



Dear Ethics Lawyer™

The Legal Ethics Project. Supporting professionalism with information.

Q: Dear Ethics Lawyer,

I am a tax lawyer with an accounting background. I practice in a smaller community and advise businesses on tax matters, as well as preparing tax returns for some of them. Today is the day that returns are due, and I have a dilemma concerning one of these clients. The owner of the business client has loaned several hundred thousand dollars from the business to his daughter, which she is using to start her own business. The loan is documented and she has been making payments on it, including interest, during the past year.

My client insists that these payments are an "informal family matter" that the IRS would never find out about, and does not want to include them as taxable income for purposes of the business's return. I have advised him that it is income that he is obligated to report, but he refuses to do so. What are my obligations? I do not wish to participate in tax fraud, but also do not want to breach an obligation to the client.

A: Tax day doesn't always bring out the best in humankind. You have correctly noted that you cannot be involved in a fraudulent act of your client. It is "professional misconduct" under Model Rule 8.4(b) and (c) "to commit a criminal act that reflects adversely on the lawyer's honesty" or to "engage in conduct involving dishonesty, fraud, deceit or misrepresentation." Model Rule 1.2(d) states that a lawyer "shall not counsel a client to engage, or assist a client, in conduct the lawyer knows is criminal or fraudulent, but a lawyer may discuss the legal consequences of any proposed course of conduct with a client." In addition, Model Rule 1.16 requires that lawyer to withdraw from a representation if the client "seeks to use or persists in using the lawyer's services to commit or further a crime or fraud." Added together, these rules first require what you have already done: counseling your client about the applicable law, and the consequences (additional taxes, penalties and interest, potential prosecution, etc.) of not following the law. If the client persists in the intention to fraudulently hide income you believe is required to be disclosed, then you must withdraw from the representation under Rule 1.16, doing nothing to assist the client in the fraudulent conduct.

This means that if this is a client for whom you normally prepare the return, you should withdraw without doing so, and without your name attached to or associated with the filing. If this issue has arisen at the last minute before the return is due, you may have to assist the client with the paperwork to obtain an extension. But again I

recommend you not associate your name with even this filing once you are unable to dissuade your client from proceeding with the conduct in question. You should also advise the client to seek additional legal advice.

Are you also required to make a disclosure of the client's intention to commit a tax fraud, to the IRS or anyone else? There are two matters to consider. Attorney-client privilege would ordinarily apply to the discussions with your client about what the law requires, and that privilege belongs to your client. There is an exception to privilege, however, for discussions pertaining to the intention to commit a crime or fraud, so that privilege may not apply here. But, even if not, Model Rule 1.6 comes into play. It requires the lawyer to keep confidential all "information relating to the representation of a client" unless the client consents to disclosure, or unless one of several exceptions set forth in subsection (b), which permit disclosure ("a lawyer may reveal information") applies. Rule 1.6(b)(2) and (3) are potentially implicated here. These subsections allow disclosure to prevent a client from committing crime or fraud that is reasonably certain to result in substantial injury to the financial interests or property of another, or to rectify or mitigate injury that has occurred, but only if the crime or fraud is one that "in furtherance of which the client has used or is using the lawyer's services." In this case, if you timely withdraw now, and do not associate your name or further services with the actual filing of a fraudulent return, these subsections would not apply. Of course, even if they did apply, then pursuant to Rule 1.6, you would be permitted (not required) to make a disclosure.

There is one other consideration that may apply here. If your client is an organization (e.g., a corporation or partnership), you must consider whether you have obligations under Rule 1.13(b). Under this rule, when a lawyer knows that a constituent of the organization intends to act in a manner related to the representation that is a violation of law that reasonably might be imputed to the organization and likely to result in substantial injury to the organization, then the lawyer must proceed in the best interests of the organization. This includes referring the matter to higher authority in the organization. In this case, if the business you represent has a higher officer than the constituent you are dealing with, you may be required to refer the matter to them (including to a board of directors, if applicable).

The Ethics Lawyer

About Dear Ethics Lawyer

The twice-monthly "Dear Ethics Lawyer" column is part of a training regimen of the Legal Ethics Project, authored by [Mark Hinderks](#), former managing partner and counsel to an AmLaw 132 firm; Fellow, American College of Trial Lawyers; and speaker/author on professional responsibility for more than 25 years. Mark leads Stinson LLP's [Legal Ethics & Professional Responsibility](#) practice, offering advice and "second opinions" to lawyers and law firms, consulting and testifying expert service, training, mediation/arbitration and representation in malpractice litigation. The submission of questions for future columns is welcome: please send to mark.hinderks@stinson.com.

Discussion presented here is based on the ABA Model Rules of Professional Conduct, but the Model Rules are adopted in different and amended versions, and interpreted in different ways in various places. Always check the rules and authorities applicable in your relevant jurisdiction – the result may be completely different.