No. 17-663

In The

Supreme Court Of The United States

THE GREEN SOLUTION RETAIL, INC., A COLORADO CORPORATION; KYLE SPEIDELL,
Petitioners,

v.

UNITED STATES OF AMERICA; INTERNAL REVENUE SERVICE; JOHN KOSKINEN, INTERNAL REVENUE SERVICE COMMISSIONER; DAVID HEWELETT, IN HIS OFFICIAL CAPACITY, AUDITOR FOR THE INTERNAL REVENUE SERVICE,
Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

REPLY TO GOVERNMENT'S BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

1) Does the Internal Revenue Service ("IRS"), as an executive agency of the United States, have authority to investigate and administratively determine that a taxpayer is criminally culpable under federal criminal drug laws?

2) Does the *Anti-Injunction Act*, 26 U.S.C. §7421, preclude the Courts from exercising its constitutional power to take appropriate action to preclude the executive branch (IRS) from acting in excess of its power?

3) Does the *Declaratory Judgment Act*, 28 U.S.C. 2201 preclude the Courts from determining whether the executive branch (IRS) is acting in excess of its authority when conducting administrative investigations into violations of federal criminal drug laws?

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SUMMARY OF REPLY

Assuming the Court grants certiorari, this will be the first case where the Court has interpreted Section 280E of the Tax Code.

The Government is incorrect that the broad reading of the AIA is uniformly applied. At best, the courts are split on this issue with at least one circuit directly rejecting the Government's broad reading. Nor do appellate decisions on the AIA support the broad reading *post-Direct Marketing*. The Court needs to resolve whether the AIA should be interpreted broadly or more narrowly as *Direct Marketing* suggests.

The Government claims that Section 280E is not a penalty. The rationale is that since the Government has the power to deny deductions it can do so and its actions can never be considered a penalty. This is not true. The test is *not* whether the Government has the power to impose the exaction. The test is whether Section 280E is a sanction or punishment for an unlawful act or omission.

Regarding the merits, the Government is incorrect that the IRS has authority to investigate inherently criminal activity under Section 280E. As discussed further below, the *Leary* "constitutional difficulty" discussed in the Petition, precludes an interpretation of Section 280E that (1) allows the IRS to investigate inherently criminal activity for tax administration purposes, and (2) be able to share the information with the Department of Justice without

immunity provided to the taxpayer. This Court has been very clear that if Congress uses its tax power to delegate to the IRS authority to investigate an area directed at a group inherently suspect of criminal activities (rather than an essentially noncriminal and regulatory area of inquiry), it can only be done if Congress prohibits the sharing of incriminating evidence with law enforcement or provides absolute immunity. Otherwise the statute is unconstitutional. Section 280E does not provide such protection. Thus, Section 280E should not be construed as giving the IRS authority to investigate the facts and find that a person has violated federal criminal drug laws. Otherwise, Section 280E will be unconstitutional.

ARGUMENT

A. The Courts are Split on the "Broad Reading" of the AIA.

The Government incorrectly asserts that the courts have "uniformly" adopted the broad reading of the AIA to preclude any litigation on all "activities leading up to, and culminating in, such assessment and collection.."[1] Opp., p. 8. The District of Columbia Circuit disagrees:

> "The Commissioner . . . insists that *Bob Jones* and *"Americans United"* require a broad approach to what constitutes prohibited 'tax litigation' . . .

[1] The Government in its string cite to support its proposition of uniformity does not cite to a single case post *Direct Marketing*.

> [H]owever, in [*Cohen v. U.S.,* 650 F.3d 717 (D.C. Cir. 2011)] we rejected this view of "a world in which no challenge to the [the IRS's] actions is ever outside the closed loop of its tax authority."

Z Street v. Koskinen, 791 F.3d 24, 30 (D.C. Cir. 2015).

The court continued:

> "Our rejection of the Commissioner's broad reading of the Act finds support in the Supreme Court's recent decision in *Direct Marketing Association v. Brohl*, U.S., 135 S.Ct. 1124, 191 L.Ed.2d 97 (2015). There, interpreting the Anti Injunction Act's cousin, the Tax Injunction Act, which serves a similar function for federal court challenges to state taxes, the Court read "restrain" in that statute as having a "narrow[ ] meaning ... captur[ing] only those orders that stop ... assessment, levy and collection" rather than "merely inhibit" those activities. Id. at 1132 (internal quotation marks omitted). True, the two statutes differ: the Tax Injunction Act pairs "restrain" with 'enjoin' and 'suspend' suggesting that the word is used "in its narrow[ ] sense," id., while the word "restraining" stands alone in the Anti–Injunction Act. Yet *Brohl's* holding is significant here because the Court "assume[s] that words used in

> both Acts are generally used in the same way." *Id.* at 1129.

Z Street, 791 F.3d at 30-31.

There is indication that the Fifth Circuit would not accept the broad reading post *Direct Marketing*. In *Chamber of Commerce of the United States v. IRS*, U.S. Dist. LEXIS 166985 (W.D. Tex., Oct. 6, 2017), the Plaintiffs brought a lawsuit claiming the IRS was acting outside of its statutory jurisdiction. In assessing whether the Plaintiffs' claims were barred by the Anti-Injunction Act, the court applied the narrow reading of the AIA, citing to *Direct Mktg. Ass'n v. Brohl,* 135 S. Ct. 1124, 1131 (2015). "Assessment and collection of taxes does not include all activities that may improve the government's ability to assess and collect taxes. . . (applying Tax Injunction Act but stating that Court "assume[s] that words used in both Acts are generally used in the same way. . ." *Id.*

The district court also found that the Plaintiffs, in challenging the IRS' statutory authority, were not seeking to restrain the assessment or collection of a tax. Rather, the court found that the Plaintiffs were challenging the validity of an IRS rule so that a reasoned decision could be made about whether to engage in a potential future transaction that would subject them to taxation under the rule. *Id.*

The Tenth Circuit was not clear that *Direct Marketing* had implicitly overruled the broad reading in *Lowrie.* The court stated:

> "[The *Direct Marketing* Court] came to [its] conclusion for two reasons, the first of which supports [Green Solution's] argument that *Direct Marketing* implicitly overruled *Lowrie*, the second of which does not."

App., p.23.

The Tenth Circuit continued to discuss that the Court in *Direct Marketing* rejected the Tenth Circuit's broad reading of "restrain" as "to hold back" because "'virtually any court action related to any phase of taxation might be said to hold back collection'". App., p. 24.

On the other hand, the Court stated:

> Unlike in the TIA, "restrain" in the AIA stands alone. Recall that the AIA states: "[N]o suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person." I.R.C. § 7421(a). To the extent it keeps company, it does so with the phrase "for the purpose of restraining the assessment or collection."

App., p. A-25.

In summary, the Tenth Circuit stated:

> "And it is therefore even more unsettled how the Court would assess a similar action to enjoin federal taxing

> authorities under the distinct language of the AIA."

App., p. A-26

There is now a split in the circuits of whether the broad reading should apply.

B. The AIA and TIA Should be Construed Alike.

The Government concedes that *Direct Marketing* requires a narrower reading of the TIA. However, the Government contends that the AIA and TIA should now be read as substantively different – that "*Brohl's* interpretation of the TIA did not abrogate *Lowrie's* interpretation of the Anti-Injunction Act." Opp., p. 6. As discussed above, the Petitioners believe *Direct Marketing* did abrogate *Lowrie*.

However, there is an important reason not to follow the Government's argument and separate the AIA and TIA substantively. The AIA and TIA have historically been interpreted as being substantively identical.

> "Despite the federal-state distinction between the AIA and the TIA, the text and effects of the statutes are substantially identical, and cases that treat the definitions and applications of the statutes are used as interchangeable precedent by default in current jurisprudence."

COMMENT: The Label Test: Simplifying the Tax Injunction Act after NFIB v Sebelius, 84 U. Chi. L. Rev. 2103, 2104 (2017).

Should the Court now decide that the AIA and TIA are substantively different, such a ruling would destroy the previous jurisprudence of the two acts. The apple cart would be upset indeed.

C. This Is Not a Matter Suitable for a Refund Action.

The AIA "does not apply at all where the plaintiff has no other remedy for its alleged injury." *Z Street,* 791 F.3d at 31. "The Act was intended to apply only when Congress has provided an alternative avenue for an aggrieved party to litigate its claims." *Id.*

The Government claims that a refund action and the ability to defend against IRS summonses provide the alternative avenue to litigate its claims. These are not sufficient in this case.

The refund statute, Section 7422(a) addresses suit "for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected . . ." However, the Petitioners are not seeking recovery of wrongly paid sums. They are seeking to stop an unlawful investigation by the IRS into nontax crimes. "This is simply not a typical tax refund action in which an individual taxpayer complains of the manner in which a tax was assessed or collected and seeks reimbursements for wrongly paid sums." *See, King v. Burwell,* 759 F.3d 358, 367 (4th Cir. 2014).

The wrong could not be addressed by a refund action. The IRS using the tax power to generally investigate violations of nontax crimes is tantamount to a general warrant - thus violating Petitioners Fourth Amendment rights. See *Coolidge v. New Hampshire*, 403 U.S. 443, 467 (1971). Recovery of overpaid tax is simply not applicable in this situation.

The Government's statement that this matter is suitable for a refund action is also inconsistent with what it states *in* the refund action. See *Alpenglow Botanicals v. United States,* 1:16-cv-00258 (D.Colo. 2016), a refund action. In *Alpenglow,* the Government claimed that any resolution of the IRS's power is likewise barred in a refund suit. The Government stated:

> "The Anti-Injunction Act, 26 U.S.C. § 7421(a), generally bars any action seeking to enjoin the collection of taxes by the Government . . . The Anti-Injunction Act does not contain an exception for 26 U.S.C. § 280E. Thus, there are no statutory exceptions to the Anti-Injunction Act that permit plaintiffs' lawsuit."

Government Motion to Dismiss, Alpenglow Botannicals v. United States, 1:16-cv-00258 [Doc.11], p. 10.

Nor is the defense of an IRS summons an appropriate avenue. First, the Petitioners have no control if and when the IRS may issue a summons. Second, the petition to quash is limited to only

whether the summons is proper. See 26 U.S.C. Section 7609.

D. Section 280E is a Penalty for Purposes of the AIA.

The Government argues that since Congress has the power to deny deductions, such a denial can never be considered a penalty. In other words, if Congress can do it, the actions can never be considered a penalty. This Court has rejected such a wide interpretation. See *LaFranca, infra.*

It is clear that Congress denied all deductions under Section 280E as a sanction for wrongdoing. The Senate Committee on Finance stated:

> "Ordinary and necessary trade or business expenses are generally deductible in computing taxable income. . . [However], [t]here is a sharply defined public policy against drug dealing. To allow drug dealers the benefit of business expense deductions at the same time that the U.S. and its citizens are losing billings of dollars per year to such persons is not compelled by the fact that such deductions are allowed to other, legal, enterprises. Such deductions must be disallowed on public policy grounds."

Senate Rept. 97-494, Vol. 1, p. 309.

Thus, it is clear Congress sought to sanction unlawful "drug dealers" through Section 280E.

> "[A] tax is a pecuniary burden laid upon individuals or property for the purpose of supporting the Government." *United States v. Reorganized CF & I Fabricators of Utah, Inc.*, 518 U.S. 213, 224, 116 S. Ct. 2106, 135 L. Ed. 2d 506 (1996). A penalty, on the other hand, connotes a sanction or a punishment for an unlawful act or omission. See *id.; United States v. LaFranca*, 282 U.S. 568, 572, 51 S. Ct. 278, 75 L. Ed. 551 (1931) ("A tax is an enforced contribution to provide for the support of government; a penalty, as the word is here used, is an exaction imposed by statute as punishment for an unlawful act."). As the Supreme Court succinctly observed in *United States v. LaFranca,* [t]he two words [tax vs. penalty] are not interchangeable . . . . and if an exaction [is] clearly a penalty it cannot be converted into a tax by the simple expedient of calling it such." *LaFranca*, 282 U.S. at 572.

Goudy-Bachman v. United States HHS, 764 F. Supp. 2d 684, 695-96 (M.D. Pa. 2011).

> "[I]f the concept of penalty means anything, it means punishment for an unlawful act or omission . . ."

United States v. Reorganized Cf&I Fabricators, 518 U.S. 213, 224 (1996).

Since the purpose of Section 280E is to sanction unlawful drug dealers, Section 280E is a penalty.[2]

The Government contends that Section 280E is not a penalty because it falls under the provisions starting with IRC Section 261, which disallow deductions for various reasons. However, Section 280E being found in this part does not help the Government because "No inference, implication, or presumption of legislative construction shall be drawn or made by reason of the location or grouping of any particular section or provision or portion of this title." 26 U.S.C. § 7806(b). Such a construction would also violate *LaFranca, supra.*

E. The IRS Does Not Have the Authority Under Section 280E to Investigate Inherently Criminal Activity.

The Government contends that 280E gave the IRS the power to investigate nontax crimes because Section 280E disallows all deductions to those engaged in drug trafficking crimes. It cites 26 U.S.C. Section 6201 for its authority. However, the Government sidesteps the fact that if 280E gives the IRS authority to investigate federal criminal drug law violations, Section 280E is in the crosshairs of unconstitutionality.

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[2] The undersigned cannot find any cases discussing whether a statute specifically denying a deduction is a tax for AIA purposes. Nor does the Government cite to any such authority.

The Government discounts the *Leary* "constitutional difficulty" claiming that in *Leary,* the finding of unconstitutionality of the Marihuana Tax Act was not applicable to the present situation. The Government again misses the point.

The investigation centers on an area the Government concedes is of inherently criminal activity. See Opp., p. I, Questions Presented: "Whether the Internal Revenue Service is authorized to investigate and determine whether a business ***is engaged in illegal drug-trafficking activity*** . . ." (emphasis added). See also Opp., p. 2 stating that the conduct in which the IRS alleges the Petitioners are engaging violates the Controlled Substances Act.

Despite the Government's assertion that it seeks the information solely to assess tax, the audit investigation and Section 280E are directed to an area "permeated with criminal statutes", towards a group "inherently suspect of criminal activities". *Marchetti v. United States,* 390 U.S. 39 (1968). As a result, the standard analysis of the regulatory tax system does not apply. This is because the IRS's investigation of inherently criminal activity poses a "constitutional difficulty" – sacrificing Fourth and Fifth Amendment rights when the information is compelled through the use of the tax power. *Id.*

The federal courts have generally provided a relaxed standard of Fourth and Fifth Amendment protections when faced with a tax power investigation. See, e.g., *United States v. Powell*, 379 U.S. 48 (1964) (No probable cause necessary for

searches under the tax summons power); *United States v. Lehman*, 468 F.2d 93 (7th Cir. 1972) (*Miranda* warnings unnecessary in criminal tax investigations, but tax agents may not by fraud or deceit misrepresent that the interview is strictly civil). However, unchecked, great abuses of Fourth and Fifth Amendment rights would occur if tax power is used to investigate nontax crimes.

This Court has recognized a "constitutional difficulty" - that there is a crossroad where the IRS cannot pass in investigating nontax crimes without constitutional protections instituted by Congress. In series of cases, *Leary v. United States,* 390 U.S. 6 (1969), *Marchetti v. United States,* 390 U.S. 39 (1969); *Grosso v. United States,* 390 U.S. 62 (1969); and *Haynes v. United States,* 390 U.S. 85 (1969), this Court addressed the crossroads of tax and nontax investigatory powers. For purposes of this case, the crossroad can be summarized as follows:

> *If Congress uses its tax power to allow the IRS to investigate inherently criminal activity, it must provide the following constitutional protections:*
>
> 1. *Prohibit the IRS from sharing the incriminating information with law enforcement; or*
>
> 2. *Provide absolute immunity from prosecution.*

Otherwise, the IRS enters an impermissible area of Fourth and Fifth Amendment violations.

In *Marchetti v. United States, supra.,* the Court found the constitutional difficulty in the Wagering Tax Act because the IRS could compel information of inherently criminal activity and share with law enforcement. The Court noted the Congressional limitations:

> "We are fully cognizant of the importance for the United States' various fiscal and regulatory functions of timely and accurate information (citation omitted); but other methods, entirely consistent with constitutional limitations, exist by which Congress may obtain such information."

Marchetti v. United States, 390 U.S. at 60.

The Supreme Court cited to *Counselman v. Hitchcock,* 142 U.S. 547 (1892) for its authority. In *Counselman*, the Supreme Court held that if Congress wishes to use its tax power to compel books and records, Congress must afford absolute immunity against future prosecution for the offence to which the question relates. *Counselman*, 142 U.S. at 586.

Congress corrected this constitutional difficulty in the wagering excise tax laws by prohibiting IRS from sharing the incriminating evidence with law enforcement and provided absolute immunity from prosecution. See 26 U.S.C. § 4424; see also *United*

States v. Sahadi, 555 F.2d 23 (2d Cir. 1977) (discussing the corrective actions taken by Congress).

Congress knows how to address the constitutional difficulty in taxing illegal income. So, the fact that Section 280E does not have the constitutional protections is indicative that Congress did not intend to give the IRS the investigatory authority into inherently criminal activity.

CONCLUSION

Given the above, certiorari should be granted on the Questions Presented.

Respectfully Submitted,

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