle contains evidence relevant to the crime of arrest. Because neither rationale justified the search of Gant's car, the Court concluded that the search was unreasonable.

### **Ninth Circuit Applies *Gant* to Vehicle Search on Remand**

In *United States v. Gonzalez*, 578 F.3d 1130 (9th Cir. 2009), a vehicle search case remanded by the Supreme Court, the Ninth Circuit held that the Court's decision in *Arizona v. Gant*, 129 S.Ct. 1710 (2009), required that the defendant's motion to suppress be granted and his conviction be reversed.

Police conducted a traffic stop of a car in which Ricardo Gonzalez ("Gonzalez") was riding and arrested another passenger for outstanding warrants. While Gonzalez was handcuffed and secured in a patrol vehicle, the police searched the passenger compartment of the car and found a loaded weapon. Based on this evidence, Gonzalez was convicted of unlawful possession of a firearm. At trial, he claimed that the search violated the Fourth Amendment. The district court disagreed and denied his motion to suppress the firearm. On appeal, the Ninth Circuit affirmed, citing the Supreme Court's holding in *New York v. Belton*, 453 U.S. 454, 460 (1981), which the court interpreted as permitting a warrantless vehicle search incident to the arrest of an occupant of the vehicle.

The Supreme Court vacated the Ninth Circuit's decision and remanded the case for further consideration in light of the Court's April 2009 ruling in *Arizona v. Gant*, which limited the search-incident-to-arrest exception for vehicle searches to situations in which the arrestee is within reach of the vehicle or it is reasonable to believe the vehicle contains evidence of the offense of arrest.

On remand, the government argued that the search was in good faith under the then-prevailing interpretation of *Belton*, but the Ninth Circuit declined to apply the good faith exception under these circumstances. Holding that *Gant* required suppression of the evidence derived from the search, the court reversed Gonzalez's conviction.

### **Ninth Circuit Introduces New Procedural Requirements for Computer-Related Searches and Seizures**

In *United States v. Comprehensive Drug Testing, Inc.*, 579 F.3d 989 (9th Cir. 2009), an en banc opinion involving the search of a non-suspect third party's computers, the Ninth Circuit set forth new procedures for the search and seizure of electronic data containing commingled seizable and non-seizable records.

In 2002 the government began investigating a laboratory suspected of providing steroids to professional baseball players. The same year, the Major League Baseball Players Association agreed to suspicionless drug testing of all players on the condition that the results would remain confidential. Comprehensive Drug Testing, Inc. ("CDT") administered the drug testing program and maintained the results in its computer database.

In the course of the investigation, federal agents learned that ten players had tested positive for steroids. The government obtained a warrant to search CDT's facilities for the records of those ten individuals. Although the records sought were only those of the ten identified players, the warrant authorized the wholesale seizure of computers containing the records of hundreds of other individuals. The warrant stated that the data would be segregated by computer personnel prior to review by the investigating agents. Once the computers were seized, however, the investigating agents themselves reviewed all the data and used their findings to expand their investigation.

Pursuant to Federal Rule of Criminal Procedure 41(g), CDT and the players moved for the return of the records seized. The district court ordered the seized property returned, with the exception of materials pertaining to the ten identified players. The government appealed, and, after a partial reversal by a divided panel of the Ninth Circuit, the circuit court reviewed the case *en banc* and affirmed.

On appeal, the government argued that it was not required to return any records showing steroid use by other players because that evidence was in plain view

once the investigating agents examined the seized materials. The Ninth Circuit rejected this application of the plain view doctrine and held that the agents' review of information not covered by the warrant amounted to unlawful conduct.

The court concluded by setting forth the following guidelines for computer-related searches and seizures:

1. Magistrates should insist that the government waive reliance upon the plain view doctrine in digital evidence cases. ...
2. Segregation and redaction must be either done by specialized personnel or an independent third party. ...
3. Warrants and subpoenas must disclose the actual risks of destruction of information as well as prior efforts to seize that information in other judicial fora. ...
4. The government's search protocol must be designed to uncover only the information for which it has probable cause, and only that information may be examined by the case agents. ...
5. The government must destroy or ... return non-responsive data, keeping the issuing magistrate informed about when it has done so and what it has kept.

579 F.3d at 1006. The court described these procedures as a means of preventing the segregation of seizable electronic data from becoming "a vehicle for the government to gain access to data which it has no probable cause to collect." *Id.*

### **Ninth Circuit Establishes Test for Standing to Challenge Search of Business Premises and Applies Partial Suppression to Overbroad Seizure**

In *United States v. SDI Future Health, Inc.*, 568 F.3d 684 (9th Cir. 2009), the Ninth Circuit set forth a test for determining a shareholder/officer's standing to challenge a search of workplace areas beyond his or her internal office. In addition, the court held that the search warrant at issue was overbroad and that partial suppression should have been granted.

The defendants – a medical diagnostic testing company and two of its shareholders/officers – were targets of an

IRS-led search of the company's premises. Following the search, they were indicted for health care fraud, tax evasion, and other offenses. They filed a motion to suppress the evidence obtained in the search, arguing that the warrant was vague and overbroad. The district court granted total suppression of the items seized.

On appeal, the circuit court held that, in order to challenge the search of a workplace, an individual must show a personal connection to the places searched and the materials seized. The strength of this connection, the court explained, should be assessed with reference to the following factors: (1) whether the item seized was personal property or kept in a private place; (2) whether the individual had custody or control of the item when it was seized; and (3) whether the individual took precautions on his own behalf to secure the place searched or the things seized. Concluding that the record was not adequately developed on these points, the court remanded the case for further fact-finding.

The court then turned to the company's claim that the warrant was insufficiently particular and overbroad. Although it concluded that the warrant properly incorporated the affidavit and was therefore sufficiently particular in describing the items to be seized, the court determined that five of the categories of items listed in the warrant were overbroad because probable cause did not exist to seize everything in those categories. In the absence of evidence that the agents relied on the affidavit to limit their search, the court declined to apply the good faith reliance exception.

Because the overbroad categories concerned a relatively small subset of the items to be seized, the court held that partial, rather than total, suppression should have been granted.

### **District Court Holds Freezing Assets of Suspected Terrorist Organization Violated Fourth Amendment**

In *KindHearts for Charitable Humanitarian Development, Inc. v. Geithner, et al.*, No. 3:08CV2400, 2009 WL 2514057 (N.D. Ohio Aug. 18, 2009), the district court granted the plaintiff's motion for partial summary judgment on the ground that the Treasury's Office of Foreign Assets Control ("OFAC") violated the Fourth Amendment when it froze the plaintiff's assets without obtaining a warrant.

KindHearts for Charitable Humanitarian Development, Inc. ("KindHearts"), was a non-profit corporation with the stated goal of providing humanitarian aid without

regard to religious or political affiliation. OFAC alleged that KindHearts provided material support to Hamas, a Specially Designated Global Terrorist ("SDGT"). In 2006, without obtaining a warrant, OFAC blocked all of KindHearts' assets pending investigation into whether KindHearts itself should be designated an SDGT. At the time this case was decided, the organization's assets remained frozen, although OFAC had not designated KindHearts an SDGT. KindHearts challenged OFAC's actions in district court, alleging that the block violated the Fourth Amendment.

The district court began its analysis by examining whether the Fourth Amendment was applicable. First, noting that interference with a target's possessory interest in property is sufficient to trigger Fourth Amendment scrutiny, the court concluded that OFAC's block was a "seizure" in Fourth Amendment terms. Second, the court reasoned that, as an American corporation with assets derived from U.S. residents, KindHearts was entitled to Fourth Amendment protection. Third, the court determined that applying the Amendment to OFAC's blocking actions would be consistent with the Amendment's historic role in preventing the abuse of governmental power. Finally, based on its reading of case law, the court rejected the government's argument that deference to the executive branch in matters of national security precluded application of the Fourth Amendment in this case.

Having determined that the Fourth Amendment was applicable to OFAC's blocking of KindHearts' assets, the court next addressed whether this action satisfied Fourth Amendment requirements. In the absence of a recognized exception, the court observed, a seizure is "reasonable" under the Fourth Amendment only when conducted with a judicial warrant supported by probable cause. Noting that the government had not explained why it lacked sufficient time to obtain a warrant before imposing the block, the court concluded that no exception to the warrant requirement applied to OFAC's actions. The court held that, under current law, OFAC's warrantless blocking of KindHearts' assets did violate the Fourth Amendment.

## **CORPORATE DIVERSIONS**

### **Ninth Circuit Holds Offer of Proof Insufficient to Support Return-of-Capital Theory in *Boulware* Remand**

In *United States v. Boulware*, 558 F.3d 971 (9th Cir. 2009), a corporate diversion case remanded by the Supreme Court, the Ninth Circuit examined the record to determine whether the defendant's offer of proof was sufficient to justify his presentation of a return-of-capital theory to the jury. Applying the guidelines set forth in *Boulware v. United States*, 128 S.Ct. 1168 (2008), the circuit court concluded that the defendant's offer of proof was insufficient, and it affirmed the district court's denial of the proffer.

Michael Boulware ("Boulware") diverted more than \$10 million from his closely-held corporation without reporting it on his personal income tax returns. He was convicted of tax evasion and filing false tax returns. As part of his defense, Boulware proffered evidence of the corporation's lack of earnings and profits to support his theory that the diverted funds were nontaxable returns of capital. The government moved to bar the evidence on the grounds that a return-of-capital defense required a showing that the distribution was intended to be a return of capital. The district court granted the motion, and the Ninth Circuit affirmed.

The Supreme Court vacated the Ninth Circuit's decision. The Court explained that the existence of a tax deficiency is an essential element of tax evasion under 26 U.S.C. § 7201 and noted that the deficiency determination in this case turned on 26 U.S.C. §§ 301 and 316(a). Because sections 301 and 316(a) did not have an intent requirement, the Court concluded that the existence of a deficiency did not depend on intent. Holding that a diverter of corporate funds facing charges of criminal tax evasion could claim return-of-capital treatment without producing evidence of intent, the Court remanded the case to the Ninth Circuit.

The circuit court interpreted the Supreme Court's opinion as setting forth three elements necessary to the assertion of the theory: "(1) a corporate distribution with respect to a corporation's stock, (2) the absence of corporate earnings or profits, and (3) the stockholder's stock basis be in excess of the value of the distribution." 558 F.3d at 975. Like the Supreme Court, the circuit court declined to define the requirements for proving that a distribution was with respect to stock, but it did indicate that intent is not among these requirements. Instead, it stated that "at the very least a taxpayer must tender some evidence of

nexus between the corporate distribution and stock ownership, or show that there were no other alternate explanations, in order to proceed with a return of capital theory at trial." *Id.* at 977. Applying this standard, the court found that Boulware had failed to show that the distribution was with respect to the corporation's stock.

The court declined to discuss the second element of the return-of-capital theory, *i.e.*, the absence of corporate earnings and profits, because it was included in Boulware's offer of proof. With respect to the third element – the stockholder's basis – the court concluded that the evidence tendered was insufficient to show that Boulware had a stock basis in excess of the \$10 million he received. Based on Boulware's failure to satisfy two of the three requirements for the return-of-capital theory, the circuit court affirmed the trial court's decision to preclude him from presenting this theory to the jury.

## **MONEY LAUNDERING**

### **First Circuit Holds Failure to File Tax Returns May Be Act in Furtherance of Money Laundering Conspiracy**

In *United States v. Upton*, 559 F.3d 3 (1st Cir. 2009), the First Circuit affirmed the defendant's conviction for money laundering conspiracy, holding that the conspirators' failure to file tax returns extended the life of the conspiracy, and therefore the conviction was not barred by the statute of limitations.

In 1997, George Upton ("Upton") and his girlfriend stole \$900,000 in cash. They divided part of the stolen cash among several individuals, who deposited it into their personal bank accounts and purchased thirteen cashier's checks made out to Upton and his girlfriend. Upton and his girlfriend used the checks to purchase a piece of real property, which they rented out and then sold in January 1999 at a profit. They neglected to report the stolen funds and the rental income on their tax returns, and neither of them filed a 1999 tax return. Upton was ultimately convicted of money laundering conspiracy and tax offenses, but he appealed only the money laundering conspiracy conviction.

On appeal, Upton argued that the conviction was barred by the statute of limitations, claiming there was no evidence that the conspiracy continued to a time within five years of the May 12, 2004 superseding indictment. He characterized his tax offenses, which occurred in 2000, as acts intended to cover up the conspiracy after its termination, rather than acts in furtherance of the conspiracy.

The circuit court noted that a conspiracy endures as long as the co-conspirators endeavor to attain the “central criminal purposes” of the conspiracy. Here, the indictment had charged Upton with money laundering conspiracy under 18 U.S.C. §§ 1956(a)(1)(B), which prohibits financial transactions designed to conceal or disguise certain characteristics of the proceeds of unlawful activity. The court cited *Cuellar v. United States*, 128 S.Ct. 1994 (2008), to support its conclusion that the statute requires the government to prove there was a purpose or plan to conceal or disguise, *i.e.*, that concealing or disguising certain attributes of the funds was the central objective of the conspiracy. To avoid the statute of limitations bar, the government also had to prove that one of the tax offenses was in furtherance of this objective.

The court held that the jury reasonably could have found that Upton's failure to file the 1999 return was in furtherance of the central objective of the conspiracy because, by failing to report the profits from the sale of real property purchased with the stolen funds, Upton facilitated the concealment aim of the money laundering transactions. The court explained its holding as follows:

Where ... the substantive crime that is the object of the conspiracy has the intent to conceal as an element, the success of the conspiracy itself may depend on further concealment. Consequently, additional acts of concealment that facilitate the central aim of the conspiracy are in furtherance of the conspiracy.

559 F.3d at 13. Because the evidence of the conspirators' failures to file 1999 tax returns was sufficient for the jury to conclude that the conspiracy lasted at least until May 12, 1999, the circuit court concluded that Upton's conspiracy conviction was not time-barred.

## **SENTENCING**

### **Third Circuit Holds Sentencing Judge May Consider Variance on Basis of Fast-Track Disparity**

In *United States v. Arrelucea-Zamudio*, No. 08-4397. 2009 WL 2914495 (3d Cir. Sept. 14, 2009), the Third Circuit held that a sentencing judge has the discretion to consider a downward variance on the basis of a disparity in sentencing among immigration defendants in fast-track and non-fast-track districts.

Pedro Manuel Arrelucea-Zamudio (“Arrelucea”) illegally

entered the United States in 1979. In 1991 he was convicted of a narcotics offense and subsequently deported to Peru. In 2000, he illegally reentered the United States. He was arrested in 2006 for another narcotics offense and was sentenced to five years imprisonment. After serving 15 months, he was indicted on one count of illegal reentry, in violation of 8 U.S.C. § 1326(a) and (b)(2), to which he pleaded guilty. At his sentencing, which took place in a district that did not have a fast-track program for immigrant defendants, he argued for a downward variance based on the disparity in sentences between fast-track and non-fast-track districts. The district court rejected this argument, concluding that it was precluded from considering a variance on this basis as a matter of law, and sentenced him to 48 months' imprisonment.

On appeal, Arrelucea challenged the district court's rejection of his fast-track argument. The Third Circuit analogized the case to *Kimbrough v. United States*, 128 S.Ct. 558 (2007), in which the Supreme Court held that a district court may deviate from the Guidelines range for crack cocaine offenses if it concludes that the disparity between ranges for crack and powder cocaine results in a sentence greater than necessary to achieve the objectives of 18 U.S.C. § 3553(a). Applying the logic of *Kimbrough* to the fast track/non-fast track disparity, the circuit court concluded that the sentencing judge was not barred from considering a variance on this basis when evaluating the applicable § 3553(a) factors to determine the sentence. The court noted that, to justify a reasonable variance by the district court, a defendant must show that he would have qualified for fast-track disposition in a fast-track district, and that he would have taken the fast-track guilty plea if offered.

Because the district court incorrectly believed it was precluded from considering the defendant's fast-track argument, the circuit court vacated Arrelucea's sentence and remanded the case for reconsideration.

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