

INTERNAL POLICY DIRECTIVE 2008-3

November 14, 2008

REVENUE ACT FRIVOLOUS PROTEST PENALTY

This Internal Policy Directive (IPD) is intended to provide additional guidance in the administration of the frivolous protest penalty found in the Revenue Act at MCL 205.21(4).

POLICY ISSUES

- A. What is a frivolous protest for the purposes of MCL 205.21(4)?
- B. How is the frivolous protest penalty at MCL 205.21(4) imposed?
- C. When will the Department begin applying the specific criteria as to what constitutes a frivolous protest enumerated in this IPD?

POLICY DETERMINATIONS

A. A frivolous protest is one in which a taxpayer raises a defense that is clearly not supported in law or that has previously been raised repeatedly without success by other taxpayers. A protest made for the purpose of delaying or impeding the administration of taxes may also be frivolous. The following specific criteria are among those that will be applied in determining when a protest is frivolous:

- 1. Raising Fifth Amendment objections including:
 - A. Self-incrimination
 - B. Taxes are a taking of property without due process of law
- 2. Asserting the unconstitutionality of the tax based on the:
 - A. Gold and silver standard
 - B. Supremacy Clause of the U.S. Constitution
 - C. 13th Amendment to the U.S. Constitution
 - D. 16th Amendment to the U.S. Constitution
 - E. Non-uniformity of income taxes among the States
- 3. Arguing that payment received for labor (salaries and wages) is a return of capital and not income, including "Right to Labor" arguments
- 4. Asserting that compensation is not profits
- 5. Arguing that filing of a tax return and payment of tax is voluntary
- 6. Asserting exemption from tax when no Federal Exemption is cited
- 7. Arguing that the taxpayer is not a citizen of the State, only a citizen of the United States (or vice versa)
- 8. Demanding a jury trial
- 9. The filing of zero-returns (returns filled in with all zeros)

10. All similar objections

B. The frivolous protest penalty at MCL 205.21(4) is imposed through a Decision and Order of Determination issued by the State Treasurer's designee subsequent to an informal conference.

C. The Department will begin applying the criteria as to what constitutes a frivolous protest that are enumerated in this IPD beginning with requests for informal conferences filed after January 1, 2009.

DISCUSSION

This Internal Policy Directive (IPD) is provided to offer procedures on how and when the frivolous protest penalty can be imposed, as well as guidance as to what constitutes a frivolous protest. This IPD applies to all requests for informal conference received on or after January 1, 2009.

The frivolous protest penalty is included in the Revenue Act under MCL 205.21(4), which provides:

If a protest to the notice of intent to assess the tax is determined by the department to be a frivolous protest or a desire by the taxpayer to delay or impede the administration of taxes administered under this act, a penalty of \$25.00 or 25% of the amount of tax under protest, whichever is greater, shall be added to the tax.

FRIVOLOUS PROTESTS

"Frivolous" as defined in Revenue Administrative Bulletin (RAB) 2005-3 is:

A term that describes a taxpayer's attempts to avoid or delay the payment of tax by raising arguments that are clearly insufficient or have been repeatedly found to have no merit in prior litigation.

RAB 2005-3, in pertinent part, discusses frivolous protests and gives several examples:

A penalty (the greater of \$25.00 or 25% of the tax due) may be imposed when a taxpayer attempts to avoid or delay payment of tax by raising arguments that are either not valid on the surface of the argument or have repeatedly been found to have no merit in prior litigation. The Treasurer or authorized agent will apply this penalty when a taxpayer uses this tactic to delay paying a Michigan tax.

Examples include:

1. Fifth Amendment (privilege against self-incrimination) objections:
 - A. Taxpayer engaged in unlawful activities.

- B. Taxpayer failed or refused to file a return with another taxing authority.
- 2. Unconstitutionality of the tax, asserting a basis that has repeatedly been found to be without merit:
 - A. Gold and silver standard.
 - B. 16th Amendment to the U.S. Constitution.
- 3. Arguing that payment received for labor (salaries and wages) is a return of capital and not income.

Additionally, section 21(2)(c) of the revenue act [MCL 205.21(2)(c)] provides the following:

"If the taxpayer serves written notice upon the department within [60]¹ days after the taxpayer receives a notice of intent to assess, **remits the uncontested portion of the liability**, and provides a statement of the contested amounts and an explanation of the dispute, the taxpayer is entitled to an informal conference on the question of liability for the assessment." (Emphasis added)

Therefore, a taxpayer is required to remit payment on the uncontested portion of the tax due within [60] days of receiving the billing. If results of the conference indicate that any portion of the unpaid liability is uncontested, the frivolous penalty will apply to that uncontested portion.

The following are additional examples of arguments raised in both state and federal courts that have been found frivolous and totally without merit.

Some taxpayers assert that they are not required to file federal tax returns because the filing of a tax return is voluntary. In *Johnson v Comm'r*, 78 TCM 468, 471 (1999), the court found Johnson liable for the failure to file penalty and rejected his argument "that the tax system is voluntary so that he cannot be forced to comply" as "frivolous." In *Bonaccorso v Comm'r*, 90 TCM 554 (2005), the taxpayer filed zero returns based on the argument that he found no Code section that made him liable for any income tax. The court held that the taxpayer's argument was frivolous and also imposed a \$10,000 sanction against the taxpayer for making frivolous arguments. "Courts have consistently found the arguments made by Plaintiffs, or ones very similar, in support of an all zero return to be frivolous." *Schultz v US*, 2005 WL 1155203, at 3 (WD Mich 2005).

Some taxpayers argue that they have rejected citizenship in the United States in favor of state citizenship; therefore, they are relieved of their federal income tax obligations. A variation of this argument is that a person is a free born citizen of a particular state and thus was never a citizen of the United States. In *US v Sileven*, 985 F2d 962 (CA 8, 1993), the court rejected the argument that the district court lacked jurisdiction because

¹ Statutory language modified to comport with 2006 PA 11 which changed the period for seeking an informal conference to 60 days from 30 days.

the taxpayer was not a federal citizen as “plainly frivolous.” Also, in *US v Studley*, 783 F2d 934, 937 (CA 9, 1986), the court affirmed a failure to file conviction, rejecting the taxpayer’s contention that she was not subject to federal tax laws because she was “an absolute, freeborn, and natural individual” and went on to note that “this argument has been consistently and thoroughly rejected by every branch of the government for decades.”

Other taxpayers assert that the collection of federal income taxes constitutes a taking of property without due process of law, in violation of the Fifth Amendment. The United States Supreme Court stated in *Brushaber v Union Pacific R.R.*, 240 US 1, 24; 36 S Ct 326; 60 L Ed 493 (1916):

[I]t is . . . well settled that the Fifth Amendment is not a limitation upon the taxing power conferred upon Congress by the Constitution; in other words, that the Constitution does not conflict with itself by conferring upon the one hand a taxing power, and taking the same power away on the other by limitations of the due process clause.

Some argue that taxpayers may refuse to file federal income tax returns, or may submit tax returns on which they refuse to provide any financial information, because they believe that their Fifth Amendment privilege against self-incrimination will be violated. The failure to comply with the filing and reporting requirements of the tax laws will not be excused based upon blanket assertions of the constitutional privilege against compelled self-incrimination under the Fifth Amendment. *US v Sullivan*, 274 US 259; 47 S Ct 607; 71 L Ed 1037 (1927).

Another “constitutionally-based” argument is founded on the premise that all federal income tax laws are unconstitutional because the Sixteenth Amendment was not officially ratified. In *Socia v Comm’r*, 23 F3d 941 (CA 5, 1994), the court held that defendant’s appeals which challenged Sixteenth Amendment income tax legislation were frivolous and warranted sanctions.

Some taxpayers argue that the Sixteenth Amendment to the United States Constitution did not authorize a tax on wages and salaries, but only on gain or profit. This argument asserted that wages, tips, and other compensation received for personal services are not income, because there is allegedly no taxable gain when a person exchanges labor for money. In *Lonsdale v Comm’r*, 661 F2d 71, 72 (CA 5, 1981), the court rejected as “meritless” the taxpayer’s contention that the “exchange of services for money is a zero-sum transaction” Additionally, in *Comm’r v Kowalski*, 434 US 77; 98 S Ct 315; 54 L Ed 2d 252 (1977), the Supreme Court found that payments are considered income where the payments are undeniably accessions to wealth, clearly realized, and over which a taxpayer has complete dominion.

Courts perceive the above protests to be “wholly without merit and not worthy of further analysis” and no longer address these arguments. *Blake v Comm’r*, 75 TCM 2256

(1998); *Reichenbach v Comm'r of Internal Revenue*, 99 F3d 1139 (CA 6, 1996). In *Kish v Comm'r*, 75 TCM 1571 (1998), the court stated:

[A]ll of petitioner's arguments are similar to rejected arguments of other taxpayers who have previously petitioned this Court in protest of their liability for Federal income tax. Petitioner's assertions are characteristic of the tax protestor rhetoric that has been universally rejected by this and other courts. We will not painstakingly address petitioner's assertions as to the validity of the Federal income tax system or the authority of this Court...

In accordance with the foregoing, the frivolous protest penalty shall be included in a Decision and Order of Determination if a taxpayer raises any of the following protests:

1. Raising Fifth Amendment objections including:
 - A. Self-incrimination
 - B. Taxes are a taking of property without due process of law
2. Asserting the unconstitutionality of the tax based on the:
 - A. Gold and silver standard
 - B. Supremacy Clause of the U.S. Constitution
 - C. 13th Amendment to the U.S. Constitution
 - D. 16th Amendment to the U.S. Constitution
 - E. Non-uniformity of income taxes among the States
3. Arguing that payment received for labor (salaries and wages) is a return of capital and not income, including "Right to Labor" arguments
4. Asserting that compensation is not profits
5. Arguing that filing of a tax return and payment of tax is voluntary
6. Asserting exemption from tax when no Federal Exemption is cited
7. Arguing that the taxpayer is not a citizen of the State, only a citizen of the United States (or vice versa)
8. Demanding a jury trial
9. The filing of zero-returns (returns filled in with all zeros)
10. All similar objections²

Department personnel may alert the Administrator of the Hearings Division to additional arguments of a frivolous nature for consideration and possible inclusion in this list.

DELAY OR IMPEDIMENT

A desire by the taxpayer to delay or impede the administration of taxes administered under this act will be presumed in a situation where a taxpayer timely requests an informal conference, yet presents no arguments at conference. A taxpayer who merely bides his time through the informal conference process without presenting any arguments will be considered to be delaying or impeding the administration of taxes.

² See the IRS publication "The Truth About Frivolous Tax Arguments, November 30, 2007" (available at http://www.irs.gov/pub/irs-utl/friv_tax.pdf, last visited 6/30/2008).

The Court in *Haines v. Commissioner*, 79 TCM 1844 (2000) stated “[p]etitioner knew or should have known that his position was groundless and frivolous, yet he persisted in maintaining this proceeding primarily to impede the proper workings of our judicial system and to delay the payment of his Federal income tax liabilities.”

Also, in *Sigerseith v Commissioner*, TCM 2001-148 (2001), the Court stated that dealing with the Petitioner’s case was “a waste of limited judicial and administrative resources that could have been devoted to resolving bona fide claims of other taxpayers.”

PROCEDURE

A Department representative may request that a frivolous protest penalty be made part of a hearing referee’s recommendation or, alternatively, a hearing referee may independently determine a protest is frivolous and recommend that the frivolous protest penalty be imposed. Once a frivolous protest penalty has been recommended in a hearing referee’s informal conference recommendation, the Administrator of the Hearings Division shall evaluate the grounds supporting the recommendation and, if accepted by the Administrator, the penalty shall be incorporated into the Decision and Order of Determination in the matter.

The frivolous protest penalty is applied only to a frivolous protest or desire by a taxpayer to delay or impede the administration of an Intent to Assess, not to a claim for refund.

Due process requires the taxpayer to receive notice and an opportunity for a hearing. The taxpayer receives notice of the imposition of the frivolous protest penalty upon receipt of the Decision and Order of Determination resulting from his or her informal conference. The Final Bill for Taxes Due advises the taxpayer that he may appeal the Final Bill either to the Michigan Tax Tribunal within 35 days of the issuance date or, after full payment of the bill, a taxpayer may appeal to the Michigan Court of Claims within 90 days of issuance date. The opportunity for an appeal in either of the above-stated forums provides the taxpayer with the requisite due process procedures after application of a frivolous protest penalty.