

Tax Litigation Issues

Expert Analysis

‘United States v. Sertich’: Affirmative Obligations of Taxpayers

Under the Internal Revenue Code, employers are responsible for accounting for and paying over to the IRS taxes that they withhold from their employees. In *United States v. Sertich*, 879 F.3d 558 (5th Cir. 2018), the U.S. Court of Appeals for the Fifth Circuit held that an employer who willfully fails *either* to account for *or* to pay over such taxes commits a felony under 26 U.S.C. §7202. In so holding, the court rejected the defendant’s argument that the statute’s use of the conjunctive “and” means that it is only violated when the employer breaches *both* the obligation to account for *and* the obligation to pay over the withheld taxes. The Fifth Circuit in *Sertich* also rejected the defendant’s claim that the government had failed to establish that he had willfully violated his tax obligations.

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‘Sertich’

In 2015, Anthony P. Sertich Jr., a plastic surgeon and owner of two medical entities, was indicted in the Western District of Texas on 10 counts of failing to remit to the IRS payroll taxes that he had withheld from employees between 2008 and 2010, in violation of §7202, and on one count of tax evasion, in violation of §7201. At trial, the jury heard evidence that, while Sertich had filed accurate statements reflecting the withheld taxes, he had used the withheld funds to pay himself millions of dollars and had engaged in extensive efforts to avoid paying over \$2.9 million to the IRS.

Specifically, the government established that, starting in 2004, Sertich filed numerous bankruptcy petitions in an effort to block the IRS’s attempts to collect past due payroll taxes. Each of these petitions, however, was dismissed when Sertich failed to make scheduled payments. Sertich also attempted to avoid his payment obligations by closing one

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entity—South Texas Otorhinolaryngology (STO)—and moving himself and all of his employees to a second entity, Advanced Artistic Facial Plastic Surgery of Texas (Advanced Artistic).

Several IRS officers testified regarding their attempts to contact

Sertich to encourage him to pay over the withheld payroll taxes. Sertich failed to comply with those requests and in 2007 the IRS levied his bank accounts. Sertich apparently evaded this and other levies by using cashier's checks to pay his employees. The government also presented evidence that Sertich's accountants and lawyers had repeatedly warned him that he needed to pay the taxes he owed to the IRS on a timely basis.

After a five-day trial, the jury convicted Sertich on all counts, and he was sentenced to 41 months' imprisonment and ordered to pay more than \$2.9 million in restitution. On appeal, Sertich argued that the trial court's jury instruction on the elements of Section 7202 was erroneous, and that the evidence was insufficient to establish that he had acted with the requisite willfulness.

Section 7202

Section 7202 provides that "[a]ny person required under this title to collect, account for, and pay over any tax imposed by this title who willfully fails to collect or truthfully account for and pay over such tax shall ... be guilty of a felony." It was undisputed that Sertich had collected his employees' payroll taxes; rather, he was charged with having failed to "truthfully account for and pay over" the withheld taxes. While Sertich had accurately reported the withheld taxes, the government argued that a conviction could be predicated on evidence that Sertich

had *either* failed to account for *or* to pay such taxes over to the IRS. The trial court agreed with the government's reading of Section 7202 and instructed the jury that it could convict Sertich if he "failed to comply with one of the two duties."

On appeal, Sertich argued that Section 7202's use of the conjunctive "and" means that a violation only occurs if a person fails to meet *both* obligations. Sertich contended that the government's construction (i.e., reading the word "and" as if it meant the disjunctive "or") was inconsistent with the statute's plain language. Indeed, the Supreme Court has held that "and" presumptively should be read in its "ordinary" conjunctive sense, see *Crooks v. Harrelson*, 282 U.S. 55, 58-59 (1930), and it is a well-accepted rule of statutory construction that "and" and "or" "ordinarily ... are not interchangeable. ... The literal meaning of these terms should be followed unless it renders the statute inoperable or the meaning becomes questionable." 1A Norman J. Singer, *Statutes and Statutory Construction* §21.14 (7th ed. 2017).

The Fifth Circuit agreed with Sertich that §7202 identifies two responsibilities that must be read in the conjunctive, but nonetheless affirmed the district court's jury instruction. Thus, rather than requiring the government to establish that the defendant failed to comply with both duties, the Fifth Circuit joined the Second, Third and Ninth Circuits

in holding that §7202 creates a "dual obligation" to *both* (a) truthfully account for *and* (b) pay those taxes over to the IRS. See *United States v. Gilbert*, 266 F.3d 1180, 1183-85 (9th Cir. 2001); *United States v. Thayer*, 201 F.3d 214, 220-21 (3d Cir. 1999); *United States v. Evangelista*, 122 F.3d 112, 120-22 (2d Cir. 1997).

The Fifth Circuit reasoned that Sertich's proposed interpretation would create an absurd result of imposing a greater penalty on an employer who failed to collect taxes than on one who collected and truthfully accounted for the taxes, but then used the funds for his own purposes. In support of its conclusion, the Fifth Circuit pointed to *Slodov v. United States*, 436 U.S. 238 (1978), in which the Supreme Court construed §7202's civil counterpart, 26 U.S.C. §6672, and concluded that both statutes "were designed to assure compliance by the employer with its obligation to withhold *and* pay the sums withheld." The court also concluded that the statute was not sufficiently ambiguous to warrant application of the rule of lenity, but noted that, to the extent there was any ambiguity in the statute, the title of §7202—"[w]illful failure to collect *or* pay over tax"—supported its conclusion that the failure to pay over taxes was itself enough to sustain a conviction.

Willfulness

Sertich next argued that the evidence at trial was insufficient to

sustain his conviction under §7202 because it failed to establish that he had acted willfully, as required under *Cheek v. United States*, 498 U.S. 192 (1991). In *Cheek*, the Supreme Court defined “willfully” as requiring proof that “the defendant knew of [a legal duty imposed on him], and ... voluntarily and intentionally violated that duty.” The court further

found that Sertich willfully violated §7202, that the jury clearly rejected Sertich’s “loan” defense, and that it is not the court’s role to “second guess the jury in its choice of which witnesses to believe.”

Similarly, Sertich also contended that his purported good-faith belief that the withheld but unpaid funds constituted a loan undermines any finding that he acted with the willfulness necessary to support his conviction for tax evasion under 26 U.S.C. §7201. The court had little difficulty rejecting this argument in light of the multiple bankruptcy petitions that Sertich had filed in an attempt to halt the IRS’s collection efforts, with these petitions often being dismissed shortly after they were filed because Sertich had failed to make his required tax payments, and Sertich’s repeated interactions with the IRS through which he was clearly told that the taxes were due and owing. Thus, the Fifth Circuit emphasized that evidence of willfulness is often circumstantial and can be established by “any conduct, the likely effect of which would be to mislead or to conceal.” Accordingly, the court concluded that the jury could infer from Sertich’s “pattern of conduct” that he knew he was obligated to pay the taxes, and was voluntarily and intentionally evading payment. Considering the evidence in its totality, including Sertich’s occasional use of cashier’s checks to pay his employees in order to avoid having money in an

account that the IRS could levy, the court easily rejected Sertich’s claim of good faith.

Conclusion

While criminal statutes often set forth prohibited conduct, in *Sertich* the Fifth Circuit followed several other circuits in concluding that §7202 imposed affirmative duties that defendants must satisfy in order to *avoid* committing a crime. Thus, *Sertich* and its predecessors put defendants on notice that, although a criminal statute lists a series of acts using the conjunctive “and”, courts may nonetheless conclude that it imposes mandatory obligations, all of which must be *affirmatively fulfilled*. Moreover, *Sertich* also serves as an important reminder that, while the government bears the heightened burden to prove willfulness in criminal tax cases, that burden is not insurmountable, especially where the defendant’s claims of good faith may be viewed as implausible.

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held that a defendant’s good-faith belief that he was not violating any federal tax laws would negate the willfulness element.

At trial, Sertich—who took the stand in his own defense—claimed that he believed his tax delinquency represented an interest-bearing loan from the IRS, which he always intended to repay. The government rebutted that argument with evidence that IRS revenue officers and Sertich’s own accountants and attorneys had repeatedly told Sertich that he had a legal duty to pay over the withheld taxes. The Fifth Circuit observed that the government had presented substantial evidence from which a rational jury could have