Rader v. Commissioner, 143 T. C. 376 (2014)

In Rader v. Commissioner, the U. S. Tax Court upheld the IRS's use of substitutes for returns (SFRs) to assess tax deficiencies against a non-filing taxpayer, Steven Rader, for the years 2003-2006 and 2008. The court rejected Rader's technical challenges to the SFRs and his Fifth Amendment claim, confirming his liability for the deficiencies and related additions to tax. The decision underscores the IRS's authority to prepare SFRs and the stringent requirements for taxpayers to challenge them, emphasizing the consequences of failing to file tax returns and the limited scope of judicial review in such cases.

Parties

Vivian L. Rader and Steven R. Rader, the petitioners, were both Colorado residents at the time the petitions were filed. The respondent was the Commissioner of Internal Revenue. Vivian L. Rader and Steven R. Rader were co-petitioners at the trial court level, but during the trial, it was stipulated that any tax deficiencies and related additions to tax would be attributed solely to Steven R. Rader.

Facts

Steven Rader, a self-employed plumber, did not file federal income tax returns for the years 2003 through 2006 and 2008. The IRS conducted an examination and used the bank deposits method to reconstruct Rader's income for those years, determining that he had substantial earnings from his plumbing business. Additionally, Rader received income from the sale of two parcels of Colorado real property in 2006, from which 10% of the proceeds were withheld due to the buyers' inability to confirm Rader's non-foreign person status under section 1445 of the Internal Revenue Code. Rader failed to provide the required taxpayer identification number or certification of non-foreign status, which would have exempted the sales from the withholding requirement.

Procedural History

The IRS issued notices of deficiency to Vivian L. Rader and Steven R. Rader for the years 2003-2006 on February 11, 2011, and a separate notice to Steven R. Rader for 2008. These notices were based on substitutes for returns (SFRs) prepared by the IRS under section 6020(b). The IRS later amended its answer to change the filing status from "single" to "married filing separate" for the years 2003-2006, which increased the proposed deficiencies and additions to tax. At trial, the parties stipulated that any deficiencies and related additions to tax would be attributed solely to Steven R. Rader.

Issue(s)

1. Whether the IRS's substitutes for returns (SFRs) were valid under section 6020(b) of the Internal Revenue Code.

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2. Whether Steven Rader was liable for the income tax deficiencies as determined by the IRS for the years 2003-2006 and 2008.
3. Whether the tax withheld from the proceeds of the 2006 real property sales could be used to offset Steven Rader's tax deficiency for that year.
4. Whether Steven Rader's Fifth Amendment claim was valid in refusing to testify about his non-filing of returns.
5. Whether Steven Rader was liable for additions to tax under sections 6651(a)(1), 6651(a)(2), and 6654 of the Internal Revenue Code for the years in question.
6. Whether Steven Rader was subject to a penalty under section 6673(a)(1) for maintaining proceedings primarily for delay or based on frivolous arguments.

Rule(s) of Law

1. Under section 6020(b), the IRS may prepare a substitute for return (SFR) if a taxpayer fails to file a required return. The SFR must be subscribed, contain sufficient information to compute the tax liability, and purport to be a return.
2. Section 6211 defines a "deficiency" as the amount by which the tax imposed exceeds the excess of the tax shown on the return plus previous assessments over rebates. The definition excludes credits under sections 31 and 33 from the computation of a deficiency.
3. Section 1445 requires withholding on dispositions of U. S. real property interests by foreign persons, giving rise to a credit under section 33.
4. Section 6651 imposes additions to tax for failure to file or pay taxes, unless the failure is due to reasonable cause and not willful neglect.
5. Section 6654 imposes an addition to tax for underpayment of estimated tax, with no exception for reasonable cause.
6. Section 6673 authorizes the Tax Court to impose a penalty of up to $25,000 if a taxpayer institutes or maintains proceedings primarily for delay or if the taxpayer's position is frivolous or groundless.

Holding

1. The IRS's SFRs were valid under section 6020(b).
2. Steven Rader was liable for the income tax deficiencies as determined by the IRS for the years 2003-2006 and 2008.
3. The tax withheld from the proceeds of the 2006 real property sales could not be used to offset Steven Rader's tax deficiency for that year because it constituted a section 33 credit, which is excluded from the deficiency calculation under section 6211.
4. Steven Rader's Fifth Amendment claim was invalid as there was no evidence of a criminal investigation.
5. Steven Rader was liable for the additions to tax under sections 6651(a)(1), 6651(a)(2), and 6654 for the years in question, but the increase in the section 6651(a)(2) addition to tax based on the amended answer was rejected due to the lack of an amended SFR.
6. Steven Rader was subject to a $10,000 penalty under section 6673(a)(1) for

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maintaining proceedings primarily for delay and based on frivolous arguments.

Reasoning

The court found that the IRS's SFRs met the requirements of section 6020(b), as they were subscribed, contained sufficient information to compute the tax liability, and purported to be returns. The court rejected Rader's argument that the SFRs were invalid due to the lack of a Form 1040 or a statutory citation, citing precedents that upheld the validity of SFRs without these elements. The court also rejected Rader's claim that the tax withheld under section 1445 could offset his 2006 deficiency, reasoning that the withheld tax constituted a section 33 credit, which is excluded from the deficiency calculation under section 6211. Rader's Fifth Amendment claim was dismissed due to the lack of evidence of a criminal investigation and the absence of a well-founded fear of prosecution. The court upheld the additions to tax under sections 6651 and 6654, finding no evidence of reasonable cause or lack of willful neglect. The increase in the section 6651(a)(2) addition to tax was rejected because the amended answer did not include a new SFR. Finally, the court imposed a penalty under section 6673(a)(1) due to Rader's frivolous arguments and apparent intent to delay tax collection.

Disposition

The court entered a decision in favor of Steven Rader in docket No. 11409-11 (2003-2006 tax years) and appropriate decisions in docket Nos. 11476-11 and 27722-11 (2003-2006 and 2008 tax years, respectively), reflecting the court's findings on the tax deficiencies, additions to tax, and the penalty under section 6673(a)(1).

Significance/Impact

Rader v. Commissioner reinforces the IRS's authority to prepare SFRs and the validity of those SFRs in the absence of taxpayer-filed returns. The decision highlights the importance of timely filing and paying taxes, as well as the consequences of failing to do so, including the imposition of additions to tax and potential penalties for frivolous litigation. The case also clarifies the treatment of withheld taxes under section 1445 as credits that do not offset deficiencies, emphasizing the need for taxpayers to provide necessary documentation to avoid such withholding. This decision serves as a reminder to taxpayers of the importance of complying with tax filing and payment obligations and the limited grounds for challenging IRS determinations based on SFRs.

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