Lessons from the Lynnette Harris and Leigh Ann Conley Cases

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Bernard McGuirk, the Executive Producer for the now discontinued daily radio show "IMUS In The Morning", for many years did a skit as Cardinal John O'Connor (Bishop of New York), during which he frequently posed the question, “Which doesn't belong and Why?” Applying that same question to the Internal Revenue Code ("IRC") results in the following takeaway, "love and passion do not belong with gross income, taxable income, gift tax, and the like." Yet, the federal tax law is replete with cases where distinguishing between love, services, and affection have played out. The cases of Lynnette Harris and Leigh Ann Conley, twin sisters, are instructive on the difference between payments for affection and payments for services. The magnitude of the cases is illustrated because these were *criminal* cases where the defendants received jail time by the United States District Court. The convictions and sentences of Harris and Conley were *reversed* by the Seventh Circuit Court of Appeals, the second-highest court in the United States. The Seventh Circuit framed the issue in this way:

David Kritzik, now deceased, was a wealthy widower partial to the company of young women. Two of these women were Leigh Ann Conley and Lynnette Harris, twin sisters. Directly or indirectly, Kritzik gave Conley and Harris each more than half a million dollars over the course of several years. For our purposes, either Kritzik had to pay gift tax on this money or Harris and Conley had to pay income tax. The United States alleges that, beyond reasonable doubt, the obligation was Harris and Conley's. In separate criminal trials, Harris and Conley were convicted of willfully evading their income tax obligations regarding the money…

Harris was sentenced to ten months in prison, to be followed by two months in a halfway house and two years of supervised release. She was also fined $12,500.00 and ordered to pay a $150.00 special assessment. Conley was sentenced to five months in prison, followed by five months in a halfway house and one year of supervised release. She was also fined $10,000.00 and ordered to pay a $100.00 assessment.

Were the payments for love or sex? In reversing the United States District Court, the Seventh Circuit examined Kritzik's motive for the payment. Of course, the evidence was sparse. The Department of Justice, which represented the prosecution, showed that Kritzik had not listed the payments on his IRS form 709, Gift Tax Return, and that on a bank card, Conley listed Kritzik as her “employer.” The Seventh Circuit was unpersuaded. The Court of Appeals stated that it would not permit a verdict based on “piling inference upon inference.” Whether intended as a pun, the Court stated:

"…the *bare facts* of Kritzik's gift tax return, the bank card, and the form of the payments are as consistent with an inference of innocence as one of guilt. (italics added)."

What does the holding mean? Good tax advice is always essential in any transaction.