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A PLEA FOR BETTER TAX PLEADING

A CRITIQUE OF PLEADING IN TAX CONTROVERSIES BEFORE THE BOARD OF TAX APPEALS*

RANDOLPH E. PAUL†

The hiatus of time from Coke to Cardozo has resulted in a considerable liberalism of pleading and procedure, notwithstanding the "hue and cry" of modern liberal pleading pedagogues to the contrary.¹ The twentieth century has seen a liberalization in pleading in the so-called code states. The angular corners of strict common law "form of action" pleading² have been polished smooth. Though the former stereotyped rigid rules characteristic of the early common law are now more or less legal history, the process is still fluid and there is a real need for advocates of liberal pleading.

The spirit of experimentalism which has brought about this change need not pine for more worlds to conquer. One branch of the law, perhaps the most important branch from the standpoint of the amount of money involved, remains so far as pleading is concerned, a child. In it no real thought has been given to pleading.³ The emphasis has been on determination and results; it has been forgotten that pleading has a vital connection with determination and results.

Lack of attention to matters of pleading is today costing government and taxpayers millions annually and is hampering the expeditious handling of tax cases. Of further importance is the fact that if we are not careful, this lack of attention will seriously affect the growth of a body of substantive income and estate tax law.⁴

The effect of poor pleading on the substantive law of taxation is twofold. In the first place, judges are best able to function in their judicial capacity when the issues of the controversy are clearly

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¹See e. g. Sunderland, *The English Struggle for Procedural Reform* (1925) 39 HARV. L. REV. 725.

²The Code of Procedure in New York in 1848, the adoption of code provisions in numerous other states and the New Jersey Practice Act modeled on the earlier English reforms in procedure are some examples of the twentieth century liberalization.

³E. g., The Enabling Act under which the Board of Tax Appeals was first created and functioned—Title IX, Revenue Act of 1924, is wholly devoid of any provisions regarding the type of pleading upon which appeals to the Board shall be based.

⁴Dean Wigmore in his very able critique on our system of evidence points out that under our system of law generally, rules of evidence and procedure are built up by the court at the expense of the parties litigant.

presented. The soundness of the decision may often depend on the clarity with which the issues are presented. In this respect Board members are no different from members of the bench generally, able and skilled they may be as a result of their experience in a specialized field. They are not endowed, however, with a discernment sufficiently omniscient to enable them to select the vital issues out of the confusion of issues that often results from poor pleading. Secondly, pleading which is loose in the sense that it does not apprise the parties of the issues involved frequently results in a failure of proof.⁵ The great number of cases⁶ which are lost because of a failure of proof,

⁵This is especially true under existing tax procedure; see the discussion *infra*, at p. 511.

⁶The following are but a few cases which taxpayers have lost because of a failure of proof: Commissioner v. Whitman, 49 F. (2d) 1087 (C.C.A. 2d, 1931) *aff'g* 16 B.T.A. 197 (1929); Industrial Co. v. U. S., 38 F. (2d) 711 (1930); Hubinger v. Commissioner, 36 F. (2d) 724 (C.C.A. 2d, 1930) *aff'g* 13 B.T.A. 960 (1928) certiorari denied. 281 U. S. 741 (1930); Washer v. Commissioner, 35 F. (2d) 1023 (C. C. A. 2d, 1929) *aff'g* 12 B.T.A. 632 (1928); Emil Ries, 25 B.T.A. 896 (1932); EauClaire Book & Stationery Co., 25 B.T.A. 535 (1932); Philadelphia Paper Mfg. Co., 25 B.T.A. 1231 (1932); R. L. Hague, 24 B.T.A. 288 (1931); Virginia H. Parmelee, et al., 24 B.T.A. 48 (1931); Isaac P. Keeler, 23 B.T.A. 467 (1931); I. A. Van Dyke, et al., 23 B.T.A. 946 (1931); A. Eimer, 23 B.T.A. 496 (1931); Roy & Titcomb Inc., 23 B.T.A. 12 (1931); California Fireproof Building Co., 22 B.T.A. 1128 (1931); Rising Sun Brewing Co., 22 B.T.A. 826 (1931); L. G. Hathaway, 21 B.T.A. 1280 (1931); Berkowitz Envelope Co., 21 B.T.A. 685 (1930); E. L. Potter, 20 B.T.A. 252 (1930); L. M. Klein, et al., 20 B.T.A. 1057 (1930); Tom Moore, 19 B.T.A. 140 (1930); Arcade Department Stores, Inc., 18 B.T.A. 1172 (1930); C. B. Hayes, 17 B.T.A. 86 (1929); Panyard Machine & Mfg. Co., 17 B.T.A. 1053 (1929); R. T. Coburn, 16 B.T.A. 1344 (1929); W. J. Paul, et al., Exrs., 16 B.T.A. 459 (1929); National Straw Works, 16 B.T.A. 463 (1929); Consolidated Companies, Inc., 15 B.T.A. 645 (1929); F. Russell Beebe, et al., Exrs., 15 B.T.A. 1022 (1929); Seimon Bache & Co. Inc., 15 B.T.A. 183 (1929); Louis Gunsberg, 14 B.T.A. 769 (1928); J. E. Robertson, 13 B.T.A. 550 (1928); Theodore Aaron, 12 B.T.A. 556 (1928); The Fair Store Corp., 11 B.T.A. 1033 (1928); H. Symons, 11 B.T.A. 886 (1928); Young Bros., 10 B.T.A. 530 (1928); Davidson Grocery Co., 9 B.T.A. 390 (1927); Foer Wallpaper Co., 9 B.T.A. 377 (1927); J. B. Rolater, 9 B.T.A. 73 (1927); J. H. Hulme, 9 B.T.A. 31 (1927); Calumet Steel Co., 9 B.T.A. 174 (1927); R. W. Farmer Co., 9 B.T.A. 856 (1927); F. A. Douty, 9 B.T.A. 218 (1927); L. A. Coleman, 9 B.T.A. 1386 (1928); Palatine Analine & Chemical Corp., 8 B.T.A. 1149 (1927); N. B. Jordan, 7 B.T.A. 458 (1927); Kanawha Drug Co., 7 B.T.A. 683 (1927); Joseph E. Barlow, 7 B.T.A. 1232 (1927); L. T. Perls, et al., 7 B.T.A. 568 (1927); Estate of T. J. Taylor, 7 B.T.A. 931 (1927); Powers Mfg. Co., 7 B.T.A. 786 (1927); J. R. Buchanan, 7 B.T.A. 893 (1927); B. S. Catlett, 7 B.T.A. 213 (1927); Booth Furniture & Carpet Co., 6 B.T.A. 886 (1927); T. G. Wilsford, 6 B.T.A. 813 (1927); S. L. Fowler, 6 B.T.A. 250 (1927); C. B. Haynes Co. Inc., 6 B.T.A. 88 (1927); Donaghey Real Estate & Construction Co., 5 B.T.A. 766 (1926); Charles W. Nass, 5 B.T.A. 665 (1926); Hart-Wood Lumber Co., 5 B.T.A. 117 (1926); Barnett Weiss, 3 B.T.A. 228 (1925).

results in a body of law which if properly read stands only as a monument to remind the taxpayer that he has the burden of proof in tax controversies. More often, however,—and here lies the real danger—they are apt to be read in the light of the results, that is, that the board has, for example, refused to allow a certain type of deduction. It is in this latter connection that the cases resulting from poor pleading may alter and shape the substantive law.⁷

Income taxes and estate taxes have come to stay, and of our many needs today not the least is a sound, uniform and rational body of law relating to these forms of taxation.

Income and estate tax controversy has become concentrated in the Board of Tax Appeals. That body has had jurisdiction since 1926 to determine refunds in cases where the Commissioner has determined a deficiency. Practically the only jurisdiction left for the District Court and the Court of Claims are cases in which no deficiency has been determined by the Commissioner of Internal Revenue. Such cases are becoming increasingly rare.⁸

The Board of Tax Appeals is not a court.⁹ In the words of the Supreme Court:

“It is an executive or administrative board upon the decision of which, parties are given an opportunity to base a petition for review before the courts after the administrative inquiry of the board has been had and decided.”¹⁰

Whatever may be the exact status of the Board—and the distinction between a board and court is not material to this discussion—it functions in practical fact as a court. In redetermining deficiencies it exercises powers which are clearly judicial. Moreover, its proced-

⁷The reader should not imply from the author's criticism of the present system of practice that it is altogether stereotyped. In all fairness to the board it should be noted that the rules with respect to amending petitions are quite liberal. (See for example, *Bankers Realty Syndicate*, 20 B.T.A. 612, 615 (1930)) Rule 18 permits the taxpayer to amend his petition as of course any time before the answer is filed; after answer, by consent of the commissioner or on leave of the board. The board in its discretion may even permit a party to a proceeding to amend his pleadings at any time before the conclusion of the hearing. Such an amendment of pleadings to conform to proof should be made upon motion.

⁸High tax rates, present economic conditions, and the necessity of collecting more taxes, all impinging on the national budget situation, will undoubtedly be reflected in the immediate future in a more rigorous analysis and contest of tax returns; *deficiency* determination will doubtless increase tremendously.

⁹See e.g., Van Fossan, *The United States Board of Tax Appeals* (1933) 1 FEDERAL BAR ASS'N JOURNAL 17, in which the author, a member of the United States Board of Tax Appeals, discusses the “judicial” nature of the Board.

¹⁰*Old Colony Trust Co. v. Commissioner*, 279 U. S. 716, 49 Sup. Ct. 340 (1929).

ure is in fact similar in vital respects to the procedure in state and federal courts in non-jury cases. Evidence is taken in precisely the same manner,¹¹ objections are noted, exceptions are taken, closing arguments are made on the basis of testimony taken, etc.¹² The fact is that the Board of Tax Appeals is in income and estate tax matters the ultimate fact-finding body,¹³ as such it will long remain one of the most important tribunals disposing of controversies between government and citizen,¹⁴ if not the most important tribunals disposing of all controversies.

Many lawyers will go so far as to urge that the facts are the only important thing in any controversy;¹⁵ all will agree that they are of the greatest and often decisive importance. In tax cases the responsibility for finding the facts rests upon the Board. The Circuit Court of Appeals will not review the Board upon the facts; if there is any substantial evidence to support the Board's findings they will be respected.¹⁶

¹¹Rule 38 of the Rules of Practice of the Board of Tax Appeals provides that: "The parties may, by stipulation in writing filed with the Board or presented at the hearing, agree upon any facts involved in the proceeding."

¹²Board members, like judges, differ in the degree of formality characterizing trials before them. Generally speaking, trials before the board are not less formal than trials before the United States District Courts and the State Courts. They are certainly not less formal than trials before the Court of Claims where the evidence is taken before Commissioners corresponding to Masters in Chancery and Referees in Bankruptcy.

¹³*Burnet v. Leininger*, 285 U. S. 136 (1931); *Phillips v. Commissioner*, 283 U. S. 589, 51 Sup. Ct. 82 (1930).

¹⁴This type of controversy is more and more in the work of the lawyer replacing the controversy between citizen and citizen.

¹⁵See JEROME FRANK, *LAW AND THE MODERN MIND* (1930), p. 146.

¹⁶*Burnet v. Leininger* and *Phillips v. Commissioner*, *supra* note 13; *Commissioner v. Norfolk Southern R. Co.*, 63 F. (2d) 304 (C.C.A. 4th, 1933) *aff'g* and *rev'g* 22 B.T.A. 302 (1931); *Universal Steel Co. v. Commissioner*, 46 F. (2d) 908 (C.C.A. 3d, 1931) *aff'g* 16 B.T.A. 788 (1929); *American Savings Bank & Trust Co. v. Burnet*, 45 F. (2d) 548 (C.C.A. 7th, 1930) *aff'g* 18 B.T.A. 397 (1929); *Saxman Coal & Coke Co. v. Commissioner*, 43 F. (2d) 556 (C.C.A. 3d, 1930) *aff'g* 2 B.T.A. 175 (1925); *Prey Bros. Live Stock Commission Co. v. Commissioner* 36 F. (2d) 326 (C.C.A. 10th, 1929) *aff'g* 9 B.T.A. 534 (1927); *Atlantic Coast Distributors v. Commissioner*, 33 F. (2d) 733 (C.C.A. 4th, 1929) *rev'g* 9 B.T.A. 690 (1927); *Twin City Tile & Marble Co. v. Commissioner*, 32 F. (2d) 229 (C.C.A. 8th, 1929) *aff'g* 6 B.T.A. 1238 (1927).

The rule that the Circuit Court will determine if there is sufficient evidence to sustain the Board's decision calls for a distinction between primary and ultimate facts. For example, in *Bishoff v. Commissioner*, 27 F. (2d) 91 (C.C.A. 3d, 1928) *aff'g* 6 B.T.A. 570 (1927), the court accepted as primary findings the Board's decision that the business of the taxpayer was credit and delivery, as distinguished from cash and carry, that the books were carelessly kept, etc. However, the

Counsel engaged in tax work need not be reminded of the complexity of the facts upon which the decision in most tax cases depends. But intricacy of facts is not the only concern of counsel. The handling of complex facts is a matter of trial technique; the difficulty is more deep-rooted.

As will be seen from the discussion following, the litigant is confronted with the problem of meeting any one or more of a number of theories of law or contentions offered by the Commissioner. Thus, uncertainty of the Commissioner's theory of the tax disputed—based as it is on the present system of pleading—multiplies the facts so needlessly that only a technician skilled in practice before the Board is able to maintain a proper perspective. Persons less skilled are apt to incur considerable expenses for the client by proving too much or become so lost in the maze of detail that they fail in the proof of some essential point of fact.¹⁷ The very complexity and multiplicity of the facts coupled with *the immunity of the Board's determination of them from attack* makes it necessary to pause and think of the importance of the machinery for finding the facts.¹⁸ Is that machinery designed to produce most easily the most efficient result? Does it produce that sort of result with the least trouble and expense to government and taxpayer? Does it do so with reasonable dispatch?

These are broad questions the answers to which are beyond the scope of this short article. It is task enough at the moment to limit the question and to analyze one part of the mechanism designed to

Board's decision that the taxpayer's books did not clearly reflect his income was an ultimate fact which the court would scan to determine if it was supported by the evidence. It is clear, therefore, that the Circuit Court of Appeals has ample power to search the record to find whether any substantial evidence supports the findings of the Board because whether there is any such evidence is a question of law and not of fact: *Franklin Lumber & Power Co. v. Commissioner*, 50 F. (2d) 1029 (C.C.A. 4th, 1931) *rev'g* 18 B.T.A. 1207 (1930); *Edson v. Lucas*, 40 F. (2d) 398 (C.C.A. 8th, 1930) *rev'g* 11 B.T.A. 621 (1928); *St. Paul Abstract Co. v. Commissioner*, 32 F. (2d) 225 (C.C.A. 8th, 1929) *aff'g* 6 B.T.A. 1225 (1927).

¹⁷See, e.g., *Alger-Sullivan Lumber Co. v. Commissioner*, 57 F. (2d) 3 (C.C.A. 5th, 1932) *rev'g* 20 B.T.A. 1109 (1930) and more particularly the court's statement at p. 5, " * * * it is apparent that the point was not deemed to be material by either petitioner or respondent in the proceedings before the Board * * * ". Finding the question material the court was compelled to remand the case to the board for a further hearing.

¹⁸As a member of the Board of Tax Appeals has said, *Van Fossan, op. cit. supra note 9* at 22, "In the matter of appeals the records show approximately two affirmances to each reversal of Board opinions.

In this fact is to be seen the importance of an adequate presentation before the Board. A taxpayer represented by inefficient counsel who fails to make adequate presentation of his case or timely reservation of his rights at the time of the hearing is in poor shape to secure a reversal of an adverse decision."

arrive at the issues and the facts of a tax controversy. How do we begin to ascertain the issues and facts? Is our basis sound? In other words, what is the system of pleading?

The first step in what ultimately becomes a board of tax appeals case is a *letter*,¹⁹ purporting to be written by the Commissioner of Internal Revenue, and in fact written by one of his numerous subordinates. This fact in itself is astonishing. It is certainly startling that the basis for all subsequent procedure in litigated tax matters before the Board of Tax Appeals should be an informal letter addressed to the taxpayer, written by one of the many assistants of the Commissioner of Internal Revenue, and that the writer of this letter instituting the entire action should never again have any connection therewith except in connection with settlement negotiations and then not always. Bearing in mind the nature of a formal complaint or bill in an action at law or in equity, one needs only to refer to a not untypical 60-day letter to note the marked contrast between these two documents both of which serve to initiate litigation.²⁰

The department's procedure is certainly to be contrasted with that almost universally characterizing other forms of litigation in which the first important papers instituting the cause of action are prepared by a person with legal training who is compelled, by the very nature of general legal procedure, to devote the requisite study to the legal theories of his case and who presumably will subsequently continue to act for the complainant throughout the course of the litigation. Thereafter the study and preparation, which precede the institution of important causes of action, is in most litigation carefully crystallized in the complaint or bill, carefully prepared and drawn with some elaboration to set forth exactly the basis for the cause of action. On the other hand, if the department's procedure were a criterion for pleading in other causes of action, it would suffice for the complainant to set forth some meagre facts referring back perhaps to extrinsic papers and reports and concluding with the statement that the defendant is indebted to the plaintiff in a certain amount. The defendant would, if such were the case, know as much about the nature of the claim against him as many taxpayers who receive deficiency letters.

It has been indicated that the letter written by the Commissioner of Internal Revenue determining a deficiency corresponds in board

¹⁹Referred to in tax parlance as a "60-day letter".

²⁰The 60-day letter does not serve to initiate tax litigation if the taxpayer chooses to abide by the deficiency determination; on the other hand, if the taxpayer takes his appeal to the Board the letter does serve as the "complaint".

practice to what is known in other actions as the complaint or bill. If this is true, the petition filed by the taxpayer with the Board of Tax Appeals is analogous to the answer of the defendant in other cases; the Commissioner's answer then corresponds to the reply in other cases.

The petition required to be filed by the taxpayer in board of tax appeals cases may not, like the deficiency letter of the Commissioner, treat informally the subject matter of the controversy.²¹ The Board of Tax Appeals rules carefully indicate what shall be the contents of the petition,²² and the rules even include for the information of the taxpayer a form of petition.²³ The petition prescribed must be verified,²⁴ if it is not verified with technical perfection a motion to dismiss will be made immediately.

For the first time we have in the petition a recognizable legal document in which certain jurisdictional facts must be alleged and in which the taxpayer must state the legal errors upon which the deficiency²⁵ is based, the facts upon which he relies as a basis of the proceeding and a prayer for relief. In this connection it should be noted that although the 60-day letter is vague and indefinite, as has been indicated, the rules²⁶ provide that the petition should contain:

"(d) Clear and concise assignments of error alleged to have been committed by the Commissioner. Such assignments of error shall be numbered.

(e) Clear and concise numbered statements of the facts upon which the petitioner relies as sustaining the assignments of error; except those assignments of error in respect of which the burden of proof is by Statute placed upon the Commissioner. (See sections 601, 602 of the Revenue Act of 1928.)

The petition shall be complete in itself so as fully to inform the Board of the issues to be presented."²⁷

²¹It is true that a most informal document may be enough to establish jurisdiction in the board but it must be later amended.

²²See Rule 5 of the Board of Tax Appeals Rules of Practice; in substance it requires: (1) proper jurisdictional allegations; (2) the Commissioner's deficiency determination, etc.; (3) clear and concise assignments of error alleged to have been committed by the Commissioner; (4) clear and concise statements of fact sustaining the assignment of errors; (5) prayer for relief; (6) verification, etc.

²³See the appendix to the Rules, *ibid.*

²⁴Rule 5, *ibid.*

²⁵Though he may not be able to discover the theory of the deficiency he must point out its legal errors. Rather an unfair burden.

²⁶Rule 5, *ibid.*, *supra* note 22.

²⁷The Board must be informed by the petitioner, who frequently must guess what is in the mind of the Commissioner's assistant who writes the deficiency letter. Why let the Board be informed through a prism?

It is indeed a paradoxical situation which requires a taxpayer to base a formal petition on an informal letter.

The next document is the Commissioner's answer, which is likewise required to be formal and exact. It refers to the petition paragraph by paragraph and admits or denies the allegations thereof. As a matter of practical fact, most answers are prepared by attorneys in the General Counsel's office who have not theretofore heard of the controversy and have no time²⁸ to make any attempt to investigate the facts. The result generally is that everything in the petition, including many purely formal facts, is denied. The taxpayer is thus put, at least in the beginning, to the necessity upon the pleadings themselves of proving every fact necessary to his cause of action.²⁹

Digressing for the moment, one specific illustration will be cited to show the gravamen of the Department's denial of formal facts. The petitioner by his counsel alleges as one of the formal allegations that the tax for the year in question was duly paid, etc.; such allegations are frequently denied although the information is peculiarly within the knowledge of the department. Counsel must therefore have his client locate the checks showing payment. Not infrequently the case involves a group of petitioners in widely scattered parts of the country. The taxpayers have paid their taxes in installments. The number of exhibits in the case is immediately increased by the number of checks—assuming of course counsel is able to collect these evidences of payment—by no means a simple matter where the payment was many years ago. If clients are unable to locate checks, counsel has the alternative of writing to a number of collectors and receiving—after a lapse of weeks—transcripts of the record. This laborious collecting of formal facts at a time when counsel is concerned with procuring the more important facts of the case could be easily obviated, and the example cited is but one illustration of other similar situations. It is only fair to urge that the department admit allegations the truth of which are peculiarly within its own knowledge.³⁰

²⁸Rule 14 of the Rules of Practice before the Board of Tax Appeals provides that the Commissioner shall have 60 days within which to file his answer or 45 days within which to move in respect to the petition.

²⁹It must be recognized that most attorneys in the General Counsel's office in charge of tax Board litigation on behalf of the government, are favorably disposed toward stipulation of as many facts as possible, and that they freely cooperate to this end with the taxpayers' attorneys.

³⁰*Cf.* for example, § 323 of the New York Civ. Prac. Act which provides that: "Admission of facts. Any party, by notice in writing, *given not later than ten days before the trial*, may call on any other party to admit, for the purposes of

The Board of Tax Appeals practice is therefore *sui generis*. In no other field of legal controversy do we find a series of pleadings beginning with an informal *letter* and ending with two documents having all the formality of court pleadings.³¹ Is there in tax controversies some special consideration justifying this distinction in procedure?

A negative answer to this question is not enough. There is in tax controversies a special consideration making the distinction particularly unjustifiable. There is in the ordinary controversy no magic in the plaintiff's first pleading. Not *any* pleading suffices to ground the plaintiff's cause of action; the pleading offered must stand the rigor of a multiplicity of motions designed to throw the litigant out of the field of combat. But this informal deficiency letter of the Commissioner is lifted above the plane of ordinary pleadings; it is endowed with a presumption of correctness.³² It suffices if it alleges a de-

the cause, matter or issue only, any specific fact or facts mentioned in such notice. In case of refusal or neglect to admit the same within six days after service of such notice, or within such further time as may be allowed by the court or a judge, the expenses incurred in proving such fact or facts must be ascertained at the trial and paid by the party so neglecting or refusing, whatever the result of the cause, matter or issue may be, unless at the trial or hearing the court or a judge certify that the refusal to admit was reasonable, or unless the court or a judge, at any time, shall order or direct otherwise. Any admission made in pursuance of such notice is to be deemed to be made only for the purposes of the particular cause, matter or issue, and not as an admission to be used against the party on any other occasion or in favor of any person other than the party giving the notice. The court or a judge, at any time, may allow any party to amend or withdraw any admission so made on such terms as may be just."

See also New York Civ. Prac. Act, § 322.

³¹Interesting is the change in Interstate Commerce Commission procedure with respect to the recapture of excess income—the Commission's only activity of a money-collecting nature. Several years ago the Commission revised its procedure, the details of which are not material here. Suffice it to say generally that the service by the Commission of a tentative recapture report in advance of hearing and the right of the railroad to inspect the Commission's underlying records is designed to and does apprise the railroad of the issues and legal principles involved. Not to be implied is the suggestion that the Board practice be modeled after the Interstate Commerce Commission practice. The recent change in the Commission practice does, however, suggest that a loose, vague, uninformative system of practice is not a necessary concomitant of practice before an administrative tribunal.

In other "special proceedings", such as mandamus actions—and appeals to the Board have been likened to "special proceedings" inasmuch as the Board is not a Court—the action is started by a "petition". Unlike Board practice, however, the "petition" in special proceedings is not based on anything analogous to the Commissioner's informal 60-day letter.

³²Gamm v. Commissioner, 39 F. (2d) 73 (C.C.A. 5th, 1930) *aff'd* 15 B.T.A. 594

iciency;³³ the reasons assigned by the Commissioner are immaterial in that they may be unsound or badly expressed. It may conceal the theory of the deficiency behind a veil of vague generalities; not infrequently the letter makes no attempt to explain the Commissioner's theory. There is no relief, statutory or otherwise, from the vagueness of such a letter. The Commissioner's determination is *prima facie* correct and the burden is on the taxpayer to prove that it is incorrect;³⁴ in addition thereto he must prove all the facts necessary to the computation of the correct deficiency.³⁵

(1929); *Onondaga Co. et al. v. Commissioner*, 50 F. (2d) 397 (C.C.A. 2d, 1931) certiorari denied 284 U. S. 671 (1931) *aff'g* 18 B.T.A. 944 (1930); *Kaufman v. Commissioner*, 44 F. (2d) 144 (C.C.A. 3rd, 1930) *rev'g* and *aff'g* 15 B.T.A. 141 (1929); *American Conservation Service Corp.*, 24 B.T.A. 183 (1931); *E. C. Hopkins, Exec.*, 24 B.T.A. 805 (1931); *E. P. McCabe, et al. Exrs.*, 23 B.T.A. 1375 (1931); *H. A. Whitlock, et al.*, 22 B.T.A. 1355 (1931); *F. L. Roche*, 21 B.T.A. 1139 (1931); *G. R. Craven*, 21 B.T.A. 78 (1930); *E. H. R. Green*, 19 B.T.A. 904 (1930); *C. H. Reinholdt & Co.*, 13 B.T.A. 905 (1928); *Rossmann, Inc.*, 13 B.T.A. 1266 (1928).

³³*Edgar M. Carnrick*, 21 B.T.A. 12, 21 (1930): "If the Commissioner finds one fact or reason which he believes supports his adverse determination, he is not required to express his views on any or all other matters relating to the item, and his failure to deal with them carries no implication as to their treatment. It is not the Commissioner's method of determination or computation which is the substance of the proceeding, for the deficiency may be correct despite a weakness in arriving at it or explaining it. *Woodside Cotton Mills Co.*, 13 B.T.A. 266 (1928); *Jacob F. Brown et al.*, 18 B.T.A. 859 (1930). 'It is immaterial whether the Commissioner proceeded upon the wrong theory in determining the deficiencies. In any event the burden was on petitioner to show that the assessment was wrong.' *Altschul Tobacco Co. v. Commissioner*, 42 F. (2d) 609 (1930)." *James P. Gossett*, 22 B. T. A. 1279 (1931): "The Board has consistently held that the subject matter of the proceeding before it is the tax liability of the petitioner. When a deficiency is determined, the reasons given do not constitute or confine the issues. . . . The petitioner may in his petition assail the deficiency for reasons not theretofore suggested and may go so far as thereby to convert the deficiency into an overpayment, and the respondent may, on the other hand, defend on new grounds. . . . The primary issue is the correctness of the ultimate determination of deficiency, and the ordinary presumption is not destroyed by the reason given, even if it be unsound or badly expressed."

³⁴*Brown v. Commissioner*, reported in 1930 COMMERCE CLEARING HOUSE REPORTS, Par. 9702, modifying 12 B.T.A. 841 (1928); *Wright v. Commissioner*, 50 F. (2d) 727 (C.C.A. 4th, 1931) certiorari denied 284 U. S. 652 (1931) *aff'g* 19 B.T.A. 541 (1930); *Portage Silica Co. v. Commissioner*, 49 F. (2d) 985 (C.C.A. 6th, 1931) *aff'g* 11 B.T.A. 700 (1928); *Glendinning, McLeish & Co. Inc.*, 24 B.T.A. 518 (1931) *aff'd* in 61 F. (2d) 950 (C.C.A. 2d, 1932); *W. L. Walls*, 21 B.T.A. 1417 (1931); *J. B. Dortch*, 19 B.T.A. 159 (1930); *Watson McMaster, et al.*, 18 B.T.A. 1119 (1930); *Atlas Plaster & Fuel Co.*, 18 B.T.A. 1123 (1930).

³⁵*Saxman Coal & Coke Co. v. Commissioner*, *supra* note 16; see also: *Louis Friedman*, 21 B.T.A. 38 (1930); *H. P. Parker*, 14 B.T.A. 1185 (1929); *Ohio Valley Fluorspar Co.*, 10 B.T.A. 289 (1928).

No reasonable taxpayer will quarrel with this special endowment of *correctness* bestowed upon the Commissioner's letters. It is historically well founded and it is necessary as an aid to the collection of revenues, nor will any sane taxpayer object to the companion burden-of-proof rule which is little more than another way of saying the same thing.

Nor will any person sufficiently disillusioned by years of practice in the courts contend that the informality of the Commissioner's deficiency letter is *per se* a fault. Formality and informality are not the point. The matter is one of substance, not form. It is conceivable that a letter may express the subject matter with even greater clarity than a complaint or any strictly formal document. The objection goes not to the form of the opening pleading but to its contents. A taxpayer must uphold a burden of proof. The dice are properly loaded against him. All the more important then for him to know whereof he speaks. The contents of the deficiency letter are to him a matter of vital concern; the basis of the deficiency, the *pièce de résistance* of his cause of action.

We come at this point to another astonishing thing. The Revenue Act of 1932, Section 272 (a),^{35a} authorizes the Commissioner to send "notice" of a deficiency by registered mail and the taxpayer is, if he wishes to appeal from the deficiency determination, authorized to file a petition within sixty days for a redetermination of the deficiency. Nothing about what the notice shall say to the taxpayer, other than that it shall state a deficiency. The statute exhibits concern in the registered mail provision that the taxpayer shall receive the "notice". Is it not somewhat amazing that so little concern is manifested about what shall be received? Why so much concern about the *receipt* of the notice and so little concern about the *contents* thereof?

In actual practice the "notice" is the letter that has been discussed. These deficiency letters sometimes adequately serve their purpose. For some occasions any instrument will suffice; the fact that axes will break thread does not justify the failure to use scissors. Sometimes these deficiency letters laboriously end in justice. Current economic conditions, however, cry out for expeditious handling of cases of extreme economic importance to the government and taxpayer. Because it is so little appreciated, it should be emphasized that the lack of precision and informal looseness of deficiency letters impedes the work of the Board of Tax Appeals, the collection of revenue and the early disposition of controversies.

^{35a}47 Stats. 233 (1932), 26 U.S.C.A. § 3271 (1932).

The essential elements of deficiency letters in practice are:

- (a) A recomputation of tax liability, item by item, according to the Commissioner's contentions; and
- (b) An explanation of the reasons for the adjustments which have been made.

In neither of these respects have they uniformity. In neither respect do they adequately give notice to the taxpayer as to what he must refute.

The tax recomputations are usually clear as far as they go. The trouble here is in the starting point. Reference to typical letters shows that they sometimes start with income *as per return*, and sometimes with income *as per a revenue agent's report*, and sometimes with income *as per a previously mailed letter*. Because the letters are often not self-contained, it frequently becomes necessary in preparing a petition to refer to extrinsic papers such as revenue agent's reports, 30-day letters and the like. The objection to the necessity of referring to extrinsic papers goes not only to the fact that it is difficult to assemble these papers. The real objection lies in the more difficult task of reconciling the various figures. In adjusting returns by partners, for example, the adjustment in the deficiency letter may be based upon the adjustment of the partnership return. The adjustment may or may not be readily available to the petitioner for any number of reasons.³⁶ In this connection it should be noted that there is no uniformity of practice in writing these 60-day letters. Not infrequently then laborious study is often necessary to discover what the letter means. Many letters cannot be understood without conference with the Bureau of Internal Revenue in Washington,³⁷ and this is not always possible in the 60-day period allowed for the filing of a petition.³⁸

The practice of incorporating by reference agent's reports, 30-day letters, etc. ignores pragmatic considerations. It assumes that the taxpayer can, upon the receipt of a deficiency letter, gather up the

³⁶As in the case of a retired or special partner.

³⁷In Washington because the file is then there, and it is usually inaccessible there because it is in transit.

³⁸The period cannot be extended. Van Fossan, *op. cit. supra* note 9 at 19, "This provision for filing a petition within 60 days has been construed by the Board and the Courts uniformly to be jurisdictional and a filing within 60 days is mandatory. This jurisdictional requisite has proven a stumbling block to thousands of would-be petitioners who through misunderstanding, delay of counsel or otherwise, have attempted to file their petitions subsequent to the expiration of the statutory period. This failure has necessarily resulted in the dismissal of all such cases."

other papers incorporated by reference and sit down to a complete understanding of his newly found liability. He cannot always do so; and if he can, it is only by a needlessly complicated reconciliation of several documents.

The defect in many 60-day letters lies not so much in the inadequate statement of the reasons underlying the Commissioner's determination; the real defect or vice lies in the failure to state the grounds or legal principles upon which the Commissioner relies.

It is not unreasonable to place upon the taxpayer the burden of proving his case. It is hardly reasonable to place upon him the burden of discovering what case he must prove. The reasoning of the Commissioner must be known to the taxpayer if he is to know what facts to plead and later to prove. If he does not know, he will, as a prudent taxpayer, plead and prove all facts which *may* be relevant as he *imagines* the Commissioner's contentions. Sometimes the imagination of the most speculative taxpayer is non-plussed. The result is at least waste,³⁹ often it is an unsound result. The taxpayer's petition is unnecessarily difficult to follow and the record is needlessly encumbered. Neither of these facts help the Board to quick and correct decisions. The citation of several specific illustrations again warrants a digression. A partnership return shows certain deductions for salaries paid to several individuals who have recently been employed by the partnership. The contract of employment requires these employees to give up their own business and to devote their efforts to the sale of the partnership services to the employee's former clients. The deduction is disallowed. Upon all the facts—not material to this discussion—counsel feels reasonably certain that the point at issue is whether the payments to the employees is a capital expenditure, i.e., payment for good will. On the other hand, he is not certain whether he must also prove, if he proves the payments are salaries, that the salary is *reasonable*.⁴⁰ And it is conceivable that the disallowance of the deduction is based simply on the fact that the salary is not reasonable; true it is that this is unlikely because in such a situation the Commissioner would doubtless allow part of the deduction.

³⁹As in the Alger-Sullivan case discussed *supra* note 17.

⁴⁰In Alger-Sullivan Lumber Co. v. Commissioner, *supra* note 17, the 60-day letter stated that "Your contention that the capital stock issued * * * to employees constituted a bonus and therefore an allowable deduction is denied. The information on file in this office discloses that the stock so issued constituted a sale of capital stock; a capital transaction in which no deduction may be allowed." The circuit court having found that the stock so issued was bonus stock, the taxpayer was in the dilemma of having offered no proof on the question of reasonableness—a material element in the deduction of compensation paid or incurred.

Take the simple case of the disallowance of a deduction for business expense. Is the disallowance based on the fact that the deduction is (1) not a business expense, or (2) that it is not an ordinary and necessary expense, or (3) that it is not reasonable (in the case of salary deductions)? Consider the disallowance of a worthless debt deduction. Is it based on the fact that the (1) debt is not worthless, or (2) if it is worthless, that it was not charged off in the year when ascertained to be worthless, or (3) that the debt was not charged off? These illustrations—and countless others could be given—are merely the simple cases and as such can be handled with reasonable dispatch. The point is that the same uncertainty carries over into the more complex cases. In addition thereto, the apparently simple examples cited frequently co-exist with more involved points and then the petition—and the record—become burdened with much matter which might be eliminated.

Consider the case⁴¹ of a taxpayer who excluded from income moneys received, from the state, for services rendered as an engineer. Upon the receipt of a deficiency letter which included the moneys as gross income the taxpayer was led to believe that the issue was a simple question of whether he was a state employee and so exempt.⁴² The Commissioner's theory, sustained by the board, was that the taxpayer was an independent contractor. On appeal the Circuit Court⁴³ pointed out that the finding that the taxpayer was an independent contractor entitled him to a deduction for business expense and that since this question had not been raised at the hearing before the board, the taxpayer was entitled to have the case remanded for a rehearing. Here we have an example of the expense and delay to both government and taxpayer which might otherwise be eliminated. Here both government and taxpayer find, after bearing the reasonable expense of a board hearing and appeal to the Circuit Court, that they are sent back to the board for a rehearing and then the taxpayer is not sure whether he is throwing good money after bad.⁴⁴

⁴¹Underwood v. Commissioner, 20 B.T.A. 1117 (1930), *rev'd* and remanded 56 F. (2d) 67 (C.C.A. 4th, 1932) petition for rehearing denied March 7, 1932.

⁴²Compensation paid state employees is exempt. Whether the taxpayer is a state employee is often a question of fact.

⁴³Underwood v. Commissioner, 56 F. (2d) 67 (1932).

⁴⁴See e.g., statement of the Circuit Court on the denial of the petition for rehearing Underwood v. Commissioner, (56 F. (2d) 67, 74): "If it shall appear at the hearing of the case by the Board that proper deductions for expenses have been allowed, the former decision of the board may be reaffirmed;". In other words, the taxpayer may be confronted with a new hearing which will consider whether the expenses were *proper* etc.

Let us be more specific in dealing with the results of this loose practice. They may be summarized as follows:

1. The preparation of the taxpayer's petition is rendered more than necessarily difficult; and when prepared it is apt to be needlessly complicated.

2. Taxpayers are too frequently required to amend petitions, which unreasonably adds to their work and the work of the General Counsel's office.

3. The burden of the preparation of the taxpayer for trial is increased.

4. Surprise at trials is not infrequent; in any event, the taxpayer has throughout the period antedating trial a sense of insecurity based upon a doubt whether he has understood the Commissioner's case.

5. The record is over-voluminous and less helpful to the member or members who have the responsibility of a decision.

6. The necessity for rehearings before the Board is multiplied; and as in the *Underwood* case⁴⁵ the Circuit Court of Appeals finds it more often necessary to remand cases for further evidence.

7. The expense of trial and appeal is augmented for both government and taxpayer.

8. The work of the Board is unduly increased, which makes for delay in a particular case and other pending cases.

The writer has not forgotten that deficiency letters are often prepared at the last moment before the expiration of the statute of limitations. Any requirements limiting the period now available to the Commissioner would be against public interest. But a change of requirement as to the *contents* of deficiency letters need have no such effect. The liberality extended to taxpayers in respect to amendments of the petition may be granted to the Commissioner in respect to amendments of the deficiency notice. The practice might be modified to permit the Commissioner to issue a 60-day letter which would indicate briefly one or more contentions on which the deficiency is based. Should the Commissioner find it desirable at some later date to base the deficiency on additional theories he could issue an amended letter and under the existing liberal practice of amending petitions the taxpayer could be given an opportunity to amend the petition to conform to the amended letter.

Better still would be a practice analogous to that extant in most jurisdictions whereby the statute of limitations can be tolled for a short period by the delivery of a summons to the sheriff.⁴⁶ The department could be given the opportunity to toll the statute by the sending of a preliminary deficiency letter to the taxpayer. It is submitted

⁴⁵*Supra* note 43.

⁴⁶See, for example, the provision in New York Civ. Prac. Act, § 17.

that the extension of the statute of limitations by a period of sixty days or less is, to the taxpayer, more desirable than a practice which would require the Commissioner to send out a letter within the normal statute of limitations and then to permit him to amend in order that the letter adequately inform the taxpayer of the basis for the Commissioner's deficiency. A practice permitting the Commissioner to amend his deficiency letter from time to time would be less desirable because it would either delay the preparation of petitions in the first instance or cause the taxpayer to amend the petition to conform to the amended deficiency letter.

The suggested change that the Commissioner be permitted to toll the statute by a preliminary 60-day letter is but one step in a modification of existing practice. It implies, of course, that the letter would serve merely to give notice of a deficiency and that it be followed by some other pleading from which the taxpayer would have adequate information on which to base his appeal.

The Board of Tax Appeals will soon round out its tenth year.⁴⁷ At the date of this writing⁴⁸ it has 16,829 cases⁴⁹ on its docket, and, on the whole, it has functioned with distinction in disposing of 53,437 cases. The difficulty lies not in the functioning of the Board but rather in the machinery designed to place the issues before the Board. It is submitted that the state of the practice warrants a reappraisal based on our decade of experience with Board practice. A study should be made of the present procedure with a view to improving the conditions set forth.^{49a}

As a basis for such study some consideration might be devoted to the following suggestions:

⁴⁷A brief reference to the board's historical background may be found in HOLMES, FEDERAL TAXES (6th Ed. 1925) § 4; see also *Old Colony Trust Co. v. Commissioner*, *supra* note 10.

⁴⁸These figures alone warrant some thought on technique designed to clear the docket of a number of cases.

⁴⁹Mr. Robert C. Tracy, Secretary of the Board, advises the writer that 70,266 cases were docketed with the Board up to February 28, 1933, that during March 575 new cases were filed and 28 reopened. Up to February 28, 1933 the board disposed of 53,437 cases, leaving 16,829 cases on the docket. During March the board disposed of a total of 763 cases, leaving 16,696 cases on hand at April 1, 1933. There were on the latter date 1789 cases pending before members for decision.

Of extreme importance to the correct procedure before the board is the fact that up to March 31, 1933 only 2407 cases were appealed to the circuit courts, 1739 having been disposed of to March 31, 1933.

^{49a}The history of procedural reforms, the Field Code in New York for example, indicates only too clearly that such reforms are necessarily the work of a group of persons representing the bench, the bar and the administration. The writer is not so presumptuous as to assume such a role.

(1) The informal 60-day letter should not form the basis of appeals to the Board of Tax Appeals.

(a) The letter should serve to notify the taxpayer that a deficiency has been determined. It should toll the statute of limitations for a short period.

(2) The actual appeal to the Board should be based on a more formal pleading originating with the Commissioner. His pleading should serve to notify the taxpayer of the theories on which the deficiency is determined; it may state any number of theories in the alternative and should not limit the Commissioner to an original choice of the correct theory.

(a) Some thought should be given a study of a modified motion practice which would test adequately the sufficiency of the litigant's theories.⁵⁰ Whether motions to strike out the "complaint" or "answer" for failure to state a cause of action would be feasible and desirable depends on:

(1) Whether the Board has sufficient jurisdiction for such practice, and

(2) Assuming the first point, would an extension of motion practice clutter up the Board's docket to the detriment of other controversies? Could this be obviated by provision for the award of costs to be imposed on the unsuccessful moving party?

(b) The Commissioner should be required to admit (in his answer) purely formal facts which are peculiarly within his own knowledge as well as certain facts which are contained in public records. An alternative provision might be made for the award of costs to the party put to the proof of formal facts peculiarly within the knowledge of the opponent.

In conclusion it should be said that the writer has not attempted to set forth all of the items of Board of Tax Appeals practice which require consideration and improvement, nor has he offered the above suggestions as being sufficient to cure the evils pointed out, or as limiting the study of what should be adopted as the procedure in respect to these evils. The idea has been, rather, simply to show that certain evils exist and that the time is ripe for an inventory of Board of Tax Appeals practice. The need for an improved procedure is particularly great at the moment because it is so necessary at this time to handle tax litigation inexpensively and expeditiously. Matters of procedure also affect the growth of a body of substantive tax law. Taxes will be with us for a long time, and the growth of a body of substantive law taxation has assumed an increased importance since the depression.

⁵⁰The writer is not unmindful of existing wide and liberal motion practice before the board. It apparently fills a need or it would not exist—if this is true, might it not be worth while to carry it to a logical conclusion and work out the problem of appeals from such motions?