

MLI
#9Fivolous Issues Penalty Under IRC § 6673 and Related
Appellate-Level Sanctions

SUMMARY

From June 1, 2015 through May 31, 2016, the federal courts issued decisions in at least 19 cases involving Internal Revenue Code (IRC) § 6673 “frivolous issues” penalty and in at least five cases involving similar penalties at the appellate level.¹ These penalties are imposed for maintaining a case primarily for delay, raising frivolous arguments, unreasonably failing to pursue administrative remedies, or filing a frivolous appeal.² In five of the cases TAS reviewed, taxpayers escaped liability for the penalty and two cases resulted in a split decision on the requested penalties.³ Additionally, in three cases, the courts raised the issue of penalties *sua sponte* and did not impose the contemplated penalties but warned the taxpayers they could face sanctions for similar conduct in the future.⁴ Nonetheless, TAS included these cases in its analysis to illustrate what conduct will and will not be tolerated by the courts.

TAXPAYER RIGHTS IMPACTED⁵

- *The Right to Appeal an IRS Decision in an Independent Forum*

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.⁶ The maximum penalty is \$25,000.⁷ In some cases, the IRS requests that the Tax Court impose the penalty.⁸ In other cases, the Tax Court exercises its discretion, *sua sponte*,⁹ to consider whether the penalty is appropriate.

- 1 One of these cases also reviewed the Tax Court’s imposition of the Internal Revenue Code (IRC) § 6673 penalty; it is only counted once, our total case count is 23 distinct cases. See *Myers v. Comm’r*, 630 F. App’x 207 (4th Cir. 2016) (denying the Commissioner’s motion for sanctions but upholding \$5000 IRC § 6673 penalty), *aff’g* T.C. docket No. 30321-13L (May 28, 2015).
- 2 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 are authorized to 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.
- 3 See, e.g., *Hare v. Comm’r*, T.C. Memo. 2015-250.
- 4 “*Sua sponte*” means without prompting or suggestion, on its own motion. BLACK’S LAW DICTIONARY (10th ed. 2014). 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., *Shakir v. Comm’r*, T.C. Memo. 2015-147.
- 5 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 6 IRC § 6673(a)(1)(A), (B), and (C).
- 7 IRC § 6673(a)(1).
- 8 The standards for the IRS’s decision to seek sanctions under IRC § 6673(a)(1) are found in the Chief Counsel Directives Manual. See Chief Counsel Directives Manual (CCDM) 35.10.2 (Aug. 11, 2004). For sanctions of any attorney or other person authorized to practice before the Tax Court, under IRC § 6673(a)(2), 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 (Aug. 11, 2004).
- 9 See, e.g., *Crummey v. Comm’r*, T.C. Memo. 2016-9, *appeal docketed*, No. 16-60620 (5th Cir. Sept. 16, 2016).

Taxpayers who institute actions in United States District Courts under IRC § 7433¹⁰ for certain unauthorized collection actions can be subject to a maximum penalty of \$10,000 if the court determines the taxpayer's position in the proceedings is frivolous or groundless.¹¹ In addition, IRC § 7482(c)(4) (United States Courts of Appeal and the Supreme Court),¹² §§ 1912 (United States Courts of Appeal and the Supreme Court) and 1927 (all federal courts) of Title 28 of the U.S. Code,¹³ and Rule 38 of the Federal Rules of Appellate Procedure (United States Court of Appeals)¹⁴ (among other laws and rules of procedure) authorize various 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 19 opinions issued between June 1, 2015, and May 31, 2016, in which courts addressed the IRC § 6673 penalty. Thirteen of these opinions were issued by the Tax Court, and six were issued by U.S. Courts of Appeals in cases brought by taxpayers seeking review of the Tax Court's imposition of the penalty. The Courts of Appeals sustained the Tax Court's position in all six cases. Five decisions were issued by other courts on similar penalties (one of these cases also reviewed the Tax Court's imposition of the IRC § 6673 penalty; it is only counted once, our total case count is 23 distinct cases).¹⁵

In seven cases, the Tax Court imposed penalties under IRC § 6673, with the amounts ranging from \$1,000 to \$15,000. In four cases, taxpayers prevailed when the IRS asked the court to impose a penalty, and in one case, the court fined the taxpaying husband but not the taxpaying wife, resulting in a split decision.¹⁶ In most of these cases, the court warned the taxpayers not to bring similar arguments in the future.¹⁷ All taxpayers appeared *pro se* (represented themselves) before the Tax Court. The taxpayers 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*:

10 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.

11 IRC § 6673(b)(1).

12 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.

13 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 troublesome multiplying proceedings; such person may be required to personally pay the excess costs, expenses, and attorneys' fees reasonably incurred because of his or her conduct.

14 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.

15 See *Myers v. Comm'r*, 630 F. App'x 207 (4th Cir. 2016) (denying the Commissioner's motion for sanctions but upholding \$5000 IRC § 6673 penalty), *aff'g* T.C. docket No. 30321-13L (May 28, 2015).

16 See *Stanley v. Comm'r*, T.C. Memo. 2016-26.

17 See, e.g., *Martens v. Comm'r*, T.C. Memo. 2015-213.

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.¹⁸

In the Tax Court cases TAS 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:** TAS identified two cases this year where taxpayers made arguments that taxes or how they are collected are unconstitutional.¹⁹ The taxpayers in these cases advanced common arguments regarding the constitutionality of the income tax and procedures to collect it, including that their Fifth Amendment rights were denied and that they were not afforded due process under the Fourteenth Amendment. Both courts in these cases imposed penalties on the taxpayers.
- **IRS forms and notices violate the Paperwork Reduction Act (PRA) because they do not display a valid Office of Management and Budget (OMB) Control Number:** In at least one case, the taxpayer argued that IRS forms and notices violated PRA, and therefore he had no duty to file a tax return.²⁰ The taxpayer asserted that OMB had not approved IRS Form 1040, *U.S. Individual Income Tax Return*, in violation of the PRA. The court raised the issue *sua sponte* but declined to impose the penalty, and instead warned the taxpayer against future similar behavior.
- **Taxpayers are not United States persons or wages are not income:** Taxpayers in at least four cases presented arguments that they are not United States persons subject to tax or that wage income is not taxable.²¹ In one case, a taxpayer argued that the definition of income is a cat with a pink bow, and he earned no income.²² The court imposed a penalty of \$3,500 in this case.

CONCLUSION

Taxpayers in the cases analyzed this year presented the same arguments raised and repeated every year, which the courts routinely and universally reject.²³ Of the 23 cases reviewed, taxpayers avoided the IRC § 6673 penalty where the IRS requested it in only four cases and one split decision; the Tax Court often warned the taxpayers in these cases not to bring similar arguments in the future. Moreover, even when the Tax Court acknowledges that a penalty will likely not dissuade the taxpayer from raising frivolous arguments in the future, it nonetheless recognizes that the penalty “serves as a warning to other taxpayers considering these or similar arguments.”²⁴ Where the IRS has not requested the penalty, the court may

18 *Crain v. Comm’r*, 737 F.2d 1417, 1417-18 (5th Cir. 1984). See, e.g., *Foryan v. Comm’r*, T.C. Memo. 2015-114.

19 See *Clark*, U.S. v., 642 F. App’x 614 (7th Cir. 2016), *aff’g* 116 A.F.T.R.2d (RIA) 5229 (E.D. Wis. 2015); *Briggs v. Comm’r*, T.C. Memo. 2016-86.

20 See *Shakir v. Comm’r*, T.C. Memo. 2015-147.

21 See, e.g., *Foryan v. Comm’r*, T.C. Memo. 2015-114; *Leyshon v. Comm’r*, T.C. Memo. 2015-104, *aff’d by docket* No. 15-2020 (4th Cir. May 20, 2016).

22 *Bruhwiller v. Comm’r*, T.C. Memo. 2016-18.

23 See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 523-26.

24 *Nitschke v. Comm’r*, T.C. Memo. 2016-78, *motion to vacate denied* (June 2, 2016).

nonetheless raise the issue *sua sponte*, and in all cases identified either imposed the penalty or cautioned the taxpayer that similar future behavior will result in a penalty.²⁵

Finally, the U.S. Courts of Appeals have shown their willingness to uphold the penalties imposed by the Tax Court without fail in the cases analyzed for the period between June 1, 2015, and May 31, 2016, continuing a trend of upholding all penalties in cases TAS has analyzed since June 2005.

25 See, e.g., *Crummey v. Comm’r*, T.C. Memo. 2016-9 (court raised the issue *sua sponte* and warned the taxpayer not to assert similar arguments in the future).