04-0196-cv

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Robert L. Schulz

Plaintiff-Appellant

NDNY Case No.
1:03-CV-1354 (lead)
1:03-MC-0050 (Consol.)
1:03-MC-0071 (Consol.)

-vs-

IRS, United States, Anthony Roundtree

Defendants-Appellees

REPLY BRIEF FOR PRO-SE PLAINTIFF-APPELLANT

DATED: September 2, 2004

ROBERT L. SCHULZ
Pro Se
2458 Ridge Road
Queensbury, NY 12804
518) 656-3578

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PRELIMINARY STATEMENT

Defendants, relying on *Reisman*, argue that district courts lack jurisdiction to hear cases initiated by citizens to quash IRS summonses issued under 26 U.S.C. Section 7602, and that parties summoned must wait to be sued by the IRS in district court before the parties summoned can challenge the legitimacy of the summons. In reply, Plaintiff analyzes *Reisman*, showing that, in fact, the *Reisman* court recognized the legitimacy of both approaches, i.e., the legitimacy of parties summoned to initiate a challenge to IRS summonses in court, and the legitimacy of parties summoned to challenge the IRS summonses before the hearing officer.

Defendants also say, "It is difficult to understand how 'promotion of an abusive tax shelter' could be considered a legitimate 'petition for redress of grievances,' Brief at 16,18, that issue is not before this Court." However, Plaintiff argues that it is difficult to understand how a legitimate 1st Amendment "petition for redress of grievances" could ever be represented as a "promotion of an abusive tax shelter."[1]

I. DISTRICT COURT HAD JURISDICTION

Defendants argue, in effect, that citizens are utterly helpless and unable to challenge illegitimate IRS summonses issued under Section 7602, no matter how groundless and abusive of fundamental Rights the summonses may be, unless and

[1] See Defendants' Brief, fn page 2-3. This is the fundamental, constitutional issue that is inextricably intertwined with the question of judicial jurisdiction and the question of whether plaintiff was at least entitled to a hearing in district court to require defendant IRS to publicly appear and prove its Summonses were not an impermissible ruse to obtain plaintiffs books and records, or an unlawful effort to chill the exercise of their First Amendment rights.

until the United States sues the citizen for contempt (for failing to comply), thereby publicly humiliating the citizen by publicly classifying him as a "Defendant" in a lawsuit that he must vigorously defend against to avoid the consequences – including attachment and arrest.[2] The case to *enforce* a 7602 Summons is thereby brought by the U.S. in the same District Court that closed its doors to the citizen as a Plaintiff.

There is no merit in law or equity to the proposition that district courts are prohibited from entertaining a motion to quash an IRS administrative summons unless and until the IRS and DOJ initiate an "enforcement action" under 7402 or 7604. The service of a Summons is an "enforcement action," and Plaintiff has a due process Right to challenge in district court the arbitrary exercise of the IRS's administrative power by raising a substantial question regarding Plaintiff's constitutional Rights and by holding Defendants accountable to the "legitimate purpose," "minimum standard," and "clearly erroneous" tests set forth by the line of court cases, all under the district court's jurisdiction authorized by 28 U.S.C. 1331, 1346 and 42 U.S.C. 1983.

"Once a summons is challenged it must be scrutinized by a court to determine whether it seeks information relevant to a legitimate investigative purpose and is not meant 'to harass the taxpayer or to put pressure on him to settle a collateral dispute, or for any other purpose reflecting on the good faith of the particular investigation'…The cases show that the federal courts have taken seriously their

[2] "Attachment of a witness who has neither defaulted nor contumaciously refused to comply would raise constitutional considerations, which need not be considered at this time under our reading of the statute." *Reisman*, n8 page 449

obligation to apply this standard to fit particular situations, either by refusing enforcement or narrowing the scope of the summons. *U.S. v. Bisceglia* (1975), 420 U.S. 141 at 146, quoting *United States* v. *Powell* (1964), 379 U.S. 48 at 58.

Reisman v. Caplin, 375 U.S. 440 (1964)

In their reply, defendants assert that, "the magistrate judge properly relied on cases that all cited *Reisman* in holding that the adequacy of the statutorily prescribed remedy at law divested the district court of jurisdiction to grant the requested relief." Defendants have misconstrued *Reisman*.

In fact, in *Reisman*, the Supreme Court held, "The petitioners make no claim that [Section 7602] suffers any constitutional infirmity on its face. This Court has never passed upon the rights of a party summoned to appear before a hearing officer under § 7602. However, the Government concedes that a witness or any interested party may attack the summons before the hearing officer. There are cases among the circuits which hold that both parties summoned and those affected by a disclosure may appear or intervene before the District Court and challenge the summons by asserting their constitutional or other claims. *In re Albert Lindley Lee Memorial Hospital*, 209 F.2d 122 (C. A. 2d Cir.); *Falsone* v. *United States*, 205 F.2d 734 (C. A. 5th Cir.); and *Corbin Deposit Bank* v. *United States*, 244 F.2d 177 (C. A. 6th Cir.). We agree with that view and see no reason why the same rule would not apply before the hearing officer." *Reisman* at 445.

In other words, the *Reisman* Court recognizes both the Right of parties summoned to appear in District Court to challenge the summons, and their Right to attack the summons before the IRS hearing officer.

The *Reisman* Court recognized the Right of summoned parties to appear in District Court to challenge the summons when it said, "There are cases among the circuits which hold that both parties summoned and those affected by a disclosure may appear or intervene before the District Court and challenge the summons by asserting their constitutional or other claims…We agree with that view…."

At the same time, and for the first time, the Supreme Court recognized the legality of attacking the summons before the IRS hearing officer when it said, "We agree with that view and see no reason why the same rule would not apply before the hearing officer." *Reisman* at 445.

What the *Reisman* Court DID say was that for the first time, the court was addressing itself to the question of the constitutionality of Section 7602 and, for the first time, the court was passing upon the rights of a party summoned to appear before a hearing officer under Section 7602.

Contrary to defendants' interpretation, *Reisman* does NOT say, "District courts are now without jurisdiction to decide challenges to IRS Summonses; parties summoned must now challenge their Summonses before an IRS hearing officer and, if they fail to comply with the directive of the hearing officer because

they disagree they must wait for the IRS to initiate an action in district court to enforce the summons before they can mount a challenge to the Summons, and if that ruling goes against them, they can appeal to Court of Appeals and seek a stay of the enforcement of the district court's order pending the appeal." [3]

Having addressed one Summons resolution schema of the Code, and finding that it works "no injustice and suffers no constitutional invalidity," the *Reisman* Court concluded, "we remit the parties to the comprehensive procedure of the Code, which provides full opportunity for judicial review before any coercive sanctions may be imposed. Cf. *United States* v. *Babcock*, 250 U.S. 328, 331 (1919)." *Reisman* at 449.[4]

This was merely the Court's solution for the parties in *Reisman*, not the solution for all parties summoned by the IRS at all times going forward.

Unlike the case at bar, *Reisman* was an action for declaratory relief, raising for the *Reisman* courts the legal question of the Right to declaratory relief in light of the existence of another remedy at law.

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[3] A search of cases in the circuits to quash IRS summonses, since *Reisman*, shows jurisdiction has been maintained throughout the district courts. See for instance; *PAA Management v. U.S.*, 962 F.2d 212 (2nd Cir, 1992); *St. German of Alaska Eastern Orthodox Catholic Church v. U.S.*, 840 F.2d 1087 (2nd Cir., 1988); *Ponsford v. United States*, 771 F.2d 1305 (9th Cir. 1985); *Miller v. United States*, 150 F.3d 770 (7th Cir. 1998).Of course, there are numerous examples of the courts' jurisdiction before *Reisman*, including those cited by the Supreme Court in *Reisman* itself.

[4] At the time of service of the summonses in *Reisman*, there were four civil tax cases pending in the Tax Court contesting alleged deficiencies in income tax returns of the Bromleys. In addition, a criminal investigation of Mr. Bromley on the tax matters was in progress. No such proceedings or investigative predicates were present in the instant case. In other words, the use the summons authority in *Resiman* was a good-faith pursuit of the authorized purposes of Section 7602. Here, the material issue of fact is that the use of the summons authority in not a good-faith pursuit of the authorized purposes of 7602 AND the use of the summons authority fails to meet the requirements of the *Powell* decision, which followed *Reisman* by a few months.

The *Reisman* Court fashioned a reasonable remedy, by remitting THOSE parties to the comprehensive procedure of the code, saying, in effect, that if the IRS now wants to enforce its summonses, the code allows them to bring an enforcement action in district court. The Court was constrained by the points of procedural departure that had already taken place and by all the complexities and extenuating facts and circumstances of the case, including the findings by the District Court and by the Court of Appeals.

The case before the bar suffers from no such complications; it is a simple motion to quash subject to the rigors of *Powell,* albeit with exceptional First Amendment circumstances.

The *Reisman* Court affirmed dismissal concluding, "petitioners have an adequate remedy at law and that the complaint is therefore subject to dismissal for want of equity." *Reisman* at 443

II. THE SUMMONSES ARE IMPERMISSABLE RETALIATION

Congress has carefully restricted the IRS' summons power to certain rather precisely delineated purposes: "ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability." 26 USC § 7602. This language indicates unmistakably that the summons

power is a tool for the genuine investigation of particular taxpayers, and is not to be used to quash a serious and intelligent Petition for Redress of Grievances, or to chill the enthusiasm of People to participate in the Petition for Redress process.

Any attempt by the IRS to use its Summons power to methodically force disclosure of whole categories of transactions, information and communications related to the Petition for Redress participants, and to closely monitor the myriad operations of the Petition for Redress process, on the theory that the information thereby accumulated might expose some kind of "tax shelter" or facilitate the assessment and collection of some kind of a federal tax from somebody, is constitutionally impermissible and can be challenged in district court pursuant to Titles 28 and 42. "Although the summons power provisions of the Internal Revenue Code are to be liberally construed, a court must be careful to insure that its construction will not result in a use of the power beyond that permitted by law." *United States* v. *Humble Oil & Refining Co*., 488 F.2d 953 at 958 (5th Cir. 1974).

"The Congress has recognized that information concerning certain classes of transactions is of peculiar importance to the sound administration of the tax system, but the legislative solution has not been the conferral of a limitless summons power. Instead, various special-purpose statutes have been written to require the reporting or disclosure of particular kinds of transactions, e. *g*., 26 U. S. C. §§ 6049, 6051-6053, 31 U. S. C. §§ 1081-1083, 1101, and 1121-1122, and 31

U. S. C. §§ 1141-1143 (1970 ed., Supp. III). Meanwhile, the scope of the summons power itself has been kept narrow. Congress has never made that power coextensive with the Service's broad and general canvassing duties set out in Section 7601. Instead, the summons power has always been restricted to the particular purposes of individual investigation, delineated in § 7602.

"The canvassing duties and the summons power have always been found in separate and distinct statutory provisions. The spatial proximity of the two contemporary provisions is utterly without legal significance. 26 U. S. C. § 7806 (b). The general mandate to canvass and inquire, now found in § 7601, is derived from § 3172 of the Revised Statutes of 1874. See *Donaldson* v. *United States*, 400 U.S. 517, 523-524. The summons power, however, has different historical roots. Section 7602, enacted in 1954, was meant to consolidate and carry forward several prior statutes, with 'no material change from existing law.' H. R. Rep. No. 1337, 83d Cong., 2d Sess., A436; S. Rep. No. 1622, 83d Cong., 2d Sess., 617. The relevant prior statutes were §§ 3614 and 3615 (a)-(c) of the Internal Revenue Code of 1939. See Table II of the 1954 Code, 68A Stat. 969. Section 3614 granted the summons power to the Commissioner 'for the purpose of ascertaining the correctness of any return or for the purpose of making a return where none has been made.' Sections 3615 (a)-(c) granted the summons power to 'collectors' and provided that a 'summons may be issued' whenever 'any person' refuses to make a

return or makes a false or fraudulent return. Thus, like the present § 7602, these earlier provisions clearly limited use of the summons power to the investigation of particular taxpayers." *U.S. v. Bisceglia*, 420 U.S. 141 at 154-155. (dissenting opinion by MR. JUSTICE STEWART and MR. JUSTICE DOUGLAS).

Plaintiff's books and records are not subject to disclosure through summons merely because they are generally "tax relevant" -- but only when the summoned information is reasonably pertinent to an ongoing investigation of somebody's tax status. The Supreme Court through *Powell* has prohibited a summons that is wholly unconnected with an investigation of somebody's tax status. The summons must be incident to an ongoing, particularized investigation. Here, there was absolutely no investigative predicate prior to the service of the Summons on plaintiff. On their face, the IRS's Summonses are clearly erroneous. They fail to refer to any legal purpose or code section; the only apparent purpose is to obtain information on those people associated with the Petition process.

A major premise of *Powell* was that an extrastatutory "probable cause" requirement was unnecessary in view of the "legitimate purpose" requirements already specified in § 7602, *Powell* at 56-57. By failing to give any consideration to the exceptional circumstances of the case at bar, and by not requiring Defendants to meet their minimal prima facie burden, the District court's dismissal was arbitrary and capricious.

The court abused its process. The Record shows that the summons was issued for an improper purpose, viz. to harass Plaintiff and to put pressure on Plaintiff to settle the collateral dispute related to the government's failure to respond to Plaintiff's Petition of Redress of Grievances. Such conduct reflects poorly on the good faith of any particular investigation. Plaintiff has met his burden of proving Defendant's abuse of the District Court's process.

Plaintiff raised substantial constitutional questions, such that failure to grant the motion to quash was an abusive violation of the court's process. At a minimum, Defendants should have been ordered to appear and be required, by affidavit, to verify that the Summons was part of an investigation being conducted pursuant to a legitimate purpose, that the inquiry was relevant to the purpose, that the information sought is not already within the Commissioner's possession, and that the administrative steps required by the Code have been followed -- in particular, that the Secretary or his delegate, after investigation, had determined the further examination to be necessary and had notified Plaintiff in writing to that effect. See *U.S. v Powell*, 379 U.S. 48, 52-58. Defendants should have been required to show up in court, and demonstrate by affidavit or otherwise that they had met the minimum standard. See also *U.S. v. Stuart,* 489 U.S. 353, 1989

In light of the substantial constitutional questions raised by Plaintiff, the court's order effectively directing Defendants to "recommence" enforcement

proceedings under Section 7402 or 7604, with the pre-hearing sanctions of attachment and arrest peculiar to Section 7604(b), was capricious and unjust.

Under the facts and the law, the District Court should have satisfied itself, via sworn testimony of the Defendant, that the IRS is not acting arbitrarily and capriciously, and that there was a plausible reason for believing fraud is being practiced on the revenue. The District Court is free to act in a judicial capacity, free to disagree with the administrative decision to summon if a substantial question is raised or the minimum standard is not met. The District Court reserves the right to prevent the "arbitrary" exercise of administrative power, by nipping it in the bud. See *United States* v. *Morton Salt Co*., 338 U.S. 632, 654.

The IRS at all times must use the summons authority in good-faith pursuit of the authorized purposes of Sect. 7602. *U.S. v. La Salle N.B.*, 437 U.S. 298 (1978).

Plaintiff has clearly been undertaking to exercise his constitutionally protected freedom under the Petition, Speech, Publish and Assembly clauses and he had no other purpose. Therefore, the subject summonses are <u>impermissible retaliation</u>.

A court may not permit its process to be abused by allowing the IRS to continue on with an illegitimate summons, without a hearing. Where plaintiff has made a substantial preliminary showing of such abuse, he is entitled to an opportunity to substantiate his allegations by way of an evidentiary hearing. See *U.S. v. Millman*, 765 F.2d 27, (2nd Cir., 1985)

I.R.C. § 7602 authorizes the issuance of summonses for the purpose of ascertaining the correctness of any return. The Internal Revenue Service is required to declare a good-faith pursuit of the congressionally authorized purposes of Section 7602. *U.S. v. White*, 853 F.2d 107 (2nd Cir, 1988).

As the long Record before the court clearly shows, Defendants have intentionally evaded being held accountable to the Constitution, and the court, by refusing to respond to Plaintiff's legitimate Petition for Redress of Grievances. Instead, Defendants are attempting to quash Plaintiff's Petition for Redress of Grievances, by purposefully and unlawfully interfering with the constitutionally protected Right of those who choose to associate with it, by characterizing--in bad-faith--the Petition for Redress of Grievances as an "abusive tax shelter", and publicly prosecuting its principal architect, organizer and spokesman for promoting an "abusive tax shelter".

Plaintiff petitioned the District Court for protection from the IRS, which was retaliating against Plaintiff for lawfully and respectfully exercising his fundamental First Amendment Right to Petition the government for Redress of Grievances (together with his Right to Associate freely and to Speak and Publish freely).

Rather than properly respond to the legitimate questions presented in Plaintiff's Petition for Redress, Defendants are attempting to abuse the court's process, and to publicly denigrate Plaintiff by improperly characterizing the

Petition for Redress as an "abusive tax shelter". Adding further injury to Plaintiff, Defendants are demanding, without lawful authority, that Plaintiff turn over to the IRS personal and private records, including the records of all those who have signed the Petitions for Redress, and who have supported the First Amendment Petition process. This is patently and Constitutionally objectionable.

Plaintiff has innocently put Defendants into a position of being required to publicly answer a few questions and openly account for their official behavior and they apparently deeply resent it.[5]

Included with Plaintiff's Motion was an extraordinary affidavit that detailed the long process of Petitioning the government for Redress of Grievances, supported by an abundance of evidentiary material. Plaintiff's Motion was met with repeated injury by Defendants, who made no appearance at all.

Defendants chose not to enter the trial court where they would have faced the record of Plaintiff's Petition for Redress, and would have been forced to reconcile their "6700" letter and Summonses with that record. Defendants chose not to respond to the substantial question of abuse of fundamental Rights. Defendants decided there would be but a one-sided record on appeal. Defendants claim the

[5] For the record, plaintiff objects to defendants' first footnote. Brief at page 2. It is designed to bias the court against plaintiff by having plaintiff appear as a "tax protestor." In fact, plaintiff's Petitions for Redress make no claim that the IRS lacks authority to tax. Plaintiff's Petitions for Redress merely ask the government for answers to specific questions regarding the tax, war, money and debt and "privacy" clauses of the Constitution. Plaintiff has a long history (25 years) of closely scrutinizing government's behavior, comparing that behavior with the requirements of his state and federal constitutions, and bringing before the judiciary instances of unconstitutional behavior by government officials. Schulz has prevailed on many, precedent setting cases initiated by him in State and Federal Courts. A recent inquiry by plaintiff revealed the fact of 140 reported decisions in cases brought by Schulz.

trial court had no jurisdiction under 28 USC sections 1331 and 1346 or 42 USC 1983, and that Defendants did not have to bother appearing to argue jurisdiction or anything else. Defendant's willful disrespect for the court's process, and for Plaintiff's due process Rights, should not be permitted.

Plaintiff humbly requests that this Court compare and examine Plaintiff's Petition for Redress, which began in 1999 (see for instance Civil Docket For Case #1:03-mc-00050, entry #2 and 5-15), with the language of the IRS's so-called "6700" letter, which is the basis of IRS's demand for Plaintiff's personal and private records, and which resulted in the filing of this complaint.[6]

There is not a scintilla of evidence, in or out of court, to support the notion that Plaintiff is, or ever has been, involved with any type of "tax shelter", much less an abusive one, or that Plaintiff has ever been involved with any so-called "investors." On the other hand, there is an abundance of evidence to support Plaintiff's claim that the IRS's motive behind its "6700" letter is simply to shut down the Petition for Redress process and to chill the enthusiasm of the People to associate with it.

[6] The "6700" letter from the IRS reads, "We have reviewed certain materials with respect to your tax shelter promotion. We are considering possible action under 6700 and 7408 of the Internal Revenue Code relating to penalties and an injunction action for promoting abusive tax shelters. In addition, we plan to consider issuing "pre-filing notification" letters to the investors who have invested in this promotion. You are requested to meet with the examiner at the above date, time and location. Enclosed is a list of documents, books and records that you should have available and questions you should be prepared to reply to at that time…. " See A-152.

The IRS had an opportunity in District Court to argue otherwise. They intentionally failed to do so.[7] Instead, the IRS now appears in the Court of Appeals to argue for this court's affirmation of the district court's dismissal, for the sole purpose of allowing the IRS to recommence the action in district court to force Plaintiff to comply with the very Summonses the IRS chose not to defend in the instant case. This is wrong.

IRS's summonses are clearly not relevant to Plaintiff's tax liability, but were intended to compromise Plaintiff's role as the architect and organizer of the Right to Petition process. Although its investigative powers are broad, IRS has no lawful authority to examine any personal and private records unless they are relevant to the tax liability of the person(s) under investigation. The IRS certainly has no legal or moral authority to deploy the vast resources of the United States against individual citizens who are clearly exercising and seeking the protections guaranteed them by the First Amendment to the United States Constitution.

CONCLUSION

For the foregoing reasons, the Court should reverse and remand.

ROBERT L. SCHULZ, pro se
2458 Ridge Road
Queensbury, NY 12804

[7] Plaintiff has searched, unsuccessfully, for another example of a case where the IRS and the government failed to appear – failed to respond—to a motion in a District Court to quash an IRS summons. Plaintiff could find no other example of such behavior on the part of the government.