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## TAXPAYERS' UNDEVELOPED MUSCLE—THE REFUND SUIT

*Allen E. Brennecke\**

In the field of federal income taxation, an overzealous revenue agent or a nonacquiescing Commissioner creates unique problems for the lawyer. Frequently, his client is faced with a proposed adjustment to income which does not amount to a large amount of tax—often less than \$1,000.00. Of course, if the tax is owing, it is paid and the audit is concluded. A problem which arises too frequently is that the proposed adjustment is not supported by, or is in direct conflict with the decisions of the United States Courts of Appeal and/or the United States District Courts and sometimes the Tax Court. The inconsistency may be pointed out to the revenue agent with a response of the Commissioner's nonacquiescence or an effort to distinguish your authority on factual distinctions lacking substantive difference. It is at this juncture the lawyer faces the "you probably do not owe the tax, but it will cost you more to fight than the amount of tax involved" explanation to his client.

This does little to smooth the feathers of the client who feels that he has already paid his "fair share" and does not relish paying one cent more. There are still a few hardy souls who put principle above money and for them the fight is on. Normally this is an administrative contest; first to the District Conference; then to the Appellate Division; and then to the Tax Court, and perhaps even to the United States Court of Appeals. In all, it is an expensive contest. Depending upon the geographic location of the taxpayer and his lawyer, far too much legal time is spent traveling to and from (as well as at) the various conferences involved.<sup>1</sup>

The refund suit in the United States District Court represents an entirely different procedure for contesting a disputed tax case. The smaller cases may frequently involve only a disputed question of law. This lends them peculiarly to the refund suit due to the provisions for summary judgment<sup>2</sup> under the Federal Rules of Civil Procedure.

Unlike many of the problems besetting our nation, adequate representation for taxpayers on small tax cases does not need new legislation. The refund suit in the district court has been too long and too completely neglected. The myth that any federal court case must involve a large amount of money confuses the issue. There is no jurisdictional amount necessary on a tax refund suit. A second myth is the notion that any federal court case must be expensive from the standpoint of lawyer costs. This notion can and should be destroyed. Far less lawyer time is needed in a refund suit than in working up the administrative ladder of the Internal Revenue Service.

The basic advantages of the refund suit are that they allow the average tax-

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<sup>1</sup> While the conference may be waived and the 90-day letter issued upon the taxpayer's request to allow taking a case directly to the Tax Court, this practice does not appear to be frequently followed. Normally there is a stop at each rung in the administrative ladder.

<sup>2</sup> FED. R. CIV. P. 56.

payer to have full-fledged representation without the expense of legal counsel considered customary in a tax case fought up the administrative ladder of the Internal Revenue Service. The lawyer can handle almost all of the work from within the confines of his own office; obtain the full procedural support of the decisions of the United States Courts of Appeal and United States District Courts; shift a large portion of the travel problem and its expenses from the taxpayer to the Government; and provide his client with the jury trial protection felt helpful where the moral equities of the case lie with the taxpayer.

The refund suit may be especially appropriate in cases where a revenue agent disallows certain matters which appear to be "bargaining material." These should *not* be objected to; the tax on them should be paid along with the major issues in dispute. Thereafter, when the case is ready for trial in the district court, the "bargaining material" issue, wherein the taxpayer's case is strongest, becomes the first issue for trial. By attacking the issue where the Government's case is weakest, the taxpayer may be able to strengthen the rest of his case in the eyes of the jury, and perhaps even the court, as it will appear the Government was overbearing on the entire tax audit.

Basically, the tax refund suit involves a four-step process.

1. First of all, the taxpayer must pay *all* of the tax claimed to be owing.
2. Secondly, the taxpayer files a claim for a refund with the Internal Revenue Service.
3. The claim for refund must be denied by the Internal Revenue Service or six months must first expire.
4. The taxpayer then brings his refund suit action in the United States District Court.

### I. Payment of the Tax

The Supreme Court made it very clear in *Flora v. United States*<sup>3</sup> that the taxpayer must pay all of the tax in question before filing the refund claim and commencing suit in the district court. For many years prior to the *Flora* case, there was some question about this. Hopeful taxpayers desiring to avoid the Tax Court would, pay part of the tax owing, file a claim for refund for the partial tax paid, hold off the Commissioner and then litigate the question of liability in the district court. The net effect was to get the advantages of the refund suit without tasting one of its few unpleasant flavors—full payment before suit of the tax alleged to be owing.

The Supreme Court did not directly pass on the question of whether or not interest also had to be paid as a prerequisite to the refund suit. The statute which requires payment of the "tax" before suit can be filed does not speak in terms requiring payment of interest.<sup>4</sup> A well-reasoned post-*Flora* district court decision has held that interest need not be paid.<sup>5</sup> However, by dictum, the Seventh Circuit

<sup>3</sup> 357 U.S. 63 (1958), *aff'd on rehearing*, 362 U.S. 145 (1960).

<sup>4</sup> 28 U.S.C.A. § 1346(a)(1).

<sup>5</sup> *Kell-Strom Tool Co. v. United States*, 205 F. Supp. 190 (D. Conn. 1962).

has held to the contrary.<sup>6</sup> Safe procedure calls for payment of the interest and penalty as well as the tax to eliminate the question from arising.

## II. The Refund Claim

After payment of the tax has been made, the refund claim may be filed at any time, subject to the following limits:

. . . within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later, or if no return was filed by the taxpayer, within 2 years from the time the tax was paid.<sup>7</sup>

Since the claim is based upon an overpayment of tax, it should not be filed until after the tax, interest, and penalty have been fully paid. Premature filing of a refund claim is invalid unless the Internal Revenue Service waives the defect. Waiver may result if the Internal Revenue Service acts upon the refund claim on the merits.<sup>8</sup>

Form 843 is used to file a refund claim. It is at this point in time that a lawyer begins to plead his case. Even if it is highly unlikely that the claim for refund would be allowed, all of the facts upon which the overpayment is based need to be set out to properly apprise the Internal Revenue Service of the grounds upon which the overpayment is based. A subsequent suit in the district court on the refund claim is limited to the grounds stated in the claim.<sup>9</sup> A full disclosure must be made to eliminate later objection during the refund suit that the claim for refund failed to raise the issues upon which suit is based.<sup>10</sup>

There is a further advantage to a full explanation of all of the facts in the claim for refund. In looking ahead to possible negotiation and settlement with the Tax Division of the Department of Justice, a lawyer is able to set out more of the facts and details surrounding the equities of his case than might be permissible under pleadings in a subsequent refund suit. While the Department of Justice lawyer may not be greatly swayed by a recital of the equities, he recognizes the hazards of litigation inherent in jury-trial cases. Unlike the revenue agent who argues his case by trying to explain why the Commissioner is not following a line of cases that is favorable to the taxpayer, the Tax Division lawyer has to be practical when the cases do not support the Commissioner. A full and complete statement of all of the facts helps to develop a claim which may later be conducive to settlement possibilities.

The claim for refund is filed with the Internal Revenue Service Center where

6 *Kisting v. Sauber*, 325 F.2d 316 (7th Cir. 1963). The taxpayer had not paid the tax in full either, so the precise question of whether the taxpayer can pay all of the tax, but not all of the interest was not passed on.

7 26 U.S.C.A. § 6511(a).

8 *Continental Illinois Nat. Bank and Trust Co. v. United States*, 39 F. Supp. 620 (Ct. Cl. 1941); *Fidelity Trust Co. v. United States*, 39 F. Supp. 451 (W.D. Pa. 1939).

9 *Real Estate-Land Title Co. v. United States*, 309 U.S. 13 (1940).

10 *Herrington v. United States*, 416 F.2d 1029 (10th Cir. 1969). Treas. Reg. § 301.6402-2(b)(1) provides in part:

The claim must set forth in detail each ground upon which a credit or refund is claimed and facts sufficient to apprise the Commissioner of the exact basis thereof. . . . A claim which does not comply with this paragraph will not be considered for any purpose as a claim for refund or credit.

the tax return was originally filed for the year in question.<sup>11</sup> Only an original of the refund claim needs to be filed. The Internal Revenue Service then has six months in which to act upon the refund claim.<sup>12</sup> During the six-month period, the Internal Revenue Service can take one of four courses of action. First of all, it can allow the claim in full; secondly, it can disallow the claim in full; thirdly, it can allow the claim in part; or fourthly, it can fail to act at all.

A refund claim timely mailed is presumed to be timely filed even if it is received after the refund period expired,<sup>13</sup> and if mailed by registered or certified mail, it will be deemed to have been delivered upon the date of postmark.<sup>14</sup>

If the Internal Revenue Service denies it ever received the claim, the burden is upon the taxpayer to prove it was delivered. Unless there is a record of mailing, such as registered or certified mail would provide, the taxpayer's burden may be most difficult to discharge.<sup>15</sup>

The formal requirements of the refund claim are few in number but important. The claim must be in writing,<sup>16</sup> must be signed under the penalties of perjury,<sup>17</sup> and there must be a separate refund claim filed for each taxable year.<sup>18</sup> The correct year to which the refund applies must be stated and the amount of the claim must be stated and there must be a "demand" for refund. In addition, each ground upon which the claim is based must be stated in detail,<sup>19</sup> and there must be sufficient facts to apprise the Internal Revenue Service of the grounds for the claim.

In preparing the demand for the amount of tax to be refunded, the refund claim should state the amount with the additional language "or such greater amount as may be legally refundable."<sup>20</sup>

The Government may waive certain defects in a claim for refund relating to the form and content thereof even though there are statutory requirements relating to the refund claim.<sup>21</sup> The best evidence that the Treasury has waived any defects in the form and content of the refund claim is a formal denial of the refund claim on its merits with no request being made by the Internal Revenue Service for additional evidence in order to allow it to act on the refund claim.<sup>22</sup> Even though a refund claim may not be technically correct, if the Internal Revenue Service understands the claim well enough to act on the merits of the claim, the refund claim is sufficient.<sup>23</sup> In addition, during trial of the refund case, if the Department of Justice lawyer is not careful, he may open the door to

11 Treas. Reg. § 301.6402-2(a)(2). Prior to April 15, 1968, refund claims were filed with the District Director to whom the tax was paid.

12 26 U.S.C.A. § 6532(a)(1).

13 26 U.S.C.A. § 7502(a).

14 26 U.S.C.A. § 7502(c); Treas. Reg. § 301.7502-1(c)(2).

15 See *Jones v. United States*, 226 F.2d 24 (9th Cir. 1955).

16 *Wrightsmen Petroleum Co., v. United States*, 35 F. Supp. 86 (Ct. Cl. 1940).

17 Treas. Reg. § 301.6402-2(b)(1).

18 Treas. Reg. § 301.6402-2(d).

19 Treas. Reg. § 301.6402-2(b)(1).

20 *Austin Nat. Bank v. Scofield*, 84 F. Supp. 483 (W.D. Tex. 1948); *F. W. Woolworth Co. v. United States*, 91 F.2d 973 (2d Cir. 1937).

21 *Tucker v. Alexander*, 275 U.S. 228 (1927). See *United States v. Garbutt Oil Co.*, 302 U.S. 528 (1938).

22 *Ford v. United States*, 402 F.2d 791 (6th Cir. 1968). See *South Coast Corp. v. Commissioner of Internal Rev.*, 180 F.2d 878 (5th Cir. 1950).

23 *Keneipp v. United States*, 184 F.2d 263 (D.C. Cir. 1950); *Con-Rod Exchange, Inc., v. Henricksen*, 27 F. Supp. 427 (W.D. Wash. 1938).

waiving a defect in the refund claim by cross-examination of the taxpayer or other witnesses on the issue involved.<sup>24</sup> However, the statutory period for filing refund claims may not be waived and once the time period has expired there can be no waiver of this defect of the refund claim.<sup>25</sup>

The claim for refund may be amended under certain circumstances. During the refund claim period, a taxpayer may file as many different refund claims or as many amendments in respect to an issue as he desires, as long as the claim has not been disallowed on the merits. Once the Internal Revenue Service has rejected the refund claim, a subsequent amendment is too late.<sup>26</sup> In the event the original refund claim was timely filed, it may be amended after the time for filing a refund claim has expired if the Internal Revenue Service has not formally rejected the refund claim,<sup>27</sup> unless the amendment raises entirely new matters which are not set forth in any respect in the original refund claim as filed.<sup>28</sup>

If the claim for refund is based upon an overpayment of tax on a joint income tax return, the claim for refund must be signed by both spouses.

If the taxpayer received formal denial of his refund claim within the six-month period from the date of filing of the claim he may then commence his refund suit in the district court. In the event no formal notice of denial is received within the six-month period the taxpayer is also free to then commence the refund suit. Since the exact expiration date of the six-month period may be important, it is advisable to request confirmation of the date the refund claim was received by the Internal Revenue Service Center with the cover letter accompanying the claim for refund.

A taxpayer has two years to commence the refund suit from the date formal denial of the refund claim is mailed to the taxpayer.<sup>29</sup>

### III. The Refund Suit

The refund suit is a civil action commenced in the United States District Court. The taxpayer is the plaintiff and the United States of America is the defendant. The District Director may not be sued as the defendant in a refund suit.<sup>30</sup> Jurisdiction exists regardless of the amount of tax involved, as there is no

24 *United States v. Smith*, 418 F.2d 589 (5th Cir. 1969).

25 *United States v. Garbutt Oil Co.*, 302 U.S. 528 (1938); *Tucker v. Alexander*, 275 U.S. 228 (1927); *Commissioner of Internal Rev. v. Rieck*, 104 F.2d 294 (3d Cir. 1939).

26 *United States v. Memphis Cotton Oil Co.*, 288 U.S. 62 (1933); *Solomon v. United States*, 57 F.2d 150 (2d Cir. 1932); *Young v. United States*, 203 F.2d 686 (8th Cir. 1953).

27 *United States v. Factors & Finance Co.*, 288 U.S. 89 (1933).

28 *United States v. Garbutt Oil Co.*, 302 U.S. 528 (1938); *United States v. Andrews*, 302 U.S. 517 (1938).

29 26 U.S.C.A. § 6532(a)(1). In the event the Internal Revenue Service fails to formally reject the refund claim, the statute of limitations appears not to run.

30 Prior to January 31, 1967, taxpayers had the option of choosing between two defendants, the United States of America or the District Director. In some cases, this allowed the taxpayer to bring his suit in the judicial district where the District Director resided rather than in the district where the taxpayer resided. Congress ended the taxpayers' option of forum shopping. 26 U.S.C.A. § 7422(f)(1), added by Pub. L. 89-713. If suit is inadvertently brought against the District Director after January 31, 1967, it is not a fatal defect; the United States of America will be substituted as the party defendant and upon the request of the United States the case will be transferred to the District or division in which it would properly have been brought if suit was initially against the United States of America. 26 U.S.C.A. § 7422(f)(2).

minimum amount necessary to invoke jurisdiction of the district court.<sup>31</sup>

Venue for a refund suit is the judicial district in which the taxpayer resides at the time the action is begun.<sup>32</sup>

The refund suit may not be commenced prior to the expiration of six months from the date of filing of the refund claim, unless the claim has been formally rejected within the six-month period. In addition, the refund suit must be commenced within two years from the date of mailing of the notice of disallowance of the refund claim.<sup>33</sup> Unlike certain state procedure acts, in the district court suit is commenced by filing the complaint.<sup>34</sup>

In general, the complaint should contain the following allegations:

1. That plaintiff is a resident of the judicial district wherein the suit is brought.
2. The claim arises under the Internal Revenue laws of the United States and that the court has jurisdiction pursuant to Title 28, Section 1346(a)(1) U.S.C.A.
3. The income tax accounting year used by the plaintiff taxpayer at all times material.
4. The adjustments made to taxpayer's income by the Internal Revenue Service.
5. As a result, additional tax and interest was asserted and assessed by the Internal Revenue Service and was paid by the plaintiff, showing the amount of tax, the year involved and the date of payment.
6. A claim for refund was filed, setting forth the date of filing, the amount of the claim and the year involved.
7. The claim for refund was formally denied and the date of the denial (or that more than six months has expired since the filing of the claim for refund and the claim for refund has not been allowed or approved).
8. The tax was wrongfully collected from the plaintiff with a statement of the facts relied upon in detail to show the theory upon which the refund was claimed.
9. Judgment is demanded in the amount of the claim plus interest as provided by law, and costs.

Service is made by serving a copy of the complaint and the summons upon the United States Attorney in the district where the action is being brought and by sending a copy to the Attorney General of the United States by registered mail.<sup>35</sup> The summons is prepared and issued by the clerk and service is made by the United States Marshal.<sup>36</sup>

From the time the taxpayer was first advised of the proposed adjustment of his tax liability, to the time of payment of the tax and the filing of the refund claim and commencement of the refund suit,<sup>37</sup> the entire case may be handled

31 28 U.S.C.A. § 1340.

32 28 U.S.C.A. § 1402(a)(1).

33 26 U.S.C.A. § 6532(a)(1).

34 FED. R. CIV. P. 3.

35 FED. R. CIV. P. 4(d)(4).

36 FED. R. CIV. P. 4(a).

37 A sufficient number of copies of the complaint, which may vary with local rules, should be mailed to the Clerk with the \$15.00 filing fee. 28 U.S.C.A. § 1914.

by mail and it is not necessary that the taxpayer's lawyer ever leave his office.

At the time the refund suit is commenced, a basic shift in government functions takes place. Prior to this time, the Internal Revenue Service of the United States Treasury Department has had sole control of the case—from auditing the return to receipt of payment of the tax. But once the complaint is filed, the Internal Revenue Service no longer has an active role in the case. It is shifted administratively from the Internal Revenue Service to the United States Department of Justice. No longer does the taxpayer's lawyer deal with the revenue agent; his adversary is a lawyer in the Tax Division of the Justice Department.

Due to the time necessary to forward and transmit all of the files from the Internal Revenue Service to the Department of Justice, the United States as a party defendant is granted sixty days to file an answer to the complaint.<sup>38</sup>

It is after the answer is filed that the taxpayer may find he has one or two opportunities which do not exist when he deals with a revenue agent or the Internal Revenue Service in an administrative appeal. The first of these is the possibility of a prompt settlement of the case on favorable grounds, especially if the administrative position of the Internal Revenue Service was contrary to the controlling decisions of the United States Courts of Appeal or the United States District Courts. While the Department of Justice is a capable adversary, lawyers rather than revenue agents are making the basic decisions regarding the prospects of prevailing—or not prevailing—on the merits; and, in addition, they are much closer to the "Courtroom door" than a revenue agent at the audit or district conference level. If the law is enough in the taxpayer's favor, he may be able to obtain a one hundred percent refund on a settlement basis without his lawyer ever having to leave his office.

The second new opportunity for the taxpayer to take the offensive in the district court arises under the provisions of the federal rules providing for summary judgment.<sup>39</sup> Under summary judgment, the taxpayer is afforded a complete determination on the merits in those cases where the dispute involves solely a question of law rather than one of fact. As a result, the time, expense and work involved in a trial are avoided, yet the taxpayer gets the benefit of the authority of case decisions of the federal courts on the issue at hand. Frequently the smaller tax cases may involve exclusively a question of law and therefore lend themselves most appropriately to the summary judgment procedure.

When a motion for summary judgment is filed, it may be submitted to the court without oral argument. Even when oral argument is required or felt advisable by the taxpayer, this becomes the first occasion when the taxpayer's lawyer must leave his office. This is a long way from traveling back and forth to argue with the Internal Revenue Service in the administrative procedure, particularly when the issue may be one where no one in the entire Revenue Service has authority to compromise on a given issue where the Commissioner fails to agree with case decisions favoring a taxpayer.

In the refund suit, the grounds for recovery set out in the complaint should be the same as those stated in the refund claim. As mentioned above, the tax-

38 FED. R. CIV. P. 12(a).

39 FED. R. CIV. P. 56.

payer's right of recovery in the refund suit is limited to the grounds set forth in his claim for refund.<sup>40</sup>

No reply is necessary by the taxpayer to the Government's answer unless there is a counterclaim made by the Government. Allegations in the answer will be deemed to be denied.<sup>41</sup> If the Government does file a counterclaim, the taxpayer is granted twenty days in which to reply.<sup>42</sup>

#### IV. Refund Suit Advantages

The refund suit in the district court has several distinct advantages over an administrative determination by the Internal Revenue Service and ultimately a judicial determination by the Tax Court. While the advantages of the refund suit may vary from one case to another, the following are some of those which indicate the refund suit is preferable to an administrative determination and Tax Court adjudication of the tax liability. It must be kept in mind, however, that the refund suit and its advantages are predicated upon full payment of the tax assessed and are not available unless full and complete payment has been made.<sup>43</sup>

##### A. *The Jury Trial*

A major difference between the United States District Courts and the Tax Court is the availability of a jury trial in the district court regardless of the amount in controversy. To the contrary, all Tax Court cases are tried to the court without a jury. While there may be a difference of opinion in the minds of lawyers, it is submitted that the opportunity for a jury trial is an advantage to the taxpayer. The demand for a jury trial should be attached to the complaint and served with it so that the demand will be timely made.<sup>44</sup> If the case is one which the lawyer feels should be tried to the court rather than the jury, this is permissible in the district court as long as both parties agree.

##### B. *The Travel Factor*

One of the most "costly" features of a small tax case when the administrative procedure is followed is the amount of time the taxpayer's lawyer has to spend traveling to and from the various hearings set out in the administrative procedure. It is not only time consumed in travel, but there is the additional time of argu-

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40 See footnote 19 and accompanying text, *supra*. When a taxpayer files his refund claim and the complaint based upon one theory and added an alternative ground in an amendment to his complaint because of a Supreme Court decision handed down between the time of the claim and of the complaint, the amendment was allowed to stand. The Court held that the requirement of the claim is that it set forth the ground upon which the refund is claimed and sufficient facts to apprise the Commissioner of the basis of the claim. The Court held that these requirements had been met by the taxpayer. *United States v. Henderson Clay Products*, 324 F.2d 7 (5th Cir. 1963).

41 FED. R. CIV. P. 7(a) and 8(d).

42 FED. R. CIV. P. 12(a).

43 See footnotes 3-6 and accompanying text, *supra*.

44 The demand may be made at any time not later than ten days after service of the last pleading directed to the issue. FED. R. CIV. P. 38(b). If not timely made the right to jury trial will be considered waived. FED. R. CIV. P. 38(d).

ment with the Internal Revenue Service and the time necessary to prepare for each argument at each step of the administrative ladder.

By contrast, the district court refund suit offers the opportunity to fully litigate the tax appeal with a minimum of lawyer time invested, since most matters can be handled by the lawyer from his office.

### *C. Difference in the Courts*

In the Tax Court, the judge who will try the case is frequently new to the lawyer and his preference for handling matters in the courtroom is unknown to most practicing lawyers. The Tax Court cases are frequently handled by stipulation of the facts which limits somewhat the lawyer's opportunity to try a case the way he is accustomed to trying cases.

In the district court, however, the taxpayer's lawyer normally knows or has a better understanding of the individual judge and his preferences and this often creates a more familiar or relaxed atmosphere than is present in the Tax Court. In addition, cases in the district court are frequently assigned for a particular week or perhaps a certain day, depending upon the scheduling policies of the court. By contrast, Tax Court cases may be assigned on the first day of the week, with many slated for trial during that session. This, of course, requires the taxpayer's lawyer to be ready to go to trial on short notice which may make the preparation for trial exceedingly difficult, especially if there are a number of witnesses involved.

### *D. Chances of Winning*

The most important factor to the client is winning. Comparable statistics are sparse relating to the taxpayer's opportunity of prevailing in the district court as opposed to the Tax Court. However, it has been reported that taxpayers won only 21% of the cases in the Tax Court during fiscal year 1969 compared to 45% of the cases in the district court.<sup>45</sup> These statistics disregard cases which were partially won by the taxpayer and partially won by the Government.

The raw statistics may be somewhat misleading, especially in view of the fact that some Tax Court cases are argued by the taxpayer without the benefit of counsel. Nevertheless, reports such as this support the position of those who feel they have a better chance of winning in the district court.

### *E. Settlement Prospects and Procedure*

Since the Internal Revenue Service is no longer involved in the conduct of the trial in the district court, the settlement prospects are frequently more opportune than in the administrative procedure. One of the key factors creating this difference is that one is dealing with a lawyer as your adversary rather than a revenue agent. As a lawyer, he is more fully aware of the hazards of litigation

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<sup>45</sup> RESEARCH INSTITUTE OF AMERICA, TAX COORDINATOR BI-WEEKLY ALERT, February 11, 1970.

and recognizes them at an earlier date than a revenue agent who may never have seen the inside of a courtroom, or felt the pointed remarks of a judge who feels the law is very clearly settled in the taxpayer's favor on a given point and who is not persuaded by the Commissioner's administrative determination to the contrary.

As a matter of procedure, one of the first matters of correspondence which the taxpayer will receive from the Department of Justice after the complaint has been filed is a form letter inquiring as to whether or not the taxpayer's counsel anticipates the suit is one which is susceptible to settlement. This letter normally invites the taxpayer's counsel to submit any offer and settlement proposal which he may desire on an informal basis by letter to the Department of Justice for consideration. Experience indicates that the Department of Justice has more discretion and authority to settle on disputed questions of law than the Internal Revenue Service where the Commissioner has taken an attitude or position contrary to the decisions of the federal courts.

Another aspect of the settlement opportunity with the refund suit is that the attorneys for the Tax Division of the Justice Department will frequently be interested in exploring the settlement possibilities prior to getting to the courthouse door. This also aids the taxpayer in holding down the cost of his litigation as he may well determine soon after suit is commenced that his case has certain settlement possibilities which will not require extensive legal work beyond filing of the complaint.

#### *F. Summary Judgment*

As mentioned above, in the refund suit the opportunity for summary judgment under the Federal Rules of Civil Procedure may be of double advantage to the taxpayer. First, as to questions of law, it allows a prompt and expeditious determination where frequently the Commissioner is unwilling to follow the weight of authority. The opportunity for partial summary judgment on only one (or more) of the issues should not be overlooked as it will cut down the number of issues for trial and perhaps improve your overall settlement position. Secondly, the fact that the taxpayer has available to him the tools of summary judgment may help to bring about a more prompt disposition or settlement of the case as the Justice Department lawyer recognizes that the summary judgment provisions of Rule 56 are a very effective tool for the taxpayer.

#### *G. Discovery*

By using the district court, the taxpayer has available the full discovery provisions of the Federal Rules of Civil Procedure. This is in sharp contrast to their absence in the administrative procedure of the Internal Revenue Service and the more restrictive discovery of the Tax Court.

In addition, the pretrial conference rules in the district court may require the government to list all of their exhibits and witnesses, which gives the taxpayer's lawyer an early preview of the real strength of the Government's case.

### H. Interest

Until the taxpayer pays the full amount of the assessment against him, interest accrues on the assessment at the rate of six percent per annum.<sup>46</sup> When the taxpayer prefers not to pay the tax and to go to the Tax Court (although he may pay the tax in full *after* the 90-day letter has been issued and still go to the Tax Court if he wishes) the interest continues to accrue at the rate of six percent on the tax. After the Tax Court has made its decision, the interest continues to accrue on the unpaid tax until it is paid.

By contrast, in the refund suit the taxpayer has paid all of the tax alleged to be owing. Thereupon, in the event there is a settlement of the case which is either partially or entirely favorable to the taxpayer, the taxpayer receives not only the tax erroneously collected but also a pro rata portion of the interest collected (and perhaps of the penalty and also receives interest upon the total refund at the same rate of six percent per annum).<sup>47</sup> In the event judgment is rendered in favor of the taxpayer in whole or in part, any refund ordered by the court will also bear interest at six percent.<sup>48</sup>

### I. Burden of Proof

In any tax case, if the Commissioner has made a determination, there is a presumption of correctness with respect to that determination unless the taxpayer proves to the contrary.

In the refund suit, the burden of proof is upon the plaintiff taxpayer as in any civil action. The taxpayer must show by a preponderance of the evidence that he is entitled to the refund and the amount thereof.<sup>49</sup> Where the determination of the amount of tax may be difficult to compute, pretrial stipulations in the district court may provide for a determination at trial of the question of liability with the actual amount of refund, if any, to be recomputed by the parties subsequent to the trial subject to the court's approval. A stipulation of this type may well shorten considerably the time needed for trial as well as the amount of work necessary to prove the taxpayer's case.

Where the issue of fraud is involved, however, the burden of proving fraud is upon the Government.<sup>50</sup> In addition, if the Government makes a counterclaim to the taxpayer's refund suit, it has the burden of proving the facts upon which its counterclaim is based.

### Conclusion

Discussion of the above matters has related primarily to pointing out the

46 26 U.S.C.A. § 6601(a).

47 26 U.S.C.A. § 6611(a).

48 28 U.S.C.A. § 2411(a).

49 *United States v. Anderson*, 269 U.S. 422 (1926). In contesting the discharge of this burden, the Fourth Circuit has ruled that the Government may be permitted, for impeachment purposes, to cross-examine in regard to unconstitutionally seized evidence. *Compton v. United States*, 334 F.2d 212 (4th Cir. 1964).

50 26 U.S.C.A. § 7454(a). *Carter v. Campbell*, 264 F.2d 930 (5th Cir. 1959).

opportunities and advantages which the refund suit has for smaller tax cases. However, its use should also be recognized to be of particular value in tax cases involving a large amount of money. First of all, by payment of the tax in full the continuing accrual of interest is terminated. The advantages of the district court suggested above, when compared with the Tax Court, may actually afford the taxpayer's lawyer who is not a "tax specialist" the opportunity to furnish his client proper representation on a basis which is not only feasible for him but also advantageous to his client.

These suggestions have been set forth to encourage consideration and re-evaluation of the possibility that the district court refund suit is a very effective instrument for use in the smaller tax cases where the amount of tax is not large but where the law appears to favor nonliability of the taxpayer. It is submitted that the costs of pursuing and representing a client by using the available procedures under the Federal Rules of Civil Procedure may permit a determination for the client on the merits which would not be possible from an economic standpoint if his lawyer pursues the usual administrative steps within the Internal Revenue Service. The district court refund suit may not be the desirable route for every tax case, but the present practice of using it very infrequently seems to indicate that the pendulum is swung out of balance and needs to be tilted the other way.