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Frivolous Issues Penalty Under IRC § 6673 and Related Appellate-Level Sanctions

SUMMARY

From June 1, 2013, through May 31, 2014, the federal courts issued decisions in at least 22 cases involving the Internal Revenue Code (IRC) § 6673 “frivolous issues” penalty, and at least ten cases involving analogous penalties at the appellate level. These penalties may be imposed against taxpayers for maintaining a case primarily for delay, raising frivolous arguments, unreasonably failing to pursue administrative remedies, or filing a frivolous appeal.¹ In many of the cases we reviewed, taxpayers escaped liability for the penalty but were warned they could face sanctions for similar conduct in the future.² Nonetheless, we include these cases in our analysis to illustrate what conduct will and will not be tolerated by the courts.

PRESENT LAW

The U.S. Tax Court is authorized to impose a penalty against a taxpayer if the taxpayer institutes or maintains a proceeding primarily for delay, takes a frivolous position in a proceeding, or unreasonably fails to pursue available administrative remedies.³ The maximum penalty is \$25,000.⁴ In some cases, the IRS requests that the Tax Court impose the penalty;⁵ in other cases, the court exercises its discretion, *sua sponte*,⁶ to do so.

Taxpayers who institute actions under IRC § 7433⁷ for certain unauthorized collection actions can be subject to a maximum penalty of \$10,000 if the court determines the taxpayer’s position is frivolous or groundless.⁸ In addition, IRC § 7482(c)(4),⁹ §§ 1912 and 1927 of Title 28 of the U.S. Code,¹⁰ and Rule

1 The Tax Court generally imposes the penalty under IRC § 6673(a)(1). Other courts may impose the penalty under IRC § 6673(b)(1). U.S. Courts of Appeals generally impose sanctions under IRC § 7482(c)(4), 28 U.S.C. § 1927, or Rule 38 of the Federal Rules of Appellate Procedure, although some appellate-level penalties may be imposed under other authorities.

2 See, e.g., *Aldrich v. Comm’r*, T.C. Memo. 2013-201.

3 IRC § 6673(a)(1)(A), (B), and (C).

4 IRC § 6673(a)(1).

5 The standards for the IRS’s decision to seek sanctions under IRC § 6673(a)(1) are found in the Chief Counsel Directives Manual (CCDM). See CCDM 35.10.2, *Special Procedures When Attorneys’ Fees and Sanctions Are Sought, Penalties and Sanctions* (Aug. 11, 2004). For sanctions under IRC § 6673(a)(2) of attorneys or other persons admitted to practice before the Tax Court, all requests for sanctions are reviewed by the designated agency sanctions officer (currently the Associate Chief Counsel (Procedure & Administration)). This review ensures uniformity on a national basis. See, e.g., CCDM 35.10.2.2.3, *Sanctions Requiring National Office Review* (Aug. 11, 2004).

6 “*Sua sponte*” means without prompting or suggestion; on its own will or motion. *Black’s Law Dictionary* (10th ed. 2014), available at www.westlaw.com. Thus, for conduct that it finds particularly offensive, the Tax Court can choose to impose a penalty under IRC § 6673 even if the IRS has not requested the penalty. See, e.g., *Toth v. Comm’r*, T.C. Memo. 2013-142.

7 IRC § 7433(a) allows a taxpayer a civil cause of action against the United States if an IRS employee intentionally or recklessly, or by reason of negligence, disregards any IRC provision or Treasury regulation in connection with collecting the taxpayer’s federal tax liability.

8 IRC § 6673(b)(1).

9 IRC § 7482(c)(4) provides that the United States Courts of Appeals and the Supreme Court have the authority to impose a penalty in any case where the Tax Court’s decision is affirmed and the appeal was instituted or maintained primarily for delay or the taxpayer’s position in the appeal was frivolous or groundless.

10 28 U.S.C. § 1912 provides that when the Supreme Court or a United States Court of Appeals affirms a judgment, the court has the discretion to award to the prevailing party just damages for the delay, and single or double costs. 28 U.S.C. § 1927 authorizes federal courts to sanction an attorney or any other person admitted to practice before any court of the United States or any territory thereof for unreasonably and vexatiously multiplying proceedings; such person may be required to personally pay the excess costs, expenses, and attorneys’ fees reasonably incurred because of his/her conduct.

38 of the Federal Rules of Appellate Procedure¹¹ (among other laws and rules of procedure) authorize federal courts to impose penalties against taxpayers or their representatives for raising frivolous arguments or using litigation tactics primarily to delay the collection process. Because the sources of authority for imposing appellate-level sanctions are numerous and some of these sanctions may be imposed in nontax cases, this report focuses primarily on the IRC § 6673 penalty.

ANALYSIS OF LITIGATED CASES

We analyzed twenty-two opinions issued between June 1, 2013, and May 31, 2014 that addressed the IRC § 6673 penalty. Eighteen of these opinions were issued by the Tax Court and four by U.S. Courts of Appeals in cases where taxpayers sought review of the Tax Court's imposition of the penalty. The Courts of Appeals sustained the Tax Court's position in all cases.

In ten cases, the Tax Court imposed penalties under IRC § 6673, with the amounts ranging from \$1,500 to \$225,000.¹² In three cases, taxpayers prevailed when the IRS asked the court to impose a penalty but in all of these cases, the court warned the taxpayers not to bring similar arguments in the future.¹³ Two taxpayers were represented by attorneys or other persons admitted to practice before the Tax Court; all sixteen others appeared *pro se* (represented themselves). The taxpayers in these cases presented a wide variety of arguments that the courts have generally rejected on numerous occasions. Upon encountering these arguments, the courts almost invariably cited the language set forth in *Crain v. Commissioner*:

We perceive no need to refute these arguments with somber reasoning and copious citation of precedent; to do so might suggest that these arguments have some colorable merit. The constitutionality of our income tax system—including the role played within that system by the Internal Revenue Service and the Tax Court—has long been established.¹⁴

In the Tax Court cases we reviewed, taxpayers raised the following issues that the court deemed frivolous. Consequently, the taxpayers were subject to a penalty under IRC § 6673(a)(1) (or, in some cases, the court warned that such arguments were frivolous and could lead to a penalty in the future if the taxpayers maintained the same positions):

- **Taxes and procedures to collect taxes are unconstitutional:** Taxpayers in at least four cases argued that taxes, or the actions used by the IRS or the courts to collect them, violate their constitutional rights.¹⁵ Taxpayers generally argued that taxes and the courts' actions were unconstitutional, as well as arguing specifically that taxes and the collection of taxes violated the First, Fourth, Fifth, and Sixteenth Amendments. The IRS prevailed on the issue of sanctions in three of the cases. In

11 Federal Rule of Appellate Procedure 38 provides that if a United States Court of Appeals determines an appeal is frivolous, the court may award damages and single or double costs to the appellee.

12 The maximum penalty is \$25,000 in a Tax Court proceeding, but in *Jones v. Comm'r*, T.C. Memo. 2014-101, the Tax Court imposed \$225,000 (nine cases consolidated and the penalty was imposed in each of the nine cases).

13 See, *Carothers v. Comm'r*, T.C. Memo. 2013-165, *Haag v. Commissioner*, T.C. Memo 2014-11, and *MacDonald v. Comm'r*, T.C. Memo. 2014-42.

14 *Crain v. Comm'r*, 737 F.2d 1417, 1417-18 (5th Cir. 1984).

15 See, e.g., *Buckhardt v. Comm'r*, 548 F. App'x 433 (9th Cir. 2013), *aff'g* T.C. Docket. No. 22131-10 (Oct. 13, 2011) (taxpayer argued that the Tax Court violated his First, Fourth, and Fifth Amendment rights).

the fourth case, the court upheld the § 6673 penalty but declined to impose any additional sanctions under 28 U.S.C. § 1912 or the Federal Rules of Appellate Procedure.¹⁶

- **IRS forms invalidate tax assessments:** In at least two cases, taxpayers argued that various IRS forms invalidated the tax assessments.¹⁷ One taxpayer argued the tax was not properly imposed since it was not validated on a Form 23C, “Assessment Certificate-Summary Record of Assessments” and the other taxpayer argued that IRS forms violate the Paperwork Reduction Act of 1995. Both courts declined to impose any penalties, but warned the taxpayers that further similar conduct could result in penalties.
- **Only income earned from the United States government or entities associated with the United States government is taxable:** Taxpayers in at least six cases argued that only federal government employees, public servants, or those who earn income from the United States government or military are subject to the income tax.¹⁸ The IRS prevailed in four cases and the court raised the issue *sua sponte* in the other two cases, deciding not to impose the penalty in the present cases but warning the taxpayers not to raise similar arguments in the future.

CONCLUSION

Taxpayers in the cases analyzed this year presented the same or similar arguments raised and repeated year after year, which the courts routinely and universally reject.¹⁹ Taxpayers avoided the IRC § 6673 penalty in only three cases where the IRS requested it, demonstrating the willingness of the courts to penalize taxpayers when they offer frivolous arguments or institute a case merely for delay. Whether the taxpayer has a history of making frivolous or groundless arguments may result in a larger penalty being imposed, but that may not always be the case.²⁰

Where the IRS has not requested the penalty, the court may nonetheless raise the issue *sua sponte*, and in many cases imposes the penalty or cautions the taxpayer that similar future behavior will result in a penalty.²¹ Finally, the U.S. Courts of Appeals have shown their willingness to uphold the IRC § 6673 penalties imposed by the Tax Court without fail in the cases analyzed for the period between June 1, 2013, and May 31, 2014, continuing a trend of upholding all penalties in cases we have analyzed since June 2005.

16 See *Herriman v. Comm’r*, 521 F. App’x 912 (11th Cir. 2013), *aff’g* T.C. Docket. No. 25048-11 (May 8, 2012) (court granted IRS’s motion for sanctions pursuant to the Federal Rules of Appellate Procedure); *Golub v. Comm’r*, T.C. Memo. 2013-196 (court, *sua sponte*, imposed sanctions under IRC § 6673); *Young v. Comm’r*, 551 F. App’x 229 (5th Cir. 2014), *aff’g* T.C. Docket No. 4664-12 (Mar. 20, 2013) (court affirmed § 6673 penalty and granted IRS’s motion for sanctions pursuant to the Federal Rules of Appellate Procedure); *Buckhardt v. Comm’r*, 548 F. App’x 433 (9th Cir. 2013), *aff’g* T.C. Docket. No. 22131-10 (Oct. 13, 2011) (court affirmed IRC § 6673 penalty but denied IRS’s motion for sanctions pursuant to 28 U.S.C. § 1912 and the Federal Rules of Appellate Procedure).

17 See *Pflum, U.S. v.*, 112 A.F.T.R.2d (RIA) 7200 (W.D. Wash. 2013), *aff’g* 112 A.F.T.R.2d (RIA) 7303 (E.D. Wash. 2013); *Burt v. Comm’r*, T.C. Memo. 2013-140, appeal docketed, No. 13-1946 (6th Cir. Oct. 17, 2013).

18 See, e.g., *Hill v. Comm’r*, T.C. Memo. 2013-265; *Jones v. Comm’r*, T.C. Memo. 2014-101.

19 See, e.g., National Taxpayer Advocate 2013 Annual Report to Congress 399-402.

20 See, e.g., *Golub v. Comm’r*, T.C. Memo. 2013-196 (court imposed \$15,000 penalty and had imposed \$10,000 penalty in an earlier case). Compare with *Burt v. Comm’r*, T.C. Memo. 2013-140, appeal docketed, No. 13-1946 (6th Cir. Oct. 17, 2013) (court declined to impose the IRC § 6673 penalty even though the taxpayer was no stranger to the court and had been penalized \$20,000 in an earlier case).

21 See, e.g., *Aldrich v. Comm’r*, T.C. Memo. 2013-201 (court raised the issue *sua sponte* and warned the taxpayer not to assert similar arguments in the future).