

The Infernal Revenue Service

CHAPTER 1

The internal Revenue Service

We of modern day America have many unique problems and situations that we have to deal with. These problems may not be unique to us in the world, but they contradict the true meaning of what our great country stands for. One of the problems, if not the most unique, concerns the “volunteering” of an average of 35 % of our yearly incomes to the federal government in the form of an income tax. In addition to this, we have sales and other miscellaneous taxes which we have to pay on a daily basis. After one finishes cringing at the sheer mention of the dread income tax, the question may arise: Why is it unique? Well, that explanation will come as you read on.

The average citizen knows very little of the income tax, and much less about its mentor, the Internal Revenue Service (IRS). There is a curious note here, one of human behavior. Nowadays, it is commonly known that “nobody likes the IRS.” Whenever it is mentioned in conversation, people perspire, worry and generally try to make a joke of it. One can find information virtually anywhere about how to minimize, or avoid paying taxes—on television there are commercials for tax shelters and investments. In books one can find out stronger methods of protecting money, and magazines and newspapers are constantly running ads or articles designed to “lower your taxes.” In addition to all of the media coverage on tax reduction, accountants and attorneys are making a fortune trying to get or make “loopholes,” or hidden clauses in the tax code to help their clients escape large tax payments and keep their earnings. All of this for a procedure called the income tax, which in the past has been declared unconstitutional, but nonetheless an amendment was passed to make it “legal.” It has been argued and debated in Congress and in private forums, and writers like John C. Lincoln have called it

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legalized stealing, like in his 1958 pamphlet, *Stop Legalized Stealing*. The point in question is as follows: it is overwhelmingly apparent that a vast majority of our people do not like the income tax, and much less the tactics of the IRS, and though a few don’t file at all, many still succumb to it. Now, in a country that is supposed to be by the people, for the people, and of the people, that sounds a little ironic, if not totalitarian. The entire situation can be compared to an analogy of the man with pebbles in his shoes. The pebbles hurt the man’s feet, therefore he has two alternatives: he can either take the pebbles out of his shoes, or keep walking while striving to live with the pebbles in his shoes, even though they hurt. In a way, we are all like that man, we are walking around with pebbles in our shoes that very few like, yet endure their presence. How much do you know about the IRS and the income tax? How much do you know about the pebbles in your shoes?

In 1862, President Lincoln was facing a very big problem, he had a nation at civil war, a big national debt due to the costs of the war, a falling-off of customs duties, and generally a pretty big mess. Short on time and money for the government, the Revenue Act of 1862 was drawn up and passed rather quickly.

The Revenue Act of 1862 was designed to organize the collection of federal taxes (which up until then was mainly made up of customs and excise taxes) by establishing the Bureau of Internal Revenue. The Bureau of Internal Revenue, although given a new name several years later, still exists and its duty has always been the supervision and enforcement of the collection of all U.S. federal taxes. The Revenue Act of 1862, under the supervision of the new Bureau was a very comprehensive measure. The act placed a tax on nearly all manufactured items, inheritances, death duties, and a very original clause that placed a tax on net personal income.

There was little immediate opposition to the new income tax, for several reasons. The main and most obvious reason was that there was a civil war going on, and not very many people paid attention to a new bill just passed. The second reason is that the tax was on a *net* income figure, and that net was figured out by the taxpayer, with little or no supervision, so the individual was free to list whatever deductions he felt necessary to reach a net income figure. The third reason was that the original tax consisted

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of a flat 3% tax on income up to \$10,000, over the deductible of \$699, and 5% on income over \$10,000. This tax affected very few people, since in that time, few made such large amounts of money. By 1864 however, there was

the beginning of strong opposition to the tax, to the point of calling for the repeal of the tax in Congress.

The creation of the Bureau of Internal Revenue also established the office of the Commissioner of Internal Revenue, an office which exists to this day. The commissioner, as well as the new bureau, were responsible to the Treasury Department, and was given a small office in the Treasury Buildings in Washington.

There were 185 collection districts under the original Bureau, and these were all handled by the commissioner, his three office employees, and a handful of field agents called appraisers. This changed, however, as the bureau grew more efficient and organized under the watchful eyes of George S. Boutwell, who was the first commissioner of Internal Revenue. Within two years of its conception, the Bureau of Internal Revenue grew to 4,000 employees, and would remain at this level of employment for the next fifty years.

During the first four years of its operation, the bureau raised 311 million dollars in taxes for the government, which increased its previous intake of revenue by almost 10 times. After the Civil War, however, taxpayers began realizing the unfairness of the income tax, and thus began a grudging battle which occurs every year at tax time, even today. The seeming unpopularity of the income tax apparently had no bearing when Congress decided to extend the tax, in 1870, for two more years. The tax table was changed to a meager 2.5% flat tax over the personal exemption of \$2,000.

The American citizens fought the tax. The platform used was not based on the amount of the tax, but on the principle of the tax itself. The people's arguments prevailed, and the Revenue Act of 1862 died an unmourned death in 1872, with only 72,949 returns filed.

The American public would not see the ugly head of the income tax for the next forty years. This was a time when nearly 90% of all U.S. taxes came from excises on spirits, fermented liquors and tobacco. All of the taxes were still the responsibility of the Bureau of Internal Revenue, and they administered the collection of these taxes.

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Only once would the income tax threaten again during the period of time from 1872 to 1913, and that was in 1884, when another income tax law was put through Congress. This law however, was struck down and heavily criticized by the United States Supreme Court by a 5-4 vote. The decision was a deadly blow to pro-income tax legislators, as this was a precedent that could not be combated with mere legislation. This situation had to be met by a much more severe tactic.

On July 12, 1909, Congress submitted the Sixteenth Amendment to the Constitution for ratification among the states. The amendment read:

The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration.

How in the world would any red-blooded American citizen allow such a ridiculous and unconstitutional piece of legislation to be passed, much less amend the Constitution? Well, it was done, On February 3, 1913, Wyoming was the 36th state to ratify the amendment, and on February 25, 1913, the great seal of the United States was affixed to the document. A sad day indeed, that our government would allow the reinstatement of a form of slavery in the United States of America. Almost immediately after the amendment was ratified, the Unerwood Simmons Tariff Act was drawn up by Cordell Hull, a Democrat Congressman from Tennessee, and passed. This was the first comprehensive income tax law passed in forty years.

How did all of this come about, when 40 years before, such a tax was declared unconstitutional? Well, it was simple. They made it a part of the Constitution and defended it by saying that the tax was directed at the very wealthy. This argument was backed by a tax table of a 1% tax on income up to \$20,000, after the exemptions of \$3,000 for single persons, and \$4,000 for married persons. After the first \$20,000, the tax was as follows:

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2% on \$20,001	—\$50,000
3% on \$50,001	—\$75,000
4% on \$75,001	—\$100,000
5% on \$100,001	—\$250,000
6% on \$250,001	—\$500,000
7% on \$500,001	—up

Should this tax table have been made part of the amendment, and remained constant through the years, with allowance for inflation, the modern day tax rebellion would simply be a matter of principle instead of principle and money. This because the exemption of \$3,000 for single and \$4,000 for married persons in 1913 would equal \$18,360 for single and \$24,480 for married people in 1976 dollars.

The above comparison makes it easier to understand how the pro-income tax politicians were able to pawn this amendment on the electors, because not too many people would be paying taxes, and those who would have the money to pay.

The tax table was not a part of the amendment however, and that was the fatal blow, because the amendment simply stated that Congress shall be able to collect taxes on income "from whatever source derived" That power is what turned the income tax from the relatively harmless "leech on the wealthy" to the monstrous home and business wrecking instrument it is today, sapping almost 35% of the average person's annual pay.

In 1913, the Bureau of Internal Revenue became the Internal Revenue Service, IRS and by 1920 its 4,000 employees had grown to roughly 15,800, and thus began the raping of our people.

Today in 1985, the IRS, with its roster of over 82,000 employees, (an exact number is difficult, since turnover is constant) is one of the top five employers in the world. In relation to the massive Internal Revenue Code book, that is almost one employee per page of the 82,000-plus page book.

Over the years, and especially with the 1952 reorganization of the IRS, the service has spread into a complex nationwide and international net of offices and employees that process some 125 million tax returns, 428 copies of wage and information documents, over 100 different specialized tax guides, and about 323 miscellaneous forms concerning tax matters that generally intimidate the taxpayer into complying with Mr. 1040 and the some

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where near fifty schedules that accompany him. In addition to this, the service closely combs as many returns as possible and audits roughly two and a half million returns annually that have supposed "errors." All of this to raise an average annual sum of 300 billion dollars (since 1975), over half of which comes from personal income tax payments from workers.

Just how did this massive operation get organized? The IRS is divided into National, Regional District, and Local operational offices, which are spread out all over the U.S. and total over 1,000 offices. (see addendum 1)

The IRS has many resources available at its fingertips to help enforce its codes, but none of them are as infamous or as feared as the special agent. The special agent is but one of the types of field agents which the IRS uses to spread its web of intimidation. The question that arises most often concerning the special agent is this: "With thousands of special and field agents who are out committing illegal activities under the guise of a federal agency, why hasn't even one been found guilty of breaking any laws?" Well, the IRS has found a wonderful excuse. You see, the IRS code is very general and vague to begin with; its volumes number over 80,000 pages and its contents are carefully censored from public records. The ambiguity of this code, coupled with the fact that the IRS has complete power of interpretation of these laws, enables the service to "be flexible" in the way it operates. To be more concise, if the service runs into a situation that it doesn't like, it simply "interprets any relevant law to its advantage, and thus escapes legal persecution.

Special agents receive an abbreviated copy of the Internal Revenue Code as their manual. It is interesting to note that it is suspected that every "manual" that is issued to agents-in-training is different, and the particular agents are delegated the authority to interpret and enforce laws individually. Many times this use of what might be called "make up a law as you go along," is used during actual investigations, conversations with taxpayers, audits, property seizures or any other situations where it is vital that the service not set the precedent of losing a battle.

The process of the ever-changing interpretations of federal tax laws grants the IRS almost complete invulnerability from the law, as the service also has the power to collect taxes "by any

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means whatsoever." Many times, this means espionage and surveillance equipment, on which the IRS spends millions of dollars each year. Each special agent is specially trained in all surveillance techniques, many of which include phone taps, hidden cameras, hidden microphones, and even set ups that resemble the FBI sting operations, but without the publicity.

All of this is justified in the eyes of the IRS, and as far as they know, the service does nothing illegal. Well, it certainly helps if you can bend the law to meet your needs.

Many members of the general public do not know the methods which the IRS will use to collect the money they feel is due them. Even if the amount is \$5.00, you will not sleep in peace until they collect it. Following are some condensed case histories of several people who have encountered the IRS and survived to tell about it.

1. An unnamed gentleman filled out his 1040 form one year and discovered he owed a nominal amount to the IRS. The exact amount is not known publicly, but it is believed to be less than \$100. This particular gentleman was in a very bad financial situation at the time, with no job, and very little if nothing to his name. He tried to contact and co-operate with the IRS on a method of payment, to which he received only the traditional IRS procedure. They wrote him a letter saying he owed money, then wrote a stronger letter marked "URGENT," then they called him on the phone to let him know that he owed money. By this time, the gentleman was upset and frustrated at being told he had to pay money which he did not have and then he got upset with the entire situation. Upon his informing the IRS of his state of disagreement with their methods, The IRS responded by confiscating his refrigerator (for reasons unknown), and proceeded to sell it at an auction for much less than the gentleman owed them.

2. Another gentleman in the same situation as the gentleman in example 1. (the only difference being the exact amount owed, although both were nominal), went through the same grueling experiences as his predecessor in this text, and finally had his car confiscated by the IRS. His car was the only means of transportation he had, and thus the IRS had destroyed a man's means of livelihood.

3. A Kansas City, Missouri housewife was at home nursing

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her six-week-old baby one day several years ago, when she received a knock at the door. There were two IRS agents there who proceeded to enter her home uninvited, and commenced interrogating her concerning her father's tax records, with which there was apparently a small discrepancy. The young mother asked the men to please come back when her father was at home, and that she was very busy since her new born baby required all of her attention. In the following four hours of questioning, the young lady tried to call both her father and a lawyer for advice, but was harshly reprimanded with screams, and she was told that contacting a lawyer would only make it "worse for her father. In this matter she was literally held prisoner in her own home. Eventually, her father was cleared of any wrongdoing with his taxes, but that was no consolation for his daughter, who suffered a nervous breakdown from her experience with the "Infernal Revenue Service."

4. A grave situation of IRS "misaction" concerns a large production company in the midwest who owed a large tax bill to the IRS. The owners could not handle this financial burden, and decided to close the company. The employees of the company, who did not want to lose their jobs, pooled their money and bought the company. The new owners began recycling much of their pay back into the company to boost its production, and began a repayment plan with the IRS to pay back the large sum that was owed. The IRS decided that the amount they were receiving monthly as installment payments was not enough, and took possession of the physical factory and auctioned off all the company assets, causing all employees to lose their jobs. The IRS got very little from the auction, and as it disastrously ended up, they received much less than they would have if they had let the employee/owners pay back the entire bill in installments. In addition to losing the tax owed, the IRS also lost all of the income taxes they would have collected from the salaries of all the workers in the plant. It just goes to show that irrational action and greed will give you less than you deserve, all the time.

5. A famous fashion designer was found guilty of bribing two IRS agents so that they would reduce his tax liability by nearly \$800,000. The designer was of course, found guilty and ended up paying close to \$1 million in back taxes to the IRS. Nobody knows if the IRS agents were charged with taking a bribe, or

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even if they were reprimanded in any way.

Although the purpose of this book is not to merely complain about these pebbles in our shoes, called the Internal Revenue Service, but to actually present a feasible and legal substitute for the income tax. One can not help but wonder: "How can I protect myself now?" There is enough information on case histories and documented trespasses of the IRS to fill thirty volumes, but there are also many people who have found a way to alter the system we now have.

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CHAPTER 2

The purpose of this chapter is neither to condone nor reject any of those means employed by citizens to avoid the redistribution of their income, their personal wealth or their property by government decree. Rather, the purpose is to heighten the taxpayer's awareness of changing sentiments towards present federal tax policy.

Tax Deviants

What in the world is a tax deviant? Deviants are people who pay their income taxes, but try their hardest to hold on to some of their earnings. Deviation can be achieved through two methods: the use of tax loopholes, and tax deferments. These are both ways of “bending” the tax laws to be able to shelter, or hide your money under tax-free “umbrellas.” Using these devices could classify anyone as a deviant, though they are not really deviant qualities in a bad sense. They are just people trying to keep and enjoy what is rightfully theirs.

Tax deviants have been around as long as the income tax has. In the 1860s, right after the institution of the first income tax, a large portion of those few who were affected by it protested the new tax. As the years went by, the scope of the income tax grew, encompassing more people. Subsequently, the number of tax deviants grew, and so did their ingenuity. The early deviants fared well, since the first income tax was based on a net income figure, and the taxpayers themselves came up with their own net. This situation proved a perfect setting for the birth of the deduction which will be explained later.

The IRS growth strengthened the service's determination to persevere in the maximizing of tax revenues. Stricter guidelines were enacted, and taxpayers countered with even more ingenious

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ways of escaping them. By the Second World War, this process had grown into a full-fledged battle, and people with different income and educational levels settled into particular patterns of deviation which have held constant to this day. These patterns include the use of lobbyists to argue for the enactment of protection of tax deviation methods and fight against the destruction of loopholes and deferments. An example can be seen in the movement of the IRS in late 1982 to withhold taxes from interest on personal bank accounts directly at the bank. This would have been much like the withholding procedure at work, where an amount is withheld from a person's paycheck to pay for personal income taxes. The IRS proposed that the banks withhold taxes owed on interest earnings paid by the banks. The banks in the United States fought this vehemently, since it would have meant much more work for their accounting departments, resulting in an increase in expense and a great inconvenience to their customers. Thanks to lobbying and debate, the banks of this country managed to defeat this movement and thus restore sanity to the already troubled economic system.

Tax Loopholes

Tax loopholes often called tax shelters or tax umbrellas, are ways of bending the federal tax code, or interpreting undefined stipulations in the code. Taken literally, a loophole is a hole or flaw in the code through which one can escape paying a portion of their taxes. These loopholes almost always concern an investment of some kind in which the use one's money is put to, is tax-free. There are thousands of tax shelters which can be used by people of all income levels to aid them in reducing their taxes. We shall examine some of the more popular loopholes here in these pages, but for someone who desires more information, the public library is full of books like Robert Horman's *Take It Off*, Judith M. McQuown's *Tax Shelters That Work For Everyone*, and Martin A. Larson's *The IRS Vs The Middle Class* and *The Continuing Tax Rebel/ion*, which contain many methods of tax deviation.

One very popular way of sheltering money or income from the Taxes inherent in stocks, real estate or other property holdings, is to put the assets in what is called a Clifford Trust. This is a

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trust fund usually put in the name of one's child or other beneficiary who is in a much lower tax bracket than the former of the trust. This trust is valid for ten years and one day, after which all of the assets revert to the original owner. During this ten year period, the income is taxed in the beneficiary's tax bracket, which can provide a savings. Practically, this works as follows: a landowner makes \$10,000 per year in dividends on a piece of property he owns that is worth \$130,000. Under normal circumstances, since he is in a 70% tax bracket, as recipient of the dividends he would have to pay roughly 70% of the total or \$7,000 in taxes. Should the owner put the property under his daughter's name, in a living trust for the benefit of her college education, the assets of \$10,000 would be taxed according to the twelve-year-old daughter's tax level, which would be nominal. Let us say that the tax at the daughter's level total \$1,000 out of the \$10,000. In this way, the family can save 6/7 of the tax payments they would normally pay, and keep \$6,000. At the end of ten years, the property or stock reverts back to the original owner, and the tax dividends have already been accumulated, reinvested, or whatever, for ten years. This method could easily pay for your child's education, just in the cash savings on taxes, and still leave a nice cash sum at the end.

Charitable gifts are another way to save money on your taxes from otherwise highly taxable income. There are many valuable items, like jewelry, artworks, antiques or other highly appraisable items that can be acquired through auctions, or other forms of negotiation at a price much lower than the real or appraised value. Should this item or items be appraised at a higher value, and then be donated to a charitable organization, the subsequent value is used as a tax deduction for the contributor.

For example, let us hypothetically assume that John Q. Deviant, who is in the 70% tax bracket, purchased a Rembrandt, or other valuable painting for \$150,000 at an auction. This painting was then donated to the Smithsonian Institute for its art gallery. The Smithsonian appraised the painting at \$800,000 which the investor was able to deduct from his income as a charitable contribution, resulting in a substantial tax savings. One does not have to buy a Rembrandt though, to reduce one's taxes through deductions and loopholes. There are many other methods to be used.

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One of the most popular loopholes or tax shelters to lower tax liability is the use of depreciation of buildings, vehicles, equipment, or whatever else is legally considered to depreciate and can be "written off." There are three basic forms of calculating the depreciation of an asset. These methods are called the sum-of-the-digits, double declining balance, and the most common form is called straight line depreciation. While all of the forms of depreciation result in the same deduction, it is only the methods of calculation that differ. Let us take the straight method as an example, and work out the depreciation of a tractor, which was purchased for \$20,000. The rest of the information needed to calculate the depreciation of the asset are the salvage value, and the life of the asset. In this case, the salvage value or the value of the tractor at the end of its working life, is \$700, since that is what it will bring in for scrap and parts. The life expectancy of the tractor is 10 years. The straight line formula works by taking the salvage value from the cost, or $\$20,000 - \$700 = \$19,300$. The answer to the above is then divided into the number of years of the life expectancy; in this case it would be $\$19,300$ divided by 10 $\$1,930$. The final sum of \$1,930 is the amount of depreciation one can deduct annually, and for the total of 10 years, one can recover almost the entire cost of the asset in tax write-offs. It is curious to note that the government itself participates in this form of deviation. Since 1981, local governments have been allowed to sell the depreciation rights to expensive equipment owned by the city. This is done because since the local governments do not pay federal income tax, or any federal taxes, they cannot claim the depreciation on the machinery. The depreciation rights are sold to big corporations in order to pay for part of the cost of the equipment, and to allow the big corporation to write off the value of the equipment. Such a situation is currently happening in Miami, Florida, where the local government is selling depreciation rights to the new Metrorail Rapid Transit System. The local government expects to bring in \$13 million from the sale of the depreciation rights by selling the rights to 134 rail cars.

While loopholes are effective and many are, by far, the most popular form of tax deviation, there is a second type which is known as tax deferments. Tax deferments work a lot like trust funds, except that they do not require as big an initial investment.

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Tax deferments are mostly run by banks now, and are available in many different forms, among which the most popular are the IRA's (Individual Retirement Accounts), CD's (Certificate of Deposit), and Money Market accounts. These deferments work in the following manner. There is usually a minimum deposit of \$1,000 or \$2,000 required in order to open of these accounts. These accounts are tax-free because the length of the term of the account is

usually anywhere from ten to fifty years, or until you retire, or go below the minimum balance, by withdrawals. One can keep depositing in these accounts, and get up to a \$2,000 deferral of deduction from their income tax, every year. These types of deferrals are valuable and cost effective for your taxes, the only drawback being that you have to keep at least \$2,000 of your liquid funds in a bank account.

So, these methods are what make up a tax deviant. There are probably many of you out there who are right now saying, "Gee I guess I'm tax deviant." Well, that is not so bad, because you are more than likely not a harmful person. These are not the only ways of acting against the income tax, however. "How?" you say? Enter the tax avoider.