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CLERK, U.S. DISTRICT COURT
EASTERN DISTRICT OF CALIFORNIA

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IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF CALIFORNIA

UNITED STATES OF AMERICA,

Plaintiff,

No. CIV S-03-1531 DFL GGH

vs.

JAMES O. MOLEN and SANDRA L.
MOLEN, d/b/a TOUCH OF CLASS
FLORIST,

Defendants.

ORDER and FINDINGS &
RECOMMENDATIONS

Introduction and Summary

The United States has brought this action against defendants¹ to obtain injunctive relief on account of defendants alleged failure to comply with the tax laws of the United States, inter alia, failing to withhold appropriate taxes from employees' pay, failure to make their own appropriate employer tax payments, and to file appropriate paper work regarding taxes that all

¹ Defendants believe the form of their names to be very significant to the outcome of this motion; that is, defendants demand that dashes and colons be utilized in their names, and the male defendant disclaims use of his last name, "Molen." The court does not share defendants' viewpoint on this matter, and is persuaded that no matter how called, the persons appearing before the undersigned on September 11, 2003 were in fact the defendants in the above captioned case. The court will simply utilize the term defendants, and this terms includes the defendants as named, as well as James-Orbin: and Sandra-Lyn:Molen, and any other combinations of punctuation marks used with such names.



1 employers routinely do file. The United States seeks a preliminary injunction to compel
2 defendants to pay all back taxes owed as well as orders to comply with all applicable provisions
3 of tax laws. The United States has disavowed use of the ordinary IRS administrative remedies
4 such as levy because “[l]ike Sisyphus with his boulder, absent an injunction the IRS will have to
5 spend considerable resources in a never-ending cycle of preparing substitute returns, assessing
6 taxes, and attempting to collect taxes through levies....”

7 This motion involves the request of the United States for a preliminary injunction
8 compelling the ultimate relief requested pending final adjudication. After consideration of the
9 unopposed motion,² the undersigned recommends that a preliminary injunction be entered as set
10 forth below.

11 With respect to the Clerk’s entry of default docketed on September 26, 2003, said
12 entry of default is vacated as defendants’ filing of September 11, 2003 (“Of the Specific Negative
13 Averment by the Affidavit of One...”) may have been perceived by defendants as their answer.
14 Defendants will be given one more opportunity to answer in conformance with Fed. R. Civ. P.
15 8(b) (the answering party must specifically admit or deny the allegations in the complaint as well
16 as raise affirmative defenses).

17 Facts

18 As defendants have not opposed the Motion for Preliminary Injunction on its
19 merits, the court finds the facts as set forth by the United States.

20 James O. and Sandra L. Molen are the sole proprietors of Touch of
21 Class Florist. Although they have about four employees to whom
22 they pay wages, the Molens have not withheld federal taxes from
23 their wages, made federal employment tax deposits, or paid federal
24 unemployment taxes since 1999. The last complete Employer’s
25 Quarterly Federal Tax Return (IRS Form 941) they filed was for
26 the fourth quarter of 1999; the last Employer’s Annual FUTA Tax
Return (IRA Form 940) they filed was for 1999, and the last Forms
W-2 they filed were for the year 1999.

² Defendants appeared but offered no argument or evidence whatsoever on the merits of the motion.

1 The Molens announced to the IRS their intention to stop
2 withholding and paying federal employment and unemployment
3 taxes in a letter dated August 3, 2000. They explained that based
4 on their patently frivolous misinterpretation of I.R.C. § 861, they
5 did not consider the compensation they paid to their employees to
6 be wages or gross income. The Molens summarized their position,
7 known as the § 861 argument, to the IRS as follows:

8 [T]he definition of gross income in the 16th
9 Amendment and . . . [I.R.C. §] 61 both reveal that
10 income must derived from a 'source.' . . . The U.S.
11 Congress set forth a section of law at . . . [I.R.C. §]
12 861 to deal with the term 'source'. . . [T]he
13 regulations for section 861 apply for the
14 determination of income that is taxable for the
15 purposes of the income tax. ...In light of the fact that
16 Touch of Class Florist has no evidence that any of
17 its vendors or suppliers were living abroad for the
18 years 1997, 1998, 1999 ... and none of the
19 remuneration was involved in any U.S. island
20 possession, then Touch of Class Florist hereby
21 claims that no gross income as paid, as defined by
22 the Rules of the Secretary of the Treasury.

23 The Molens further argued that the compensation they paid their
24 employees was not "wages," because "these individuals'
25 remuneration [was] paid to them while living in the United States."

26 The Molens instructed their employees, in a letter dated January
31, 2001, "DO NOT REPORT any of your actual income from the
Company [Touch of Class Florist] when filing your tax returns."
They told their employees in this letter that because they are a
"U.S. domestic employer hiring U.S. Citizens, all wages paid are
exempt from Federal income taxes ... [and] State income taxes" as
well as Social Security and Medicare taxes. The Molens advised
their employees that if "the IRS, State, or Social Security tries to
make a determination that you owe a tax on the income from the
Company, rest assured that it is a fraudulent attempt." For the
2000, 2001, and 2002 tax years, the Molens have issued their
employees IRS Forms W-2, Wage and Tax Statements, reporting
that they paid their employees \$0.

Not only did the Molens stop withholding and paying over
employment and unemployment taxes, they sought to recover the
taxes they had paid in 1997, 1998, and 1999. They filed IRS
Forms 941c, Supporting Statement to Correct Information,
changing the gross wages that they had previously reported for
1997 through 1999 to \$0. They also filed IRS Forms 843, Claim
for Refund and Request for Abatement, seeking refunds of federal
employment and unemployment taxes for 1997 through 1999. The
IRS erroneously refunded the Molens \$30,698.03 for employment

1 and unemployment taxes for 1997 through 1999.

2 The Molens' failure to obey the tax laws causes injury to the
3 United States Treasury. By refusing to withhold taxes from their
4 employees' wages, refusing to pay over employment taxes to the
5 IRS, and falsely claiming entitlement to a refund, the Molens have
6 cost the United States an estimated \$100,927.63 in lost revenue,
7 excluding penalties and interest, as of June 30, 2003. For each new
8 quarter in which they continue to flout the tax laws they cause an
9 additional estimated loss exceeding \$5,700 in federal income and
10 FICA taxes, every year results in additional loss exceeding \$3,700
11 in FUTA taxes. Recovering this lost revenue may prove
12 impossible as the Molens' liabilities surpass their ability to pay,
13 and because the IRS has limited resources available to determine
14 and collect taxes.

9 Discussion

10 Save for one traditional injunctive relief criteria (irreparable harm), which will be
11 discussed at length below, the court has no trouble with finding the traditional injunctive relief
12 factors, success on the merits and balance of hardships, in favor of the United States. See
13 Southwest Voter Registration Project et al. v. Shelley, __ F.3d __, _____ (9th Cir. 2003) (en banc)
14 setting forth the traditional injunctive relief factors. Those factors are *unopposed* by defendants.
15 Although the issue of irreparable harm is also unopposed, the court has more difficulty with this
16 factor in that the United States concedes that it has available remedies at law, albeit remedies
17 which the government would rather not utilize in this case.

18 Normally, a concession that adequate remedies at law remain to the party seeking
19 an injunction would sound the death knell of any injunctive relief request, especially in a tax
20 case. Sokolow v. United States, 169 F.3d 663, 665 (9th Cir. 1998). However, the United States
21 relies on 26 U.S.C. 7402(a):

22 The district courts of the United States at the instance of the United
23 States shall have such jurisdiction to make and issue in civil
24 actions, writs and orders of injunction, and of ne exeat republica,
25 orders appointing receivers, and such other orders and processes,
26 and to render such judgments and decrees as may be necessary or
appropriate for the enforcement of the internal revenue laws. The
remedies hereby provided are in addition to and not exclusive of
any and all other remedies of the United States in such courts or
otherwise to enforce such laws.

1 The undersigned acknowledges that the language: “The remedies hereby provided are in addition
2 to and not exclusive of any an all other remedies of the United States,” provides a strong
3 indication that Congress was deleting the traditional irreparable harm criteria from injunctive
4 relief actions brought by the United States. If an adequate remedy at law was sufficient to deny
5 an injunction to the United States in tax matters, the quoted language would be rendered
6 superfluous—and that is not something to be done lightly. On the other hand, one could validly
7 question whether an injunction to collect tax monies is so encompassed by specific statutes and
8 regulations that such an injunction would be “necessary or appropriate for the enforcement of
9 internal revenue laws.”

10 The court cannot find any authorized use of § 7402(a) in a published case ordering
11 the payment of past due tax monies. The United States has submitted an ordered preliminary
12 injunction (the form of which it prepared) in United States v. Thompson, CIV-S-03-1532 FCD
13 GGH, which did so. Seminal cases with explained reasoning which have utilized § 7402(a) are
14 ones such as: United States v. Ernst and Whinney, 735 F.2d 1296, 1300 (11th Cir. 1984) (district
15 court had power to enjoin unlawful “tax adviser” services under § 7402(a), but also holding that
16 traditional equitable principles are also at play in ultimate decision to issue injunction). Ernst
17 determined:

18 In addition to factual disputes that must be resolved, the decision to
19 issue an injunction under § 7402(a) is governed by the traditional
factors shaping the district court’s use of the equitable remedy.

20 Ernst, 735 F.2d at 1301

21 Foremost among the principles governing the use of the injunctive
22 remedy is the traditional requirement “that courts of equity should
23 not act ... when the moving party has an adequate remedy at law
and will not suffer irreparable injury if denied equitable relief.”
24 Younger v. Harris, 401 U.S. 37, 43-44, 91 S.Ct. 746, 750, 27
L.Ed.2d 669 (1971); O’Hair v. Hill, 641 F.2d 307, 310 (5th
25 Cir.1981). In determining whether the IRS is entitled to an
injunction in this case, it will be necessary for the district court to
26 examine the extent to which its interests are protected by available
legal remedies.

1 Ernst, 735 F.2d at 1301 (n.11).

2 Collection of past due tax monies, as the United States concedes, is encompassed
3 by specific remedial statutes which govern the usual procedures to collect such monies. See e.g.,
4 26 U.S.C. §§ 6201 et seq. (assessments), 6321 et seq. (liens), 6330 et seq. (levy), 6751 (penalties).
5 However, this case is one of those extraordinary cases in which the usual methods of collecting
6 monies is not adequate. First, from their non-opposition on the merits, and the groundless
7 arguments made on irrelevant technicalities, it appears to the court that defendants' main concern
8 is simply to obstruct efforts of the IRS to perform its job and collect lawful revenue, rather than
9 to litigate any bona fide tax law contention. Relegating the government to its usual remedies
10 would simply feed into this plan in that obstruction would continue not only for past debts owed,
11 but also future ones. Each year's levy or assessment would be subject to stall tactics and the like
12 until such time, as the United States points out, the monies owed would dwarf any ability to pay
13 by defendants. Moreover, the ordinary taxpayer would be penalized by having to fund such
14 obstructionist tactics vis-a-vis non-ending activity on defendants' cases by government
15 employees. Finally, it is not only the individual tax owed by defendants themselves which is at
16 issue. Defendants are setting up a situation where their employees may be penalized, temporarily
17 or permanently, by defendants' failure to pay the employees' payroll taxes (including Social
18 Security). See Declaration of Joseph F. Schiendl, Jr.; see also authorities cited at page 9 of the
19 United States' moving papers: taxpayers must pay all of their federal tax regardless of the
20 employer's failure to withhold, social security records will become confused, and unaware
21 employees may fail to pay quarterly social security taxes due and the like). Constant omissions
22 of payment by defendants over the years will result in an administrative snafus at the very least.
23 In light of the above, the undersigned does not believe that the usual remedies are adequate.

24 Conclusion

25 Having found that the United States has shown that it will likely succeed on the
26 merits, that defendants do not dispute that the balance of hardships tips squarely in favor of the

1 United States, and that the United States and third parties will suffer irreparable harm because the
2 remedies at law are inadequate, therefore, the undersigned recommends that a preliminary
3 injunction issue in the following form:

4 1. That defendants fully comply with the tax payment, withholding and reporting
5 requirements set forth in 26 U.S.C. § § 3101, 3102, 3111, 3301, 3402, 6011 and 6041;

6 2. No actual *past* payment of taxes, interest and penalties allegedly due will be
7 ordered paid in this preliminary injunction;

8 3. No security need be posted by the United States;

9 4. Defendants (individually and doing business as Touch of Class Florist or any
10 other name or using any other entity), and their representatives, agents, servants, employees,
11 attorneys, and those persons in active concert or participation with them, are enjoined from
12 failing to withhold and pay over to the IRS all employment taxes, including federal income,
13 FICA, and FUTA taxes, required by law.

14 5. Defendants shall file timely employment tax returns, including Forms 940 and
15 941, with the IRS, and file timely Forms W-2 with the Social Security Administration (SSA) and
16 send copies of such returns and Forms W-2 to counsel for the United States at the same time that
17 he files the originals.

18 6. Effective immediately, pending final adjudication of this action, within three
19 days of each business payroll, defendants shall make employment tax deposits with their bank
20 and send by fax to IRS Revenue officer Charles Delao at 530-343-2438, a receipt for each
21 employment tax deposit;

22 7. Defendants shall amend and correct their Form 941 for all quarters of 2000-
23 2003.

24 8. Defendants shall file with the SSA and issue to his employees amended Forms
25 W-2 for 2000 and send copies of these Forms W-2 to counsel for the United States at the same
26 time that he files the originals.

1 9. Defendants shall within ten days of the date of this Order deliver to all of his
2 current employees, and any former employees employed at any time since January 1, 2000, a
3 copy of this court's findings and preliminary injunction. Defendants shall bear all expenses
4 associated with this mailing. He must file a sworn certificate of compliance, swearing that he has
5 complied with this portion of the order, within twelve days of the date of this Order.

6 10. Defendants shall within ten days of the date of this Order post and keep
7 posted in one or more conspicuous places on his business premises where notices to employees
8 are customarily posted, a copy of this court's findings and preliminary injunction.

9 These findings and recommendations are submitted to the United States District
10 Judge assigned to the case, pursuant to the provisions of 28 U.S.C. § 636(b)(1). Within twenty
11 days after being served with these findings and recommendations, any party may file written
12 objections with the court and serve a copy on all parties. Such a document should be captioned
13 "Objections to Magistrate Judge's Findings and Recommendations." Any reply to the objections
14 shall be served and filed within ten days after service of the objections. The parties are advised
15 that failure to file objections within the specified time may waive the right to appeal the District
16 Court's order. Martinez v. Ylst, 951 F.2d 1153 (9th Cir. 1991).

17 The court further ORDERS that the default entered against defendants is vacated
18 and that defendants shall file an answer specifically admitting or denying the allegations of the
19 complaint within ten days of the filed date of this order.

20 DATED: September 30, 2003.

21 
22 GREGORY G. HOLLOWES
23 UNITED STATES MAGISTRATE JUDGE

24 GGH:gh:035
25 molen.pi
26

United States District Court
for the
Eastern District of California
October 1, 2003

* * CERTIFICATE OF SERVICE * *

2:03-cv-01531

USA

v.

Molen

I, the undersigned, hereby certify that I am an employee in the Office of the Clerk, U.S. District Court, Eastern District of California.

That on October 1, 2003, I SERVED a true and correct copy(ies) of the attached, by placing said copy(ies) in a postage paid envelope addressed to the person(s) hereinafter listed, by depositing said envelope in the U.S. Mail, by placing said copy(ies) into an inter-office delivery receptacle located in the Clerk's office, or, pursuant to prior authorization by counsel, via facsimile.

Rex K Lee
United States Department of Justice
Tax Division
PO Box 683
Ben Franklin Station
Washington, DC 20044-0683

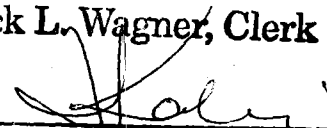
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