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CHOOSING TAX PROCEDURES FOR TACTICAL ADVANTAGE

*John L. Carey**

Introduction

The very nature of the self-assessment of taxes devised by the United States Congress invites and spawns disagreement. This disagreement might well finally escalate into a pitched fight, with the Supreme Court as the battlefield and millions of dollars in the balance. From the outset of an official dispute over the self-assessment, it is most important for the lawyer to assume the aggressive posture of an advocate. Certified public accountants and tax attorneys too often either forget this need or feel that more bees can be attracted by honey than by vinegar. The Treasury Department often stings like a bee, but is never attracted by an attitude of "honied" condescension.

This is not to say that the tax advocate should ignore good manners in dealing with tax collectors and heap Biblical scorn upon them. Rather, a firm and frank approach will achieve the desired result: an equitable resolution of the client's tax assessment. By playing "Mr. Nice," the lawyer is saying in effect, "the Treasury only imposes taxes on difficult people, and the law as written means nothing." This view insults the intelligence of all dedicated, sophisticated Revenue employees. There will be no reluctance on their part, however, to file away, for later use against your client, all the information you give, but the hoped-for settlement has undergone serious, if not fatal, setbacks. Since one cannot buy "out" with a smile, he must win his client's settlement with preparation and advocacy that radiate professional competency.¹

Cooperation Between Advisors

The single most essential factor in successful tax litigation is the require-

* B.S., St. Ambrose College, 1941; LL.B., Georgetown University, 1948; LL.M., Georgetown University, 1950; former Trial Counsel for the Cincinnati Region of the Internal Revenue Service; partner, *Oare, Thornburg, McGill & Deahl*, South Bend, Indiana.

¹ Except for the extremely small dependency or expense cases which, from a financial point of view, must ordinarily be settled upon the Internal Revenue agent's terms, the techniques in a small case are substantially the same as those employed in a large case.

ment of mutuality between the attorney and the certified public accountant. Obviously, each has very unique functions to perform, but it is the joint effort that results in successful termination of a tax dispute.

Certain functions more properly should be performed by one than by the other. Attorneys should not prepare federal income tax returns, especially if they do not have a strong accounting background. This preparation is essentially an accounting function. While legal questions are often involved as to how certain items are to be handled, once these determinations are made, the actual preparation of the return is not within the professional province of an attorney. Of course, not all attorneys agree. Among attorneys specializing in taxation, however, there is almost unanimous support for this position.

All initial contacts with the Internal Revenue agent should be made by the CPA and not the taxpayer.

The taxpayer should have absolutely minimal contacts with the Internal Revenue agent. A fortuitous remark, the change of a facial expression or, as is more often the case, an innocent answer to a technical question which the taxpayer does not fully comprehend is the prelude to many unwarranted and time-consuming examinations and explanations.² The attorney should be briefed as to any extraordinary issues raised by the agent, but should not officially come into the case at this time. Disclosure of his presence has somewhat the same effect as a fire-fighting batallion standing by at a marshmallow roast: it causes more alarm than benefit. Despite the CPA's best efforts, settlement with the Internal Revenue Service may be impossible.

Two questions then arise:

1. What administrative route shall be taken?
2. Assuming no administrative settlement, what court should be selected?

Actually, if these questions arise only after receipt of a Statutory Notice of Deficiency (the "90-day letter"),³ the attorney has not been planning his client's strategy thoroughly. The selection of a possible judicial forum should be uppermost in his mind from the very outset of any controversy with the IRS. Many of the tactical decisions which he must make at the administrative level will necessarily be influenced if not controlled by the forum which he intends to employ should litigation become necessary.

Assuming that the appropriate forum has been tentatively chosen ("tentatively" because decisions valid today may be totally inappropriate at the time the judicial forum must be finally chosen),⁴ he must decide his administrative strategy.

² All pertinent records and books belonging to the client which the agent wishes to examine should be sent to the certified public accountant's office. The agent appreciates the better working conditions available there and the ready answers to questions which arise during the examination.

³ Int. Rev. Code of 1954, § 6212; INT. REV. CODE OF 1954, § 6213. Both the SNOD and the "90-day letter" describe the launching of the tax dispute into the administrative and judicial orbits. The terms will be used interchangeably within this article.

⁴ See *Southern Maryland Agricultural Ass'n v. United States*, 16 F.R.D. 100 (1954). The plaintiff sought leave to dismiss his tax suit without prejudice from the District Court, apparently because of the Fourth Circuit's reversal of a favorable precedent rendered by this same District Court. He was intending to seek the Court of Claims to avoid the Circuit's mandate. The District Court held the choice of forum irrevocable and denied his motion to dismiss without prejudice.

*The informal conference:*⁵ The attorney should always take advantage of this opportunity, even though he might well be convinced that it will not result in a settlement of the instant controversy because (i) his position, while supported by the courts, has been non-acquiesced in by the Commission;⁶ (ii) the regulations are against his position;⁷ or, (iii) the issue is one that the national office of the IRS has reserved the right to adjudicate.⁸

Even though his case fits one of these categories, the attorney does not waste time in going to the informal conference. It is at this level that an attempt should be made to correct the record. It is amazing how many times erroneous information finds its way into the work papers of the Revenue agent. Once an error is reduced to paper, a later effort to correct it is an awesome task. The error seems to enjoy a greater dignity, almost a conclusive presumption of correctness, merely by virtue of its having been written. These errors in the record are not the result of either malice or slipshod performances on the part of the examiner, but rather flow from the lack of an appreciation by the agent of the overall operation of the particular client's business. Too, individuals viewing the same facts from their own perspectives will invariably reach grossly different results.

After the informal conference, the 30-day letter is received.⁹ It is at this point that the first important tactical decision must be made: to which Appellate Staff should the appeal be taken?

*Choosing the appellate staff:*¹⁰ Experience has indicated that it may be more desirable to argue a given issue before one appellate staff than before another. For example, if the litigation involves a considerable amount of money — officers' salaries or an unreasonable accumulation of surplus — the attorney should choose the appellate staff which has the greatest familiarity with large financial transactions. On the other hand, a more subtle factor may prove decisive. Certain personality clashes or other obstacles to meaningful communication between the practitioner and the agency people are unavoidable.

A further requirement is that of honoring the Technical Advisor's recommended proposed settlement.¹¹ If the Technical Advisor's settlement is repudiated by the Chief of the Appellate Division, the practitioner is placed in the untoward position of selecting one of two great evils: (1) raising the recommended proposed settlement modestly, thereby appeasing the Chief of the Appellate Division and consequently arousing the ire of the Technical Advisor to whom he had presumably given his "highest figure," thus destroying imme-

5 Rev. Pro. 64-38, 1964 INT. REV. BULL. No. 38, at 40.

6 United States v. City Loan & Savings Co., 287 F.2d 612 (6th Cir. 1961).

7 Regulations are generally binding upon both the taxpayer and the Commissioner. *Helvering v. Reynolds Tobacco Co.*, 306 U.S. 110 (1939).

8 INT. REV. CODE OF 1954, § 501(c), termination of exempt status for organizations.

9 Treas. Reg. § 601.105(d)(1)(iv), 12 Fed. Reg. 12688 (1961). As a result of the taxpayer's disagreement with the Service's conclusion reached at the informal conference (*supra* note 5), and his refusal to sign a waiver of restrictions on assessment and collection of tax, he will receive a summary of the conference in report form, together with a letter explaining the deficiency and allowing the taxpayer thirty days in which to select his next move.

10 Treas. Reg. § 601.106, 12 Fed. Reg. 12688 (1961). See also, Cullen, *Functions and Operations of the Appellate Division*, 29 TULANE L. REV. 504 (1955).

11 The Technical Advisor is the administrative hearing officer that presides over the informal conference.

diately the hope of any further rapport with him in future controversies involving this or any other client; or, (2) sticking to the settlement agreed to by the Technical Advisor and trying the case at a cost well in excess of an obtainable "sweetened" settlement figure.

If the attorney has chosen a city other than the home city of his District Director as the site of his next skirmish, how does he effect a transfer of the case to that Region? The procedure is simple — he does not file a protest to the 30-day letter. Shortly thereafter, the Audit Division determines that a protest in fact is not filed. It will then proceed to the issuance of the Statutory Notice of Deficiency. Upon receipt of the 90-day letter, a petition is filed with the Tax Court, including a request that City *X* be designated the place of hearing.¹² It is imperative that the request for designation of place of hearing be prepared by the taxpayer's attorney and filed with the petition; otherwise the respondent's attorney will file the request with his answer, asking for a hearing in the home city of the District¹³ and all planning will probably have gone for nought.

Upon receipt of the petition, if the attorney's request for a City *X* hearing was filed appropriately, representatives of the United States in the home city will transfer jurisdiction of the case, and both the administrative and the legal file, to City *X*.¹⁴

Tactical Advantage of Audit Division Issuing 90-Day Letter

Let us assume that the agent's determination is not the best possible position from a legal standpoint for the Government on the particular issue in controversy. It must be remembered that if a protest is filed, the Appellate Division will be the agency "arm" which prepares the 90-day letter, whereas, if the attorney does not file a protest, the Audit Division will prepare the letter. The personnel of the Audit Division are under a tremendous work-load pressure, which pressure precludes the legal attention necessary to a 90-day letter. The Appellate Division, however, is able to devote greater time and effort to the preparation of its 90-day letters.

The Government can change its position after the issuance of the 90-day letter. However, because a new determination made *after* the issuance of the 90-day letter will not have the presumed correctness of the original determination,¹⁵ the Government is at an extreme tactical disadvantage.¹⁶ The client's interests are better served by allowing the Audit Division to draft its letter. Thus, the Government is committed to a legal posture from which it will be reluctant to depart for fear of leaving the safe harbor of the correctness pre-

¹² Treas. Reg. § 601.106(e)(1), 26 Fed. Reg. 12688 (1961).

¹³ Treas. Reg. § 601.106(e)(2), 26 Fed. Reg. 12688 (1961).

¹⁴ The legal file contains the taxpayer's petition to the Tax Court while the administrative file contains the agent's work papers and related information dealing with the assessment of the tax.

¹⁵ T. C. R. 32: "Burden of Proof: The burden of proof shall be upon the petitioner, except as otherwise provided by statute, and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent.

¹⁶ This is nothing more than the Hornbook concept of "he who pleads must prove." Thus the Commission hesitates to answer the taxpayer petition with any new matter.

sumption. A review of the reported cases will reveal very few instances of government-raised affirmative issues decided in its favor.¹⁷

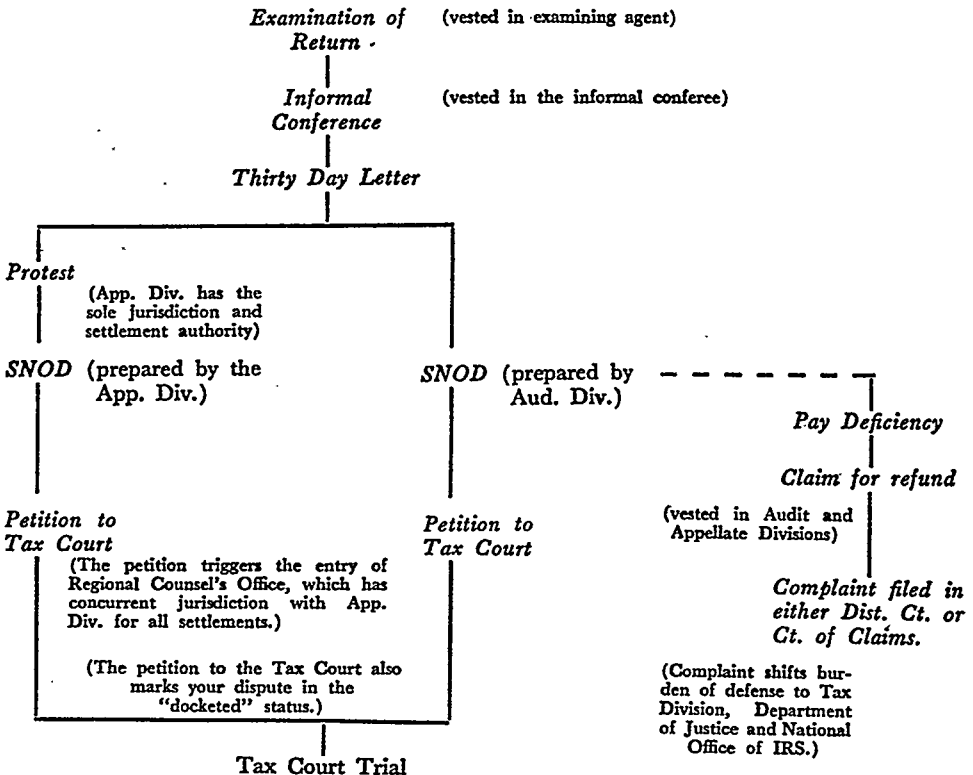
Settlement Authority¹⁸

If the dispute comes before the Appellate Division in a non-docketed status, as a result of filing a protest, the Appellate Division has sole settlement jurisdiction at this stage of the proceeding. On the other hand, if settlement negotiations are conducted in the docketed status either because the case was not protested and a petition to the Tax Court was filed or after the Statutory Notice of Deficiency issued by the Appellate Division has been received, then the Appellate Division and the Regional Counsel's Office have concurrent settlement jurisdiction.¹⁹ Because the concurrence of the two entities within the Treasury Department is necessary for settlement, many practitioners to save time bypass the Appellate Division in the predocketed status. This is especially so in disputes involving essentially legal issues as opposed to questions of fact.

17 See, e.g., *Tex.-Penn. Oil Co. v. Comm'r*, 83 F.2d 518 (3rd Cir. 1936); *Thomas Wilson*, 25 T.C. 1058 (Feb. 21, 1956); *Sheldon Tauber*, 24 T.C. 179 (May 9, 1955). *But see* *W. H. Weaver*, 32 T.C. 411 (May 29, 1959), *aff'd*, *Bryan v. Comm'r*, 281 F.2d 238 (4th Cir. 1960).

18

Settlement Authority



19 During the period and only during the period the Tax Court is sitting in a particular city, sole settlement jurisdiction is vested in the Regional Counsel. This can range from one day to two weeks, depending upon the docket set for that city.

Following an analysis of the issues raised by the Audit Division in its report, if the attorney does not anticipate that new decisive issues will be raised by the Commissioner and if there are no essentially factual issues involved, he should then file a protest. This saves time and better serves the client's interests. The Appellate Division in the home District will retain jurisdiction of the dispute. Similarly, the local Regional Counsel's Office will normally try the case regardless of where the case is ultimately docketed for trial.

The preparation of the protest, which is the route to the Appellate Division of the home city, deserves some comment. The discussion of the metamorphosis of a tax case indicated that preparation of the federal income tax return was primarily the responsibility of the CPA. The major burden of preparing the protest, on the other hand, should be assumed by the attorney. Protests half-heartedly prepared inevitably return to torment the taxpayer if the case is actually tried. Further, it should be remembered that protests are signed under penalty of perjury.²⁰ This fact alone should warrant acute consciousness of every detail of the protest.

The next step is the Appellate Division, either in the non-docketed status as the result of filing a protest, or in a docketed status as the result of filing a Petition to the Tax Court. Except for the fact that in a docketed status a representative of the Chief Counsel's Office will be present and will have concurrent settlement authority, there is absolutely no difference in the settlement procedure.

One of the snares that often traps the unwary advocate in settlement conferences before the Appellate Division is the practice of immediately complying with requests by the Technical Advisors for affidavits²¹ prior to the time of settling the entire tax dispute. One should assure the appellate staff that the facts are true but with the further understanding that the necessary affidavits will be procured upon final settlement. If a settlement in principle is agreed upon, the promised affidavits should be immediately obtained: no settlement, no affidavits. The loosely-drafted affidavit, like the poorly-drawn protest, may come back to plague the taxpayer and his counsel at the trial.

If the attorney files a protest and conference with the Appellate Division indicates that settlement is impossible, the next step in the procedure is the issuance of the Statutory Notice of Deficiency by the Appellate Division.²² Within ninety days after receipt of this letter, the choice of legal forum must be finally made. Obviously, if the attorney has waited until this time to decide the all-important strategy, he has not been adequately representing his client.

Choice of Forum

The forum should be tentatively selected early in the proceedings. The three courts open to the client in a tax dispute are: (1) the Tax Court; (2) the federal district court; and (3) the Court of Claims. Each court has a definite

²⁰ I.R.S. Publication No. 5 (Rev. 9-61).

²¹ Treas. Reg. § 601.106(c) (1954), as amended by Fed. Reg. 12688 (1961): "Testimony under oath is not taken, although matters alleged as fact may be required to be submitted in the form of affidavits. . . ."

²² *Supra* note 1. The attorney is now strategically situated just as if he had not protested. See note 18 *supra*.

usefulness in specific situations. The trick is to choose the correct one at the correct time. However, even if one specific court is the right one at the right time, resort may be foreclosed by limitations upon its jurisdiction. For example, the Tax Court has jurisdiction only over actions involving income, estate and gift taxes.²³ On the other hand, questions involving excise or employment taxes must be tried in the Court of Claims or in the district court. The district court and the Court of Claims have concurrent jurisdiction over any allegedly improper assessment of federal taxes. Immediate payment of the asserted tax liability is a prerequisite for their jurisdiction. If the taxpayer can afford to pay and seek a refund, all three forums are available to him. If he cannot, he must bring his action in the Tax Court. Finally, the jurisdiction of these three courts no longer depends upon the amount in controversy.²⁴

Precedents

The most important threshold question is: where are the most favorable precedents? This question can only be answered by thorough research. Perhaps this can best be illustrated by an example involving an issue much litigated currently.

In recent years, the Internal Revenue Service has on a number of occasions questioned the nature of payments by employers to the widows of deceased employees. Most employers routinely treat such payments as a business expense and claim deductions upon their tax returns.²⁵ But the widows almost invariably report the payments as gifts²⁶ and do not pay income tax upon them. The Service has with regularity challenged the position of the widows. In 1960, the United States Supreme Court in the landmark case of *Duberstein v. Commissioner*²⁷ announced a principle which, by extension, controls the "widow payment" situation. This case involved an alleged gift of a Cadillac automobile to a business associate. The Court rejected the Commissioner's argument that a single test could, as a matter of law, resolve the question in all instances,²⁸ and left the issue to the trier of facts.²⁹

The Tax Court decisions since *Duberstein* have consistently been unfavorable to the taxpayer,³⁰ while almost all decisions rendered by the district courts have been favorable.³¹ Complicating the matter is the fact that the Courts of Appeals for the Sixth³² and Eighth Circuits³³ have rendered opinions either

23 INT. REV. CODE OF 1954, § 7442; Treas. Reg. § 301.6512-1 (1956).

24 28 U.S.C. 1346, 72 Stat. 348 (1958); INT. REV. CODE OF 1954 § 7402.

25 INT. REV. CODE OF 1954, § 162(a).

26 INT. REV. CODE OF 1954, § 102(a).

27 363 U.S. 278 (1960).

28 *Id.* at 284.

29 *Id.* at 287-90. See, e.g., Pelisek, *Conflict in Widows' Cases Continues as Supreme Court Denies Certiorari*, 18 J. TAXATION 118 (1963).

30 Estate of Mervin G. Pierpont, 35 T.C. 65 (Oct. 19, 1960), *rev'd sub nom.*, Poyner v. Comm'r, 301 F.2d 287 (4th Cir. 1962); H. D. Penick, 37 T.C. 999 (Feb. 27, 1962). See notes 32 and 33, *infra* for Tax Court Decisions reversed by the Circuit Courts.

31 Rice v. United States, 197 F. Supp. 223 (E.D. Wis. 1961); Corasaniti v. United States, 212 F. Supp. 229 (D. Md. 1962). *Contra*, Gaugler v. United States, 204 F. Supp. 493 (S.D.N.Y. 1962), *aff'd* 312 F.2d 681 (2d Cir. 1963).

32 Kuntz' Estate v. Comm'r, 300 F.2d 849 (6th Cir. 1962).

33 United States v. Frankel, 302 F.2d 666 (8th Cir. 1962) and Olsen's Estate v. Comm'r, 302 F.2d 671 (8th Cir. 1962).

reversing Tax Court decisions in favor of the Commissioner or affirming the district court judgments for the widow; further, the Third Circuit³⁴ and, most recently, the Seventh Circuit³⁵ have rendered three decisions favorable to the Government. On the basis of the present state of the law, an attorney handling a widow payment case would have to have exceedingly persuasive reasons for advising his client to bring his case in the Tax Court.³⁶ At the moment, the climate in the district courts is much more favorable.³⁷

However, it is at this juncture that some of the earlier decisions as to forum become undone. For an example, an attorney working within the Seventh Circuit jurisdiction on such a widow's case decides, early in the proceeding, together with the CPA, that if the issue could not be settled, the client would pay the tax and sue for a refund in the district court. The widow is informed of this and complies with the request to keep her finances liquid. The dispute is not settled, the Statutory Notice of Deficiency is received, the widow pays the tax and the claim for refund is filed. Then, the Seventh Circuit unleashes its adverse decision, making foolhardy pursuit of the original plan to sue in the district court. Obviously, the Court of Claims, which to date has taken no position upon widows' cases, becomes the more appropriate forum.

It should be noted that appeal from the Court of Claims is only to the United States Supreme Court.³⁸ Hence, when he files in that court, the attorney is, in effect, "going for broke," inasmuch as nine out of ten times the decision rendered by the Court of Claims is final. Alternatively, if avoiding payment of the tax is the important consideration, an appeal to the Tax Court could perhaps be justified. If the client lives in the Sixth or Eighth Circuits, he still might go to the Tax Court since an unfavorable decision would most likely be overturned on appeal.³⁹

If research into the applicable precedents does not conclusively dictate the choice of forums, then certain other factors should be weighed. From a financial standpoint the Tax Court may be the best forum. Only in the Tax Court is it unnecessary to pay the tax prior to testing the Government's position.⁴⁰ Moreover, even if the taxpayer has the funds, he may decide that he would rather use the money during the period of litigation. It is also important to remember that the statutes now allow the taxpayer to pay the deficiency

34 *Smith v. Comm'r*, 305 F.2d 778 (3d Cir. 1962) and *Martin v. Comm'r*, 305 F.2d 290 (3d Cir. 1962).

35 *Fritzel v. United States*, 339 F.2d 995 (7th Cir. 1964).

36 *Supra* note 31.

37 *Supra* note 32.

38 28 U.S.C. § 2101(c), 63 Stat. 104 (1949).

39 Why does the Tax Court not follow decisions of particular Courts of Appeal? The Tax Court views itself as a national court and while giving considered judgment to the views of the reversing court will not follow that court in a subsequent case even if appeal will be to the reversing circuit. For an excellent summary of the Tax Court's position, see, *e.g.*, Arthur L. Lawrence, 27 T.C. 713 (1957).

There has been sentiment, both in Congress and in the ABA for a rule of law requiring the Tax Court to change its views if it is overruled by the Court of Appeals. This problem has not been solved and is one of the "sore spots" from the taxpayer's standpoint in the administration of the federal tax laws.

40 INT. REV. CODE OF 1954 § 6213 and Treas. Reg. § 301.6213-1 (1954), as amended, T. D. 6585, 1962-1 CUM. BULL. 290-1.

after having filed a petition to the Tax Court.⁴¹ This procedure eliminates the interest cost inherent in a long Tax Court controversy.

Another factor in selecting the Tax Court is present where the issue is highly technical and intricate. Tax Court judges are experts in the tax field⁴² and may be better qualified to decide the point than would a lay district court judge. This expertise has been recognized by the courts on numerous occasions.⁴³ Also, the attorneys in the local Regional Counsel's Office are always available for help and discussion of your case. It is therefore possible to develop an excellent working relationship with these attorneys. Obviously, it is much easier mechanically to stipulate facts with an attorney who has gotten to know you and your method of presentation. Such a relationship is not available when the case is in the district court or in the Court of Claims since representatives of the Department of Justice, which handles tax cases in these courts, are not decentralized as are members of the Chief Counsel's Staff.⁴⁴

The Tax Court is much more likely to disregard strict rules of evidence than is the district court or the Court of Claims.⁴⁵ Thus, if the attorney has any doubts as to the admissibility of evidence under a strict interpretation of the rules, he should proceed in the Tax Court. Conversely, if the Government's case rests on evidence of questionable admissibility, then perhaps he should not choose the Tax Court.⁴⁶

The number of taxpayers who will choose to pay an arbitrary assessment by the Commissioner rather than expose their personal business affairs to public scrutiny is amazing. Should this sentiment become a major problem, the Tax Court⁴⁷ and the Court of Claims present excellent choices to avoid this valid

41 Treas. Reg. § 301.6213-1(b)(3) (1954), as amended, T. D. 6585, 1961-1 CUM. BULL. 290-1.

42 INT. REV. CODE OF 1954 § 7443(b).

43 INT. REV. CODE OF 1954 § 7482(a), which in fact reverses *Dobson v. Comm'r*, 320 U.S. 489 (1943), substituting in its stead the clearly erroneous rule:

JURISDICTION. The United States Courts of Appeals shall have exclusive jurisdiction to review the decisions of the Tax Court, except as provided in section 1254 of Title 28 of the United States Code, in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari. . . .

In respecting and acknowledging the expertise of the Tax Court judges, one is prompted to ask if this is a genuine deference to the opinion of an expert or but another shield behind which the Courts of Appeal might hide in sustaining the Tax Court finding? See *Huckins Tool and Die, Inc. v. Comm'r*, 289 F.2d 549 (7th Cir. 1961) and *Duval Motor Co. v. Comm'r*, 264 F.2d 548 (5th Cir. 1959).

The "law and fact" controversy has a long history of providing higher courts with a judicial glideway to a resolution more harmonious with their view of the case than that rendered by the court below.

44 28 U.S.C. 507, 63 Stat. 910 (1949).

45 It should be pointed out that the Court of Claims is not as strict as the district courts in this regard.

46 INT. REV. CODE OF 1954 § 7453 and T. C. R. 31(a). Though the evidentiary rules for the Tax Court are framed so as to reflect the rules in a non-jury trial in a federal district court, the district judges tend to be more "admissibility conscious." There is no doubt due to their daily living under the threat of reversible error for improper admissions in other litigated matters, whereas Tax Court judges are not concerned about reversals based upon admissibility of evidence.

47 Under the T. C. R. 26(a), the request for a trial at a particular city is incorporated within the petition to the Tax Court. See also, INT. REV. CODE OF 1954, § 7446 as to taxpayer convenience and expense.

INT. REV. CODE OF 1954 § 7458 clearly provides that Hearings shall be open to the public. This news blackout is the result of few paper-selling attractions being presented to the Tax Courts which warrant newspaper coverage.

and serious objection to "notoriety." Except for cases involving civil fraud or infamous personalities, tax trials in these two courts are ignored by the news gathering agencies. The fact that the Tax Court⁴⁸ and the Court of Claims hold their hearings in Washington⁴⁹ and distant cities adds to the lack of publicity.

Since the Government's lack of factual knowledge in most tax disputes is the taxpayer's greatest single asset, the discovery procedure is of great importance. In the Tax Court such procedures are extremely limited.⁵⁰ Discovery under the Federal Rules⁵¹ is, on the other hand, very broad. In fact, it is possible that some of the younger attorneys in the Department of Justice tend to abuse this power. In cases involving only a few thousand dollars, taxpayers have been required to spend several days gathering the information required to answer written interrogatories.⁵² The taxpayer can also resort to the discovery arsenal and should do so to neutralize the aggressive government attorney.⁵³ Of course, this inelegant maneuvering is especially regrettable when one realizes that the factual information requested by Justice in most instances was available or should have been available to them in the files of the Internal Revenue Service.

In many districts there is only one federal judge. This judge may be familiar to the taxpayer and his counsel. The Tax Court judge, however, is a modern day circuit rider with his home office in Washington and with annual or biennial calendars in selected cities throughout the United States. The district court will be more aware of local conditions and more likely to be a fairer judge of the credibility of local witnesses. Inasmuch as the district judge is a lay judge in the sense that he is not a tax specialist, he is not likely to be impressed with technical arguments that would result in an inequitable exaction of tax.

48 INT. REV. CODE OF 1954 § 7446.

49 Pavenstedt, *The United States Court of Claims as a Forum for Tax Cases*, 15 TAX L. REV. 1 (1959).

50 See T. C. R. 44-47 for subpoena and deposition provisions. Rule 28 provides for Tax Court pre-trial procedures. As a practice, the Tax Court judges quash this matter with a strictness that negatives, for all intent and purposes, the rules as written.

51 FED. R. CIV. P. 26-37.

52 FED. R. CIV. P. 33.

53 *Rule 33*: Within 10 days after service of interrogatories a party may serve written objections thereto together with a notice of hearing. . . .

The number of interrogatories . . . is not limited except as justice requires to protect the party from annoyance, expense, embarrassment or oppression. The provisions of Rule 30(b) are applicable for the protection of the party from whom answers to interrogatories are sought under this rule. . . .

Rule 26(b): Unless otherwise ordered by the Court as provided by Rule 30(b) or (d), the deponent may be examined regarding any matter not privileged, which is relevant . . . in the pending action. . . .

Rule 30(b): . . . or the Court may make any other order which justice requires to protect the party or witness from annoyance, embarrassment, or oppression.

Rule 30(d): . . . upon a showing that the examination is being conducted in bad faith or in such manner as unreasonably to annoy, embarrass, or oppress the deponent or party, the Court . . . may order . . . to cease forthwith . . . or . . . limit the scope and manner of the taking of the deposition. . . .

Statute of Limitations

If the attorney suspects that the Service might raise additional issues, not already raised by the agent, then the Tax Court should be avoided. A petition to the Tax Court tolls the Statute of Limitations and a new issue may be raised by an affirmative pleading in any stage of the Tax Court proceedings.⁵⁴ In the case of the district court and that of the Court of Claims, the Statute of Limitations continues to run and will bar the assessment of new deficiencies even though a claim for refund suit is pending. As a matter of fact, there are situations in which the attorney is able to let the statute on assessment expire before filing the refund claim or instituting his suit.⁵⁵

The party defendant in a tax suit in the district court may be either the United States of America or the District Director.⁵⁶ If the United States is named, the suit must be brought in the district where the taxpayer resided,⁵⁷ or, if a corporation is suing, where the corporation has its principal place of business.⁵⁸ By instituting suit against the District Director to whom the tax was paid, the plaintiff gains an additional venue since the District Director might have been transferred to another area by the Service or might have retired. The venue is still valid in the district court of his current residence.⁵⁹

The jurisdiction of the Court of Claims and that of the district courts in tax refund cases are identical.⁶⁰ There are a number of factors which make the Court of Claims preferable as a forum for the refund action: (a) the high probability of obtaining a decision which will not be reviewed;⁶¹ (b) the tendency of the court to disregard technical rules if the taxpayer can make a convincing case that he has paid more tax than good conscience entitles the Government to retain; and (c) the willingness of the Court of Claims on occasion to make "new law" to prevent such unjust enrichment. Since the operation of the Court of Claims is likely to be a mystery to most practitioners, its relative simplicity may come as a surprise. In this connection it is important to note that the hearing commissioners, who are extremely competent men, not only make findings of fact but conclusions of law. The findings and conclusions are then reviewed by the whole court.

Finally, in considering which court to choose, the advocate should consider some statistics. In his annual reports for 1961 and 1962, the Commissioner of Internal Revenue has noted the number of decisions for the Government, the number for the taxpayer and the number of "Partials" in each court for the last two fiscal years:

54 Treas. Reg. § 301.6503(a)-1 (1954).

55 An examination of the local district court docket might reveal a delay sufficiently long to overcome all Statute of Limitations problems.

56 28 U.S.C. § 1346(a)(1), 72 Stat. 348 (1958); *Eastman Kodak Co. v. United States* 292 F.2d 901, 903 (Ct. Cl. 1961). When both the United States and the District Director are named, the motion to dismiss one of the two will not be granted: *French v. United States*, 180 F. Supp. 773 (E.D.N.Y. 1960).

57 28 U.S.C. 1402(a)(1), 72 Stat. 1770 (1958).

58 28 U.S.C. 1402(a)(2), 72 Stat. 1770 (1958).

59 28 U.S.C. 1391(e)(1), 77 Stat. 473 (1963).

60 28 U.S.C. 1346, 72 Stat. 348 (1958).

61 28 U.S.C. 1254, 62 Stat. 928 (1948); U.S. SUP. CT. R. 41.

| | <i>Year Ended June 30, 1961</i> | | |
|-----------------|---------------------------------|---------------------|-----------------|
| | <i>For Government</i> | <i>For Taxpayer</i> | <i>Partials</i> |
| Tax Court | 313 | 108 | 159 |
| District Courts | 166 | 192 | 39 |
| Court of Claims | 17 | 24 | 5 |

| | <i>Year Ended June 30, 1962</i> | | |
|-----------------|---------------------------------|---------------------|-----------------|
| | <i>For Government</i> | <i>For Taxpayer</i> | <i>Partials</i> |
| Tax Court | 275 | 93 | 163 |
| District Courts | 192 | 213 | 44 |
| Court of Claims | 27 | 23 | 6 |

Jurisdictional Prerequisites of Refund Litigation

Jurisdictional requirements of tax refund litigation include:

- (a) Payment of tax;
- (b) Adequate and timely claim for refund;
- (c) Passage of time for administrative action on the claim; and
- (d) Timely filing of suit.

A. Payment of Tax

If your dispute involves income, estate or gift taxes, this requirement is particularly harsh: the tax must be paid in full for an entire taxable period.⁶² If the attorney is concerned with excise, withholding or F.I.C.A., where the only recourse is a refund suit, he need not satisfy the entire assessment. Such taxes are divisible.⁶³ For excise taxes, the taxpayer need pay only the tax for one divisible item or period rather than the entire assessment. Of course, there may be some dispute over what is the correct period. Probably he will need to satisfy the liability asserted with respect to only one employee in the case of withholding or F.I.C.A. taxes. In a very interesting recent district court case, it was held that only the tax and not the interest assessed need be paid as a prerequisite to jurisdiction.⁶⁴

Of course, payment of a tax can only be made when the Service has made an assessment. If the Internal Revenue Service is only considering an assessment, you cannot deposit funds with the District Director and immediately institute a suit for refund. One taxpayer unsuccessfully attempted this, possibly to avail himself of the discovery procedures incident to tax refund litigation in certain criminal tax matters.⁶⁵

B. Adequate and Timely Claim for Refund

After payment of the tax, the next major jurisdictional prerequisite is a timely claim for refund.⁶⁶ The general rule is that a claim must be filed in the

62 *Flora v. United States*, 362 U.S. 145 (1960).

63 *Steele v. United States*, 280 F.2d 89 (8th Cir. 1960). Payment of a single employee's liability is sufficient to invoke the District Court's or the Court of Claims' jurisdiction.

64 *Kell-Strom Tool Co. v. United States*, 205 F. Supp. 190 (D. Conn. 1962).

65 *Farnsworth & Chambers Co. v. Phinney*, 178 F. Supp. 330 (S.D. Tex. 1959). The Court granted the Government's motion to dismiss the action.

66 *Treas. Reg. § 301.6402-2* as amended by T.D. 6498, (1954), 1960-1 C.F.R. 301.

District Director's office where the tax was paid within two years after such payment, or within three years after the return was filed.⁶⁷ The period may be extended if it is waived⁶⁸ or if the claim is derived from a net operating loss or is based on a bad debt deduction.⁶⁹ The claim is customarily filed on Form 843. A separate claim is required for each taxable period.⁷⁰ One cannot emphasize too much the importance of properly spelling out all the grounds upon which the refund claim is based. This is necessary because a ground not raised in a timely claim cannot later be asserted in court as a basis for recovery.⁷¹

If one has filed a timely claim asserting grounds for refund, he may not later file an untimely second claim and rely upon new grounds asserted therein if the new grounds are wholly unrelated to those in the first claim.⁷² If the attorney concludes, after the claim has been filed but before suit has been started, that grounds for a refund exist other than those specified in the claim, these should be brought promptly to the Service's attention.⁷³ For this purpose, a new claim should be filed immediately if the limitations period has not yet expired. If the limitations period has run, and the original claim has not yet been denied, he still may be able to file another claim and contend that it is an amendment to a timely claim rather than a new claim.⁷⁴ Finally, if the limitations period has expired, and the first claim either has been rejected or is already in Court,⁷⁵ it may still be possible to contend that newly asserted theories of recovery are embodied within the facts set out in the timely refund claim.⁷⁶

C. Action by Commissioner

The claim must have been pending for a period of six months or rejected by the Commissioner before suit may be filed for the refund.⁷⁷ During this "limbo" period, all the administrative procedures previously available, such as the informal conference and hearings, are revived. What has been unavailing for settlement purposes before will generally not be rewarding the second time around. On the contrary, in addition to a duplicate investment of time, there is always the threat of showing the wrong card at the wrong time. Unless you have an item upon which the limitations period has run and which you wish to interject into the contest at this time, it is strongly recommended you waive the "second time at bat."

D. Timely Filing of Suit

A suit must be filed within two years after the Service's notice of rejection

67 INT. REV. CODE OF 1954 §§ 6511 & 6532.

68 *Ibid.*

69 INT. REV. CODE OF 1954 § 6511.

70 Treas. Reg. § 301.6402-3 (1954).

71 Real Estate Land Title Co. v. United States, 309 U.S. 13, 17-18 (1940).

72 Andrews v. United States, 302 U.S. 517 (1938).

73 This will enable the attorney to meet a later charge of surprise should the Government resist his introduction of the matters into the case.

74 Consolidated Coppermines Corp. v. United States, 296 F.2d 743 (Ct. Cl. 1961).

75 FED. R. CRV. P. 15.

76 There is a recognizable tendency upon the part of the Court of Claims to construe any resistance to the tax payment by the taxpayer as a "claim." It is thus advisable for the attorney to check his file to ascertain if any correspondence might gain the benefit of this tendency.

77 INT. REV. CODE OF 1954 § 6532(a).

of the refund claim. In one case, a taxpayer filed his refund claim in 1923 and amended it in 1948. It was rejected by the Commissioner in 1951 and within two years thereafter, almost 30 years after the claim was filed, suit was filed. The Court held the suit timely filed.⁷⁸

Conclusion

Statutory limitations narrowly confine the lawyer at every step of the way toward the resolution of a tax dispute. The absence of the latitude present in other "cases and controversies" is disconcerting and frustrating. A healthy respect for these statutory strictures, coupled with thorough planning will minimize the discomforts and supply an added element of challenge ordinarily not presented to him. The limitations also render the opposing advocate more predictable, and understandably, less flexible. Indeed, at times he may appear to be intransigent. It should be remembered, however, that part of his intransigence stems from the fact that he has 180 million clients whose interests are jealously guarded by his several superiors through the progress of the litigation. In spite of this inflexibility, the tax attorney has a number of alternative procedures from which to choose. In exercising this discretion he is well advised to consider the tactical points discussed in this article.

But beyond tactics, the tax attorney should never forget that there is no substitute for preparation. A castle built on sand will not withstand attack, and with the submission of each letter, document or form to the government, one adds a beam in the construction of his case. There is no margin of allowable error; the foundation must be sturdy. The filing of the protest, if proper procedure, demands the utmost care. The protest preparation requires a complete mastery of the factual situation, the supporting laws that do or may affect the client's cause. The expenditure of time at this juncture will repay the attorney many times over during the course of the controversy. By manifesting less than diligent representation the tax attorney performs a disservice not only to his client and himself, but also to taxpayers the country over.

78 *Detroit Trust Co. v. United States*, 130 F. Supp. 815 (Ct. Cl. 1955).