**UNITED STATES TAX COURT**
**WASHINGTON, DC 20217**

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| DRILL RIGHT CONSULTANTS, LLC, | ) | |
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| Petitioner(s), | ) | |
| | ) | |
| v. | ) | Docket No. 16986-14. |
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| COMMISSIONER OF INTERNAL REVENUE, | ) | |
| | ) | |
| Respondent | ) | |
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**O R D E R**

This worker-classification case remains in pretrial mode. Drill Right Consultants has moved for an order shifting the burden of proof in this case and relies on cases that discuss situations in which we have shifted the burden of proof to the Commissioner in deficiency proceedings. Drill Right carefully observes that worker-classification cases might be different because we have held that informal IRS determinations are enough to give us jurisdiction. *See SECC Corp. v. Commissioner*, 142 T.C. 225, 231 (2014). It notes perspicaciously that we did not address in *SECC* "whether the presumption of correctness attaches to an informal determination."

That's the question we have to analyze here.

## Background

There hasn't been a trial of this case, but Drill Right alleges in its motion papers that it has been the victim of sore bureaucratic abuse. It identifies itself as an LLC owned by William Sewell, who has been in the business of supplying temporary workers to the oil-services industry for many years. For all of those

years, including 2010-2013, Drill Right acts as a labor-market middleman. It finds qualified workers for oil-field operators in the Permian Basin -- welders, drivers, and the like -- tells them where to go if they want the work, and to take their tools with them. The workers get hourly wages and Drill Right collects a small margin on what they are paid. At the end of the year, the company sent out 1099s and not W2s, because it takes the position that the workers are independent contractors and not its employees. If Drill Right is right, it is a facilitator for the oil field's equivalent of a Hollywood production team of the sort we analyzed in *Quintanilla v. Commissioner*, 111 T.C.M. 1017 (2016).

Its current troubles began when the Texas Workforce Commission called and insisted that Drill Right owed unemployment-compensation tax, not just for Sewell and other core staff, but for all the workers that it had long treated as independent contractors. That tax is not large -- at least in comparison to the cost of lawyers skilled in the field -- and Drill Right made the business decision to just pay it and move on.

But government agencies talk to each other. At some time after Drill Right began paying off the Workforce Commission, an IRS revenue officer found out. According to Drill Right, the revenue officer used the Commission's filings to prepare a substitute return under I.R.C. § 6020(b) for federal payroll taxes from 2010 through 2014. And, since such taxes are not subject to deficiency procedures but may be summarily assessed, the revenue officer just went straight to collection without pausing for a normal examination and administrative appeal.

Federal payroll taxes are not small, even compared to the cost of a lawyer skilled in the field, and Drill Right found itself facing a bill of over $2.5 million with possibly worse consequences for later years. It filed a petition under I.R.C. § 7436(a), which gives taxpayers the right to come to Tax Court for relief if "in connection with an audit of any person, there is an actual controversy involving a determination by the Secretary as part of an examination that—(1) one or more individuals performing services for such person are employees of such person . . . ." Filing the petition led to the abatement of the assessments. I.R.C. § 7436(d).

But who has the burden of proof on the question of the proper classification of Drill Right's workers?

**Discussion**

The textualist answer to this question is easy. Rule 142(a)(1) says that "The burden of proof shall be upon the petitioner, except as otherwise provided by statute or determined by the Court." Our rules put the burden on the Commissioner when he asserts an increased deficiency or raises an affirmative defense, but this isn't a deficiency case and there aren't any affirmative defenses at play.

The Code itself has a number of sections that govern the burden of proof in specific situations (none of which are relevant here), but also addresses the burden of proof in a general way in I.R.C. § 7491. That section shifts the burden to the Commissioner when a taxpayer

> introduces credible evidence with respect to any factual issue relevant to ascertaining the liability of the taxpayer for any tax *imposed by subtitle A or B* . . . .

But notice the italicized phrase: Subtitle A is about income tax; subtitle B is about estate and gift taxes. The employment taxes that vex Drill Right are imposed by neither title.

So, the Commissioner wins.

Or does he?

Drill Right argues that there is a judge-made exception to these rules -- that the presumption of correctness does not apply to a "naked assessment." The paradigmatic case is *Scar v. Commissioner*, 814 F.2d 1363, 1370 (9th Cir. 1987), where the IRS sent a notice of deficiency to a taxpayer determining a large deficiency from a tax shelter that had no connection to the taxpayer or his return. That made the notice so arbitrary as to make it invalid. Because our deficiency jurisdiction depends on a valid notice and a timely petition, the Ninth Circuit held that we should have dismissed the taxpayer's case for lack of jurisdiction. *Id.*

Drill Right doesn't want *that* -- it wants us to find instead that its classification of workers was correct, and for that we need jurisdiction. It just wants to shift the burden to the Commissioner so that he has to show that his determination was correct. It cites to *Portillo v. Commissioner*, 932 F.2d 1128, 1133 (5th Cir. 1991), where the Fifth Circuit held that even where the

Commissioner has issued a valid notice of deficiency, he still has the burden of proof in a deficiency case to show a taxpayer received unreported income where that taxpayer shows that "the assessment is arbitrary and erroneous."

*Portillo*, however, is distinguishable: Right now, there is no assessment against Drill Right, naked or clothed, because the Commissioner has abated the one he made,[1] and our review is not about unreported income but an entirely unrelated and different factual issue -- the proper classification of Drill Right's workers from 2010 through 2014. After *Portillo* and similar cases were written, Congress considered the issue of the burden of proof, and did shift it, but only in some cases and for some issues.

Cases to determine the proper classification of workers to determine whether a taxpayer owes employment tax are not among them.

It is therefore

ORDERED that petitioner's motion to shift the burden of proof is denied.

**(Signed) Mark V. Holmes**
**Judge**

Dated: Washington, D.C.
January 28, 2019

[1] A trial judge must always hesitate before pointing out an infelicity of expression by a court that reviews his work. But the phrase "naked assessment" doesn't really work even in the usual deficiency case. "Assessment" has a precise definition in tax law -- it's the recording of a liability in the records of the IRS. I.R.C. § 6203. Absent unusual situations like a jeopardy assessment, there is no assessment of a deficiency while a deficiency case is underway. So we think a more precise understanding of the Fifth Circuit's holding in *Portillo* is that the Commissioner's *determination* on a particular issue might be arbitrary.