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Federal Taxation

by Steven C. Evans*

The federal tax cases decided by the Eleventh Circuit during 1991 reversed one trend and continued another trend of 1990. The Eleventh Circuit decided a number of procedural tax cases during 1991.¹ This trend is similar to the number of procedural cases decided in years prior to 1990, but is substantially more than the number of procedural cases decided by the Eleventh Circuit in 1990.² Cases decided under the Employment Retirement Income Security Act of 1974 ("ERISA"),³ as amended, continued to constitute the majority of the substantive tax cases decided by the Eleventh Circuit during 1991.⁴

I. INDIVIDUAL INCOME TAX ISSUES

A. At Risk Rules

The case of Young v. Commissioner⁵ is important for practitioners who have been involved in sale/leaseback arrangements. Taxpayers in Young purchased equipment from a company named Elmco, Inc. or its wholly-owned subsidiary CTC (collectively referred to as "Elmco"). The purchase price was paid by taxpayers in the form of a partial cash payment, a recourse note, and an installment note that was characterized as partially recourse and partially nonrecourse. Elmco had acquired com-

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² See infra text accompanying notes 54-124.


⁵ 926 F.2d 1083 (11th Cir. 1991).
puter equipment from third-party lessors, who had leased the equipment to end-users. The third-party lessors acquired the equipment with a loan from a bank, and the bank had a first lien on the equipment. Elmco acquired the equipment subject to the end-user leases and the bank lien. Elmco, in turn, assigned its rights under the lease, including the receipt of rent, to taxpayers. In the documentation of the transaction, Elmco agreed to indemnify the taxpayers for any breach of its representations or obligations in the agreement. In addition, third-party lessors guaranteed the rent obligations of the end-users. Interestingly, and probably by design, the nonrecourse note payments due to the third-party lessors from Elmco equaled exactly the partial recourse note payments due from taxpayers to Elmco. Furthermore, the rental payments due from the third-party lessors to Elmco (and in turn to taxpayers) always equaled or exceeded the payments due from Elmco to the third-party lessors under the nonrecourse note.6

As the result of these transactions, rent was paid by the third-party lessors to Elmco and by Elmco to taxpayers, while taxpayers made note payments to Elmco, who in turn made note payments to the third-party lessors. Actually, rent payments were never made to anyone unless the rent due under the leases exceeded the amount of the nonrecourse note payments due to the third-party lessors from Elmco under its nonrecourse note. Instead, bookkeeping entries to reflect these transactions were made. Periodically, any excess of the rent payments less the note payments was paid by the third-party lessors to Elmco and then, in turn, by Elmco to taxpayers.7

The Internal Revenue Service (“IRS”) sought a deficiency with respect to losses claimed by taxpayers with respect to these transactions. At trial the Tax Court concluded that those losses were not allowed as deductions and, instead, limited the losses to the amount “at risk” within the meaning of the Internal Revenue Code (“Code”) section 465.8

On appeal taxpayers first objected to the Tax Court permitting the IRS to amend its answer to set forth the “at risk” theory a few days prior to the commencement of the trial.9 The Eleventh Circuit noted that Rule 41(a) of the Rules of Practice and Procedure of the United States Tax Court10 allowed the court to amend freely when justice so required.11 The Eleventh Circuit concluded that the Tax Court did not abuse its discre-

6. Id. at 1086.
7. Id.
9. 926 F.2d at 1086-87.
11. 926 F.2d at 1087.
tion by allowing the amendments to the answers because the amendments
had been proposed over thirty days prior to the trial date.\textsuperscript{12}

The Eleventh Circuit then analyzed whether taxpayers were "at risk"
as required by Code section 465 with respect to the long-term installment
notes. The Eleventh Circuit reviewed the analysis of the Tax Court which
determined that if the third-party lessor defaulted on the rental pay-
ments, the third-party lessor was merely paying rent to itself and Elmco
would not be motivated to attempt to collect the notes from the taxpay-
ers because Elmco's notes to the third-party lessor were nonrecourse.\textsuperscript{13}

Taxpayers argued that neither the guarantee by the third-party lessor nor
the indemnification clause in the purchase agreement limited their losses
under the arrangement. However, the Eleventh Circuit viewed the trans-
actions in accordance with economic reality and determined that the tax-
payers were not at risk in the circular arrangement.\textsuperscript{14} The Eleventh Cir-
cuit noted that the Tax Court's factual findings were to be given
substantial weight on appeal.\textsuperscript{15} The Eleventh Circuit observed that the
Tax Court had focused on the result of the transactions through which
taxpayers had assumed Elmco's nonrecourse liability to the third-party
lessors.\textsuperscript{16} In addition, the indemnification clause and the guarantee of the
rent obligation together with the assumption of nonrecourse note pre-
vented any actual circumstance from arising under which a demand for
payment would be made.\textsuperscript{17} The Young case should be carefully studied by
tax practitioners who are involved in providing advice for sales/leaseback
transactions. The Young case shows that guarantees and indemnification
clauses can be used as substantial evidence of arrangements that serve to
limit liability for losses and, consequently, could be used to deny deduc-
tions under Code section 465.

\textbf{B. Profit Motive and Tax Exemptions}

Taxpayer in \textit{Kartrude v. Commissioner}\textsuperscript{18} had been assessed deficiencies
by the IRS for the 1980 and 1982 tax years. Taxpayer and his wife had
purchased Sport Aircraft, Inc. ("Sport"), a Subchapter S corporation that
held title to a stunt plane. Taxpayer operated the stunt plane in air shows
and instructed students in aerobatics beginning in 1978. In late 1979 or
early 1980, taxpayer's flying partner went to Jordan to train its aerobatics
team. By his own admission, taxpayer "let his business go" and Sport's

\begin{itemize}
  \item \textsuperscript{12.} \textit{Id.}
  \item \textsuperscript{13.} \textit{Id. at 1087-88.}
  \item \textsuperscript{14.} \textit{Id. at 1088.}
  \item \textsuperscript{15.} \textit{Id.}
  \item \textsuperscript{16.} \textit{Id. at 1088-89.}
  \item \textsuperscript{17.} \textit{Id. at 1089.}
  \item \textsuperscript{18.} 925 F.2d 1379 (11th Cir. 1991).
\end{itemize}
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revenues were drastically reduced after the departure of his partner. Taxpayer began working at an aviation center on a full-time basis in 1980. In 1982 Pan Am rehired taxpayer on a full time basis as a ground school instructor. The plane remained in a hanger during this time, and taxpayer's business continued to fall apart. Taxpayer failed to file tax returns for the 1978, 1980, and 1982 tax years. The Commissioner of the Internal Revenue Service ("Commissioner") issued notices of deficiencies to taxpayer and imposed penalties.

Taxpayer filed a petition for a redetermination of his deficiency. Taxpayer represented himself pro se at the Tax Court trial. Numerous issues were presented at trial, although the Tax Court ruled against taxpayer on all but one issue—whether taxpayer had a profit motive during 1978 in order to deduct his share of the losses from the operation of Sport under Code section 183. Taxpayer appealed the decision of the Tax Court.

On appeal taxpayer objected to all of the findings of the Tax Court. Although space prohibits discussion of all of the issues raised on appeal, two of the issues are substantive. First, taxpayer contended that his operation of Sport was engaged in for profit. The Eleventh Circuit noted that its review was limited to whether the Tax Court's decision was clearly erroneous. Pointing out that Code section 183(a) disallows deductions of losses from activities that are not engaged in for profit, the Eleventh Circuit then reviewed the nine factors used to determine whether an activity is engaged in for profit. In applying these nine factors to this case, the Eleventh Circuit concluded that the Tax Court was correct in its determination that taxpayer did not have the requisite profit motive for his stunt flying operation in 1980 or 1982. The Eleventh Circuit noted that taxpayer admitted he had "let the business go" in late 1979 and early 1980 and that he knew that if he didn't devote full-time efforts to the business, he could not make a profit. The Eleventh Circuit also noted that taxpayer was employed by others on a full-time basis during this time and that taxpayer had spent a sizeable amount on advertising and upkeep of the plane in 1978, but little or nothing on these items in 1980 or 1982. Finally, the Eleventh Circuit noted that taxpayer had admitted that his original reason for purchasing the plane was recreational.

19. Id. at 1381.
21. 925 F.2d at 1381-82.
22. Id. at 1383 (citing Burger v. Commissioner, 809 F.2d 355, 358 (7th Cir. 1987)).
24. 925 F.2d at 1383 (citing Treas. Reg. § 1.183-2(b) (1972)).
25. Id.
26. Id.
27. Id.
28. Id.
result, the Eleventh Circuit affirmed the decision of the Tax Court on this issue.29

The Eleventh Circuit also reviewed taxpayer's contention that the Tax Court erred in denying his entitlement to personal exemptions for his wife and two children in computing his tax deficiency for the years in question.30 Taxpayer noted that his stipulation of facts with the Commissioner which stated that he was married and had two children misled him into believing that the issue of exemptions had been settled. The Eleventh Circuit concluded that the Tax Court erred in failing to examine whether taxpayer was entitled to any additional personal exemptions.31 The Eleventh Circuit noted that a taxpayer's entitlement to exemptions under Code section 15232 is a legal issue and cannot be determined by a stipulation of fact.33 Furthermore, the Eleventh Circuit pointed out that taxpayer was proceeding pro se and could have been misled by the stipulation.34 The Eleventh Circuit remanded this issue to the Tax Court to determine whether taxpayer was entitled to additional exemptions.35

II. Partnership Tax

A. Sham Transaction and Economic Substance

Taxpayers in Karr v. Commissioner36 were limited partners in Peat Oil and Gas Associates, Ltd. ("POGA"), a limited partnership. POGA was allegedly formed to exploit a new energy process called the "Koppelman Process" and to acquire and develop oil and gas interests. The Koppelman Process is a process by which wood, peat, lignite, and other low grade biomass or fossil fuel is placed into a reactor, dried and carbonized at high temperatures, and developed into a dry, stable, high heating value solid fuel that physically resembles coal. Richard Basile was the promoter of POGA and another limited partnership. Basile was also a partial owner of other corporations that were formed to exploit the Koppelman Process.37

The offering memorandum for POGA described POGA's general partner as a certified public accountant and financial consultant who did not have any technical background relevant to the partnership's proposed ac-
tivities. The memorandum estimated tax losses during the initial four years of the partnership to average 401 percent of each investor's investment. As a result, each investor purchasing one partnership unit for $37,500 could deduct $150,376 in tax losses over four years. The offering memorandum also clearly warned that the financial success of the partnership was highly unlikely. The reasons for this included: (1) commercially unproven technology; (2) lack of experience; (3) conflict of interest; (4) large obligations incurred without arms-length negotiations; (5) environmental and health problems; (6) severe competition; and (7) inadequate capital (after payments to the promoters and their associates).

POGA and another limited partnership entered into several contracts with the companies partially owned by Basile. Under these contracts, POGA paid license fees that were based on the number of partnership units sold. POGA also agreed to pay service fees based on the number of partnership units sold. Taxpayers deducted amounts on their 1981 and 1982 tax return as their distributive share of POGA's partnership losses. The Commissioner disallowed these deductions on the grounds that the activity in which POGA was engaged in was not entered into for profit. Taxpayers petitioned the Tax Court to redetermine their tax deficiencies as set forth in the Commissioner's notice of deficiency. After trial the Commissioner conceded that taxpayers could deduct their distributive shares of partnership losses attributable to oil and gas investments. However, the Tax Court concluded that tax motivations shaped the limited partnership and that POGA's activity lacked economic substance apart from the anticipated tax benefits. The Tax Court also sustained the Commissioner's assessment of penalty and interest. Taxpayers appealed.

On appeal the Eleventh Circuit noted that "[a] sham transaction is one which, though it may be proper in form, lacks economic substance beyond the creation of tax benefits." Taxpayers contended that the Tax Court erred in determining that POGA's activities lacked economic substance because the Tax Court had applied the "generic tax shelter" test to determine whether the transaction lacked economic substance. However, the Eleventh Circuit observed that the Tax Court did not merely characterize

38. Id.
39. Id. at 1021.
41. Id.
42. Id. at 1022-23 (citing Knetsch v. United States, 364 U.S. 361, 365-66 (1960); Kirchman v. Commissioner, 862 F.2d 1486, 1491 (11th Cir. 1989)).
43. Id. at 1023.
the transaction as a generic tax shelter. Instead, the Eleventh Circuit stated that the Tax Court considered several characteristics of generic tax shelters to aid in identifying transactions that lacked economic substance. Taxpayers also argued that the Tax Court's conclusions were "erroneous because the Tax Court never determined that no reasonable possibility of profit existed." Taxpayers argued that POGA had a reasonable prospect of profit in the range of twenty-five to forty percent at the time of the partnership's inception. At trial, taxpayers relied on the testimony of an expert witness who had assumed that the Koppelman Process would be commercially successful and did not consider the various risk factors discussed in POGA's offering memorandum.

Noting that the record contained substantial evidence indicating that POGA's activity lacked economic substance, the Eleventh Circuit stated that the offering memorandum emphasized the tax benefits of the partnership. Moreover, the Eleventh Circuit noted that the purchasers of partnership units did not negotiate for the price of their shares, that POGA had no tangible assets, and that the fees paid were based upon the number of partnership units sold and not the result of arms-length negotiations. The Eleventh Circuit also stated that the structure of these fees could have caused POGA to pay fifty-six to one hundred and twelve times the price paid by the corporations owned by Basile, even though the partnership did not receive as many rights as these corporations.

The Eleventh Circuit also noted that the bulk of POGA's payments consisted of promissory notes that were significantly more than the amount of the liability due to Basile's companies. Finally, the Eleventh Circuit reviewed the testimony of the partnership's attorney, who had stated at trial that many of the transactions had been structured in order to accomplish desired tax results. As a result, the Eleventh Circuit affirmed the decision of the Tax Court including the assessments of penalties and interest.

44. Id.
45. Id. (citing Rose v. Commissioner, 88 T.C. 386, 412 (1987), aff'd, 868 F.2d 851 (6th Cir. 1989)).
46. Id.
47. Id. at 1024.
48. Id.
49. Id.
50. Id.
51. Id.
52. Id. at 1024-25. Query: whether the testimony of the attorney was subject to the attorney-client privilege?
53. Id. at 1026.
III. PROCEDURAL TAX CASES

A. Responsible Person Status

Taxpayer in *Williams v. United States*\(^5^4\) was the president, chief operating officer, and fifty percent stockholder of American Intermedical Resources, Inc. ("AIR"), a corporation providing respiratory and cardiology services to hospitals and clinics. The other fifty percent stockholder, Williams, was secretary, treasurer, and chairman of the board of AIR. Williams established a banking relationship with Central Bank of the South (the "Bank") after the inception of AIR. In 1982 and 1983, AIR came into some financial difficulty. The Bank closely monitored AIR's debts and checking account during this time. The federal employment taxes that were withheld from AIR employees in the third quarter of 1983 were due to be paid in October 1983. Normally, AIR submitted these tax payments directly to the Bank for deposit into an IRS account. However, on several occasions the Bank would not accept these deposits because AIR's account did not contain sufficient funds. On these occasions, taxpayer mailed the payments directly to the IRS. Because the Bank was "sweeping" AIR's checking account (or applying all of the proceeds of AIR's checking account to offset outstanding loans), several checks made payable to the IRS were returned for insufficient funds. In February 1984, AIR's indebtedness to the Bank was discharged. Taxpayer subsequently opened an account with another bank, and Williams resigned from AIR assigning his stock in the company to taxpayer. From March 1984 to November 1984, taxpayer made payments to the IRS in an attempt to reduce the amount of past due withholding taxes. In November 1984, AIR ceased to conduct business.\(^5^5\)

The IRS assessed a one hundred percent penalty for failure to remit withholding taxes against taxpayer for the first quarter of 1983, the first quarter of 1984, and the third quarter of 1984. Taxpayer filed a suit in district court seeking a refund of the partial payment he had made of this penalty.\(^5^6\) At trial, the jury concluded that taxpayer was a responsible person under Code section 6672,\(^5^7\) but concluded that taxpayer was not acting willfully when he failed to turn over withholding taxes during the third quarter of 1983 and the third quarter of 1984.\(^5^8\) The jury also determined that taxpayer was not a responsible person during the first quarter.

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54. 931 F.2d 805 (11th Cir.), modified, 939 F.2d 915 (11th Cir. 1991).
55. 931 F.2d at 807-08.
56. *Id.* at 808.
58. 931 F.2d at 809.
of 1984. The government made a motion for a judgment notwithstanding the verdict, which was denied by the district court.\textsuperscript{59}

On appeal the Eleventh Circuit noted that it must consider all of the evidence in the light most favorable to the party opposed to the motion in reviewing a district court’s denial of a motion for judgment notwithstanding the verdict.\textsuperscript{60} The Eleventh Circuit also noted that the courts have interpreted broadly who constitutes a “responsible person” under Code section 6672.\textsuperscript{61} The Eleventh Circuit observed that taxpayer had been the president and chief operating officer of AIR, that he had signed checks on behalf of AIR, that he had owned fifty percent of the stock of AIR and later all of the stock of AIR, and that he controlled and supervised AIR’s daily operations.\textsuperscript{62} As a result, the Eleventh Circuit concluded that taxpayer was a responsible person within the meaning of Code section 6672 as a matter of law.\textsuperscript{63}

The Eleventh Circuit then noted that it had held previously “that the willfulness requirement of section 6672 is satisfied if a responsible person has knowledge of payments to other creditors after becoming aware of the failure to remit withholding taxes.”\textsuperscript{64} The Eleventh Circuit observed that taxpayer had signed AIR’s payroll checks in the first and third quarters of 1984 even though he was aware that the withholding taxes had not been paid.\textsuperscript{65} During the first quarter of 1984, the Eleventh Circuit noted that taxpayer had testified that the withholding taxes had not been paid because AIR’s bank account had been garnished by a creditor.\textsuperscript{66} The Eleventh Circuit stated that a responsible person’s expectation that funds would be available at the end of the quarter does not make a failure to remit withholding taxes any less willful.\textsuperscript{67} Consequently, the Eleventh Circuit held that a taxpayer’s failure to remit withholding taxes during the first quarter of 1984 was willful as a matter of law.\textsuperscript{68} As a result, the Eleventh Circuit reversed the district court and granted the motion for a judgment notwithstanding the verdict in favor of the United States.\textsuperscript{69}

\textsuperscript{59} Id.
\textsuperscript{60} Id. (citing Smith v. United States, 894 F.2d 1549, 1552 (11th Cir. 1990); Thibodeau v. United States, 828 F.2d 1499, 1503 (11th Cir. 1987)).
\textsuperscript{61} Id. at 810 (citing Smith, 894 F.2d at 1553; Slodov v. United States, 436 U.S. 238, 246-50 (1978); Liddon v. United States, 448 F.2d 509 (5th Cir. 1971), \textit{cert. denied}, 406 U.S. 918 (1972)).
\textsuperscript{62} Id.
\textsuperscript{63} Id.
\textsuperscript{64} Id. (citing Smith, 894 F.2d at 1553; Thibodeau, 828 F.2d at 1505).
\textsuperscript{65} Id.
\textsuperscript{66} Id.
\textsuperscript{67} Id. at 810-11 (citing Thibodeau, 828 F.2d at 1506).
\textsuperscript{68} Id. at 811.
\textsuperscript{69} Id.
In a supplemental opinion, the Eleventh Circuit also noted that a responsible person can be held liable for a penalty equal to the amount of the withholding tax liability, but not for interest and penalties the taxpayer or corporation incurred for the failure to remit withholding taxes. As a result, the Eleventh Circuit concluded that neither taxpayer nor Williams could be held liable for penalties and interest incurred by AIR.

Taxpayer in *McDonald v. United States* was president and one-third owner of Environmental Protection System ("EPS"), a Tennessee corporation formed to remove asbestos. Taxpayer had negotiated and executed a financing contract with First Alabama Bank of Athens, Alabama ("First Alabama"). Under the financing arrangement, First Alabama provided EPS with a line of credit in exchange for security interest in all of EPS's accounts receivable, contract rights, inventory, and chattel paper. First Alabama also required that any future payments from the State of Alabama, EPS's primary customer, be made payable jointly to First Alabama.

EPS had two accounts at First Alabama, one for general operating expenses and another for payroll. When EPS requested a draw from its line of credit, First Alabama deposited money into EPS's general operating account. For payroll distributions, EPS issued two separate checks from its general operating account. One check was issued to the payroll account, and another check was issued to the IRS's payroll account at First Alabama.

In 1984 First Alabama expressed concern that EPS was overextended. As a result, First Alabama notified taxpayer that it would only loan EPS enough money to cover its "net" payroll and that the company would have to fund any additional amounts necessary to cover withholding taxes. As a practical matter, however, EPS had no source of credit because First Alabama had a security interest in all of the company's assets and income. EPS continued in business until late 1984. Because EPS had failed to pay its federal employment taxes, the IRS assessed a penalty against taxpayer under Code section 6672. Taxpayer paid a portion of this penalty and filed an action in federal district court.

At trial all of these facts were brought out. However, taxpayer asserted that First Alabama was responsible for the payroll tax default because First Alabama controlled EPS's funds and advanced only enough money

71. *Id.* at 916.
72. 939 F.2d 916 (11th Cir. 1991).
73. *Id.* at 917.
74. *Id.*
76. 939 F.2d at 918.
to pay net wages. At the close of evidence, the United States moved for a directed verdict. The district court denied this motion. The jury found that although McDonald was a responsible person, he had not acted willfully. The district court entered judgment in favor of taxpayer. After the district court denied the United States' motion for a directed verdict, the United States appealed.77

The Eleventh Circuit noted that the sole issue on appeal was whether taxpayer's failure to remit federal income taxes was willful within the meaning of Code section 6672.78 The Eleventh Circuit also noted that taxpayer's sole argument was that his nonpayment of payroll taxes was not willful because First Alabama had complete control over the funds of EPS.79 Citing Williams v. United States,80 the Eleventh Circuit observed that similar arguments had been presented in that case.81 Consequently, the Eleventh Circuit reversed the judgment of the district court and granted the judgment notwithstanding the verdict in favor of the United States.82

B. Abatement of Interest

Taxpayer in Horton Homes v. United States83 signed an agreement with the IRS to pay certain tax deficiencies plus interest. Prior to executing the agreement, taxpayer had asked the IRS to abate the interest on the basis that the IRS had been responsible for delays that prevented the agreement from having been finalized earlier.84 Although the IRS has the authority under Code section 6404(e)(1)85 to abate the interest, the IRS orally advised counsel for taxpayer that "office politics" prevented the IRS from admitting that it had behaved unreasonably. According to the taxpayer, the IRS had commenced the audits beginning in April 1980. Due to various suspensions, the audits had been placed on hold in 1981, 1982, 1983, and 1984. Further delays prohibited the agreement from being signed until 1987.86

77. Id. at 918-19.
78. Id.
79. Id.
80. 931 F.2d 805 (11th Cir.), modified, 939 F.2d 915 (11th Cir. 1991).
81. 939 F.2d at 919.
82. Id. at 919-20.
83. 936 F.2d 548 (11th Cir. 1991).
84. Id. at 549-50.
86. 936 F.2d at 553.
Taxpayers filed a suit in district court for a tax refund. The district court held that it lacked the authority to review the determination of the IRS not to abate interest.\textsuperscript{7} Taxpayers appealed.\textsuperscript{8}

On appeal, the Eleventh Circuit noted that the district court had subject matter jurisdiction over a refund of interest.\textsuperscript{8} The Eleventh Circuit also noted that, under section 701 of the Administrative Procedure Act ("APA"),\textsuperscript{8} a district court normally has the authority to review the action of an agency except when statutes preclude judicial review or when discretion is granted to an agency by law.\textsuperscript{9} In this case, the Eleventh Circuit observed that the legislative history of Code section 6404(e)(1)\textsuperscript{9} gave the IRS the authority to abate interest but did not mandate that it do so.\textsuperscript{8} The only exception to this case is for interest abatements with respect to erroneous refund checks issued by the IRS. The Eleventh Circuit also observed that Treasury Regulation section 301.6404-2T\textsuperscript{8} provided that the Commissioner may abate interest attributable in whole or in part to any error or delay by the IRS in performing an administrational act.\textsuperscript{8} Although the Eleventh Circuit noted that the acts alleged by taxpayer probably did not constitute administrational acts as defined in the regulation, the Eleventh Circuit stated that the discretion granted by Code section 6404(e)(1) appeared to bring into play both exceptions of the APA.\textsuperscript{8} The Eleventh Circuit concluded that the district court did not have the right to review the failure of the IRS to abate interest pursuant to Code section 6404(e)(1) and affirmed the judgment of the district court.\textsuperscript{7}

C. Federal Tax Liens

Taxpayer in \textit{Stoecklin v. United States}\textsuperscript{88} received notices of tax liens on certain real and personal property he owned. These notices were based on tax deficiencies for the years 1978 to 1983 that had been affirmed pre-

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\textsuperscript{7} Id. at 550 (citing Horton Homes v. United States, 727 F. Supp. 1450 (M.D. Ga. 1990)).

\textsuperscript{8} Id.

\textsuperscript{9} Id. (citing Trustees of Bulkeley School v. United States, 628 F. Supp. 802, 803 (D. Conn. 1986); Perkins v. Commissioner, 92 T.C. 749, 752-53 (1989)).


\textsuperscript{11} Id.

\textsuperscript{12} I.R.C. § 6404(e)(1) (1988).

\textsuperscript{13} 936 F.2d at 551 (citing H.R. Rep. 3838, 99th Cong., 1st Sess. 844, 845 (1985)).

\textsuperscript{14} Treas. Reg. § 301.6404-2T (1987).

\textsuperscript{15} 936 F.2d at 552.

\textsuperscript{16} Id. at 553.

\textsuperscript{17} Id. at 554.

\textsuperscript{18} 943 F.2d 42 (11th Cir. 1991).
Taxpayer filed suit in district court to quiet title to the property against which the government had assessed these notices of levy. The district court granted a motion to dismiss for lack of subject matter jurisdiction by the United States. Taxpayer appealed.

On appeal the Eleventh Circuit noted that the United States is immune from suit unless it consents to be sued. The Eleventh Circuit also noted, however, that under 28 U.S.C. § 2410, the United States may be named as a party in a civil suit in any district court to quiet title to real or personal property on which the United States has or claims a mortgage lien. Although a taxpayer cannot challenge the merits of the underlying assessment, the Eleventh Circuit observed that other jurisdictions have permitted taxpayers to challenge the procedural validity of a federal tax lien. Consequently, the Eleventh Circuit vacated the district court's dismissal of taxpayer's complaint and concluded that the district court had subject matter jurisdiction.

D. Fifth Amendment Privilege

Taxpayer in United States v. Argomaniz received an administrative summons to appear before an IRS officer. Although taxpayer appeared before the officer, he refused to produce any of the documents that were summoned. Taxpayer claimed that production of the documents would violate his Fifth Amendment privilege against self-incrimination. Taxpayer continued to assert his Fifth Amendment privilege before a district court judge and before a magistrate after the matter was pursued by the United States. The district court ordered taxpayer to produce the documents or to show cause why he should not be held in contempt. Taxpayer appealed this order and filed a motion to stay the enforcement of the order.

On appeal, the Eleventh Circuit noted that the Fifth Amendment privilege protects against self-incrimination from a person’s own compelled testimonial communication. The Eleventh Circuit also noted that it
"can be raised in any proceeding, civil or criminal, administrative or judicial, investigatory or adjudicatory." The Eleventh Circuit also observed that a taxpayer seeking protection of the Fifth Amendment privilege "must provide more than a mere speculative, generalized allegations of possible tax-related prosecution.'" The Eleventh Circuit stated that the taxpayer must be faced with substantial and real hazards of self-incrimination.

Although the United States argued that taxpayer’s fear of self-incrimination was remote and speculative, the Eleventh Circuit noted that the facts of this case compelled the conclusion that taxpayer, even while the IRS investigation was in a civil stage prior to transfer to the criminal division, had a legitimate fear of criminal prosecution. The Eleventh Circuit observed that if taxpayer produced the documents requested, the IRS system would be able to determine the civil tax liability and that criminal prosecution could result. As a result, the Eleventh Circuit concluded that taxpayer’s apprehension of criminal prosecution was clearly reasonable.

The Eleventh Circuit recognized, however, that the district court must make a particularized inquiry to determine whether the assertion of the privilege by taxpayer is well-founded. Specifically, the Eleventh Circuit stated that the district court must review taxpayer’s assertion on a question-by-question basis in an in camera proceeding. In other words, the Eleventh Circuit stated that the district court must first ascertain whether the taxpayer has the records sought and second, whether the records are incriminatory under the existing circumstances.

The government also argued that taxpayer must comply with the summons because the Fifth Amendment privilege had not been raised properly. The government claimed that the Fifth Amendment privilege is not applicable because the contents of business records are not privileged and because the blanket claim of self-incrimination is impermissible. The Eleventh Circuit dismissed both of these arguments. The Eleventh Circuit noted that, while the documents are not subject to the privilege, taxpayer was objecting to the act of producing the documents, not as to the

109. Id. at 1352-53 (quoting Kastigar v. United States, 406 U.S. 441, 444-45 (1972)).
110. Id. at 1353 (quoting United States v. Reis, 765 F.2d 1094, 1096 (11th Cir. 1985)).
111. Id.
112. Id.
113. Id. at 1354.
114. Id.
115. Id. at 1355.
116. Id.
117. Id.
118. Id.
119. Id. at 1355-56.
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contents of the documents.\textsuperscript{120} The Eleventh Circuit stated that taxpayer would be establishing the existence and authentication of the documents by producing them.\textsuperscript{121} The Eleventh Circuit stated that this act of production would be sufficiently testimonial to activate taxpayer's Fifth Amendment privilege.\textsuperscript{122} Because the IRS officer had terminated the interview after realizing that taxpayer would raise the privilege in response to each of her document requests, the Eleventh Circuit concluded that a blanket invocation of the privilege did not occur.\textsuperscript{123} As a result, the Eleventh Circuit remanded the matter to the district court to determine, through an \textit{in camera} inspection, existence of the Fifth Amendment privilege.\textsuperscript{124}

IV. ERISA

The Eleventh Circuit decided a number of cases arising under the Employment Retirement Income Security Act of 1974, as amended ("ERISA")\textsuperscript{125} during 1991. The most important cases are discussed below.

A. Definition of Plan and Preemption

James T. Williams ("Williams") was the general manager of Wright Pest Control Company ("WPCC"). In \textit{Williams v. Wright},\textsuperscript{126} Williams brought an action under ERISA and under state law for various benefits. The benefits were set forth in a letter from the president of WPCC to Williams dated October 23, 1981. The benefits described in the letter included monthly payments of $500, insurance benefits, country club dues, and telephone and automobile expenses. In 1985 the president of WPCC notified Williams that the benefits under the letter would be terminated. Williams filed a lawsuit alleging violations of ERISA and state law. The district court granted summary judgment to WPCC and its president on all counts, and Williams appealed.\textsuperscript{127}

On appeal, the Eleventh Circuit noted that a plan is subject to ERISA if, from the surrounding circumstances, "a reasonable person can ascertain the intended benefit, a class of beneficiaries, the source of financing

\begin{itemize}
\item \textsuperscript{120} \textit{Id.} at 1356.
\item \textsuperscript{121} \textit{Id.}
\item \textsuperscript{122} \textit{Id.}
\item \textsuperscript{123} \textit{Id.}
\item \textsuperscript{124} \textit{Id.}
\item \textsuperscript{126} 927 F.2d 1540 (11th Cir. 1991).
\item \textsuperscript{127} \textit{Id.} at 1541-42.
\end{itemize}
and procedures for receiving benefits." Although the district court concluded that these factors do not indicate the existence of an ERISA plan, the Eleventh Circuit disagreed. While ERISA requires that the assets of an employee pension benefit plan be held in trust, the Eleventh Circuit pointed out that an employer's failure to meet an ERISA requirement does not exempt the plan from ERISA. The Eleventh Circuit also observed that a procedure for receiving benefits was set forth in the letter because it stated that the company would issue a check each month and that revisions would be considered later. The Eleventh Circuit also concluded that a class of beneficiaries could refer to just one employee. Referring to several opinions of the Department of Labor to support this conclusion, the Eleventh Circuit distinguished several cases cited by WPCC: these cases promised retirement pay as part of a current employment contract, rather than for the sole purpose of paying retirement income. As a result, the Eleventh Circuit concluded that the 1981 letter primarily constituted the payment of retirement income and was not an employment contract outside the scope of ERISA.

The Eleventh Circuit also held that Williams' state law contract claims for retirement benefits and insurance benefits were preempted by section 514(a) of ERISA. The Eleventh Circuit, concluding that the country club dues and automobile expenses were not covered by ERISA, applied state laws to these claims. As a result, the Eleventh Circuit reversed the portions of the district court's opinion that held ERISA did not apply to the retirement and insurance benefits, affirmed the portion of the district court's opinion that held that state law was preempted with respect to the retirement benefits and insurance benefits, and reversed the portion of the district court's opinion that held that state law did not apply to the country club dues and automobile expenses.

B. Exhaustion of Administrative Remedies

Plaintiffs in Harrison v. United Mine Worker's of America 1974 Benefit Plan & Trust filed a class action lawsuit to compel the United Mine

128. Id. at 1543 (quoting Donovan v. Dillingham, 688 F.2d 1367, 1373 (11th Cir. 1982)).
129. Id. at 1543-44.
130. Id. at 1544 (quoting Scott v. Gulf Oil Corp., 754 F.2d 1499, 1503 (9th Cir. 1985)).
131. Id. at 1544-45.
132. Id. at 1545.
133. Id. at 1546-47.
134. Id. at 1547.
136. 927 F.2d at 1550-51 (citing 29 U.S.C. § 1002 (1988)).
137. Id. at 1541.
138. 941 F.2d 1190 (11th Cir. 1991).
Worker's of America 1974 Benefit Plan and Trust (the “1974 Plan”) to pay retroactive health and other welfare benefits. After the 1974 Plan received the complaint, the 1974 Plan initiated an investigation into the eligibility of plaintiffs. Plaintiffs were retirees of the Black Diamond Coal Company (“Black Diamond”). The 1974 Plan filed an answer to the complaint asserting that plaintiffs were not eligible for benefits, although the 1974 Plan later concluded that plaintiffs and their beneficiaries were entitled to benefits. Nevertheless, plaintiffs pursued their lawsuit. The district court granted the 1974 Plan’s motion for summary judgment, and plaintiffs appealed.  

The Eleventh Circuit affirmed the district court’s summary judgment for the 1974 Plan. The Eleventh Circuit noted that plaintiffs had failed to take the most rudimentary administrative steps to obtain their benefits. Plaintiffs had never submitted applications for benefits to the 1974 Plan nor had the 1974 Plan been petitioned to conduct a required investigation to determine the eligibility of the Black Diamond retirees. As observed by the Eleventh Circuit, “it is well-established in this Circuit that plaintiffs in ERISA cases must normally exhaust available administrative remedies under their ERISA-governed plans before they may bring suit in federal court.” The Eleventh Circuit also affirmed the district court’s granting of summary judgment for defendant on plaintiff’s claim for attorney’s fees because they concluded that the lawsuit was essentially frivolous.

C. Extra-Contractual Damages

Plaintiffs in McRae v. Seafarers’ Welfare Plan were insured beneficiaries of a health insurance plan known as the Seafarer’s Welfare Plan (the “Plan”). Plaintiff Paulette McRae had consulted a doctor about obtaining a reanastomosis, a reversal of a sterilization procedure. The doctor contacted the toll-free number of the Plan to determine whether such an operation would be covered. The doctor was informed that the operation would be covered. After undergoing the operation, however, plaintiffs were informed that the operation was not covered under the terms of the Plan. Plaintiff sued to compel the Plan to pay the cost of the operation, compensatory and consequential damages for emotional distress, embarrassment, humiliation, and damages to their financial reputation because

139. Id. at 1192.
140. Id. at 1193.
141. Id.
142. Id. (quoting Springer v. Wal-Mart Assoc. Group Health Plan, 908 F.2d 897, 899 (11th Cir. 1990)).
143. Id. at 1193.
144. 920 F.2d 819 (11th Cir. 1991).
they were unable to pay the bills. The district court awarded plaintiffs the cost of the operation as well as $50,000 for extra-contractual damages. Defendants appealed.\footnote{145}

On appeal, the Eleventh Circuit noted that ERISA section 502(a)(3)\footnote{146} does not expressly provide for extra-contractual damages.\footnote{147} The Eleventh Circuit also pointed out that the Supreme Court, in dictum, had implied that the six civil enforcement provisions of ERISA section 502(a) provide strong evidence that Congress did not intend to authorize other remedies.\footnote{148} However, plaintiffs cited a 1988 House Committee report indicating that extra-contractual damages may be appropriate in certain situations. The Eleventh Circuit stated, however, that this report carried little weight because Congress had not yet acted to provide for this type of damages.\footnote{149} As a result, the Eleventh Circuit reversed the district court's award of extra-contractual damages.\footnote{150}

D. Misrepresentation

Plaintiffs in \textit{Barnes v. Lacy}\footnote{181} were retirees from Alabama Gas Corporation ("ALAGASCO"). In November 1985, ALAGASCO announced that it was offering a Voluntary Early Retirement Opportunity Plan ("VERO"). VERO provided additional incentives to employees who were already eligible to take early retirement under the ALAGASCO Pension Plan. Two years after VERO, in November 1987, ALAGASCO announced a second early retirement program entitled the Voluntary Retirement Incentive Program ("VRIP"). VRIP offered greater benefits than the benefits obtained by plaintiffs under VERO.\footnote{152}

Plaintiffs sued ALAGASCO for misrepresentation under ERISA. The district court determined that plaintiffs failed to show that ALAGASCO either contemplated or intended to offer a second voluntary retirement incentive plan after VERO. The district court concluded, however, that ALAGASCO misled eight of the nine plaintiffs by failing to disclose that the company reserved the right to make early retirement benefits available in the future—whether higher, lower, or the same—at any time it wished to do so. The district court did not rely on any violation of ERISA

\begin{enumerate}
\item Id. at 820-21.
\item 920 F.2d at 821.
\item Id. at 821-22 (quoting Massachusetts Mut. Life Ins. Co. v. Russell, 473 U.S. 134, 146 (1985)).
\item Id. at 823.
\item Id.
\item Id.
\end{enumerate}
but, instead, applied trust principals of fiduciary responsibility. Defendants appealed.\textsuperscript{158}

On appeal, the Eleventh Circuit noted that it could not reverse findings of fact unless shown to be clearly erroneous, but that its review of the application of the law to the facts is de novo.\textsuperscript{144} The Eleventh Circuit reviewed the district court's factual findings and noted that ALAGASCO did not contemplate making any further or later offers of retirement at the time it made VERO available to its employees.\textsuperscript{108} The Eleventh Circuit also noted that the terms of the ALAGASCO pension plan expressly stated that ALAGASCO Board of Directors reserved the right to amend the terms of the Plan and that the summary plan description described ALAGASCO's power to amend.\textsuperscript{156} The Eleventh Circuit stated that ALAGASCO did not breach any fiduciary duty to its employees, even assuming that the employees did not receive notice of ALAGASCO's retention of its right to amend its retirement plan.\textsuperscript{157} Because the district court found that ALAGASCO had made no untruthful statements, the Eleventh Circuit determined that there was no material misrepresentation and reversed the decision of the district court.\textsuperscript{158}

\textbf{E. Miscellaneous Cases}

Although space prohibits a complete discussion, there are several other ERISA cases deserving of mention. In \textit{McKinnon v. Blue Cross & Blue Shield of Alabama},\textsuperscript{159} the Eleventh Circuit held that an employee's daughter, who had been named executrix of her father's estate (which had brought a fraud and bad faith claim against a benefit plan sponsored by the deceased's employer), was not a "participant or beneficiary" within the meaning of ERISA; therefore, the daughter could not bring suit under ERISA's antiretaliation provisions, even though the daughter had been allegedly discharged for the lawsuit.\textsuperscript{160} In \textit{Blank v. Bethlehem Steel Corporation},\textsuperscript{161} the Eleventh Circuit held that an employer's determination that the sale of a division of a company did not constitute a break in service was not "arbitrary and capricious" because the decision was made

\begin{footnotes}
\footnote{153. \textit{Id.} at 541-42.}
\footnote{154. \textit{Id.} (citing Fed. R. Civ. Proc. 52(a); United States v. Fidelity Capital Corp., 920 F.2d 827, 836 (11th Cir. 1991)).}
\footnote{155. \textit{Id.}}
\footnote{156. \textit{Id.} at 543.}
\footnote{157. \textit{Id.} at 544.}
\footnote{158. \textit{Id.}}
\footnote{159. 935 F.2d 1187 (11th Cir. 1991).}
\footnote{160. \textit{Id.} at 1191-92.}
\footnote{161. 926 F.2d 1090 (11th Cir. 1991), \textit{cert. denied}, 1991 US LEXIS 6410 (1991).}
\end{footnotes}
rationally and in good faith. The Eleventh Circuit held in *Andrews v. Employees' Retirement Plan of First Alabama Bancshares* that attorney fees cannot be awarded when there is no lack of bad faith shown on the part of the employee benefit plan. Obviously, all of these ERISA cases strongly favor employers.

V. CONCLUSION

The tax cases decided by the Eleventh Circuit in 1991 evidence the importance to the tax practitioner being aware of the procedural requirements of the Code. The large number of ERISA cases decided by the Eleventh Circuit during 1991 continue to evidence the increasing importance of ERISA to the tax practitioner. Although ERISA has been in existence since 1974, it is obvious from the large number of unresolved issues that face the Eleventh Circuit that the statute remains in its judicial infancy.

162. 926 F.2d at 1095.
163. 938 F.2d 1245 (11th Cir. 1991).
164. *Id.* at 1248.