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"DAY IN COURT" MAY BE COSTLY FOR FRIVOLOUS TAX CASE FILERS

WASHINGTON -- Getting their "day in court" has been an expensive proposition for some people who have recently faced stiff penalties from the Tax Court, Appeals Courts and District Courts for pursuing frivolous tax cases. The Internal Revenue Service warns that the courts are sending a clear message to others who may be considering such positions – they do so at their own risk.

"Congress was concerned about taxpayers misusing the courts and obstructing the appeal rights of others when it enacted tougher sanctions in the 1980s," said IRS Commissioner Charles O. Rossotti. "The courts are for resolving unclear issues of law, not a forum for repeating arguments that the courts have already rejected. Taxpayers intending to use the court as a soapbox should consider the potential cost."

The law allows the courts to impose a penalty of up to $25,000 when they come to any of three conclusions:

- a taxpayer instituted a proceeding primarily for delay,
- a position is frivolous or groundless, or
- a taxpayer unreasonably failed to pursue administrative remedies.

The courts' determination to use their sanctions authority to discourage the filing of frivolous tax suits is evident in some case documents which are public.

This month, the Tax Court penalized two California residents in separate cases for trying to avoid taxes through the use of trusts. On June 21, the Court said that Charles and Francesca Sigerseth of El Macero met all three of the above criteria and fined them $15,000. The Court pointed out that the case was "a waste of limited judicial and administrative resources that could have been devoted to resolving bona fide claims of other taxpayers." (Sigerseth v. Commissioner)

On June 7, the Court found that Andy Hromiko of Roseville, Calif., not his trust, was the true earner of income. It noted that he had made "shopworn arguments characteristic of the tax-protester rhetoric that has been universally rejected by this and other courts," and fined him $12,500. (Matrixinfosys Trust v. Commissioner)

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Last Dec. 4, the Tax Court imposed a $25,000 penalty against Hae-Rong and Lucy Ni, of San Jose, Calif. Contesting the IRS rejection of various deductions on their tax returns, the Nis were not responsive to orders for supporting records. Instead, they challenged the authority of the IRS to audit their returns and of the government to impose taxes. The Court concluded that the Nis had chosen "to pursue a strategy of noncooperation and delay, undertaken behind a smokescreen of frivolous tax-protester arguments." The Court also imposed sanctions of more than $10,600 against the Nis' attorney, Crystal Sluyter, for arguing frivolous positions in bad faith. (The Nis Family Trust v. Commissioner)

While at the Federal Prison Camp in Duluth, Minn., for tax evasion, Darlow Madge contended that he wasn't a taxpayer, that his income from selling hospital supplies wasn't taxable, and that only foreign income is taxable. On Dec. 7, the Tax Court imposed the maximum $25,000 fine after having warned Madge that continuing with his frivolous arguments would likely result in a penalty. (Madge v. Commissioner)

Regina Davis of Cincinnati, Ohio received a $4,000 penalty from the Tax Court on April 10 for frivolous and groundless arguments, including that the IRS is not an agency of the United States and that it is a function of the Puerto Rican Bureau of Alcohol, Tobacco and Firearms. Davis persisted in her contentions even after the Court warned her that she could be fined for doing so. (Davis v. Commissioner)

The Tax Court is not the only place for arguing tax cases. Other courts are also experiencing frivolous cases and imposing sanctions.

On Feb. 2, the Tenth Circuit Court of Appeals imposed an $8,000 penalty on Larry and Sandee Gass of Capulin, Col., for appealing district court decisions which rejected their contentions that taxes on income from real property are unconstitutional. The Appeals Court had earlier fined them $2,000 for using the same arguments in another case. (Gass v. U.S.)

Michele Brashier and Richard Hembree, of Tulsa, Okla., each drew $1,000 penalties on April 13 for arguing that requiring them to file sworn income tax returns violated their Fifth Amendment right against self-incrimination. The Tenth Circuit Court of Appeals noted that sanctions were warranted because the Tax Court had warned them that their argument -- rejected consistently for more than seventy years -- was frivolous. (Brashier v. Commissioner)

After losing the argument that his wages were not income and receiving a $500 penalty, Garnell McAfee, Jr., of Flowery Branch. Ga., returned to U.S. District Court in Northern Georgia to try to stop the government from collecting the penalty by garnishing his wages. On April 4, the judge stated that "bringing this ill-considered, nonsensical litigation before this court for yet a second time is nothing but contumacious foolishness which wastes the time and energy of the court system." He then imposed a $1,000 penalty, added 10 percent to the original penalty, and ordered McAfee to pay the U.S. Marshal's costs of serving the writ of garnishment on his employer. (McAfee v. U.S.)

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False Arguments For Noncompliance With The Tax Laws

The Internal Revenue Service is concerned that taxpayers might be misled by improper suggestions that they are not required to file tax returns or pay taxes.

Since shortly after the federal income tax was enacted in 1913, some individuals and groups have encouraged others not to comply with the law. There have been unsuccessful challenges about the applicability of tax laws using a variety of arguments. There have been assertions that the 16th Amendment was not properly ratified, that the tax law was unconstitutional, did not apply to certain types of income, only applied to certain individuals, or violated one or more constitutional rights.

Despite the courts having consistently rejected these arguments, their promoters continue to expound them, even incurring penalties for bringing frivolous cases into court or for filing frivolous tax returns. They often present their arguments in a pseudo-legal format, luring unsuspecting people into participating in their schemes to evade taxes.

Constitution-Related Arguments

First Amendment. These arguments focus on using the Freedom of Religion clause of the First Amendment to reduce income tax liability. A common scheme calls for individual taxpayers to obtain minister's credentials and a church or religious order charter by mail for a fee. The individuals set up a new organization that purports to be a church, religious order, or other religious organization. They then take a "vow of poverty" and assign their assets and income to the new organization. But filtering money through a purported church to fraudulently claim charitable contribution deductions is illegal. The tax law affords benefits to churches and other religious organizations and to those who make gifts or contributions to these organizations. The law requires, however, that such organizations actually be operated for religious purposes and not for the private benefit of individuals.

2. Fourth and Fifth Amendments. These arguments claim that filing an income tax return violates the Fourth Amendment right to privacy or the Fifth Amendment right against self-incrimination. However, the courts have consistently held that disclosure of routine financial information required on a tax return does not incriminate an individual or violate the right to privacy.

3. Sixteenth Amendment. These arguments claim that the constitutional amendment establishing the basis for income tax was never properly ratified. However, the courts have held that none of the points presented undermine the fact that the Sixteenth Amendment was indeed ratified in 1913.

Arguments Related to the Internal Revenue Code

These false arguments claim that:

- there is no Internal Revenue Code that imposes taxes;
- only "individuals" are required to pay taxes;
- Code Section 861 limits taxable income to certain sources which don't apply to most U.S. citizens; or
- the government can assess taxes only against people who file returns.

The tax law is found in Title 26 of the United States Code. Section 6012 of the Code makes clear that only people whose income falls below a certain minimum level do not have to file returns. Sections 861 through 865 determine whether income is from a U.S. or foreign source - they do not in any way exclude income from taxation for a U.S. citizen or resident. Section 6201 of the Code states that the Secretary of the Treasury is required to make assessments "of all taxes imposed by this title [Title 26]."

Trust Arguments

These arguments claim that forming a trust to receive your income and hold your assets will allow you to reduce or eliminate your tax liability. In truth, establishing a trust, foreign or domestic, for the sole purpose of hiding your income and assets from taxation is illegal and will not absolve you of your tax liability.

More information is available from the "Summary of Abusive Trust Schemes," prepared by the IRS Criminal Investigation Division. A copy is available via the Internet at **www.ustreas.gov/irs/ci/factsheets/factsheets.htm**

IRS Steps Against Noncompliance

The Internal Revenue Service has focused its efforts against noncompliance by adopting a multi-functional compliance approach:

- helping otherwise innocent taxpayers who have been misled by others to rejoin the system; and
- vigorously pursuing enforcement actions against those who continue to promote schemes or entice others to violate the law.

Regardless of the arguments used, they have two things in common:

- the arguments are consistently rejected by the courts, and
- the participants may face IRS enforcement action.

The IRS has one of the highest conviction rates in federal law enforcement. In addition to serving substantial prison sentences imposed by the courts, those convicted must also pay fines, taxes, civil penalties, and, frequently, court costs.

Additional information is available from IRS Publication 2105, "Why Do I Have to Pay Taxes?" It's available at ***www.ustreas.gov/irs/ci/factsheets/pub2105.pdf.***

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Don't Be Misled By Tax Schemes; IRS Warns of 8 Common Schemes

WASHINGTON - The Internal Revenue Service issued a nationwide alert to taxpayers warning them not to fall victim to tax scams. These schemes take several shapes, ranging from promises of special tax refunds to illegal ways of "untaxing" yourself.

"Each year, con artists shamelessly take advantage of people, sometimes charging fees for illegal tax schemes," IRS Commissioner Charles O. Rossotti said. "People should be on-guard for these scams. If something sounds too good to be true, it probably is."

If people think something may be unscrupulous, they can report suspected tax fraud to the IRS at 1-800-829-0433.

The IRS urges people to avoid these common schemes:

- NO TAXES BEING WITHHELD FROM YOUR WAGES. Illegal schemes are being promoted that instruct employers not to withhold federal income tax or employment taxes from wages paid to their employees. These schemes are based on an incorrect interpretation of tax law and have been refuted in court. If you have concerns about your employer and employment taxes, you can get help by calling the IRS at 1-800-829-1040.

- "I DON'T PAY TAXES - WHY SHOULD YOU?" Con artists may talk about how they don't file or pay taxes and then charge people a fee to share their "secret." The real secret that these people don't reveal is that many of them actually do file and pay taxes -- they just won't publicly admit it. Again, the IRS reminds people that failure to file or pay taxes is subject to civil and/or criminal tax penalties.

- AFRICAN-AMERICANS GET A SPECIAL TAX REFUND-- Thousands of African-Americans have been misled by people offering to file for tax credits or refunds related to reparations for slavery. There is no such provision in the tax law. Some unscrupulous promoters have encouraged clients to pay them to prepare a claim for this refund. But the claims are a waste of your money. Plus, those who file subsequent claims can be subject to a $500 frivolous return penalty.

- PAY THE TAX, THEN GET THE PRIZE -- The caller says you've won a prize and all you have to do to get it is pay the income tax due. Don't believe it. If you really won a prize, you may need to make an estimated tax payment to cover the taxes that will be due at the end of the year. But the payment goes to the IRS - not the caller. Whether you've won cash, a car, or a trip, the prize giver generally sends you and the IRS a Form 1099 showing the total prize value that should be reported on your tax return.

- UNTAX YOURSELF FOR $49.95. This one's as old as snake oil, but people continue to be taken in. And now it's on the Internet. The ads may say that paying taxes is "voluntary," but it is absolutely wrong. The U. S. courts have continuously rejected this and other similar arguments. Unfortunately, hundreds of people across the country have bought "untax packages" before finding out that following the advice contained in them can result in civil and/or criminal tax penalties being assessed. Numerous sellers of these bogus packages have been convicted on criminal tax charges.

- SOCIAL SECURITY TAX SCHEME. Taxpayers shouldn't fall victim to a scam offering them refunds of the Social Security taxes they have paid during their lifetimes. The scam works by the victim paying a "paperwork" fee of $100, plus a percentage of any refund received, to file a refund claim with the IRS. This hoax fleeces the victims for the upfront fee. The law does not allow such a refund of Social Security taxes paid. The IRS processing centers are alert to this hoax and have been stopping the false claims.

- "I CAN GET YOU A BIG REFUND...FOR A FEE!" Refund scheme operators may approach you wanting to "borrow" your Social Security Number or give you a phony W-2 so it appears that you qualify for a big refund. They may promise to split the refund with you, but the IRS catches most of these false refund claims before they go out. And when one does go out, the participant usually ends up paying back the refund along with stiff penalties and interest.

Two lessons to remember: 1) Anyone who promises you a bigger refund without knowing your tax situation could be misleading you, and 2) Never sign a tax return without looking it over to make sure it's honest and correct.

- IRS "AGENT" COMES TO YOUR HOUSE TO COLLECT. First, do not let anyone into your home unless they identify themselves to your satisfaction. IRS special agents, field auditors, and collection officers carry picture IDs and will normally try to contact you before they visit. If you think the person on your doorstep is an impostor, lock your door and call the local police. To report IRS impostors, call the Treasury Inspector General's Hotline at 1-800-366-4484.

The Taxpayer Advocate Service addresses taxpayer concerns that have not been resolved through regular Internal Revenue Service (IRS) contacts. The Taxpayer Advocate Service operates independently from any other IRS office. This independence allows us to work more effectively as advocates for taxpayers.