

The Lie of the Truth About Business Trusts

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By: In Memoriam - Richard J. Alan Cahan, J.D., LL.M. (1948 - 2018)

I consider myself a very lucky person in that I had the opportunity to spend a considerable time in the company of my grandmothers. As we all know grandmothers tend to be quite intelligent and can be rather philosophical at times. My grandmothers were no exception. One of Rose Cahan's (aka Nana Rose) favorite expressions was, "If something is too good to be true, it usually is..." Anna Lanken's (aka Nana Anna) favorite axiom was, "Watch out for strangers bearing gifts." ¹

Those two expressions came to mind when I was confronted with a sham trust scheme known as the "Truth About Business Trusts" (TABT). TABT is a 49 page document that is marketed in conjunction with slick sales seminars and slicker websites that entice unsuspecting individuals to purchase a program that purportedly eliminates and/or drastically reduces most US taxes including income taxes, deductions for personal expenses, depreciation deductions of an owner's personal residence and furnishings as stepped basis for property transferred to the trust, the reduction or elimination of self employed tax and the reduction or elimination of estate and gift taxes.

The TABT appears to be a legal opinion with citations from various cases and quotations from the US Constitution, the Internal Revenue Code and other authorities upon which the unsuspecting taxpayer can rely. It is neither a legal opinion, nor is it legal. It is rubbish. A careful review of the TABT shows that the citations and quotations provide "black letter" legal references to definitions without a true intergrated overview of the effect of entering into a TABT or related scheme.

For example, recently a client came to me who attended a US \$7,500.00 seminar in Mexico. As a result of that Seminar, that client purchased for an additional US \$28,000.00 an offshore scheme which included among other things a four page preprinted trust with an unknown trust company out of Nassau, Bahamas, an "untraceable offshore debit card" for an account that had no money and a mutual fund investment on a fund operated in Guernsey. He advised me that he no longer had to file US income tax returns as he filed a "tax statement" which effectively put him in "non-filer" status with the Internal Revenue Service" (IRS).

He also advised me that the 16th Amendment to the US Constitution (creating the income tax) was never properly ratified by all of the states. ² Therefore the creation of the income tax and the enforcement of tax laws was illegal. Accordingly, as the US tax laws are illegal and the 16th Amendment is not legally in existence, he does not have to pay his income taxes. According to the client, it is that simple. He no longer reports his income; he does not disclose his offshore

holdings (no Form 3520 or 3520-A filings) and since the debit card cannot be traced, all he has to do is go to an ATM machine and access his income in cash.

For the tax year ending 31 December 1998, this particular client had a tax bill of in excess of US \$200,000. For 1999 he advised me that he paid the IRS zero dollars because the 52 tax statement (which was also included in the materials he purchased) absolves him of any liability to the IRS.

I met with this client for approximately two hours and advised him of the following:

1. On 3 April 1997 the IRS issued IRS Notice 97-24 (Cumulative Bulletin Notice 97-24 IRB 1997-163 April 1997) which set forth the IRS' position on abusive trust arrangements such as that into which this client had entered. I additionally advised him that according to IRS Notice 97-24, the IRS "is undertaking a nationally coordinated effort that the nationally coordinated enforcement initiative to address abusive trust schemes - the National Compliance Strategy, Fiduciary and Special Projects. This initiative involves service personnel from the Assistant Commissioner (examination), Assistant Commissioner (Criminal Investigation), and the Office of Chief Counsel."
2. I also explained to him that, "tax protestors who question the legality of the enactment of the 16th Amendment and the Internal Revenue Code usually retain counsel who specialise in criminal tax matters not offshore estate planning and wealth preservation."
3. I tried to make it abundantly clear to this individual that as my grandmother said, "If something sounds too good to be true, it usually is." I also explained to him that he probably came to visit me because someone had confidence in my abilities and my intelligence. I said to him, "If everyone could go on non-filer status (myself included) no one would be paying taxes and no one would have potential criminal problems with the IRS. It is not that we enjoy paying taxes, we are legally obligated to do so". His response was that, "we as tax attorneys, wealth preservation planners and estate planners have a vested interest in continuing the sham perpetrated upon the people of the United States by forcing people to pay taxes that were not legally imposed. 3
4. At the end of the meeting I gave him the list of three or four top criminal tax lawyers with whom he should consult.
5. I also tried to explain to him and to other clients who have come to me with sham trust arrangements that under any set of circumstances substance, not form, controls taxation. This was clearly set forth in cases such as Gregory v Hellvering, 293 US 465 (1935), XIV-1 CB 193 and Helvering v Clifford, 309 US 331 (1940), 1940-1 CB 105.
6. I also tried to explain the importance of the Grantor Trust Rules and the effect it would have on a sham trust arrangements pursuant to IRC §671-677. Again, these arguments fell on deaf ears as this particular client and other clients who have stepped into the world of sham trusts simply would rather believe the con than believe the law.
7. I explained to this client and to other clients involved in these situations who call themselves "non-filers" that the only non-filers that I know of are: (i) those individuals or entities who for some reason have no obligation to file income tax returns with the IRS (i.e. no income) or (ii) corporation, trusts, partnerships and other entities that have dissolved and filed their final tax returns or (iii) deceased individuals after the filing of their final income tax return and estate tax return if applicable. Otherwise most 'non-filers' and tax protestors end up being guests of the Government on the American Plan (room and three square

meals a day) at such infamous vacation spots as “Club Fed” in Pensacola, Florida or Danbury, Connecticut.

8. I delivered to this client and to other clients copies of recent U.S. Tax Court decisions in the cases of: (i) Leon L. Zachman, et al v Commissioner, TC Memo 1999-392, Docket No. 14059-91, filed 1 December 1999 and (ii) Alan O. Zachman, et al v Commissioner, (companion case). In reviewing these cases, I explained to the client that these taxpayers ultimately were required to pay (in a civil tax proceeding) back taxes, penalties and interest for all years in which they participated in the scam. They also paid significant attorneys’ and accountants’ fees.
9. I explained to the client that in Zachman, the court went to great lengths to describe the ultimate resolution of cases against the promoters of the business trust by inserting the following into its opinion: “On November 16, 1985, the U.S. District Court for the District of Minnesota entered a Final Judgment of permanent Injunction as to James and Joan Noske, finding that they have engaged in conducts subject to penalty under §6700 and enjoying them from organising, assisting, selling or otherwise promoting business trust abusive trust shelters. As part of the Judgment, Noskes were ordered to supply Respondent’s district director with the names and addresses of all purchasers of the 1986 Business Trust on file with the Minnesota Secretary of State which list Armagedden and Parnel. Subsequently the Noskes identified Hillside Farm and Maplewood as being among the Business Trust being involved in the injunction action.

In September, 1995, Joan and James Noske were convicted of among other things, conspiracy to defraud the United States by impeding the Internal Revenue Service and conspiracy to evade Federal Income Taxes. The convictions were based on the Noskes participation in the scheme to assist their clients in reducing or avoiding Federal Income Taxes by forming business trust which named Armagedden and Parnel as Trustees. It was further determined that the Noskes participating in the scheme whereby their clients would transfer all of their income producing property to business trusts and then issue 60% of their trust shares to BBKA, thus effectively evading the assessment and payment of 60% of their client’s Federal Income Tax liability”.

10. I also gave this client copies of the Ninth Circuit Case of U.S. v Estate Preservation Services, et al 202 F. 3d 1093 (9th Cir. 2000) wherein the court enjoined abusive tax shelter promoters from further disseminating information concerning abusive trust arrangements. The Court stated that the promoters are prohibited from advocating shelters that provide no legitimate shelter from local taxation. Every honest and qualified tax consultant knows the difference between legitimate and plainly illegitimate tax shelters. Appellants crossed the line into the “plainly illegitimate” (emphasis supplied). In the Estate Preservation Services case, the IRS, on a routine audit of certain individual taxpayers discovered the abusive trust arrangement. It formally assessed penalties of US\$1.254 million against the taxpayers and the promoters of the scam.
11. I also delivered a copy of IRS Publication 2193 in which the IRS attempts to further admonish taxpayers to be wary of promoters who induce taxpayers to establish trust with the false promise of eliminating taxes. After I completed the first draft of this article, I also gave a copy of the draft to the potential client who, after reading the article and all of the materials herein cited, elected to keep the trust arrangement in place and risk the possibility of losing potentially all of his hard earned wealth if his number comes up in the IRS “audit lottery”.

Clearly, anyone involved in these schemes runs a significant risk of being charged with and convicted of tax crimes. However, the slicksters who sell these dangerous arrangements clothe themselves with purportedly solid legal reasoning behind their actions. Nothing can be further from the truth.

They also have another clever gimmick to help them sell these arrangements. They offer CPAs, financial advisors, attorneys and the like commissions of 35-50% of the fees paid as a commission for finding them a “dupe”. It is interesting to note that if the CPA puts a client into one of these fool hardy schemes, the CPA may also face “preparer” liability when preparing the tax return for the individual or the tax statement for the “non-filer”.

All of these arrangements sound quite exotic to the unsuspecting “pigeon” who is in the sights of the scam promoters. They go to lovely, tranquil locals, the streets of which are lined with banks and trust companies and are told that “no one pays taxes here” which may or may not be true, however, all US taxpayers must pay tax on their income.

The real truth about business trusts is that they are bad news for the clients who invest in them and possibly worse news for a professional who sanctions such actions by a client. So, I lovingly think of both of my grandmothers who knew nothing about the complexities of the Internal Revenue Code but knew a lot about life when they may have said to me, “If something is too good to be true, it usually is”, and, “Watch out for strangers bearing gifts”.

Perhaps, in this situation my Grandmother would have quoted the Meineke Muffler advertisement that says, “Pay me now or pay me a lot more later”, which is exactly what will happen when the abusive trust arrangement is identified by the IRS and the participants will be paying deficiencies, interest, maximum penalties, and significant attorneys’ and accountants’ fees to fix the situation that never should have happened.

Footnotes

1. I did not say that either of my grandmothers were original thinkers, I only said that they were intelligent and at times philosophical.
2. My copy of the Constitution indicates that the 16th Amendment was ratified on 3 February 1913.
3. His words came right from the materials he purchased at the Mexico seminar.