THIRD SECTION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

2004 JUN 29 PM 1 16

June 25, 2004

By Facsimile & Regular Mail:
Cono R. Namorato
Director, Office of
Professional Responsibility
Internal Revenue Service
Room 7217
1111 Constitution Avenue, NW
Washington, DC 20224

By Regular Mail:
Joseph R. Banister, CPA
2282 Sunny Vista Drive
San Jose, CA 95128

By Facsimile & Regular Mail:
Jay J. Kessler, Esquire
Internal Revenue Service
Office of Chief Counsel
333 Market Street, Suite 1200
San Francisco, CA 94104

By Facsimile & Certified & Regular Mail:
Robert G. Bernhoft, Esquire
Robert E. Barnes, Esquire
207 East Buffalo Street, Suite 600
Milwaukee, WI 53202

Re: Director, Office of Professional Responsibility
v. Joseph R. Banister, Complaint No. 2003-02

Gentlemen:

Enclosed please find the Decision on Appeal, constituting Final Agency Action in the above-referenced matter.

Sincerely,

David F. P. O'Connor
Special Counsel to the Senior
Counsel
Office of Chief Counsel
Internal Revenue Service
(Acting as Delegate of the
Secretary of the Treasury)

United States
Department of the Treasury

Director, Office of Professional Responsibility,	)	
	)	
Appellee-Complainant,	)	
	)	
v.	)	**COMPLAINT**
	)	**NO. 2003-02**
Joseph R. Banister,	)	
	)	
Appellant-Respondent.	)	
	)	
	)	

Decision on Appeal

Under the authority of General Counsel Order No. 9 (January 19, 2001) and the authority vested in her as Acting Assistant General Counsel of the Treasury who was the Acting Chief Counsel for the Internal Revenue Service, on April 9, 2004, Emily A. Parker delegated to the undersigned the authority to decide disciplinary appeals to the Secretary of the Treasury filed under Part 10 of Title 31, Code of Federal Regulations (Rev. 7-2002) ("Practice Before the Internal Revenue Service," sometimes known and hereafter referred to as "Treasury Circular 230"). This is such an appeal by the Respondent, Joseph R. Banister, filed pursuant to §10.77 of Treasury Circular 230.

Pursuant to §10.91 of Treasury Circular 230, any proceedings under Treasury Circular 230 instituted after July 26, 2002, are governed by Subparts D (the Rules Applicable to Disciplinary Proceedings, §§10.60-10.82) and E (the General Provisions, §§10.90-10.93) of Treasury Circular 230, but conduct engaged in prior to July 26, 2002 is judged by the provisions of

Treasury Circular 230 in effect at the time the conduct occurred. This is such a proceeding. Thus in determining both whether the conduct forming the basis of the Complaint and Amended Complaint filed against Respondent violated the duties and restrictions relating to practice before the Internal Revenue Service (Subpart B, §§10.20–10.34, of Treasury Circular 230) and what sanctions are appropriately imposed against the Respondent for any violations of such duties and restrictions (Subpart C, §§10.50–10.53, of Treasury Circular 230), the provisions of Subparts B and C of Treasury Circular 230 in effect on the date of Respondent's conduct control.

Preliminary Statement

These proceedings were initiated by the Director of the Office of Professional Responsibility (Complainant)[1] against Joseph R. Banister (Respondent) on March 19, 2003 by the filing of a Complaint pursuant to Section 10.60(a) of Treasury Circular 230. In the complaint filed on March 19, 2003 (hereafter the "Initial Complaint"), Complainant made five specific charges against the Respondent.

First, Complainant charged that the Respondent failed to exercise due diligence in violation of §§10.22(b) and 10.22(c) of Treasury Circular 230 and engaged in disreputable conduct in violation of §§10.34, 10.51, and 10.51(j) of Treasury Circular 230 by giving advice to two taxpayers [each United States citizens residing during all years in issue in the United States (hereafter, Taxpayer C and Taxpayer T)] that had no basis in law or fact and, while representing the same taxpayers before the Internal Revenue Service, took a position that had no substantive basis in law or in fact. Specifically, Complainant alleged that:

---

[1] On the date of the filing of the Complaint, the Director of the Office of Professional Responsibility was Brien T. Downing. Mr. Downing continued to serve in that capacity when the Amended Complaint was entered in these proceedings. At present, the Director of the Office of Professional Responsibility is Cono R. Namorato, who continues to prosecute the Complaint as amended.

With respect to Taxpayer C's tax liabilities for the taxable years 1989 through 1998, inclusive, Respondent advised Taxpayer C that he was not liable for income taxes because the Sixteenth Amendment to the United States Constitution was "not ratified;"

With respect to Taxpayer C's tax liabilities for the taxable years 1989 through 1998, inclusive, Respondent advised Taxpayer C that § 861 of the Internal Revenue Code of 1986 and the regulations thereunder defined "source" of income in such a way as to exclude Taxpayer C's income from taxation;

With respect to Taxpayer T's tax liabilities for the taxable years 1989 through 1998, inclusive, Respondent advised Taxpayer T that § 861 of the Internal Revenue Code of 1986 and the regulations thereunder defined "source" of income in such a way as to exclude Taxpayer T's income from taxation;

With respect to the preparation of Taxpayer T's Amended U.S. Individual Income Tax Returns for the years 1996 and 1998, Respondent on February 29, 2000 signed as preparer Taxpayer T's Form 1040X for 1996 and on January 31, 2000, Respondent signed as preparer Taxpayer T's Form 1040X for 1998, in each instance stating that Taxpayer's income for those years was not taxable income per §§ 861-865 of the Internal Revenue Code of 1986, which returns were filed with the Internal Revenue Service, thereby engaging in disreputable conduct in violation of § 10.34 of Treasury Circular 230.

Second, with respect to the above-referenced advice rendered to Taxpayer C and Taxpayer T, and in preparing Taxpayer T's Amended Individual Income Tax Returns (Forms 1040X) for the years 1996 and 1998, Complainant alleged that Respondent knowingly counseled Taxpayer C and Taxpayer T of

an illegal plan to evade Federal taxes or the payment thereof in violation of §10.51(d) of Treasury Circular 230.

Third, with respect to the above-referenced advice to Taxpayer C and Taxpayer T, Complainant alleged that Respondent violated §10.51(j) of Treasury Circular 230 by providing false opinions, either knowingly, recklessly, or through gross incompetence, to Taxpayer C and Taxpayer T.

Fourth, with respect to providing advice to Taxpayer C and Taxpayer T and by preparing Amended Individual Income Tax Returns for Taxpayer T for the years 1996 and 1998, Respondent failed to exercise due diligence in determining the correctness of oral and/or written representations he made to Taxpayer C, Taxpayer T and Internal Revenue Service personnel in violation of §§10.22(b) and 10.22(c) of Treasury Circular 230.

Fifth, with respect to his preparation of Taxpayer T's amended individual income tax returns (Forms 1040X) for the years 1996 and 1998, Respondent violated §10.34 of Treasury Circular 230 by signing as the preparer federal income tax returns that did not have a realistic possibility of being sustained on their merits and were clearly frivolous.

Complainant alleged in the Initial Complaint that each of the above charges, if proven, justified disbarment or suspension from practice before the Internal Revenue Service.

On March 24, 2003, Susan L. Biro, Chief Administrative Law Judge of the Environmental Protection Administration, designated Administrative Law Judge William B. Moran to act as the Administrative Law Judge in these proceedings.

On April 30, 2003, Respondent filed his Statement of Facts, Answer and Affirmative Defenses in these proceedings.

On June 9, 2003, Judge Moran filed his Prehearing Order in these proceedings. The prehearing exchange contemplated by

the Prehearing Order included (A) a list of the names of any witnesses, including expert witnesses, intended to be called at the hearing, together with a brief narrative description of their expected testimony, (B) copies of all documents and exhibits intended to be introduced into evidence (including the curriculum vita or resume of each identified expert witness), and (C) an estimate of the time needed to present the party's direct case.

On August 8, 2003, Complainant filed a Motion to Amend the Initial Complaint, indicating that subsequent to the filing of the Initial Complaint, Complainant and Complainant's counsel had become aware that Respondent had failed to file individual income tax returns (Forms 1040) for the taxable years 1999, 2000, 2001 and 2002. Complainant sought leave to amend the Initial Complaint to add four additional charges, in each instance indicating that Respondent was required by 26 USC §§ 1, 6011(a), 6012(a) et seq., 6013 and/or 6072(a) to file an individual income tax return (Form 1040) for one of the four years specified no later than April 15th of the following year, that in each instance Respondent had failed to do so with respect to the year in question, and that each such allegation, if proved, constituted disreputable conduct punishable by disbarment or suspension under §10.51(d) of Treasury Circular 230.

By letter dated September 23, 2003, Christopher J. Ertl, acting in his capacity as Counsel for Respondent, wrote Judge Moran, stating:

> "Please be advised that the Respondent, Joseph R. Banister will take no position on the Petitioner's [sic] motion to amend the complaint. We will wait for the court's order regarding this matter prior to taking a position on answering the proposed amended complaint."

On October 17, 2003, Judge Moran entered an Order granting Complainant's Motion to Amend the Initial Complaint.

On October 17, 2003, Judge Moran also entered an Order setting October 31, 2003 as the cut-off date for motions in these proceedings.

On October 21, 2003, Complainant filed the Amended Complaint in these proceedings.

On October 21, 2003, Complainant also filed a Motion to Amend Prehearing Exchange Exhibits in these proceedings. The additional exhibits sought to be introduced related to the charges raised for the first time in Complainant's Amended Complaint and consisted of business records of the Internal Revenue Service indicating that Respondent had not filed individual income tax returns for the tax years 1999, 2000, 2001 and 2002.

On October 29, 2003, Respondent filed a Motion to Abate the Case and Supporting Memorandum, as well as a Declaration of Robert G. Bernhoft in these proceedings. Respondent alleged that the Government was utilizing these proceedings as a means of obtaining evidence for a criminal prosecution under the "cloak" of a civil process.

On October 29, 2003, Respondent also filed a Motion for Discovery and Supporting Memorandum seeking to issue interrogatories to eighteen (18) current or former Internal Revenue Service or IRS Chief Counsel employees, including Complainant's counsel in these proceeding.

On October 31, 2003, Complainant filed a Motion for Summary Judgment in these proceedings.

On November 4, 2003, Complainant filed a document entitled Motion in Opposition to Respondent's Motion to Abate the Case in these proceedings. However, the document was in substance an Opposition to Respondent's Motion for Discovery filed in these proceedings, and is hereafter referred to, as it was by Respondent, as Complainant's Motion in Limine.

On November 7, 2003, Complainant filed a Motion in Opposition to Respondent's Motion to Abate the Case in these proceedings.

On November 7, 2003, Complainant also filed an Opposition to Respondent's Motion to Adjourn the Proceedings in these proceedings.

On November 10, 2003, Complainant filed an Opposition to Respondent's Motion to Dismiss the Amended Complaint in these proceedings.

On November 14, 2003, Respondent filed a Brief in Opposition to Complainant's Motion in Limine in these proceedings.

On November 17, 2003, Respondent filed a document entitled, "Respondent's Brief in Opposition to the IRS's Motion for Summary Disbarment" in these proceedings. In substance, the document was a Brief in Opposition to Complainant's Motion for Summary Judgment filed in these proceedings on October 31, 2003, and hereafter will be referred to as Respondent's Opposition to Complainant's Motion for Summary Judgment.

On November 17, 2003, Judge Moran entered an Order on the Respondent's Motion to Dismiss the Complaint, denying the Respondent's Motion.

On November 17, 2003, Judge Moran also entered an Order on Respondent's Motion for Discovery, denying the Respondent's Motion.

On November 17, 2003, Judge Moran also entered an Order on Complainant's Motion to Amend the Amended Complaint and to Amend Complainant's Prehearing Exchange Exhibits, granting both of Complainant's motions.

On November 17, 2003, Judge Moran also entered an Order Regarding Respondent's Motion to Adjourn the Hearing, denying Respondent's Motion.

On November 17, 2003, Judge Moran also entered an Order on Respondent's Motion to Dismiss the Amended Complaint, denying Respondent's Motion.

On November 19, 2003, Judge Moran entered an Order Regarding Respondent's Motion to Abate the Case, denying the Respondent's Motion.

On November 21, 2003, Judge Moran entered an Order Regarding Complainant's Motion in Limine. With the limited exceptions noted in his Order, Judge Moran granted the Complainant's Motion.

On November 24, 2003, Judge Moran entered an Order on Complainant's Motion for Summary Judgment. The Order, which incorporated by reference the other Orders entered in these proceedings between November 17, 2003 and November 21, 2003, granted Complainant's Motion as to liability, finding that Complainant had demonstrated by clear and convincing evidence that Respondent had committed each of the violations described in the Initial Complaint, as well as each of the violations first described in the Amended Complaint. As to the choice of a sanction to be imposed for these violations, Judge Moran reserved that issue to be addressed in a later Order.

On November 25, 2003, Complainant filed a Revised Witness List in these proceedings, noting that since the issues to be considered during the hearing had been limited to a consideration of the sanction to be imposed, David Finz, a Senior Attorney in the Office of Professional Responsibility, would be the Complainant's sole witness at the hearing.

On November 25, 2003, Respondent filed a Proffer of Offers of Proof and Argument at Hearing, requesting that six current or

former Internal Revenue Service or IRS Chief Counsel employees be called to testify at the hearing. Respondent also proposed to call undesignated witnesses named on his earlier filed witness list to testify as to his "good character, extraordinary skill, and exceptional ability as a practitioner on behalf of his clients . . .," as well as his record while in public service.

On November 25, 2003, Complainant filed a Response to Respondent's Proffer of Offers of Proof and Argument at Hearing.

On November 26, 2003, Complainant filed a Motion to Move Complainant Exhibits into Evidence at the Hearing.

On November 26, 2003, Judge Moran entered an Order regarding Admissible Evidence at the Sanctions Phase of Proceeding in which Judge Moran denied Respondent the right to introduce much of the evidence Respondent sought to introduce in his Proffer, on which Judge Moran had ruled previously in his Order on Complainant's Motion in Limine filed earlier in these proceedings. Judge Moran allowed Respondent to make a statement in his own behalf without being sworn or cross-examined, but refused Respondent's request that his counsel be permitted to present oral argument in the sanctions phase of the proceeding on subjects that had earlier been found by Judge Moran to be either immaterial or irrelevant to both the liability and sanction determinations to be made in these proceedings.

On December 1, 2003, Judge Moran presided at the hearing in these proceedings. The hearing consisted of: the direct, cross, re-direct and re-cross examination of the Complainant's sole witness, Mr. Finz; the reading of an unsworn statement by the Respondent (with respect to which Respondent was not cross-examined); and closing arguments by the counsels for the parties.

On December 24, 2003, Judge Moran entered the Decision of the Administrative Law Judge in these proceedings, finding the Respondent to have committed each of the violations

described in the Initial Complaint and the Amended Complaint, and disbarring the Respondent from practice before the Internal Revenue Service. In his Decision, Judge Moran noted that proof of either the charges contained in the Initial Complaint or the charges added by the Amended Complaint alone would support his decision to disbar Respondent.

On January 23, 2004, Respondent filed a Notice of Appeal and Appeal to the Secretary of the Treasury in these proceedings.

On February 27, 2004, Complainant filed Appellee-Complainant's Reply Brief, responding to the Respondent's Appeal in these proceedings.

The remainder of this Decision is divided into five parts. Part 1 deals with the scope and purpose of Circular 230 and the functions and purposes of the Administrative Law Judges and the Secretary of the Treasury or his or her delegate acting as the appellate authority in Treasury Circular 230 disciplinary proceedings. Part 2 deals with the allegations contained in the Initial Complaint. Part 3 deals with the allegations introduced by Complainant for the first time in the Amended Complaint. Part 4 deals with various constitutional and/or procedural objections raised by Respondent in his Appeal with respect to actions of the Complainant or Administrative Law Judge in these proceedings. Part 5 sets forth the Final Agency Decision in these proceedings.

1. Treasury Circular 230: Scope, Purpose and Roles of the Administrative Law Judge and Secretary's Delegate

31 U.S.C. §330, the statute under which Treasury Circular 230 was promulgated, provides the Secretary of the Treasury with express authority to regulate the practice of practitioners before the Department of the Treasury. 31 U.S.C. §330 provides, in pertinent part:

> "(a) Subject to section 500 of title 5 [5 U.S.C. § 500],

the Secretary of the Treasury may –

(1) regulate the practice of representatives of persons before the Department of the Treasury; and

(2) before admitting a representative to practice, require that the representative demonstrate –

(A) good character;

(B) good reputation;

(C) necessary qualifications to enable the representative to provide to persons valuable service; and

(D) competency to advise and assist persons in presenting their cases."

"(b) After notice and opportunity for a proceeding, the Secretary may suspend or disbar from practice before the Department a representative who –

(1) is incompetent;

(2) is disreputable;

(3) violates regulations prescribed under this section; or

(4) with intent to defraud, willfully and knowingly misleads or threatens the person being represented or a prospective person to be represented."

Moreover, Federal courts have long recognized that an administrative agency has general inherent authority to adopt rules of procedure, including the right to set standards for who may practice before it, even absent an express statutory grant of such authority. Goldsmith v. U.S. Board of Tax Appeals, 270 U.S. 117, 120-122 (1926). See also, Herman v. Dulles, 205 F.2d 715, 716 (D.C. Cir. 1953); Touche Ross & Co. v. SEC, 609 F.2d 570, 581-582 (2d Cir. 1979).

The scope and purpose of Treasury Circular 230, and of the statutory authority granted the Secretary of the Treasury by 31 U.S.C. § 330 and its statutory predecessor, 31 U.S.C. § 1026, have been considered by several Federal courts. See, e.g., Alker v. Humphrey, 247 F.2d 22 (D.C. Cir. 1957), cert. denied, 355 U.S.

841 (1957); Harary v. Blumenthal, 555 F.2d 1113 (2d Cir. 1977); Owrutsky v.Brady, 925 F.2d 1457 (4th Cir. 1991); Washburn v. Shapiro, 409 F. Supp. 3 (S.D. Fla. 1976); Poole v. United States, 84-2 U.S.Tax Cas. ¶ 9612 (D.D.C. 1984); Sicignano v. United States, 127 F. Supp. 2d 325 (D. Conn. 2001). These precedents establish that Treasury Circular 230 and its authorizing statute apply only to persons who practice before the Internal Revenue Service. In these proceedings, Respondent has admitted in his Answer, and the administrative record clearly reflects, both that Respondent, as a certified public accountant licensed to practice in the State of California, was authorized to practice before the Internal Revenue Service, and that he in fact has represented clients before the Internal Revenue Service. Accordingly, this threshold jurisdictional requirement for the application of Treasury Circular 230 to Respondent has been met.

The first case to examine in detail the scope and purpose of Treasury Circular 230 was Poole v. United States, supra. Poole, a certified public accountant authorized to practice and who in fact did practice before the Internal Revenue Service, was disbarred for willfully failing to file tax returns for three taxable years. Poole asserted that the statute under which Treasury Circular 230 was promulgated applied only to those who represented "claimants" before the Internal Revenue Service, which Poole asserted included only those individuals seeking monetary reimbursement. Poole also asserted that Congress' only concern was protecting the interests of claimants seeking reimbursement from the Department of the Treasury. Accordingly, Poole asserted that, even if the term "claimant" was expanded to include the representation of any taxpayer on any matter before the Internal Revenue Service, his conduct in failing to file his own tax returns was unrelated to these areas of Congress' concern.

The Court found that "neither the plain language of 31 U.S.C. § 330 (formerly § 1026) (1983), its legislative history, nor common sense supports plaintiff's interpretation." Rather than finding the language of the statute or its legislative history to be

so limited in scope or purpose, the Court found that, "[r]ather, Congress intended to regulate, in a general way, the activities of practitioners before the Treasury Department."

The Court also found that whatever ambiguity may have existed concerning the original Congressional debate surrounding the enactment of 31 U.S.C. §1026 had been well settled by subsequent Congressional and administrative developments. Noting that (i) the Treasury Department had interpreted its statutory authority to permit the regulation of all those who practice before the Internal Revenue Service since 1922, (ii) courts must uphold an agency's reasonable interpretation of a statute it administers (citing Howe v. Smith, 452 U.S. 473, 485 (1981), and Udall v. Tallman, 380 U.S. 1, 16 (1965)), and (iii) the Department's interpretation of its statutory authority enjoyed prior judicial approval (citing Goldsmith v. U.S. Board of Tax Appeals, supra), the Court concluded that an administrative agency has the inherent authority to prescribe its rules of procedure and as part thereof may set standards for determining who may practice before it.

Poole next argued that his failure to file his own tax returns did not constitute "disreputable conduct" which could appropriately make him subject to disbarment. In effect, Poole argued that the failure to file a tax return, while clearly defined as disreputable conduct under §10.51(d) of Circular 230, did not constitute "disreputable conduct" within the meaning of 31 U.S.C. §1026 (later 31 U.S.C. §330). The Court disagreed, finding that the word "disreputable" has several different meanings, depending on the context in which the term is used. The Court went on to note:

> **"With respect to attorneys or other agents, 'disreputable' conduct has generally included 'unprofessional' conduct and, at the time the Act of July 7, 1884 was written, was well understood to include 'any conduct violative of the ordinary standard of professional obligation and honor.' Garfield v. United States ex rel.**

Stevens, 32 App. D.C. 109, 140 (1908). That failure of a certified public accountant to file his own tax returns falls outside the range of ordinary professional obligation seems plain enough. Cf. Evans v. Watson, 269 F.2d 775, 778 (D.C. Cir. 1959), cert. denied, 361 U.S. 900 (1959) . . .."

The Court went on to note that a disbarment proceeding under Treasury Circular 230 had been found by the Court in Harary v. Blumenthal, supra, to be essentially a determination of one's "fitness to practice" before the Internal Revenue Service, and further found that it was appropriate for the agency to consider factors in determining whether to allow someone to continue to practice before the agency that would not appropriately have been considered in determining his or her initial admission to practice (finding Poole's failures to file to be such a factor). The Court concluded:

"As determined by the Treasury Department, willful failure to file tax returns, in violation of federal revenue laws, is dishonorable, unprofessional, and adversely reflects on the petitioner's fitness to practice. This is particularly true in a tax system whose very effectiveness depends upon voluntary compliance."

Treasury Circular 230's purpose was further explained in Sicignano v. United States, supra:

"[T]he Treasury Department's rules and regulations governing practice before the IRS are aimed at protecting the integrity of a tax system that depends upon voluntary compliance."

Id. at 332.

To insure that integrity, and in recognition of the fact that practitioners who represent taxpayers before the Internal Revenue Service discharge both obligations to their clients and obligations to the agency before which they practice, Treasury

Circular 230 sets forth rules and regulations relating to a practitioner's activities as a taxpayer representative, as an adviser to taxpayers and relating to the practitioner's conduct of his or her own tax and other affairs.

In United States v. Boyle, 469 U.S. 241 (1985), a case involving a civil penalty imposed against an executor for the late filing of an estate tax return, the issue before the United States Supreme Court was whether the executor had "reasonable cause" for his late filing because he had relied on a tax practitioner to assure that he met his filing obligations in a timely manner. The record showed that Boyle had hired a competent lawyer and had been diligent in following up with the lawyer concerning his obligations as executor, including his obligation to timely file an estate tax return. The Court nevertheless found that his failure to timely file was not due to "reasonable cause" and upheld the Internal Revenue Service's assertion of a civil failure to file penalty against him. In so holding, the Court discussed the importance of timely compliance with our tax laws and the duties and responsibilities assigned to taxpayers and practitioners alike in assuring that compliance:

> **"Deadlines are inherently arbitrary; fixed dates, however, are often essential to accomplish necessary results. The Government has millions of taxpayers to monitor, and our system of self-assessment in the initial calculation of a tax simply cannot work on any basis other than one of strict filing standards. Any less rigid standard would risk encouraging a lax attitude toward filing dates. Prompt payment of taxes is imperative to the Government, which should not have to assume the burden of ad hoc determinations.**
>
> **"Congress has placed the burden of prompt filing on the executor, not on some agent or employee of the executor. The duty is fixed and clear; Congress intends to place upon the taxpayer an obligation to ascertain the statutory deadline and then to meet that deadline, except in a very narrow range of situations. Engaging an attorney**

to assist in the probate proceedings is plainly an exercise of the 'ordinary business care and prudence' prescribed by the regulations . . . , but that does not provide an answer to the question we face here. To say that it was 'reasonable' for the executor to *assume* that the attorney would comply with the statute may resolve the matter as between them, but not with respect to the executor's obligations under the statute. Congress has charged the executor with an unambiguous, precisely defined duty to file the return within nine months; extensions are granted fairly routinely. That the attorney, as the executor's agent, was expected to attend to the matter does not relieve the principal of his duty to comply with the statute.

"This case is not one in which a taxpayer has relied on the erroneous advice of counsel concerning a question of law. . . .

"When an accountant or attorney advises a client on a matter of tax law, such as whether a liability exists, it is reasonable for the taxpayer to rely on that advice. . . .

"By contrast, one does not have to be an expert to know that tax returns have fixed filing dates and that taxes must be paid when they are due. . . ."

Id. at 249-251 (footnote omitted).

This language underscores the importance of assuring the competence and integrity of practitioners given practitioners' important role in assuring compliance with our tax laws and in making a fair determination of correct tax liabilities in our self-assessment tax system. It is that which the Department of the Treasury seeks to assure through Treasury Circular 230.

The powers of the Administrative Law Judge in disciplinary proceedings initiated under §10.60 of Treasury Circular 230 are specified in §10.70(b) of Circular 230. In general, they include the power to (1) administer oaths and affirmations; (2) make rulings on motions and requests; (3) determine the time and place of hearing and regulate its course and conduct; (4) adopt and

modify rules of procedure; (5) rule on offers of proof, receive relevant evidence and examine witnesses; (6) take or authorize the taking of depositions; (7) receive and consider oral or written argument on facts or law; (8) hold or provide for the holding of conferences for the settlement or simplification of issues to be considered with the consent of the parties; (9) perform such acts and take such measures as are necessary or appropriate to the efficient conduct of any such proceeding; and (10) make decisions. In effect, the Administrative Law Judge acts as the trial court in the proceedings, determining, among other things, whether the Director of the Office of Professional Responsibility has met his burden of proof with respect to the specific allegations supporting the charges leveled in the complaint (or, in these proceedings, in the Initial Complaint and the Amended Complaint). All such determinations are made de novo. Under § 10.76(a) of Treasury Circular 230, the extent of the Complainant's burden of proof in any proceeding depends upon the sanction the Complainant seeks to have imposed. If the requested sanction is either censure or suspension for a period of less than six months, the Complainant must prove his case by a preponderance of the evidence. If the requested sanction is suspension for a period of six months or more, or disbarment (as in these proceedings), the Complainant must prove his case by clear and convincing evidence.

The decision of the Administrative Law Judge is the initial determination of the agency. If neither the Complainant nor the Respondent appeals the Decision of the Administrative Law Judge within thirty days, the decision of the Administrative Law Judge becomes the final decision of the agency without further proceedings. §10.76(b) of Treasury Circular 230.

If either the Complainant or the Respondent timely appeals the decision of the Administrative Law Judge, the Secretary of the Treasury or his or her delegate acts as an appellate authority to review the Administrative Law Judge's preliminary decision. §10.77 of Treasury Circular 230. The Director of the Office of Professional Responsibility provides a copy of the entire record

in the proceedings to the Secretary or his or her delegate and it is that record which forms the basis of the appellate review. Id. Decisions of the Administrative Law Judge will not be reversed unless the appellant establishes that the decision is clearly erroneous in light of the facts in the record and the applicable law. However, issues that are exclusively questions of law (as opposed to questions of fact or mixed questions of fact and law) are reviewed de novo. In the event that the Secretary or his or her delegate determines that there are unresolved issues raised by the record, the case may be remanded to the Administrative Law Judge to permit the development of additional testimony or evidence. Decisions of the Secretary or his or her delegate in any such appeals constitute final agency action. §10.78 of Treasury Circular 230.

2. Allegations Raised in the Initial Complaint

The Initial Complaint in these proceedings contained five charges alleging various violations of Treasury Circular 230 by Respondent:

Complainant charged that Respondent failed to exercise due diligence in violation of §§10.22(b) and 10.22(c) of Treasury Circular 230 and engaged in disreputable conduct in violations of §§10.34, 10.51, 10.51(d) and 10.51(j) by giving advice to Taxpayer C and Taxpayer T that had no basis in law or fact and, while representing the same taxpayers before the Internal Revenue Service, took a position that had no substantive basis in law or fact. Complainant made four specific allegations in support of this charge which are delineated in the Preliminary Statement above. Specifically, Complainant alleged that, with respect to Taxpayer C, Respondent advised the taxpayer with respect to tax liabilities for the taxable years 1989 through 1998, inclusive, that (1) Taxpayer C was not liable for income taxes because the Sixteenth Amendment to the Constitution of the United States was "not ratified" and (2) §861 of the Internal Revenue Code of 1986 and the regulations thereunder defined "source" of income in such a way as to exclude Taxpayer C's income from taxation.

Futher, Complainant alleged that, with respect t[illegible]axpayer T and his tax liabilities for the years 1989 through 1998, inclusive, Respondent (1) advised Taxpayer C that §861 of the Internal Revenue Code of 1986 and the regulations thereunder defined "source" of income in such a way as to exclude Taxpayer T's income from taxation, and (2) signed as a paid preparer Taxpayer T's Amended U.S. Individual Income Tax Returns (Forms 1040X) for the years 1996 and 1998, in each instance stating that Taxpayer T's income for these years was not taxable income per §§861-865 of the Internal Revenue Code of 1986, which returns were filed with the Internal Revenue Service, thereby engaging in disreputable conduct in violation of §10.34 of Treasury Circular 230. Of the four specific allegations supporting these charges contained in the Initial Complaint, only the fourth [relating to the preparation of Taxpayer T's Amended Tax Returns (Forms 1040X) for 1996 and 1998 supports the charge that Respondent violated §10.34 of Treasury Circular 230.

§§10.22(b) and 10.22(c) of Treasury Circular 230, as amended and in effect on the dates of the alleged conduct, provided, in pertinent part:

> "Each attorney, certified public accountant, enrolled agent, or enrolled actuary shall exercise due diligence:
>
> * * * * * * * * *
>
> (b) In determining the correctness of oral or written representations made by him to the Department of the Treasury; and
>
> (c) In determining the correctness of oral or written representations made by him to clients with reference to any matter administered by the Internal Revenue Service."

§10.34 of Treasury Circular 230 (setting forth standards for advising with respect to tax return positions and for preparing or signing returns), as amended and in effect as of the dates of the

conduct forming the basis of these charges, provided, in pertinent part:

> **(a) *Standards of Conduct* – (1) *Realistic possibility standard.* A practitioner may not sign a return as a preparer if the practitioner believes that the return contains a position that does not have a realistic possibility of being sustained on its merits (the realistic possibility standard) unless the position is not frivolous, and is adequately disclosed to the Service. A practitioner may not advise a client to take a position on a return, or prepare the portion of the return on which the position is taken, unless –**
>
> **(i) The practitioner determines that the position satisfies the realistic possibility standard; or**
>
> **(ii) The position is not frivolous and the practitioner advises the client of any opportunity to avoid the accuracy-related penalty in section 6662 of the Internal Revenue Code of 1986 by adequately disclosing the position and of the requirements for adequate disclosure.**
>
> **(2) *Advising client on potential penalties.* A practitioner advising a client to take a position on a return, or preparing or signing a return as a preparer, must inform the client of the penalties reasonably likely to apply to the client with respect to the position advised, prepared or reported. The practitioner also must inform the client of any opportunity to avoid any such penalty by disclosure, if relevant, and of the requirements for adequate disclosure. This paragraph (a)(2) applies even if the practitioner is not subject to a penalty with respect to the position.**
>
> * * * * * * * * *
>
> **(4) *Definitions.* For purposes of this section:**
>
> **(i) *Realistic possibility.* A position is considered to have a realistic possibility of being sustained on its merits if a reasonable and well-informed analysis by a person knowledgeable in the tax law would lead such a person to conclude that the position had**

approximately a one in three, or greater, likelihood of being sustained on its merits. The authorities described in 26 CFR 1.6662-4(d)((3)(iii), or any successor provision, of the substantial understatement penalty regulations may be taken into account for purposes of this analysis. The possibility that a position will not be challenged by the Service (e.g., because the taxpayer's return may not be audited or because the issue may not be raised on audit) may not be taken into account.
(ii) *Frivolous*. A position is frivolous if it is patently improper.

(b) *Standard of discipline*. As provided in §10.52, only violations of this section that are willful, reckless, or a result of gross incompetence will subject a practitioner to suspension or disbarment from practice before the Service."

§10.51 of Treasury Circular 230, as amended and in effect on each of the dates in issue, provided in pertinent part:

> **"Disreputable conduct for which an attorney, certified public accountant, enrolled agent, or enrolled actuary may be disbarred or suspended from practice before the Internal Revenue Service includes, but is not limited to:**
>
> *** * * * * ***
>
> **(d) Willfully failing: to make a Federal tax return in violation of the revenue laws of the United States, or evading, or attempting to evade, or participating in any way in evading or attempting to evade any Federal tax or payment thereof, knowingly counseling or suggesting to a client or prospective client an illegal plan to evade Federal taxes or payment thereof, or concealing**

assets of himself or another to evade Federal taxes or the payment thereof.

* * * * * * * * *

(j) Giving a false opinion, knowingly, recklessly or through gross incompetence, including an opinion which is intentionally or recklessly misleading, or a pattern of providing incompetent opinions on questions arising under the Federal tax laws. False opinions described in this paragraph include those which reflect or result from a knowing misstatement of fact or law; from an assertion of a position known to be unwarranted under existing law; from counseling or assisting in conduct known to be illegal or fraudulent; from concealment of matters required by law to be revealed; or from conscious disregard of information indicating that material facts expressed in the tax opinion or offering material are false or misleading. For purposes of this paragraph, reckless conduct is a highly unreasonable omission or misrepresentation involving an extreme departure from the standards of ordinary care that a practitioner should observe under the circumstances. A willful pattern of conduct is a factor that will be taken into account in determining whether a practitioner has acted knowingly, recklessly or through gross incompetence. Gross incompetence includes conduct that reflects gross indifference, preparation which is grossly inadequate under the circumstances, and a consistent failure to perform obligations to the client."

While not a provision referred to by Complainant in the Initial Complaint, also germane to these charges is §10.52 of Treasury Circular 230, which provides:

> **"A practitioner may be disbarred or suspended, from practice before the Internal Revenue Service for any of the following:**
>
> **(a) Willfully violating any of the regulations contained in this part.**
>
> **(b) Recklessly or through gross incompetence (within the meaning of § 10.51(j)) violating §10.33 or § 10.34 of this part."**

§10.33 of Treasury Circular 230, as amended and in effect on the dates in issue, deals with standards applicable to tax shelter opinions and has no relevance to the charges contained in the Initial Complaint. As noted above, §10.34 of Treasury Circular 230, as amended and in effect for the dates in issue, has relevance to the charges contained in the Initial Complaint only with respect to Respondent's actions in preparing Taxpayer T's Amended U.S. Individual Income Tax Returns (Forms 1040X) for 1996 and 1998, both of which were submitted to the Internal Revenue Service. Accordingly, with respect to all other charges contained in the Initial Complaint, only willful violations of the provisions of Treasury Circular 230 form a basis for disbarment or suspension from practice before the Internal Revenue Service. §10.52(a) of Treasury Circular 230.

With respect to a practitioner's actions in preparing tax returns, a practitioner must either (1) ascertain that an asserted position has a realistic possibility of being sustained on the merits, or (2) assure both that the position be adequately disclosed to the Internal Revenue Service and that the position not be frivolous. The "realistic possibility" standard, borrowed from the civil penalty regime established under § 6662(d)(2)(B)(i) of the Internal Revenue Code of 1986, as amended and in effect during the periods in issue, excludes items for which there is a "realistic possibility" that the position will be sustained on its

merits and, in some instances, items that are adequately disclosed and non-frivolous from the calculation of "substantial understatements" of income tax. The "realistic possibility" standard is a substantially higher standard than the requirement that an item not be frivolous. §10.34(a)(4) of Treasury Circular 230 requires that a reasonable and well-informed analysis of the law and the facts by a person knowledgeable in the tax law would lead that person to conclude that there was a one in three, or greater, chance of the taxpayer's position on the issue being sustained on its merits.

While Treasury Circular 230 does not provide an extensive definition of "frivolous" (§10.34(a)(4)(ii) of Treasury Circular 230 defining the term only as meaning "patently improper"), the term has been widely used by many courts in cases involving the determination of whether it is appropriate to impose both civil and criminal tax penalties, and is applied by the courts in determining the permissible scope of advocacy before tribunals.

For example, Rule 33(b) of the Rules of Practice of the United States Tax Court provides, in pertinent part:

> **"RULE 33. SIGNING OF PLEADINGS.**
>
> * * * * * * * * * *
>
> **(b) Effect of Signature: The signature of counsel or a party constitutes a certificate by the signer that the signer has read the pleading; that, to the best of the signer's knowledge, information and belief formed after reasonable inquiry, it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law; and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation."**

Likewise, Rule 11(b) of the Federal Rules of Civil Procedure

provides:

> **"Representations to Court. By presenting to the court (whether by signing, filing, submitting, or later advocating) a pleading, written motion, or other paper, an attorney or unrepresented party is certifying that to the best of the person's knowledge, formed after an inquiry reasonable under the circumstances, --**
>
> (1) **it is not being presented for an improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation;**
>
> (2) **the claims, defenses, and other legal contentions therein are warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law;**
>
> (3) **the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery; and**
>
> (4) **the denials of factual contentions are warranted on the evidence or, if specifically so identified, are reasonably based on a lack of information or belief."**

See also Rule 38 of the Federal Rules of Appellate Procedure (discussed at p. 27, infra).

Similarly, with regard to oral and written representations made to either the Treasury or to a client in connection with any

matter administered by the Internal Revenue Service, each attorney, certified public accountant, enrolled agent and enrolled actuary is required to exercise due diligence in determining the correctness of such statements. §§ 10.22(b) and 10.22(c) of Treasury Circular 230. These obligations exist both with respect to factual representations and representations with respect to the law and the law's application to the facts present in a particular case. Certainly, any argument that is found frivolous is also incorrect, and an argument that is found to be frivolous is certainly incapable of meeting the higher "realistic possibility" standard.

Respondent has asserted that his conduct should be judged by the state of the law as it existed on the dates of his alleged violations. Respondent has also asserted that in assessing his conduct, the Secretary should be mindful of the need to preserve zealous advocacy by practitioners on behalf of taxpayers, and that particular sensitivity to such concerns is appropriate in unsettled areas of the law.

While I am in general agreement with these propositions, none stands without limits. Zealous advocacy does not constitute license for the assertion of frivolous positions when representing taxpayers before the Internal Revenue Service. Nor does the concept extend, at least in the same manner, to a practitioner's functions as an adviser. Moreover, while it is true that the Secretary should exercise particular sensitivity in challenging arguments in unsettled areas of the law, that does not mean that it is never appropriate to question the assertion of clearly erroneous positions merely because they have never before been considered by the courts. In addition, while I agree that a practitioner's conduct should be considered solely in light of the state of the law on the date(s) of his conduct, if a later decision considers the merits of an argument and does so in a manner that casts light on the legitimacy of the argument on earlier relevant date(s), that later consideration may also shed light on whether the theory was frivolous on those earlier date(s). Finally, for the reasons set forth below, I find that these theories

have little effect on these proceedings since I agree with Judge Moran that the law, both with respect to Respondent's Sixteenth Amendment argument and with respect to his "source" argument under §§ 861-865, was well settled on the relevant dates.

The constitutionality of the 16th Amendment to the United States Constitution was sustained by the United States Supreme Court as early as 1916. Brushaber v. Union Pacific Railroad Company, 240 U.S. 1 (1916). Subsequently, an uninterrupted line of decisions by various United States Courts of Appeals have reaffirmed that conclusion against claims that the 16th Amendment was either "not ratified" or "fraudulently adopted." See, e.g., Miller v. United States, 868 F.2d 236 (7th Cir. 1989); United States v. Sitka, 845 F.2d 43 (2d Cir. 1988); Pollard v. Commissioner, 816 F.2d 603 (11th Cir. 1987); United States v. Thomas, 788 F.2d 1250 (7th Cir. 1986); United States v. Stahl, 792 F.2d 1438 (9th Cir. 1986); Sisk v. Commissioner, 791 F.2d 58, 60 (6th Cir. 1986); Knoblauch v. Commissioner, 749 F.2d 200, 202 (5th Cir. 1984); Parker v. Commissioner, 724 F.2d 469, 471 (5th Cir. 1984).

Several of these decisions were either criminal convictions involving willfulness determinations or findings by the courts in civil tax cases that the argument asserted was frivolous. See, e.g., Miller v. United States, supra; Knoblauch v. Commissioner, supra. In Knoblauch v. Commissioner, supra, the Court of Appeals imposed sanctions under Rule 38 of the Federal Rules of Appellate Procedure against a taxpayer proceeding pro se, finding that the appeal was baseless, presented no colorable claim of error and raised repeatedly rejected contentions. Rule 38 of the Federal Rules of Appellate Procedure, which serves a function similar to Rule 11 of the Federal Rules of Civil Procedure, provides:

> "If a court of appeals shall determine that an appeal is frivolous, it may award just damages and single or double costs to the appellee."

Similarly, in Miller v. United States, supra, the court found the appeal (premised, inter alia, on Sixteenth Amendment arguments) "patently frivolous" and, quoting Granzow v. Commissioner, 739 F.2d 265, 269-270 (7th Cir. 1984), noted "we can no longer tolerate abuse of the judicial review process by irresponsible taxpayers who press stale and frivolous arguments . . .." Id. at 242.

In summary, more than a decade before the conduct giving rise to Respondent's alleged violations, the courts had both uniformly sustained the constitutionality of the 16th Amendment and found that arguments to the contrary were frivolous when asserted by ordinary taxpayers, let alone by experienced tax practitioners.

Respondent's argument premised on the "sourcing" rules of §§ 861-865 of the Internal Revenue Code of 1986, as amended and in effect during the years in issue, stand on no firmer footing. §§1(a), 1(b), 1(c) and 1(d) of the Internal Revenue Code of 1986, as amended and in effect during the years in issue, imposed a tax on the taxable income of (i) married individuals filing joint returns and surviving spouses, (ii) heads of households, (iii) unmarried individuals (other than surviving spouses and heads of households), and (iv) married individuals filing separate returns, respectively. §61(a) of the Internal Revenue Code of 1986, as amended and in effect during the years in issue, provided:

> **"Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) [fifteen enumerated items]." (Emphasis added.)**

§1.61-1(a) of the Treasury Regulations further elaborated on this statutory language:

> **"Gross income. – (a) *General definition.* Gross income means all income from whatever source derived, unless excluded by law. Gross income includes income realized in**

any form, whether in money, property, or services. Income may be realized, therefore, in any form, whether in money, property or services. Income may be realized, therefore, in the form of services, meals, accommodations, stock, or other property, as well as in cash. Section 61 lists the more common items of gross income for purposes of illustration. For purposes of further illustration, § 1.61-14 mentions several miscellaneous items of gross income not listed specifically in section 61. Gross income, however, is not limited to the items so enumerated." (Emphasis added.)

The language of §61(a) itself and the language of the regulations issued thereunder, which have the force and effect of law, both demonstrate that Congress intended §61(a) to encompass all sources of income. The courts have also recognized the all-encompassing scope of §61(a) and the fact that it is intended to have an ambit equaling that of the Sixteenth Amendment. See, e.g., Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955), where the United States Supreme Court noted that, "Congress applied no limitations as to the source of taxable receipts." Id. at 429.

In each of the years here in issue, in the case of United States citizens and resident aliens, the United States generally taxed the worldwide income of such individuals under §§ 1(a), 1(b), 1(c) or 1(d) of the Internal Revenue Code of 1986, as amended and in effect. With two limited exceptions, the sourcing rules of §§861-865 of the Internal Revenue Code of 1986, as amended and in effect during those years, had no effect on the determination of the United States tax liabilities of United States citizens and resident alien individuals. § 911(a) of the Internal Revenue Code of 1986, as amended and in effect for the years in issue, excluded from the gross income of an electing qualified individual, (1) the "foreign earned income" of that individual (an amount subject to an inflation adjusted "cap") and (2) the "housing cost amount" of the individual. Also, to ameliorate the effects of double taxation on income of United States persons (including United States citizens and resident alien individuals)

from sources "without the United States," §§ 901-908 of the Internal Revenue Code of 1986, as amended and in effect during the years in issue, allowed such persons a limited credit against their United States tax liabilities for taxes paid with respect to sources of income without the United States that were subjected to specified forms of tax imposed on the same income by those foreign jurisdictions. Neither of these specific provisions departing from the general rules had any application to Taxpayer C or Taxpayer T.

The source of income rules, now codified as §§861-865 of the Internal Revenue Code of 1986, had their origin in provisions adopted as early as 1913. The Revenue Act of 1913, ch. 16, 38 Stat. 114, imposed a tax on nonresident aliens with respect to net income "from all property owned and of every business, trade or profession carried on in the United States by persons residing elsewhere," and on foreign corporations with respect to net income "accruing from business transacted and capital invested within the United States. Revenue Act of 1913, ch. 16, §§II(A)(1), II(G)(a), 38 Stat. 114, 166, 172. The sourcing rules were then more explicitly addressed in the enactment of the Revenue Act of 1916, which imposed a tax on the net income of foreign persons (nonresident alien individuals and foreign corporations) from sources within the United States. Ch. 463, 39 Stat. 756. These rules were not substantively modified by the Revenue Act of 1917, which only changed the statutory rates on the income so subjected to tax. Ch. 63, §§2-3 (nonresident aliens) and §4 (foreign corporations), 40 Stat. 300, 301, 302.

Initially, neither these statutory provisions nor the regulations issued thereunder (see, e.g., Treas. Reg. 33, art. 66 (1918)) provided detailed rules or methodologies for determining the sources of income. Over the years, both the statutes themselves and the regulations issued thereunder adopted more specific source of income rules. However, both the statutes and regulations continued to reflect Congress' basic statutory scheme of taxing the worldwide income of U.S. persons (including U.S. citizens, resident aliens and U.S. corporations,

while adopting a "water's edge" regime for the taxation of foreign persons (including nonresident alien individuals and foreign corporations). Thus the purpose and intent of the "source of income rules was hardly a closely guarded secret at the time of Respondent's conduct. For example, the opening "PORTFOLIO DESCRIPTION SHEET" of BNA's Tax Management Portfolio 905 (Source of Income Rules) at all times relevant to these proceedings provided:

> **"Tax Management Portfolio 905, *Source of Income Rules,* analyzes the rules applicable in determining whether income is treated as from sources within the United States or from foreign sources. In the case of persons who are not citizens or residents of the United States or domestic corporations, and thus are not subject to tax on their worldwide income, the source of income rules generally are pivotal in determining whether the tax jurisdiction of the United States extends to the income. In addition, in the case of all persons who are subject to U.S. tax, the source of income rules are critical to determining to what extent a credit is available for income taxes or taxes in lieu of income taxes paid to a foreign government. The source of income rules are applied in conjunction with the rules governing the allocation and apportionment of expenses between domestic and foreign sources in order to determine foreign source taxable income for purposes of the foreign tax credit limitation prescribed for each separate limitation category under § 904."**

Blessing, 905 T.M., *Source of Income Rules.* See also Section I.A.1 of the Detailed Analysis contained in the same secondary source material (dealing with the taxation of "U.S. persons," defined to include United States citizens, resident alien individuals and U.S. corporations), Id. at A-1. In addition, several IRS publications providing general information to taxpayers provide information on the appropriate uses of §§861-865's "source of income" rules. See Publication 54 (US Tax Guide for US Citizens and Resident Aliens Living Abroad), Publication 514

(Foreign Tax Credit for Individuals), Publication 515 (Withholding of Tax on Nonresident Individuals), and Publication 519 ((US Tax Guide for Aliens).

The purpose and intent of the "source of income" rules were hardly a closely guarded secret at the time of Respondent's conduct. The argument advanced by Respondent and his counsel, also asserted by Respondent in a submission pertaining to a Collection Due Process Hearing Respondent sought on behalf of Taxpayer C, and by Respondent in the 1996 and 1998 amended federal individual income tax returns (Forms 1040X) he prepared for Taxpayer T for 1996 and 1998 that were later filed with the Internal Revenue Service, would stand the sourcing rules on their head, using them as a basis for limiting the tax liabilities of U.S. citizens and resident aliens residing in the United States with respect to income sourced within the United States.

These arguments were first directly considered by a court in Solomon v. Commissioner, T.C. Memo. 1993-509, 66 T.C.M. (CCH) 1201 (1993), affirmed without published opinion, 42 F.3d 1391 (7th Cir. 1994), where Judge Dawson found that neither §§861(a)(1) and 861(a)(3) nor § 911(d)(2)(A) provided a basis for excluding from gross income (i) interest income from sources within the United States or (ii) compensation received for the performance of personal services within the United States when received by a United States citizen residing in the United States.

A similar argument was next considered by the Tax Court in Aiello v. Commissioner, T.C. Memo 1995-40, 69 T.C.M. (CCH) 1765 (1995) where the taxpayer asserted that (1) no Federal statute imposed a tax on the income of citizens or residents of the United States that is derived from sources within the United States and (2) Federal income taxes were imposed only on the privilege of nonresident aliens and foreign corporations to receive income from sources within the United States. Noting that the taxpayer's first argument was clearly rebuffed by the existence of § 61(a) and that his argument that the source rules

of §861 somehow limited the all inclusive scope of §61(a)'s gross income definition was unclear, Special Trial Judge Wolfe held that the taxpayer was clearly required to include income from whatever source derived in calculating his gross income, his taxable income and his liability for tax.

The Tax Court next considered the argument in Williams v. Commissioner, 114 T.C. 136 (2000), where the Tax Court clearly stated that the taxpayer was arguing that since his income was not from any of the sources enumerated in § 1.861-8(a) of the regulations, that income was not appropriately subject to taxation in the United States. In assessing this argument, Judge Vasquez stated:

> **"We shall not painstakingly address petitioner's assertions 'with somber reasoning and copious citation of precedent; to do so might suggest that these arguments have some colorable merit.' *Crain v. Commissioner,* 737 F.2d 1417, 1417 (5th Cir. 1984). Accordingly, we conclude that petitioner is liable for the deficiency determined by respondent."**

Id. at 139.

Judge Vasquez then considered whether he should sustain the §6673 penalty imposed against the pro se petitioner. Noting that such a penalty is appropriately imposed only if the position taken is frivolous, Judge Vasquez noted that a position is frivolous only "where it is 'contrary to established law and unsupported by a reasoned, colorable argument for a change in the law.'" Id. at 144 (citing Coleman v. Commissioner, 791 F.2d 68, 71 (7th Cir. 1986)). Considering this standard, Judge Vasquez nonetheless imposed the §6673 penalty against the taxpayer.

The Tax Court again considered the arguments first advanced in Solomon v. Commissioner, supra, in Furniss v. Commissioner, T.C. Memo 2001-137, 81 T.C.M. (CCH) 804 (2001). Judge Marvel found that "[n]either section 911 nor section 861

operates to prevent section 61 from applying to petitioner's receipts."

Accordingly, on four separate occasions, three different Judges and one Special Trial Judge of the United States Tax Court determined that the § 911 argument, the § 861 argument or both in combination did not prevent the income of a United States citizen, residing in and earning income from sources within the United States, from being included in gross income under §61(a) and from being subject to tax under §§1(a), 1(b), 1(c) or 1(d). The only decision of the Tax Court appealed was affirmed on appeal, again prior to the dates of Respondent's conduct.

Moreover, even earlier, in 1985, a United States District Court issued an opinion in Peth v. Breitzmann, 611 F. Supp. 50 (E.D. Wisc. 1985), in which a pro se taxpayer sought to enjoin collection of Federal income taxes and to obtain a refund of taxes alleged to have been wrongfully withheld from his pay. The taxpayer argued, inter alia, that his compensation was excludable from the definition of gross income under §861(a)(3)(C)(ii) as "compensation . . . for labor or services performed in the United States as an employee of or under a contract with . . . an individual who is a citizen or resident of the United States, a domestic partnership, or a domestic corporation, if such labor or services are performed for an office or place of business maintained in a foreign country or in a possession of the United States by such individual, partnership, or corporation." The court gave short shrift to this argument, noting:

> **"Suffice it to say that if plaintiff wished to avail himself of § 863(a)(3)(C)(ii), he would have to show that his work was done for a foreign office, or an office in a United States possession, of a domestic business entity. He has not alleged this, and it is clear from the record that he performed his work in the State of Wisconsin for Wisconsin employers."**

Id. at 55. The court could also have noted that even in those circumstances, §861(a)(3)(C)(ii) would have excluded the income from inclusion in United States gross income only if the recipient was also a nonresident alien temporarily in the United States for a period or periods not exceeding 90 days during the taxable year. Finding these and the other arguments advanced by the plaintiff to be without merit, the court imposed Rule 11 sanctions against the pro se taxpayer. Id. at 56-57.

The District Court's decision in Peth v. Breitzmann, supra, the Tax Court decision and 7th Circuit's summary affirmance in Solomon v. Commissioner, supra, and the Tax Court's decision in Aiello v. Commissioner, supra each preceded the dates of Respondent's conduct. Further, the dispatch with which Judge Vasquez dealt with petitioner's arguments in Williams v. Commissioner, supra, and the fact that he saw fit to impose a §6673 penalty against a pro se taxpayer based on the same state of the law that existed on the dates of Respondent's conduct, support Judge Moran's conclusion that each of the actions undertaken by Respondent as alleged in the Initial Complaint involved the assertion of frivolous arguments in violation of the various sections of Treasury Circular 230 cited in the Initial Complaint. While I would have phrased the point differently, I agree with the spirit of the following statement by Judge Moran, appearing at page 6 of his Order on Complainant's Motion for Summary Judgment:

> **"Interestingly, the language of IRC Section 61 is the same as that used in the Sixteenth Amendment. Thus, the 861 argument and the non-ratified Sixteenth Amendment argument share a related lunacy in that, for differently concocted reasons, neither accomplishes the presumed goal of creating a Federal income tax on U.S. citizens."**

Accordingly, I find that Respondent's arguments are now and were at the time of Respondent's conduct patently improper and therefore frivolous. See §10.34(a)(4)(ii) of Treasury Circular 230.

Having concluded that both Respondent's Sixteenth Amendment argument and his argument predicated on the §§861-865 "source" rules are now and were then frivolous, I next turn to the question of whether the conduct in question is an offense of the type justifying disbarment or suspension under §10.52 of Treasury Circular 230. For the reasons stated below, I find that the violations in question independently justify Judge Moran's decision to disbar Respondent.

Respondent's actions in preparing Taxpayer T's amended Federal income tax returns (Forms 1040X) for the years 1996 and 1998 are to be judged under the standards set forth in both §10.52(a) and §10.52(b) of Treasury Circular 230. As noted elsewhere in Section 2 of this Decision (see pp. 39 -- 58, infra), I also agree that Respondent's conduct was willful. Under §10.52(a) of Treasury Circular 230, a practitioner may be disbarred or suspended from practice before the Internal Revenue Service for willfully violating any of the regulations contained in Treasury Circular 230, while under §10.52(b) of Treasury Circular 230 a practitioner may be disbarred or suspended for recklessly or through gross incompetence (within the meaning of §10.51(j) of Treasury Circular 230) violating either §10.33 or §10.34 of the Circular.

Treasury Circular 230 does not itself contain a definition of "willfulness." §10.51(j) of Treasury Circular 230, however, quoted verbatim at p. 22, supra, defines and provides examples of conduct deemed either "reckless" or "grossly incompetent."

I agree with Judge Moran's finding that the preparation of Taxpayer T's amended individual income tax returns (Forms 1040X) for the years 1996 and 1998 constituted conduct both reckless and grossly incompetent within the meaning of §10.52(b) of Treasury Circular 230. I believe that Judge Moran's decision with respect to the conduct underlying these two charges is supported by the obviously frivolous nature of the argument. It is obvious that this argument would have the effect of largely gutting the individual income tax, or at least its

application to United States persons with respect to income sources within the United States. That alone would give even a layman pause, let alone an experienced tax practitioner. The fact that every Federal court that had considered the argument found it to be without merit, and that more than one court had characterized the argument as groundless, should have, and I believe did, provide Respondent with adequate notice that the argument was frivolous.

Respondent has argued that since the Internal Revenue Service itself did not publish guidance indicating that the §861 "source" of income argument until it published Notice 2001-40 in 2001 that the law was unsettled until that guidance appeared. Respondent's argument is without merit. The longstanding legislative history of the sourcing rules as well as the various cases alluded to above provided Respondent with ample notice of the frivolous nature of his argument and of the Internal Revenue Service's position on the issue.

The fact that the Internal Revenue Service has not published public guidance on any issue does not demonstrate the Service's acceptance of a position, nor does it indicate that the law on the issue is unsettled. As a general rule, when the Service publishes interpretive public guidance on an issue, it normally does so "retroactively," reflecting the fact that the law which the guidance interprets (a statutory enactment by the Congress or interpretative decisions by Federal Courts, for example) existed prior to the publication of the published guidance. In those instances where the guidance reflects either a change in the law (because of the enactment of new legislation) or an adverse change in prior published favorable guidance of the Internal Revenue Service that provided taxpayers with a basis for reliance, the Internal Revenue Service typically exercises the authority granted it by §7805(b) of the Internal Revenue Code of 1986 and gives that new published guidance prospective only application. When published guidance is intended to have prospective only application, the Service notes that fact in the guidance itself.

This rule accommodates the fact that the Internal Revenue Service and the IRS Chief Counsel are responsible for administering complex laws applying to literally hundreds of millions of taxpayers, yet are provided limited resources with which to address a myriad of technical issues. These resource constraints mean that at any given time, the Internal Revenue Service has literally hundreds of issues it hopes to address through published guidance. Because of its singular importance to the uniform administration of our tax laws, in allocating scarce technical resources, the Internal Revenue Service and the IRS Office of Chief Counsel accord published guidance priority over other forms of guidance, such as internal guidance to Internal Revenue Service personnel and guidance provided to individual taxpayers through private letter rulings. However, the Internal Revenue Service and the IRS Office of Chief Counsel recognize that private letter rulings (on which particular taxpayers requesting the rulings but not the general public may rely) also serve an important function in our tax system, particularly in areas where public guidance providing the general public with a basis for reliance is lacking. In most areas, by paying a "user's fee," taxpayers may generally request a private letter ruling on issues where they feel they need a basis for reliance in entering into transactions or before taking positions on their returns.

In the absence of published guidance applicable to the public as a whole or a private letter ruling issued to the taxpayer, taxpayer and practitioners cannot assume that the tax results anticipated from a transaction will follow or that the position he is considering taking on a return will be accepted. It is here where the advice provided by tax practitioners is critical to the proper functioning of our tax system. This is because the fact that the Internal Revenue Service has not yet issued guidance on an issue provides taxpayers or practitioners with neither any basis for "reliance" nor an indication that existing law on the issue is unsettled.

Over the years, the Internal Revenue Service has generally limited its published guidance to issues it considers be non-frivolous and of wide importance under our tax laws. In part, this decision reflects the resource considerations described above. In part, it reflects concerns similar to those expressed by Judge Vasquez in Williams v. Commissioner, supra. When the Internal Revenue Service has issued public guidance on matters it considers frivolous, it normally indicates in the guidance that it considers the issue to be frivolous and settled under existing law and that taxpayers risk exposure to civil and criminal tax penalties if they assert the position. The Internal Revenue Service did so with respect to the §861 "source of income" argument in both Notice 2001-40, 2001-1 C.B. 1355, and more recently in Rev. Rul. 2004-30, 2004-12 I.R.B. 622 (March 22, 2004).

It is worth noting that when Respondent prepared the Amended U.S. Individual Income Tax Returns (Forms 1040X) for Taxpayer T's 1996 and 1998 tax years, he did not in any way reference the adverse case precedents discussed above that clearly disclosed the frivolous nature of Respondent's argument. Given Respondent's education, training and experience, it taxes credulity to either assume or believe that these omissions were innocent in nature. Complainant did not charge that Respondent's failures to include a reference to and a discussion of these adverse precedents in Taxpayer T's amended returns called into question the adequacy of the disclosures prepared by Respondent for Taxpayer T, though I think he would have been justified had he done so. However, that issue is not before me and I see no need to remand this matter to Judge Moran to permit him to determine whether to allow Complainant to further amend his Initial Complaint given my agreement with Judge Moran that the position in question was frivolous and had no realistic possibility of success on the merits. However, as I will note below, I do find these omissions relevant to the question of whether Respondent was acting in good faith, not only in preparing the amended returns in question but in his overall

conduct, at least as it relates to Respondent's §861 "source of income" argument.

The next question is whether Respondent's violations as set forth in the Initial Complaint were "willful" within the meaning of §10.52(a) of Treasury Circular 230. As noted above, Treasury Circular 230 itself does not define the term "willful." Absent such a regulatory definition, it is appropriate to ascribe a meaning to the term that comports with that given the term in the case law interpreting the criminal provisions of the Internal Revenue Code of 1986, which in some respects punish like conduct. See, e.g., §§ 7201-7207 of the Internal Revenue Code of 1986, as amended and in effect during the years in issue. Likewise, in those instances where it is relevant to determine whether Respondent acted "knowingly" in violating the provisions of Treasury Circular 230 set forth in the Initial Complaint, I also find these precedents instructive.

The leading United States Supreme Court decisions defining "willful" conduct within the meaning of §§7201-7207 of the Internal Revenue Code of 1986 are United States v. Pomponio, 429 U.S. 10 (1976), and United States v. Bishop, 412 U.S. 346 (1973). In United States v. Pomponio, supra, the respondents were charged with willfully filing false tax returns in violation of §7206(1) of the Internal Revenue Code of 1954, as amended and in effect during the years in issue (a predecessor provision identical in all respects to §7206(1) of the Internal Revenue Code of 1986, as amended and in effect during the years here in issue). At issue were jury instructions issued by the District Court judge that the Court of Appeals found erroneous because the Court of Appeals believed that "the statute at hand requires a finding of a bad purpose or evil motive." United States v. Pomponio, 528 F.2d 247, 249 (4th Cir. 1975). The Fourth Circuit's opinion was based on its reading of United States v. Bishop, supra. Finding that reading of Bishop incorrect, the Supreme Court reversed and remanded, stating:

"[T]he jury was instructed that 'good motive alone is never a defense where the act done or omitted is a crime,' and that consequently motive was irrelevant except as it bore on intent. The Court of Appeals held this final instruction improper because 'the statute at hand requires a finding of a bad purpose or evil motive.' 528 F.2d at 249. In so holding, the Court of Appeals incorrectly assumed that the reference to an 'evil motive' in *United States v. Bishop, supra,* and prior cases meant something more than the specific intent to violate the law described in the judge's instruction."

"In *Bishop,* we held that the term 'willfully' has the same meaning in the misdemeanor and felony sections of the Internal Revenue Code, and that it requires more than a showing of careless disregard of the truth. We did not, however, hold that the term requires proof of any motive other than an intentional violation of a known legal duty. We explained the meaning of willfulness in §7206 and related statutes:

> **"The Court, in fact, has recognized that the word 'willfully' in these statutes generally connotes a voluntary, intentional violation of a known legal duty. It has formulated the requirement of willfulness as 'bad faith or evil intent,' *[United States v.] Murdock,* 290 U.S. [389,] 398, or 'evil motive and want of justification in view of all the financial circumstances of the taxpayer,' *Spies [v. United States],* 317 U.S. [492,] 498, or knowledge that the taxpayer 'should have reported more income than he did.' *Sansone [v. United States],* 380 U.S. [343,] 353. See *James v. United States,* 366 U.S. 213, 221 (1961); *McCarthy v. United States,* 394 U.S. 459, 471 (1969).' 412 U.S., at 360.**

"Our references to other formulations of the standard did not modify the standard set forth in the first sentence of the

quoted paragraph. On the contrary, as the other Courts of Appeals that have considered the question have recognized, willfulness in this context simply means a voluntary, intentional violation of a known legal duty. *United States v. Pohlman,* 522 F.2d 974, 977 (CA8 1975) (en banc), cert. denied, 423 U.S. 1049 (1976); *United States v. McCorkle,* 511 F.2d 482, 484-485 (CA7) (en banc), cert. denied, 423 U.S. 826 (1975); *United States v. Greenlee,* 517 F.2d 899, 904 (CA3), cert. denied, 423 U.S. 985 (1975); *United States v. Hawk,* 497 F.2d 365, 366-369 (CA9), cert. denied, 419 U.S. 838 (1974). The trial judge in the instant case adequately instructed the jury on willfulness. An additional instruction on good faith was unnecessary."

429 U.S. at 11-13.

Respondent has argued that the United States Supreme Court's decision in Cheek v. United States, 498 U.S. 192 (1991), supports his contention that he lacked "willfulness" in asserting the §861 "source of income" argument. Respondent also argues that Judge Moran's decision to decide the liability issues in these proceedings through Motion for Summary Judgment rather than a full evidentiary hearing on the liability issues, precluded Judge Moran from considering the evidence necessary to permit him to make a determination as to "willfulness" given the Supreme Court's holding and discussion in Cheek.

Cheek was an airline pilot charged with attempting to evade income taxes in violation of §7203 of the Internal Revenue Code of 1954, as amended and in effect during the years there in issue (a provision identical to §7203 of the Internal Revenue Code of 1986, as amended and in effect during the years here in issue). Cheek had been convicted by a jury that acted pursuant to jury instructions issued by a United States District Court judge, acting as the trial judge. That conviction had been affirmed by the United States Court of Appeals for the Seventh Circuit.

The issue considered by the United States Supreme Court, which proved the basis for the Supreme Court's decision vacating Cheek's conviction and remanding the case for further consideration by the Seventh Circuit, was the propriety of the jury instructions issued by the trial judge. Cheek had filed tax returns for all taxable years to and including 1979. During 1980, Cheek filed a Form W-4 with his employer increasing his claimed withholding allowances to 60. Cheek asserted that he did so, and that he failed to file tax returns for several subsequent years because he believed he owed no tax. Cheek asserted two bases for his belief – that the Sixteenth Amendment to the United States Constitution had not been duly ratified and that wages were not income subject to tax (the latter being a matter of statutory interpretation).

While both arguments were rejected, Cheek argued that he had not "willfully" violated the law because his beliefs were honestly held and entitled to be so treated even if not objectively reasonable. The trial judge initially issued one jury instruction during the first day of the jury deliberations, which the United States Supreme Court did not find objectionable. That instruction provided:

> **"[A] person's opinion that the tax laws violate his constitutional rights does not constitute a good faith misunderstanding of the law. Furthermore, a person's disagreement with the government's tax collection systems and policies does not constitute a good faith misunderstanding of the law."**

At the end of the first day's deliberations, the jury indicated that it still had not reached agreement.

When the jury commenced its second day of deliberations, the trial judge issued a second jury instruction. That instruction, which was the subject of the United States Supreme Court's criticism, provided:

> ""[A]n honest but unreasonable belief is not a defense and does not negate willfulness."

After receiving that instruction, the previously deadlocked jury convicted Cheek on all counts.

In his decision for the Court, Justice White noted that "[t]he general rule that ignorance of the law or a mistake of law is no defense to criminal prosecution is deeply rooted in the American legal system." Id. at 199. "Based on the notion that the law is definite and knowable, the common law presumed that every person knew the law." Id. Citing Bishop v. United States, supra, and Pomponio v. United States, supra, Justice White indicated that:

> "Taken together, *Bishop* and *Pomponio* establish that the standard for the statutory willfulness requirement is the 'voluntary, intentional violation of a known legal duty." Cheek v. United States, supra, at 201.

Justice White went on to note that:

> "Willfulness, as construed by our prior decisions in criminal tax cases, requires the Government to prove that the law imposed a duty on the defendant, that the defendant knew of this duty, and that he voluntarily and intentionally violated that duty." Id.

With regard to the second of the three required proofs (knowledge), Justice White noted that, with respect to knowledge of matters of statutory construction under the tax laws, when Congress imposed a "willfulness" standard it intended to depart from the common law rule presuming knowledge of the law (a rule of presumed general intent) to a rule requiring proof by the Government of knowledge of the law on the part of the defendant (a rule requiring the Government to prove a specific subjective intent). Cheek v. United States, supra, at 200-201. Justice White went on to note that:

"[C]arrying this burden requires negating a defendant's claim of ignorance of the law or a claim that because of a misunderstanding of the law, he had a good faith belief that he was not violating any of the provisions of the tax laws. This is so because one cannot be aware that the law imposes a duty upon him and yet be ignorant of it, misunderstand the law, or believe that the duty does not exist." Id. at 202.

Justice White then indicated that this same modification of the common law conclusive presumption of knowledge did not extend to issues involving the constitutionality of the tax laws, where the common law rule of conclusive presumption of knowledge continued to apply. Justice White explained the Court's reasons for not extending the specific intent standard to constitutional questions as follows:

"Such a submission is unsound, not because Cheek's constitutional arguments are not objectively sound or frivolous, which they surely are, but because the *Murdock-Pomponio* line of cases does not support such a position. Those cases construed the willfulness requirement in the criminal provisions of the Internal Revenue Code to require proof of knowledge of the law. This was because in 'our complex tax system, uncertainty often arises even among taxpayers who earnestly wish to follow the law,' and '[i]t is not the purpose of the law to penalize frank difference of opinion or innocent errors made despite the exercise of reasonable care.'" Id. at 204-205 (citing United States v. Bishop, supra, at 360-361 as quoting Spies v. United States, 317 U.S. 492, 496 (1943)).

With respect to issues involving matters of statutory construction under the Internal Revenue Code, Justice White next discussed the specific question posed for the Supreme Court's consideration: What factors should be considered in determining the defendant's knowledge, and specifically, should

such determinations be limited only to issues where a purported good faith belief was predicated on an objectively reasonable, as opposed to unreasonable or frivolous, argument? Justice White acknowledged that both of Cheek's asserted arguments were not objectively reasonable and were frivolous. Id. at 205. In construing the statutory "willfulness" requirement in the context of a criminal tax prosecution that raised Sixth Amendment considerations (". . . this Court, where possible, interprets congressional enactments so as to avoid raising serious constitutional questions . . ." – Id. at 203), and in light of more generalized concerns about preserving for the factfinder (in Cheek, the jury) the role of considering what factors should and should not be considered in determining whether the defendant had an honest but mistaken belief that wages were not income ("{k]nowledge and belief are characteristically questions for the factfinder, in this case the jury . . ." – Id.), Justice White indicated that:

> **"Characterizing a particular belief as not objectively reasonable transforms the inquiry into a legal one and would prevent the jury from considering it. It would of course be proper to exclude evidence having no relevance or probative value with respect to willfulness; but it is not contrary to common sense, let alone impossible, for a defendant to be ignorant of his duty based on an irrational belief that he has no duty, and forbidding the jury to consider evidence that might negate willfulness would raise a serious question under the Sixth Amendment's jury trial provision." Id. at 203.**

On this basis, the Court vacated the judgment of the Court of Appeals and remanded the case for further proceedings consistent with its opinion. In so doing, however, the Supreme Court was careful to note:

> **"Of course, the more unreasonable the asserted beliefs or misunderstandings are, the more likely the jury will consider them to be nothing more than simple**

disagreement with known legal duties imposed by the tax laws and will find that the Government has carried its burden of proving knowledge." Id. at 203-204.

Accordingly, while the Court found that the question of whether a belief was objectively reasonable was inappropriately inserted in the process to preclude consideration of the matter by the factfinder, Cheek does not stand for the proposition that the objective reasonableness of an argument is irrelevant to the determination of whether a good faith belief exists that the argument is proper. To the contrary, the Court's opinion makes it clear that objective reasonableness may be a highly reliable indicator of whether an asserted belief is subjectively made in good faith.

Upon remand, the Seventh Circuit reiterated the same point, stating:

> **"Tax evaders that persist in their frivolous beliefs (such as that wages are not income or that Federal Reserve Notes do not constitute cash or income) should not be encouraged by the [Supreme] Court's decision in *Cheek* or our decision today. While a defendant is now permitted to argue that his failure to file income tax returns and to pay income taxes was the result of his incredible misunderstanding of the tax law's applicability, the government remains free to present evidence demonstrating that he knew what the law required but simply chose to disregard those duties. . . . And, as the [Supreme] Court noted, 'the more unreasonable the asserted beliefs or misunderstandings, the more likely the jury will consider them to be nothing more than a simple disagreement with known legal duties imposed by the tax laws and will find that the Government has carried its burden of proving knowledge."**

United States v. Cheek, 931 F.2d 1206, 1208-1209 (7th Cir. 1991).

The United States Court of Appeals for the Tenth Circuit had its own way of characterizing the tasks left for the trial judge and the jury as factfinder after Cheek when the asserted argument is not objectively reasonable. In United States v. Willie, 941 F.2d 1384, 1392 (10th Cir. 1991), the Tenth Circuit stated:

> **"Thus, his belief must be descriptive – he must believe that the law *does not* apply to him. A normative belief that the law *should not* apply to him leaves Willie fully aware of his legal obligations and simply amounts to a disagreement with his known legal duty and a 'studied conclusion . . . that [the law is] invalid and unenforceable." (Citing the Supreme Court's decision in Cheek v. United States, supra, at 205-206).**
>
> **"It is apparent that it is a delicate balance to differentiate between a belief that the law *should* be different and a belief that the law *is* different. The difficulty of discerning the often subtle distinctions is magnified by the fact that much of the same evidence can be used to prove both types of belief and because the word 'belief' itself is used loosely in describing both sides of the dichotomy. As a result, the precise purpose for which the evidence is offered becomes crucial to the trial court's determination of admissibility, particularly in cases of this nature where the careless admission of evidence supporting both relevant and irrelevant types of belief could easily obfuscate the relevant issue and tempt the jury to speculate that the mere existence of documentary support for the defendant's position negates his independent knowledge that he has a legal duty. . . . The defendant must, therefore, persuasively show the trial judge that the evidence is being offered for a permissible purpose by making a proffer of great specificity regarding the type of belief he seeks to prove." United States v. Willie, supra, at 1392-1393.**

These considerations become even more complex where the fervent nature of the taxpayer's belief in what *should be*

colors the taxpayer's perception of what *is* and causes him to turn a blind eye to what plainly can be seen. Taxpayers (and practitioners) can be "blind" to questions of both fact and law. Courts have found that defendants cannot deny a finding that they acted with requisite knowledge through "willful blindness" (an unwillingness to examine and consider what is there to be seen). See, e.g., United States v. Jewell, 532 F.2d 697 (9th Cir. 1976), where (in a case involving the possession of controlled substances) the Ninth Circuit considered the following jury instruction:

> **"The Government can complete their burden of proof by proving, beyond a reasonable doubt, that if the defendant was not actually aware that there was marijuana in the vehicle he was driving when he entered the United States his ignorance in that regard was solely and entirely a result of his having made a conscious purpose to disregard the nature of that which was in the vehicle, with a conscious purpose to avoid learning the truth."**

Id. at 700. The Ninth Circuit went on to note:

> **"The substantive justification for the rule is that deliberate ignorance and positive knowledge are equally culpable. The textual justification is that in common understanding one 'knows' facts of which he is less than absolutely certain. To act 'knowingly,' therefore, is not to act only with positive knowledge, but also to act with an awareness of the high probability of the existence of the fact in question. When such awareness is present, positive knowledge is not required."**

Id. The "willful blindness" doctrine has also been applied in criminal tax prosecutions. See, e.g., United States v. Willis, 277 F.2d 1026, 1031-1032 (8th Cir. 2002).

Applying these precedents regarding "willfulness" and "knowledge" to these proceedings, It is appropriate to note at

the outset some significant differences between these proceedings and the proceedings in Cheek.

First, Cheek involved a criminal proceeding and this case does not. This becomes an important distinction both because these proceedings do not raise questions of rights secured by the Sixth Amendment and for the broader reason that the division of functions between the trial judge and the jury in Cheek do not exist here. In disciplinary proceedings under Treasury Circular 230, all such functions are performed by the Administrative Law Judge. See §10.70(b) of Treasury Circular 230. For this reason, these proceedings do not raise the issue of whether Respondent's belief is objectively reasonable in a manner that prevents the issue from being considered by the factfinder. Here, the determination of the objective reasonableness of Respondent's beliefs is only considered as the Supreme Court indicated in Cheek it should be considered – as relevant and probative evidence indicating whether Respondent is credible in asserting his subjective good faith but mistaken belief, and in assessing the nature of that belief.

Second, the Supreme Court's decision in Cheek v. United States, supra, involved an ordinary taxpayer, not an experienced tax professional. This factual distinction may be relevant for four reasons.

Ordinary Taxpayers v. Tax Practitioners. **in light of the distinctions made in United States v. Boyle, supra, between the nature of responsibilities assumed in our tax system by ordinary taxpayers, on the one hand, and experienced tax practitioners, on the other, it is unclear whether the rationale underlying the Supreme Court's decision would apply at all to an experienced tax practitioner, even in a criminal tax prosecution. At the very least, the rationale would appear not to apply with equal force in the case of an experienced tax practitioner.**

This distinction was suggested in the Sixth Circuit's decision in United States v. Alt, 996 F.2d 827 (6th Cir. 1993).

There, the issue under consideration was whether a jury instruction similar to the one in Cheek should be cause to overturn the conviction of a married couple. One of the issues before the Sixth Circuit was the determination of whether the error in giving the instruction constituted harmless error. In determining whether the error was harmless, the court examined the background and experience of each of the taxpayers.

In the case of the husband, there was no direct evidence in the record of his knowledge of Federal taxation. The court refused to infer that knowledge, and on that basis found that giving of the instruction was not harmless error as to the husband.

The court found that the question of whether the instruction was harmless error was as to the wife was a closer question. The Government had introduced evidence that the wife took financial management and federal income tax courses and operated a financial management business, which the court described as direct evidence of her knowledge of the tax laws. The evidence also showed that she managed all of her husband's financial affairs and prepared the returns that were the subject of the prosecution. But the defense offered what the court characterized as a "substantial amount" of evidence indicating that the wife was less than proficient in financial matters, especially matters dealing with taxation. The Sixth Circuit found that, in light of the conflicting evidence in the record as to the wife, the jury's presumption that she knew her legal duty may well have been critical to the jury's decision as to the wife. As a consequence, the Sixth Circuit found that it could not safely conclude that the jury instruction was harmless error as to the wife either.

Two aspects of the Sixth's Circuit's decision in Alt are noteworthy. The Sixth Circuit did not reflexively assume that Cheek compelled reversal of the convictions with respect to the husband and the wife. Rather, the court examined the education, background and work experience of each defendant to determine

the nature and extent of their familiarity with the tax laws. Moreover, neither the husband nor the wife in Alt had a familiarity with the tax laws that remotely approached that which Respondent possessed on the dates of his questioned conduct.

No Denial of Consideration by the Factfinder. **Even if a court were to determine that Cheek's underlying rationale applied, albeit in modified form, in the case of a criminal tax proceeding against an experienced tax practitioner, it would appear clear from Cheek that a factfinder could consider both the absence of objective reasonableness of the argument advanced by the practitioner and the nature and extent of his familiarity with federal tax matters in assessing the practitioner's credibility in asserting a good faith mistake defense.**

Purpose of the Proceeding. **Unlike criminal tax prosecutions such as the one in Cheek, these proceedings have as their purpose determining Respondent's fitness to practice before the Internal Revenue Service. Even if one were to conclude that an objective reasonableness limitation placed on the scope of a factfinder's factual inquiry in a criminal tax prosecution was an unwarranted limitation on the factfinder, it would not necessarily follow that the same would or should be true in a disciplinary proceeding under Treasury Circular 230. Given the duties and responsibilities respectively assigned to taxpayers and tax practitioner in our tax system (see discussion of United States v. Boyle, supra), it is appropriate that the higher standards of competence required of experienced tax practitioners at the least be accompanied by a correspondingly greater skepticism in disciplinary proceedings under Treasury Circular 230 when such practitioners seek to establish good faith mistake defenses with respect to positions that are not objectively reasonable.**

Inapplicability to Respondent's Sixteenth Amendment Argument. **Under Cheek, the "honest mistake" defense, whether based on an objectively honest belief or not, is not available with**

respect to mistakes involving the constitutionality of the income tax. Taxpayers and practitioners alike are conclusively presumed to have knowledge of the constitutional law. As a consequence, Cheek offers Respondent no comfort whatsoever with respect to his statements to Taxpayer C in the course of his representational activities that the Sixteenth Amendment had not been properly ratified.

Turning to the Decision of the Administrative Law Judge (including the Orders of the Administrative Law Judge incorporated by reference) and to the administrative record, I find that Judge Moran had ample reason for finding that Respondent's conduct was willful and knowing under the standards discussed above and that his conduct, as alleged in the Initial Complaint, had been proven by clear and convincing evidence and justified disbarment from practice before the Internal Revenue Service.

At page 2 of the Decision of the Administrative Law Judge in these proceedings, Judge Moran made the following statement with respect to the charges contained in the Initial Complaint:

> **"A fundamental purpose of a hearing or trial is to determine whether the allegations of fact, as set forth in the Complaint, occurred. But where there is no dispute as to the underlying facts, obviously there is no need for a court to resolve whether one party's version of the facts is more believable than the other side's version. That is what happened in this case. In fact, in Mr. Banister's answer to the original Complaint he *admitted* that the facts alleged in the Complaint occurred. Thus, Mr. Banister *admitted* that he so advised his client "C" that the Sixteenth Amendment to the United States Constitution was not ratified and he *admitted* that he advised client "C" that Internal Revenue Code sections 861 through 865 defined "source of income" so as to exclude C's earnings. Similarly, Banister *admitted* that he also advised client "T" that Internal Revenue Code sections 861 through 865 defined "source of income" so as**