

High-Profile Lawyer Indicted for Old-School Tax Obstruction

By Donald P. Board • Wood LLP

Under Code Sec. 7212(a), anyone who “corruptly ... obstructs or impedes, or endeavors to obstruct or impede, the due administration of [Title 26]” can be fined \$5,000 or imprisoned for up to three years. In *C.J. Marinello* [S.Ct., 138 S.Ct 1101 (2018)], the Supreme Court held that Code Sec. 7212(a) does not apply unless the defendant’s obstructive conduct is directed at a pending, or at least reasonably foreseeable, audit or other administrative proceeding. Predictably, the courts are now dealing with a wave of challenges to convictions for obstruction under Code Sec. 7212(a) and similar federal obstruction statutes.

The Fourth Circuit, for example, recently considered whether a taxpayer who submitted fake documents to a U.S. Attorney’s office could be convicted of attempting to obstruct a pending grand jury proceeding in violation of 18 USC §1512(c). [See *P.E. Sutherland*, CA-4, 921 F3d 421 (2019).] Invoking *Marinello*, the defendant argued (unsuccessfully) that the government had failed to establish the required nexus between his attempt to mislead the U.S. Attorney and what was happening in the grand jury room.

We can count on plenty more cases exploring the scope of obstruction. The indictment of Michael Avenatti, on the other hand, charges the high-profile lawyer with conduct that seems to fall squarely within Code Sec. 7212(a). We should note at the outset that Mr. Avenatti has not been convicted of anything, and that he is entitled (as he has tweeted) “to a FULL presumption of innocence.”

The 36-count indictment, made public on April 11, 2019, charges Mr. Avenatti with embezzling millions of dollars of settlement funds that had been wired to his various client

trust accounts. On the tax side, it alleges that Mr. Avenatti failed to file personal and business tax returns, failed to pay over payroll taxes, and obstructed or impeded the IRS in violation of Code Sec. 7212(a).

The indictment describes Mr. Avenatti as the “effective owner” of Global Baristas, LLC (GB LLC), a holding company that owns 100 percent of Global Baristas US LLC (GBUS). GBUS operated Tully’s Coffee, a troubled chain of stores peddling java in California and Washington. The indictment asserts that GBUS failed to pay over about \$3.2 million in employment taxes during 2015–2017, including \$2.4 million withheld from its employees’ paychecks.

The IRS initiated a collection action in September 2016. In October, an IRS revenue officer spoke with Mr. Avenatti, who claimed (falsely, according to the government) that he was not involved in GBUS’s finances, and that he was unaware of any failure to pay over payroll taxes. From this point forward, Mr. Avenatti would have been aware of the pending proceeding for *Marinello* purposes.

In June 2017, the IRS filed a \$5 million tax lien against GBUS in Washington. In August, the IRS started sending levy notices to financial institutions and companies associated with GBUS. Early in September, according to the indictment, Mr. Avenatti directed Tully’s Coffee to stop depositing cash into GBUS’s usual bank account, which he knew was subject to an IRS levy notice. The stores were ordered to make deposits to an account at Bank of America instead.

That may not have been a great idea. The indictment alleges that the BofA account was associated with GB Autosport, LLC, the

entity that managed Mr. Avenatti's personal car racing team. (Mr. Avenatti has competed at Le Mans and Daytona.) By the end of 2017, about \$860,000 of coffee-company cash had been deposited into the GB Autosport account.

The indictment also alleges that Mr. Avenatti changed the name, EIN, and bank account information associated with GBUS's merchant credit card processing accounts, on which the IRS had also levied. Mr. Avenatti substituted GB LLC for GBUS, and he provided information about a new bank account that had been established in GB LLC's name. In December 2017, Mr. Avenatti allegedly caused GBUS to open a fresh set of merchant accounts for Tully's Coffee in GB LLC's name.

None of this sounds good. But if Mr. Avenatti was corruptly attempting to obstruct the IRS, it seems at least slightly odd that he would move GBUS's receipts into two closely related entities. GB LLC, after all, was GBUS's only member, and GB Autosport was a vehicle for pursuing an expensive hobby. Both of these entities would (or should) have been flashing on the IRS's radar screen. But even a futile attempt to impede the IRS violates Code Sec. 7212(a), provided that the defendant acts with corrupt intent.

Mr. Avenatti has tweeted that he is "confident that justice will be done once ALL of the facts are known." When the issue is intent, the significance of a series of financial transactions can be a matter of interpretation. We need to hear Mr. Avenatti's side of the story.

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