

Summary: *The Constitution originally forbade direct, invasive taxes. The Sixteenth Amendment removed this protection and gave birth to the modern income tax, sacrificing our individual liberties, our legal principles and protections to government's insatiable desire for revenue. A primary criterion for tax reform should be the restoration of the individual liberties intended by the Founders.*



THE ROAD MAP TO TAX REFORM™

A MONUMENT OF DEFICIENT WISDOM: *The Constitutional Conflict in Federal Income Tax Law Enforcement*

By Daniel J. Pilla

It's been said that the genius of our nation's Founders was their capacity to understand human nature and the nature of government in general, and then strike a delicate balance between the liberties on one hand and the need for social order on the other. As a result, they developed a government that was afforded only those powers necessary to protect the life, liberty, and property of the citizens. Otherwise there were powers and rights not transferred from the citizenry to the government.

Yet throughout our history there has been a well-documented and undeniable friction between the cause of liberty and the growth of government, and nowhere has this friction been more apparent—and more detrimental to the interests of liberty—than in the area of taxation. The unchecked power to tax and enforce the collection of taxes dispossesses citizens of their inalienable rights.

The challenge today is to erect a taxation that allows government to raise needed revenue for legitimate purposes but to do so in a manner that is not invasive to the people.

To achieve such a system, we must first understand the workings of the current scheme and then make a conscious decision as a society that it is necessary and desirable to limit the reach of government's taxing power to the fullest extent possible.

THE GROWTH OF THE INCOME TAX CODE

The income tax as we know it began in 1913 and today's code numbers 18,000 pages of laws and regulations. There are also tens of thousands of pages of Revenue Rulings and Procedures issued by the IRS, voluminous guidance papers issued by the Office of Chief Counsel, and hundreds of thousands of court decisions (annually) from the nation's judiciary.

Just in the 1980s, the code was changed more than 100 times, including the massive Tax Reform Act of 1986. Between 1996 and 1998 there were six major tax reform laws that affected in excess of 3,000 code sections and subsections, and the entire code has been amended 78 times. And just in terms of complexity, the effects of these repeated and sweeping tax law changes are staggering for both taxpayers and preparers.

Reasonable people ask, “Why can’t the tax laws be simpler?” They can be, but Congress uses the tax laws for reasons other than those for which they were intended. Our Founders imparted taxing authority to the federal government for the sole purpose of funding legitimate, clearly defined constitutional functions: pay the debts of the nation, provide for national defense, and ensure the general welfare of the country. Yet for more than 50 years, Congress has used the graduated income tax system as a means of enforcing the now transient notion of “social justice.” Rather than simply raising revenue, tax laws are used to modify behavior by rewarding certain conduct perceived by current policymakers as desirable and penalizing other conduct perceived as undesirable.

The Founders never intended such a power to exist for one simple, logical reason. The social agenda of a nation is subject to change with each change of power in the capital. If each faction is allowed to use the public’s standard of living as the means of affecting its peculiar social agenda, then citizens are deprived of their most basic constitutional rights—property and the pursuit of happiness. Moreover, taxation to accomplish social change has already been tried—by Karl Marx.

Some argue that the constitutional term “general welfare” covers a lot of ground and, therefore, taxation is appropriate. Unfortunately, this clause is the source of great misunderstanding. By canvassing the broad political spectrum of the Founders, one finds that both conservatives (Madison) and liberals (Hamilton) wanted the powers imparted to the new government limited, even though they differed on how proactive that government should be. Their belief was that taxation and government spending were intended for the country as a whole, not for particular inhabitants or locales and certainly not for individual classes of society or industry. In wanting to establish the greatest amount of individual liberty possible, the Founders recognized that unlimited taxing power was a direct threat to those liberties.

ARE ALL MEN CREATED EQUAL?

From Locke to Lincoln the so-called “equal protection” clause of the Constitution has been a cornerstone of liberty. The purpose of the clause is to guarantee that no special favor or privilege is extended to anyone at the expense of another by mere virtue of their social or economic standing. However, the current tax code is replete with examples of unfair and unequal treatment among taxpayers. For instance:

- *The graduated income tax rate.* Our current system sports six different tax rates from 10 to 38.6%

based on nothing more than the social proposition that those who earn more should pay more. The chief problem with the rate is that they are arbitrary. They are not based on any sound legal or economic principle. It is functionally impossible to define how it is “fair” for one person to pay at a 27% rate and another at a 38.6% level. Would 50% be even “more fair?” Because these questions have no answers, the notion of a graduated income tax is fundamentally *unfair*.

- *Tax return filing status.* The current code provides five filing classifications (single, married filing jointly, married filing separately, head of household, and surviving spouse). Each classification ensures preferential treatment to each class based solely on social standing. For instance, based on these five categories and the so-called marriage penalty, there are 59 provisions in the tax code where tax liability depends, in whole or in part, on whether a person is married or single. This disparate treatment only polarizes citizens within their various social groups.
- *The alternative minimum tax (AMT).* In essence, this is a flat tax that operates alongside the graduated tax system and is designed to make sure everybody pays some tax even if they are entitled to legal deductions, credits, and exemptions.
- *Defining a child.* There are six definitions of a child and a combination of up to five different fact tests that must be met in order to comply with the code.
- *Deduction and exemption phase-outs.* All the phase-outs, exclusions, and disparate tax treatments within the code are too numerous to itemize, but one of the most common affects a married couple filing jointly. When their income exceeds \$100,000, those citizens lose the benefit of legal deductions that other taxpayers are entitled to claim.

Ex Post Facto Laws

The first object of government is to protect the life, liberty, and property of its citizens. The Founders knew that in order to preserve liberty, the broad powers of the legislature would have to be restrained and an independent judiciary would have to be established to ensure that Congress could not overstep its bounds. As a result, several lawmaking powers were denied outright, including the ability to pass *ex post facto* legislation. An *ex post facto* law applies retroactively from the date of its enactment. The Founders were so concerned with this scenario that they precluded both the federal and the state governments from enacting such legislation.

Tax laws are particularly offensive when they are retroactive. Citizens are denied their rights to plan personal and business affairs in order to pay taxes and they are denied the right to

rearrange their affairs in order to minimize their tax burdens. Moreover, retroactive tax laws unreasonably deny a person the full use and enjoyment of property.

But despite the pernicious nature of these laws and the plain language of the Constitution, retroactive tax laws have been authorized for a number of years. The Supreme Court has ruled that *ex post facto* legislation may be permitted when the retroactive periods are “modest and not excessive.” As a result of such decisions, citizens are afforded little protection from such legislative intrusions.

REVERSING THE FOUNDATION OF AMERICAN JURISPRUDENCE

“Innocent until proven guilty” is a cornerstone of law. Citizens are not to be considered guilty at any level in the judicial process until after a trial. The accuser, whether in a criminal or civil context, is solely responsible to prove the verity of his claims against the accused before any punishment can be applied.

However, income tax laws and regulations transfer to the shoulders of citizens innumerable requirements to carry out affirmative duties under the pain of imprisonment, civil penalties, and additional tax and interest assessments. In all but a few exceptions, the IRS never has to prove that its actions or determinations are correct. The citizen has the task of proving that such actions are wrong. This shift in the burden of proof does not apply to the criminal provisions of the tax code. But because the vast majority of the penalty provisions are civil in nature, the overwhelming number of penalty assessments is likewise civil. As a result, the courts are content to dissolve the historic protection in most civil cases.

What’s at risk is not so much loss of liberty but loss of property. For more than six decades the prevailing idea has been that taxes are “the lifeblood of government” and collecting them is “an imperious need.” In other words, government’s need for money is sufficient to override constitutional protections.

Take, for instance, a computer notice issued by the IRS that alleges an error in a taxpayer’s return. While the law provides a means for the citizen to challenge the notice, the burden is on the taxpayer to respond to the notice in a timely fashion, craft a response to apprise the IRS of the objection, and then prosecute the objection through the system—all the while carrying the burden of not only proving the IRS determination is wrong but also what the correct determination should be.

Recognizing that taxpayers are usually not prosecutors, Congress enacted tax reform in 1998 to shift the burden of proof to the IRS—if the citizen “first” introduces credible evidence concerning the issue. So the citizen bears the burden of proof necessary to shift the burden of proof.

WHAT’S LEFT OF THE RIGHT TO TRIAL BY JURY

The Seventh Amendment fashioned a protection that guaranteed all citizens the right to have the facts of a civil case heard and determined by an impartial jury. While this right is considered to be an indispensable element of personal liberty, it has been effectively eliminated in most tax disputes because of the system Congress established for remedying tax disputes. Basically there are two options, each fraught with dangers. One is pre-payment where there is a review before paying the tax. The second is post-payment in which the citizen first pays the tax and then obtains review.

- *Pre-payment.* The natural constitutional order suggests that a person who legitimately disputes an IRS claim should have the matter heard and resolved prior to being required to pay the tax. This is the essence of due process. Yet the government’s compelling need to collect revenue has allowed the courts and Congress to substantially alter this basic and fundamental protection. For example, The U.S. Tax Court was created to hear disputes between the IRS and citizens. But because this is not a “court” as outlined in Article III of the Constitution, litigants before the Tax Court are not entitled to constitutional protections—such as trial by jury—that otherwise exist. The consensus is that it may look like a court, talk like a court, and act like a court, but it is not a court. In the meantime, citizens are effectively dispossessed of their otherwise inalienable rights.
- *Post-payment.* If a taxpayer wants to avail himself of constitutional rights in connection with a tax dispute, he must lodge his case in the U.S. District Court, not the Tax Court. District Courts are courts and, as such, retain full Seventh Amendment rights. However, there is often one insurmountable problem. In order to gain access to the District Court, the tax must first be paid in full—including interest and penalties! During the time-consuming process the citizen is deprived of the use and enjoyment of property.

Basically taxpayers must choose between the right to trial by jury and the right to the peaceful use and enjoyment of property.

ERODING THE RIGHT TO DUE PROCESS OF LAW

Due process is a necessary ingredient in the recipe for liberty. It holds government enforcement action at bay until after a citizen is adjudged liable at law or guilty of a crime. Unfortunately, the courts have arrived at the conclusion that property rights are not on the same level as other rights. That distinction is based on governmental need.

In keeping with that philosophy, Congress has erected substantial barriers to traditional due process that apply only in tax cases. Both the Anti-Injunction Act and the Anti-Declaratory Judgment Act effectively deprive federal courts of general jurisdiction to enjoin or restrain the assessment or collection of taxes. In other words, the courts cannot stop IRS enforcement action outside the narrow scope of available statutory remedies.

Lack of due process was one of the major complaints against the IRS heard by Congress in the 1997 abuse hearings. As a result, Congress enacted the "collection due process" protections where citizens invoke rights prior to IRS collection. Unfortunately, the onus is still on the citizen at every level of the process to invoke the protections. Moreover, hearings are still held before the IRS, not an independent judiciary.

THE ELECTRONIC VERSION OF UNREASONABLE SEARCHES

The bitter experiences the colonists had with the King's general warrants and arbitrary property seizures were directly responsible for the Fourth Amendment and the right against unreasonable searches. The Amendment was more than just protecting personal property. It also extended to the reasonable expectation of privacy in conducting one's affairs—a zone of privacy.

But where the IRS is concerned, there is no zone of privacy. The IRS is free to summons any person and all records to aid any investigation or examination, including records from one's accountant and attorney. In short, if there is a transaction in the life of a taxpayer, the IRS can gain access to that information. That's because the Fourth Amendment's usually stringent probable cause requirements do not apply to the IRS, according to the Supreme Court. Even more ominous is the Court's declaration that the IRS has "a power of inquisition" not derived from judicial function.

This lust for information is called an "information reporting safety net." The theory is that the more the IRS knows, the less likely an individual will cheat. Since the 1986 Tax Reform Act, there has been an explosion in the requirements for submitting information returns. At last count more than 1.3 billion information returns are filed annually with the IRS.

PLEADING THE FIFTH

While the right against self-incrimination is sound and necessary in a free society, such protections are not upheld in matters of tax. For instance, the individual tax return must be signed under penalty of perjury. By signing, a taxpayer may incriminate himself. By not signing, he faces criminal prosecution. Put another way, asserting Fifth Amendment rights by not signing opens one up to prosecution. On the other hand, signing the return waives Fifth Amendment rights!

CONCLUSION

There is no longer any semblance of either order or stability to our tax system. In the interest of collecting revenue, the Supreme Court has allowed Congress to encroach and vitiate individual rights. The income tax is a frontal assault on our constitutional liberties, and the enforcement of the system erodes the restrictions on the power of government. Liberty and an income tax cannot coexist. Which is the American people more willing to live without?

This study is a summary of IPI Policy Report # 165, *A Monument of Deficient Wisdom: The Constitutional Conflict in Federal Income Tax Law Enforcement*, by Daniel J. Pilla, Executive Director, Tax Freedom Institute, Inc.

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