

# LAW OFFICES OF SANFORD I. MILLAR

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## **You're being audited; do you need a Lawyer?**

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Not all audits are the same and therefore not all response approaches should be the same. There is a type of audit, referred to as an "egg shell" audit which requires legal more than accounting advice. An "egg shell" audit is where the taxpayer knows of specific omissions of income, false statements or illegal conduct that if discovered could result in a criminal referral (tax fraud or evasion, false statement crimes, money laundering). Examples of omissions of income, include unreported income from offshore bank accounts and unreported income from illegal gambling. Examples of false statements would be deliberate misclassification of marital status, mischaracterization of cash payments as to a deductible expense item when the payment was for an improper action, like bribery or payments for illegal labor. The point is the taxpayer knows the nature and extent of the problem conduct and should be represented by counsel at an early stage.

The reason a lawyer should be involved early is that communications with a lawyer, are generally subject to the attorney client privilege, as to the disclosure of the actions, whereas there is no taxpayer accountant privilege as to items on the return. The approach to an "egg shell" audit requires full and frank disclosure between the taxpayer client and the attorney which is facilitated by the privilege. All statements made and documents provided to the auditor need to be screened by counsel for accuracy and completeness to insure that no new "false statements" are made.

Counsel may wish to retain an accountant under a work product letter (known as a Kovel letter) who would analyze the returns in question and report back to counsel. The use of an independent accountant is very important in maintaining privileges and aiding the lawyer in making recommendations to the taxpayer.

Accountants who prepared the return under exam may find that it can be difficult to know just when to bring in lawyers, particularly when the accountant does not know all the facts himself/herself. But, once the client tells the accountant enough to put the accountant on notice that there are possible criminal issues a lawyer should be brought in. It is the best advice for the client and the safest response for the accountant.

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