

Judge	_____
Mag.	_____
Journal	_____
Case	_____
Entered	_____

IN THE UNITED STATES DISTRICT COURT FOR THE
SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION

UNITED STATES

Plaintiff,

v.

ROBERT W. WELTI, individually
and d/b/a BOPAT ENTERPRISES

Defendant.

C-1-02 243

Civil No. **J. DLOTT**

J. HOGAN

U.S. DISTRICT COURT
SOUTHERN DISTRICT OF OHIO
WEST DIV. CINCINNATI

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FILED
KENNETH J. MURPHY
CLERK

Complaint and Request for Injunctive Relief

Plaintiff United States of America, for its complaint against defendant Robert W. Welti individually and doing business as Bopat Enterprises states as follows:

Jurisdiction and Venue

1. Jurisdiction is conferred on this Court by 28 U.S.C. §§ 1340 and 1345 and §§ 7401, 7402(a), 7407, and 7408 of the Internal Revenue Code of 1986 (26 U.S.C.) (IRC).
2. This suit is brought to restrain and enjoin the defendant from:
 - a. further acting as a federal-income-tax-return preparer;
 - b. engaging in activity subject to penalty under IRC § 6694, including understating taxpayers' liabilities;
 - c. engaging in activity subject to penalty under IRC § 6695, including failing to supply a list of clients or provide copies of clients' tax returns to the IRS on request;
 - d. engaging in activity subject to penalty under IRC § 6701, including preparing and/or assisting in the preparation of documents related to a matter material to the internal revenue laws that include a position that he knows will result in the understatement of tax liability;
 - e. engaging in any other activity subject to penalty under IRC §§ 6694, 6695, or 6701; and

- e. engaging in any other activity subject to penalty under IRC §§ 6694, 6695, or 6701; and
- f. engaging in other conduct that substantially interferes with the proper administration and enforcement of the internal revenue laws.

3. An injunction is warranted based on (a) Welti's conduct as a tax-return preparer who prepares federal income tax returns that understate tax liability based on abusive trust schemes, and (b) Welti's conduct as a taxpayer representative who repeatedly impedes and obstructs lawful IRS investigations.

4. Welti has prepared federal income tax returns for individuals and trusts that understate tax liability based on the false and fraudulent positions that taxpayers can eliminate their income tax liability through the use of sham trusts. The trusts used by Welti's clients are similar to the abusive trusts described in IRS Public Notice 97-24. That notice describes trust arrangements that falsely promise that taxpayers can claim tax benefits from trusts with no meaningful change in the taxpayer's control over or benefit from the taxpayer's income or assets.

5. On behalf of taxpayers he represents before the IRS, Welti has asserted a frivolous position known as the "§ 861 argument" or "foreign sources argument." This argument asserts that U.S. citizens and residents are not subject to federal income tax on their wages and other income earned or derived within the United States. This position is based on the false claim that federal tax law imposes taxes only on income derived from certain foreign-based activities listed in an immaterial Treasury regulation. The IRS has informed the public that the § 861 argument is frivolous, the United States Tax Court has sanctioned taxpayers who assert the frivolous position, and a United States District Court has enjoined a return preparer who asserted it on tax returns.

6. If Welti is not enjoined, his continuing actions will result in additional understatements of tax liability, and additional improper obstruction of lawful IRS investigations.

7. This action has been authorized and requested by the IRS Chief Counsel, a delegate of the Secretary of the Treasury, and commenced at the direction of a delegate of the Attorney General under IRC §§ 7401, 7402, 7407, and 7408.

8. Welti resides at 135 North Third Street, Ripley, Ohio. Welti is preparing income tax returns through Bopat Enterprises, which uses the same address. Venue is proper in this Court under 28 U.S.C. §§ 1391 and 1396.

Count I

(Injunction under IRC § 7407)

9. IRC § 7407 authorizes a court to enjoin a person from, among other things,
1. engaging in conduct subject to penalty under IRC § 6694 (which penalizes a return preparer who prepares or submits a return that contains an unrealistic position) or IRC § 6695 (which penalizes a return preparer who fails to keep a list of clients or turn over the client list to the IRS upon request), and
 2. engaging in any other fraudulent or deceptive conduct that substantially interferes with the proper administration of the internal revenue laws.

If the return preparer's conduct is repeated and the Court finds that a narrower injunction (*i.e.*, prohibiting only the specific enumerated conduct) would not be sufficient to prevent that person's interference with the proper administration of federal tax laws, the Court may enjoin the person from further acting as a return preparer.

10. Welti is a certified public accountant with tax-return-preparation clients in at least 20 states across the country.

11. Welti lists his business on his 1998 federal income tax return as being conducted through a sole proprietorship, Bopat Enterprises, with the principal business or profession listed as “accounting, financial services, network marketing.”

12. For the 2000 and 2001 tax years, Welti prepared federal income tax returns for trusts and individuals in Alabama, Arizona, California, Florida, Georgia, Hawaii, Illinois, Kansas, Michigan, Missouri, New York, North Carolina, Ohio, Oregon, Pennsylvania, South Dakota, Tennessee, Texas, West Virginia, and Wisconsin. On information and belief, each trust customer pays Welti \$2,400 per year to prepare tax returns based on the abusive trusts described above.

13. Heritage sells packages, often to self-employed individuals, that promote the use of abusive trusts to which the customer’s personal assets, residence, and business are transferred. The trust packages purport to reduce taxable income by: (1) allocating or assigning income between different trusts; (2) artificially inflating the basis of assets; and (3) deducting expenses that are unsubstantiated or not deductible under the Internal Revenue Code.

16. In *Muhich v. Commissioner*, T.C. Memo 1999-192, 1999 WL 390695, *affirmed*, 238 F.3d 860 (7th Cir. 2001), the Tax Court and Seventh Circuit held that the taxpayers in that case used sham trust packages sold by Heritage Assurance Group to claim improper income tax deductions. Welti has prepared federal income tax returns for at least some 75 clients claiming similar improper deductions and otherwise understating income based on substantially similar sham trusts.

17. In representing clients before the IRS, Welti has advocated what is known as the “US sources” or “IRC § 861 argument.” Welti and others promoting this frivolous argument falsely posit that a regulation promulgated under IRC § 861 (26 CFR § 301-1.861-8(f)) provides the exclusive list

of sources of income subject to federal income tax. Since that list is narrow, and focuses on foreign income of US citizens and similar international tax issues, § 861-argument proponents assert that US-sourced income earned by US citizens is not subject to income taxation.

18. As a certified public accountant, Welti is or should be aware that the § 861 argument has been rejected by every judge that has considered it, beginning as early as 1993 in *Solomon v. Commissioner*, 66 T.C.M. (CCH) 1201, 1993 WL 444615 (1993). The Tax Court reiterated its rejection of the § 861 argument in 1995 in *Aiello v. Commissioner*, TC Memo 1995-40, 69 T.C.M. (CCH) 1765, 1995 WL 33283 (1995), and as recently as last year in *Furniss v. Commissioner*, TC Memo 2001-137, 81 T.C.M. (CCH) 1741, 2001 WL 649000 (2001). In addition, the Tax Court has sanctioned three taxpayers for asserting the position, imposing \$5,000 penalties against taxpayers in *Solomon and Williams v. Commissioner*, 114 T.C. 136 (2000), and a \$25,000 penalty against another taxpayer in *Darlow T. Madge v. Commissioner*, Tax Court Docket No. 01-1531.

19. Welti's assertion of the § 861 Argument on behalf of clients is an attempt to impede the lawful functions of the IRS. In addition, Welti has used other frivolous diversionary tactics to obstruct and impede IRS audits of his abusive-trust clients. These improper tactics include:

- threatening to sue IRS employees if they proceed with auditing his clients;
- asserting IRS agents have no right to examine the underlying trust documents;
- asserting that the federal income tax is unconstitutional based on the Thirteenth Amendment's prohibition against involuntary servitude;
- asserting that there is a (legitimate) "constitutional" United States and a (illegitimate) "corporate" United States, which went bankrupt years ago and is now illegally collecting taxes;

- asserting that the IRS is only an “organization,” not part of the “constitutional government,” and therefore not “authorized” by Congress to collect taxes.

These positions are frivolous, have been universally rejected by the courts, and generally subject those who assert them in court to sanctions and penalties. Welti’s repeated assertion of these frivolous positions to IRS officials during IRS audits of his clients substantially interferes with the IRS’s ability to audit Welti’s clients and enforce the tax laws.

20. The IRS estimates that Welti’s total tax understatements on his trust clients’ returns is \$92,172 per return, with a total estimated underreporting of tax liability of \$3,226,020 per year.

21. Welti has refused (in violation of IRC § 6107) to give the IRS his client list or copies of all returns he has filed. Thus, the IRS is currently unable to establish with certainty how many improper trust returns Welti has prepared. Welti’s failure to provide a list of clients impedes the IRS’s ability to investigate the abusive trust schemes and assess and collect the proper tax liabilities of participants in these schemes.

22. In one egregious instance, Welti prepared individual and trust tax returns on behalf of Michael E. Diesel of Saint Marys, Kansas, that resulted in an estimated underreporting of \$1,417,072 in 1999 taxable income and \$1,589,330 in 2000 taxable income. For the 1999 tax year, Welti prepared trust returns on behalf of six sham trusts (the Diesel Watercraft Trust, the Diesel Vehicle Trust, the Diesel Training Trust, the Diesel Acceptance Trust, the Diesel Equipment Trust, and the Diesel Family Trust), purporting to reduce taxable income to zero based on frivolous deductions and income distributions to the Diesel Business Trust. The Diesel Business Trust then purportedly distributed \$1,417,072 in taxable income to the Pernour International Trust, 1416 Unity Boulevard,

Suite 100, Belmopan, Belize, a tax-haven country. By deducting this distribution, the Diesel Business Trust reduced its reported taxable income to \$0. On information and belief, because Michael Diesel is named as the fiduciary of the foreign trust, he retains full dominion and control over the \$1,417,072. By this improper structuring, Diesel purportedly eliminated approximately \$1,417,072 in 1999 taxable income. For the 2000 tax year, Diesel was able to eliminate approximately \$1,589,330 in taxable income through similar frivolous deductions and sham distributions to various trusts.

23. Welti prepared individual and trust income tax returns for another client, Steven J. Welbourn of Brentwood, Tennessee, that resulted in the underreporting of approximately \$380,000 in taxable income. Welbourn claimed a bogus expense on his tax return of \$380,000 for “management services.” In turn, the Form 1041 trust income tax return for “Green Hill Asset Management Company,” a purported business sharing the same address as Welbourn, listed taxable income of \$378,071 (for the “management services” referenced above). Green Hill purportedly distributed the \$378,071, as reported on an IRS Form K-1, to Concord Enterprises International Trust, 1416 Unity Boulevard, Suite 100, Belmopan, Belize. Green Hill then deducted this amount as “Other Expenses” on Green Hill’s tax return, reducing its reported taxable income to \$0. On information and belief, because Welbourn is named as the fiduciary of the foreign trust, he retains full dominion and control over the \$380,000. By this improper structuring, Welbourn purportedly eliminated approximately \$380,000 in taxable income. Welti prepared all federal income tax returns pertaining to this bogus scheme.

24. Another Welti return-preparation client, Charles Oliver of Springfield, Ohio, used a trust scheme in connection with Welti-prepared tax returns to purportedly eliminate \$689,929 in income by transferring it as a “management services” fee to Strategic Financial Asset Management Trust, which in

turn purportedly transferred it to the Chico International Trust, 1416 Unity Boulevard, Suite 100, Belmopan, Belize. Welti prepared all federal income tax returns pertaining to this bogus scheme.

25. Another Welti return-preparation client, Charles W. Lucas of Dayton, Ohio, used a trust scheme in connection with Welti-prepared tax returns to purportedly eliminate \$15,907 in taxable income by transferring it as a “management services” fee to “Anchor Deep Asset Management Trust,” which in turn purportedly transferred it to the Sponsio International Trust 1416 Unity Boulevard, Suite 100, Belmopan, Belize. Welti prepared all federal income tax returns pertaining to this bogus scheme.

26. Welti-prepared tax returns filed with the IRS reported similar results from sham trusts for clients throughout the country. On information and belief, using the trust packages sold by abusive-trust promoters, most or all of Welti’s clients set up their purported international trusts at the same address—1416 Unity Boulevard, Suite 100, Belmopan, Belize.

27. The IRS wrote to Welti on November 30, 2001, informing him that he was under investigation for possible violations of IRC § 6701. The letter also informed Welti that he could be enjoined under IRC § 7408. The letter requested that Welti provide a variety of documents, including documents describing the trust arrangements and the names and addresses of his clients.

28. Welti declined to meet with the IRS or provide any documents.

29. By letter dated January 17, 2002, Welti replied to the IRS agent conducting the IRC § 6701 investigation. Welti refused to produce any documents and asserted several frivolous tax arguments, including that the Internal Revenue Code is not “positive law” and thus of “limited application to residents of the fifty states.” Welti also stated that the provisions of the Internal Revenue

Code pertaining to abusive-tax-shelter promoters “only [apply] to Alcohol, Tobacco and Firearms activities, not income tax activities.”

30. Welte’s actions are subject to injunction under IRC § 7407(b)(1)(A) and the Court should enjoin him as requested below. Subparagraph (1)(A) authorizes courts to enjoin conduct subject to penalty under IRC §§ 6694 or 6695. Welte’s conduct is subject to penalty under IRC § 6694 because he knowingly prepared and filed returns resulting in understatements of income-tax liability on income-tax returns filed by approximately 75 clients in 20 states, resulting in an estimated \$3,226,020 annual underreporting of income. Welte’s conduct is subject to penalty under IRC § 6695 because he failed to supply a list of clients or provide copies of clients’ tax returns to the IRS on request.

31. Welte’s repeated assertion—on behalf of his clients during IRS audits—of frivolous positions about the tax laws is fraudulent and deceptive conduct that substantially interferes with the proper administration of the internal revenue laws, and thus is subject to injunction under IRC § 7407(b)(1)(D).

32. Welte should be enjoined from acting as an income-tax-return preparer and from representing clients in federal tax matters because of his pattern of continual and repeated abusive conduct, as described above.

Count II

(Injunction under § 7408 for violation § 6701)

33. The United States incorporates by reference paragraphs 1 through 32.

34. IRC § 7408 authorizes a court to enjoin persons who have engaged in conduct subject to penalty under IRC § 6701 from engaging in further such conduct. Section 6701 imposes a penalty on

any person who aids in the preparation of any portion of a return, who knows the portion will be used to assert a position under the internal revenue laws, and who knows the portion (if so used) would result in an understatement in tax liability.

35. Welti has prepared tax returns and assisted in the preparation of tax returns and other documents for other people that were intended to be used (and were in fact used) in connection with material matters arising under the internal revenue laws. Welti knew that these returns and other documents (if so used) would result in understatements of tax liabilities of these other persons, thus subjecting Welti to penalties under IRC § 6701. The United States is entitled to an injunction under IRC § 7408 to prevent Welti from engaging in further conduct subject to penalty under IRC § 6701.

Count III

(Unlawful Interference with the Enforcement of the Internal Revenue Laws)

36. The United States incorporates by reference paragraphs 1 through 35.

37. Through the conduct described above, Welti has engaged in conduct that substantially interferes with the administration and enforcement of the internal revenue laws. Even after being told by the IRS that he is engaging in conduct subject to penalty, Welti has refused to stop preparing returns understating income based on sham trust schemes and has engaged in other conduct that substantially interferes with enforcement of the internal revenue laws. Unless enjoined by this Court, Welti is likely to continue to engage in such conduct. Welti's conduct is causing irreparable injury to the United States, and the United States has no adequate remedy at law:

- a. Welti's conduct, unless enjoined, is likely to cause a substantial loss of revenue to the United States Treasury. Unless he is enjoined the IRS will have to expend substantial

time and resources to detect future returns with substantial understatements, and may be unable to detect all of them.

- b. The detection and audit of Welti's clients with substantial understatements from abusive trust schemes will place a serious burden on the IRS's resources. Even if all understatements can be detected and corrected, the IRS may not be able to collect all taxes and penalties due.
- c. If Welti is not enjoined, he likely will continue to engage in conduct subject to penalty under IRC §§ 6694, 6695, and 6701 that substantially interferes with the enforcement of the internal revenue laws.

WHEREFORE, the plaintiff, United States of America, respectfully prays for the following:

- A. That the Court find that Welti (individually and doing business as Bopat Enterprises), has engaged in conduct subject to penalty under IRC §§ 6694 and 6695, and that injunctive relief is appropriate under IRC § 7407 to prevent him from acting as an income-tax-return preparer;
- B. That the Court find that Welti (individually and doing business as Bopat Enterprises), engaged in conduct subject to penalty under IRC § 6701, and that injunctive relief is appropriate under IRC § 7408 to prevent him from engaging in further such conduct;
- C. That the Court find that Welti (individually and doing business as Bopat Enterprises), engaged in conduct that interferes with the enforcement of the internal revenue laws and substantially interferes with the proper administration of the internal revenue laws, and that injunctive relief against him is appropriate to prevent the recurrence of that conduct pursuant to IRC §§ 7407 and 7402(a);
- D. That the Court, pursuant to IRC § 7407, enter a permanent injunction prohibiting Welti (individually and doing business as Bopat Enterprises), from acting as an income-tax-return preparer;
- E. That the Court, pursuant to IRC §§ 7402, 7407 and 7408, enter a permanent injunction prohibiting Welti (individually and doing business as Bopat Enterprises), and his representatives, agents,

servants, employees, attorneys, and those persons in active concert or participation with him, from directly or indirectly:

- (1) Further engaging in any conduct subject to penalty under IRC § 6694, *i.e.*, preparing any part of a return or claim for refund that includes an unrealistic position;
- (2) Further engaging in any conduct subject to penalty under IRC § 6695, *i.e.*, failing to turn over a list of clients to the IRS upon request;
- (3) Further acting as a federal-income-tax return preparer or representing clients before the IRS;
- (4) Further engaging in any conduct that interferes with the administration and enforcement of the internal revenue laws, including asserting frivolous positions and engaging in abusive tactics designed to impede, obstruct, or delay lawful IRS investigations of clients; and
- (5) Further engaging in conduct subject to penalty under IRC § 6701, *i.e.*, assisting others in the preparation of any tax returns, forms, or other documents to be used in connection with any material matter arising under the internal revenue laws and which they know will (if so used) result in the understatement of income tax liability; and

F. That the Court, pursuant to IRC §§ 7402, 7407, and 7408, enter an injunction requiring Welte and Bopat Enterprises to contact all persons and entities for whom they prepared any federal income tax returns or other tax-related documents after January 1, 1997, or whom they represented in connection with a matter before the IRS after January 1, 1997, and inform those persons of the entry of the Court's findings concerning the falsity of representations made by Welte and Bopat Enterprises on clients' tax returns and in communications on behalf of clients to the IRS, and the fact that a permanent injunction has been entered against Welte (individually and doing business as Bopat Enterprises).

G. For such other and further relief as the Court deems appropriate.

GREGORY D. LOCKHART
United States Attorney

A handwritten signature in black ink, appearing to read "Michael R. Pahl", is written over a horizontal line.

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