Section on Taxation

REPORT

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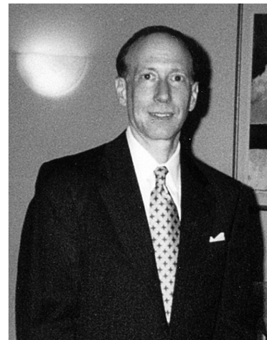
Letter from the Section Chair
Stephen A. Sherman

I hope that you enjoy this issue of the Report. There is much to share. This issue includes the first and second place winning research papers from the Section on Taxation's 2010 law student writing competition. First place was awarded to Charlotte Erdmann, Barry University School of Law, for her paper entitled "A Time for Change, A Time For Hope: The AMT's Adverse Effects on Large Families and Congress' Season to Change It." This paper discusses the history and purpose of the Alternative Minimum Tax (AMT), analyzes the impact of the AMT on large families in middle-income and upper-middle income tax brackets, and suggests comprehensive reform to ensure that the AMT does not apply inequitably to large families. Second place was awarded to Thomas Harvey, Southwestern Law School, for his paper entitled "The UBS Settlement: An Excursion Into Tax 'Fishing Expeditions.'" This paper provides an overview of the general problem faced by U.S. authorities trying to obtain tax information from abroad, describes the recent offshore tax compliance developments with regard to UBS, and discusses possible solutions to prevent future offshore tax evasion.



In addition, we have an informative interview with Daniel Patrick Mullarkey, acting deputy assistant attorney general for the Civil Section of the Tax Division of the U.S. Department of Justice. The interview chronicles Mullarkey's distinguished career and provides some of his insights regarding tax litigation at the Justice Department.

The section recently hosted three major conferences this past year. The 34th Annual Tax Law Conference was held on March 5, 2010, and was attended by approximately 400 participants. Jennifer Acuna and I co-chaired the conference, which featured a number of distinguished speakers from the government and private practice, including Thomas Barthold, chief of staff, Joint Committee on Taxation, and William J. Wilkins, chief counsel, Internal Revenue Service. The conference included 20

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panels that covered current issues in corporate and partnership tax, international tax, employee benefits, the taxation of financial products, tax accounting, and tax enforcement and procedure.

At the Tax Conference, the section was pleased to honor Fred T. Goldberg as the 2010 Kenneth S. Liles Award winner at a special ceremony. The section presents the Liles Award annually to a person who, over the course of his or her career, significantly contributes to federal tax policy and tax administration. Goldberg is currently a partner at Skaden, Arps, Slate, Meagher & Flom and is a former commissioner of the Internal Revenue Service and assistant secretary for Tax Policy of the U.S. Treasury.

The 35th Annual Tax Conference will be held be on Feb. 25, 2011, at the Ronald Regan Building and International Trade Center in Washington, D.C., and is being co-chaired by Christian Wood and James Kroger. The conference is shaping up to be another outstanding event. At this year's conference, Martin D. Ginsburg (posthumously) will be honored as our 2011 Liles Award recipient. U.S. Supreme Court Justice Ruth Bader Ginsburg will be accepting the award on behalf of her late husband.

The 22nd Annual Insurance Tax Seminar was held on June 3-4, 2010, at the JW Marriott in Washington, D.C., and was chaired by Lori Jones. The seminar featured William J. Wilkins as the luncheon speaker and had more than 440 registrants. Topics covered included Schedule UTP, tax legislative and audit issues affecting insurance companies, and international reporting and withholding issues. The 23rd Annual Tax Insurance Seminar is scheduled for May 26-27, 2011, at the Marriott Wardman Park Hotel in Washington, D.C.

The 11th Invitational Conference on Tax Administration and the Legislative Process was held on Nov. 3– 4, 2010, at the Airlie House Conference Center in Airlie, Va., approximately 50 miles outside Washington, D.C. The conference is limited to approximately 50 participants and included senior Congressional staff, current and former senior administration officials, academics and tax practitioners. The round table discussions seek to promote a wide-ranging discussion of topics related to tax policy and tax administration, with a view to lessons learned and possible improvements.

In addition, the section also sponsored a number of successful smaller events. The section sponsored two breakfast discussions: one entitled "*Textron v. United States*: Are Tax Accrual Work Papers Protected Work Product?" and the second entitled "Schedule UTP and Related Guidance." The section also sponsored two Women in Tax Law programs with themes focused on career paths and financial planning. We also sponsored a Young Tax Lawyers reception entitled "The Revolving Door Between the Private Sector and Government: Why, When, and How?" as well as well as a Careers in Tax Law luncheon for summer law clerks. Both programs focused on career guidance and paths and included panelists from the public and private sector.

I assumed the role of chair in October 2010 after Kari Larsen led our section through a successful year of conferences and programs. We also welcome Martin Milner as chair-elect, Jennifer Ray as treasurer, and Andrew Strelka as secretary. We have recently named our writing competition after the illustrious tax practitioner Donald C. Alexander, who, among other notable positions, served as a commissioner of the Internal Revenue Service and was a Liles Award recipient. Thanks to Michael Quigley, James Kroger, and Ed Froelich for their work on this matter. New this year is our sponsorship of the June 2011 issue of *The Federal Lawyer*. Martin Milner is our point person and will be working with the editors of our newsletter, John Bates and Mary Prosser, and with the co-chairs of our writing competition, Christine Hooks and Marissa Rensen, in putting together the June issue. Thanks also to John Bates and Mary Prosser for their work on this issue of the *Report*.

I welcome the opportunity to serve as section chair, and I know it will be a great experience to work with so many fine tax attorneys within both the government and the private sector. The section relies on volunteers, and I am impressed by the energy and enthusiasm of our section members who have developed programs, monitored our budget, and guided the section. The FBA staff, and in particular Adrienne Woolley and Kate Faenza, have been a tremendous help as well. I am privileged to work with our fine steering committee members as we plan an exciting schedule for 2011.

I look forward to hearing from you, our members, about your ideas or suggestions to improve the section. If you would like to become more involved in the section, or have ideas for a program, or just want to let us know how we are doing, please feel free to contact me. Also, please visit our Web site (www.fedbar.org/Sections/Section-on-Taxation.aspx) for announcements regarding section programs or to be added to our email distribution list. Thank you for your continued support of the FBA and of the Section on Taxation. ❖

Save the Date

The Federal Bar Association

in conjunction with

The Office of Chief Counsel
Internal Revenue Service

present the 23rd Annual

Insurance Tax Seminar

May 26–27, 2011
Marriott Wardman Park
Washington, D.C.

A Dialogue with Government Personnel on Property-Casualty and Life Insurance Tax Issues

Coordinated by Lori J. Jones and Nancy Vozar Knapp

Why Attend the Insurance Tax Seminar?

- It provides a unique forum for a productive exchange of ideas between the IRS and the private sector.
- The seminar features ample opportunity to ask questions of panelists, who are experts on insurance taxation.
- Events include a reception and refreshment breaks designed for more informal dialogue among participants.
- Multiple break-out sessions allow choice among currently hot topics.

Who will be attending?

- IRS personnel from Exam and Appeals as well as personnel from the Department of Justice and the IRS Office of Chief Counsel—including the Chief Counsel as this year's luncheon speaker.
- Attorneys, accountants, and others with an active interest in the federal income taxation of insurance companies and their products.

The **Marriott Wardley Park** is located at 2600 Woodley Road, NW, Washington, DC For reservations, call (800) 228-9290. *Please mention the **Federal Bar Association Insurance Tax Seminar** to receive the conference rate.*

More information and registration materials on the seminar will be available in the Spring of 2011.

Questions? Contact the Federal Bar Association at (571) 481-9100 or kfaenza@fedbar.org.

www.fedbar.org

An Interview with Patrick Mullarkey, Acting Deputy Assistant Attorney General, U.S. Department of Justice, Tax Division

Patrick Mullarkey was appointed the DOJ Tax Division's acting deputy assistant attorney general (DAAG) for civil trial matters in January 2010. In that role he oversees the litigation functions and other operations of the six regional Civil Trial Sections, the Court of Federal Claims Section, and the Office of Civil Litigation. Prior to being appointed acting DAAG, Mullarkey served as chief of the Civil Trial Section, Northern Region, for over 30 years. He received his B.S. in accounting from Marquette University and his J.D. and LL.M in taxation from Georgetown University.

FBA: Where did you start your career, and how did you come to work at the DOJ Tax Division?

PM: After graduating from college, I worked for a summer as an auditor for the Wisconsin Department of Taxation (WDOT) reviewing state tax returns, about 300 per day. I then attended law school at Georgetown University, and joined the *Law Review*. When it was discovered that I had worked as an auditor for the WDOT, I became the tax person on the *Law Review*. Paul Dean, then the dean of the law school, was an estate tax expert, and I had the opportunity to turn a couple of his speeches into an academic article. This experience first caused me to consider a career in tax law.

I also was drawn to litigation and wanted to be like Perry Mason, so I clerked for a senior district court judge who handled only civil jury trials. Observing these trials gave me vicarious trial experience. I was also able to take most of the credits necessary for an LL.M in tax law at night at Georgetown during my clerkship. It helped to have written an article for the dean because he let me take an extra-heavy course load. One of my housemates worked at DOJ. He convinced me to join a trial section in the DOJ Tax Division, which I did in 1966, at the end of my clerkship.

I considered going into private practice after completing my four-year commitment to the Tax Division. But, at that time, an attorney in private practice against whom I had litigated a case asked me to help him get a job at the Tax Division. He said that the case we had together was the most interesting case he had worked on. I told him that I had fifty of those cases. That, and the fact that I was a bachelor at the time, lived for virtually nothing in a house with a bunch of guys, and banked half my paycheck, pretty much convinced me to stay put.

It was unusual in those days for anyone to stay beyond the four-year commitment. It was as though the job was a four year course in litigation which, upon graduation, one left for the big bucks. Today that is not as true. Many of our attorneys elect to stay because they see their classmates from law school in private practice still writing memos for partners five or six years into practice, while our attorneys are handling those cases against the partners. In many respects, the Tax Division offers a higher-quality career than private practice, even though there is less financial reward.

FBA: How have your responsibilities at the Tax Division evolved over your career? Also, how has the Tax Division changed?

PM: When I joined the Tax Division, three sections handled solely tax refund claims arising in different geo-

graphical areas, one section handled refund cases before what is now the Court of Federal Claims, and one section focused on general litigation, which included bankruptcy, summons enforcement, collection and everything that wasn't refund work, for the whole country. I worked for 10 years as a trial attorney in a tax refund section before a reorganization in 1976 in which the general litigation and geographical refund sections were abolished and four geographical sections were formed to handle all cases, refund and general litigation, arising in a geographical area. I was a trial attorney in one of those sections for about a year before becoming an assistant section chief. After about a year, I was appointed the division's special litigation counsel. Shortly after that, I was appointed chief of one of the trial sections, a position which I occupied for over 30 years.

Becoming a section chief was a bit of a shock because, even after the reorganization, I previously had handled primarily refund suits. Suddenly, I had general litigation responsibilities involving lien, levy, and bankruptcy issues. These general litigation issues required more creativity and overall legal knowledge than the substantive tax issues, which could be more easily compartmentalized. Fortunately I had a great teacher in my assistant chief, Jerry Fridkin, who had spent his career in general litigation. My favorite aspect of working as a section chief was reviewing and getting involved in individual cases.

The overall work handled by the Tax Division has changed during my tenure. The 1977 reorganization was caused by the fact that it became evident by the 1970's that the number of tax refund cases was declining, while general litigation work was increasing. A general litigation attorney might have a docket of over 150 cases, while a refund attorney might have as few as 20 cases. Before the reorganization, management of the Tax Division was dominated by former refund attorneys and there were far more refund attorneys than general litigation attorneys. The reorganization caused a major cultural change within the Tax Division. It dispelled the then-common misconception that the refund attorneys were stronger litigators.

Today there are so few refund suits that, had the Tax Division not been reorganized, there would be no need for more than one refund section. A large percentage of our cases now are what would have been considered general litigation cases in the old days, such as actions to collect unpaid taxes or bankruptcy cases in which the government is competing with other creditors, although the average refund suit consumes more resources than the average general litigation type suit. In the 1970's, it was common for a civil section to have 20 to 25 jury trials per year, whereas now the entire Tax Division may have as few as 15 civil jury trials in a year.

The day-to-day life of a Tax Division trial attorney also has changed. When I started, I spent more time on the road than is common for an attorney today. Refund suits normally took several days to try. Trial attorneys now spend less time on the road because courts permit more teleconference hearings and most court appearances, and even trials, can be concluded in a single day. I was attracted to the Tax Division by the opportunity to be on my feet in court, so I didn't mind the travel. The Tax Division still is the best place to get trial experience in my view, although there is more emphasis now on pre-trial motions than there used to be.

FBA: What caused the decline in tax refund litigation?

PM: I think one factor is that the IRS places greater emphasis on resolving disputes administratively. Another factor is increased litigation costs and overburdened judicial dockets. For many taxpayers, resolving cases with the IRS through the administrative process is a more efficient and intelligent way of conducting their affairs than going to court. In most instances, the same is true for the United States. For example, the Tax Division used to be asked to litigate trust fund recovery cases involving tremendous potential liability, even though there was no chance of actually recovering significant amounts. In the last ten to fifteen years, the IRS has focused not only on liability and legal merit, but also on collectability, leading to more administrative resolutions and more efficient tax administration.

Tax shelter litigation has, to some extent, filled the void left by the decrease in tax refund cases. Tax shelter cases are resource intensive. Many tax shelter cases are partnership proceedings and technically are not refund cases, but substantively they are very similar to traditional refund work. Also, the Tax Division now seeks tax return preparer injunctions and injunctions against promoters of abusive tax schemes. Sadly, in the last ten years we have seen, and continue to see, many more cases involving professionals who attempt to profit from helping others underreport their taxes.

FBA: When the history of the Tax Division is written, what will be the highlights of the last several decades?

PM: That is a difficult question to answer because it is easy to get caught up in current issues. I believe that the ongoing tax shelter litigation, which began in the late 1990's, will prove to be very important because it is essential that taxpayers believe that the system is fair. It would have been devastating to tax enforcement in general for us not to be able to stop or at least limit the abusive tax shelters.

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Our tremendous success in prominent early tax shelter cases persuaded many taxpayers not to continue litigating shelter cases. There still are some shelters being litigated, like foreign tax credit generators, but overall we've seen a decrease in the number of sophisticated shelters coming in, which is good news for tax administration. It is less clear to me whether tax shelter cases now are being settled at the administrative level or whether the taxpayers are simply accepting their fate.

Our injunction program targeting abusive tax return preparers and shelter promoters also has been important. Injunctions are necessary because it takes too long to criminally prosecute the offenders and the schemes are easily replicated, so they can do much damage in a short period of time if left unchecked.

FBA: What is the Tax Division's relationship with the IRS Office of Chief Counsel?

PM: In a sense, the IRS is our client, and we work closely with, and communicate freely with, the Office of Chief Counsel, certainly more so than 30 years ago. In a tax refund action, for example, if the Tax Division and Office of Chief Counsel disagree on a position, we hold a joint conference to discuss the issues. These meetings often are enlightening. The Tax Division benefits from the Chief Counsel Office's substantive tax expertise, and the Chief Counsel Office benefits from our broader litigation expertise. Often, even in a substantive tax case, there are considerations other than substantive tax issues, such as how a case will play out in bankruptcy proceedings, which convince the Chief Counsel Office to change its view of litigation hazards. Also, Chief Counsel attorneys are assigned to some of our tax shelter cases involving technical issues as a part of the trial team.

FBA: How does the Tax Division make decisions regarding settling or appealing cases?

PM: With respect to both compromises and appeals, the views of the trial attorneys and the chief counsel are important. In many cases, there is agreement between the Tax Division and the chief counsel on which course of action is in the best interests of the United States. On occasion, there is disagreement and we have procedures for resolving those situations.

Regarding settlements, the relevant section chief will make the decision whether or not to settle a case in cases involving less than $500,000, assuming the Office of Chief Counsel does not object. Trial attorneys do not have that authority, although a recommendation by a trial attorney generally will be followed if it is reasonable. Settlement decisions relating to cases involving amounts over $500,000 are made by higher level officials within the Tax Division, or where more than $2 million is involved, the Associate Attorney General, unless it is a case that must go to the Joint Committee on Taxation.

Regarding appeals, if the Tax Division receives an adverse decision, the relevant trial section and the appellate section will make recommendations to the Solicitor General's office. If the trial and appellate sections agree, the recommendation becomes the Tax Division's official position. If they don't agree, there will be a conference and the Tax Division's position will be decided upon by the deputy assistant attorney general for appellate. The Chief Counsel's Office will also make a recommendation to the solicitor general. Ultimately, the solicitor general's office decides whether to appeal the case. As a practical matter, if the solicitor general's office disagrees with the Tax Division's position, or that of the chief counsel, it will typically offer a conference, rather than simply dismissing the recommendation. Conferences regarding appeal are always extremely interesting.

FBA: Which skills are most important for litigators entering the Tax Division?

PM: Because so much of our work now is motions-based, we look for good writers. I try to avoid hiring lawyers who shy away from conflict, so I look for participation in competitive athletics, moot court, theater, politics, or student body—anything that evinces the courage to stick your neck out. I also look for attorneys who are collegial, as collaboration is what makes the Tax Division run.

We provide litigation training, so we don't expect attorneys to have those skills already. Each new hire is assigned a formal mentor, but informal mentoring by experienced attorneys is more important in my view. For example, I recall once waiting in a line that stretched down the hall to talk to a Tax Division attorney who had tremendous expertise in liens and levies. It was like waiting to talk to a professor after class. This collaborative environment is what many former Tax Division attorneys tell me they miss most.

The reward for a young Tax Division attorney for working hard is getting harder cases. There is a difference between talking about how to swim and throwing someone in the water to see if they can swim, and there is no learning experience quite like actually writing a brief and having to defend your argument on your feet, knowing that the United States is depending on you to do your best. ❖

A Time for Change, A Time for Hope: The AMT's Adverse Effects on Large Families and Congress' Season to Change It

Charlotte Erdmann

I. Introduction

"Change we can believe in."[1] "Change we need."[2] "Yes we can."[3] In 2008, on the campaign trail, Barrack Obama made the following campaign promise: "I can make a firm pledge. Under my plan, no family making less than $250,000 a year will see any form of tax increase. Not your income tax, not your payroll tax, not your capital gains taxes, not any of your taxes."[4] America needs such a plan as the Alternative Minimum Tax (AMT) is increasingly affecting large families who make less than $250,000 a year.[5]

The Klaassen family has been affected by the AMT for many years. David Klassen is a family man. He is a sole practicing attorney and his wife, Margaret, is his secretary.[6] They are the proud parents of thirteen children, one of whom battled childhood leukemia and won.[7] The frugal family made ends-meet by producing their own food and using free tax forms from the post office.[8] The forms were filled out in pencil and then Margaret used a typewriter for the final versions.[9] The Klaassens were hit with an audit notice and a demand for penalties and interest for their 1994 tax return.[10] They properly claimed their personal exemptions and exemptions for their dependent children for a total of twelve exemptions on their Form 1040.[11] However, they failed to compute and attach the Alternative Minimum Tax (AMT) computations.[12]

When computing the AMT, some deductions that can otherwise be used in calculating the regular income tax may not be used when calculating the AMT, including itemized deductions for state and local taxes[13] and personal and dependent exemptions.[14] Also, when calculating the AMT, a ten percent floor applies to medical expenses instead of the regular seven and a half percent floor.[15] Sadly, the Klaassens were responsible for the AMT not because of any tax preference items, but rather because of these adjustments to their AMT determination in addition to the fact that they had a large family and lost the value of personal or dependent exemptions when calculating their AMT liability.[16]

In Tax Court, David Klassen argued not that the AMT was calculated incorrectly, but that the AMT "adversely affects large families and results in an application of the alternative minimum tax that is contrary to congressional intent."[17] Klaassen also argued that the AMT violates the right to religious freedom.[18] The Klaassens are members of the Reformed Presbyterian church and believe that children "are a blessing from God" and so they do not practice birth control.[19] Unfortunately, the Court held that the Klaassens remained liable for the AMT because

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[1]Barack Obama, Presidential candidate, 2008 Presidential campaign slogan, *available at* presidentsusa.net/campaignslogans.html (last visited Dec. 31, 2009). *See also* David Cay Johnston, *Taxing the Sick is Sick*, 122 Tax Notes 145, 145 (2009).

[2]Obama, 2008 Presidential campaign slogan, *supra* note 1.

[3]*Id*.

[4]Barack Obama, Presidential candidate, Address in Dover, N.H. (Sept.12, 2008), *cited at* www.reuters.com/article/pressRelease/idUS258402+28-Apr-2009+PRN20090428 (last visited Jan. 4, 2010). Unfortunately, President Obama broke that promise when he passed a federal excise tax on tobacco just 16 days into his presidency. John Kartch, *Obama's Broken Promise: No Tax Hikes on Those Making Less Than $250,000*, www.reuters.com/article/pressRelease/idUS258402+28-Apr-2009+PRN20090428 (last visited Jan. 4, 2010).

[5]*See infra*, notes 32, 59-60, 80, 171 and accompanying text.

[6]David Cay Johnston, *Taxing the Sick is Sick*, 122 Tax Notes 145, 145 (2009) [hereinafter Johnston, *Taxing*].

[7]David Klaassen's statement, Ways and Means Committee, *available at* waysandmeans.house.gov/hearings.asp?formmode=view&id=2449&keywords=david+klaassen (last visited Jan. 4, 2010). [hereinafter *Klaassen* statement]. Aaron Klaassen is now free of cancer and works as a fiscal analyst for the Kansas state government. Johnston, *Taxing*, *supra* note 6, at 145.

[8]Johnston, *Taxing*, *supra* note 6, at 145.

[9]Johnston, *Taxing*, *supra* note 6, at 145.

[10]*Id*.

[11]*Klaassen v. Commissioner*, T.C. Memo. 1998-241, 1998 WL 352260 (1998).

[12]*Id*.

[13]I.R.C. § 56(b)(1)(A)(ii) (all references are to the Internal Revenue Code of 1986, as amended, unless otherwise stated).

[14]I.R.C. § 56(b)(1)(E).

[15]I.R.C. § 56(b)(1)(B).

[16]*Klaassen v. Commissioner*, T.C. Memo. 1998-241, 1998 WL 352260 (1998).

[17]*Id*.

[18]*Id*.

[19]*Klaassen v. Commissioner*, T.C. Memo. 1998-241, 1998 WL 352260 (1998). *See also* David Cay Johnston, *Funny, they Don't Look Like Fat Cats*, N.Y. Times, (Jan. 10, 1999), *available at* www.nytimes.com/1999/01/10/business/funny-they-don-t-look-like-fat-cats.html?sec=&spon=&pagewanted=all) (last visited Jan. 4, 2010).

even though Congress may not have meant to catch large families such as the Klaassens, "[t]he clearest expression of legislative intent is found in the actual language used by Congress in enacting legislation."[20] In other words, courts cannot examine legislative history for intent if the statute is clear and unambiguous. Since the AMT provisions of the code are unambiguous in disallowing certain deductions when calculating the AMT, there is no equitable relief available from the courts for large families who fall into the trap of the AMT provisions, even if Congress never intended to catch large families in those provisions.[21]

David Klaassen appealed the Tax Court decision and argued "that Congress did not intend to disallow personal exemptions for taxpayers at their income level when no § 57 [preferences] are involved."[22] The Klaassens were not involved in any tax shelter activities and did not hold any tax-preferenced investments.[23] The Tenth Circuit Court of Appeals nevertheless held that "the statute's plain language unequivocally reaches the Klaassens, and our inquiry is therefore complete. While the law may result in some unintended consequences, in the absence of any ambiguity, it must be applied as written. It is therefore from Congress that the Klaassens should seek relief."[24] The court system was unable to provide the Klaassens with equitable relief because of the plain meaning rule, which will be examined in this paper as it relates to the AMT.[25] The court tossed the responsibility for AMT reform back to those who created it, Congress, to reexamine and reform the law.[26]

The appeal was decided ten years ago; in the meantime more families are being caught by the AMT. In 2004, the Ways and Means Committee asked David Klaassen to fly to Washington, D.C. to testify about how the AMT has affected him and his family.[27] He submitted a written statement and testified that he and his wife claimed twelve to fifteen personal exemptions per year for years 1994 through 2004.[28] He testified:

> the subtle mathematics of the AMT in effect has reduced the total exemption amount to which we are entitled each year. In this manner, the AMT has become a penalty on large families solely because of their size. I doubt that this was an intended purpose of the AMT. However, it is in this very manner that the AMT has cost my family in excess of $25,000.00 over the past ten years.[29]

At the end of his statement David Klaassen pleaded with the Ways and Means Committee to help him and his family, and likely all large families, in obtaining an equitable solution to the effects of the AMT from Congress.[30]

Although the Klaassens' cases are relatively old, the cases and their entire story illustrates the ill affects of the AMT on large families; 1.3 Million taxpayers were subject to the AMT in 2001.[31] It is estimated that the AMT will affect between 29 and 33 million taxpayers by 2010.[32] With the passage of time the adverse impact of the AMT on large families will likely continue to get worse unless Congress takes action to reform or repeal the AMT.

This article will examine the concept and calculation of the AMT, as well as its history and policy objectives. The AMT is thought to be unfair, outdated, complex, and unduly burdensome, thus adversely affecting large families. Those criticisms will be examined in turn. It will then be considered whether taxpayers can receive any equitable relief from the court system at which time the plain meaning rule will be examined and any exceptions to the plain meaning rule will be considered as viable options for relief from the court system. The plain meaning rule of statutory

[20] *Klaassen v. Commissioner*, T.C. Memo. 1998-241, 1998 WL 352260 (T.C. July 2, 1998).

[21] *See infra*, notes 47-49 and accompanying text.

[22] *Klaassen v. Commissioner*, 1999 WL 197172, at *2 (10th Cir. Apr. 7 1999).

[23] *Klaassen* statement, *supra* note 7.

[24] *Klaassen v. Commissioner*, 1999 WL 197172, at *2 (10th Cir. Apr. 7 1999).

[25] *See infra*, notes 90-92 and accompanying text.

[26] *Klaassen v. Commissioner*, 1999 WL 197172, at *2.

[27] Johnston, *Taxing*, *supra* note 6, at 145. David Cay Johnston notes that David Klaassen was invited to Washington to testify provided he pay his own way. He states that "asking him to pay his own way shows how much our lawmakers favor those with the resources to work Capitol Hill. This makes it hard for lawmakers to hear the voices of those without such means." Johnston, *Taxing*, *supra* note 6, at 145.

[28] *Klaassen* statement, *supra* note 7.

[29] *Id.*

[30] *Id.*

[31] Gabriel O. Aitsebaomo, *The Individual Alternative Minimum Tax: An Argument in Favor of Repeal*, 74 UMKC L. Rev. 335, 337 (2005) [hereinafter Aitsebaomo, *Argument*], *see also* Staff of Joint Comm. On Taxation, 107th Cong., Study of the Overall State of the Federal Tax Systems and Recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1986, at 17 (Comm. Print 2001).

[32] *Id.* at 337, *noted in The Alternative Minimum Tax*, Congress. Budget Office Revenue and Tax Pol'y Brief, Apr. 2004 at 2, *available at* www.cbo.gov/doc.cfm?index=5386&type=0 (last visited Jan. 4, 2010).

construction limits the sources the courts can consider when hearing statute-based disputes.[33] By understanding the rule better, one can more fully appreciate the important role of the legislative branch since it is likely the only branch that can provide equitable relief to families who are likely to be subjected to the AMT. Possible solutions to the AMT to mitigate or eliminate its harsh affects on families will then be considered.

II. The AMT and How it is Calculated

The AMT is a tax system that operates parallel to the regular income tax system, but has a broader taxable base than regular income tax.[34] The AMT is defined by "a tax equal to the excess (if any) of the tentative minimum tax for the taxable year over the regular tax for the taxable year"[35] and its provisions are found in I.R.C. §§ 55-59.[36] Like the regular income tax, the AMT is computed by determining gross income. The AMT's tax base is called alternative minimum taxable income (AMTI).[37] Many deductions that are allowed under the regular income tax system are excluded when computing one's AMTI.[38] Personal and dependent deductions are not to be considered in the AMTI, and the seven and a half percent floor of allowable medical expenses under the regular income tax system is increased to a ten percent floor under the AMT provision.[39] An exemption amount is deducted which allows many taxpayers to avoid AMT liability,[40] but is phased out for higher income earners.[41] The exemption amounts have been adjusted yearly in the form of AMT patches, which have been enacted to help taxpayers, especially the middle-class, avoid AMT liability.[42] Once the AMTI is determined, the AMT tax rate of twenty-six percent or twenty-eight percent is applied.[43] If the taxpayer's tentative minimum tax is more than his or her regular tax liability, the taxpayer is to pay the difference between between the two, which results in the taxpayer's AMT liability.[44]

III. The History and Policy Objectives of the AMT

A. *Origin and Policy of the AMT*

Ironically, the AMT and its predecessor were originally designed to promote fairness and vertical equity. However, with the passing of history, inadequate patches to the AMT and amendments to other tax code provisions, the AMT is far from the goal it seeks to accomplish. In 1966, Joseph Barr testified before Congress that 154 people with an AGI in excess of $200,000 paid no income tax in 1966 "by using substantial deductions and exclusions to completely eliminate their taxable income."[45] By 1969, Congress enacted the add-on minimum tax,[46] the AMT's predecessor, for the following purpose:

> The prior treatment imposed no limit on the amount of income which an individual ... could exclude from tax as a result of various tax preferences. As a result, there were large variations in the tax burdens placed on individuals ... with similar economic incomes ... Individuals [who] received the bulk of their income from such sources as capital gains or were in a position to benefit from ... tax preference activities tended to pay relatively low rates of tax. In fact, many individuals with high incomes who could benefit from these provisions paid lower effective rates of tax than many individuals with modest incomes. In extreme cases, individuals enjoyed large economic incomes without paying any tax at all.[47]

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[33] *See infra*, notes 117-121 and accompanying text.

[34] Daniel S. Goldberg, *To Praise the AMT or To Bury It*, 24 Va. Tax Rev. 835, 839. *See also* Jobs and Growth Tax Relief and Reconciliation Act of 2003, Pub. L. 108-27, §§ 105, 106, 177 Stat. 752, 755 (2003).

[35] I.R.C. § 55. If one's tentative minimum tax is $5000 and one's regular tax liability was $3000, one's AMT tax liability would be $2000 ($5000-$3000 = $2000). One would pay $3000 in regular income tax plus the $2000 AMT for total of $5000.

[36] I.R.C. §§ 55-59. *See also* Aitsebaomo, *Argument*, *supra* note 31, at 343.

[37] Goldberg, *supra* note 34, at 840.

[38] I.R.C. § 56(b).

[39] *Id.*

[40] I.R.C. § 55(d), *discussed in* Goldberg, *supra* note 34, at 840.

[41] I.R.C. § 55(d), *discussed in* Goldberg, *supra* note 34, at 840-41.

[42] See *infra*, notes 50-61 and accompanying text.

[43] I.R.C. § 55(b). For income less than $175,000, the twenty-six percent tax rate is applied and for income of more than $175,000, the twenty-eight percent tax rate is applied. *Id.*

[44] *Id.*

[45] Gabriel O. Aitsebaomo, *The Individual Alternative Minimum Tax and the Intersection of the Bush Tax Cuts: A Proposal for Permanent Reform*, 23 Akron Tax J. 109, 112 (2008) [hereinafter Aitsebaomo, *Proposal*]. *See also* S. Rep. No. 91-552, 2039 (1969). "Twenty-one of these had incomes over $1 million." *Id.*

[46] Tax Reform Act of 1969, Pub. L. No. 91-172, § 301, 83 Stat. 580-81 (1969). *See also* Aitsebaomo, *Proposal*, *supra* note 45, at 112.

[47] Staff of Joint Comm. on Taxation, 107th Cong., Study of the Overall State of the Federal Tax Systems and Recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1986, at 17 (Comm. Print 2001), *available at* 2001 WL 36044094 [hereinafter Joint Comm. Report 2001], *quoting* Staff of Joint Comm.

The AMT itself was enacted in 1978 with the "purpose to ensure that no individual with substantial economic income can avoid paying any federal income tax.[48] Congress stated that:

> Congress amended the present minimum tax provisions applying to individuals with one overriding objective: no taxpayer with substantial economic income should be able to avoid all tax liability by using exclusions, deductions and credits. Although these provisions provide incentives for worthy goals, they become counterproductive when individuals are allowed to use them to avoid virtually all tax liability. The ability of high-income individuals to pay little or no tax undermines respect for the entire tax system and, thus, for the incentive provisions themselves. Therefore, Congress provided an alternative minimum tax which was intended to insure that, when an individual's ability to pay taxes is measured by a broad-based concept of income, a measure which can be reduced by only a few tax incentives provisions, tax liability is at least a minimum percentage of that broad measure. The only deductions allowed, other than costs of producing income, are for important personal or unavoidable expenditures (housing interest, medical expenses and casualty losses) or for charitable contributions, the deduction of which is already limited to a percentage of adjusted gross income.[49]

As demonstrated by the Klaassen case, the AMT has not only gone astray from its purpose, but is achieving the very unfairness it sought to avoid.

B. Recent Patches to the AMT

Throughout the years, Congress has enacted various patches to the AMT in an attempt to reduce the burden of the AMT on taxpayers, including middle-class taxpayers and those with large families, but has failed to permanently fix or repeal the AMT altogether.

In 2001, Congress passed the Economic Growth and Tax Relief Reconciliation Act (EGTRRA), which patched the AMT temporarily by increasing the exemption amounts provided under I.R.C. § 55(d) for tax years 2001 to 2004.[50] The exemption amount for individual taxpayers was increased from $33,750 to $35,750 and increased for married taxpayers filing jointly from $45,000 to $49,000.[51] The Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) of 2003 increased the AMT exemption amounts to $58,000 for married taxpayers filing jointly and $40,250 for single taxpayers for taxable years 2003 and 2004 only.[52] Under the Working Families Tax Relief Act of 2004, the JGTRRA exemption amounts were extended to 2005.[53] Another patch was enacted for tax year 2006 increasing the exemption amount for married taxpayers filing a joint return to $62,550 and $42,500 for single taxpayers.[54] A similar patch was passed in 2007 raising the exemption to $66,250 for joint filers.[55]

In 2008, the Tax Extenders and Alternative Minimum Tax Relief Act of 2008 was passed.[56] In that legislation, the exemption amounts were once again increased and other AMT adjustments were also made.[57] For "taxable year beginning in 2008," the exemption amount was raised to $46,200 for single filers and $69,950 for married taxpayers filing jointly.[58] Representative Earl Pomeroy commented:

> I rise today to support this relief from the Alternative Minimum Tax, AMT. If Congress does not pass this legislation, over 25 million middle-class tax payers [sic] would find themselves subject to this tax.
>
> It is important that we provide relief to millions of

on Taxation, *General Explanation of the Tax Reform Act of 1969*, JCS-16-70, Dec. 3, 1970, at 105.

[48] Aitsebaomo, *Proposal*, *supra* note 45, at 119. *See also* Staff of Joint Comm. on Taxation, 97th Cong., General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982.

[49] Aitsebaomo, *Proposal*, *supra* note 45, at 119, *quoting* Staff of Joint Comm. on Taxation, 97th Cong., General Explanation of the Revenue Provisions of the Tax Equity and Fiscal Responsibility Act of 1982.

[50] The Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, §701(a)(b), 115 Stat. 148 (2001).

[51] *Id.*

[52] The Jobs and Growth Tax Relief Reconciliation Act of 2003, Pub. L. No. 108-27, § 106(a), 117 Stat. 752, 755 (2003).

[53] The Working Families Tax Relief Act of 2004, Pub. L. No. 108-311, § 103, 118 Stat. 1166, 1168 (2004).

[54] The Tax Increase Prevention and Reconciliation Act of 2005, Pub. L. No 109-222, § 301, 120 Stat. 345, 353 (2006).

[55] Jeanne Sahadi, *One Year AMT Fix is a Done Deal*, money.cnn.com/2007/12/19/pf/taxes/amt_vote_walkup/index.htm (last visited Jan. 4, 2010).

[56] The Tax Extenders and Alternative Minimum Tax Relief Act of 2008, Pub. L. No. 110-343, Div. C. § 102, 122 Stat. 3765, 3863 (2008).

[57] *Id.*

[58] *Id.*

> American families who want a better life for their families. The current structure of the AMT leaves middle-class households vulnerable to a significant unexpected tax bill while many very wealthy households pay no AMT. In these economic times, enacting AMT relief can put more money in their pockets rather than subject them to taxes that were not intended to apply to middle-class families.[59]

Representative Pomeroy acknowledged that a patch was needed but understood it to be only temporary and looked forward to a time when comprehensive AMT reform could be completed:

> I will cast my vote for the Alternative Minimum Tax Relief Act today so that this tax does not fall on families struggling to meet increasing prices with wages that have not kept pace with inflation . . . I do so with the hope that Congress will work next year with a new administration to advance commonsense tax reform that includes paid for AMT relief.[60]

Sadly, Representative Pomeroy's hope was not realized as another AMT relief patch was passed in 2009 as part of the American Recovery and Reinvestment Act of 2009.[61]

IV. AMT Criticisms as they Relate to Large Families

The AMT has been criticized as unfair, outdated, complex and unduly burdensome. This article examines these claims in turn in relation to their affect on large families.

A. *Unfair*

The AMT is particularly unfair to couples who file a joint tax return. It is estimated that in 2009 five percent of married couples filing jointly will owe the AMT while only one percent of single taxpayers will owe the AMT.[62] Under the current law it is expected that 40 percent of married couples filing jointly will owe the AMT in 2010 while only three percent of single taxpayers are expected to owe the tax.[63] Since 2007, the exemption amount for married taxpayers has been $66,250,[64] whereas single taxpayers filing received an exemption of $44,350,[65] resulting in the unmarried couple receiving a larger exemption by $22,450.[66] In discussing the marriage penalty in 2001, Professor Angela V. Langlotz pointed out that not only do the AMT exemption amounts benefit two single taxpayers more than a married couple, but also the point at which the exemption phase-out begins likewise favors two single taxpayers more than a married couple.[67] Since the phase-out begins at $112,500 for singles and $150,000 for married couples,[68] "[a]n unmarried couple may earn an alternative minimum taxable income of $225,000 before phase-out begins, giving them a $75,000 income advantage over a married couple."[69] She also notes that [t]he exemption amount is completely phased out at $330,000 for married couples and at $495,000 for two singles, again giving the unmarried couple a tremendous advantage of earning an additional $165,000 before losing the exemption.[70]

B. *Outdated*

Various tax reform measures under the Bush administration led to reduced tax rates under the regular income tax system but failed to correspondingly reduce AMT rates.[71] Before the Jobs and Growth Tax Relief Reconciliation Act of 2003, the top regular tax rate brackets included twenty-eight percent, thirty-one percent, thirty-six percent, and thirty-nine percent.[72] While the top regular tax brackets were so high, the AMT rates were at twenty-six percent and twenty-eight percent, and there was a substantial exemption to the AMT resulting in the AMT affecting only a few taxpayers.[73] Professor Goldberg

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[59]Hon. Earl Pomeroy of North Dakota, 154 Cong. Rec. E2149-04, 2008 WL 4377112 (Sept. 24, 2008).

[60]*Id.*

[61]*See* Pub. L. No. 111-5 §1012 123 Stat. 115, 319 (effective Dec. 31, 2008).

[62]Katherine Lim & Jeffrey Rohaly, *The Individual Alternative Minimum Tax: Historical and Projections*, *Updated October 2009*, (Urban Institute & Brookings Institute (Urban-Brookings Tax Policy Institute), Washington, D.C.), Oct. 2009, at 7, www.urban.org/UploadedPDF/411968_AMT_update.pdf (last visited Jan. 6, 2010).

[63]*Id.*

[64]I.R.C § 55(d)(1).

[65]*Id.*

[66]*Id.*

[67]Angela V. Langlotz, *Tying the Knot: The Tax Consequences of Marriage*, 54 Tax Law 329, 348-49 (2001).

68I.R.C § 55(d)(3).

[69]Langlotz, *supra* note 67, at 348-49.

[70]*Id.*

[71]Aitsebaomo, *Proposal*, *supra* note 45, at 123.

[72]Goldberg, *supra* note 34, at 845-46. *See also* JGTRRA, *supra* note 52, at 755.

[73]Goldberg, *supra* note 34, at 845. *See also* Omnibus Budget Reconciliation Act of 1993, Pub. L. 103-66, §§ 13,201, 13,202, 107 Stat. 312, 458, 461-62 (1993) (legislation that lowered regular income tax brackets while leaving the AMT tax rates

credits the increased numbers of taxpayers subject to the AMT to the reduction of the top regular income brackets from those listed above without a proportional reduction to the AMT tax brackets.[74] A narrow spread between regular income tax rates and AMT tax rates results in more taxpayers being subject to AMT liability.[75] Furthermore, as already discussed above, the various patches that the legislature enacted are only temporary, and the exemption amounts they provide are not substantial enough to protect middle- income taxpayers and large families.[76] Yet, without them, the exemption amounts would revert to pre-EGTRRA amounts, having disastrous affects.[77] Therefore, the AMT is outdated as it cannot withstand current day demands.

Also, employers often provide employees with cost of living pay increases to combat the effects of inflation on their income and purchasing power, which has the effect of pushing a taxpayer into a higher regular tax bracket.[78] The regular income tax has been adjusted for inflation annually since 1985 through the adjustment of personal exemptions, standard deductions, rate brackets and the earned income credit, but there have not been corresponding changes to the AMT.[79]

The very structure of the AMT affects disproportionately large families.[80] Standard deductions and personal and dependency deductions that are allowed under the regular income tax system are disallowed under the AMT system under I.R.C. § 56(b)(1)(E) when determining one's AMTI.[81] "By disallowing the . . . exemptions, the AMT effectively treats these ordinary deductions as though they were the prohibited tax preference items the AMT was designed to restrain. . . .,"[82] thereby compounding the systematic failures of the AMT by allowing the AMT to reach in and adversely affect the standard income tax provisions.

The Child Tax Credit ("CTC") allows families to take a credit against their income tax liability[83] thereby assisting with a family's cost of living which is generally higher than a childless family's cost of living and considers a family's ability to pay when computing regular income tax liability.[84] Yet, a similar credit is not considered when computing the AMT.[85] Not having a similar adjustment before calculating the AMT has the effect of subjecting families with children to AMT liability.[86] The CTC adjustment together with the disallowance of personal exemptions and deductions in the computation of the AMT leads large families particularly susceptible to the AMT when they are especially unable to pay it, because the higher cost of maintaining a larger family is further compounded by the reach of the AMT into the income tax provisions. Therefore the AMT effectively reduces the benefit provided by the CTC. Such consequences are contrary to the tax policy of taxing individuals, in part, based upon ability to pay. Furthermore, the AMT's tax rates at twenty-six and twenty-eight percent also tend to replace a progressive tax rate system that is found within the regular income tax system with a nearly flat rate system, affecting the vertical equity of the AMT.[87]

C. Complex and Unduly Burdensome

The AMT runs parallel to the regular income tax resulting in a system that is exceedingly complex and administratively burdensome.[88] Although many taxpayers may not have AMT liability, most taxpayers must compute the AMT to see whether they have any AMT liability causing the AMT to affect many more taxpayers than just those who are subject to AMT liability.[89] The AMT also involves performing different computations for the same items of income, credits, and deductions, making the AMT difficult and burdensome to compute.[90] As the 2001 report of the Joint Committee on Taxation stated:

> for individuals: there is a 13-line worksheet to determine if the taxpayer must file a 50-line form (Form 6251) to be used for computing the alternative minimum tax) with the taxpayer's annual income return. There is a 48-line form (Form 8801) to determine the taxpayer's credit for prior payments of the alternative minimum tax. There are ten pages of IRS instruction relating to these worksheets and forms. Complying with the alternative minimum tax requires taxpayers to devote

unchanged); Leonard E. Burman et. al., *The AMT: Projections and Problems*, 100 Tax Notes 105, 105 (2003).

[74]Goldberg, *supra* note 34, at 845.

[75]Goldberg, *supra* note 34, at 845.

[76]*See infra* notes 79-170 and accompanying text.

[77]Aitsebaomo, *Proposal*, *supra* note 45, at 123.

[78]Aitsebaomo, *Proposal*, *supra* note 45, at 138.

[79]Joint Comm. Report 2001, *supra* note 47, at *17.

[80]Aitsebaomo, *Argument*, *supra* note 31, at 350.

[81]*Id.*

[82]*Id.*

[83]I.R.C. § 24.

[84]*Id.*

[85]Joint Comm. Report 2001, *supra* note 47, at *11.

[86]*Id.*

[87]Goldberg, *supra* note 34, at 846.

[88]*Id.*

[89]Joint Comm. Report 2001, *supra* note 47, at *10.

[90]*Id.*

> considerable time to try and understand and use the maze of tax rules relating to the tax.[91]

The Joint Committee further noted that "[a]lthough there are no studies specifically measuring the compliance costs arising from the alternative minimum tax, the IRS estimates that taxpayers spend over 29 million hours annually on Form 6251."[92]

V. Is There Viable Relief Available from the Judicial System?

A. *Holdings in AMT Cases*

Where is the taxpayer burdened with the high costs of the AMT to turn for equitable relief? The taxpayer may take his or her case to court to challenge any tax imposed against the taxpayer. However, the court system often does not have relief to offer. The courts must uphold the law which is contained within the AMT provisions of the code.[93] When seeking Congress' intent, courts often refuse to look beyond the plain meaning of the statute to the legislative history in cases where the statute is highly specific and unambiguous.[94] "A Court might then adopt a textual or plain meaning approach to statutory interpretation, closing its eyes to legislative history, statutory structure, or tax policy, suggesting a congressional intent at odds with the result dictated by the language of the statute."[95] This is the situation in AMT cases because the statute is unambiguous. The AMT provisions are mechanical and clear in the calculations even if the consequences they produce are contrary to the purposes of the statutes' enactment.[96]

In *Katz v. Commissioner*, the Tax Court held that the taxpayer was liable for the alternative minimum tax even if the taxpayer was a low or moderate income earner.[97] The taxpayer in *Katz* claimed the status of married filing separately had an adjusted gross income of $46,834.16, itemized deductions of $54,275.81, and $2,800 in personal exemptions.[98] He had no regular income tax liability.[99] After computing his AMT liability, his total tax liability for the year 2000 was based solely on the AMT and was assessed at $4,214.[100] The Court dismissed the case during summary judgment and cited the unanimous opinion of *Crooks v. Harrelson*[101] as follows:

> Courts have sometimes exercised a high degree of ingenuity in the effort to find justification for wrenching from the words of a statute a meaning which literally they did not bear in order to escape consequences thought to be absurd or to entail great hardship. But an application of the principle so nearly approaches the boundary between the exercise of the judicial power and that of the legislative power as to call for great caution and circumspection in order to avoid usurpation of the latter ... It is not enough merely that hard and objectionable or absurd consequences, which probably were not within the contemplation of the framers, are produced by an act of legislation. Laws enacted with good intention, when put to the test, frequently, and to the surprise of the lawmaker himself, turn out to be mischievous, absurd, or otherwise objectionable. But in such case the remedy lies with the law making authority, and not with the courts.[102]

The *Katz* Court concluded that the taxpayer "must look to congress for relief."[103]

In *Wiese v. Commissioner*, the Wieses claimed three personal exemptions, one of which was for the disabled brother of James Weise, as well as a $2,914 deduction for medical expenses (in excess of seven and a half percent of

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[91]Joint Comm. Report 2001, *supra* note 47, at *11.

[92]Joint Comm. Report 2001, *supra* note 47, at *11.

[93]*See infra* notes 95-96 and accompanying text. *See also United States v. Am. Trucking Assocs., Inc.*, 310 U.S. 534, 543 (1940) ("[t]here is ... no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes.").

[94]David Shores, *Textualism and Intentionalism in Tax Litigation*, 61 Tax Lawyer 1, 53 (2007).

[95]*Id. See also Gitlitz v. Commissioner*, 531 U.S. 206, 220 (2001) ("Because the Code's plain test permits the taxpayers here to received these benefits, we need not address this policy concern"); *Commissioner v. Soliman*, 506 U.S. 168, 174 (1993) ("In interpreting the words in a revenue Act, we look to the ordinary, everyday senses of the words.") (internal citations omitted); *Textron, Inc. v. Commissioner*, 336 F.3d 26, 31 (1st Cir. 2003) ("The Supreme Court has repeatedly emphasized the importance of the plain meaning rule, stating that if the language of a statute or regulation has a plain and ordinary meaning, courts need not look further and should apply the regulation as it is written.").

[96]*See Klaassen v. Commissioner*, T.C. Memo. 1998 WL 352260; *Wiese v. Commissioner*, 2005 WL 1677527 (U.S. Tax Ct.) (upholding the assessment against the taxpayers by the IRS because the calculations were correct based on the unambiguous statute). *See also infra* notes 97 – 114 and accompanying text.

[97]*Katz v. Commissioner*, T.C. Memo 2004-97, 2004 WL 739852.

[98]*Id.*

[99]*Id.*

[100]*Id.*

[101]*Id., quoting Crooks v. Harrelson*, 282 U.S. 55, 60 (1930).

[102]*Id., quoting Crooks v. Harrelson*, 282 U.S. 55, 60 (1930).

[103]*Katz v. Commissioner*, 2004 WL 739852 at *3.

the taxpayers' adjusted gross income), and deductions for state and local income taxes, and real estate taxes in the amounts of $32,099 and $20,445, respectively, in 2002.[104] The Wieses, who filed jointly, reported $9,631 of taxable income and a tax liability of $963. They failed to complete and attach their Form 6251 for reporting the AMT for individuals, and they did not report any AMT liability on their Form 1040.[105] The Wieses asked the court for equitable relief in the form of a waiver of the $5,328 additional AMT tax liability ($6,291 for the tentative minimum tax - $963 from regular income tax liability).[106] The Weises faced a financially disastrous business failure in the 1990's that left their state and local income taxes and real estate taxes accrued but unpaid until they were able to catch up in 2002.[107] For both the Klaassens and the Weises, the AMT was assessed on the basis of the provisions that disallow deductions for state and local income taxes and real estate taxes,[108] allow deductions for medical expenses only in excess of ten percent of the taxpayers' AGI,[109] and the exclusion of all personal exemptions,[110] thereby attacking large families and families having ill or disabled children or other dependants.

The court in *Weise* said that "[t]he clearest expression of legislative intent is found in the actual language used by Congress in enacting legislation."[111] The Weise Court quoted favorably the United States Supreme Court's decision in *United States v. Am. Trucking Associations, Inc.*, stating "[t]here is ... no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes."[112] The Tax Court also followed the reasoning of *Rath v. Commissioner* which held that the plain language of the statute would be controlling unless doing so would produce absurd results.[113] Finally, the Weise Court also quoted a 1989 Supreme Court Case holding that "[i]n the absence of a clearly expressed legislative intention to the contrary, the language of the statute itself must be regarded as conclusive."[114]

In *Weise*, while impressed with the "conscientious taxpayers who take their tax responsibilities seriously and follow the rules,"[115] the court ultimately held that the Weises were liable for the AMT that was assessed even though the court said it was "cognizant of the inequity that [the taxpayers] perceive in the application of the AMT under the circumstances of their case."[116] Yet, perhaps there is a glimmer of hope for the taxpayer who seeks relief from the court system when absurd results are produced or when there is legislative intent to the contrary.

B. Plain Meaning Rule and Textualism

Since the plain meaning rule of statutory construction is applied to AMT tax cases, it is important to understand the rule and examine if there are any viable exceptions to the rule. Any possibility that would allow courts to consider legislative history and tax policy with regard to the AMT could produce a more equitable result for a burdened taxpayer. Because it is not a viable option, however, based on the available precedent previously discussed, it is nevertheless beneficial to understand why equitable statutory construction is not a viable option to illustrate the importance and urgency needed for Congress to take action (since a permanent solution to the inequities of the AMT rests solely in the hands of Congress). The plain meaning rule as applied to tax cases presents a greater concern because equity is an overarching policy goal of the tax code and the plain meaning of the AMT statutes produce inequitable results.

The plain meaning rule is a "rule of statutory construction ... followed by jurists who subscribe to the textualist approach, which asserts the 'primacy of the language and structure of the statute as the basis for discerning Congress' intent in enacting the law.'"[117] There are multiple benefits to the plain meaning rule. The plain meaning of the text is more reliable than legislative history when gleaning the intent of the legislative branch,[118] particularly considering the statute is the final expression of all that was considered during the legislative process. The plain meaning of the statute is "more accessible and

[104] *Wiese v. Commissioner*, 2005 WL 1677527, at *3.
[105] *Id.*
[106] *Id.*
[107] *Id.*
[108] I.R.C. § 56(b)(1)(A)(ii).
[109] I.R.C. § 56(b)(1)(B).
[110] I.R.C. § 56(b)(1)(E).
[111] *Wiese v. Commissioner*, 2005 WL 1677527, at *3.
[112] *Id., quoting United States v. Am. Trucking Associations, Inc.*, 310 U.S. 534, 543 (1940).
[113] *Wiese v. Commissioner*, 2005 WL 1677527, at *3, *quoting Rath v. Commissioner*, 101 T.C. 196, 200 (1993).
[114] *Id., quoting Burlington N. R.R. Co. Okla Tax Comm.*, 481 U.S. 454, 461 (1987).
[115] *Wiese v. Commissioner*, 2005 WL 1677527, at *4.
[116] *Id.*
[117] Eric S. Lasky, *Perplexing Problems With Plain Meaning*, 27 Hofstra L. Rev. 891, 894-95, *quoting* Eric W. Lam, *The Limit and Inconsistency of Application of the Plain Meaning Rule to Selected Provisions of the Bankruptcy Reform Act of 1994*, 20 Hamline L. Rev. 111, 111 (1996).
[118] *Id.* at 892. *See* William N, Eskridge, Jr., *The New Textualism*, 37 UCLA L. Rev. 621, 623 (1990).

comprehensible to officials and citizenry affected by the legislation"[119] and the plain meaning rule is a more effective vehicle in constraining judicial discretion than by having recourse to legislative history.[120]

One criticism against the plain meaning rule is that one must look to the language of the statute unless that language produces absurd results. Yet, often it is difficult to ascertain whether absurd consequences will result when limited to the text of the statute itself.[121]

The plain meaning rule has gone through various forms[122] ranging from a strict formalist approach where the words of the statute were interpreted literally even if such a rule would lead to absurd results[123] to a type of golden rule which will apply the facts to the literal plain meaning of a statute unless such application would lead to absurd results.[124]

Supreme Court Justice Scalia's approach for statutory interpretation has been dubbed the "new textualism."[125] This variation of the golden rule is characterized by "refusing to use statutory purpose to determine the meaning of a statute, but also considers the use of statutes *in pari materia* (upon the same matter or subject) in determining meaning."[126] Despite the multiple variations of the plain meaning rule, when it is invoked, controlling weight is given to the text of the statute itself.[127] In other words, the statute's meaning is gleaned by examining the very wording of the statute.[128]

When interpreting the tax code, and in particular the AMT provisions, courts adopt a form of textualism where the statutory language provides the clearest expression of Congress' intent even when the application of the plain meaning rule results in absurd or inequitable results, such as the *Klaassen* case.[129] However, courts will often look to other code provisions, legislative history, statutory structure, and tax policy when determining the meaning of specific words when the statutory language is ambiguous.[130]

Professor Michael Livingston points out that it is particularly difficult to apply the plain meaning rule to tax law cases simply due to the very nature of tax law itself.[131] He notes that the tax code is not "a series of unrelated enactments,"[132] but is self-contained, highly contextual, extremely detailed, and frequently amended.[133] Due to the unusual nature of tax law, courts should consider legislative history that explains a provision of the code.[134] Professor Livingston notes:

> The plain meaning rule is not helpful because there is so rarely a plain meaning in tax cases. Plain meanings are rare because of the contextual style of tax decision-making and the need to rely upon nonstatutory sources for the definition of even basic tax terms. Attempting to categorize tax provisions as 'ambiguous' or 'unambiguous' may actually obscure the issues in a case.[135]

He suggests that courts should consider legislative history when the history explains a statute and does not

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[119]*Id. See* William N, Eskridge, Jr., *The New Textualism*, 37 UCLA L. Rev. 621, 623 (1990).

[120]*Id. See* William N, Eskridge, Jr., *The New Textualism*, 37 UCLA L. Rev. 621, 623 (1990).

[121]*Id. See* Lam, *The Limit and Inconsistency*, supra note 117.

[122]*Id.*

[123]*Id. See also* Daniel A. Farber, *The Inevitability of Practical Reason: Statutes, Formalism, and the Rule of Law*, 45 Vand. L. Rev. 533, 544 (1992).

[124]Lasky, *supra* note 117, at 896. *See also* R. Randall Kelso, *Statutory Interpretation Doctrine on the Modern Supreme Court and Four Doctrinal Approaches to Judicial Decision-making*, 25 Pepp L. Rev. 37, 48 (1997).

[125]Lasky, *supra* note 117, at 898, *discussing* William N Eskridge, Jr., *Should the Supreme Court Read The Federalist but Not Statutory Legislative History?*, 66 Geo. Wash. L. Rev. 1301, 1302 (1998).

[126]*Id.* at 897-98. *See also* Maxwell O. Chiundu, *Structure and Structuralism in the Interpretation of Statutes*, 62 U. Cin. L. Rev. 1439, 1456 (1994); Kelso, *Statutory Interpretation Doctrine*, *supra* note 124, at 54.

[127]*Id.* at 898.

[128]Gregory E. Maggs, *Reconciling Textualism and the Chevron Doctrine: In Defense of Justice Scalia*, 28 Conn. L. Rev. 393, 396 (1996). *See also Connecticut Nat'l Bank v. Germain*, 503 U.S. 249, 253-54, (1992) ("[C]ourts must presume that a legislature says in a statute what it means and means in a statute what it says there. When the words of a statute are unambiguous, then, this first canon is also the last; judicial inquiry is complete.") *quoted in Am. Online, Inc., v. United States*, 64 Fed.Cl 571, 577 (Court of Federal Claims March 30, 2005); *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341 (1997) ("The plainness or ambiguity of a statute is determined by reference to the statute itself, the specific context in which that language is used, and the broader context of the statute as a whole.") *quoted in Am.Online, Inc., v. United States*, 64 Fed.Cl 571, 577 (Court of Federal Claims March 30, 2005).

[129]*See Klaassen v. Commissioner*, T.C. Memo.1998-241, affd. without published opinion 182 F.3d 932 (10th Cir. 1999); Wiese v. Commissioner, 2005 WL 1677527, at *4.

[130]Shores, *supra* note 94, at 53.

[131]Michael A. Livingston, *Congress, the Courts, and the Code: Legislative History and the Interpretation of Tax Statutes*, 69 Tex. L. Rev. 819, 826. (1991).

[132]*Id.* at 827.

[133]*Id.*

[134]*Id.* at 850.

[135]*Id.* at 872.

just embellish it.[136] "[I]n interpreting tax statutes, notions such as the plain meaning rule and legislative intent must be considered *in light* of the peculiarities of the tax legislative process."[137] He contends "[t]he tax legislative process does not support a plain meaning approach. Because of the conceptual nature of that process, there is little reason to assume that the statutory language is always right and the committee reports, or other legislative history, are wrong."[138] Livingston therefore suggests that courts should give greater deference to legislative history that primarily explains a statute's meaning and purpose as opposed to legislative history that applies a statute to an example.[139]

Professor David Shores makes a distinction between cases that turn on an issue of statutory construction that arise from statutes that are general in nature, like section 162 that allows ordinary and necessary business deductions, and those where a statute is highly specific.[140] When answering questions of the more general type, David Shores says that:

> courts will often look to legislative history, statutory structure, or tax policy in an effort to determine exactly what Congress intended when it adopted the provision or term in question [and that such an] intentionalist approach is, of course, in keeping with conventional rules of statutory construction that call for a determination of congressional intent when no clear answer can be obtained by applying the statutory language to the issue at hand.[141]

While both Professor Livingston and Professor Shores' suggestions may be helpful to the tax context in general, their suggestions would do little to assist taxpayers burdened with the AMT provisions. The AMT provisions are specific in nature and rigid in what calculations are required. Looking at a family's circumstance in light of the legislative history will not change how the calculation is applied.

C. Are there any Viable Exceptions to the Plain Meaning Rule?

Regardless of whether courts should consider the legislative history, such as those situations that professor Livingston discusses,[142] there are exceptions carved out of the plain meaning rule that allow courts to consider legislative history and intent. Yet those exceptions have not been applied in the AMT context.[143] For example, courts may consider a statute's legislative intent when the application of a statute's plain meaning would lead to absurd or futile results,[144] but this was not done in Klaassen or other AMT cases with similar "absurd" results.

Rath v. Commissioner held that controlling effect will *generally* be given to the plain meaning of a statute unless doing so would produce absurd results.[145] However, it is unclear what an "absurd result" means for the courts when deciding AMT cases. There is no direct precedent where the application of the AMT led to absurd results such that a court decided to grant equitable relief. In *Speltz v. Commissioner*, the taxpayers, a family with three children,[146] were liable for over $125,000 in AMT due to the exercise of incentive stock options.[147] However, the stock acquired by the Speltz's upon exercising their incentive stock options "dropped precipitously."[148] The court in Speltz was sympathetic to the taxpayers, but stated: "The unfortunate consequences of the AMT in various circumstances have been litigated since shortly after the adoption of the AMT. In many different contexts, literal application of the AMT has led to a perceived hardship, but challenges based on equity have been uniformly rejected."[149] Based on the Speltz case and those cited by the Tax Court in Speltz, an inequitable result is not an absurd result. However, it is absurd that the Court talks about the Speltz's plight as a perceived hardship when the harm they and their children suffered was both real and

[136] *Id.* at 881.
[137] *Id.* at 819 (emphasis added).
[138] *Id.* at 872.
[139] *Id.* at 819.
[140] Shores, *supra* note 94, at 53.
[141] *Id.*

[142] Livingston, *supra* note 131, at 881.
[143] *See Hillman v. I.R.S*, 250 F.3d 228, 232-33 (4th Cir. 2001), *rev'g* 114 T.C. 103 (2000) (Taxpayers are arguing that a plain meaning rule exception should apply to I.R.C. § 469).
[144] *United States v. Am. Trucking Assocs., Inc.*, 310 U.S. 534, 543 (1940).
[145] *Rath v. Commissioner*, 101 T.C. 196, 200, 1993 WL 338664 (U.S. Tax Ct.).
[146] *Speltz v. Commissioner*, 124 T.C. 165 (2005).
[147] *Id.*
[148] *Id.* at 166.
[149] *Id.* at 167. The court then lists the following cases where taxpayers have sought relief from the AMT on equitable grounds and have been denied that relief: *Alexander v. Commissioner*, 72 F.3d 938 (1st Cir. 1995), affg. T.C. Memo. 1995-51; *Okin v. Commissioner*, 808 F.2d 1338 (9th Cir. 1987), affg. T.C. Memo. 1985-199; *Warfield v. Commissioner*, 84 T.C. 179 (1985); *Huntsberry v. Commissioner*, 83 T.C. 742, 747-753 (1984); *Prosman v. Commissioner*, T.C. Memo. 1999-87; *Klaassen v. Commissioner*, T.C. Memo.1998-241, affd. without published opinion 182 F.3d 932 (10th Cir. 1999).

extensive.[150] The Tax Court noted how the AMT affected the Speltz's lifestyle:

> Lifestyle changes were necessary, including: Petitioner June M. Speltz had to get a job instead of staying home with the children; the oldest daughter had to switch schools; petitioners were unable to contribute to their retirement and to their children's education fund; and they had to reduce their charitable donations. Finally, they could not afford to have a fourth child, which they had wanted.[151]

Unfortunately, with the *Speltz* case as a precedent, any relief based upon a possible 'absurd result' exception to the plain meaning rule in the application of the AMT is tenuous at best.

Also, there is a frustration of purpose exception that allows the legislative intent to control "when the plain meaning of the statute produces results demonstrably at odds with the intentions of its drafters."[152] In the AMT context, this exception seems to be the strongest contender in allowing courts to decide cases contrary to the plain meaning of the AMT statutes, because the specific AMT provisions are at odds with its policy objectives. The frustration of purpose argument fails when "[a]pplication of 'broad purposes' of legislation at the expense of specific provisions ignore . . . the complexity of the problems Congress is called upon to address and dynamics of legislative action."[153] "Congress may be unanimous in its intent to stamp out the vague social or economic evil; however, because its members may differ sharply on the means for effectuating that intent, the final language of the legislation may reflect hard-fought compromises."[154]

The consideration of legislative history would greatly help the taxpayer burdened with the AMT when the AMT produces inequitable results. Not only can consideration of legislative history help illuminate drafting errors,[155] but such consideration would also give context to the statute in how it should be applied beyond the mechanics of the calculations.

Yet, if courts provide such equitable relief, they should do so carefully as textualism definitely has its place, particularly when dealing with tax issues. Professor John F. Coverdale argues that courts should not adopt antitextual readings of statutes when deciding tax cases and considers three landmark tax cases where courts have made decisions based on antitextual readings of the applicable code provision.[156] For Coverdale, antitextual means imposing interpretations on the text of the statute that neither the statute itself nor the legislative history supports.[157] While antitextual interpretations are beyond the scope of this article, Coverdale does discuss textualism in connection with the code and believes the statutory language is "the best evidence of the legislature's intent."[158] He further states:

> In cases in which a party urges the court to reject the solution required by the text enacted by Congress and to impose on the statute a reading its text will not bear, 'the debate is to be conducted before Congress, and resolution against the presently prescribed system is to be effected by statutory amendment rather than judicial gerrymandering of the existing provisions.'[159]

As exemplified in the cases of *Klaassen*, *Weise*, and *Katz*, discussed above, that is exactly what happened. "[W]hen courts seek to determine congressional intent and legislative purpose, their focus should be on 'the purposes Congress sought to achieve by the words it used,'[160] rather than on 'disembodied purposes, reasons cut loose from language.'"[161]

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[150] *Id.*

[151] *Id.*

[152] *Am. Online, Inc. v. United States*, 64 Fed. Cl. 571, 577 (Fed. Ct. Appeals March 30, 2005); *see also United States v. Ron Pair Enters., Inc.* 489 U.S. 235, 242 (1989); *United States v. Am. Trucking Assocs.*, 310 U.S. 534, 543 (1940).

[153] *Id., quoting Bd. of Governors of the Fed. Reserve Sys. v. Dimension Fin. Corp.*, 474 U.S. 361 at 373-74 (1986).

[154] *Id., quoting Bd. of Governors of the Fed. Reserve Sys. v. Dimension Fin. Corp.*, 474 U.S. 361 at 373-74 (1986).

[155] Lasky, *supra* note 117, at 892. *See also* Stephen Breyer, *On the Uses of Legislative History in Interpreting Statutes*, 65 S. Cal. L. Rev. 845, 869 (1992).

[156] John F. Coverdale, *Text as Limit: A Pleas for a Decent Respect for the Tax Code*, 71 Tul. L. Rev. 1501, 1501 (1997).

[157] *Id.* at 1504-05.

[158] *Id.* at 1518, *quoting* Earl M. Maltz, *Statutory Interpretation and Legislative Power: The Case for a Modified Internationalist Approach*, 63 Tul. L. Rev. 1, 22 (1988).

[159] *Id.* at 1520, *quoting Gott v. Walters*, 756 F.2d 902, 916 (D.C. Cir.) (Scalia, J.), vacated, 791 F.2d 172 (D.C. Cir. 1985); *see also Continental Can Co. v. Chicago Truck Drivers*, 916 F.2d 1154, 1160 (7th Cir. 1990) (Easterbrook, J.) ("disappointment with the results may supply a good reason for Congress to change the law; it does not provide a reason for a court to change the law.").

[160] *Id., quoting Walton v. United Consumers Club, Inc.*, 786 F.2d 303, 310 (7th Cir. 1986) (Easterbrook, J.).

[161] *Id., quoting Walton v. United Consumers Club, Inc.*, 786 F.2d 303, 310 (7th Cir. 1986) (Easterbrook, J.).

In addition to respecting the relative and separate roles of the legislative and judicial branches with respect to textual interpretation, Congress chose to enact the code in a rule-like form and such a formal form ought to be respected.[162] Yet such precise rules come at a high cost in that Congress cannot contemplate every circumstance to which such a rule will be applied.[163] "Rules will, therefore, in a number of cases, produce decisions different from those courts would render if they were free simply to do justice by taking into account all relevant circumstances.[164]

Furthermore, since Congress chose such formal form in enacting the code, "[using] legislative history and an imputed 'spirit' ... dishonors the legislative choice [of a rule] as effectively as expressly refusing to follow the law."[165]

Professor Coverdale also believes that courts should not update the code by interpreting statutes in light of developments that occur after the statute was enacted rather than interpreting the statute itself.[166] Yet, since legislation is enacted frequently, particularly within the code, and such legislation is effected by other code provisions, courts should take into consideration, at the very minimum, other related code provisions. For instance, as previously discussed, the Jobs and Growth Tax Relief Reconciliation Act of 2003 lowered the top regular tax rate bracket from thirty-nine percent[167] to thirty-five percent without a proportional reduction to the AMT tax brackets, which stand at twenty-six percent and twenty-eight percent.[168] Perhaps the courts should consider such code provisions when applying the AMT. Congress could not have intended certain taxpayers to be trapped by the AMT when Congress did not know that those taxpayers would be ushered into the AMT provisions by subsequent legislation, even if the AMT provisions as written were unambiguous. The clearest expression of legislative intent is not always found within the statute itself, but should be read in light of, at a bare minimum, other code provisions. Failure to do so will often lead to absurd results.

[162]*Id.* at 1521-22.

[163]*Id.* at 1523.

[164]Coverdale, *supra* note 156, at 1523.

[165]*Id.* at 1525, *quoting* Frank H. Easterbrook, *Text, History, and Structure in Statutory Interpretation*, 17 HARV. J.L. & PUB. POL'Y 61, 67 (1994).

[166]*Id.* at 1525-26.

[167]Goldberg, *supra* note 34, at 845-46.

[168]Goldberg, *supra* note 34, at 845.

VI. A Solution to the AMT Must Reside with Congress

Although these are possible arguments for relief, the precedent stands strong, so courts are almost certain to stand by the plain meaning rule and not consider the legislative history or intent in order to provide equitable relief. As noted in *Kenseth v. Comissioner*, "[i]t is not a feasible judicial undertaking to achieve global equity in taxation . . . [a]nd [even] if it were a feasible judicial undertaking, it still would not be a proper one, equity in taxation being a political rather than a jural concept."[169] Also, the court in *Katz* quoted a Supreme Court case discussing tax statutes:

> The cases before us concern the construction of existing statutes. The relevant question is not whether, as an abstract matter, the rule advocated by petitioners accords with good policy. The question we must consider is whether the policy petitioners favor is that which Congress effectuated by its enactment of § 6501. Courts are not authorized to rewrite a statute because they might deem its effects susceptible of improvement.[170]

Congress must then solve this issue. Article 1, section 1 of the Constitution vests all legislative power in Congress making Congress the primary policymaker, not the courts.[171]

While there are numerous benefits to the plain meaning rule, like simplification, one must consider to what extent equity suffers since it was the very purpose such legislation was enacted in the first place. Although one must weigh the administrative costs against the laudable goal of equity, at some point equity must win over simplification. As demonstrated, the responsibility of equitable relief to taxpayers with large families is in the hands of Congress.

VII. Possible Solutions to the AMT that Congress Should Consider

A. *Exempt Taxpayers with an Adjusted Gross Income (AGI) of $250,000 or Less from the AMT*

Professor Gabriel Aitsebaomo suggests that one way

[169]*Kenseth v. Commissioner*, 259 F.3d 881, 885 (7th Cir. 2001), affg. 114 T.C. 399 (2000).

[170]*Bradaracco v. Comissioner*, 464 U.S. 386, 398, 104 S.Ct. 756 (1984).

[171]Coverdale, *supra* note 156, at 1525; *see also* U.S. Const. Art. I, § I.

to remedy the ill effects of the AMT is to exempt taxpayers with an AGI of $250,000 or less from AMT liability altogether.[172] Because middle and upper-middle income taxpayers are increasingly subjected to AMT liability, such a solution would allow the AMT to fulfill its policy objective of ensuring that only wealthy individuals would be subject to the AMT.[173] Such a change to the AMT provisions would also allow the current administration to work toward President Obama's campaign promise: "Under my plan, no family making less than $250,000 a year will see any form of tax increase."[174]

Such a remedy would be a more permanent fix to the problem as opposed to the exemption patches that Congress must pass yearly.[175] It would also alleviate the taxpayer's administrative burden of "calculating their AMT liability before getting the benefit of the increased exemption amounts whereas, under the proposed permanent exemption of individuals with AGIs of up to $250,000, no taxpayer with [an] AGI of $250,000 or less would be required to even prepare an AMT return of any kind."[176] This type of provision, therefore, would not only relieve the middle class taxpayer by eliminating their AMT liability, but would also relieve them from having to calculate AMT liability and restore integrity to the voluntary self-assessment tax system by simplifying the AMT to a level that ordinary taxpayers could understand.[177]

B. Index the AMT for Inflation and Provide a Permanent and Substantial Exemption

Professor Aitsebaomo also suggests another way to provide relief to middle-income taxpayers, by increasing the AMT tax brackets and exemption amounts yearly to account for inflation.[178] Such a provision would not only reduce the gap between the income tax brackets and the AMT brackets, allowing fewer middle-class and large families to be subject to the AMT, but would also realign the AMT with its policy objectives. Since the regular income tax brackets and exemptions are indexed for inflation, a corresponding adjustment in the AMT system would promote fairness and vertical equity.

C. Allow Standard or Itemized Deductions and Personal Exemption Deductions for AMT Purposes

Like the Klaassens and Weises, the disallowance of standard deductions and dependency deductions when calculating the AMT is one of the main reasons that large families are trapped into having AMT liability.[179] Furthermore, when one considers the cost of living for a large family, the AMT, in disallowing standard, personal, and dependency deductions, does not reflect a family's ability to pay the AMT. $150,000 for a married couple without children may seem like a lot of money, but when a couple must provide the basic necessities of life, such as food and clothing, for twelve, thirteen, or even three children, their ability to pay the AMT is greatly decreased. Ability to pay, and ultimately, equity, is one of the very reasons why the standard, personal, and dependency deductions are allowed when computing regular income tax. Should such deductions not likewise apply in the calculation of Alternative Minimum Taxable Income? Allowance of personal and dependency deductions would help fulfill the purpose of the AMT in ensuring that only the truly wealthy are subject to the AMT.[180]

D. Add AMT-like Protection Measure to the Regular Income Tax System

By incorporating AMT-like provisions in the calculation of regular income tax, Congress can reinvent a mechanism that would only subject the wealthy to a minimum tax while protecting middle and upper-middle class families. As a result, those families would be free from AMT liability because all the benefits of personal and dependency deductions would be available to them. Furthermore, Congress can build in safeguards for middle-income families by including adjustments for inflation and more permanent exceptions such as those listed above.

E. Repeal the AMT Altogether

Perhaps Congress should just repeal the AMT altogether because it does not fulfill the policy objective of insuring that individuals and families with *substantial* income pay their fair share of the tax burden. Such an action would be in accordance with a recommendation from the Joint Committee on Taxation as late as in 2001. The Joint Committee noted:

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[172]Aitsebaomo, *Proposal*, *supra* note 45, at 139.
[173]*Id.*
[174]Obama, Address in Dover, N.H., *supra* note 4.
[175]Aitsebaomo, *Proposal*, *supra* note 45, at 139.
[176]*Id.*
[177]*Id.*
[178]Aitsebaomo, *Proposal*, *supra* note 45, at 139.
[179]*Id.* at 140.
[180]Aitsebaomo, *Proposal*, *supra* note 45, at 140.

The UBS Settlement: An Excursion into Tax "Fishing Expeditions"

Thomas Harvey

Abstract

This paper discusses the current efforts in offshore tax compliance. First, the paper begins with an overview of the general problem faced by U.S. Authorities trying to obtain tax information from abroad. Second, the paper discusses the UBS Settlement in detail. Third, the paper explains the intricacies of the case and its future implications. Fourth, the paper describes why the settlement itself is not enough to end offshore tax evasion in other tax secrecy jurisdictions. Fifth, the paper describes the advantages and disadvantages of current international tax compliance efforts. Last, the paper discusses further solutions to prevent offshore tax evasion.

I. Overview

It was once said that "the avoidance of taxes is the only intellectual pursuit that carries any reward."[1] Still, "taxes are a price we pay for civilization."[2] The difference between tax avoidance and tax evasion sometimes becomes blurred;[3] tax avoidance is considered a patriotic duty while tax evasion clearly violates the law. Obviously, placing money in an offshore account and electing not to disclose it falls into the tax evasion category. Nonetheless, just because a taxpayer has money in another country's bank does not mean that they are engaged in tax evasion. To avoid penalties, a U.S. taxpayer must indicate on Form 1040 if they have a foreign account of more than 10,000 dollars.[4] Some taxpayers may have money in other countries for business-related traveling expenses, while others may be engaged in foreign investment. Tax evaders, on the other hand, purposefully do not identify foreign accounts so as to avoid the higher income taxes they would have to pay if their money was located in the U.S.

"Tax haven" countries remain a popular destination for foreign capital for the tax evader and the corporation with a foreign subsidiary. Although there is no formal definition for a tax haven, the United States Gordon Report[5] has identified traits common to these countries: (1) low rate of tax; (2) secrecy or confidentiality to persons transacting business; (3) modern banking facilities; (4) advanced communications network; (5) lack of currency controls; (6) self promotion as a tax haven; and (7) favorable tax treaties.[6]

Recognizing the benefits of obtaining foreign deposits by offering bank secrecy and nominal tax rates, these tax havens have continued to thrive. According to one 1999 estimate, there are over 1 trillion U.S. dollars hidden in offshore accounts, resulting in 40-70 billion tax dollars of evasion.[7] Financial intermediaries have added further fuel to the fire by creating sham transactions and other hidden foreign deposits by using personal investment corporations ("PICs") so a taxpayer can effectively place assets in other countries without having to report it on IRS Form 1040.[8] Since these PICs, which are essentially investment shells, are incorporated in tax havens, the bank secrecy laws of the tax haven restrict the disclosure of the persons who own the account, which in turn, allows the PIC's owners to avoid detection.[9] These PICs are typically managed from offices and financial intermediaries located within the U.S.[10] The Union Bank of Switzerland ("UBS") is

[1]John Maynard Keynes

[2]Oliver Wendell Holmes, Jr.

[3]According to Judge Learned Hand "…a transaction, otherwise within an exception of tax law, does not lose its immunity, because it is actuated by the desire to avoid, or, if one chose, to evade, taxation." *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. Mar. 19, 1934). He continues, "[a]ny one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes." Id.

[4]*See generally* IRS Form 1040.

[5]Gordon, Tax Havens and Their Use by United States Taxpayers—An Overview, in TWELFTH ANNUAL INSTITUTE ON INTERNATIONAL TAXATION 191, 261-63 (Practicing Law Institute 1981).

[6]Some of these countries include: The Cayman Islands, Switzerland, Lichtenstein, The Cook Islands, Jersey, and The Isle of Man. For a more complete list of tax secrecy jurisdictions, please visit www.secrecyjurisdictions.com/PDF/SJ_Mapping.pdf (last visited on Oct. 19, 2009).

[7]Minority & Majority Staff Report for Permanent Subcommittees on Investigations on Tax Abuses: The Enablers, The Tools and Secrecy, August 1, 2006 p. 1 [hereinafter "The Enablers, The Tools and Secrecy"].

[8]Minority Staff Report for Permanent Subcommittees on Investigations Hearing on Private Banking and Money Laundering: A case study of Opportunities and Vulnerabilities, Nov. 9, 1999, pp. 881-882.

[9]*Id.*

[10]Federal Reserve Bank of New York, Guidance on Sound Risk Management Practices Governing Private Banking Activities, July 1997.

a multinational financial institution that has capitalized on bank secrecy. Accordingly, the U.S. government has affirmed that UBS employees were engaged in a criminal conspiracy with U.S. taxpayers to evade paying taxes to the Internal Revenue Service ("IRS"). After a lengthy criminal investigation, U.S. taxpayers, UBS bank employees, foreign nationals, and UBS itself were named as defendants. As a result, UBS signed a deferred prosecution settlement agreement in exchange for 4,450 undisclosed American accountholders.

The IRS and the Department of Justice ("DOJ") have been working hard to bring tax evasion to an end; excluding diplomacy, little can be done directly to the tax haven. Instead, U.S. authorities have been aggressively targeting taxpayers electing not to disclose foreign accounts and the financial intermediaries who have helped to hide these taxpayers' assets. Despite increasingly novel and aggressive tactics employed by U.S. authorities, little can be done to stop tax evasion without further worldwide cooperation by bringing these criminals to justice.

The Organization of Economic Cooperation and Development ("OECD") is at the forefront of international tax compliance. The OECD has created a model convention of tax information sharing treaties where Double Taxation Agreements[11] ("DTAs") and Tax Information Exchange Agreements[12] ("TIEAs") are proposed and launched.[13] Even though the model convention lacks worldwide, multilateral support, the main purpose of the convention is to improve "the process for resolving tax disputes."[14] While the UBS Settlement may be at the vanguard of tax information sharing because nations with bank secrecy laws typically do not allow for "fishing expeditions",[15] the strategy used on the Swiss will not be enough to open the doors to unrestricted mutual exchange of tax information. However, the threat of further prosecution of foreign banks may trigger increased compliance.

First, this paper analyzes the background of the UBS Settlement and its implications for gaining undisclosed taxpayer information from a tax secrecy jurisdiction. Next, this paper discusses why the UBS Settlement will not be enough by itself to end cross border tax evasion. Last, this paper proposes further solutions to prevent tax evasion.

II. The UBS Settlement: an Illustration of the Leverage Needed to Get Tax Information on Unidentified Accountholders

A. *Background of the UBS Settlement*

In its aggressive pursuit of tax evasion, the IRS has achieved the unprecedented when they were able to get the UBS Settlement. Under the agreement, the IRS will dismiss its "John Doe Summons" ("the Summons") in exchange for the names of U.S. taxpayers they believe have failed to disclose their offshore accounts in Switzerland.[16] The IRS was able to get this agreement because they used a typical law enforcement method of "finding the bigger fish to fry."

UBS is a well-to do international bank based in Switzerland. Like other foreign banks, UBS recognized the advantages of the IRS's Qualified Intermediary ("QI") program.[17] Before becoming a QI, UBS was required to make U.S. tax withholdings on all income earned from U.S. securities regardless of whether the person was a U.S. citizen or not.[18] So by becoming a QI, UBS would be

[11]Double taxation treaties are comprehensive agreements between two states to prevent income or profits from being taxed twice. The major reason countries sign such agreements is to foster foreign investment. Typically, within Article 26 of these treaties, the countries in agreement will allow for an exchange of tax information by a requesting country. *See infra* TJN Briefing.

[12]Tax Information Exchange Agreements are bilateral agreements which foster the exchange of tax information. Unlike the double taxation treaties, these agreements are for smaller, tax secrecy nations which do not typically engage in foreign investment. Also, these nations would not benefit from having double taxation treaties because they have low or no taxes on income or profits. The bulk of these agreements were signed as a result of pressure from the OECD after the Harmful Tax Practices Project of 2002 was initiated. *See infra* TJN Briefing.

[13]Draft Tax Justice Network Briefing Paper, Markus Meinzer (April 2009), www.taxjustice.net/cms/upload/pdf/TJN_0903_Exchange_of_Info_Briefing_draft.pdf (last visited on Oct. 19, 2009). [hereinafter "TJN Briefing"].

[14]The Organisation of Economic Co-operation and Development, www.oecd.org/document/38/0,3343,en_2649_33767_43777958_1_1_1_1,00.html (last visited on Oct. 19, 2009).

[15]By analogy, the term "fishing expedition" is used to describe actions of the IRS to locate information not readily available on delinquent tax-payers. Since "Congress has given the IRS broad powers to investigate 'all persons who may be liable for federal taxes,' [the IRS may] obtain items of even potential relevance to any ongoing investigation, without reference to its admissibility." *Thomas v. U.S.*, 1996 WL 679495 (D. Or. Sept. 17, 1996).

[16]Excerpts From IRS Commissioner Doug Shulman's Press Remarks on UBS, www.irs.gov/newsroom/article/0,,id=212203,00.html.

[17]The Matter of the Tax Liabilities of:, U.S. District Court for the Southern District of Florida, Case No. 08-21864-MC-Lenard/Garber, Memorandum in Support of Ex Parte Petition to Leave to Serve "John Doe Summons," Pg.3 (June 30, 2008) [hereinafter "the Memo in Support"].

[18]*Id.*

allowed to limit or forgo these withholdings for their non-U.S. taxpayer clients. In exchange for the status, UBS would be required to maintain IRS Form W-8BEN for non-U.S. taxpayers and W-9 for U.S. taxpayers.[19] In addition, the QI status required UBS to inspect their clients by checking formal identification, citizenship paperwork and residency requirements.[20] Also under the QI program, UBS was required to prepare and file Form 1099, which reported U.S. investment income—dividends, capital gains, and interest.[21] When a U.S. taxpayer refused to file the documentation, however, UBS was required to withhold twenty-eight percent on all U.S. source income.[22] Thus, the QI agreement "was intended to mark a significant departure from the historically strict financial secrecy laws enjoyed by U.S. taxpayers with Swiss accounts, which often resulted in concealing otherwise taxable income to the IRS."[23]

At one time, a tax secrecy jurisdiction would not allow "fishing expeditions," even when a tax information sharing treaty was in place. However, the circumstances surrounding UBS's misconduct has been a different case entirely. On December 12, 2007, Mr. Olenicoff pled guilty under a plea agreement, and as a condition, he was required to cooperate with U.S. authorities. According to Mr. Olenicoff, he had used different organizations, including Barclays and UBS, to send money from his accounts in the U.S. to other countries and eventually to UBS accounts he had in Switzerland. He elected to answer "NO" to possessing foreign accounts to which he was signatory.[24] According to court documents, Mr. Olenicoff was aided by UBS employee Bradley Birkenfeld to hide 200 million dollars in assets resulting in 7.2 million dollars in taxes being evaded.[25] Birkenfeld was indicted for his involvement and he agreed to cooperate with authorities in exchange for a plea agreement.[26] Birkenfeld's testimony stated that UBS personnel, instead of keeping proper forms as required by the QI agreement, would treat U.S. taxpayers as if they were non-U.S. taxpayers and therefore, would prepare and file the IRS Form 8-WBEN in lieu of the W-9.[27] Also, the testimony revealed that bank employees from Switzerland would come to the U.S. to market Swiss bank secrecy to wealthy, U.S. clients for them to evade U.S. taxes. According to Birkenfeld's estimate, some 20 billion dollars of unaccounted for assets were offshore in UBS accounts that belonged to some 20,000 U.S. taxpayers.[28]

On June 30, 2008, the DOJ obtained an *ex parte* leave by the Southern District Court of Florida to serve a John Doe Summons on UBS.[29] Under section 7609 of the Internal Revenue Code, the Secretary of the Treasury is authorized to summon records for the purpose of inquiring after "persons who may be liable to pay any internal revenue tax."[30]

Under 7609(f), [a]ny summons … which does not identify the person with respect to whose liability the summons is issued may be served only after a court proceeding in which the Secretary establishes that:

> (1) the summons relates to the investigation of a particular person or ascertainable group or class of persons;
>
> (2) there is a reasonable basis for believing that such a person or group or class of persons may fail or may have failed to comply with any provision of any internal revenue law; and
>
> (3) the information sought to be obtained from examination of records or testimony (and the identity if the person or persons with respect to whose liability the summons is issued) is not readily available from other sources.

26 U.S.C. §7609(f)

First, the summons related to an ascertainable class of persons because UBS had separated accountholders into either (1) those who filed the W-9 forms or (2) those who chose to remain undisclosed. Therefore, the undisclosed persons were ascertainable.[31] Second, there was a *reasonable basis*[32] for the belief that this group was failing to

[19]*Id.* at p. 4.
[20]Rev. Proc. 2000-12, 2000-4 I.R.B. 387, Sec. 3.02 (2000).
[21]1 Casey Fed. Tax Prac. §3:30:50
[22]Treas. Reg. §1.1441-1(e)(5)(iii) (2007).
[23]The Memo in Support at p. 3.
[24]26 U.S.C. 7206(1) (requiring a taxpayer to certify documents which they believe to be true under the penalty of perjury).
[25]The Memo in Support at p. 5.
[26]*Id.*
[27]*Id.*

[28]Department of Justice Press Release, "Swiss Bank Executive Charged with Aiding U.S. Taxpayers Evade Income Tax" (Nov. 12, 2008), www.usdoj.gov/opa/pr/2008/November/08-tax-1001.html (last visited on Aug. 29, 2009).
[29]26 U.S.C. §7609 (2009); *See also* 26 U.S.C. §7601 (2009).
[30]26 U.S.C. §7609 (2009).
[31]The Memo in Support at p. 8.
[32]The memo cites other cases where there was a *reasonable basis*: *United States v. Pittsburgh Trade Exchange, Inc.*, 644 F.2d 302, 306 (3d Cir. 1981) (ruling the reasonable basis test had been met when barter transactions of the type arranged by the Pittsburgh Exchange were "inherently susceptible to tax error"); *United States v. Ritchie*, 15 F.3d 592, 601 (6th Cir. 1994) (holding there

comply with the provision of the Internal Revenue Code because money transfers between the U.S. and Switzerland have been "inherently reasonably suggestive of tax avoidance" because of the Swiss's "widely known reputation for protecting the identity of [its] accountholders."[33]

Last, since the undisclosed accounts were located in Switzerland, the information sought for examination was not readily available because the two sources of international relief, the Mutual Legal Assistance Treaty ("MLAT") and the Double Taxation Treaty with Respect to Taxes of Income ("The Swiss Treaty" or "The Double Taxation Treaty"), were not typically viable sources.[34] Under the MLAT between the U.S. and Switzerland, the Swiss would typically exchange information under specific criminal charges of persons whose identity was readily known. Since the purpose of the Summons was for a civil matter and the exact identities of the persons were unknown, an MLAT treaty request would not have been the best alternative. Under The Swiss Treaty, the specific requests for information will typically only be granted when the identity of the taxpayers are identified. Since UBS had been maintaining the accounts in such a manner the IRS could not learn the undisclosed accountholder's identity, the use of the Summons was the only way to ascertain that information.[35]

After the petition for the Summons was granted and after the appeal that followed was denied,[36] UBS and the U.S. Authorities signed a deferred prosecution agreement where the Summons will not be issued on UBS. Originally, the U.S. was asking the Swiss to produce roughly 52,000 names.[37] However, under the agreement they negotiated, the U.S. Authorities will not seek criminal prosecution of UBS in exchange for approximately 4,450 names of persons they believed failed to comply with the Internal Revenue Code.[38] To help comply with the treaty request, the agreement states that the Swiss Confederation should establish a special task force enabling the Swiss Federal Tax Administration ("SFTA") to make final decisions on the names to disclose. The agreement further states that the first 500 decisions of SFTA must be fulfilled within 90 days and the balance of the 4,450 must be fulfilled within 360 days of the treaty request.[39]

The Swiss have been working hard to come to an acceptable conclusion to the matter. Since the agreement, they appointed Hans-Jörg Müllhaupt to head the special task force whereby thirty audit firms, forty lawyers and other tax specialists will aid in the exchange of the names.[40] Further, the agreement between the U.S. and Swiss governments even expands additional treaty requests if "they are based on a pattern of facts and circumstances that are equivalent to those of the UBS AG case."[41] What makes up "equivalent facts and circumstances" remains to be seen; even so, none of the 4,450 names have been produced.

B. The UBS Settlement's Application Towards Furthering Tax Information Sharing

It is hard to imagine that UBS executives ever believed that Swiss bank secrecy laws would be in jeopardy when they became a QI. Indeed, the agreement may have increased UBS's presence in the American Market, increased its profit share, and increased its exposure to American laws. Undeniably, the novel and aggressive strategy employed by U.S. Authorities shows the dedication and the complexity in receiving tax information through a tax information treaty request—case in point, the deferred prosecution agreement. As Senior Trial Attorney Kevin Downing stated, "[The UBS Settlement is] the beginning of this process, not the end."[42] So, the deferred prosecution agreement has opened the proverbial "can of worms" because it has shown other tax havens that the American government will seek cooperation through the threat of prosecution. In summary, the U.S. gained leverage over the tax evaders hiding their money in Switzerland because of three reasons: (1) the breach of the QI agreement produced greater willingness on behalf of the IRS to prosecute UBS's wrongdoing; (2) given that UBS's insiders became willing to disclose offshore miscon-

was a reasonable basis when legal services were being paid by large sums of cash).

[33] *Id.* at p. 9-12.

[34] The Memo in Support at p. 12-14.

[35] *Id.*

[36] *U.S. v. U.B.S. A.G.*, 2009 WL 2241122 (S. D. Fla. July 7, 2009)

[37] Government Press Releases, "UBS-IRS Settlement Over Tax Evasion Leaves Open Questions." 2009 WLNR 16485569. (Aug. 24, 2009).

[38] The U.S.-Swiss Governments' Agreement, www.irs.gov/pub/irs-drop/us-swiss_government_agreement.pdf (last visited on Oct. 19, 2009).

[39] *Id.*

[40] Stewart, David, "Swiss Agree to Expedite Process of 4,450 UBS Accounts Under Treaty Request," www.taxanalysts.com/www/features.nsf/Articles/669D6C15AE87B0B085257618007700E8?OpenDocument (last visited on Oct. 19, 2009).

[41] The Declaration of the U.S. and Swiss Governments regarding the UBS AG case, www.irs.gov/pub/irs-drop/declarations__us.pdf. (last visited Oct. 19, 2009).

[42] Downing, Kevin, Depart. of Justic. Keynote address at The American Bar Association Fall Meeting (Sept. 2009).

duct, the IRS had a reasonable basis to believe there was an ascertainable class of individuals who did not account for their offshore accounts; and (3) the treaties, to which the Swiss and U.S. are parties, could no longer prevent tax evaders from hiding behind Swiss bank secrecy laws.

1. U.S. Authorities' Willingness to Pursue Wrongdoing

UBS's strategy to solicit wealthy persons to engage in tax evasion increased its gross profits, but also increased its scrutiny to U.S. authorities. Indeed, the QI agreement helped to shelter UBS's misconduct. But, having a QI status as a foreign bank is a privilege, and it does come at a price. Initially, the IRS allowed only foreign financial institutions to apply for the QI status if there was a tax information sharing agreement in place between the U.S. and the jurisdiction to which the financial institution is located.[43] However, the IRS subsequently decided to expand the QI program to include jurisdictions with proper "Know-Your-Customer"[44] ("KYC") rules because the status itself creates a self-regulation regime.[45]

In exchange for simplified information reporting duties and the ability not to disclose proprietary accountholder information, the QI agrees to assume certain documentation and withholding responsibilities.[46] For example, if a payment of U.S. source income from securities exists and it is reportable on Form 1099 because there is no exception, then the QI must receive a Form W-9 from the taxpayer.[47] If a foreign bank that is a party to a QI agreement (1) knows that an account holder is a U.S. taxpayer who should be providing documentation, and (2) the foreign bank is prohibited by law from disclosing the account holder, then the foreign bank must request from the account holder the authority to disclose his identity or exclude U.S. securities from his account.[48] Essentially, if the accountholder does not document their status, the QI would be required to withhold U.S. source payments.[49]

[43]1 Casey Fed. Tax Prac. §3:30.50

[44]KYC rules may vary between jurisdictions. Essentially, the foreign banks must have policies and procedures in place for opening accounts, keeping records, verifying identities, etc. *See Generally* Rev. Proc. 2000-12, 2000-4 I.R.B. 387, Sec. 3.02(9).

[45]*See* Announcement 2000-48.

[46]Qualified Intermediary FAQs at Section 1: Becoming a QI, Answer 1, please visit www.irs.gov/businesses/international/article/0,,id=139238,00.html (last visited Oct. 12, 2009).

[47]*See* Rev. 2000-12, 2000-4 I.R.B. 387, Sec. 2.

[48]The Matter of the Tax Liabilities of:, U.S. District Court for the Southern District of Florida, Case No. 08-21864-MC-Lenard/Garber, Declaration of Daniel Reeves Pg. 3 (June 26, 2008) [hereinafter "The Shott Declaration"].

[49]*Id.*

Although each jurisdiction has different KYC rules, the foreign bank must have minimal policies and procedures for gathering accountholder information.[50] Also, the IRS is not allowed to do external audits of the QI under the agreement; rather, an outsider will perform the task.[51] The IRS, however, may require the outsider to make further inquiries into the QI if findings become questionable.[52] A default of the QI agreement will result in the termination of the agreement.[53] If the QI loses its status, then it will have to account for the U.S. source income for both U.S. and Non-U.S. taxpayers as it did before the agreement.[54]

By and large, the QI program itself has been a success. Instead of bullying foreign institutions into revealing information against the rule of their internal law, it allows for cooperation of withholding duties so that the U.S. may receive some tax revenue. Of course, violating the agreement will result in stricter IRS scrutiny, such as "imposing increased or more rigorous audit requirements or stricter enforcement standards on businesses operating in such jurisdictions."[55] Thus, the QI agreement itself becomes a double-edge sword. If the entity continues to cooperate, they will enjoy the benefits of lower reporting duties. But, if there is a breach, then the entity will not enjoy the wrath of the U.S. Government.

UBS opened itself up to stricter scrutiny by IRS auditors because they breached their QI agreement. They breached the agreement because did not withhold U.S. source payments of undisclosed accountholders. Before the QI agreement was breached, only outsiders were allowed to audit the financial records of UBS. Since UBS intentionally manipulated the tax records of its undisclosed accountholders to look as though they were non-U.S. accountholders, the outside auditors would not have been able to tell the difference on paper between the U.S. taxpayers who elected to disclose their offshore accounts and those who did not. After the QI was breached, UBS now became required to disclose both its U.S. accountholders and non-U.S. accountholders because a foreign branch is required to disclose all U.S. source income from securities regardless of whether the person was a citizen or not. UBS could no longer hide behind the QI agreement because the IRS has the long arm of the law and the "John Doe Summons."

Again, the QI status is a privilege; it creates self-

[50]*See* Rev. Proc. 2000-12, 2000-4 I.R.B. 387.

[51]Rev. Proc. 2000-12, 2000-4 I.R.B. 387, Sec. 10.01.

[52]Rev. Proc. 2000-12, 2000-4 I.R.B. 387, Sec. 10.06.

[53]Rev. Proc. 2000-12, 2000-4 I.R.B. 387, Sec. 11.02.

[54]*See* Announcement 2000-48.

[55]*Id.*

regulation standards and helps to ease reporting requirements. But even if a bank elects not to become a QI, the U.S. government will still likely assert jurisdiction even though there has been no contact between the U.S. and any bank employee.[56] For example, the U.S. Attorney's office in the past has prosecuted foreign nationals under the Foreign Corrupt Practices Act[57] based simply on corrupt money passing through a New York bank.[58] There is no doubt that bankers and wealthy clients who conspire to evade income taxes are guilty of the crime of conspiracy. Obviously, the fact the conspiracy took place overseas will not deter law enforcement from prosecuting the crime.[59] As a result, the future prosecution of banks, bankers, and tax evaders will continue regardless of whether the foreign bank is a QI or not. Thus, the fear of prosecution will create future compliance with the QI program.

2. UBS's Insiders Became "Willing" to Disclose Offshore Misconduct

There are so many examples of people becoming witnesses for prosecutors. Examples range from mafia hit man turning on their bosses to a Liechtensteiner bank employee cooperating with authorities in exchange for 7.3 million Euros.[60] No matter the example, the premise remains the same: if you want to catch the bigger fish, then you must entice the smaller ones. To entice the smaller ones, they need to become willing to disclose misconduct. So, the best way to receive cooperation under a treaty request is to get "snitches" to prosecute other foreign banks.

Specifically, the use of the John Doe Summons on UBS resulted after the IRS was able to get enough information from cooperating witnesses. This information allowed the first prong of section 7609(f) to be met in the UBS matter because Birkenfeld stated that UBS was keeping accountholders in separate piles marked undisclosed and disclosed. By having this undisclosed category, the IRS had an ascertainable group of individuals that needed to account for their income on Form 1040. Thus, if the IRS can get cooperating witnesses from other foreign banks who are engaged in tax evasion conspiracies, they may be able to issue further "John Doe Summons" because the second and third parts of section 7609(f) may be met nearly by default after the UBS matter.

In particular, there was a reasonable basis for the belief that persons were evading income taxes because the Swiss have a "widely known reputation for protecting the identity of [their] accountholders." So, invariably U.S. Authorities will use the UBS precedent in future John Doe Summonses' requests by stating that "Singapore or the Cayman Isles are 'widely known … for protecting the identity of [their] accountholders.'" Therefore, making the second part of section 7609(f) met nearly by default.

Also, the third part of section 7609(f) may be met in further investigations because the information will not be readily available. In particular, tax havens have bank secrecy laws and they do not typically disclose the accountholder's information through a treaty request without the person being readily identifiable. The only place the IRS will be able to learn the identity of the person is through the financial intermediaries engaged in tax evasion. Therefore, U.S. Authorities can argue the third prong of section 7609(f) can best be met through a John Doe Summons' Request and making the standard met nearly by default.

And the further use of the John Doe Summons will open the doors to criminal litigation. If a court allows an *ex parte* leave to grant a summons, the IRS will be allowed to audit all the tax records the financial intermediaries are keeping. As a result, the undisclosed accountholders should receive indictments from U.S. Authorities. In the case at bar, UBS quickly took a deferred prosecution agreement after clients and employees began to unravel the schemes the company's personnel were undertaking. A civilized country such as Switzerland cannot overlook criminal actions of its citizens and businesses in other countries and be a party to treaties expressing objections to such behavior. By having witnesses to criminal conduct, U.S. authorities can continue to make treaty requests under MLAT, under the Swiss Treaty, or under the newly agreed to U.S.-Swiss declaration, if the facts and circumstances are equivalent. Switzerland will nevertheless be obligated to fulfill such requests because they cannot continue to uphold international cooperation when its citizens are engaging in criminal conduct in other countries.

3. U.S.-Swiss Bilateral Treaties in Force

Conventions between nations can add opportunities for growth and greater duties to one another. The Double Taxation Treaty is one such series of bilateral treaties that several OECD countries signed with one another.

[56]Zeidenberg, Peter R., The Long Arm of the U.S. government: the harsh reality for foreign banks, www.dlapiper.com/the-long-arm-of-the-us-government:the-harsh-new-reality-for-foreign-banks/#page=1 (last visted on Oct. 12, 2009) [hereinafter "The Long Arm"].

[57]15 U.S.C. §§ 78dd, et seq. (2009).

[58]The Long Arm.

[59]*Id.*

[60]Senator Carl Levin, Key Note Address at the Conference on Increasing Transparency in Global Finance: A Development Imperative [hereinafter "Cong Docs"].

This series of treaties was promulgated to allow foreign persons the ability to engage in business in a foreign jurisdiction without the obstacle of paying taxes to both the jurisdiction where the person was engaging in foreign business as well as the person's host country. As a result, the double taxation treaty allows foreign persons the ability to compete with local business because their products and services now have a more comparable advantage. However, the Double Taxation Treaty has created greater exchange of information duties.[61] In particular, the Swiss Treaty requires the competent authority in Switzerland will "provide information…in the form of authenticated copies of unedited original records or documents" to U.S. authorities when there is an issue of tax fraud.[62] Even though either country does have the opportunity to terminate the treaty, the diplomatic process of terminating the agreement takes six months to carry out.[63] The UBS settlement agreement marks the first time the Swiss have allowed for a fishing expedition. Before the settlement, the Swiss were willing to cooperate with a treaty request if the U.S. authorities "clearly identif[ied] the taxable person concerned."[64] Of course, with UBS's employees engaging in conspiracy and the resulting media hype, the Swiss are following through with this fishing expedition.

In addition, the MLAT has further taken away from the Swiss's immunity from international liability. In 1977, the MLAT treaty went into force.[65] The treaty was undertaken "to afford each other … mutual assistance in investigations or court proceedings in respect to offenses the punishment of which falls … within the jurisdiction of the judicial authorities requesting state [and compliance with such a request requires] effecting the production … of judicial or other documents, records, or articles of evidence."[66] However, the MLAT treaty between the U.S. and Switzerland does "not apply to investigations or proceedings concerning violations with respect to taxes…" unless the person or persons are involved violent organized crime.[67] Nevertheless, certain offenses result in compulsory measures such as fraud against the requesting state and subordination of perjury.[68] A person is guilty of committing fraud against the United States when they "knowingly execute, or attempt to execute, any scheme or artifice with the intent to defraud the United States."[69] A person is guilty of subordination of perjury in the United States when they "procure another to commit perjury."[70]

Even though the U.S. Authorities chose a request under the Swiss treaty, they could have been entitled to an MLAT treaty request because helping clients to file tax documents without disclosing offshore accounts is subordination to perjury.[71] By allowing clients such as Olenicoff to certify false tax documents when UBS was the QI charged with ensuring the quality of the tax records, it committed a criminal offense. Also, bank employees marketed bank secrecy to wealthy clients to evade taxes, which is a major fraud because it was a scheme to defraud the United States. Even if the MLAT treaty does not allow for treaty requests for tax violations, the treaty does clearly allow for a compulsory exchange of information for subordination of perjury and fraud against the requesting state. So, such a request would still bind the Swiss to the agreement.

In summary, by opening itself up to international cooperation through treaties, having people turn state's evidence on the actions of its companies, and the U.S. law enforcement's painstaking pursuit of wrongdoers, tax evaders will not have the ease as they did before to hide their money in Swiss accounts. Since the Swiss are now bound to the agreement because of the UBS Settlement, they cannot as easily rely on their bank secrecy laws.

III. Why The U.S. May Not Gain the Same Leverage Over Tax Evaders in Other Tax Havens

If nothing else, the UBS Settlement shows the extent of pressure needed to allow a fishing expedition of unidentified accountholders under a tax information treaty request. With that said, U.S. Authorities may be worse off diplomatically with other tax havens in comparison. For example, the U.S. has only entered fourteen different TIEAs[72] with tax havens in the last decade.[73] Nonetheless, like the treaties set up between the U.S. and Switzerland,

[61] *See* Convention for the Avoidance of Double Taxation with Respect to Taxes on Income, U.S.-Swiss, Jan. 7, 2007, 3 U.S.T 3972.

[62] Article 26(1)(b), 3 U.S.T. 3972.

[63] Article 30, 3 U.S.T. 3972.

[64] *See* Article 26, 3 U.S.T. 3972.

[65] Mutual Assistance in Criminal Matters, U.S.-Swiss, May 25, 1973, 27 U.S.T. 2019.

[66] Article 1, 27 U.S.T. 2019.

[67] *See* Article(s) 2; 6(2) (a); 6(3), 27 U.S.T. 2019.

[68] Schedule: Offenses for Which Compulsory Measures Are Available, 27 U.S.T. 2019.

[69] 18 U.S.C. §1031 (2009).

[70] 18 U.S.C. §1622 (2009).

[71] 26 U.S.C. §7206(1).

[72] "Tax Information Exchange Agreements"

[73] Addison, Timothy V., *Shooting Blanks: The War on Tax Havens*, 16 Ind. J. Global Legal Stud. 703, 715-716, (2009) [hereinafter "Shooting Blanks"].

eighty-seven nations have pledged to adopt other OECD tax information sharing agreements.[74] Moreover, other nations may have chosen to adopt similar agreements because of new multilateral support for economic incentives and sanctions.[75] Of all the nations that were requested to comply with the OECD Model Convention, none are now considered "blacklisted."[76] All formerly blacklisted nations are now in compliance (including Switzerland) or plan to be sharing tax information in the future.[77] Even though the OECD model convention has not infiltrated all tax secrecy jurisdictions, it is the best effort undertaken so far to thwart tax abuse. Accordingly, there are disadvantages and advantages to the accomplishments of the OECD Model Convention.

A. The Advantages of the Model Convention in Preventing Tax Evasion

The OECD is a multilateral cooperation effort to bring nations' goals and objectives together. The convention is comprised of both model DTAs[78] and model TIEAs depending on what is more suitable for the nations that are signing such agreements. DTAs, on the one hand, favor richer countries because the purpose of such an agreement is to help ease foreign direct investment ("FDI") and richer countries are more likely to be engaged in FDI. TIEAs, on the other hand, are essentially informational sharing devices which better serve the poorer countries that may have no or low taxes on income or profits. Accordingly, cooperation through model convention agreements has led to remarkable tax compliance between nations.

Unlike any other multinational undertaking involving taxation, the OECD's global forum remains unmatched. The organization itself has over 200 committees and boasts some 40,000 senior officials.[79] Because of the extensive participation by member countries, the model convention serves as the principal source of guidance. For example, the model convention itself undertook the task of creating model TIEAs for smaller tax secrecy jurisdictions and forced cooperation with such arrangements through the threat of sanctions and blacklisting.[80]

In addition, the OECD is receiving a larger foundation base as time goes by. Since April 2009, ninety TIEAs have been signed and sixty TIEAs have been negotiated or renegotiated to reflect the new amendments.[81] Also, all major onshore and offshore centers have embraced the standards of tax information exchange proposed by the OECD, or they are removing the impediments surrounding the cooperation.[82] Clearly, because of the worldwide support surrounding the issue, tax evasion in offshore banking centers might be losing its lackluster.

B. The Disadvantages of the Model Convention in Preventing Tax Evasion

Some of the OECD Model Convention's aspects stand in stark contrast of its purpose. Given that many of these smaller island nations have come to depend on the revenue based on offshore tax evaders, micro compliance by financial institutions will surely go to the wayside. Although a great majority of tax secrecy jurisdictions are now in compliance or will be in the future, there are still many obstacles the OECD needs to work through.

First, the framework of the model convention does not allow for ease in creating multinational agreements because there are roughly ninety member countries. For example, the new amendments to the convention must first pass the scrutiny of all member countries and if one or more countries do not agree with such a provision, the model convention itself will say something similar to "Austria does not agree with the article" or "Mexico reserves the right to…."[83] This seeming lack of uniformity is a result of internal laws and administrative practices followed by each member state.[84] Without changes to such laws, the model convention lacks the uniformity needed to allow for complete multilateral compliance.

Second, revealing information under a treaty request may cause problems because such information may not be readily available or it may have been collected in a

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[74] *See* Cong. Docs

[75] G20Summit: An Update on the Move to Greater Transparency and International Cooperation in Tax Matters, www.oecd.org/document/38/0,3343,en_2649_201185_43777958_1_1_1_1,00.html (last visited on Oct. 21, 2009).

[76] A Progress Report On The Jurisdictions Surveyed By The OECD Global Forum In Implementing The Internationally Agreed Tax Standard (Oct. 20, 2009), www.oecd.org/dataoecd/50/0/43606256.pdf (last visited on Oct. 21, 2009).

[77] *Id.*

[78] "Double Taxation Treaty"

[79] Ault, Hugh J., Reflections on the Role of the OECD on Developing International Tax Norms, 34 Brook. J. Int'l L. 757, 758. (2009).

[80] TJN Briefing.

[81] Gurría, Angel. G20 Summit: An Update on the Move to Greater Transparency and International Cooperation in Tax Matters, (Pittsburgh Sept. 25, 2009), www.oecd.org/document/38/0,3343,en_2649_37427_43777958_1_1_1_1,00.html (last visited on Oct. 19, 2009).

[82] *Id.*

[83] *See* The 2008 update to the Model Tax Convention, www.oecd.org/dataoecd/20/34/41032078.pdf.

[84] *See* TJN Briefing.

manner intended to deliberately avoid detection.[85] In particular, the only requirement under a TIEA request is that the requested party "uses all relevant information gathering measures to provide the applicant party what they requested."[86] Even if the country subscribes to KYC rules, "all relevant informational gathering measures" will serve little purpose if the identity is falsely recorded or intentionally altered. Even if information is collected correctly, exchanging that information may take time to process because bilateral treaties lack an automatic exchange.[87] Instead, under the current exchange protocol, a requesting party must deliver a detailed case of the person involved and the information being sought.[88] One example of an automatic information exchange program is The European Union's Savings Directive,[89] but the OECD does not have an automatic exchange even in the planning stages. Instead, a requesting party must make treaty requests but receiving such information under the current agreement standard "is sporadic, difficult and unwieldy for tax administrators under the best of circumstances."[90] Therefore, much more needs to be done to create further disclosure of tax information so informational requests become "continuous, easy and manageable."

IV. The Three-Pronged Approach To Further Prevention of Offshore Tax Evasion

Notwithstanding the major advances made since the Gordon Report was published in 1981, more can be done to prevent tax evasion in the future. With all the advances made because of the UBS Settlement, further prevention will require a systematic, three-pronged approach aimed at three major reasons contributing to such abuse: (1) the tax-haven hiding behind its secrecy laws; (2) the financial intermediary marketing evasion; and (3) the wealthy individual who believes it is their God-given right not to pay taxes.

A. *At the International Level*

International diplomacy can be the strongest weapon against tax abuse. Although tax havens have gained their notoriety through liberal tax laws, incentives and sanctions can be used to loosen such laws. Currently, eighty-seven countries have joined the OECD Model Treaty.[91] Although the model convention faces criticism for having fundamental flaws, it is the best international taxation compliance venture thus far. By incentivizing and sanctioning countries into bilateral tax information exchanges, U.S. Authorities can further prevent tax evasion.

The OECD convention seems to be an answer to worldwide cooperation. By creating standards for nations to follow, cross-border tax evasion is slowly ending. The biggest problem, however, is the automatic exchange of information. Even so, an automatic exchange of information by itself may not be enough because KYC standards are flawed. In particular, the IRS initially considered granting QI statuses to countries which had tax information treaties or exchanges.[92] But subsequently, the service decided to expand the QI program to include countries that they considered to have "acceptable KYC rules."[93] There are inherent problems with appointing foreign banks as QIs. For example, the IRS's current KYC standard for foreign accountholders in the Cayman Islands requires only photo identification such as a passport or driver's license.[94] By allowing foreign banks the ability to become a qualified intermediary, the agreement implies the entity will engage in the necessary tax withholdings of the U.S. taxpayers and grants an immunity of sorts of direct IRS auditing.[95] Instead, an outsider is in charge of the auditing, and the IRS is granted review of the outsider's findings.[96] Of course, if there is an inconsistency, the IRS can order more audits.[97] But the main problem remains the adequacy of the information obtained and the ease of access to that adequate information. So, if the convention increases KYC standards combined with an automatic exchange of information, taxpayers' information would automatically be disclosed to the IRS. If KYC identification standards are increased so all member OECD countries are required to fingerprint every foreigner accountholder, then an automatic information exchange will prove more effective.

Like any other large, international organization,

[85] *Id.*
[86] *Id.*
[87] *Id.*
[88] *Id.*
[89] *See* Council Directive 2003/48, 2003 O.L. (L 157) (EC) (directive dealings with the taxation of savings income in the form of interest payments in EU countries).
[90] *See* Sheppard, Lee 2009: Don't Ask, Don't Tell, Part 4: Ineffectual Sharing in: Tax Notes (March 23, 2009). 1411-1418.
[91] *See* Cong Docs.
[92] 1 Casey Fed. Tax Prac. §3:30:50
[93] *Id.*
[94] The Qualified Intermediary Agreement between the U.S. and the Cayman Islands, Section 4(i), www.irs.gov/pub/irs-trty/qiattachcaymanis.pdf (last visited Oct. 10, 2009).
[95] *See* Rev. Proc. 2000-12, 2000-4 I.R.B. 387.
[96] Rev. Proc. 2000-12, 2000-4 I.R.B., Sec. 10.01.
[97] Rev. Proc. 2000-12, 2000-4 I.R.B., Sec. 10.06.

change can take time. The OECD's primary purpose so far is collecting a membership base; but inevitably, they will need to provide tougher standards and quicker information exchange within the model treaty in the future.

B. At the Transactional Level

Since the IRS began the Offshore Credit Card Program ("OCCP"),[98] John Doe Summonses were sent to MasterCard, American Express, Visa, and other financial and nonfinancial companies within the U.S.[99] Despite these summonses producing U.S. taxpayer transaction information, it failed to produce most of the names of the accountholders.[100] The IRS then embarked through the pain staking process of identifying "high risk, high income return" individuals who might match the transactions discovered through the summonses.[101] Even though the OCCP has largely been a success with identifying transactions, little can be done to the undisclosed accountholders who do not use their accounts for debit card transactions. Unsurprisingly, these tax secrecy jurisdictions have laws that are unfavorable towards American interests. Since forcing such nations into compliance with American interests can be brought about by sanctions, scrutiny and preventing Americans from doing business with such nations, the U.S. should consider forbidding Americans from having offshore accounts in these jurisdictions until they come into compliance with U.S. interests.

One of the best preventive measures the U.S. authorities can do in forcing compliance is to "lock-out" financial institutions from doing business with American businesses. Congress should grant the broad authority to "the Treasury Department to bar U.S. financial institutions from doing business with the offending banks or jurisdictions and essentially locking them out of the U.S. financial system."[102] One such organization within the Treasury that regulates foreign transactions is the Office of Foreign Asset Control ("OFAC").[103] Besides serving foreign policy objectives, OFAC ensures compliance by assessing and imposing civil penalties and potential criminal charges for violators. For example, OFAC will impose a fine of 250 dollars if a person is in possession of a 250 dollar box of Cuban cigars. While the agency's primary purpose is to target enemy transactions of the U.S., it can be granted broad authority to block wire transfers to and from tax secrecy jurisdictions, impose civil fines on institutions engaged in business with such nations, and impose criminal fines on those who place their money in the nation's accounts. By tracking the source and implementing the strategy used in the UBS settlement, U.S. Authorities can bring lawsuits against the organizations who engage in such transactions. Therefore, this lock-out measure will prevent future transactions from taking place until substantial compliance with tax information standards is met.[104]

Since G-20 nations[105] essentially control economic incentives and sanctions, compliance with information exchange is inevitable. If tax information is being exchanged from tax secrecy jurisdictions, tax evaders will be less likely to hide their money in those countries. On the other side, if financial institutions are barred from transacting with offending jurisdictions, then tax evaders cannot send their money to hidden offshore locations. Of course, the "lock-out" provision will not block wealthy individuals from filling up their yachts with gold bars and setting sail for a tax secrecy jurisdiction. But again, this "lock-out" provision will add one more layer in ensuring tax compliance.[106]

C. At the Taxpayer Level

The unfortunate part of having a great standard of living means having higher taxes. For example, in 2007 the top 1 percent of wealthy individuals in the U.S. paid 40.42

[98] *See* The Offshore Credit Card Program, www.irs.gov/privacy/article/0,,id=131233,00.html (last visited on Oct. 10, 2009)

[99] *See generally* The IRS Newsroom discussing John Doe Summonses Being Issued on Several Companies, www.irs.gov/newsroom/article/0,,id=105698,00.html (last visited on Oct. 10, 2009). [hereinafter "VMA"].

[100] Shafiroff, Ira L. Internal Revenue Service Prac. & Proc. Deskbook, §3:2.4, 3-19 (2006).

[101] *Id.*

[102] Cong Docs.

[103] *See* the OFAC website, www.treas.gov/offices/enforcement/ofac/ (last visited on Oct. 10, 2009)

[104] *Id.*

[105] The G-20 nations are the economic powerhouse countries (and regions) of the world. This list includes: The U.S., The EU, United Kingdom, Brazil, China, Argentina, Russia, and Saudi Arabia. Please visit www.g20.org/about what is g20.aspx (last visited Oct. 20, 2009).

[106] Congress may add another prevention method to the QI agreement. On Oct. 27, 2009, a new bill was introduced to the house ways and means committee. Foreign Account Tax Compliance Act of 2009, S._, 111th Cong. (2009). "The Bill would … impose a 30% tax on payments made to foreign financial institutions, unless they comply with disclosure and certification requirements relating to their U.S. accountholders, and to foreign non-financial institutions in certain circumstances." Humphreys, Merali, Reigersman. "Foreign Account Tax Compliance Act of 2009—United States to Financial Institutions: Cooperate with Anti-Tax Evasion Efforts or Else" (Oct. 2009), www.mofo.com/news/updates/files/16106.html#page=1. Although President Obama and Treasury Secretary Geithner have expressed unqualified support for the bill, it is still presently in committee. Id.

percent of all federal income taxes.[107] Until recently, these individuals were able to park their money in offshore accounts and use debit cards for their transactions.[108] But the long arm of the law has finally got closer to catching these individuals when the UBS settlement occurred. As a result, the IRS has allowed for the VDP, whereby individuals who elected to not disclose their offshore accounts can now make a disclosure without the risk of a criminal lawsuit.[109] Of course, these individuals are subject to civil penalties and the IRS may want an interview with the individual depending on the facts of the case. Certainly, the VDP has seen remarkable results.[110]

Whatever the reason for the VDP, the fear of U.S. Authorities has prompted some of these undisclosed accountholders to elect to voluntarily disclose. Nonetheless, an increase of auditing "high wealth, high risk" individuals will only intensify this fear: "While the IRS audited almost 9.25 percent of all individuals with incomes over 1 million in 2007, only 2.26 percent of those with incomes of between 200,000 and 1 million dollars were audited…leav[ing] a total of 3,942,702 individuals with an income of over 200,000 dollars [unaudited]."[111] So, increases in audits will likely be preventive towards tax evasion, but some of these individuals will be sophisticated enough to hide their assets from auditors. Even so, adding an increase of audits with the trilogy of other preventive measures will help to curb the number of individuals engaged in tax evasion.

In addition, raising the maximum prison sentence for those who engage in tax evasion will not only deter more tax evasion, it will result in further voluntary disclosure. Accordingly, the maximum prison sentence for filing a false tax return is 3 years in prison and a 100,000 dollar fine or both.[112] The maximum prison sentence is 5 years and a 250,000 dollar fine or both for tax evasion.[113] Also, a willful and wanton nondisclosure of a foreign bank account carries a maximum of 10 years imprisonment and a fine of 500,000 dollars or both.[114] Of course, a judge could order a taxpayer who is guilty of all the aforementioned crimes to serve the maximum sentence of 18 years—the 3, 5, and 10 year sentences combined concurrently—but the mandatory prison sentences are too low to serve as a sufficient deterrent.

Surely, Congress and the President have not felt the political pressures after the UBS Settlement as they did when the Bernie Madoff and Enron scandals came to light. If they had, public outcry would require stiffer penalties on those who engage in tax evasion. Indeed, the bankers and the wealthy Americans who are engaged in tax evasion are in a conspiracy to commit fraud. Therefore, Congress should enact a new statute that targets bankers and wealthy individuals conspiring to commit fraud against the American Government.

In particular, Congress should pass a new law that specifically targets financial institutions and wealthy clients who intentionally conspire or attempt to conspire with one another to evade taxes by using an offshore account. The effect of such a law would be devastating for financial institutions, if they choose to break the law. Not only would the banks face hefty criminal sanctions, but they would also face derivative lawsuits on behalf of shareholders. Not even the business judgment rule[115] could protect institutions from engaging in conspiracy.

By creating tougher penalties and standards, financial institutions and wealthy individuals will be less likely to engage in tax fraud. Financial institutions will create internal compliance initiatives to self-regulate and wealthy clients will be less likely to want to place their money offshore because presumably they are smart enough to know "if you can't do the time, then don't do the crime." Again, creating new laws with stiff penalties and increasing audits undertaken will add to further prevention of tax evasion. And by increasing measures aimed at the taxpayer, the likelihood a person would engage in such a crime will diminish significantly.

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[107]Prante, Gerald. Summary of Latest Federal Individual Tax Data (July 30, 2009), www.taxfoundation.org/publications/show/250.html (last visited on Oct. 21, 2009).

[108]*See* VMA.

[109]*See generally* the IRS' Voluntary Disclosure Program, www.irs.gov/newsroom/article/0,,id=210027,00.html (last visited on Oct. 11, 2009).

[110]Originally, only 7,000 people were thought to have disclosed their accounts. Wingfield, Brian, "IRS Sees Success In Anti-Evasion Campaign" (Forbes Nov. 17, 2009), www.forbes.com/2009/11/17/irs-amnesty-offshore-business-washington-tax.html (last visited on Nov. 17, 2009). However, IRS Commissioner Shulman announced that more than 14,700 U.S. taxpayers have participated in the VDP. Id.

[111]Shooting Blanks at 725 (the author calculated his percentages from the INTERNAL REVENUE SERVICE, FISCAL YEAR 2007 IRS ENFORCEMENT AND SERVICE STATISTICS (2007), www.irs.gov/newsroom/article/0,,id=177701,00.html)

[112]26 U.S.C. 7206(1).

[113]26 U.S.C. 7201.

[114]31 U.S.C. 5322(b).

[115]*Navellier v. Sletten*, 262 F.3d 923, 946 (9th Cir. 2001) (holding that the "business judgment rule" requires "[r]ationally believ[ing]…[the] business judgment is in the best interest of the [company].").

V. Conclusion

Even though the problem of tax fraud will continue to happen in the future, progress can be made to prevent future funds from being hidden overseas. The UBS Settlement shows the persistence required before a tax secrecy jurisdiction will go on a fishing expedition. With greater information exchange standards, more transparency, and intimidation of institutions and wealthy individuals, U.S. authorities can sort out what tax liability is owed to the Government.

Until the U.S. Government moves to a national sales tax and does away with income taxes, people will continue to evade taxes. At this point in time, the benefits of having an undisclosed offshore account may continue to outweigh the risk. However, an argument for a nationwide sales tax is beyond the scope of this paper. What we have for now is a problematic system which can only be fixed through cooperation. ❖

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> that the individual alternative minimum tax no longer serves the purposes for which it was intended. The ... structure of the individual alternative minimum tax expands the scope of the provisions to taxpayers who were not intended to be alternative minimum taxpayers. The number of individual taxpayers required to comply with the complexity of the individual alternative minimum tax calculations will continue to grow due to the lack of indexing of the minimum tax exemption amounts and the effect of individual alternative minimum tax on taxpayers claiming nonrefundable personal credits. The alternative minimum tax can be a trap for the unwary, especially for large families, and creates disparate treatment of taxpayers depending on where they live.[181]

[181]Joint Comm. Report 2001, *supra* note 47, at *12-13.

VIII. Conclusion

Middle and upper-middle income families, particularly large families, are adversely affected by the AMT. While its original intentions were equitable, the forty-year-old provisions and their accompanying band-aid patches result in a system that is burdensome, complex, outdated, and unfair. When families seek equitable relief from the AMT through the court system, it is always denied. Based on AMT precedent and the plain meaning rule, courts cannot provide equitable relief to taxpayers who are burdened. Taxpayers only recourse is Congress, who has talked about reform for years, but has been slow to provide comprehensive reform. Instead, Congress has tried to provide the AMT with yearly crutches to make sure the AMT system does not collapse while at the same time reaping the revenues it provides. Congress must act comprehensively in addressing meaningful AMT change that is equitable for all families, large and small, and must do so seasonably. Now is the time for change. ❖

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