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The Dangers of Symbolic Legislation: Perceptions and Realities of the New Burden-of-Proof Rules

Steve R. Johnson*

There is a growing political science and legal literature on the use of symbolism in the political and legislative process.¹ Tax law is a natural arena for such inquiry as tax law touches virtually every type of human interaction, is heavily value-driven, and is a perennial political battleground.² This article examines a recent tax law change—the enactment of new burden-of-proof rules in the summer of 1998—concluding that it is a pernicious exercise in symbolic legislation.

Burden-of-proof rules determine how much evidence a party must introduce at trial in order to prevail. In theory, a dispute-resolution system could operate without established burden-of-proof rules, but such a system would impose greater demands of perspicacity on its triers of fact and likely would be less predictable as to its outcomes.³ Thus, discussion and debate about what burden-of-proof rules should prevail have been part of our legal

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1. See, e.g., MURRAY EDELMAN, *THE SYMBOLIC USES OF POLITICS* (1964); CHARLES D. ELDER & ROGER W. COBB, *THE POLITICAL USES OF SYMBOLS* (1983); John P. Dwyer, *The Pathology of Symbolic Legislation*, 17 *ECOLOGY L.Q.* 233 (1990).

2. Some scholarship exists regarding symbolism in tax legislation. See, e.g., William Blatt, *The American Dream in Legislation: The Role of Popular Symbols in Wealth Tax Policy*, 51 *TAX L. REV.* 287 (1996); Michael Livingston, *Risky Business: Economics, Culture and the Taxation of High-Risk Activities*, 48 *TAX L. REV.* 163, 182-85 (1993) (stating that the Code is an important means of communicating cultural values between the nation and its citizens). The potential for further work along these lines is great.

3. A purely inquisitorial system (in which the court gathers the evidence) has less need for burden-of-proof rules. They are central, however, to our adversarial system which relies on the litigants to gather and present the evidence. See, e.g., JOHN H. WIGMORE, 9 *WIGMORE ON EVIDENCE* 276 (Chadbourn rev. 1970); Bruce L. Hay & Kathryn E. Spier, *Burden of Proof in Civil Litigation: An Economic Perspective*, 26 *J. LEGAL STUD.* 413, 413-15 & n.5 (1997). Solomon's threat to bisect the baby was a way to resolve a dispute between litigants who otherwise appeared to have presented equal proof. See 1 *Kings* 4:16-28. Because judges in our system may not have such an option available to them, they presumably would resolve a comparable dispute adversely to the party deemed to bear the burden of proof.

system for centuries.⁴

For generations, the allocation of the burden of proof in tax litigation was settled. With well understood exceptions, the taxpayer bore the burden of proof in civil tax litigation. In summer 1998, however, Congress unsettled the area. As part of major legislation restructuring the Internal Revenue Service,⁵ Congress created new Internal Revenue Code § 7491. This section provides that, if certain conditions are met and certain exceptions are avoided, the civil tax burden of proof is now on the Government.

However, those conditions and exceptions are so broad that they essentially swallow the rule. As a result, § 7491 will meaningfully alter allocation of the tax burden of proof in only rare cases. Section 7491 is a largely self-canceling section, but, despite that, not a harmless section. The uncertainties and frustrations bred by § 7491—indeed, by any section which “takes away with the left hand what it bestows with the right hand”—will decrease the efficiency of our system of dispute resolution and will reduce public support for our tax administration system.

This article examines these concerns in six parts. Part I is foundational. It describes the burden allocation that existed before enactment of § 7491, stressing its four key qualities: its longevity, flexibility, consistency with burden-of-proof theory generally, and widespread approval. Thereafter, Part I describes § 7491.

Part II details the conditions and exceptions in the new section. It demonstrates that major classes of tax litigants and tax issues are categorically ineligible for burden shifting. It further shows that, even when burden shifting is theoretically available, the limiting conditions imposed render such a shift, as a practical matter, largely worthless to taxpayers. Thus, § 7491 is without substance.

Two related questions are raised by the foregoing. If, as argued in Part I, the former rule was long established, well reasoned, and widely supported, why did Congress choose to write a new statute?⁶ Further, if Congress thought change really was needed, why did it write the new statute in

4. Thayer remarked that the subject of burden of proof “belongs to universal jurisprudence,” and he saw its roots extending back as far as Roman law. James B. Thayer, *The Burden of Proof*, 4 HARV. L. REV. 45, 47 (1890).

5. Internal Revenue Service Restructuring and Reform Act, Pub. L. No. 105-206, 112 Stat. 685 [hereinafter the “Restructuring Act”].

6. As late as 1996, there existed a “bipartisan consensus in the tax world that [reversing the burden of proof] would prove disastrous.” *Shifting the Burden of Proof to The IRS: Considering the Possibilities*, 72 TAX NOTES 1328, 1328 (1996); see, e.g., Jerry A. Kasner, *Why Burden-of-Proof Rules Will Affect Valuation Issues*, 81 TAX NOTES 239, 239 (1998) (calling § 7491 “an amazing change in the law”). Yet Congress enacted § 7491, which purportedly changes the burden, in 1998. In the space of two years, how did we get from the former bipartisan consensus to § 7491?

a way that defeats the possibility of substantial change in allocation of the burden?

These questions are addressed in Part III. It shows that Congress was responding to two conflicting forces: the desire to garner political advantage by chastising or curbing the IRS, and the reality that a true, general shift of the burden of proof would have enormous, adverse effects. Steering between these, Congress chose the path of symbolism. It enacted something that looks like a reassignment of the burden of proof (garnering political points) but which, practically, will have little or no effect on the outcomes of actual tax cases (avoiding the worst of the adverse effects).

The symbol, however, does not come free of cost. To say that § 7491 is ineffectual is not to say that it is innocuous. Parts IV and V explain the harms that Congress permitted in order to achieve its symbol. Part IV concentrates on harms to the tax controversy system, including reduced production of information on audit and increased expense and inconvenience at trial. Part V focuses on a more subtle but ultimately even more serious type of harm: reduced public confidence in, and support for, the nation's tax system.

Finally, Part VI offers a proposal. Before § 7491 was enacted, taxpayers usually bore the burden of proof in civil tax litigation although numerous specific, rifle-shot exceptions existed that placed part or all of the burden on the IRS when warranted by the nature of the issue or procedural circumstances. That was the responsible choice. Part VI proposes that Congress go "back to the future," reinstating a general rule placing the burden on taxpayers, ameliorated appropriately by specific, situational exceptions. It describes two alternative ways to accomplish that result.

I. SECTION 7491 AND ITS ANTECEDENT

Golden ages are mythic, and invocations of them usually are exercises in selective recall. The pre-§ 7491 regime was not perfect. As far as the imperfection of human affairs allows, however, it was pretty good. As shown in subparts I.A. through I.C., it was long standing, highly flexible, consistent with factors traditionally governing allocation of the burden of proof, and widely supported. Subpart I.D. describes § 7491.

A. LONG TENURE OF THE PRE-§ 7491 RULE

For over a century,⁷ it has been customary to distinguish between two

7. The pioneering work distinguishing between these two aspects of the burden of proof was done by James Bradley Thayer in the 1890s. See JAMES BRADLEY THAYER, A PRELIMINARY

aspects of the burden of proof: the duty of bringing forward evidence (the burden of production), and the risk of nonpersuasion (the burden of persuasion).⁸ Although courts and commentators are often less than precise in their use of terms in the area, the unelaborated term "burden of proof" is typically intended to mean only the burden of persuasion.⁹ That is my intended meaning when I use that term in this article.

In criminal tax litigation, both the burden and standard of proof are the same as in other varieties of criminal law. The Government prevails only if it proves the defendant-taxpayer guilty beyond a reasonable doubt.¹⁰

In civil tax litigation, however, it was settled, before enactment of § 7491, that the burden of proof typically was on the taxpayer, usually dischargeable through a preponderance of the evidence.¹¹ That rule enjoyed long tenure. The burden was placed on the taxpayer virtually from the beginning of the modern income tax, and that allocation had antecedents in federal tax law in the 1800s.

The most frequently cited case in this country's tax jurisprudence is the Supreme Court's 1933 decision in *Welch v. Helvering*.¹² Although that case is important in defining when business expenses are "ordinary and necessary" within the meaning of I.R.C. § 162, most citations to *Welch* relate to its statement of the allocation of the civil tax burden of proof: "[The Commissioner's] ruling has the support of a presumption of correctness

TREATISE ON EVIDENCE AT THE COMMON LAW 353 (1898); Thayer, *supra* note 4, at 8.

8. See, e.g., Director, Office of Workers' Compensation Programs, Dept. of Labor v. Greenwich Collieries, 512 U.S. 267, 272-75 (1994) (discussing the definition of burden of proof); Texas Dep't of Community Affairs v. Burdine, 450 U.S. 248, 252-58 (1981) (discussing the purpose behind the two aspects of the burden of proof); FLEMING JAMES, JR. ET AL., CIVIL PROCEDURE 337-43 (4th ed. 1992) (examining in treatise fashion the two burdens); 21 CHARLES A. WRIGHT & KENNETH W. GRAHAM, FEDERAL PRACTICE & PROCEDURE: EVIDENCE ¶ 5122 (1977) (examining in treatise fashion the two burdens); John T. McNaughton, *Burden of Production of Evidence: A Function of a Burden of Persuasion*, 68 HARV. L. REV. 1382, 1382-83 (1955).

9. See, e.g., Rockwell v. Commissioner, 512 F.2d 882, 887 (9th Cir. 1975), *cert. denied*, 423 U.S. 1015 (1975) (identifying the burden of persuasion as the burden of proof); WRIGHT & GRAHAM, *supra* note 8, at 555 (explaining the various uses of the term "burden of proof"); Theodore Ness, *The Role of Statutory Presumptions in Determining Federal Tax Liability*, 12 TAX L. REV. 321, 330 (1957).

10. E.g., *Holland v. United States*, 348 U.S. 121, 126 (1954).

11. E.g., *United States v. Janis*, 428 U.S. 433, 440 (1976) (stating that the burden of proof is on the taxpayer); *Helvering v. Taylor*, 293 U.S. 507, 515 (1935) (stating that "unquestionably the burden of proof is on the taxpayer"); *Anastasato v. Commissioner*, 794 F.2d 884, 887 (3d Cir. 1986) (stating that the burden of production and burden of persuasion are on the taxpayer); *Estate of Todisco v. Commissioner*, 757 F.2d 1, 6 (1st Cir. 1985) (stating that the burden of proof rests on the taxpayer).

12. 290 U.S. 111 (1933). A computer search on June 4, 1998, revealed 5733 citations to *Welch*.

and the [taxpayer] has the burden of proving it to be wrong.”¹³

Despite its vintage, however, *Welch* was far from the first occasion on which this burden had been cast on taxpayers. The burden of proof fell on taxpayers under the United States’ first income tax in 1862¹⁴ and under other revenue measures in the 1800’s.¹⁵ Thus, the former burden rules had “been in place for well over a century and [were] closely woven into the fabric of our [tax] system.”¹⁶

The rules for burden of proof governing tax cases applied without regard for the type of tax issue involved. Most federal tax cases are either prepayment suits in the Tax Court or bankruptcy court, or refund actions in the Court of Federal Claims, district court, or bankruptcy court.¹⁷ Although some differences existed among the various fora, the taxpayer typically bore the burden of proof regardless of where the case was tried. For example, from its inception, the Board of Tax Appeals (the forerunner of the Tax Court) imposed the burden on taxpayers in most instances.¹⁸ In ensuing revisions of its rules, the Tax Court repeatedly reaffirmed the general thrust of the Board’s rule.¹⁹

In a refund action, while the taxpayer’s burden is, in theory, higher than it is in a Tax Court case, the burden remained with the taxpayer. In Tax Court, the taxpayer discharges his burden of proof by showing that the IRS’s determination was arbitrary and excessive, whereupon the burden to show the correct amount of tax liability shifts to the IRS.²⁰ In a refund action, however, the taxpayer must do more than show the IRS’s determina-

13. *Id.* at 115.

14. *Former IRS Chiefs Say IRS Should Not Bear Burden of Proof in Court*, 95 TAX NOTES TODAY 75-20 (Apr. 18, 1995) (reproducing letter from 10 former IRS Commissioners to the Chairs of the House Ways & Means Committee and Senate Finance Committee).

15. See, e.g., *Arthur v. Unkart*, 96 U.S. 118, 122 (1877) (involving a refund action of federal import duties).

16. *Exploring the Development of Taxpayer Bill of Rights II Legislation: Hearings Before the Subcommittee on Oversight of the House Comm. on Ways & Means* 104th Cong. 40, 45 (1995) [hereinafter “*TBOR II hearing*”] (statement of Margaret Milner Richardson).

17. For a fuller discussion of the various tax trial tribunals, see Steve R. Johnson, *The Phoenix and the Perils of the Second Best: Why Heightened Appellate Deference to Tax Court Decisions Is Undesirable*, 77 OR. L. REV. 235, 238-42 (1998). Traditional descriptions of the tax trial system omit the bankruptcy court. However, the growing number, dollar magnitude, and sophistication of tax issues tried in that court require the bankruptcy court to be taken seriously as a tax trial forum. See *id.* at 240-42 (discussing the growing significance of the bankruptcy court as a tax trial forum).

18. See B.T.A. Rule 20 (July 1, 1924 ed.); see also *Avery v. Commissioner*, 22 F.2d 6, 8 (5th Cir. 1927) (stating that the burden of proof on taxpayers is a well-settled rule).

19. See generally TAX CT. R. 32; TAX CT. R. 142. For exceptions under these rules, see *infra* text accompanying notes 319 to 331.

20. See, e.g., *Helvering v. Taylor*, 293 U.S. 507, 515 (1934) (explaining this burden-shifting procedure).

tion was incorrect; she also must establish the amount of the refund to which she is entitled.²¹

A second difference also exists. Refund actions often involve counterclaim or set-off issues raised by the Government. The burdens as to such issues are complex and can shift between the parties.²² The matter is simpler in Tax Court prepayment cases. There, the IRS typically will raise all adjustments in the statutory notice of deficiency. If the IRS realizes there was an adjustment it missed, it will raise the adjustment in its pleadings and will bear the burden of proof as to that adjustment.²³

By contrast, although all bankruptcy courts impose at least some burden on the debtor-taxpayer, there is a split as to how great that burden is. In a bankruptcy proceeding, creditors may file proofs of claim reflecting what they believe the debtor owes them. A properly filed proof of claim constitutes *prima facie* evidence of both the validity and the amount of the debt or liability.²⁴ However, the debtor or bankruptcy trustee may object to the claim. If he does, and if he presents evidence to rebut the *prima facie* correctness of the claim, the creditor bears the ultimate burden of proof as to the claim.²⁵

Before the enactment of § 7491, when a tax issue was tried in bankruptcy court via objection to an IRS proof of claim, some courts concluded that the above scheme overrode the usual burden-of-proof allocation.

21. *Id.* at 514-15; see also *Lewis v. Reynolds*, 284 U.S. 281, 283 (1932); *Forbes v. Hassett*, 124 F.2d 925, 928 (1st Cir. 1942); Comment, *Burden of Proof in Tax Litigation: Offset and Equitable Recoupment*, 15 BUFF. L. REV. 616, 617-19 (1966).

This theoretical difference likely matters little. Evidence that the taxpayer presents to persuade the Tax Court that the IRS's determination was arbitrary and excessive typically also suffices (along with the other evidence introduced at trial) to permit reasonable determination of true tax liability. See IRA L. SHAFIROFF, INTERNAL REVENUE SERVICE PRACTICE AND PROCEDURE DESKBOOK 160 (2d ed. 1989).

22. In a case of some vintage, the Court of Claims (an ancestor of the current Court of Federal Claims) set out perhaps the most intricate allocation. It divided setoffs into four categories: (1) an item in the same tax period involving the same tax as the taxpayer's refund claim, (2) an item in the same period involving a different tax but which is related to and ultimately affects the amount of the tax liability at issue, (3) an item in the same period involving a different tax unrelated to the tax in the refund claim, and (4) an item in a different tax period involving any type of tax whether related or unrelated to the tax in the refund claim. The court held that the Government bears the burden as to setoffs of the third and fourth types and that, as to setoffs of the first and second types, the Government must present some substantial evidence in support of the setoff whereupon the burden settles on the taxpayer. *Missouri Pacific R.R. v. United States*, 338 F.2d 668, 670-71 (Ct. Cl. 1964).

For other discussions of the burden of proof as to counterclaims and setoffs in refund actions, see, for example, MARVIN GARBIS ET. AL., FEDERAL TAX LITIGATION 17-29 (1985).

23. TAX CT. R. 142(a) (1998).

24. 11 U.S.C. § 502(a) (West 1999); B.R. 3001(f).

25. *E.g., In re Holm*, 931 F.2d 620, 623 (9th Cir. 1991).

These courts held that, upon objection to the IRS's claim and presentation of evidence in support of the objection, the burden of persuasion was on the IRS.²⁶ Other courts, however, concluded that the character of the issue controlled over the forum in which it was being litigated, and therefore held that the usual burden-of-proof allocation applied even when a tax issue was being litigated in the bankruptcy court.²⁷

Thus, the former rule placing the burden generally on taxpayers had deep roots and was followed, with differences in detail, in all of the tax trial tribunals. As detailed in Appendix A, Congress and the courts did carve out exceptions, altering allocation of the burden in targeted, atypical situations. However, the very pattern of those localized exceptions emphasized the settled nature of the former general rule. An observation by congressional staff as to the presumption of correctness attaching to IRS determinations²⁸ has equal force with respect to the burden of proof:

Although this presumption is judicially based, rather than legislatively based, there is considerable evidence that the presumption has been repeatedly considered and approved by Congress. This is the case because the Internal Revenue Code contains a number of civil provisions that explicitly place the burden of proof on the [IRS] in specifically designated circumstances. The Congress would have enacted these provisions only if it recognized and approved of the general rule of presumptive correctness of the [IRS's] determination.²⁹

B. PRE-§ 7491 REGIME'S FLEXIBILITY AND CONSISTENCY WITH BURDEN-OF-PROOF THEORY

Although the pre-§ 7491 regime generally placed the burden of proof on the taxpayer, there were exceptions. There were dozens of situations in

26. *E.g.*, *In re MacFarlane*, 83 F.3d 1041, 1044-46 (9th Cir. 1996), *cert. denied*, 117 U.S. 1243 (1997); *In re Placid Oil Co.*, 988 F.2d 554 (5th Cir. 1993), *nonacq.*, 1995-1 C.B. 1.

27. *E.g.*, *In re Landmark Equity Corp.*, 973 F.2d 265 (4th Cir. 1992); *Resyn Corp. v. United States*, 851 F.2d 660, 663 (3d Cir. 1988).

The National Bankruptcy Review Commission's Tax Advisory Committee voted 9 to 1 in favor of the view that the normal burden allocation as to tax issues should apply in bankruptcy proceedings as well. FINAL REPORT OF TAX ADVISORY COMMITTEE OF NATIONAL BANKRUPTCY REVIEW COMMISSION, Item 211 (1997). The full Commission agreed and included this among its recommendations to Congress. NATIONAL BANKRUPTCY REVIEW COMMISSION RECOMMENDATIONS TO CONGRESS, Recommendation 3.2.5 (1997).

28. *See infra* text accompanying notes 150-59.

29. STAFF OF THE JOINT COMMITTEE ON TAXATION, DESCRIPTION OF SENATE FINANCE COMMITTEE CHAIRMAN'S MARK RELATING TO REFORM AND RESTRUCTURING OF THE INTERNAL REVENUE SERVICE 36 (JCX-17-98) (Mar. 26, 1998).

which, by statute, court rule, or judicial decision, part or all of the burden was placed on the IRS. These exceptions were in recognition of the unusual nature of particular issues or procedural postures and were an established part of the former regime. This system shows cases that regime's flexibility. Moreover, the total package—the burden generally on taxpayers but with situationally appropriate exceptions—comported well with the principles and factors that govern allocation of the burden of proof in our legal system generally. Thus, the pre-§ 7491 regime was not some special “break” or advantage for the IRS—it was consistent with burden-of-proof theory generally.

In developing these points, an organizational challenge looms. The two conclusions above—the flexibility of the former regime and its consistency with general burden theory—are important to the arguments in this Article. However, the road to those conclusions runs through many particulars. To develop them is a painstaking endeavor and is likely to excite only tax procedure specialists.

Thus, I have resorted to the device of developing the requisite particulars as to the prior rule's flexibility in Appendix A, and those as to the rule's consistency with general burden theory in Appendix B. Once the reader has waded through enough of them to be convinced of the accuracy of the two conclusions, I urge her to proceed to subpart I.C. for discussion of a further aspect of the previous regime.

C. WIDESPREAD SUPPORT FOR PRE-§ 7491 RULE

Over the long tenure of the pre-§ 7491 rule, occasional proposals were made to shift the burden of proof to the IRS as to all or most tax issues.³⁰ For instance, the original version of the first Taxpayer Bill of Rights contained a provision to shift the burden, but it was removed from the legislation before enactment.³¹ The most persistent advocate of reversal, Representative James A. Traficant, Jr., of Ohio, introduced a series of bills to this effect.³²

30. *E.g.*, H.R. 2389, 97th Cong. (1981).

31. The original version was in S. 604, 100th Cong. § 16(a) (1987), and H.R. 634, 100th Cong. § 11 (1987). The enacted version was Technical and Miscellaneous Revenue Act, §§ 6226-6235, 102 Stat. 3730-3737 (1988).

32. These included H.R. 5286, 103d Cong. (1994); H.R. 250, 104th Cong. (1995); H.R. 390, 104th Cong. (1995); H.R. 2450, 104th Cong. (1995); and H.R. 367, 105th Cong. (1997). Among other legislation introduced by Representative Traficant was H.R. 5005, 102d Cong. (1992), which would have provided: “Any person operating a trade or business in the State of Ohio shall be exempt from all Federal laws and regulations applying with regard to such a trade or business.”

For completeness, Representative Traficant's personal difficulties with the IRS should

What is striking about such proposals, however, is how relatively few there were, how handily they were defeated, and how general the opposition to them was. When a burden-shift proposal emerged—whether § 7491 or some prior proposal—a familiar coalition rallied against it.

First, tax administrators consistently opposed a general burden shift.³³ For example, ten former IRS Commissioners voiced their opposition to such a shift to the Chairs of the House Ways & Means Committee and the Senate Finance Committee. They stated: "It is clearly beyond the realm of possibility that our income tax system could continue in anything like its present form if this proposal were to become law."³⁴

Judges experienced with tax litigation also repeatedly explained the necessity of maintaining a system in which the burden of proof lay with the taxpayer. An original member of the Board of Tax Appeals made this point when testifying to Congress in 1925,³⁵ and subsequent judges have confirmed it in decisions,³⁶ legislative statements,³⁷ and commentary.³⁸

be noted. The IRS determined that he was liable for deficiencies and civil fraud penalties for failing to report and pay tax on bribes he received. The Tax Court and the Sixth Circuit upheld those determinations although Representative Traficant was acquitted of related criminal tax evasion charges. See Sheryl Stratton, *Shifting the Burden of Proof to the IRS: Considering the Possibilities*, 72 TAX NOTES 1328, 1329 (1996) (quoting former IRS Commissioner Donald C. Alexander: "Traficant has been pushing [reversing the burden of proof] ever since he found out, to his surprise, that bribes were income.").

Ironically, Representative Traficant still would have lost his Tax Court case even if his proposals had been the law. The IRS has long borne the burden of proof in fraud cases, even under the old regime. See *infra* text accompanying note 315.

33. See, e.g., *TBOR II hearing*, *supra* note 16, at 17 (1995) (statement of Cynthia G. Beerbower, Deputy Assistant Secretary of the Treasury for Tax Policy); *id.* at 40 (1995) (statement of Margaret Milner Richardson, Commissioner of Internal Revenue).

34. *Former IRS Chiefs Say IRS Should Not Bear Burden of Proof in Court*, 95 TAX NOTES TODAY 75-20 (Apr. 18, 1995) (reproducing letter from Shirley D. Petersen, Randolph W. Thrower, Donald C. Alexander, Mortimer M. Caplin, Sheldon S. Cohen, Roscoe L. Egger Jr., Fred T. Goldberg Jr., Lawrence B. Gibbs, Jerome Kurtz & Johnnie M. Walters).

Other statements of opposition from these former Commissioners include *TBOR II hearing*, *supra* note 16, at 136 (statement of Donald C. Alexander); *id.* at 130 (statement of Lawrence B. Gibbs); *id.* at 141 (statement of Sheldon S. Cohen); *id.* at 119 (statement of Fred T. Goldberg, Jr.); *IRS Restructuring and Oversight Hearings Before the Senate Finance Comm.*, 105th Cong., 2nd Sess. 282 (1998) [hereinafter "*IRS Restructuring*"] (statement of Fred Goldberg, Jr., Assistant Secretary of the Treasury for Tax Policy); *id.* at 264 (statement of Sheldon S. Cohen).

35. *Hearings on Revenue Revision, 1925, Before the House Comm. on Ways & Means*, 69th Cong. 908-09 (1925) (statement of James S. Ivins).

36. E.g., *Rockwell v. Commissioner*, 512 F.2d 882, 886-87 (9th Cir. 1975); *United States v. Rexach*, 482 F.2d 10, 16 (1st Cir. 1973), *cert. denied*, 414 U.S. 1039 (1973).

37. E.g., *Burden-of-Proof Provision Could Spur Disputes, Tax Court Chief Judge Says*, 98 TAX NOTES TODAY 12-58 (Jan. 20, 1998) (reproducing letter from Chief Judge Mary Ann Cohen to Senate Finance Committee).

In addition, tax academics argued against burden shifting. An important article written when Congress was considering the first Taxpayer Bill of Rights concluded that "the apparently attractive notion of making the tax collector's job more difficult [by reversing the burden of proof] is short-sighted and simplistic."³⁹ There was a notable outpouring of academic opposition to § 7491 at various phases in the legislative process⁴⁰ and criticism of it after its enactment.⁴¹ Other commentators also weighed in against a general shift of the tax burden of proof. The strong balance of such commentary supported the previous burden allocation in tax cases and opposed burden-shifting proposals.⁴²

Perhaps most interestingly, leading taxpayers' representatives also repeatedly spoke against a general shift of the tax burden of proof. At first blush, one might think that tax lawyers and other representatives would lead the chorus for the shift, but they have not. Recognizing that a shift would disadvantage honest taxpayers relative to dishonest ones,⁴³ could lead to more—not less—intrusive audits,⁴⁴ and would severely compromise

38. E.g., CCH TAXDAY, Oct. 22, 1997 (quoting Samuel Sterrett, former Chief Judge of the Tax Court); cf. Theodore Tannenwald, Jr., *The Erwin N. Griswold Lecture: The United States Tax Court: Yesterday, Today, and Tomorrow*, 15 AM. J. TAX POL'Y 1, 12-15 (1998) (detailing the difficulties that will be caused by § 7491).

39. Leo P. Martinez, *Tax Collection and Populist Rhetoric: Shifting the Burden of Proof in Tax Cases*, 39 HASTINGS L.J. 239, 282 (1988).

40. See, e.g., *Burden of Proof—Response to the Tax Profs*, 78 TAX NOTES 1066 (1998) (letter from Prof. Richard B. Malamud); *Reject Burden-of-Proof Shift, Urges Tax Prof*, 78 TAX NOTES 753 (1998) (reprinting letter from Prof. Bernard Wolfman to Senators William V. Roth, Jr., and Daniel Patrick Moynihan); *Tax Profs Urge Rejection of Burden-of-Proof Shift*, 78 TAX NOTES 755 (1998) (reprinting letter from ninety-seven tax professors to Senate Finance Committee members); *IRS Restructuring: Burden of Persuasion vs. Burden of Production*, 77 TAX NOTES 624 (1997) (reprinting letter from Prof. Calvin H. Johnson to Senator William V. Roth, Jr.); *Burden of Proof Shift Worries Tax Professors From Coast to Coast*, 77 TAX NOTES 623 (1997) (reprinting letter from Profs. Glenn Coven, Jerome Borison, John K. McNulty and Richard Westin to Senators William V. Roth, Jr., and Daniel Patrick Moynihan). Professor Daniel Q. Posin communicated his opposition electronically to Senator John Breaux of the Finance Committee in December 1997.

41. See Leandra Lederman, *Unforeseen Consequences of the Burden of Proof Shift*, 80 TAX NOTES 379 (1998) (arguing that the consequences of the burden of proof shift ultimately will be unfavorable to taxpayers). Another recent article concluded that § 7491 will usually have a negligible effect on the outcome of litigated tax cases but could give taxpayers a strategic advantage in some instances. Nathan E. Clukey, *Examining the Limited Benefits of the Burden of Proof Shift*, 82 TAX NOTES 683 (1999).

42. E.g., Lee A. Sheppard, *Shifting the Burden or Just Shifting the Blame?*, 77 TAX NOTES 484 (1997); Note, *The Presumption of Correctness: Should the Commissioner Be Required To Carry the Initial Burden of Production*, 55 FORDHAM L. REV. 1087, 1108 (1987).

43. See *infra* notes 216-19 and accompanying text.

44. See *infra* notes 191-206 and accompanying text.

the effectiveness of our tax system,⁴⁵ responsible taxpayers' representatives acknowledged that their interests and those of their clients are better served by leaving the burden on the taxpayer in most instances. In recent years, this view has been expressed by, among others, representatives of the American Bar Association Section of Taxation,⁴⁶ the New York State Bar Association Tax Section,⁴⁷ the Tax Executives Institute,⁴⁸ the Community Tax Law Project,⁴⁹ the National Association of Enrolled Agents,⁵⁰ individual taxpayers' representatives, and others.⁵¹

Of course, unanimity in these affairs is not to be expected, and so, inevitably, occasional voices advocated burden shifting.⁵² What is notable, however, is the rarity of such voices and the overwhelming consensus that the burden of proof generally should rest on the taxpayer, not the IRS.

D. SECTION 7491

The Restructuring Act had its roots in the work of the National Commission on the Restructuring of the Internal Revenue Service, popularly known as the Kerry-Portman Commission.⁵³ The Commission presented its

45. See *infra* notes 207-15 and accompanying text.

46. E.g., *IRS Restructuring*, *supra* note 34, at 417 (statement of Stefan F. Tucker); *Recommendations of the National Commission on Restructuring the Internal Revenue Service and Taxpayer Protections and Rights, Hearings Before the Subcomm. on Oversight of the House Comm. on Ways & Means*, available in 1997 WL 14151435, at *49 (1997) (statement of Pamela F. Olson); *TBOR II hearing*, *supra* note 16, at 158 (statement of N. Jerold Cohen).

47. E.g., *NYSBA Urges Slowdown of Burden-Shift Express*, 77 TAX NOTES 619 (1997) (reprinting letter from Richard O. Loengard Jr. to Representatives Bill Archer and Charles Rangel); New York State Bar Ass'n, *Memorandum to the Members of the House Ways & Means Subcommittee on Oversight, Re: H.R. 390—Burden of Proof in Tax Cases*, Tax Rep. no. 832 (Mar. 23, 1995) (on file with author).

48. *Tax Executives Institute Comments on IRS Reform Bill*, 79 TAX NOTES 1411 (1998); Paul Cherecwich, Jr., *Law 101: Burden of Proof Differs in Civil and Criminal Cases*, 77 TAX NOTES 489 (1997) (reprinting letter to Representative Bill Archer). The Tax Executives Institute represents about 5000 in-house tax professionals employed by 2800 of the leading companies in the United States and Canada.

49. *IRS Restructuring*, *supra* note 34, at 329 (statement of Nina E. Olson).

50. *TBOR II hearing*, *supra* note 16, at 146 (statement of Joseph F. Lane).

51. E.g., *IRS Restructuring*, *supra* note 34, at 367 (1998) (statement of Michael I. Saltzman); Carolyn Joy Lee, *Tax Professionals Lick Chops in Anticipation of Burden of Proof Shift*, 77 TAX NOTES 622 (1997) (reprinting letter to Representative Bill Archer).

52. In 1925, a representative of the American Institute of Accountants unsuccessfully urged burden reversal. *Hearing on Revenue Revision, 1925, Before the House Comm. on Ways & Means*, 69th Cong. 877 (1925). More recent advocates include Douglas C. Burnette in *IRS Restructuring*, *supra* note 34, at 233, 238 and Bernard J. Long, Jr., *Burden of Proof Shift: Tom Jefferson Would Be Proud*, 77 TAX NOTES 625 (1997).

53. Congress created the Commission in 1995. See Treasury, Postal Service, and General Government Appropriations Act, Pub. L. No. 104-52, 109 Stat. 468 (1996) (appropriating

report in June 1997. The Commission considered the burden of proof matter, but it made no recommendation in its report.

Legislation was introduced to enact some of the Kerry-Portman recommendations.⁵⁴ Like the Commission's report, the bill, as originally introduced, contained no burden-of-proof provision. In mark-up in the House Ways and Means Committee, however, Chairman William Archer inserted a burden provision into the bill.⁵⁵ The committee recommended the bill to the full House, and the House overwhelmingly approved it. The following year, the Senate Finance Committee recommended its version of a Restructuring Act—including a burden-of-proof provision—and the full Senate approved it after floor amendment.

The House and Senate versions of the burden-of-proof provision differed. The Conference Committee adopted the Senate versions with minor changes. Both houses approved the Restructuring Act, including the burden-of-proof provision, by lopsided majorities.⁵⁶

The general burden rule under the new legislation, codified in § 7491(a), is as follows:

- (1) General rule. If, in any court proceeding, a taxpayer introduces credible evidence with respect to any factual issue relevant to ascertaining the liability of the taxpayer for any tax imposed by subtitle A or B [of the Code], the [IRS] shall have the burden of

funds to government agencies). It was co-chaired by Senator Robert Kerry and Representative Rob Portman.

54. See, e.g., H.R. 2292, 105th Cong. (1997).

55. H.R. 2676, 105th Cong. § 301 (1997). Under § 301 of the House bill, § 7491 would have read as follows:

(a) GENERAL RULE. The [IRS] shall have the burden of proof in any court proceeding with respect to any factual issue relevant to ascertaining the income tax liability of a taxpayer.

(b) LIMITATIONS. Subsection (a) shall only apply with respect to an issue if—

(1) the taxpayer asserts a reasonable dispute with respect to such issue,
(2) the taxpayer has fully cooperated with the [IRS] with respect to such issue, including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer, as reasonably requested by the [IRS], and
(3) in the case of a partnership, corporation, or trust, the taxpayer is described in section 7430(c)(4)(A)(ii).

(c) SUBSTANTIATION. Nothing in this section shall be construed to override any requirement of this title to substantiate any item.

Id.

56. The vote in the House was 402 to 8; the vote in the Senate was 96 to 2. The President signed the Restructuring Act on July 22, 1998.

proof with respect to such issue.

(2) Limitations. Paragraph (1) shall apply with respect to an issue only if—

(A) the taxpayer has complied with the requirements under [the Code] to substantiate any item,

(B) the taxpayer has maintained all records required under this title and has cooperated with reasonable requests by the [IRS] for witnesses, information, documents, meetings, and interviews, and

(C) in the case of a partnership, corporation, or trust, the taxpayer is described in [Code] section 7430(c)(4)(ii).

(3) Coordination. Paragraph (1) shall not apply to any issue if any other provision of [the Code] provides for a specific burden of proof with respect to such issue.

In addition, the legislation enacted two specific burden-of-proof rules. First, § 7491(b) provides, with respect to individual taxpayers, that the IRS has “the burden of proof in any court proceeding with respect to any item of income which was reconstructed by the [IRS] solely through the use of statistical information on unrelated taxpayers.”

Second, § 7491(c) deals with penalties. It provides, again with respect to individual taxpayers, that the IRS has “the burden of production in any court proceeding with respect to the liability . . . for any penalty [or similar addition to tax].”

All portions of new § 7491 are effective with respect to court proceedings relating to IRS examinations beginning after July 22, 1998, the date of enactment of the Restructuring Act.⁵⁷ The provision that created new § 7491 was the first of the over seventy items included in the “Taxpayer Protection and Rights” title of the Restructuring Act. Presumably, this was not accidental, but instead reflected the importance, whether real or symbolic, Congress attached to § 7491.

57. Internal Revenue Service Restructuring Reform Act of 1998, Pub. L. No. 105-206, § 3100(c)(1), 112 Stat. 726 (1998). If no examination occurs, § 7491 is effective for court proceedings relating to tax periods beginning after, or events occurring after, July 22, 1998. § 3100(c)(2).

For these purposes, “[a]n audit is not the only event that would be considered an examination.” Specifically, the matching of an information return against the tax return and the review of refund claims are “examinations” for effective date purposes. H.R. REP. NO. 105-599, at 242 (1998) (Conf. Comm.).

On the whole, § 7491(a) as enacted is more narrow than the version passed by the House;⁵⁸ that is, § 7491(a) as enacted is less likely to result in burden shifting. The House version was more limited in two respects: it applied only to income taxes, not transfer taxes, and required the taxpayer to "fully" cooperate with the IRS. It is unclear, however, if the courts will interpret the "cooperation" condition as enacted as falling far short of full cooperation.

Moreover, the enacted version is more limited than the House version in ways that are likely to prove significant. First, § 7491(a)(1) requires that the taxpayer present "credible evidence," which is likely a higher standard than the requirement set forth in the House bill, that the taxpayer is asserting "a reasonable dispute."⁵⁹ Second, § 7491(a)(2)(A) requires that the taxpayer comply with all substantiation rules "under" the Code, as opposed to substantiation rules "of" the Code under the House bill.⁶⁰ The "under" language more clearly includes substantiation requirements in the Treasury Regulations promulgated under the Code. The "of" language might have limited compliance to substantiation requirements in the statute. Third, § 7491(a)(2)(B) requires the taxpayer to maintain required records as a condition of a burden shift.⁶¹ There was no comparable requirement in the House version. Thus, the House bill would have encouraged taxpayers not to make and keep original documentation of transactions. Fourth, § 7491(a)(3) provides that the general rule of § 7491(a) yields to specific burden-of-proof rules elsewhere in the Code.⁶² Again, the House bill had no such requirement.

Thus, to those—like me—dubious of the enterprise of shifting the burden of proof in tax cases generally, the rule now on the books is less objectionable than the rule originally passed by the House. The Senate legislative history does not discuss whether that body intended to weaken the House version of the legislation or why the Senate considered the above changes necessary. The absence of such discussion is perhaps further support for the argument of this Article that § 7491 was not intended as a serious substantive measure.

58. For the text of the House's version of the rule, see *supra* note 55.

59. See *infra* notes 160-63 and accompanying text.

60. See *infra* notes 139-45 and accompanying text.

61. See *infra* notes 138, 146-47 and accompanying text.

62. See *infra* notes 120-36 and accompanying text. However, there is a constructional principle that subsequently enacted general statutes do not oust more specific, prior statutes absent clearly expressed intent to this effect. *E.g.*, *Kepner v. United States*, 195 U.S. 100, 125 (1904); *Coleman v. United States*, 363 F.2d 190, 199 (9th Cir. 1966). If courts applied this principle, they would have reached the same result even under the House version of § 7491.

II. SYMBOL WITHOUT SUBSTANCE

The general burden rule in the Restructuring Act is contained in § 7491(a). Subsections § 7491(b) and (c) harbor specific rules dealing with statistical information and penalties, respectively.⁶³ To the extent they have practical significance, subsections (b) and (c) could have been enacted separately, without the general rule of subsection (a).⁶⁴ The question, then, is whether § 7491(a) provides anything of meaning.

This article contends that it does not. Congress hedged § 7491(a) with many conditions and exceptions and, as a result, rendered the section empty. There are eleven limitations, of varying degrees of significance, on the burden shift under § 7491(a). For completeness, I mention all eleven below, in the order in which they appear in the statute.⁶⁵ However, as developed hereafter, they are not of equal significance. The limitations include:

(1) The shift applies, if at all, only to "court proceedings," not to administrative proceedings.⁶⁶

(2) Any shift is predicated upon the taxpayer's introduction of "credible evidence" as to the issue in controversy.⁶⁷

(3) The shift applies only to "factual issue[s]."⁶⁸

(4) The shift applies only to issues "relevant to ascertaining the liability of the taxpayer" for tax.⁶⁹ Thus, cases involving issues other than liability and cases involving the liability of persons other than the taxpayer are outside the ambit of § 7491.

(5) The shift applies only to controversies involving taxes "imposed by subtitle A or B [of the Internal Revenue Code]," *i.e.*, only to the income, estate, gift, and generation-skipping transfer taxes.⁷⁰

(6) Only "the burden of proof" can shift,⁷¹ thus leaving intact the presumption of correctness in favor of the IRS.⁷²

(7) The taxpayer's compliance with all applicable statutory and regu-

63. See *infra* notes 282-88 and accompanying text.

64. This would have been in keeping with the many situational, localized burden shifts under the prior regime. See *infra* Appendix A pp. 70-77.

65. For the full text of I.R.C. § 7491(a), see *supra* pp. 12-13.

66. I.R.C. § 7491(a)(1).

67. *Id.*

68. *Id.*

69. *Id.*

70. *Id.* Self-employment taxes are treated as income taxes for this purpose. H.R. REP. NO. 599, *supra* note 57, at 242 n.15.

71. I.R.C. § 7491(a)(1).

72. See *infra* notes 150-59 and accompanying text (discussing the presumption of correctness).

latory substantiation requirements is prerequisite to any burden shift.⁷³

(8) To qualify for the burden shift, the taxpayer must have maintained "all records" required by the Code and Regulations.⁷⁴

(9) The burden will shift only if the taxpayer "has cooperated with reasonable requests by the [IRS] for witnesses, information, documents, meetings, and interviews."⁷⁵

(10) Large partnerships, corporations, and trusts are not eligible for the burden shift.⁷⁶

(11) Other Code sections providing for specific burden rules supersede § 7491(a).⁷⁷

The taxpayer bears the burden of proving that she satisfies the conditions for burden shifting.⁷⁸ In other words, the taxpayer bears the burden of proof as to who bears the burden of proof in a specific factual scenario.

Cumulatively and, in some instances, individually, these limitations eviscerate a general burden shift. In terms of their effects, the limitations fall into two groups: those that prevent the burden from shifting at all, and those that permit the shift but denude it of practical significance.

A. LIMITATIONS PREVENTING BURDEN SHIFT

Many of the above conditions and exceptions prevent shifting of the burden of proof. The first is likely to be fairly unimportant, and therefore can be disposed of quickly. Section 7491(a) applies only in a "court proceeding."⁷⁹ Most tax controversies, of course, never get to court and, instead, are resolved in administrative proceedings, such as audits, supervisory conferences, and conferences with the Appeals Office. On occasion, Revenue Agents or Appeals Officers have taken a mulish view of the burden of proof, saying to the taxpayer "you'll have to prove that to me," then labeling as "insufficient" reasonable attempts by the taxpayer to do just that. In theory, this still could happen under § 7491(a). However, such conduct

73. I.R.C. § 7491(a)(2)(A).

74. I.R.C. § 7491(a)(2)(B).

75. *Id.*

76. See I.R.C. § 7491(a)(2)(C) (noting that in order to qualify under this statute when the taxpayer is a "partnership, corporation, or trust," the taxpayer must meet the requirements outlined in § 7430(4)(A)(ii)).

77. I.R.C. § 7491(a)(3).

78. H.R. REP. NO. 599, *supra* note 57, at 240. The legislative history of the House version of § 7491 was to the same effect. H.R. REP. NO. 105-364, at 57 (1997) ("Taxpayers who fail to substantiate any item . . . will . . . be unable to avail themselves of this provision regarding the burden of proof.").

79. I.R.C. § 7491(a)(1).

has always been contrary to IRS policy⁸⁰ and, fortunately, rarely occurs. Thus, excepting administrative proceedings from § 7491(a) likely will have little significance.⁸¹

However, as discussed below, other categorical limitations should prove to be more significant. The importance of each will depend on court interpretation. The predictions below are based on the statutory language, history, and the case law background on which they are superimposed. Bear in mind that technical correction legislation is always possible to cure unintended consequences of legislative inadvertence or sloppy drafting.⁸²

1. "Liability of the Taxpayer" for Designated Types of Taxes

Section 7491(a) applies only to the taxes imposed by subtitles A and B of the Code,⁸³ which apply only to cases that involve federal income, estate, gift, and generation-skipping transfer taxes. Thus, the section does not apply to cases involving the employment taxes imposed by subtitle C or the excise taxes imposed by subtitles D and E. These omitted taxes raise significant revenue amounting to approximately a third of the federal tax take.⁸⁴ Although they are involved in fewer controversies than the income tax, employment and excise taxes have generated thousands of litigated cases.

As to the taxes to which it does apply, a generous construction of the statute's "liability of the taxpayer" language seems appropriate to effectuate the section's purpose, and this will obviate some potential problems. For

80. See, e.g., I.R.M. 4244.

81. For a view that such a limitation does matter, see *IRS Restructuring*, *supra* note 34, at 238 (statement of Douglas C. Burnette, National Society of Accountants) (arguing that the bill would make the IRS insist on "intensive examination" during audits in order to show full cooperation on the part of the taxpayer).

One could argue that § 7491(a) would further discourage such untoward behavior, that it would be especially short-sighted for the IRS to "demand strict proof" at audit or Appeals if the IRS would bear the burden of proof at trial. The problem with such an argument, though, is that, because of the other conditions and exceptions discussed in Part II, there rarely will be a meaningful burden shift to the IRS at trial, even under § 7491(a).

82. Assuming, of course, that the future Congress feels the same way about § 7491 as the enacting Congress did, that Congress perceives the problem and, given competing demands for attention, cares enough to effect correction, that a political "critical mass" forms behind a given solution, and that no accident of the legislative process shelves or defeats the effort. All these are significant "ifs." Technical correction of § 7491(a) is possible but uncertain, especially if Congress truly cared more about the section as symbol than as substance.

83. I.R.C. § 7491(a)(1).

84. For the fiscal year ending September 30, 1996, employment taxes represented 33.1% of federal taxes collected and excise taxes represented 2.8%. INTERNAL REVENUE SERVICE DATA BOOK: OCTOBER 1, 1995 TO SEPTEMBER 30, 1996, at 3 tbl. 1 (1997).

instance, the Tax Court has jurisdiction to hear unified partnership cases,⁸⁵ and jurisdiction to hear declaratory judgment actions relating to retirement-plan qualification, tax-exempt status of state and local governmental obligations, and qualification or classification of exempt organizations and foundations.⁸⁶ Often, the entity litigating the case will not have its own tax liability on the line. Instead, the impact ultimately will be on the tax liability of others associated with the entity, such as the partners in the partnership, the holder of the state or local bond, or the contributors to the charity who wish to deduct their contributions. The "liability of the taxpayer" language should not be interpreted so narrowly as to exclude such cases from the ambit of § 7491. The disposition of these cases will directly affect how much tax is owed by persons who are taxpayers, and that should suffice.

However, even under a generous reading of the language in question, § 7491(a) does not include all cases involving federal income, estate, gift, and generation-skipping transfer taxes. At least three classes of cases appear to be outside the statutory language.

First, many tax cases—particularly in district court and bankruptcy court⁸⁷ are collection cases.⁸⁸ In these cases, there usually is no dispute about liability. It is acknowledged that the taxpayer owes tax; the issue typically is whether the IRS has properly used one or another of the collection tools at its disposal.⁸⁹ Since "liability" is not at issue, § 7491(a) would not seem to apply and, thus, the burden of proof would not shift in such collection cases.

Second, when the IRS makes a jeopardy or termination assessment of tax (shortcutting the normal deficiency procedures), taxpayers are entitled to administrative and judicial review of the assessment in district court and

85. See TAX CT. R. 240-251 (discussing the Tax Court Rules that apply in partnership actions).

86. See TAX CT. R. 210-218 (discussing the Tax Court Rules that apply in declaratory judgment actions).

87. Certain collection matters also may be at issue in collateral proceedings in the Tax Court. See *infra* notes 339-43 and accompanying text (discussing the circumstances under which the Tax Court can enjoin the collection of tax).

88. For descriptions of the tax collection process, see MICHAEL I. SALTZMAN, *IRS PRACTICE AND PROCEDURE* ch. 14 (1991); James K. Wilkens & Thomas A. Matthews, *A Survey of Federal Tax Collection Procedure: Rights and Remedies of Taxpayers and the Internal Revenue Service*, 3 ALASKA L. REV. 269 (1986).

89. Some Supreme Court cases are illustrative. In *United States v. Rodgers*, 461 U.S. 677 (1983), the IRS imposed tax liens on, and sought judicial sale of, homestead property. The Court held that this practice is valid, subject to certain equitable principles. *Id.* at 680. In *United States v. National Bank of Commerce*, 472 U.S. 713, 719-33 (1985), the Court upheld an IRS levy on joint bank accounts to satisfy tax debts of one of the depositors. In both cases, the existence and amounts of the tax liabilities were uncontroversial. The disputes related to the amenability of the assets at issue to enforced collection by the IRS.

sometimes the Tax Court. Such review involves two issues: whether the making of the assessment was reasonable and whether the amount assessed was reasonable.⁹⁰ It is well established that a § 7429 case is a preliminary proceeding and that the determinations reached in it will have “no effect upon the determination of the correct tax liability in a subsequent proceeding. [The § 7429 case] is unrelated, substantively and procedurally, to any subsequent [Tax Court or refund] proceeding to determine the correct tax liability.”⁹¹ Accordingly, § 7429 cases also seem to be outside the reach of § 7491.⁹²

Third, a significant trend in tax procedure in the last decade has been the increase, via the various Taxpayer Bills of Rights, in the Tax Court’s jurisdiction over various special or ancillary proceedings. These proceedings divide into three classes for § 7491(a) purposes: those to which the section does apply;⁹³ those to which § 7491(a) does not apply, but which are covered by other burden rules;⁹⁴ and those to which neither § 7491(a) nor any other specific burden rule applies (for example, a proceeding to compel the IRS to make refunds of determined overpayments).⁹⁵ These proceedings do not relate to the liability of the taxpayer. Thus, § 7491(a) would not authorize imposition of the burden of proof on the IRS in such proceedings.⁹⁶

2. Eligible Taxpayer

Congress’s professed concern with respect to the burden of proof was protection of individual taxpayers and small business taxpayers.⁹⁷ Consis-

90. I.R.C. § 7429(b)(3)(A) (1994).

91. S. REP. NO. 94-938, pt. 1, at 365 (1976), *reprinted in* 1976 U.S.C.A.N. 3439, 3795.

92. I.R.C. § 7429(g)(1) contains special burden-of-proof rules for jeopardy and termination assessment review cases. See *infra* text accompanying notes 311-13.

93. See, e.g., TAX CT. R. 261 (giving the Tax Court authority, under certain conditions, to redetermine interest on a deficiency); TAX CT. R. 280-84 (giving the Tax Court authority to review IRS failures to abate interest). The Code provides that interest “shall be assessed, collected, and paid in the same manner as taxes.” I.R.C. § 6601(e)(1). That should put interest-liability cases within the scope of § 7491(a).

94. See, e.g., TAX CT. R. 230-233 & 270-274 (giving the Tax Court authority to hear actions for litigation and administrative costs); Tax Ct. R. 220-229A (granting the Tax Court authority to hear disclosure actions). These do not determine a taxpayer’s liability for tax, so would be outside § 7491(a). However, they are governed by their own pre-existing burden-allocation rules. TAX CT. R. 229, 232(f) & 270(d).

95. See TAX CT. R. 260 (describing proceedings to enforce overpayment determinations).

96. A case could be made that, because the IRS is in a better position to know whether a refund was made and, if not, why not, the burden of proof in such proceedings should be imposed on the IRS by judicial decision. However, the matter is not settled.

97. “The committee is concerned that individual and small business taxpayers frequently

tently with that end, Congress excepted large entities from the "benefit" of § 7491. Through cross-reference to § 7430,⁹⁸ Congress provided that § 7491(a) will not shift the burden in cases in which the taxpayer is a corporation, trust, or partnership with a net worth in excess of \$7,000,000.⁹⁹

This exception will be of only limited importance as to trusts. Certain kinds of trusts can be taxpayers,¹⁰⁰ and a few important cases have featured trusts as the taxpayers.¹⁰¹ Still, the number of litigated cases which involve trusts as taxpayers is small.¹⁰²

The exception also will be of only limited importance with regard to partnerships. Indeed, an argument could be made that a partnership cannot be a "taxpayer" as that term is used in § 7491(a), thus rendering this exception meaningless as to partnerships. Partnerships do not pay estate, gift, generation-skipping transfer taxes, or income taxes.¹⁰³ Partnerships are litigants in TEFRA unified partnership proceedings,¹⁰⁴ but their role there

are at a disadvantage when forced to litigate with the Internal Revenue Service. The committee believes that the present burden of proof rules contribute to that disadvantage." H.R. REP. NO. 105-364, *supra* note 79, at 56.

98. Section 7430 provides that, if certain conditions are met, a victorious taxpayer may recover from the IRS some or all of the taxpayer's administrative and litigation costs incurred to contest IRS adjustments. I.R.C. § 7430. Concluding that large taxpayers can protect themselves, however, Congress excepted them from eligibility for such cost shifting.

99. Section 7491(a) "shall apply with respect to an issue only if . . . in the case of a partnership, corporation, or trust, the taxpayer is described in section 7430(c)(4)(A)(ii)." I.R.C. § 7491(a)(2)(C). The referenced provision in § 7430 itself references another statute, 28 U.S.C. § 2412(d)(1)(B) (as in effect on October 22, 1986). The substance of the rule is that entities with net worth over \$7,000,000 as of the date the action commences are excluded from eligibility. *E.g.*, Treas. Reg. § 301.7430-5(f)(2); H.R. REP. NO. 599, *supra* note 57, at 240.

100. See I.R.C. §§ 641-668 (defining, among other things, what kinds of trusts can be taxpayers).

101. *E.g.*, Metzger Trust v. Commissioner, 693 F.2d 459 (5th Cir. 1982); Haft Trust v. Commissioner, 510 F.2d 43 (1st Cir. 1975); Commissioner v. Morris Trust, 367 F.2d 794 (4th Cir. 1996); Quick's Trust v. Commissioner, 54 T.C. 1336 (1970), *aff'd per curiam*, 444 F.2d 90 (8th Cir. 1971).

102. There are numerous cases in which the IRS has sought to disregard family trusts or business trusts under assignment-of-income principles, the sham-transaction doctrine, or other theories. *E.g.*, Vnuk v. Commissioner, 621 F.2d 1318 (8th Cir. 1980) (a case in which the IRS sought to disregard a family trust under assignment-of-income principles). However, in such cases the deficiency notices are issued to the creators or beneficiaries of the "trust" and the creators or beneficiaries are the petitioners seeking relief in court. *Id.* at 1319. Since such cases do not involve a trust as the "taxpayer" within the meaning of § 7491(a), the net-worth exception would not apply to them. (Other exceptions likely would, however. For instance, those creating sham trusts are unlikely to cooperate with the IRS on audit.)

103. See, *e.g.*, I.R.C. § 701 (exempting partnerships from income tax).

104. See I.R.C. §§ 6221-6233 (describing the tax treatment of partnership items). These sections were added to the Code by the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA"), Pub. L. No. 97-248, §§ 402-406, 96 Stat. 324 (1982). Since 1997, there also has been a unified audit system for electing partnerships with over 100 members. See I.R.C. §§

is as representative rather than as real-party-in-interest.¹⁰⁵ They are petitioners, but they are not "taxpayer[s]," which is the operative word for § 7491(a) purposes. Yet, the courts usually are loathe to interpret a statute so as to render any part of it meaningless.¹⁰⁶ If that approach is applied in this context, the likely construction would be that § 7491 cannot apply when the partnership in a TEFRA case has a net worth over \$7,000,000 dollars. Such cases, however, are not numerous.

The exclusion from § 7491(a) of corporations with net worth over \$7,000,000 dollars is a significant exception. Such taxpayers represent the great bulk of the revenue involved in audit adjustments proposed by the IRS. Coordinated Examination Program (CEP) taxpayers are only a subset of corporations exceeding the § 7491(a) net worth threshold, yet about two-thirds of the total dollar amount of adjustments proposed by IRS auditors are proposed with respect to CEP taxpayers.¹⁰⁷

3. Factual Issues

"For purposes of standard of review, decisions by judges¹⁰⁸ are traditionally divided into three categories: denominated questions of law (reviewable *de novo*), questions of fact (reviewable for clear error), and matters of discretion (reviewable for 'abuse of discretion')."¹⁰⁹ "Matters of discretion" typically are procedural in nature, and the substantive issues in tax cases involve the other two categories.

By its terms, § 7491(a) applies only to "factual issue[s],"¹¹⁰ not to legal

6240-6255 (describing large partnership treatment).

105. In cases subject to the TEFRA rules, the tax treatment of an item is determined at the partnership level. I.R.C. § 6221. If a dispute exists as to an item, the tax matters partner (or, in some cases, another partner) may file a petition on behalf of the partnership contesting the IRS's determination. I.R.C. § 6226(a) & (b); *see* TAX CT. R. 240(d) & 241 (describing commencement of partnership action). However, the partners themselves also are considered as parties to the action, I.R.C. § 6226(c), and partners not originally named may intervene in the action, TAX CT. R. 245. If the IRS prevails in the case, it will be the partners themselves (not the partnership) against whom the IRS will make assessments and from whom the IRS will collect additional amounts due. I.R.C. §§ 6225 & 6230; Treas. Reg. § 301.6231(a)(6)-1(a).

106. *See, e.g.,* *United States v. Parker*, 376 F.2d 402, 408 (5th Cir. 1967) (stating that statutory interpretation cannot be done by excision); *Trotz v. Commissioner*, 361 F.2d 927, 930 (10th Cir. 1966) (refusing to infer a value test that would render the statutory wording obsolete).

107. *See* Saltzman, *supra* note 88, at S8-14 (1997 cum. supp. no. 2). CEP was started in the late 1960's and covers about 1700 of the nation's largest corporate taxpayers.

108. Most tax cases are tried in the Tax Court, which does not offer jury trials. Even in the other tribunals, the overwhelming majority of tax trials involves a judge as the finder of fact.

109. *Pierce v. Underwood*, 487 U.S. 552, 558 (1988).

110. I.R.C. § 7491(a)(1) (1998).

issues. At first blush, this would seem to matter little. Our legal system depends on the parties to develop the facts, but judges do not shrink from discovering (or creating) the law themselves. Armed with statutory text, precedents, legislative history, canons of construction, and the like, judges need not rely on a burden of proof as to legal issues.

But an important class of issues—variously called mixed questions of fact and law, ultimate facts, or applications of law to fact¹¹¹—combines elements of fact and law, and therefore does not fit neatly into the “fact versus law” dichotomy. Many litigated tax cases involve such issues.¹¹² Thus, if such issues are not considered “factual issues” for § 7491(a) purposes, the scope of that section will be narrow.

What, then, is a “factual issue” for § 7491(a) purposes? The statutory phrase is not self-defining, and the legislative history does not clarify the matter. Conceptually, at least three readings of the phrase are possible. One possibility is that a “factual issue” exists as long as the issue has *any* factual component. Such a reading would keep all mixed issues within § 7491(a). Another option is that a “factual issue” exists if the issue involves *only* factual components. This reading would exclude all mixed issues from § 7491(a). Finally, it is possible that a “factual issue” exists if the mixed issue is “more factual than legal,” but not if it is “more legal than factual.”

My suspicion is that most courts will gravitate towards the third reading. Perhaps as a lingering effect of the common-law tradition, American courts are sometimes hesitant about adopting bright-line, polar rules. Also,

111. See, e.g., Robert L. Stern, *Review of Findings of Administrators, Judges and Juries: A Comparative Analysis*, 58 HARV. L. REV. 70, 93-120 (1944) (describing instances where law and fact combine).

112. Examples include the following, among other possibilities: (1) whether an asset is a capital asset, *United States v. Winthrop*, 417 F.2d 905, 910 (5th Cir. 1969); (2) whether an asset qualifies for a particular depreciation regime, *ABC Rentals of San Antonio, Inc. v. Commissioner*, 142 F.3d 1200, 1203 (10th Cir. 1998); (3) whether an economic activity rises to the level of a trade or business, *Suburban Realty Co. v. United States*, 615 F.2d 171, 181 (5th Cir.), *cert. denied*, 449 U.S. 920 (1980); (4) whether a particular arrangement should be classified as a sale, *Estate of Franklin v. Commissioner*, 544 F.2d 1045, 1048 n.3 (9th Cir. 1976); (5) whether a payment constitutes a loan or a capital contribution, *In re Larson*, 862 F.2d 112, 116-117 (7th Cir. 1988) (noting conflicting cases); (6) whether a loan is business or non-business in nature, *Price v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50, 432, at 84, 185 (7th Cir. 1998) (designated not for publication); (7) whether the “all events” test was satisfied so as to permit a deduction to an accrual method taxpayer, *Gibson Products Co. v. United States*, 637 F.2d 1041, 1045 (5th Cir. 1981); (8) the proper characterization of a transaction for tax purposes, *Frank Lyon Co. v. United States*, 536 F.2d 746, 750 (8th Cir. 1976), *rev’d on other grounds*, 435 U.S. 561 (1978); (9) whether a given instrument constitutes debt or equity, *Scriptomatic, Inc. v. United States*, 555 F.2d 364, 372 n.13 (3d Cir. 1977); and (10) whether a condition constitutes “reasonable cause” to prevent imposition of a tax penalty, *Marrin v. Commissioner*, 147 F.3d 147, 152 (2d Cir. 1998); *In re Craddock*, No. 95-1437, 1998 WL 423450, at *4 (10th Cir. July 28, 1998).

as discussed later, the third approach will maximize maneuver-room in particular cases, a result typically cherished by judges.¹¹³

Moreover, judges are perennially fond of analogies to the familiar, and adoption of the third reading would put them in accustomed territory. Specifically, courts are accustomed to encountering the "mixed question" or "ultimate question" category in the context of appellate review. In that context, having classified the issue for review as a mixed issue, appellate courts usually then apply deferential review if factual elements predominate in the issue, or they apply de novo review if legal elements predominate.¹¹⁴

If courts do interpret "factual issue" for § 7491(a) purposes by reference to the "predominant character" analysis familiar from appellate review, a significant constraint will be imposed on possible burden shifting. For instance, to take just a smattering of recent appellate tax cases, whether an exchange qualified for the like-kind non-recognition rules,¹¹⁵ whether a sale was a disqualified related-party transaction,¹¹⁶ whether securities were capital assets,¹¹⁷ and whether assets qualified for special cost recovery,¹¹⁸ all were held to be legal issues, not factual issues, in the contexts presented.¹¹⁹

4. Supervening Burden-of-Proof Rules

Section 7491 contains a coordination rule. The general burden-shift rule of § 7491(a) "shall not apply to any issue if any other provision of [the Code] provides for a specific burden of proof with respect to such issue."¹²⁰ Since the Code already lays down particular burden rules, this coordination rule directly exempts from the general shift rule areas such as accumulated

113. See Martin B. Louis, *Allocating Adjudicative Decision Making Authority Between the Trial and Appellate Levels: A Unified View of the Scope of Review, the Judge/Jury Question, and Procedural Discretion*, 64 N.C. L. REV. 993, 994 (1986) (stating that judges have room for making decisions when deciding ultimate facts).

114. For further discussion, see *infra* notes 221-29 and accompanying text.

115. *Christenstein v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50, 352, at 83, 923 (9th Cir. 1998) (designated not for publication).

116. *Meek v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50, 179, at 83, 259 (9th Cir. 1998) (designated not for publication).

117. *Marrin v. Commissioner*, 147 F.3d 147, 150 (2d Cir. 1998).

118. *ABC Rentals of San Antonio, Inc. v. Commissioner*, 142 F.3d 1200, 1203 (10th Cir. 1998).

119. Numerous similar results appear in the older cases. An example is a line of cases holding that whether property was held for sale to customers (and therefore within an exception to capital asset status) is primarily a legal issue. *E.g.*, *Biedenharn Realty Co., Inc. v. United States*, 526 F.2d 409, 416 n.25 (5th Cir. 1976); *United States v. Winthrop*, 417 F.2d 905, 910 (5th Cir. 1969); *United States v. Temple*, 355 F.2d 67, 68 (5th Cir. 1966) (Wisdom, C.J., dissenting); *Thomas v. Commissioner*, 254 F.2d 233, 236 (5th Cir. 1958).

120. I.R.C. § 7491(a)(3) (1998).

earnings tax cases,¹²¹ jeopardy and termination assessment and levy review cases,¹²² and transferee and fiduciary liability cases,¹²³ among others.¹²⁴

Moreover, this exception might be pushed considerably further. A number of important Code sections use language expressly advertent to the judgment of the Treasury Secretary and thus the IRS.¹²⁵ The legislative history of § 7491 classes such "in the Secretary's judgment" sections as substantiation rules, the satisfaction of which is prerequisite to a burden shift under § 7491(a).¹²⁶

Examples of such sections include:

1) If a taxpayer does not have a regular accounting method, or if her regular accounting method does not clearly reflect income, the taxpayer's taxable income shall be computed "under such method as, in the opinion

121. See I.R.C. §§ 533-534 (stating what constitutes evidence of the purpose to avoid income tax and explaining when the burden of proof of whether a business has accumulated beyond the reasonable needs of business shall be on the taxpayer). These sections contain both burden-of-production and burden-of-persuasion rules. Section 7491(a) refers to the "burden of proof," which typically means the burden of persuasion. See *supra* note 9 and accompanying text. As a practical matter, however, the courts likely will read the section broadly enough to encompass the whole accumulated earnings tax burden-allocation scheme.

122. See I.R.C. § 7429(g) (stating that the burden of proof on whether the making of a jeopardy assessment is reasonable is on the Secretary, but that the burden of proof as to reasonableness of the amount of the assessment is on the taxpayer).

123. See I.R.C. § 6902(a) (providing that the burden of proof is on the transferee as to whether the transferor owed additional tax but is on the IRS as to whether the transferee is secondarily liable therefor).

124. See I.R.C. §§ 341(c)(1) (stating certain situations which are evidence of a collapsible corporation); 357(b)(2) (stating the burden-of-proof rule as to exception to non-recognition rule for incorporation and reorganization exchanges); 2040(a) (stating that the whole of jointly owned property is included in the gross estate unless the taxpayer proves the extent of contributions of owner(s) other than decedent); 2501(a)(4) (establishing a split burden of proof as to gift tax cases involving loss of U.S. citizenship).

Other examples come from the Restructuring Act. Section 3202(a) of the Restructuring Act creates new I.R.C. § 6511(h), which suspends the statute of limitations on refunds for "financially disabled" taxpayers. The statute specifies that no such disability will be recognized unless "proof of the existence thereof is furnished in such form and manner as the Secretary may require." I.R.C. § 6511(h)(2)(A) (1998). Also, § 3201 of the Act creates new Code § 6015, which replaces the former "innocent spouse relief" provisions of § 6013(e). The new rules are complex. The burden of proof is on the IRS as to some matters (for example, that the spouse claiming innocence had actual knowledge of the incorrect return item or that the spouses jointly participated in a fraudulent scheme of asset transfers) and on the spouse claiming innocence as to other matters (for example, allocation of tax items between the spouses and disqualified status of assets transferred within one year of the payment due date or notice of deficiency date). See H.R. REP. NO. 599, *supra* note 57, at 253-54 (explaining the new rules governing spouses when there is a deficiency).

125. When used in the Code, "Secretary" means "the Secretary of the Treasury or his delegate," I.R.C. § 7701(a)(11), in other words, via delegation, the IRS.

126. See H.R. REP. NO. 599, *supra* note 57, at 241 & n.13.

of the Secretary, does clearly reflect income.”¹²⁷

2) The IRS is empowered to recast transactions between related taxpayers “if [the Secretary] determines that such [action] is necessary in order to prevent evasion of taxes or clearly to reflect the income of [the related taxpayers].”¹²⁸

3) Direct and indirect foreign tax credits are allowable “only if the taxpayer establishes to the satisfaction of the Secretary” all information necessary for verification and computation of the credit.¹²⁹

4) Americans working abroad can exclude from taxable income some or all of their foreign income if certain conditions, sometimes including that the taxpayer was a “bona fide resident of a foreign country,” are met. The taxpayer must establish such bona fide foreign residence “to the satisfaction of the Secretary.”¹³⁰

But the potential may exist for the Government to go even further. The courts have held that the appearance of “in the Secretary’s judgment” type language in a statute alters the standard of proof. Under it, the taxpayer, in order to prevail, must be supported by more than the usual preponderance of the evidence—she must meet the higher burden of showing that the IRS’s determination constituted an abuse of discretion.¹³¹

Based on that line of cases, the Government could plausibly argue that sections involving the above language engage two of the limits under § 7491. Each of them may be a substantiation rule and also “another provision of [the Code which] provides for a specific burden of proof with respect to such issue.”¹³² Judicial acceptance of such an argument would mean that, categorically, § 7491 cannot shift the burden in tax accounting cases involving § 446(b), in § 482 cases, in foreign tax credit cases, on the “bona fide foreign residence” issue of § 911 cases, or in cases involving any other Code section harboring similar “Secretary’s judgment” language.

The consequent erosion of § 7491(a) would be great. Measured by tax

127. I.R.C. § 446(b) (1998).

128. I.R.C. § 482.

129. I.R.C. § 905(b). *See* Treas. Reg. § 1.905-2 (as amended in 1998) (listing the requirements the taxpayer must meet in order to claim a foreign credit).

130. I.R.C. § 911(d)(1)(A).

131. *See, e.g., Thor Power Tool Co. v. Commissioner*, 439 U.S. 522, 532 (1979) (noting that §§ 446 and 471 give the IRS wide discretion); *Oakcross Vineyards, Ltd. v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50,336, at 83,834 (9th Cir. 1998) (designated not for publication) (holding that the taxpayer “faces an extremely high burden” and a “high hurdle” in challenging the Commissioner’s decision because § 446(b) grants the IRS “broad discretion”).

132. The legislative history, while (as seen above) affirming the first characterization, does not deny the second. The principle of exclusion need not apply here. Nothing in the statutory text or the legislative history indicates that substantiation rules and Code-provisions-providing-a-specific-burden are exclusive categories.

dollars at issue, § 482 controversies are by far the most important class of tax litigation,¹³³ and foreign tax credit cases are among the most important.¹³⁴ Tax accounting cases are numerous and entail substantial revenue.¹³⁵ There have been several hundred § 911 cases although none have entailed large amounts of tax dollars. Thus, in important classes of cases, other Code sections will displace § 7491(a).¹³⁶

B. LIMITATIONS ERODING SIGNIFICANCE OF BURDEN SHIFT

The remaining conditions in § 7491(a) have more subtle, but perhaps no less significant, effects. Although they do not prevent shifting the burden to the IRS, they do render the shift largely meaningless when it does occur. Below, I discuss the remaining conditions individually, then I analyze their cumulative impact. The thrust of the argument is this: As a result of the conditions in § 7491, taxpayers in the future will have to do everything they had to do in the past, both before and at trial. Moreover, trial outcomes will be affected only when the evidence is in perfect equipoise, in other words (since perfect equipoise is chimerical), virtually never. Thus, very few taxpayers will experience "relief" under § 7491(a), even in catego-

133. See, e.g., Elizabeth Magin, *ABA Court Procedure Committee Discusses Arbitration in Litigation*, TAX NOTES TODAY, May 18, 1992 (reporting that one percent of cases docketed with the Tax Court represent 78% of the dollar value).

134. This is hardly surprising because "[t]he calculation of the foreign tax credit involves some of the more intricate and complex provisions of the Code," JOHN F. COOPER & I. RICHARD GERSHON, *INTERNATIONAL TAX GUIDE: U.S. INCOME TAXATION* § 21:02 (1991), and "[t]he foreign tax credit, quite simply, stands at the intersection of the world's tax statutes, and directing traffic at that intersection is a frightfully difficult endeavor," RICHARD L. KAPLAN, *FEDERAL TAXATION OF INTERNATIONAL TRANSACTIONS: PRINCIPLES, PLANNING AND POLICY* 81 (1988).

Another limit is reinforcing. The taxpayers in § 482 and foreign tax credit cases typically are large corporations, and are therefore ineligible for § 7491 burden shifting, see *supra* note 107 and accompanying text. Such cases may be doubly outside § 7491.

135. See, e.g., MICHAEL J. GRAETZ & DEBORAH H. SCHENK, *FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES* 686 (3d ed. 1995) ("Determining when income is taxed and when deductions are permitted is often as important, in terms of a taxpayer's tax liability, as determining what is income and what is deductible."). One of the most contentious and important sets of current income tax issues involves expensing versus capitalization of costs. See, e.g., *INDOPCO v. Commissioner*, 503 U.S. 79 (1992) (denying deduction to corporation for investment banking fees and expenses incurred when transforming into a wholly owned subsidiary). The capitalization doctrine traditionally is rooted in Code §§ 263 and 446(b), of which § 446(b) may be the stronger root. See WILLIAM D. POPKIN, *FUNDAMENTALS OF FEDERAL INCOME TAX LAW* 276 (3d ed. 1998).

136. Other examples of sections containing "to the satisfaction of the Secretary" language include I.R.C. §§ 305(b)(5), 306(b)(4), 453(e)(7), 706(b)(1)(C), 1362(b)(5)(B), 1362(f)(2), and 1378(b)(2) (West 1999).

ries of cases which theoretically qualify for a burden shift.

1. Maintenance of Records and Substantiation

Section 7491(a) can apply only if the taxpayer "has maintained all records required under [the Code]"¹³⁷ and "has complied with the requirements under [the Code] to substantiate any item."¹³⁸ The legislative history amplifies the "substantiation" requirement. The rule includes "substantiation requirements, whether generally imposed, or imposed with respect to specific items,"¹³⁹ as well as "any requirement of the Code or regulations that the taxpayer establish an item to the satisfaction of the Secretary."¹⁴⁰ Furthermore,

Taxpayers who fail to substantiate any item in accordance with the legal requirement of substantiation will not have satisfied the legal conditions that are prerequisite to claiming the item on the taxpayer's tax return and will accordingly be unable to avail themselves of this provision regarding the burden of proof. Thus, if a taxpayer required to substantiate an item fails to do so in the manner required (or destroys the substantiation), this burden of proof provision is inapplicable.¹⁴¹

In short, § 7491 notwithstanding, the taxpayer still must maintain records and still must present them to support her tax return positions. If she does not, she still will bear the burden of proof and still will lose for failure to meet it. The "records" and "substantiation" conditions can have far-reaching effects, as three points make clear:

(1) A number of important Code sections feature specific substantiation rules. This includes sections governing widely claimed (and frequently litigated) deductions for travel and entertainment expenses¹⁴² and for charitable contributions.¹⁴³

137. I.R.C. § 7491(a)(2)(B).

138. I.R.C. § 7491(a)(2)(A).

139. H.R. REP. NO. 599, *supra* note 57, at 241 (footnotes omitted).

140. *Id.*

141. *Id.* However, the report adds that if "the taxpayer can demonstrate that he had maintained the required substantiation but that it was destroyed or lost through no fault of the taxpayer, such as by fire or flood, existing tax rules regarding reconstruction of those records would continue to apply," *Id.* at 241 n.14.

142. See I.R.C. § 274(d) (West 1999); Treas. Reg. §§ 1.274(d)-1 (as amended in 1998) & 1.274-5T(4) (as amended in 1997) (describing substantiation requirements for travel and entertainment deductions).

143. See I.R.C. §§ 170(a)(1) & (f)(8) (West 1999); Treas. Reg. § 1.170A-13 (as amended in 1996) (outlining the record keeping requirements for charitable deductions).

(2) A number of other important Code sections contain "satisfaction of the Secretary" language, such as §§ 446(b), 482, 905, and 911, which, as seen above,¹⁴⁴ are considered substantiation requirements by the § 7491 legislative history.¹⁴⁵

(3) In addition to rules already in existence, the IRS and Treasury have authority to create further record-keeping rules. The most general source of such authority is § 6001, which provides in relevant part:

Every person liable for any tax . . . shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgement of the Secretary it is necessary, he may require any person . . . to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not such persons is liable for tax.¹⁴⁶

Aggressive use of this authority could render this limitation on § 7491(a) as broad as needed. If (as I suspect is unlikely, given the other conditions and exceptions to burden shifting) the IRS finds itself frequently saddled with the burden of proof as to a particular type of issue, the IRS and the Treasury surely would consider using their § 6001 authority to promulgate additional record-keeping and substantiation rules as to the tax item involved.¹⁴⁷

2. Cooperation with the IRS

A further condition for burden shifting under § 7491(a) is that the taxpayer "has cooperated with reasonable requests by the [IRS] for witnesses, information, documents, meetings, and interviews."¹⁴⁸ This condition is discussed in detail in Part IV of this article. For present purposes, it is enough to note that the taxpayer's obligation involves both providing

144. See *supra* notes 127-30 and accompanying text.

145. These sections are discussed in relation to the "other specific burden rules" exception. *Supra* notes 127-36 and accompanying text.

146. Treas. Reg. § 1.6001-1. For examples of the many cases applying § 6001, see *Menequozzo v. Commissioner*, 43 T.C. 824, 831-32 (1965); *Lattin v. Commissioner*, 69 T.C.M. (CCH) 2734, 2739 (1995).

Additional, more localized authority to prescribe substantiation requirements is contained in various Code sections. See, e.g., I.R.C. §§ 302(c)(2)(iii) (1998) (requiring a distributee of stock to file agreement to substantiate these acquisitions); 6038 & 6038A (requiring reporting for certain foreign corporations).

147. Some caution would have to be exercised. Blatant abuse of the IRS's § 6001 authority would risk congressional reprisal. Still, this means of circumvention would be available within bounds of prudence.

148. I.R.C. § 7491(a)(2)(B).

information within her control *and* providing reasonable assistance to the IRS in obtaining information not within her control, including information located in foreign countries.¹⁴⁹

3. Burden of Proof Versus Presumption of Correctness

Before § 7491, the burden of proof was not the only rule that favored the IRS in tax litigation. A presumption also existed that the determination of tax liability by the IRS was correct.¹⁵⁰ The courts should, and likely will, hold that this presumption survives the enactment of § 7491 because it is clear that the presumption of correctness and the burden of proof are separate rules of law. As one court explained:

[There is a] rebuttable presumption that the [IRS's] determination . . . is correct. This presumption in favor of the [IRS] is a procedural device that requires the [taxpayer] to go forward with *prima facie* evidence to support a finding contrary to the [IRS's] determination. Once this procedural burden is satisfied, "the taxpayer must still carry the ultimate burden of proof or persuasion on the merits." Thus, the [taxpayer] not only has the burden of proof of establishing that the [IRS's] determination was incorrect, but also of establishing the merit of its claims by a preponderance of the evidence.¹⁵¹

Section 7491(a) speaks of reversal of "the burden of proof" only,¹⁵² suggesting that the measure does not overthrow the presumption of correctness. This is confirmed by the legislative history. The relevant reports all mention the presumption of correctness. They call that presumption "a fundamental element of the structure of the Internal Revenue Code,"¹⁵³ and they do not indicate that § 7491 disturbs that "fundamental element" in any fashion. Indeed, the Senate report and the Conference Committee report imply that the presumption of correctness continues to have

149. H.R. REP. NO. 599, *supra* note 57, at 240.

150. *See, e.g., Welch v. Commissioner*, 290 U.S. 111, 115 (1933) (stating that the IRS's determination of tax liability is presumed to be correct). At least one court has described this as a "strong presumption." *Travelers Ins. Co. v. United States*, 35 Fed. Cl. 138, 141 (1996).

151. *Danville Plywood Corp. v. United States*, 16 Cl. Ct. 584, 593-94 (1989) (citations omitted), *aff'd*, 899 F.2d 3 (Fed. Cir. 1990); *see also Cebollero v. Commissioner*, 967 F.2d 986, 991 (4th Cir. 1992) (stating that the taxpayer has both the burden of showing the IRS's errors and proving her own case).

152. *See* I.R.C. § 7491(a)(1) (1991) (referring to the burden of proof and not the burden of correctness).

153. H.R. REP. NO. 599, *supra* note 57, at 238; H.R. REP. NO. 364, *supra* note 78, at 55.

vitality.¹⁵⁴

Under the pre-§ 7491 regime, the presumption of correctness "add[ed] little if anything to the taxpayer's burden of proof,"¹⁵⁵ since evidence sufficient to counter the presumption usually also satisfied the burden of proof and vice versa. However, § 7491 uncouples the two, potentially shifting the burden of proof, but leaving the presumption of correctness intact.

The survival of the presumption of correctness significantly undercuts the practical importance of § 7491(a). Although the presumption is not itself evidence,¹⁵⁶ the presumption remains until the taxpayer introduces competent and relevant evidence in support of her position.¹⁵⁷ The taxpayer must present more than just some evidence; it must be believable and substantial to some undefined degree.¹⁵⁸ This fact creates tactical problems for taxpayers. Unsure of how much evidence will be enough, the taxpayer's prudent course is to fully develop and present her case.¹⁵⁹ Thus, even if the burden of proof potentially is shifted, the survival of the presumption of correctness will compel the taxpayer to put on as complete a case as before the introduction of § 7491 into the Code.

4. Credible Evidence

Another road leads to the same destination as the survival of the presumption of correctness. A precondition of any burden shift is that the tax-

154. These reports state that the status of such evidence is determined "without regard to the judicial presumption of IRS correctness." H.R. REP. No. 599, *supra* note 57, at 241. That observation would have been unnecessary had the presumption of correction been abolished by § 7491.

155. See Theodore Tannenwald, Jr., *Tax Court Trials: An Updated View from the Bench*, 47 TAX LAW. 587, 595 (1994).

156. Although this is the "black letter" rule, courts occasionally have operated as if the presumption is substantive evidence. See Leo H. Hoffman, *Overcoming the Prima-Facie Presumption of Correctness of the Commissioner's Determination*, 4 N.Y.U. INST. FED. TAX. 240, 241 (1946).

157. *E.g.*, *A & A Tool & Supply Co. v. Commissioner*, 182 F.2d 300, 304 (10th Cir. 1950). Once the taxpayer does so, the presumption vanishes and the burden of going forward shifts to the IRS. *E.g.*, *Byrum v. Commissioner*, 58 T.C. 731, 735 (1972) (holding that the burden had shifted to the IRS).

158. See, *e.g.*, *National Weeklies, Inc. v. Commissioner*, 137 F.2d 39, 42 (8th Cir. 1943) (stating that weak and improbable evidence need not be credited); Hoffman, *supra* note 156, at 240-41.

159. This has been the advice given to taxpayers' counsel for decades. See, *e.g.*, Hoffman, *supra* note 156, at 241 ("as a practical matter, you should marshal all the admissible evidence available because you cannot say beforehand how much evidentiary weight will be given the prima facie presumption of correctness in your case").

payer have "introduce[d] credible evidence" with respect to the issue in controversy.¹⁶⁰ The legislative history adds:

The burden will shift to the [IRS] under [§ 7491(a)] only if the taxpayer first introduces credible evidence with respect to a factual issue relevant to ascertaining the taxpayer's income tax liability. Credible evidence is the quality of evidence which, after critical analysis, the court would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted (without regard to the judicial presumption of IRS correctness). A taxpayer has not produced credible evidence for these purposes if the taxpayer merely makes implausible factual assertions, frivolous claims, or tax protestor-type arguments. The introduction of evidence will not meet this standard if the court is not convinced that it is worthy of belief.¹⁶¹

Two points emerge from this requirement. First, the taxpayer's obligation here is *prior* to the possibility of a burden shift. If the taxpayer fails in this obligation, the burden will remain on the taxpayer—indeed, the taxpayer will lose¹⁶²—even if the IRS puts on no evidence of its own. Second, "credible evidence" is not an easy standard. The court is instructed to subject the taxpayer's showing to "critical analysis" and to reject it, even absent contrary evidence, if the court deems it "not worthy of belief."¹⁶³ The same conclusion suggested by survival of the presumption of correctness is suggested here as well. Since the "credible evidence" condition is substantial, taxpayers do not prudently have the option of holding anything back. For the maximum chance of fulfilling this condition, a taxpayer must fully develop and present her case from the start. In other words, what was required of the taxpayer before the enactment of § 7491(a) remains required.

C. MERE SYMBOL

Consider the cumulative effect of the conditions and exceptions discussed above. Major areas of tax controversy are categorically outside the possibility of burden shift, and groups of tax litigants are categorically ineligible for it. Moreover, even when a burden shift is theoretically possible,

160. I.R.C. § 7491(a)(1) (1998).

161. H.R. REP. NO. 599, *supra* note 57, at 240-41.

162. "Credible evidence" is sufficient to support a decision for the taxpayer absent contrary IRS evidence. So, if the taxpayer fails to introduce such evidence the burden of proof will remain on her. She will not have met her burden and she will lose.

163. This conforms to present practice. Courts are accustomed to rejecting uncontroverted but non-credible evidence. See *infra* note 189 and accompanying text.

the taxpayer has to jump through tight hoops in order to qualify for it. The taxpayer must maintain adequate proof, must present it to the IRS, and must introduce it at trial. In short, taxpayers have to do no less under § 7491(a) than they had to do before its existence.

Beyond that, once the taxpayer reaches the end of this long quest, just how holy is the grails she wins? That is, how much is the taxpayer's chance of winning the case (which is her ultimate goal after all) increased if she succeeds in shifting the burden of persuasion to the IRS? As I argue below, not by much.

Appellate courts and legal theorists are fond of talking about the burden of proof, but how much practical significance in tax cases does allocation of the burden actually have? If a case is fully developed factually at trial, it matters little or not at all which party bears the burden. In a fully developed case, the taxpayer introduces its evidence; the IRS introduces its evidence; between the two, no material fact is ignored, and the judge decides which party's evidence is more persuasive.

The usual standard of proof in civil tax cases—preponderance of the evidence¹⁶⁴—renders location of the burden of persuasion insignificant in a fully developed case. A standard metaphor for the preponderance standard is an absolutely straight line; if that line is tilted at all, even by a hair's breadth, a preponderance of the evidence exists in favor of the party in whose direction the line tilts.¹⁶⁵

The burden of persuasion is outcome determinative only when complete equality or equipoise exists. This can happen in an underdeveloped case. If no evidence is adduced by either party on a critical element of a claim, equipoise is not disturbed, and the party bearing the burden loses. When full evidence is adduced, however, equipoise is little more than a theoretical possibility. Experienced trial lawyers know that the human mind abhors uncertainty, and therefore tends to take sides.¹⁶⁶ Moreover, even if both parties have offered evidence, credibility is always an issue. Based on her accumulated life experience, her sense of probabilities, and her world view, the judge nearly always finds some of the evidence more or less credible than the conflicting evidence. This disturbs the equilibrium, and even the slightest disturbance will allow disposition of the case without dependence on location of the burden of proof. Thus, location of the burden of

164. See *e.g.*, *Danville Plywood Corp. v. United States*, 16 Cl. Ct. 584, 594 (1989), *aff'd*, 899 F.2d 3 (Fed. Cir. 1990).

165. See, *e.g.*, JAMES W. MCELHANEY, *MCELHANEY'S TRIAL NOTEBOOK* 493-95 (2d. ed. 1987).

166. See, *e.g.*, HERBERT J. STERN, *TRYING CASES TO WIN* 119 (1991). As a consequence, "[w]heather you have the burden of proof or you do not is of no moment. Do not rest on the adversary's failure of proof. Use all that advances your theme." *Id.* at 82.

proof is of little or no importance in cases in which the relevant facts have been fully developed by the evidence introduced at trial, as commentators have recognized regarding both tax¹⁶⁷ and non-tax¹⁶⁸ controversies.

The Chief Judge of the Tax Court made this point clearly:

Our experience under current law leads us to believe that cases in which taxpayers have taken a reasonable position, have met the substantiation requirements, and have fully cooperated generally do not turn on who has the burden of proof. When a court has all of the relevant evidence before it, it generally can determine the controlling facts rather than decide the case on a failure of proof. Based on this perception of how the current burden of proof rules operate, the probable number of different results that would be produced if section 7491 were enacted would not be great.¹⁶⁹

Allocation of the burden does matter in underdeveloped cases, but § 7491(a) will rarely, if ever, help taxpayers in such cases. The taxpayer almost always possesses the facts, so inadequate development can be laid at the taxpayer's door. Typically, the § 7491(a) conditions discussed above, such as maintaining records, cooperating with the IRS, and presenting credible evidence, will prevent the burden from shifting to the IRS in underdeveloped cases.

In short, even in those areas in which, categorically, burden shifting is possible, a shift rarely, if ever, will occur in underdeveloped cases and rarely, if ever, will be of any practical benefit to taxpayers in developed cases. A defanged watchdog won't bite the neighbors, but it won't bite a burglar either. In rendering § 7491(a) toothless, Congress has "protected"

167. See, e.g., JAMES J. FREELAND ET AL., *FUNDAMENTALS OF FEDERAL INCOME TAXATION* 1017 (10th ed. 1998) (noting that imposition of the burden of proof on the IRS may be "cold comfort" to the taxpayer when information to support the IRS's position is developed); Tom Herman, *A Special Summary and Forecast of Federal and State Tax Developments*, WALL ST. J., July 15, 1998, at A1 (quoting N. Jerold Cohen: "It's a rare case that turns on the burden of proof."); *IRS Restructuring*, *supra* note 34, at 282, 285 (statement of Fred T. Goldberg, Jr.) ("As a practical matter, the chance that changing the burden of proof in litigated cases will make a difference is about like the odds of flipping a coin and having it land on its edge."). As an example, see *Friedman v. Commissioner*, 75 T.C.M. (CCH) 2383, 2386 (1998) (concluding that IRS would prevail even were the burden of proof shifted to it in the case).

168. See, e.g., MCELHANEY, *supra* note 165, at 493 ("[F]or the most part the burden of proof does not make much difference in the outcome of the case."); Edmund M. Morgan, *Some Observations Concerning Presumptions*, 44 HARV. L. REV. 906, 911 (1931) ("The location of the burden of persuasion is important . . . only in a situation which seldom occurs—namely, when at the close of evidence the mind of the trier of fact is in equilibrium upon the issue.").

169. *Burden-of-Proof Provision Could Spur Disputes*, *Tax Court Chief Judge Says*, 98 TAX NOTES TODAY 12-58 (Jan. 20, 1998) (reproducing letter from Chief Judge Mary Ann Cohen to Senators William V. Roth, Jr. and Daniel Patrick Moynihan).

taxpayers by giving them something which can only bark. Contrary to the "hype," taxpayers are not helped by § 7491(a). If the section has any meaning, it is symbolic only.

III. NECESSITY OF MERE SYMBOLISM

After reading Part II, the reader may wonder: "Why did Congress write § 7491(a) that way?" If it really wanted to reverse the tax burden of proof, it should have left out all or most of the exceptions and conditions. On the other hand, if the exceptions and conditions are so important, Congress should have skipped the whole enterprise of writing § 7491(a). "What's the use of a rule that's swallowed by its limitations?"

The question is perfectly sensible, and, in fact, Congress should have left § 7491(a) out of the Restructuring Act. However, the choice to enact a measure that is devoid of practical meaning, is the product of two powerful but antagonistic forces: the perceived political benefit of being viewed as doing something versus the real and disastrous consequences of *actually* doing something. These forces are described below.

A. POLITICAL NEED TO APPEAR TO ACT

Tax collectors are never popular, of course.¹⁷⁰ In recent decades, however, a number of trends have created growing dissatisfaction with the IRS and the Code it administers.¹⁷¹ For instance, the IRS is among the most visible emblems of the federal government, not an enviable position in an era of growing anti-government feeling. Also, Congress's insatiable appetite for compounding the complexity of the tax laws has left the IRS responsible for applying a Code which, year by year, moves closer to being unadministrable.

The IRS, however, has added generously to its own troubles. The inability of the IRS to design and implement an effective computer system despite expending three to four billion dollars was, perhaps more than anything else, the impetus for establishment of the Kerry-Portman Commission.¹⁷² Further, the fortress mentality and self-protective, unresponsive managerial milieu of the IRS created thousands of instances of abuse—some publicized, many not.

170. See, e.g., *Matthew* 9:9-13 (Jesus criticized for eating with tax collectors and other sinners).

171. For reflections on the declining public support for the income tax, see MICHAEL J. GRAETZ, *THE DECLINE (AND FALL?) OF THE INCOME TAX* (1997).

172. It has been suggested—properly, in my view—that the IRS's problems stem more from its antiquated computer system than from mean-spiritedness. Paul Glastris et al., *At Your Service*, U.S. NEWS & WORLD REP., May 18, 1998, at 22, 24.

In this atmosphere, perhaps the most significant event for IRS restructuring, and therefore derivatively for burden shifting, was the oversight hearings of the Senate Finance Committee in September 1997.¹⁷³ A parade of witnesses—taxpayers, taxpayers' representatives, and IRS agents—testified (sometimes anonymously and behind screens) to a litany of IRS wrongdoing.¹⁷⁴ The hearings were a staple in evening newscasts and daily newspapers and created an outpouring of anger among citizens.

As an impetus to enactment of useful Kerry-Portman recommendations and other reforms, the hearings served a salutary function. The problem, though, is that the momentum also was used to push ideas that, far from being useful reforms, were dangerous or beside the point.

The burden-shifting idea provides one good example. The abuses spotlighted in the oversight hearings involved matters other than allocation of the burden of proof. Congress is not always sensitive to nuance, however, and the oversight hearings and the reactions to them created an "IRS bad; must punish bad IRS" mindset. This led legislators to go beyond measures adapted to the problems revealed, to search for any semi-plausible, anti-IRS measure to add to the Restructuring Act, including a burden shifting provision.¹⁷⁵

Within a fortnight of the end of the oversight hearings, the Chair of the House Ways and Means Committee announced that he would add a burden-shift provision to the Restructuring Act.¹⁷⁶ The Administration originally opposed the burden-shift idea, as well as a number of other measures in the Restructuring Act.¹⁷⁷ However, the political impact of the oversight hearings continued to snowball.¹⁷⁸ Thus, in its familiar *volte face*

173. *Practices and Procedures of the Internal Revenue Service, Hearings Before the Senate Comm. on Finance*, 105th Cong. (1997). A second set of hearings in early 1998 before the same committee fizzled, without creating anything like comparable impact.

174. It is not clear that all of the specific allegations were well founded. See, e.g., Susan Meador Tobias, *IRS Abuse Debate Should Be a Two-Way Street*, 79 TAX NOTES 1071 (1998); Stephen Barr, *Report Labels IRS Testimony "Unfounded,"* WASH. POST, April 26, 1998, at A2. But that is not crucial in the larger scheme. It is undoubtedly true that the IRS has, over the years, committed numerous acts inconsistent with good administration or even basic fairness. If the hearings left that impression in the minds of the public, it left a true impression.

175. The same could be said of some other provisions of the Restructuring Act, but those are articles for another day.

176. See *JCT May Recommend New IRS Burden of Proof in Tax Litigation*, 77 TAX NOTES 265, 265 (1997).

177. See *White House Says Shifting Burden of Proof Is Political*, 77 TAX NOTES 264 (1997).

178. See, e.g., *Overhauling the IRS*, CHRISTIAN SCI. MONITOR, July 14, 1998, at 12 (the hearings made IRS reform "a political shoo-in"); *Congress Poised to Rein in IRS*, STAR-LEDGER (Newark, New Jersey), July 9, 1998, at 5 (the hearings gave IRS reform "unstoppable political momentum").

style, the Administration quickly reversed course and embraced much of what became the Restructuring Act.¹⁷⁹ The Administration did not specifically endorse § 7491, but its opposition was unorchestrated, indeed muted.¹⁸⁰ The Administration having left the field, members of Congress who might have opposed burden shifting had no rallying point and fell in line with the momentum.

In short, general trends were catalyzed by a sensational event to vault IRS reform to the top of the political agenda. The stampede for political advantage gave premium to nearly any "shot" at the IRS, even the notion of burden shifting which Congress itself had repeatedly rejected.

B. PRAGMATIC NEED TO AVOID GENUINE ACTION

Fortunately, however, the political process did not disconnect completely from reality. It still recognized that a genuine reversal of the tax burden of proof would be a prescription for disaster, and such reversal was rejected for that reason. So understood, the limitations written into § 7491(a) are not the result of inadvertence, sloppy drafting, or unwonted timidity. They are the unavoidable product of the fact that a genuine, unbridled reversal of the tax burden of proof would have grave consequences.

The starting point is the realization that the taxpayer typically is the party with superior access to the facts. Putting the burden on the IRS would discourage voluntary disclosure of the facts by taxpayers. This would create either of two negative results. On the one hand, the IRS could try to replace information no longer voluntarily produced by gathering information more aggressively through compulsory process. This, however, would make tax audits *more* intrusive and disruptive for taxpayers and third parties, the very opposite of the Act's intended effect. On the other hand, if the IRS is unable or unwilling to use compulsory process widely, the flow of information necessary to correct determination of tax liability would be obstructed. The result would be to slash federal revenues and to compromise fairness in the distribution of tax burdens.

179. See N.Y. TIMES, May 8, 1998, at A1.

180. See *Some IRS Reform Bill Provisions Trouble Treasury Official*, 79 TAX NOTES 286 (1998) (noting that Treasury Department was keeping an "intentionally low profile" and at least two officials had made conflicting comments). There was a compounding factor that took the IRS out of play as a potential opponent of § 7491. The current IRS Commissioner, Charles Rossotti, was selected precisely because he had managerial experience but was not a tax attorney or accountant. True to this profile, Commissioner Rossotti articulated no clear position when asked by legislators for his view of burden shifting. At one point, at odds with all prior IRS policy, he appeared hesitatingly to accept burden shifting. See *IRS Restructuring*, *supra* note 34, at 34 (statement of Charles Rossotti).

1. Taxpayer's Superior Access to Information

Assume that Terry Taxpayer, on his income tax return for a given year, claims a \$1200 deduction for interest paid. The odds are that the claimed deduction is proper, but, should the item become controversial, many questions would need to be answered. Did Terry actually pay out \$1200? If so, did he do so in the year covered by the return? If so, was the payment in the nature of interest, or was it something else? If it was in the nature of interest, did any of the specific § 163 rules disqualifying deduction of interest payments apply?¹⁸¹ If not, did any provision outside of § 163 prohibit the deduction or limit its usefulness to Terry for the year in question?¹⁸²

Similarly, assume that Terry's return for the year reports total gross income of \$60,000. The odds are that his gross income did not exceed that amount, but again a number of questions would arise should controversy exist. If the issue is whether Terry had an additional \$1500 of income he failed to report, a number of relevant questions would emerge. These would include: Did Terry actually or constructively receive the \$1500? If so, did he do so in the year covered by the return? If so, was the item "income" as that term is used in § 61?¹⁸³ If so, did the receipt item fall within one of the Code sections authorizing exclusion of the item from gross income?¹⁸⁴ If not, did some statute outside the Code authorize exclusion?¹⁸⁵

In both situations, Terry has better access than the IRS to the information that would answer such questions, and this is typical of the great bulk of tax issues. The taxpayer's informational advantage over the IRS has four roots. First, the taxpayer himself is, almost always, a party to the transactions at issue in the case. Having first-hand knowledge, the taxpayer is competent to testify at trial as to what happened. For instance, Terry is in a position to testify whether he paid the \$1200 (and, if so, to whom, when, and for what) and whether he received the \$1500 (and, if so, from whom, when, and for what). Second, most tax transactions involve documents of some kind: for example, checks, contracts, deeds, invoices, and the like. The taxpayer often will have kept copies of such documents. Nearly always,

181. See I.R.C. §§ 163(d)-(h) (1998).

182. See, e.g., I.R.C. §§ 55-56 (alternative minimum tax); 68 (phase-out of itemized deductions); 265(a) (deductibility of interest expenses related to production of tax-exempt income); 465 (at-risk rules); 469 (passive activity loss rules).

183. See, e.g., Rev. Rul. 58-370, 1958-2 C. B. 14; Priv. Ltr. Rul. 92-23-046 (Mar. 10, 1992) (both holding that certain types of compensatory payments did not constitute income for § 61 purposes).

184. See e.g., I.R.C. §§ 101-136.

185. See, e.g., Hostage Relief Act of 1980, Pub. L. No. 96-449, § 201, 94 Stat. 1967 (1980) (excluding from income compensation of Government employees while held hostage abroad).

the taxpayer at least had the opportunity make and keep copies of relevant documents. Third, both for tax and for tax-independent reasons, the taxpayer may have kept summaries or indirect evidence of the transactions. Terry's books and records (if he is in business) or his check register might help resolve the above controversies. Fourth, the taxpayer knows which other persons or entities were also parties to the transactions. Thus, she knows to whom to turn for additional information to supplement, complete, or confirm the information already at her disposal.

For these reasons, in the overwhelming majority of cases the taxpayer possesses a marked informational advantage over the IRS.¹⁸⁶ Moreover, in those rare situations in which this is not the case, the law has long made accommodations to ease the taxpayer's plight.¹⁸⁷

2. Incentive To Produce Information

Because the taxpayer typically has superior access to the relevant information, the burden of proof should be allocated so as to provide her an incentive to preserve and produce that information. Placing the burden on the IRS would be perverse in that regard. It would discourage the making and keeping of records and the giving of testimony, in order to deny the IRS evidence through which to sustain its burden. In contrast, placing the burden on the taxpayer encourages making, keeping, and presenting records and testimony; for without them the taxpayer will not prevail.¹⁸⁸

It might be objected that putting the burden on the taxpayer creates only an incentive for him to bring forth information *favorable* to his position, that he still has little reason to bring forth unfavorable information as well. Such an objection, however, ignores the dynamics of a tax trial. The tactic of selective and incomplete production often will fail for a number of

186. See, e.g., *United States v. Rexach*, 482 F.2d 10, 16 (1st Cir. 1973), *cert. denied*, 414 U.S. 1039 (1973); Martinez, *supra* note 39, at 272; Michael Quigley, *A Commentary on How the Proposed Regulations Affect the General Principles of Section 482 as Described in the Existing Regulations and in Case Law*, FED. BAR ASS'N SEC. TAX'N REP. 7, 10 (Spring 1992); *TBOR II hearing*, *supra* note 16, at 131 (statement of Lawrence B. Gibbs).

187. Sometimes, this took the form of shifting part or all of the proof burden to the IRS. See Appendix A *infra*. Other times, (1) the IRS was directed to obtain information for the taxpayer, e.g., I.R.C. § 1015(a) (1998) (basis information), (2) the taxpayer was given special access to information and documents possessed by third parties, e.g., I.R.C. § 6902(b); TAX CT. R. 73 (transferee liability); Temp. Treas. Reg. § 1.1041-1T, A-14 (1984) (property transfers between spouses or incident to divorce), (3) resort was made to reasonable approximation, e.g., *Cohan v. Commissioner*, 39 F.2d 540, 543-44 (2d Cir. 1930), or (4) the taxpayer was given the opportunity to reconstruct lost records, e.g., *Shores v. Commissioner*, 75 T.C.M. (CCH) 2368, 2371 (1998).

188. See, e.g., *Carson v. United States*, 560 F.2d 693, 696 (5th Cir. 1977); Martinez, *supra* note 39, at 271-72.

reasons.

In most instances, it is not extremely difficult to detect the witness or party who is trying to withhold at least part of the story. Effective cross-examination before an experienced judge usually suffices to detect omissions, exaggerations, or prevarications. Upon such detection, the case is likely to be resolved against the unforthcoming party.¹⁸⁹ In addition, any foray into production, however partial, opens the door to further disclosures. For instance, if the taxpayer presents a document, it may contain the names of other parties to the transaction, who can then be contacted or called as witnesses, or recite other verifiable information. If the taxpayer testifies, broad opportunities are presented for cross-examination. Furthermore, a taxpayer's failure to present all relevant evidence can give rise to an adverse inference. It is well established that, when a litigant can be expected to possess evidence relevant to issues in controversy and fails to offer it at trial, the court is entitled to conclude that that evidence, had it been presented, would have been adverse to that litigant's position.¹⁹⁰

Thus, allocating the burden of proof to the taxpayer largely compels the taxpayer, on pain of losing on failure-of-proof grounds, to produce at least some of the information available to him. Attempts to adduce only carefully selected and partial evidence usually fail. So, when at least some information is produced by the taxpayer, decisional accuracy is promoted.

3. Choice of Evils

As shown, the flow of information in tax controversies would slow under a "pure" reversal of the burden of proof. How would the tax system respond to this? There are two main possibilities, neither good. On the one hand, the IRS could use various investigatory tools it already possesses to attempt to develop the evidence it would need to shoulder its burden of proof. This, however, would increase cost, inconvenience, and intrusiveness for all concerned. On the other hand, political decisions or resource limitations might make it infeasible for the IRS to use those tools much more

189. The courts have held on numerous occasions that the court need not accept testimony, even if uncontroverted, if it is improbable, illogical, or otherwise unconvincing. *E.g.*, *Wood v. Commissioner*, 338 F.2d 602, 605 (9th Cir. 1964); *Rand v. Helvering*, 77 F.2d 450, 451 (8th Cir. 1935); *Niedringhaus v. Commissioner*, 99 T.C. 202, 212 (1992).

190. In Tax Court practice, this is known as the *Wichita Terminal* presumption. *See Wichita Terminal Elevator Co. v. Commissioner*, 6 T.C. 1158, 1165 (1946), *aff'd*, 162 F.2d 513 (10th Cir. 1947). A computer search on July 7, 1998, revealed 552 citations to *Wichita Terminal*. Other courts also apply this presumption in tax cases. *E.g.*, *United States v. Philatelic Leasing, Ltd.*, 601 F. Supp. 1554, 1565-66 (S.D.N.Y. 1985).

aggressively. This, however, would essentially convert the tax system into an "honor" system. The result would be a drop, likely a substantial drop, in revenue raised, and thus in resources available to fund governmental programs. Also, an honor system would create concerns about fairness of the distribution of the burden of funding the government. Honest taxpayers would bear more than their fair share; unscrupulous taxpayers would bear less than their fair share.

a. Intrusion, Expense, and Inconvenience

In the great bulk of audits, the IRS does not invoke compulsory process. It seeks information informally, asking the taxpayer what happened and asking for copies of the relevant documents. Usually, this approach yields sufficient information to allow the IRS to make a determination. The IRS directs its agents to proceed in this fashion if possible and to use formal investigatory tools only after informal means have proved unsuccessful.¹⁹¹ But the IRS's preference for proceeding cooperatively should not obscure the fact that the IRS does have a formidable array of compulsory information-gathering weapons in its arsenal.

The Code gives the IRS "a broad mandate to investigate and audit 'persons who may be liable' for taxes."¹⁹² This broad mandate is backed up by possible criminal sanctions,¹⁹³ enforcement by judicial process,¹⁹⁴ and a variety of information-gathering devices. Of such devices, the most important are the general administrative summons for either documents or testimony,¹⁹⁵ several special summonses,¹⁹⁶ and options for enforced production of documents located abroad or testimony of persons located abroad.¹⁹⁷ These tools are in addition to normal discovery options that are

191. See I.R.M. 4022.3, MT 4000B234 (July 28, 1987).

192. *United States v. Bisceglia*, 420 U.S. 141, 145 (1975); see I.R.C. § 7601(a) (giving the IRS power to canvass districts for taxable persons and objects).

193. See I.R.C. § 7212(a) (making it a criminal offense to corruptly or forcibly interfere with "the due administration of [the Code]").

194. See, e.g., I.R.C. § 7402(a) (giving the district courts jurisdiction "to render such judgments and decrees as may be necessary or appropriate for the enforcement of the internal revenue laws").

195. See I.R.C. § 7602(a) (giving IRS authority to summons persons or books for examination).

196. E.g., I.R.C. §§ 6503(j) (designated summons whose issuance tolls the running of the statute of limitations on assessment); 7609(f) ("John Doe" summons when identity of taxpayer unknown).

197. See, e.g., I.R.C. §§ 982 (formal document requests); 7456(b) (order by Tax Court); 28 U.S.C. § 1783 (order by district court). These powers are supplemented by exchange of information under tax treaties, see, e.g., I.R.C. § 6103(k)(4); United States Model Income Tax Convention of September 20, 1996, Art. 26; I.R.M. 42(10)(10), and letters rogatory, see, e.g.,

available under court rules once a matter reaches litigation.¹⁹⁸

Given this, the courts are right in characterizing as "broad" the ability of the IRS to compel taxpayers and third parties to produce information.¹⁹⁹ As one court remarked:

[T]he power of the Commissioner of Internal Revenue to investigate the records and affairs of taxpayers is greater than that of a party in civil litigation. His power has been characterized by this court as an inquisitorial power, analogous to that of the grand jury and one which should be liberally construed.²⁰⁰

Thus, if a true burden reversal decreased voluntary production of information, the IRS might attempt to use its compulsory powers more aggressively in an attempt to compensate for the information deficit. Taxpayers and third parties might seek judicial protection, but their prospects for success would not be great. IRS summonses need meet only loose requirements to be judicially enforceable.²⁰¹

Moreover, a burden shift might cause the courts to apply these loose requirements even more sympathetically to the IRS. The looseness of the limits on the Service's information-gathering tools reflects appreciation of the inherent informational disparities between taxpayers and the IRS.²⁰² A pure burden reversal would make the situation worse by discouraging voluntary production. To compensate, the courts might well relax their stan-

Tiedemann v. The Signe, 37 F. Supp. 819, 820-22 (E.D. La. 1941).

198. For a case discussing the relation between the administrative summons and judicial discovery rules, see *Ash v. Commissioner*, 96 T.C. 459 (1991).

199. E.g., *United States v. Barter Systems, Inc.*, 694 F.2d 163, 165 (8th Cir. 1982); *United States v. Joyce*, 498 F.2d 592, 594 (7th Cir. 1974); see also *United States v. Jose*, 131 F.3d 1325, 1327 (9th Cir. 1997) (stating that the IRS has "wide latitude" to summons). Commentators agree. See, e.g., ROBERT MCKENZIE ET AL., REPRESENTING THE AUDITED TAXPAYER BEFORE THE IRS, 7-1.10 (1994) ("The IRS has incredibly broad powers to demand information from taxpayers."); Saltzman, *supra* note 88, at 13-6 ("the [IRS's] power to compel production of records or testimony is extremely broad").

200. *United States v. McKay*, 372 F.2d 174, 176 (5th Cir. 1967) (citing *Falsone v. United States*, 205 F.2d 734, 742 (5th Cir. 1953), *cert. denied*, 346 U.S. 864 (1953)).

201. To secure judicial enforcement of the summons, the IRS's showing "need only be minimal." *Liberty Fin. Servs. v. United States*, 778 F.2d 1390, 1392 (9th Cir. 1985). For example, there is no probable cause requirement, e.g., *United States v. Powell*, 379 U.S. 48, 53-54 (1964), and relevance and materiality are applied more loosely than in the context of trial evidence, e.g., *Schwimmer v. United States*, 232 F.2d 855, 862 (8th Cir. 1956), *cert. denied*, 352 U.S. 833 (1956). I.R.C. § 7609 imposes special rules regarding summonses to certain types of third-party recordkeepers. However, these rules are procedural, not substantive, and the IRS typically has little difficulty satisfying them.

202. "[T]hese inquisitorial powers are justified 'because all the facts are in the taxpayer's hands.'" *United States v. McKay*, 372 F.2d 174, 176 (5th Cir. 1967) (quoting *Bolich v. Rubel*, 67 F.2d 894, 895 (2d Cir. 1933)).

dards when they review challenges to IRS summonses and the like. For like reason, courts might be inclined to allow the IRS greater latitude in discovery.²⁰³

But our society would not be improved by substituting compelled production for voluntary production. Issuing summonses and seeking or opposing their enforcement are expensive, inconvenient, and time-consuming activities for the target, the IRS, and the courts.²⁰⁴ In addition, the process can cause bitterness, distrust, and hardening of positions, all of which further erode the relationship between the IRS and the taxpayer, sowing the seeds for yet more controversy between them in the future.

The situation would be particularly vexing for third-party targets of IRS compulsory process. For instance, if a taxpayer (relying on the fact that the IRS bears the burden under a "real" burden shift) refuses to provide information as to his claimed deductions, the IRS might need to seek information from, among others, his credit card companies, his bank, his utilities providers, his mortgage lender, any charities to which he allegedly contributed, his employer, or, if a proprietor, his suppliers, customers, and employees.²⁰⁵ It is more natural to fix compliance burdens on the taxpayer whose return is under examination than on third parties who may have dealt with the taxpayer.

However the compliance burdens ultimately are distributed, though, they would be greater in the aggregate under a system depending on formal process than one depending on cooperation. Burden shifting marches under the flag of helping citizens and taxpayers. However if it causes the IRS to rely more heavily on formal information-gathering techniques, it would have the opposite effect.²⁰⁶

b. Revenue Erosion

In all practicality, however, it is unlikely that the IRS would be able to greatly increase use of formal process after a pure burden shift, even if it wanted to do so. The very forces that led to enactment of § 7491 would create political barriers to such use. Perhaps more importantly, congress-

203. The courts sometimes criticize the IRS for relying on discovery instead of adequately developing the facts during the audit. *E.g.*, *Durkin v. Commissioner*, 87 T. C. 1329, 1402-03 (1986). This attitude might soften if, because of burden reversal, developing the facts during the audit becomes more difficult for the IRS.

204. *See, e.g.*, *United States v. Bisceglia*, 420 U.S. 141, 146 (1975) (stating that IRS summonses "unquestionably involve some invasion of privacy" but are necessary to the system).

205. *See TBOR II hearing, supra* note 16, at 21 (statement of Cynthia G. Beerbower).

206. Senator Moynihan articulated this concern during the course of consideration of § 7491 and was seconded by IRS Commissioner Rosotti. *See Hearings Before the Senate Finance Comm.*, 1998 WL 212890, at *19-20 (May 1, 1998).

sional parsimony in IRS appropriations²⁰⁷ would create significant resource constraints.

Of course, the practical inability of the IRS to fully use compulsory information-gathering devices would create its own set of problems under a true, general shift of the burden of proof to the IRS. Chief among these is peril to the public fisc. A genuine shift of the burden would encourage many taxpayers to pursue a "hide the ball" strategy. They would see benefit in taking overly aggressive return positions. Then, in the event of audit, instead of producing information, they would challenge the IRS to disprove the correctness of those positions. If the IRS could not or would not use its compulsory tools, it would be unable to meet this challenge.

Certainly, there are many honest taxpayers who would eschew this strategy. But it defies human experience to assume all taxpayers are in this category. Given the numbers of taxpayers, even a small percentage decrease in compliance would render serious create consequences.²⁰⁸ Congress estimated that § 7491—which is far from a true burden shift—would cost the Treasury \$2.7 billion over a ten-year period.²⁰⁹ A genuine shift would cost much more.²¹⁰

The matter was put graphically generations ago. Explaining why the Board of Tax Appeals had, in its rules, placed the burden of proof on the taxpayer, James S. Ivins, one of the original appointees to the Board,

207. See, e.g., Amy Hamilton, *Treasury Appropriations Bill Getting Bumpy Ride in Both Houses*, 80 TAX NOTES 290 (1998).

208. "[One] survey suggests that five percent of our taxpayers cheat on their taxes, and twelve percent would do so if they thought they would not be caught. Similar studies suggest that, apart from cheating, many taxpayers are more inclined to take aggressive positions on their tax returns if they believe that they are less likely to ultimately have to pay any additional tax." *TBOR II hearing*, *supra* note 16, at 131 (statement of Lawrence B. Gibbs).

Similarly, a general burden shift would have "enormous and far-reaching adverse effects on our tax system [I]t will result in a significant reduction in the willingness of taxpayers to comply voluntarily with their tax obligations and would greatly encourage tax protestors." *Id.* at 26 (statement of Cynthia G. Beerbower, Deputy Assistant Secretary of the Treasury for Tax Policy).

209. JOINT COMMITTEE ON TAXATION, ESTIMATED REVENUE EFFECTS OF H.R. 2676, THE "INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1998," AS PASSED BY THE SENATE ON MAY 7, 1998 (JCX-42-98) (1998). In the main, this estimate is based on the assumption that the IRS will settle future cases on terms more favorable to taxpayers than it did under pre-§ 7491 law. See WALL ST. J., July 15, 1998, at A1.

Revenue scoring is notoriously inaccurate. See, e.g., WALL ST. J., June 23, 1998, at A20 (discussing inaccuracy of scoring of 1997 capital gains changes, and concluding that the revenue estimators should "shape up and start firing people, or go out of business"). The scoring of § 7491 was, I suspect, particularly conjectural.

210. See Cherecwich, *supra* note 48, at 490 ("[I]f shifting the burden were to reduce voluntary compliance by as little as one percent, there would be a \$10 billion annual decrease in the revenues.").

stated: "If you place the burden of proof on the Commissioner, you might as well repeal the income tax and pass the hat because you will practically be saying to the taxpayer, 'How much do you want to contribute toward the support of the government?'"²¹¹

Two final points as to revenue loss. First, the problem would not be limited to federal coffers—it would spill over to states and localities as well. Nearly all states and many localities have income taxes. Most of these "piggyback" onto the federal income tax, in that jurisdictions ask their taxpayers to state their income as computed on their federal tax returns, make a few modifications, then impose state tax rates on these tax bases.²¹² Thus, if a genuine burden shift would lead taxpayers to understate their income for federal purposes, it derivatively would lead to understatement for state and local income tax purposes as well.²¹³

Second, in light of international developments, it is particularly ironic that the drive for burden reversal has gathered speed now. Russia has been experiencing a severe fiscal crisis, the effects of which have resonated in global financial markets. A major factor in that crisis has been Russia's failure to collect taxes effectively,²¹⁴ which has driven the Russian government to desperate measures.²¹⁵ With this lesson before us, it is curious that some would court the revenue erosion that a genuine burden shift would threaten.

c. Unfairness

There is a further dimension of the foregoing concern. Taxpayers who win the "hide the ball" game will pay less tax than similar taxpayers who choose not to play. This would traduce an important goal of our tax system: the principle of horizontal equity, the notion that similarly situated taxpay-

211. *Hearings on Revenue Revision, 1925, Before the House Comm. on Ways & Means*, 69th Cong. 907 (1925). This concern remains valid today. A former chief judge of the Tax Court recently pronounced himself "firmly opposed to a shift of the burden of proof because more taxpayers might engage in stalling tactics during the examination process, tax avoidance and tax evasion." CCH TAXDAY, Oct. 22, 1997 (quoting Samuel Sterrett).

212. *E.g.*, JEROME R. HELLERSTEIN & WALTER HELLERSTEIN, *STATE AND LOCAL TAXATION* 868 (6th ed. 1997).

213. *See TBOR II Hearing, supra* note 16, at 45 (statement of Margaret Milner Richardson) (discussing the relative impact of shifting the burden of proof to the IRS).

214. Last year, Russia succeeded in collecting only 52% of the taxes owed it. N.Y. TIMES, Mar. 8, 1998, at A3.

215. For instance, Russia is trying to enlist men's fear of sexual impotence to improve tax compliance. One Russian television ad shows a man sitting up, partly nude, in bed. He mournfully clicks the bedside lamp on and off while an attractive woman next to him turns away angrily. This visual is accompanied by the voice-over: "Lost your desire? That's nerves. Pay your taxes and live peacefully." *Id.*

ers should be taxed similarly.²¹⁶

Certainly, there are many departures from this principle—for instance, homeowners are treated better than renters, and married couples sometimes are treated better, and sometimes treated worse, than cohabitating, unmarried couples.²¹⁷ But such departures reflect deliberate policy choices by Congress based on social or economic incentive purposes. Violations of horizontal equity resulting from differential ability and willingness to “game” the system should not be similarly countenanced. A pure burden shift would compromise the fairness with which the costs of supporting the Government are distributed among our citizens.²¹⁸

The Supreme Court has made this point in a related context:

We recognize that the authority vested in tax collectors may be abused, as all power is subject to abuse. However, the solution is not to restrict that authority so as to undermine the efficacy of the federal tax system, which seeks to assure that taxpayers pay what Congress has mandated and to prevent dishonest persons from escaping taxation thus shifting heavier burdens to honest taxpayers.²¹⁹

C. RECONCILIATION THROUGH SYMBOLISM

The clashing forces described above explain the route taken by Congress with their adoption of § 7491(a). Because of the political dynamic, a purported burden shift was too tempting to forgo. Yet, because a true burden shift would have been calamitous, a straight-forward reversal of the burden was a pragmatic impossibility.

The reconciliation of the clashing forces was a purely symbolic action. Thus, we have a § 7491(a) that allows Congress to claim to have tamed the IRS monster but that will have virtually no effect on who bears the burden in the practical order.²²⁰ Such an exercise is cynical, of course. Worse, as Parts IV and V will show, there will be costs to be paid for creating this

216. See, e.g., *Thor Power Tool Co. v. Commissioner*, 439 U.S. 522, 544 (1979); *Commissioner v. Sunnen*, 333 U.S. 591, 599 (1948); *Burnet v. Harmel*, 287 U.S. 103, 110 (1932).

217. See, e.g., Steve R. Johnson, *Targets Missed and Targets Hit: Critical Tax Studies and Effective Tax Reform*, 76 N.C. L. REV. 1771, 1774-80 (1998) (explaining different tax treatments given to individuals on the basis of marital and living status).

218. See generally Cherecwich, *supra* note 48, at 489-90 (“[U]nder the burden-shifting proposal, a dishonest taxpayer would have an incentive to stonewall the IRS and escape paying his fair share”).

219. *United States v. Bisceglia*, 420 U.S. 141, 146 (1975).

220. See *JCT May Recommend New IRS Burden of Proof in Tax Litigation*, 77 TAX NOTES 265, 267 (1997).

empty symbol.

IV. DISPUTE RESOLUTION HARMS

Part II established that, under § 7491(a), taxpayers will rarely benefit from reallocation of the tax burden of proof. But that is not the same as saying that the new section will have no effect. Section 7491(a) will meaningfully affect the lives of participants in our tax system—unfortunately, in negative ways.

Two of the limitations of § 7491(a) discussed in Part II are ambiguous and will create significant new uncertainties in tax litigation. These are the “factual issue” and “cooperation with the IRS” limitations. I will describe the uncertainties created by these two rules, then show the practical difficulties that will ensue.

A. UNCERTAINTIES

1. Uncertainties from the “factual issue” limitation

Section 7491(a)(1) confines any burden shift to factual issues.²²¹ The stress point here is mixed questions of fact and law. Courts may handle such questions for § 7491(a) purposes as they have for standard-of-review purposes: classifying them as either factual issues or legal issues based on which component predominates.²²²

But “the devil is in the details,” and it is the application of this approach that will be problematic. For standard-of-review purposes, the dichotomization of mixed questions into factual issues and legal issues has proved far from consistent or predictable.²²³ Similar uncertainty would be wrought by importing this approach into § 7491 law.

The problem has three aspects. First, appellate courts often choose to review mixed tax issues without stating which standard applies to the issues: the deferential standard for factual issues or the *de novo* standard for legal issues. Many times, the appellate opinion simply omits discussion of the applicable standard.²²⁴ Other times, the opinion notes the disagreement of

221. See *supra* notes 110-19 and accompany text.

222. See *supra* notes 114-19 and accompanying text.

223. See, e.g., Ralph S. Rice, *Law, Fact, and Taxes: Review of Tax Court Decisions Under Section 1141 of the Internal Revenue Code*, 51 COLUM. L. REV. 439 (1951) (discussing the difficulty in characterizing mixed questions as questions of fact or law).

224. For example, a series of appellate tax decisions, dealing with whether release of contract rights produced capital gains or ordinary income, reversed and remanded without ever discussing whether the mixed issue was predominantly a factual issue or a legal issue. Bisbee-

the parties as to the proper standard, then says the decision would be the same under either standard.²²⁵

Second, when different appellate courts review the same mixed tax question, they sometimes disagree as to whether the question is reviewable, based on its predominant characteristics, as a factual issue or as a legal issue.²²⁶ Of course, there is nothing unique to tax cases about this. The "fact versus law" distinction can be bedeviling, and may generate disagreement, regardless of the substantive branch of law from which the case originates.²²⁷

Third, appellate courts sometimes play a strategic game. Choice of the standard of review can go far towards justifying a substantive result the appellate court may want to reach.²²⁸ It also defines the scope of appellate inquiry, thus affecting the distribution of decisional power between the appellate courts and the trial courts. The classification choice made by a court of review may sometimes reflect such considerations.²²⁹

Applying this to § 7491, courts may interpret "factual issue" for § 7491(a) purposes by reference to factual-issue versus legal-issue as understood for standard-of-review purposes. If the judge thinks burden shifting is a good idea, the incentive would be generally to classify mixed tax questions as factual issues, thus maximizing the possibility of a shift. If, though, the judge shares the view expressed in this Article that the prior rule was superior to § 7491(a), the tendency would be to classify mixed tax issues as legal issues, for then § 7491(a) would not apply.

Baldwin Corp. v. Tomlinson, 320 F.2d 929 (5th Cir. 1963); Commissioner v. Ferrer, 304 F.2d 125 (2d Cir. 1962); Commissioner v. Starr Bros., Inc., 204 F.2d 673 (2d Cir. 1953).

225. *E.g.*, *In re Larson*, 862 F.2d 112, 117-18 (7th Cir. 1988); *Price v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50,432, at 84,185 (7th Cir. 1998) (designated not for publication); *Berry Petroleum Co. v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50,398, at 84,092 (9th Cir. 1998) (designated not for publication).

226. *Compare* *Roth Steel Tube Co. v. Commissioner*, 800 F.2d 625, 629 (6th Cir. 1986), *with* *Saviano v. Commissioner*, 765 F.2d 643, 645 (7th Cir. 1985) (disagreeing as to whether the characterization of a payment as a loan or as a contribution to capital should be reviewed as a question of law or a question of fact).

227. *See, e.g.*, *Pierce v. Underwood*, 487 U.S. 552, 558 (1988) (addressing "fact versus law" conflict between circuit courts as to "substantially justified" element with respect to award of attorney fees); *Newell Cos., Inc. v. Kenney Mfg. Co.*, 864 F.2d 757, 777-81 (Fed. Cir. 1988) (Newman, J., dissenting) (noting inconsistent holdings as to "fact versus law" nature of "unobviousness" issue in patent cases).

228. Labeling a mixed question a factual issue triggers deferential review, which is helpful if the appellate court likes the substantive result reached below. If the appellate court dislikes that result, labeling that question a legal issue triggers non-deferential, *de novo* review, making it easier to justify reversal.

229. *See, e.g.*, *Louis*, *supra* note 113, at 997, 1017-38 (discussing appellate courts' exercise of control over trial courts' "discretionary power").

In short, the "factual issue" condition of § 7491(a) can produce significant uncertainties, especially if interpreted by analogy to standard-of-review law. Many tax cases turn on mixed questions of law and fact, and it often will be difficult to predict whether the courts will consider these to be "factual issues," eligible for burden shifting.

2. Uncertainties from "Cooperation with IRS" Limitation

An important determinant of whether the burden of proof will shift under § 7491(a) is whether the taxpayer "has cooperated with reasonable requests by the [IRS] for witnesses, information, documents, meetings, and interviews."²³⁰ When will the taxpayer have complied with this requirement? The legislative history indicates that several elements are essential for compliance. The taxpayer must provide "within a reasonable period of time, access to and inspection of witnesses, information, and documents" within the taxpayer's control (but only "as reasonably requested by the [IRS]").²³¹ In addition, the taxpayer also must provide "reasonable assistance to the [IRS] in obtaining access to and inspection of witnesses, information, or documents not within the control of the taxpayer," including such material located abroad.²³² Another "necessary element" of cooperation is the taxpayer's exhausting her administrative remedies, including administrative appeal rights.²³³

However, at least two actions are not required as elements of cooperation. First, the taxpayer need not, on pain of a finding of non-cooperation, accede to an IRS request to extend the statute of limitations on assessment.²³⁴ Second, the taxpayer may, without risking an adverse finding, assert the applicability of one or another privilege²³⁵ as grounds for refusing to provide information requested by the IRS.²³⁶

230. I.R.C. § 7491(a)(2)(B) (1998).

231. H.R. REP. NO. 105-599, *supra* note 57, at 240.

232. *Id.* at 240. This includes providing English translations of foreign documents as reasonably requested by the IRS. *Id.* at 240 & n.9.

233. *Id.* at 240.

234. *Id.* In general, the IRS must assess tax liabilities within three years after the filing of the taxpayer's return (or, if later, the due date for such filing), I.R.C. § 6501(a), but that period may be extended by agreement between the IRS and the taxpayer, I.R.C. § 6501(c)(4).

235. In addition to previously recognized privileges, the Restructuring Act adds a new privilege for communications with non-attorney tax advisors. Restructuring Act, *supra* note 5, § 3411 (codified at I.R.C. § 7525). For a critical view of the new privilege, see Steve R. Johnson, *Tax Advisor-Client Privilege: An Idea Whose Time Should Never Come*, 78 TAX NOTES 1041 (1998).

236. "Cooperating also means that the taxpayer must establish the applicability of any privilege." H.R. REP. NO. 105-599, *supra* note 57, at 240. This implies that at least good-faith assertions of privilege will not constitute failure of cooperation. As to bad-faith assertions, see

While helpful, the legislative history does not answer all, or even most, of the potential questions. Indeed, the cooperation inquiry will always be a case-by-case matter, rarely susceptible to categorical resolution. That being true, the purpose of the following discussion is more to suggest the range of questions that may arise under the "cooperation" condition than to predict how the courts will answer those questions.

A taxpayer seeking to satisfy or deflect the "cooperation" condition could argue at any of four levels: (1) the IRS did not make a request for information; (2) if it did, that request was not reasonable; (3) the taxpayer complied with the request; and (4) if she did not, there was good cause therefor. A potential for ambiguity, dispute, and unpredictability exists at each of these levels.

(1) Did the IRS ask for the information during the examination? Currently, many information requests by the IRS are oral. People remember conversations differently, and, thus, the potential for "Yes, I did / No, you didn't" clashes will be ever-present under § 7491. Even written requests are not wholly immune from differences in interpretation that lead to dispute, as anyone who has been involved in discovery imbroglios can attest.²³⁷ Loosely worded information requests can be interpreted "strategically," leading to either cramped production or "box car" production. Moreover, one can only marvel at the ability of skilled counsel to find "ambiguity" in even the most carefully drafted requests for production.

(2) If the court concludes that the IRS did, in fact, request the information in question, it still must determine whether the IRS was reasonable in seeking it. Neither the statute nor the legislative history defines this concept. The most obvious analogy is to IRS summonses. Generally, IRS summonses are enforceable if (i) the investigation is conducted pursuant to legitimate purposes; (ii) the matters inquired into are relevant to that purpose; (iii) the information sought is not already in the IRS's possession; and (iv) any required administrative steps have been taken.²³⁸ Additional requirements are prescribed for summonses in special situations.²³⁹ Typically, elements of enforceability are applied loosely and sympathetically to the IRS, so as not to stifle information gathering.²⁴⁰

infra notes 242-44 and accompanying text.

237. See, e.g., LAWRENCE A. MORSE, OBJECTIONS TO INTERROGATORIES 9-1 (1990) (stating that the most common objection to the form of interrogatories is "vague and ambiguous").

238. United States v. Powell, 379 U.S. 48, 57-58 (1964).

239. See I.R.C. §§ 7609(a)-(e) & (g)-(i) (discussing third-party recordkeeper summonses), 7609(f) (describing "John Doe" summonses); see also § 7611 (explaining investigations of churches); 7612 (discussing summonses for tax-related computer software source codes).

240. See *supra* notes 202-04 and accompanying text (discussing the IRS's information gathering advantages).

Courts applying § 7491(a) will have to grapple with two questions in this context: Should the requirements that measure the enforceability of a summons also measure the reasonableness for § 7491(a) purposes of an IRS request for information? If so, should those requirements be applied with the same degree of liberality for § 7491(a) reasonableness purposes as they are for summons enforcement purposes? Plainly, there is enormous room for divergence as to these questions. One could imagine courts importing all, some, or none of the summons enforcement elements into § 7491(a) reasonableness analysis, and one could imagine courts applying them with more or less liberality.

(3) Precisely how fully need the taxpayer comply with reasonable IRS information requests in order to satisfy the "cooperation" condition for shifting the burden of proof? For example, if there are twenty issues in the case and the taxpayer fully complies with IRS requests as to nineteen of them but only partly complies with IRS requests as to the twentieth issue, who bears the burden of proof as to that twentieth issue? Likewise, if, on a given issue, the IRS asks for 100 documents and the taxpayer produces 90 of them, has the taxpayer sufficiently cooperated in order to shift the burden as to the issue? Similar questions easily could be multiplied.

The legislative evolution of § 7491 makes answering such questions more difficult. In the version originally passed by the House, the taxpayer would have been required to "*fully* cooperate []" with IRS requests for information.²⁴¹ The Senate deleted the adverb, and the Conference Committee followed the Senate's version. The legislative history does not make clear how much substantive significance Congress intended this deletion to have. Taxpayers surely will argue that this change means that something less than total cooperation can be sufficient cooperation to satisfy this condition for shifting the burden.

(4) Assume that the IRS asks Theresa Taxpayer to let it examine a particular document in her possession. Assume further that this request is reasonable but that Theresa nonetheless refuses to show the document to the IRS during the audit. On proper facts, may Theresa argue that the "cooperation" condition was met because there was good cause for her refusal? The likely answer is "yes." However, we may expect controversy as to what can constitute good cause and whether such cause is present on the facts of a given case.

The clearest candidate for such good cause is a claim of privilege as to the information sought by the IRS.²⁴² The legislative history of § 7491 im-

241. See *supra* note 55 (providing the version of § 7491 originally passed by the House).

242. Another candidate for "good cause" is assertion that the IRS was proceeding in bad faith in seeking the information. This is a well recognized category of argument in summons enforcement cases. *E.g.*, *United States v. Caltex Petroleum Corp.*, 81 A.F.T.R.2d 1798 (N.D.

plies that, notwithstanding the requirement to cooperate, taxpayers may still assert privilege claims.²⁴³ So in our scenario, Theresa may assert that the document sought by the IRS is protected by, for instance, the attorney-client privilege, and that she, therefore, had good cause excusing her refusal to divulge it.

However, matters are unlikely to remain that simple. Theresa's claim of privilege may have been: correct under the law, incorrect but reasonably arguable, or clearly incorrect. The legislative history surely means that a correct assertion of privilege excuses non-cooperation, and it may extend this as well to arguable-though-erroneous assertions. It surely, however, cannot mean to extend this to frivolous assertions.²⁴⁴ Thus, in order to determine whether the "cooperation" condition for a burden shift was satisfied, courts will not only have to separate correct from incorrect privilege claims, they also will have to sort incorrect claims into frivolous and non-frivolous categories.

B. DELETERIOUS EFFECTS

The preceding subpart showed that the "factual issue" and "cooperation with the IRS" limitations inevitably will give rise to differing interpretations. Parties adjust their behavior to the contours of the litigation landscape. Additional uncertainty will affect the behavior of taxpayers as litigants.

There sometimes is a tendency for taxpayers to see their cases through "rose-colored glasses." Taxpayers affected by this syndrome might tend too readily to think they qualify for burden shift because "sure, this is a factual issue" and "heck yes, I cooperated with the IRS, at least as far as I reasonably had to." Moreover, parties—even those rigorously striving to be realistic—are more likely to erroneously weigh the probabilities when the environment is uncertain. Two problems will ensue: taxpayers will be more likely than before to take their cases into litigation and once cases are in

Tex. 1998); *see also* SALTZMAN, *supra* note 88, ¶ 13.08 (discussing bad faith requests for taxpayer information). However, this probably is not independent of the "was the IRS's request reasonable?" facet of the inquiry.

243. *See* H.R. REP. NO. 105-599, *supra* note 57, at 240.

244. If even frivolous assertions of privilege excuse non-compliance with reasonable IRS information requests, the "cooperation" requirement would be a dead letter—taxpayers could simply assert spurious privilege claims as to every document sought by the IRS. Similarly, taxpayers are permitted to contest in Tax Court IRS determinations before having to pay the tax in controversy, but they will be penalized if they offer frivolous arguments against those determinations. *See* I.R.C. § 6673(a)(1)(B) (1998) (authorizing imposition of maximum penalty of \$25,000 against taxpayers whose positions in Tax Court proceedings are frivolous or groundless).

litigation, they will be more costly and inconvenient to resolve.

1. Increased Litigation

Even now, with the burden of proof squarely upon taxpayers, some taxpayers litigate cases that they really should have settled or conceded during audit or administrative appeal.²⁴⁵ To take an example, a substantial number of Tax Court cases involve "tax protestor" issues, in which taxpayers—undeterred by § 6673—assert such things as "the Sixteenth Amendment was never properly ratified"; "wages are not taxable income"; "payment of federal income tax is purely voluntary"; "U.S. currency has been worthless since we went off the Gold Standard"; and "I am exempt from tax as an Ambassador from the Kingdom of God."²⁴⁶ Prone to litigating even such obvious losers, tax protestors will only be encouraged by a section that allows them to make, at least, a colorable argument that the burden of proof has been shifted to the IRS.²⁴⁷

The effect need not be confined to protestors. Any taxpayer who, before enactment of § 7491(a), would have assessed the pros and cons of proceeding to litigation as relatively balanced, will now recalibrate that balance in light of the possibility of a burden shift. The uncertainties as to such a shift created by the "factual issue" and "cooperation with the IRS" requirements will cause some taxpayers, who would have settled or conceded under the prior regime, to take their chances and litigate. Cases are most likely to settle when the consequences of trial are readily predictable. Uncertainties breed varying assessments of probable outcomes, a condition that stymies settlement.

245. This is why Congress enacted I.R.C. § 6673, which imposes a penalty on the taxpayer when his Tax Court case was instituted or maintained for delay, was based on a frivolous or groundless position, or was filed before exhaustion of administrative remedies. The amount of the maximum penalty has progressively risen: from \$5,000 to \$10,000, now to \$25,000.

246. See, e.g., *Cheek v. United States*, 498 U.S. 192, 204-05 (1991) (describing various standard tax protestor arguments as "incredible" and "frivolous"); Christopher S. Jackson, *The Inane Gospel of Tax Protest: Resisting Rendering Unto Caesar—Whatever His Demands*, 32 GONZ. L. REV. 291, 301-24 (1996-1997).

247. The argument would not be even colorable as to the protestor arguments themselves, as the legislative history states. See *supra* note 161 and accompanying text. However, it might be colorable as to any facially genuine issues in the case, such as whether the taxpayer had unreported income or was eligible for deductions or credits. Cf. *TBOR II Hearing*, *supra* note 16, at 27 (statement of Cynthia G. Beerbower, Deputy Assistant Secretary (Tax Policy), Department of the Treasury) (A general burden shift would be "an obvious boon to tax protestors, who would claim all sorts of deductions to zero out their income. The IRS would spend endless hours having to disprove each item on the return. Protestors would no doubt become extremely creative in claiming deductions that would cause maximum difficulty on the part of the IRS to disprove.").

2. Increased Resolutional Costs

An even more significant problem will be that resolving tax cases that reach litigation will entail greater expense and inconvenience, for the courts, the IRS, third-party witnesses, and taxpayers themselves. Such inefficiencies will stem from more discovery, more motions practice, less stipulation and concession of facts, and more evidence and briefing.

a. Discovery

As discussed in Part III, a true, general shift of the burden of proof to the IRS would result in less voluntary disclosure of information by taxpayers during an audit. Section 7491(a)—which is far from a genuine shift of the burden—would have less of an effect in this regard, but probably still some. There is likely uncertainty as to whether a mixed question will be held a “factual issue” in any given case, and there inherently is room for disagreement as to whether there was sufficient cooperation with reasonable IRS requests for information. Given that, some taxpayers may believe that they at least “have a shot” at the burden’s being shifted to the IRS. Such taxpayers will be disinclined to voluntarily disclose any more information than the bare minimum they deem required to satisfy the “cooperation” condition.

The IRS could respond either by issuing administrative summonses during the audit²⁴⁸ or by engaging in discovery after the case begins. However, judicial supervision and resolution of discovery disputes and district court litigation as to summons enforcement are costly in both time and money. Thus, to the extent that uncertainty about § 7491’s conditions leads to substitution of summonses and discovery demands for voluntary disclosure, resolution of tax controversies will be rendered less efficient.

b. Motions

Attorneys, for both taxpayers and the IRS, will feel uncomfortable about burden-location uncertainties. In preparing for trial, an attorney wants to know whether her party bears the burden of proof or whether the other party does.²⁴⁹ Especially in the early days of our living with § 7491(a),

248. For further discussion, see *supra* notes 191-206 and accompanying text.

249. I assume here a bipolar trial (taxpayer versus IRS), which is the norm. However, tax cases exist in which there are three or more parties. These involve situations in which the persons who engaged in the transactions characterized them inconsistently for tax purposes. For instance, (1) when alimony-like payments pass between former spouses, the payer spouse

this likely will lead to parties submitting pretrial motions, asking the court to announce who will bear the burden of proof at trial.

There is support in present practice for this expectation. Sections 533 and 534 of the Code set up a complex scheme for the allocation of the burdens of production and persuasion in accumulated earnings tax (AET) cases. It has become routine in AET cases for one party or the other to move before trial for declaration by the Tax Court of who bears what burdens as to which parts of the case. Generally, counsel view this as important. Still, making, opposing, and resolving such motions add another layer of controversy to the case, sometimes wastefully.²⁵⁰

It would be unfortunate if § 7491 and its attendant uncertainties caused this practice to metastasize throughout tax litigation. Substantial additional costs would be imposed were pretrial motions as to location of the burden of proof to become routine in tax litigation. The uncertainties associated with the "factual issue" and "cooperation" conditions may raise this specter.

In actual practice, though, I suspect that courts would find ways to protect themselves from the barrage of such motions. For instance, trial judges probably would adopt a routine or semi-routine practice of not

often claims a deduction under § 215 despite the payee spouse not reporting an income inclusion under § 71; (2) when multiple assets are transferred between businesses by sale, the buyer and seller sometimes disagree as to how much of the total consideration should be allocated to each of the transferred assets, a matter which affects cost recovery and character of gain or loss; and (3) when property is used as compensation for rendition of services, the transferor and recipient sometimes disagree as to the fair market value of the property, which is the key to the transferor's deduction and the recipient's income inclusion under § 83. In such cases, the IRS, to avoid being whipsawed, often issues deficiency notices to both the parties to the transaction. The ensuing cases sometimes are consolidated, creating a triangular alignment of parties in which the real clash is between the sets of taxpayers, the IRS being largely a stakeholder.

Allocating the burden of proof under § 7491(a) in such multi-party cases will entail an extra level of complexity. For example, assume in a triangular case that the burden is held to have been shifted to the IRS and no evidence is introduced as to a critical fact. Would the IRS lose relative to both the taxpayers? For instance, would the payor spouse be allowed the deduction but the payee spouse not be required to include anything in income? Such a result clearly would entail erroneous determination of tax on a net basis. Taxpayers would receive legally incompatible benefits, to the detriment of the fisc.

250. An example is the AET case, *Iowa School of Men's Hairstyling, Inc. v. Commissioner*, 64 T.C.M. (CCH) 1114 (1992). That opinion deals only with burden of proof. The IRS moved before trial for declaration that, under §§ 533 and 534, the taxpayer would bear the burden of proof at trial. The IRS prevailed as to that motion. Thereafter, however, the case disappears from the reporters. Before trial, the IRS realized that, on the facts, the taxpayer would be able to carry its burden of proof, so the IRS conceded the case. The effort, time, and expense involved in litigating and deciding the pretrial motion as to location of the burden of proof were, after all, wasted.

holding hearings on or ruling on such motions before trial, then just adding a few, mostly boilerplate paragraphs to their opinions as to burden of proof. This would reduce waste of judicial resources, but it would not be a complete solution. Such motions probably still would be filed and answered in at least some cases, involving costs to litigants. Moreover, counsel would be distressed on account of not knowing until after the trial who bore the burden of proof at trial.

c. Stipulations and Concessions

Stipulations are central to Tax Court practice.²⁵¹ The court directs:

The parties are required to stipulate, to the fullest extent to which complete or qualified agreement can or fairly should be reached, all matters not privileged which are relevant to the pending case, regardless of whether such matters involve fact or opinion or the application of law to fact. Included in matters required to be stipulated are all facts, all documents and papers or contents or aspects thereof, and all evidence which fairly should not be in dispute The requirement of stipulation applies under this Rule without regard to where the burden of proof may lie with respect to the matters involved.²⁵²

Tax trial fora other than the Tax Court also use stipulations although they emphasize them less. All courts, of course, encourage parties to agree to or to concede matters not genuinely in dispute. However, the "factual issue" condition under § 7491(a) may create a problem in this regard. As noted in subpart II.A.3, the key question is how courts apply this condition when dealing with mixed questions of law and fact, and, in that context, courts may borrow a "predominant purpose" test from standard-of-review law. However, it is widely held, under such law, that what would otherwise have been a factual issue becomes instead a legal issue if the relevant facts have been stipulated²⁵³ or otherwise are not in dispute.²⁵⁴

251. See, e.g., Theodore Tannenwald, Jr., *Tax Court Trials: An Updated View from the Bench*, 47 TAX LAW. 587, 591 (1994) (delineating the multiple benefits from stipulation).

252. TAX CT. R. 91(a)(1).

253. See, e.g., *ABC Rentals of San Antonio, Inc. v. Commissioner*, 142 F.3d 1200, 1203 (10th Cir. 1998) (noting that once the facts have been stipulated there remains only a legal issue of how to apply the relevant Code section); *Meek v. Commissioner*, 98-1 U.S. Tax Cas. (CCH) ¶ 50, 179, at 83,259 (9th Cir. 1998) (designated not for publication) (ruling similarly); *Sennett v. Commissioner*, 752 F.2d 428, 430 (9th Cir. 1985) (ruling similarly).

254. See, e.g., *Marrin v. Commissioner*, 147 F.3d 147, 150 (2d Cir. 1998) (applying de novo standard of review because the facts were not disputed); *United States v. Winthrop*, 417 F.2d 905, 910 (5th Cir. 1969) (classifying the issue as a matter of law because the facts were not

If stipulating, or not contesting, the facts as to an issue converts that issue into one of law, there can be no possibility of burden shifting as to it under § 7491(a)'s "factual issue" condition. One can predict the effect on the behavior of taxpayers. The "factual issue" condition may lead to fewer or less comprehensive stipulations or to taxpayers at least half-heartedly controverting at trial, matters they otherwise would not have disputed, in order to prevent loss of the possibility of burden shifting. Such a result would be unfortunate for the efficiency of the system.

d. Evidence and Briefing

Lawyers are trained to try to secure every reasonably available advantage for their clients. In all but the clearest cases of non-applicability, therefore, we may expect taxpayers and their counsel to argue that § 7491(a) applies to the case, such that the burden of proof is on the IRS.

To make such arguments, taxpayers and their counsel will have to deal with the conditions and exceptions within § 7491 and establish the predicate elements for a burden shift. Unless the IRS stipulates the points, taxpayers will have to establish, for example, that they reasonably cooperated with IRS investigatory requests and that they are under the net worth threshold if they are corporations. This requires presentation of evidence, whether testimonial or documentary, and the IRS, in opposing attempted burden shifting, may introduce its own evidence on such matters. Other predicate elements, such as whether the issue in controversy is a factual issue, will require argument, though not evidence. Thus, additional categories of evidence henceforth will be offered in many, if not most, tax trials, and additional points will have to be briefed. The time required to conclude tax trials and the number of pages in tax briefs both will grow as a result of § 7491(a), to the detriment of the efficiency of our dispute resolution system.

As lawyers and judges work with § 7491 in actual practice, particular categories of such inefficiency will come to light. At least one interesting set of questions can be anticipated now. IRS summonses are not self-enforcing. If the taxpayer (or other target) does not comply, the IRS must bring an action in district court to obtain a decree directing compliance.²⁵⁵ Currently, the IRS sometimes chooses not to bring such a summons enforcement action even in the face of noncompliance. For example, the IRS may conclude that, in the total configuration of the case, obtaining the informa-

disputed); *Thomas v. Commissioner*, 254 F.2d 233, 236 (5th Cir. 1958) (ruling similarly).

255. See I.R.C. §§ 7402 (a) & (b), 7604 (1998) (granting such power to the appropriate U.S. district court).

tion involved would not be worth the resources that a summons enforcement proceeding requires. How would future situations of this type play out under § 7491(a)? Surely, whenever the taxpayer failed to comply with a summons, the IRS would argue that the taxpayer had not cooperated with the IRS, therefore that the burden of proof could not shift in the case. The taxpayer presumably would rejoin that the summons was defective or improper (so it did not constitute a “reasonable” request for information by the IRS) and that the failure of the IRS to seek judicial enforcement of the summons shows the IRS knew the summons was defective or improper.

In such a scenario, one can foresee two undesirable effects. First, to foreclose such an argument by the taxpayer, the IRS might bring an enforcement action that, absent § 7491(a), it would have chosen to forgo. If that occurs, there will be more summons enforcement cases than are optimum from an efficiency standpoint, the excess occurring simply because the IRS is factoring in the § 7491 effects of not seeking such enforcement. Second, if the propriety of the summons is not determined in a district court action, how is the court trying the ultimate tax liability case to know whether the taxpayer reasonably cooperated with a reasonable IRS request, in order to ascertain who bears the burden of proof? One could imagine a collateral hearing within the liability case on this issue, that is, a quasi-summons enforcement hearing within the liability trial in order to allocate the burden of proof in that trial. Surely, such an approach would delay and raise the costs of resolving tax disputes.

C. SUMMARY

Two of the conditions for burden shifting under § 7491(a)—the “factual issue” and “operation with the IRS” conditions—are ambiguous. Their application in particular tax trials is likely to be uncertain. Such uncertainties will affect the behavior of tax litigants. Section 7491(a) will increase the percentage of tax disputes that go to litigation; it will increase ultimately meaningless and wasteful sparring at and before trial; and it will increase litigation expense and inconvenience for all parties including taxpayers, the IRS, third-party witnesses, and the courts.²⁵⁶

256. For support for these concerns, see Tannenwald, *supra* note 251, at 12-15, and *Burden-of-Proof Provision Could Spur Disputes, Tax Court Chief Judge Says*, 98 TAX NOTES TODAY 12-58 (Jan. 20, 1998) (letter from Chief Judge Mary Ann Cohen to Senators William V. Roth, Jr., and Daniel Patrick Moynihan).

Judge Tannenwald also raises an additional concern that § 7491 is likely to complicate resolution of small tax cases (so called “S” cases), causing delay and complications for small-case taxpayers. *Supra* note 251, at 14.

V. PUBLIC CONFIDENCE HARMS

Part II showed that there is no reassuring answer to questions about § 7491's substance. This Part will demonstrate that, despite the section's emptiness, it has been touted by politicians and described by the media as being an important reform. In short, § 7491 has been vastly oversold.

Left there, my point would be saddening but unremarkable. Hyperbole and unkept promises are immemorial attributes of politics, and those with naïve expectations or delicate sensibilities may do well to avoid looking too deeply into political events and processes.

But my concern goes deeper. The legislative exercise that § 7491 represents is not just unappealing as a matter of governmental aesthetics—it will, I believe, produce real and substantial problems for this country in the long run. Those responsible for § 7491's enactment promised more than the section will deliver. Many citizens and taxpayers will start out believing the promises, then discover that they are empty only when they are actually embroiled in a controversy with the IRS. That discovery will further embitter taxpayers and increase their dissatisfaction. This is important because the success of our tax system rests on a foundation of popular support. The erosion of that foundation cannot be beneficial to the country in the long term.

A. DESCRIPTION OF § 7491 BY POLITICIANS

The promises surrounding § 7491 were not modest. While it has not always been easy to assign clear and definite meanings to the slogans used, they were clearly designed to heighten public expectations about the significance of the measure.

Burden-of-proof shift was part of candidate Bob Dole's tax proposals in his 1996 presidential campaign. He promised to "end the IRS as we know it."²⁵⁷ Specifically, shifting the burden of proof would, the electorate was told, "tame the taxman."²⁵⁸ Indeed, fundamental values were at stake: "Americans who are audited are currently presumed guilty until they prove themselves innocent. This should be reversed."²⁵⁹

This spirit carried over to the Restructuring Act, the legislation of which § 7491 was a part. In a description of the legislation, the Chair of the House Ways and Means Committee explained: "It's about putting the taxpayer first and the IRS second. It's been the other way around for entirely

257. Sheryl Stratton, *Shifting the Burden of Proof to the IRS*, 72 TAX NOTES 1328, 1328 (1996) (quoting Dole campaign literature).

258. *Id.*

259. *Id.*

too long.”²⁶⁰ The longer one thinks about this statement, the harder it is to grasp exactly what the statement could mean in the context of an operational revenue system. Nonetheless, it clearly has a “sound bite” quality and communicated to taxpayers that genuine and important change had been wrought.

The section’s proponents spread the idea that § 7491 is a meaningful part of such genuine and important change. This view was emphatically advanced by Senate Majority Leader Trent Lott. In delivering on national television the Republican response to the 1998 State of the Union address, Senator Lott discussed IRS reform and the role of burden-of-proof shift in it:

That’s why one of the first things we will tackle is REAL reform of the I.R.S. . . .

We are going to stop the abuses the I.R.S. is inflicting on American taxpayers. You’ve got our word on it.

* * * * *

[T]he only way to limit Government and expand individual freedom is to eliminate the I.R.S. as we know it today.

It is morally wrong for a free people to live in fear of any Government agency.

It is morally wrong for citizens in a democracy to be presumed guilty until proven innocent.²⁶¹

These are strong words. Reversing the pre-§ 7491 burden-of-proof rule was touted as more than just good policy: it was demanded by democracy, indeed by morality.²⁶² With further reflection, of course, this democratic

260. N.Y. TIMES, June 26, 1998, at A21, col. 1 (quoting Rep. William Archer).

261. Text of address as provided by office of Senator Lott, *reprinted in* NEW YORK TIMES, Jan. 28, 1998, at A21 (emphasis in original).

262. The rhetoric was not confined to Republicans. President Clinton was a belated convert to IRS restructuring, but then tried to lead the charge. *See* President’s State of the Union Address, *reprinted in* N.Y. TIMES, Jan. 28, 1998, at A20 (“Like every taxpayer, I’m outraged by the reports of abuses by the I.R.S. We need some changes there . . . Last year, by an overwhelming bipartisan margin, the House of Representatives passed sweeping I.R.S. reforms. This bill must not now languish in the Senate. Tonight, I ask the Senate, follow the House, pass the bipartisan package as your first order of business.”); Treasury Secretary Robert E. Rubin, *quoted in* WASH. POST, July 23, 1998, at A1 (“We would not be here today [signing the Restructuring Act] were it not for the president’s leadership.”).

In signing the Restructuring Act, President Clinton offered this intriguing observation: “The bill will give the American people an IRS they deserve.” L.A. TIMES, July 23, 1998,

and moral imperative starts to unravel. As seen in Part I, the former rule was settled and largely unchallenged for over a century; it contained many exceptions to accommodate special situations; it was consistent with well established principles of burden-of-proof theory generally; and it was defended by nearly all tax professionals, including taxpayers' representatives. All that being true, was the pre-§ 7491 rule really so anti-democratic and immoral?

In fact, the "taxpayers are guilty until proven innocent" charge mixes apples and oranges. The concepts of "guilt" and "innocence" are drawn from *criminal* law, but § 7491 amends the law applicable to *civil* cases.²⁶³ Instead, we should compare apples to apples and oranges to oranges. In criminal tax cases, the Government bears the burden of proof (just like in criminal non-tax cases) and, to meet it, must establish its case "beyond a reasonable doubt" (just like in criminal non-tax cases).²⁶⁴ Similarly, the allocation of the burden in civil tax cases under the pre-§ 7491 rule was consistent with burden-of-proof law and theory in civil non-tax cases. Where was the democratic or moral defect when tax burdens of proof were consistent with non-tax burdens of proof in both their criminal and civil aspects?²⁶⁵

However, a different defect of the "guilty until proven innocent" slogan is more germane for present purposes. As seen in Part II, § 7491(a)—by virtue of its conditions and exceptions—will leave the burden on the taxpayer in the great bulk of tax cases. That being true, either Congress, in enacting § 7491(a), has honored democracy and morality in the breach not the observance, or the democracy and morality rhetoric was hollow to begin with. Either way, legislators clearly oversold the significance of § 7491(a) and the extent to which taxpayers will benefit from it.

Hyperbole did not end with pre-enactment pronouncements. After passage of § 7491 by their respective chambers, Representatives and Senators continued to paint the measure as far more than it really was—both in legislative statements and in communication with their constituents. Chairman Archer of the Ways and Means Committee declared: "Our plan

at A16. It is not completely clear whether this means that a good people will now have a good IRS or that a wicked people will now receive their comeuppance.

263. Section 7491(a) deals with court proceeding for "ascertaining the liability of a taxpayer for tax." Tax liability is determined in civil proceedings, not criminal proceedings.

264. See, e.g., *Holland v. United States*, 348 U.S. 121, 126 (1954) (stating that "the prosecution must always prove the criminal charge beyond a reasonable doubt").

265. According to one press report, at least some members of Congress were aware of the civil-criminal distinction but chose to disregard it. See WASH. POST, July 23, 1998, at A6 ("The burden of proof is on the government in criminal cases—and in criminal tax cases, for that matter—and members said they felt taxpayers ought to be treated the same way, even through most tax disputes are civil.").

shifts the burden of proof off the taxpayer and onto the IRS.”²⁶⁶ Senator Murkowski, a member of the Senate Finance Committee, said in his newsletter to constituents: “Most importantly, whenever a dispute with the IRS winds up in Tax Court, the legislation shifts the burden of proof from the taxpayer to the IRS. Taxpayers will no longer be presumed guilty until proven innocent—the IRS will have to prove its case.”²⁶⁷

Such statements completely omit reference to the conditions and exceptions that eviscerate § 7491(a). Plainly, the authors of such pronouncements knew or should have known better. Perhaps, given political practice, this is unsurprising; in any event, it is disinformation.

B. DESCRIPTIONS OF § 7491 IN THE MEDIA

Have the media done a better job than the politicians in informing citizens and taxpayers of the true nature of the new burden-of-proof rules? Unfortunately, not by much. Most reports on television, on radio, or in the popular press did not inform their viewers, listeners, or readers that § 7491(a) typically will leave the burden where it always has been—that is, on the taxpayer in most cases.²⁶⁸ Surely, given time, space, and audience

266. *Archer Hails IRS Conference Agreement*, 80 TAX NOTES 70 (1998).

267. *News from the Office of Frank Murkowski*, Summer 1998, at 3. To similar effect, see *Upton: Vote Cast Against Subsidies for Timber Roads*, SOUTH BEND (INDIANA) TRIB., July 19, 1998, at B8 (quoting Rep. Fred Upton stating that “no longer is a person guilty until proven innocent”).

268. Worthwhile accounts include Albert R. Hunt & Alan Murray, *Have a Nice Audit: What the Coming IRS Reforms Will Mean for Your Wallet*, SMART MONEY, Aug. 1, 1998, at 71 (stating that the burden-shift provision is “less broad than it sounds” and “the change is likely to be one of nuance”); Tom Herman, *A Special Summary and Forecast of Federal and State Tax Developments*, WALL ST. J., July 15, 1998, at A1 (“Many legislators have been trumpeting [the burden] change as a major taxpayer victory. But after studying the fine print, some tax lawyers disagree.”); Paul M. Soyk, Special Letter, *Taxpayers Gain Nothing from IRS Reform*, DET. NEWS, July 28, 1998, at A6 (“The widely hailed provision to shift the burden of proof to the IRS is a bit of a sham.”).

Also, some media reports mentioned some of § 7491’s conditions, usually the “recordkeeping” and “cooperation” conditions. See, e.g., Armond Budish, *IRS Reforms Give Citizens Needed Protection*, CLEV. PLAIN DEALER, July 19, 1998, at 6J (discussing record-keeping and cooperation); James S. Horvitz, Viewpoints, *The IRS Actually Blinked*, HOUS. CHRON., July 25, 1998, at 35 (discussing record-keeping and cooperation); Charles A. Jaffe, *Reforming Tax Relief*, BOSTON GLOBE, July 20, 1998, at B4 (discussing record-keeping and cooperation); Gary Klott, *Chalk up Win for Taxpayers in the Battle Against the IRS*, FORT LAUDERDALE SUN-SENTINEL, July 4, 1998, at 15C (discussing record-keeping and cooperation); Kathy Kristof, *IRS Reforms May Help Those Who Have Had Problems*, AUSTIN AMERICAN-STATESMAN, July 19, 1998, at H2 (discussing record-keeping and cooperation); Editorials, *Overhauling the IRS*, CHRISTIAN SCI. MONITOR, July 14, 1998, at 12 (discussing record-keeping and cooperation); *IRS Bills Strengthen Taxpayer Protections*, USA TODAY, May 8-10, 1998, at 6A (discussing record-keeping and cooperation).

attention-span limits, no organ of the media could have been expected to dissect § 7491(a) in full detail.

Still, as far as § 7491(a) is concerned, there is no tension between economy and accuracy. A serviceably correct summary would be: "One section of the new Act is supposed to shift the burden of proof to the IRS. But it contains so many exceptions and conditions, that taxpayers almost never will benefit." This capsulization would have been brief enough for newspapers and news radio, maybe even for television. Instead, however, probably because time pressures prevented journalists from understanding what they were reporting, the media largely took legislators at their word. They accepted that § 7491 did meaningfully shift the burden of proof, and they reported that to the public.

In ascending order of inaccuracy, most media accounts of § 7491 fall into three categories. First are stories that include some qualifying language that the burden shift is not universal. They still, however, give the impression that a shift often will occur.²⁶⁹ Moreover, consumers of the story are more likely to remember the main idea "burden shifted to the IRS" than some vague and ill-defined qualification. In the second category are accounts that state "the burden has been shifted to the IRS" without adding any qualifying language. Such accounts—and there are many of them²⁷⁰—suggest to the public that the burden now is on the IRS in all tax cases.

269. See, e.g., Daniel Eisenberg, *Your Money: Fight Back Against the IRS*, TIME, July 20, 1998, at G8 ("[A] few million taxpayers locked in battle with the dreaded agency may soon have a fair fight. Under the law, the burden of proof in many cases would fall to the government instead of the accused."); Alan Fram, *Congress Poised to Reign in IRS, 'The Agency We Love to Hate'*, NEWARK STAR-LEDGER, July 9, 1998, at 5 ("The bill would shift the burden of proof from the taxpayer to the IRS in many tax court cases . . ."); Editorial, *Bipartisan Reform, Partisan Junk*, DAYTON DAILY NEWS, June 27, 1998, at 12A (stating that "the burden of proof will often be on the IRS"); *Clinton Signs Measure Overhauling the I.R.S.*, N.Y. TIMES, July 23, 1998, at A3. ("Among the changes the new law requires is shifting the burden of proof in many tax court cases to the I.R.S. from the taxpayer."); *How Lawmakers Voted*, ANCHORAGE DAILY NEWS, June 29, 1998, at B2 (stating that the Act "shifts the burden of proof in most civil tax disputes to the government"); *IRS Bill Expected to Pass in Senate: Approval of Reforms 'Virtually Unanimous' Top Democrats Predict*, CHI. TRIB., May 7, 1998, at 1 (stating that the new measure "shift[s] the burden of proof to the IRS in certain court cases"); WORCESTER TELEGRAM & GAZETTE, July 15, 1998, at A8 ("One provision intended to make the system fairer shifts the burden of proof in many tax court cases to the IRS.") (all emphases added).

270. See e.g., Tamara Lytle, *IRS Reforms: Will Taxpayers Really Benefit?*, ORLANDO SENTINEL, July 5, 1998, at A4 (stating that the burden of proof is now on the IRS); Ralph Vartabedian & Jonathan Peterson, *Clinton Signs Bill That Aims to Reform IRS*, L.A. TIMES, July 23, 1998, at A16 (stating that the burden of proof is now on the IRS); *All Things Considered*, (National Public Radio, Peter Kenyon reporting, July 8, 1998) available in 1998 WL 3645597 (stating that the burden of proof is now on the IRS); *Good Start in Tax Reform*, L.A. TIMES, July 24, 1998, at B8 (stating that the burden of proof is now on the IRS); *On Taxes: Reining in the IRS—But Not the Congress*, HOUS. CHRON., June 28, 1998, at 2 (stating that the burden of proof is now on the IRS); Editorial, *Who's in Charge? IRS Reform Blurs Accountability for Troubled Agency*,

uggest to the public that the burden now is on the IRS in all tax cases. Third, and worst, are accounts which not only imply a general shift of the burden but add language expressly underscoring its importance.

As examples of the third category, the *New York Daily News* said: "The legislation promises new power to taxpayers by shifting the burden of proof to the Internal Revenue Service in court battles."²⁷¹ The *Los Angeles Times* offered that the Restructuring Act "would catch up with centuries-old common law by shifting the burden of proof in tax disputes to the accuser, the IRS."²⁷² My hometown newspaper, the *Bloomington Herald-Times*, described the burden shift as "the essential mark of any genuine IRS reform."²⁷³ Others labeled it "an important step toward communicating that citizens can fight city hall"²⁷⁴ and one of the "substantial and significant changes" effected by the Restructuring Act.²⁷⁵ In short, the mass media—far from refuting them—echoed the claims of politicians that § 7491 effects a genuine and general shift of the burden of proof from taxpayers to the IRS.

C. EROSION OF TAX SYSTEM

As the above suggests, proposals that became § 7491 were wrongly explained to the public as representing fundamental and significant change. Section 7491 was "oversold" and "overpromised" by its proponents. This fact may well have long-term, adverse consequences for our tax system.

Unlike revenue systems used by some other countries, the American system relies on the taxpayer to make the first calculation of her own tax liability (on her tax return) and to pay that calculated amount. Moreover, given the low and generally declining percentage of returns the IRS audits,²⁷⁶ that first calculation and payment usually are the last as well. This being the case, our system depends heavily on the honesty and accuracy of taxpayers' returns. As the Supreme Court has recognized, "our tax struc-

SACRAMENTO BEE, July 20, 1998, at B6 (stating that the burden of proof is now on the IRS); Opinion, *IRS Switches to Carrot*, SALT LAKE TRIB., June 30, 1998, at A8; Editorial, *IRS Overhaul Bill Reins in Excesses*, TACOMA NEWS TRIB., July 27, 1998, at A6 (stating that the burden of proof is now on the IRS); WASH. POST, July 23, 1998, at A1 (stating that the burden of proof is now on the IRS).

271. Timothy J. Burger, *Congress Takes Bite Out of IRS*, N.Y. DAILY NEWS, June 25, 1998, at 10.

272. *IRS Abuses Demand Reform*, L.A. TIMES, May 3, 1998, at M4.

273. *IRS Reforms Is Needed, Overdue*, BLOOMINGTON HERALD-TIMES, July 14, 1998, at A6.

274. *Bipartisan Reform, Partisan Junk*, DAYTON DAILY NEWS, June 27, 1998, at 12A.

275. *Keep Chopping the IRS Tree*, DESERET NEWS, July 13, 1998, at A6.

276. See, e.g., Sheldon S. Cohen, *The Ervin N. Griswold Lecture*, 14 AM. J. TAX POL'Y 113, 117 (1997) ("The audit rate in 1964-68 was about 4.5 to 5 percent . . . [T]oday the audit rate is less than one percent.").

ture is based on a system of self-reporting. There is legal compulsion, to be sure, but basically the Government depends upon the good faith and integrity of each potential taxpayer to disclose honestly all information relevant to tax liability."²⁷⁷ Citizens alienated from, and distrustful of, the tax system are less likely to file honest and accurate returns.²⁷⁸ Thus, maintaining public confidence in our revenue system is an important national goal.²⁷⁹

This goal ultimately will be compromised by the gap between the rhetoric and the reality of § 7491. In the short run, the belief—predicated on the “hype” surrounding § 7491 that Congress has saddled the IRS with the civil burden of proof may increase some citizens’ satisfaction levels; however, that condition is not ultimately sustainable.

Many taxpayers will come to this discovery under circumstances which virtually guarantee maximum dissatisfaction. Those who actually believe what they have heard about § 7491 will be angry when they lose in litigation, the adverse opinion saying things like “the taxpayer should have made and kept substantiation,” “the taxpayer should have cooperated with the IRS,” “the burden of proof remains on the taxpayer,” and the like.²⁸⁰ Moreover, even if they did not fully believe the § 7491 hype, many still will

277. *United States v. Bisceglia*, 420 U.S. 141, 145 (1975); see *United States v. Rodgers*, 461 U.S. 677, 683 (1983) (“The common purpose of this formidable arsenal of collection tools is to ensure the prompt and certain enforcement of the tax laws in a system relying primarily on self-reporting.”); *Flora v. United States*, 362 U.S. 145, 176 (1960) (“Our system of taxation is based upon voluntary assessment and payment . . .”); *Helvering v. Mitchell*, 303 U.S. 391, 399 (1938) (“In assessing income taxes the Government relies primarily upon the disclosure by the taxpayer of the relevant facts.”); IRS Proc. Reg. § 601.103(a) (“The Federal tax system is basically one of self-assessment.”).

278. “As [public] dissatisfaction increases, the continued viability of the tax system is threatened—and as it is threatened, so too is the basis of support for essential governmental services and functions.” PRESIDENT’S TAX PROPOSALS TO CONGRESS FOR FAIRNESS, GROWTH & SIMPLICITY (SUMMARY) 2 (1985).

279. The IRS has acknowledged that maintaining “the highest degree of public confidence in [the] integrity, efficiency and fairness” of tax administration is key to its mission. I.R.M. P-1-1 (May 14, 1990). At least aspirationally, the legislative branch shares this perception. See, e.g., Staff of Joint Committee on Taxation, *General Explanation of the Tax Reform Act of 1986*, at 209-10 (1987) (stating that a reason for tax amendments was that “taxpayers were losing faith in the Federal income tax system”).

280. An interesting and growing area of tax scholarship uses cognitive theory to study public reactions to tax rules. See, e.g., Edward J. McCaffery, *Cognitive Theory and Tax*, 41 UCLA L. REV. 1861 (1994) (applying cognitive psychology or behavioral decision theory, which argues that people think and describe in ways that have systematic biases and distortions, to the study of taxation); Joshua D. Rosenberg, *The Psychology of Taxes: Why They Drive Us Crazy, and How We Can Make Them Sane*, 16 VA. TAX REV. 155 (1996) (same); Daniel Shaviro, *Beyond Public Choice and Public Interest*, 139 U. PA. L. REV. 1, 45-51 (1990) (same). It requires no subtle understanding of cognition, however, to anticipate that taxpayers who are told they bear the burden of proof, contrary to their expectations as to § 7491, will feel some dissatisfaction with the system.

feel themselves aggrieved. Losing litigants often feel anger and embarrassment, and blaming Congress for a lie, even if only half believed from the start, would be seductive.

In any event, once individual taxpayers, and over time a critical mass of taxpayers, come to understand that § 7491(a) is empty, public dissatisfaction will be engendered. The image of Congress, already low, will suffer another blow. Predictably, legislators will try to shift blame to the IRS for the embarrassment of Congress's own making,²⁸¹ creating confusion and furthering citizen alienation.

In summary, self-assessment is the bedrock of our tax system, and satisfactory self-assessment depends on high public confidence in the system. The empty symbolism of § 7491(a), and the inevitable public discovery of that emptiness, will undermine such confidence to the long-term detriment of the revenue system, on which the national government depends.

VI. PROPOSAL(S)

Section 7491 is unsatisfactory. In this Part, I discuss what should be done to rectify the situation.

A. BEST APPROACH

Conceptually, there are four possible burden-of-proof regimes for federal tax issues: (1) burden always on the IRS, (2) burden usually on the IRS but with exceptions, (3) burden always on the taxpayer, and (4) burden usually on the taxpayer but with exceptions. The first was considered in Part III. It would be by far the worst approach—indeed, as long as any rationality remains in the corridors of Congress, it is inconceivable as a serious possibility. The second involves an intractable dilemma, a choice between revenue and loss of fairness on the one hand (if the exceptions are few and weak), or ineffectiveness on the other (if the exceptions are numerous and substantial). The drawbacks of § 7491 suffice to reveal the inadequacy of this approach. The third approach would be too inflexible, failing to account for atypical circumstances.

We are left with the fourth approach, the one in place for generations before § 7491 was enacted. However, differences in detail are possible, indeed desirable. As shown in Appendix A, situational exceptions were common under the pre-§ 7491 regime. As appropriate, even more exceptions

281. The process is well known. For instance, Senators and Representatives vote to add new incentives, subsidies, anti-abuse rules, exemptions, transitional rules, and obscurities to the law—then thunder against the complexity of the “IRS Code,” as if the IRS, not Congress, enacted those complexities.

could be crafted, by statute, judicial rule, or case law.²⁸²

For instance, the two special rules of § 7491 could be retained. Of these, § 7491(b)—placing the burden of proof on the IRS when it has reconstructed income “solely through the use of statistical information on unrelated taxpayers”—is insignificant but innocuous.²⁸³ More important (and more beneficial) is § 7491(c), placing the burden of production on the IRS as to penalty issues. Even before § 7491, the burden of persuasion was on the IRS as to a number of tax penalties.²⁸⁴ As to most penalties, however, both the burden of production and the burden of persuasion were on the taxpayer prior to enactment of § 7491.

Congress multiplied the number of tax penalties in the 1970's and 1980's and encouraged their use, in part as a backdoor way to reduce the federal budget deficit. But cavalier assertion of penalties can be dangerous, alienating taxpayers rather than buttressing their voluntary compliance.²⁸⁵ Thus, the IRS must always contemplate with gravity the possible assertion of penalties. Putting the burden of production as to penalties on the IRS is a way to cultivate this atmosphere.

The “action” in penalty cases often involves not the *prima facie* elements of the penalty but affirmative defenses to it.²⁸⁶ Congress shifted only the production burden, not the persuasion burden, under § 7491(c) to emphasize that the taxpayer still bears the burden as to such affirmative defenses.²⁸⁷ Outside of tax law too, it long has been understood that, once a *prima facie* case has been made out, the burden usually is on the party re-

282. For one suggested additional exception, see Michael Quigley, *A Commentary on How the Proposed Regulations Affect the General Principles of Section 482 as Described in the Existing Regulations and in Case Law*, FED. BAR ASS'N SEC. TAX'N REP. 7, 10 (Spring 1992) (suggesting that the burden should be on the IRS in § 482 cases based on third-party pricing data).

283. The IRS often uses average living costs, usually determined through Bureau of Labor Statistics figures, in indirect-method unreported-income cases. However, they typically are used as a supplementary basis of the IRS's determination, not the “sole” basis.

284. See I.R.C. §§ 6703(a) (1994) (providing that the IRS has the burden of proving penalties for organizing or promoting abusive tax shelters, penalties for aiding and abetting understatement of tax liability, and penalties for filing frivolous income tax returns); 7422(e) (providing that the IRS has the burden of proving fraud penalties in refund suits); 7454(a) (providing that the IRS has the burden of proving fraud penalties generally).

285. See, e.g., *IRS Penalty Reform: Hearings Before the Subcommittee on Private Plans and Oversight of the Internal Revenue Service of the Senate Committee on Finance*, 100th Cong. 151 (1988). See generally Thomas R. Hoffman, *Studies of the Code's Tax Penalty Structure: A Fitful Step Toward Reform*, 43 TAX LAW. 201, 203 (1989) (describing Senate committee hearings on disgruntled taxpayers).

286. E.g., §§ 6651(a)(1), (2) & (3) (providing reasonable cause defense to delinquency penalties); 6662(d)(2)(B) (providing disclosure and substantial authority defenses to substantial understatement penalty); 6664(c)(1) (providing reasonable cause defense to accuracy related and fraud penalties).

287. See H.R. REP. NO. 599, *supra* note 57, at 241.

sisting a claim to establish any affirmative defense.²⁸⁸ Requiring the IRS to establish its *prima facie* case but requiring the taxpayer to establish any affirmative defenses, is a sensible approach to penalty issues.

Thus, we should go "back to the future." We should return to the rule that the taxpayer usually bears the burden of proof but should retain, and, as appropriate, expand, exceptions which place part or all of the burden on the IRS. The simplest way to do so would be to repeal § 7491(a) but retain § 7491(b) and (c).

B. ALTERNATIVE APPROACH

Now, a nod towards political reality. Having just enacted § 7491(a) with great fanfare, it would be embarrassing for Congress to do the best thing: simply repeal § 7491(a) outright. Thus, to allow legislators to save political face, I offer an alternative approach.

That approach entails not outright repeal of § 7491(a) but replacement of present § 7491(a) with a new § 7491(a) modeled on a statutory precedent: Federal Rule of Evidence 501. Below, I describe that alternative and show that it would result in restoration of the pre-§ 7491 allocation of the burden of proof.

The draft federal rules of evidence presented to Congress in 1973 dealt extensively with privileges. The proposals proved highly controversial, and a variety of alternatives were offered by commentators.²⁸⁹ Ultimately unable to decide just what privileges should apply in federal litigation, Congress enacted Rule 501, codifying an evolving common law of privilege.²⁹⁰

This approach could be adapted to another controversial area: allocation of the burden of proof in civil tax litigation. Specifically, Congress could revise § 7491(a) to read something like the following:

Except as otherwise provided in this section, in another section of

288. *E.g.*, *Irby v. Bittick*, 44 F.3d 949, 954 (11th Cir. 1995) (stating that, in EPA cases, once a *prima facie* case is made out, burden is on employer to prove affirmative defense); *Fallon v. Illinois*, 882 F.2d 1206, 1211 (7th Cir. 1989) (same); *Powers v. Russell*, 30 Mass. 69, 77 (1833).

289. For detailed discussion of this history, see 23 WRIGHT & GRAHAM, *supra* note 8, § 5421.

290. In relevant part, Federal Rule of Evidence 501 provides:

Except as otherwise required by the Constitution of the United States or provided by Act of Congress or in rules prescribed by the Supreme Court pursuant to statutory authority, the privilege of a witness, person, government, State, or political subdivision thereof shall be governed by the principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience.

Id.

this title,²⁹¹ or in rules prescribed by the courts²⁹² pursuant to statutory authority,²⁹³ the burden of proof in civil tax litigation shall be governed by the principles of the common law as they may be interpreted in the courts of the United States in light of reason and experience.

This alternative would give members of Congress more rhetorical "wiggle room" than outright repeal of present § 7491(a). Congress's proclaimed goal in enacting § 7491 was to "level the playing field" between taxpayers and the IRS.²⁹⁴ Under the above alternative, legislators could assert: "New § 7491(a) (the above alternative) does its job and accomplishes our goal. The IRS will have to abide by the same burden of proof rules as every other litigant; all will be governed by the same common law principles. The IRS will have no special advantage, no unfair advantage, as to the burden of proof."

Of course, there would be no substance behind this. The pre-§ 7491 regime *was* consistent with common-law burden-of-proof principles, so the IRS never had any special advantage as to the burden. But, of course, that is not the point. As we have seen, the rhetoric on which present § 7491(a) was justified had no contact with reality either. One may not feel clean using misleading rhetoric to extricate the nation from the effects of previous misleading rhetoric, but, unfortunately, that may be the way the game of legislation is played. If Congress needs a rhetorical device to smooth the way for undoing its past indiscretion, the above alternative provides it.

Whatever its rhetorical utility, let there be no doubt that the above alternative would accomplish the same substantive result as outright repeal of present § 7491(a): it would restore the prior rule that the taxpayer generally bears the burden of proof. As shown in Appendix B, the prior regime was consistent with common law principles, so would be restored by a rule that made those principles dispositive. Thus, the above alternative § 7491(a) would return us to the pre-1998 burden rule. Hasten the day, either by outright repeal of current § 7491(a) or by its replacement by the above alternative.

291. "Title" means Title 26 of the United States Code, *i.e.*, the Internal Revenue Code. For examples of such other sections, see *supra* text accompanying notes 120-36.

292. The legislative history of such a provision should make clear that, for this purpose, the term "courts" includes not only Article III courts (like the district courts) and units of or adjuncts to them (the bankruptcy courts) but also Article I courts (the Tax Court and the Court of Federal Claims).

293. For examples of burden allocations under court rules, see *infra* text accompanying notes 318-30.

294. See H.R. REP. NO. 364, *supra* note 78, at 56.

CONCLUSION

The previous regime placed the burden of proof on taxpayers generally, with rifle-shot exceptions to cover special situations. In contrast, § 7491 is like a shot-gun with a clogged barrel. Were it to fire, its effect would be felt widely. But, because of § 7491's clogging conditions and limitations, its shot is likely to go nowhere, or to ricochet back on itself with deleterious effect. The prior regime was better. Any perceived deficiencies in it would have been better addressed by new targeted exceptions than by a purportedly general but largely self-canceling reversal of the burden of proof.

Section 7491 will fail in its promise to help taxpayers; it will create or exacerbate problems in tax administration and adjudication; and it will undercut the citizen support essential to our revenue system. These shortcomings were predictable when the Restructuring Act was under consideration by Congress. They were given insufficient attention because the controlling momentum was the drive to create a political symbol. That symbol is not worth the harm it will produce. Hopefully, in the fullness of time—when the heat of the political moment has abated—a more deliberative Congress will return us to the civil tax burden-of-proof allocation that prevailed before enactment of § 7491.

A larger question emerges from the § 7491 affair. That provision and other unfortunate provisions of the Restructuring Act are not isolated missteps. Many have decried the deteriorating quality of tax legislation over the last decade.²⁹⁵ The tax laws have been changed too often, with too little deliberation, and with too little regard to relationship with other Code sections and to the overall complexity of the Code.

Through the various Taxpayer Bills of Rights, the Restructuring Act, and other measures,²⁹⁶ Congress has trained a spotlight on IRS abuses. But, if the way the IRS administers the Code is compared to the way Congress writes the Code, the latter is far the bigger problem for the tax system and the nation. Thus, a key question in the current climate is “can arrangements be forged—in the legislative process, through judicial review, or otherwise—to ameliorate the fact or the effects of congressional irresponsibility in tax writing?” I intend to explore this question in future articles.

295. *E.g.*, *IRS Restructuring*, *supra* note 34, at 264 (statement of Sheldon S. Cohen, former Commissioner, IRS); Glenn E. Coven, *Interpreting Tax Legislation in the 90s*, ABA SECTION OF TAX. NEWSLETTER 11, 11 (Spring 1998); Steve R. Johnson, *Further Thoughts on Interpreting Tax Statutes*, ABA SECTION OF TAX. NEWSLETTER 11, 13 (Summer 1998).

296. *E.g.*, Taxpayer Browsing Protection Act of 1997, Pub. L. No. 105-35, 111 Stat. 1104 (1997).

APPENDIX AFLEXIBILITY OF THE PRE-§ 7491
BURDEN-OF-PROOF REGIME

Although the taxpayer usually bore the burden of proof under the rule which preceded § 7491, this was not invariable. Special approaches altering allocation of either the burden of production or the burden of persuasion in tax cases emanated from statutes, judicial rules, and judicial decisions. Such special approaches were crafted to respond to the peculiar nature of a given issue or the context in which the issue arose.

A. STATUTES

Before enactment of § 7491, sections of the Internal Revenue Code (or of non-Code statutes) placed some or all of the proof burden on the IRS in over a score of situations. They included:

(1) the fair market value of property transferred in connection with performance of services, when the property is subject to a non-lapse restriction which allows transfer only at a price determined under a formula;²⁹⁷

(2) the illegality of bribes and kickbacks to government officials, for purposes of determining the deductibility of such payments;²⁹⁸

(3) the illegality of other payments (made to other than government officials);²⁹⁹

(4) whether an agreement violates generally enforced securities laws or regulations, for purposes of disallowance of deductions for excess payments under golden parachute agreements;³⁰⁰

(5) whether earnings and profits were accumulated beyond the reasonable needs of the business, for purposes of the accumulated earnings tax;³⁰¹

297. I.R.C. § 83(d)(1).

298. I.R.C. § 162(c)(1). Moreover, the IRS had to have "clear and convincing" proof in order to meet this burden. *Id.*; Treas. Reg. § 1.162-18(a)(5). Section 162(c) was enacted in 1969. *See* Tax Reform Act of 1969, Pub. L. No. 91-172, § 902, 83 Stat. 487 (1969). Before such enactment, a similar result had been reached by case law. *E.g.*, *Aetna-Standard Engage Co. v. Commissioner*, 15 T.C. 284, 292 (1950).

299. I.R.C. § 162(c)(2). Again, "clear and convincing" proof was required. *Id.*

300. I.R.C. § 280G(b)(2)(B).

301. I.R.C. § 534(a); Treas. Reg. § 1.534-2(a) (1999). There are conditions under which the burden of persuasion is on, or the burden of production shifts to, the taxpayer, depending on the existence and specificity of various notices and statements passing between the IRS and the taxpayer. *See* I.R.C. §§ 533(a) & 534(a)-(c) (establishing the burden-of-proof rules for accumulated earnings tax cases).

(6) whether it is reasonable to believe that an individual's loss of United States citizenship would substantially reduce his or her United States tax liabilities;³⁰²

(7) whether additional disclosure of written determinations and background information is appropriate;³⁰³

(8) the production of reasonable and probative information (beyond mere introduction of an information return) when the taxpayer reasonably denies receipt of additional income and has fully cooperated with the IRS;³⁰⁴

(9) the applicability of penalties for organizing or promoting an abusive tax shelter;³⁰⁵

(10) the applicability of penalties for aiding and abetting the understatement of tax liability;³⁰⁶

(11) by extension, the appropriateness of an injunction against organization or promotion of an abusive tax shelter or against aiding and abetting understatement of tax liability;³⁰⁷

(12) the applicability of penalties for filing a frivolous income tax return;³⁰⁸

(13) in a Tax Court case, whether a petitioner is liable as a transferee of property of a taxpayer owing tax;³⁰⁹

(14) whether an income tax return preparer willfully attempted to understate tax liability, for purposes of the § 6694(b) preparer penalty;³¹⁰

(15) whether the making of a termination assessment of income tax was reasonable;³¹¹

(16) whether the making of a termination assessment against a § 501(c)(3) organization on account of flagrant political expenditures was reasonable;³¹²

(17) whether the making of a jeopardy assessment of tax was reason-

302. I.R.C. §§ 877(f), 2107(d) & 2501(a)(4).

303. I.R.C. § 6110(f)(4)(A).

304. I.R.C. § 6201(d).

305. I.R.C. § 6703(a); *see* I.R.C. § 6700 (establishing the penalty).

306. I.R.C. § 6703(a); *see* I.R.C. § 6701 (establishing the penalty).

307. Conduct violative of § 6700 or § 6701 is the predicate for such an injunction. I.R.C. § 7408(a); *see* *United States v. United Energy Corp.*, 87-1 U.S. Tax Cas. (CCH) ¶ 9216, at 87,365 (N.D. Cal. 1987) (stating that the "United States must prove that defendants are subject to penalty under Section 6700 by a preponderance of the evidence").

308. I.R.C. § 6703(a).

309. I.R.C. § 6902(a). The petitioner does have the burden as to whether the transferor owed tax. *Id.* However, special discovery provisions are available to help the petitioner meet that burden. I.R.C. § 7429(g)(2).

310. I.R.C. § 7427; *see* *Treas. Reg. § 1.6694-1(b)(5)*.

311. I.R.C. § 7429(g)(1); *see* I.R.C. § 6851.

312. I.R.C. § 7429(g)(1); *see* I.R.C. § 6852.

able;³¹³

(18) whether the position taken by the IRS in the dispute was reasonable, for purposes of the cost-shifting provisions when the taxpayer prevails in the proceeding;³¹⁴

(19) whether civil fraud penalties should be imposed;³¹⁵

(20) whether a foundation manager knowingly participated in any prohibited transaction;³¹⁶

(21) whether a worker is an "employee" for purposes of the so-called "safe harbor" provisions with respect to employment taxes.³¹⁷

B. JUDICIAL RULES OF PROCEDURE

The great bulk of trials for the determination of federal tax liability are conducted before the United States Tax Court.³¹⁸ The Tax Court's Rules of Practice and Procedure repeated a number of the statutory burden reversals described above, including placing on the IRS the burden of proof as to matters involving the civil fraud penalty;³¹⁹ knowing participation in prohibited conduct by foundation managers, trustees, and organization managers;³²⁰ liability as a transferee;³²¹ accumulated earnings tax;³²² addi-

313. I.R.C. § 7429(g)(1); see I.R.C. §§ 6861 & 6862. As to all of §§ 6851, 6852, 6861 & 6862, however, the taxpayer does have the burden as to the reasonableness of the amount of the assessment. I.R.C. § 7429(g)(2).

314. I.R.C. § 7430(c)(4)(B)(i).

315. See I.R.C. §§ 7454(a) (regarding the burden of proof in fraud cases generally); 7422(e) (regarding refund suits). The IRS has to have "clear and convincing" proof to meet this burden. *E.g.*, *Stone v. Commissioner*, 56 T.C. 213, 220 (1971); *Beaver v. Commissioner*, 55 T.C. 85, 92 (1970). See also I.R.C. § 6663(b) (establishing presumption that, if the IRS proves that any part of a tax deficiency is attributable to fraud, the whole deficiency will be treated as attributable to fraud but providing that taxpayer could rebut this presumption through a preponderance of the evidence).

316. I.R.C. § 7454(b); see I.R.C. §§ 4912 (regarding tax on disqualifying lobbying expenditures of certain organizations); 4941 (regarding taxes on self-dealing); 4944 (regarding taxes on investments which jeopardize charitable purpose); 4945 (regarding taxes on taxable expenditures); § 4951 (regarding taxes on self-dealing); § 4952 (regarding taxes on taxable expenditures); § 4955 (regarding taxes on political expenditures of § 501(c)(3) organizations); 4958(c) (regarding taxes on excess benefit transactions).

317. Revenue Act of 1978, Pub. L. No. 95-600, § 530, 92 Stat. 2763, 2885-86 (1978).

318. See, *e.g.*, Arthur L. Nims, III, *The Role of the Tax Court*, Address to 10th Annual Maryland Advanced Tax Institute (Nov. 12, 1990) (on file with author) ("Ninety-five percent of all substantive civil tax litigation is conducted by the Tax Court.").

319. TAX CT. R. 142(b).

320. TAX CT. R. 142(c).

321. TAX CT. R. 142(d).

322. TAX CT. R. 142(e).

tional disclosure actions;³²³ and cost-shifting actions.³²⁴

In addition, the Tax Court's rules place the proof burden on the IRS in three situations not covered by statute:

(1) Cases typically reach the Tax Court because the taxpayer has filed a petition contesting the IRS determinations contained in a statutory notice of deficiency issued after audit.³²⁵ After the petition is filed, the IRS sometimes concludes that even more tax is owed than it determined in its statutory notice. It will assert such additional tax via pleadings or amended pleadings in the Tax Court case. By rule, the IRS bears the burden of proof as to such increases in the asserted deficiency.³²⁶

(2) The IRS also may seek to assert new matters not in the statutory notice, without claiming an increased deficiency. These may be new adjustments or may be new theories requiring different factual development in support of adjustments already in the notice.³²⁷ By rule, the IRS bears the burden of proof as to such new matters.³²⁸

(3) The IRS may rely on any of a number of affirmative defenses in its answer to the taxpayer's petition. These include *res judicata*, collateral estoppel, other varieties of estoppel, and statute-of-limitations bar.³²⁹ By rule, the IRS bears the burden of proof as to such affirmative defenses in its answer.³³⁰

C. JUDICIAL DECISIONS

Under the former regime, the courts did not confine reallocations of civil tax burdens to judicial rule. On occasion, they also reversed the burden (either as to production or persuasion) through decisions in particular cases. For instance,

(1) A major case-law alteration of the prior general burden allocation involved unreported income cases. When the IRS asserted that the taxpayer had underreported her income, a number of courts held that the IRS bore some initial burden to support the allegation. Some courts required "some substantial evidence . . . demonstrating that the taxpayer received unre-

323. TAX CT. R. 229.

324. TAX CT. R. 232(e) & 270(d).

325. See I.R.C. §§ 6212-6215 (requiring such notices for certain types of taxes and authorizing Tax Court review).

326. TAX CT. R. 142(a).

327. As to what constitutes a new matter for this purpose, see e.g., *Achiro v. Commissioner*, 77 T.C. 881, 889-91 (1981); Richard C. Forman, *The Burden of Proof*, 39 TAXES 737, 740-47 (1961).

328. TAX CT. R. 142(a); see TAX CT. R. 217(c) (stating similar rule as to declaratory judgment actions).

329. TAX CT. R. 39.

330. TAX CT. R. 142(a).

ported income."³³¹ Others required at least an IRS showing linking the taxpayer with the activity which allegedly generated the additional income.³³² Should the IRS fail to make such a showing, it would lose before such courts, even when the taxpayer introduced no evidence.³³³ A few courts went even further.³³⁴ Not content with imposing an initial burden of production on the IRS, these courts shifted the burden of persuasion to the IRS in unreported income cases.³³⁵

Thus, in unreported income cases, many courts placed an initial burden of production on the IRS and some even placed the burden of persuasion on it. The pattern among the courts was confusing and, since courts sometimes switched camps, shifting. That being so, every prudent attorney for the Government prepared and presented his case in an unreported income trial as if his client bore the full burden of proof.³³⁶ Consequently, as a practical matter, the burden of proof in unreported income cases came close to being reversed even under the former regime.

(2) When the IRS uses the "net worth method" to establish unreported income, an essential element is "opening net worth," defined as the taxpayer's net worth at the start of the first tax year at issue.³³⁷ The IRS bore the burden of proving opening net worth with reasonable certainty.³³⁸

(3) Since 1988, the Tax Court has had the authority to enjoin IRS col-

331. *Bradford v. Commissioner*, 796 F.2d 303, 305 (9th Cir. 1986); *Delaney v. Commissioner*, 743 F.2d 670, 671 (9th Cir. 1984); *see Spatafore v. United States*, 752 F.2d 415, 418 (9th Cir. 1985) (stating that the district court's finding cannot be overturned unless such a finding was clearly erroneous).

332. *Schaffer v. Commissioner*, 779 F.2d 849, 858 (2d Cir. 1985); *DiMauro v. Commissioner*, 706 F.2d 882, 884 (8th Cir. 1983).

333. *Walker v. Commissioner*, 757 F.2d 36, 38 (3d Cir. 1985).

334. Most courts, however, did not shift the burden of persuasion in unreported income cases. *Bennet v. Commissioner*, 98-1 U.S.T.C. (CCH) ¶ 50,238 (1st Cir. 1998) (per curiam) (designated not for publication); *Delaney v. Commissioner*, 99 F.3d 20, 23 (1st Cir. 1996).

335. *Cebollero v. Commissioner*, 967 F.2d 986, 990-91 (4th Cir. 1992); *Portillo v. Commissioner*, 932 F.2d 1128, 1134 (5th Cir. 1991); *Keogh v. Commissioner*, 713 F.2d 496, 501 (9th Cir. 1983); *United States v. Stonehill*, 702 F.2d 1288, 1294 (9th Cir. 1983).

336. Of course, not every attorney was prudent, especially initially. For example, when the IRS received a Form W-2 from an employer or a Form 1099 from another payor suggesting additional income the taxpayer did not report, the IRS sometimes relied on that Form alone, without conducting deeper investigation. This practice, however, was condemned in *Portillo v. Commissioner*, 932 F.2d 1128, 1134 (5th Cir. 1991), *rev'g on this issue*, 58 T.C.M. (CCH) 1386 (1990), and was proscribed by Congress in I.R.C. § 6201(d). Such reminders reinforced the circumspection with which Government attorneys usually prepared and presented unreported income cases.

337. *Holland v. United States*, 348 U.S. 121, 132 (1954).

338. *Yoon v. Commissioner*, 135 F.3d 1007, 1012 (5th Cir. 1998); *Campfield v. Commissioner*, 72 T.C.M. (CCH) 425, 429 (1996), *aff'd*, 133 F.3d 906 (2d Cir. 1997).

lection efforts under certain circumstances.³³⁹ The court has crafted shifting burdens for such injunction cases. For example, the Tax Court may enjoin the IRS from selling any property seized pursuant to a termination or jeopardy assessment and levy against a taxpayer who has filed a Tax Court petition.³⁴⁰ The court has held that, with respect to a motion to stay such a sale, the taxpayer bears the initial burden of asserting plausible and believable grounds in support of the motion. If she does, the burden then shifts to the IRS to prove that the sale is necessary and appropriate.³⁴¹

Similarly, the Tax Court may enjoin the assessment and collection of tax before completion of Tax Court review of an alleged deficiency.³⁴² The Tax Court has held that, with respect to a motion to stay such assessment and collection, the taxpayer bears the initial burden of asserting plausible and believable grounds that the assessment or collection is premature. If she does, the burden then shifts to the IRS to prove that its actions were proper.³⁴³

(4) Generally, the IRS must assess a tax liability, including any deficiency, within three years of the filing of the tax return,³⁴⁴ although a variety of exceptions can extend this period.³⁴⁵ The courts have held that, if the IRS issues its statutory notice more than three years after the return is filed, the IRS bears the burden of establishing that an exception applies.³⁴⁶ This meant that "as a matter of general practice the Commissioner ha[d] the ultimate burden of proof with respect to the statute of limitations."³⁴⁷

(5) In an action to enforce an IRS summons for information, the IRS bears the burden of establishing a *prima facie* case. If it does so, the burden shifts to the party opposing the summons to show that there is some other reason the summons should not be enforced.³⁴⁸

339. See Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, §§ 6243 & 6245(a), 102 Stat. 3749-51 (1988) (allowing the Tax Court to review certain sales of seized property).

340. I.R.C. § 6863(b) (1998).

341. *Williams v. Commissioner*, 92 T.C. 920, 935 (1989).

342. I.R.C. § 6213(a) (1998).

343. *Kamholz v. Commissioner*, 94 T.C. 11, 16-17 (1990).

344. I.R.C. § 6501(a).

345. See, e.g., I.R.C. § 6501(c), (e) (listing exceptions, such as filing a false return, failure to file a return, and omitting a significant part of gross income).

346. E.g., *Murray v. United States*, 292 F.2d 602, 603-04 (1st Cir. 1961); *Reis v. Commissioner*, 1 T.C. 9, 12 (1942); *Concrete Engineering Co. v. Commissioner*, 19 B.T.A. 212, 221-22 (1930), *aff'd*, 58 F.2d 566 (8th Cir. 1932).

347. *Forman*, *supra* note 327, at 739.

348. *United States v. Powell*, 379 U.S. 48, 57-58 (1964). To establish that *prima facie* case, the IRS must show that it has a legitimate purpose, that the inquiry may be relevant to that purpose, that the IRS does not already possess the information sought, and that required administrative steps have been followed. *Id.*

(6) The IRS bears the burden of proving that it sent a statutory notice of deficiency to the taxpayer.³⁴⁹

(7) If the taxpayer initially demonstrates that the statutory notice was arbitrary or without foundation, courts often shift the burden of proof in the case to the IRS.³⁵⁰

(8) The IRS may make only one inspection of a taxpayer's books and records for each tax year unless it notifies the taxpayer of the necessity of an additional inspection.³⁵¹ In the event of litigation, the IRS bears the burden of persuasion as to the applicability of this exception.³⁵²

(9) If the IRS made a refund that it later considers to have been erroneous, it may sue to recover it.³⁵³ The Government bears the burden of proving that some amount was refunded erroneously and what that amount was.³⁵⁴

(10) When the Government sued to collect taxes despite not having made an assessment, the burden was on the Government.³⁵⁵

(11) In addition to the above more-or-less formalized situations, courts sometimes have shifted some or all of the burden of proof to the IRS as an ad hoc remedy under the circumstances of the case at hand.³⁵⁶

In summary of the foregoing statutory, rule, and case law exceptions, one is struck by the flexibility of the pre-§ 7491 regime. Although taxpayers bore the burden of proof on most issues under the former rule, there were numerous exceptions. The regime was capable of evolving, and did evolve, over time as new conditions or problems were perceived by the legislature or the courts.³⁵⁷

349. *Traxler v. Commissioner*, 61 T.C. 97, 100 (1973), *modified*, 63 T.C. 534 (1975).

350. *Scar v. Commissioner*, 814 F.2d 1363, 1375 (9th Cir. 1987) (Hall, J., dissenting) (suggesting reversal of the burden as alternative to holding for the taxpayer outright); *Cohen v. Commissioner*, 266 F.2d 5, 11 (9th Cir. 1959).

351. I.R.C. § 7605(b).

352. *E.g.*, *Boren v. Tucker*, 239 F.2d 767, 771 (9th Cir. 1956); *U.S. Aluminum Siding Corp. v. Eshleman*, 170 F. Supp. 12, 14-15 (N.D. Ill. 1958); *In re Foster*, 159 F. Supp. 444, 447 (S.D.N.Y. 1958).

353. I.R.C. § 7405(b).

354. *E.g.*, *Soltermann v. United States*, 272 F.2d 387, 387 (9th Cir. 1959).

355. *E.g.*, *United States v. Tyson*, 40-1 U.S. Tax Cas. (CCH) ¶ 9430, at 463 (N.D. Ill. 1939).

356. *See, e.g.*, *O'Reilly v. Commissioner*, 973 F.2d 1403, 1408 (8th Cir. 1992) (partly shifting the burden of proof as to a valuation issue when the taxpayer had relied on valuation tables promulgated by the IRS); *Borchers v. Commissioner*, 95 T.C. 82, 89-91 (1990) (shifting to the IRS the burden of going forward as to investment tax credit issue); *Smith Leasing Co. v. Commissioner*, 43 T.C. 37, 41-42 (1964) (shifting to the IRS the burden of going forward as to whether claimed expenses had previously been deducted by the taxpayer or its predecessor). *See generally* John T. Piper & James M. Jerge, *Shifting the Burden of Proof in Tax Court*, 31 TAX LAW. 303 (1978).

357. Some exceptions to the former general rule, such as the IRS's burden as to civil fraud,

APPENDIX B

CONSISTENCY OF THE PRE-§ 7491
REGIME WITH
BURDEN-OF-PROOF THEORY GENERALLY

Many courts and commentators have discussed the factors relevant to allocating the burden of proof, and their formulations have been various. Writing about burden-of-proof rules generally, Professors Wright and Graham described the “Three P’s” customarily used by the courts in allocating the burden: Policy, Probability, and Possession of Proof.³⁵⁸ In a leading article, Dean Martinez discussed five general factors that inform the rules for allocating the burden in tax cases (in addition to statutory command): (1) which party has the affirmative of the issue, (2) which party is the plaintiff, (3) whether the particular contention is one disfavored by the courts, (4) which party’s scenario as to the contention is the less likely, and (5) which party has easier access to evidence as to the matter at issue.³⁵⁹

These five factors are a mixture of two styles of legal reasoning: conceptualism and functionalism.³⁶⁰ For instance, the question “which party is the plaintiff?” is a conceptual inquiry. In contrast, the question “which party has superior access to the facts?” is grounded in concerns such as ease, efficiency, and decisional accuracy, and therefore is a functional inquiry.

Everyone, of course, uses conceptualism sometimes and functionalism sometimes, but shades of preference exist. I am a confirmed functionalist. Thus, I would place principal emphasis on the practical consequences choices produce. In particular, I believe that the “possession of proof” consideration usually should be the controlling factor in allocating the civil tax

have existed for generations. See Revenue Act of 1928, § 601, ch. 852, 45 Stat. 791 (codified at I.R.C. § 7454(a)). Others, such as that in the § 7430 cost-shifting provisions, arose only recently. See Taxpayers Bill of Rights 2, § 701, Pub. L. No. 104-168, 110 Stat. 1452, 1463 (codified at I.R.C. § 7430 (1996)).

358. WRIGHT & GRAHAM, *supra* note 8, at 556-57. “Probability” involves the perceived likelihood that a given allegation will be found to be correct. The more surprising or improbable the allegation, the more likely the courts are to say to the proponent of that claim: “You’ll have to prove that.” *Id.*

359. Martinez, *supra* note 39, at 249-55, 268-73. For a discussion of factors unique to the tax field, see *id.* at 274-77.

360. Conceptualism chooses between competing answers to legal questions by asking: “Which answer follows more logically from existing precedents or rules? Which answer more closely approximates answers already given to similar questions?” Functionalism, on the other hand, asks: “Which answer is more likely to improve society? What concrete results could be expected from the different answers, and which set of results is preferable?” See Ernest J. Weinrib, *Legal Formalism: On the Immanent Rationality of Law*, 97 YALE L.J. 949 (1988) (discussing these alternative styles of legal reasoning).

burden of proof. However, the former civil tax burden-of-proof regime was capable of being embraced by both conceptualists and functionalists. By usually placing the burden on the taxpayer but reallocating it to the IRS in unusual situations, that regime comported well with *both* the conceptual and the functional factors stressed by burden-of-proof theory.

A. THE AFFIRMATIVE OF THE ISSUE

In general, the affirmative of an issue—that is, the contention that something *did* happen—is thought to be easier to establish than the negative of the issue—the contention that something *did not* happen. This has been thought to support imposing the burden on the party asserting the affirmative of an issue.³⁶¹ The usefulness of this factor has been criticized, especially since it is not always clear that a matter in controversy has a natural affirmative or negative form.³⁶² Moreover, in my opinion, this factor tends to bleed into the more important factor as to which party has better access to evidence.

Whatever the usefulness of this factor, however, the former tax burden-of-proof regime operated consonantly with it. The income tax is by far the most frequently litigated federal tax. Of litigated income tax issues, probably the majority involve the taxpayer's eligibility for a deduction (or credit). The taxpayer has the affirmative of such issues. It would be easier for the taxpayer to show that she made the expenditure in question and that the expenditure was of the nature contemplated by a particular deduction (or credit) section than it would be for the IRS to prove that she made no expenditure or that all deduction (or credit) sections in the Code are inapplicable.³⁶³

Moreover, when the issue involves not deductibility (or creditability) of an expense but whether the taxpayer had additional taxable income, the taxpayer again often is asserting the affirmative of the issue. Such disputes frequently turn on whether a particular item of receipt falls within one of the exemption or exclusion provisions of the Code.³⁶⁴ Again, it is more

361. See, e.g., JAMES ET AL., *supra* note 8, at 322 (discussing the generally accepted norms as to burden of proof).

362. See, e.g., Charles V. Laughlin, *The Location of the Burden of Persuasion*, 18 PITT. L. REV. 3, 5-6 (1956).

363. As an example, in one case, the issue involved the source that had generated a particular gain. Because the IRS raised an adjustment that was not in the statutory notice, the burden of proof was held to be on the IRS. TAX CT. R. 142(a). The taxpayer pointed to four or five possible origins of the gain, which the IRS had not expressly negated. As a result, the IRS was held not to have met its burden of proof, so lost. *Weaver v. Commissioner*, 25 T.C. 1067, 1086 (1956).

364. See, I.R.C. §§ 71-90 (listing items specifically included in gross income); 101-139

natural to compel the taxpayer to show that one particular exclusion section applies than to compel the Government to show that all exclusion sections do not apply.

The principal time when the IRS would be asserting the affirmative in an income tax case would be when the issue is whether the taxpayer had greater receipts of an admittedly taxable type than she reported on her return. Here, it seems more natural to require the IRS to show there was more income than was reported, than to require the taxpayer to "prove the negative" that there was not.³⁶⁵

But the pre-§ 7491 regime demonstrated its flexibility on this issue. As seen, many courts shifted the burden of initial production, sometimes even the burden of persuasion, to the IRS in unreported income cases.³⁶⁶ As illustrated by income tax cases, therefore, the former burden-of-proof regime fit well with the "who has the affirmative of the issue" factor. The taxpayer usually has the affirmative of tax issues and usually had the burden of proof, but a partial or complete shift of the burden to the IRS often occurred when the IRS was the party asserting the affirmative of the issue.

B. THE PLAINTIFF

Dean Martinez also indicated that allocation of the burden should be informed by which party is the plaintiff. Although this factor too has been subject to criticism,³⁶⁷ it continues to be widely applied by courts.³⁶⁸ Historically, and at least in part substantively, the former civil tax burden alloca-

(listing items specifically excluded from gross income).

365. For examples of cases in which the burden of proof shifted to the IRS, see *Anastasato v. Commissioner*, 794 F.2d 884, 887 (3d Cir. 1986); *Karme v. Commissioner*, 673 F.2d 1062, 1065 (9th Cir. 1982); *Llorente v. Commissioner*, 649 F.2d 152, 156 (2d Cir. 1981); Note, *Proving a Negative—When the Taxpayer Denies Receipt*, 70 CORNELL L. REV. 141 (1984).

However, some commentators have argued that the difficulty of proving a negative can be exaggerated. See, e.g., WILLIAM BEST, A TREATISE ON THE PRINCIPLES OF EVIDENCE § 255 (1849) (stating that proving a negative is not always as difficult as often suggested); Kevin W. Saunders, *The Mythic Difficulty in Proving a Negative*, 15 SETON HALL L. REV. 276 (1985) (stating that the difficulty in proving a negative is easily and often overstated). For an application of this to unreported income cases, see Note, *The Presumption of Correctness: Should the Commissioner Be Required To Carry the Initial Burden of Production*, 55 FORDHAM L. REV. 1087, 1102-06 (1987).

366. See *supra* text accompanying notes 331-36 (discussing court decisions shifting the burden to the IRS in unreported income cases).

367. See, e.g., Wigmore, *supra* note 3, at 288; Edward W. Cleary, *Presuming and Pleading: An Essay on Juristic Immaturity*, 12 STAN. L. REV. 5, 11 (1959).

368. "[I]n most litigation, from time immemorial, the burden of proof—i.e., the burden of persuasion—is on the plaintiff." *Rockwell v. Commissioner*, 512 F.2d 882, 887 (9th Cir. 1975); see, e.g., *Helvering v. Taylor*, 293 U.S. 507, 514 (1935).

tion was consonant with this factor.

Originally, taxpayers had no prepayment judicial recourse for contesting federal tax liabilities.³⁶⁹ They had to pay the taxes in question then sue for a refund, at first in common law assumpsit actions for money had and received,³⁷⁰ later in statutory actions.³⁷¹ In a refund suit, the Government has the money in question and the taxpayer seeks to obtain it. In this posture, the taxpayer is the plaintiff, so she would be expected to shoulder the burden of proof according to this principle.³⁷²

Prepayment remedies for taxpayers developed later, first within the revenue agency itself, then through the Board of Tax Appeals (the forerunner of the Tax Court).³⁷³ In substance, the IRS could be said to be the plaintiff in a prepayment case—it is seeking to obtain money in the taxpayer's possession.³⁷⁴ Formally, however, the matter sits differently. Typically, after audit, the IRS issues a statutory notice of deficiency stating its determination as to correct tax liability. The prepayment litigation is inaugurated when the taxpayer files a petition with the tribunal contesting the determination. In this sense, the taxpayer is the party initiating the suit. Because of this formality (and as a matter of habit carried over from the prior refund tradition), the taxpayer always has been viewed as the plaintiff, even in prepayment suits.

The "who is the plaintiff?" factor also explains some of the exceptions to the general rule as it existed before § 7491. When the IRS asserts new issues or additional deficiencies not contained in the statutory notice, or when the IRS raises by answer any affirmative defense, it becomes the proponent of those claims, in effect the plaintiff as to them. This explains why—consistently with this factor in traditional burden-of-proof theory—the IRS was assigned the burden as to such matters.³⁷⁵

369. For detailed discussions of this early period, see HAROLD DUBROFF, *THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS* 28-35 (1979); see also Martinez, *supra* note 39, at 260-62; William T. Plumb, Jr., *Tax Refund Suits Against Collectors of Internal Revenue*, 60 HARV. L. REV. 685, 686-91 (1947).

370. See, e.g., *Bend v. Hoyt*, 38 U.S. (13 Pet.) 263 (1839); *Elliott v. Swartwout*, 35 U.S. (10 Pet.) 137 (1836).

371. Tucker Act, ch. 359, 24 Stat. 505 (1887).

372. E.g., *Stone v. White*, 301 U.S. 532, 534 (1937); *David v. Phinney*, 350 F.2d 371, 376 (5th Cir. 1965).

373. In 1917, administrative prepayment review of asserted tax deficiencies became available within the Internal Revenue Bureau (now the IRS). This was followed in 1924 by creation of the Board of Tax Appeals. See Dubroff, *supra* note 369, at 35-79 (elaborating on the historical development of the IRS).

374. See FREELAND ET AL., *supra* note 167, at 1016 (outlining similarities in these types of cases).

375. See TAX CT. R. 142(a); see also *supra* text accompanying notes 325-30.

C. DISFAVORED CONTENTIONS

This traditional factor undergirds both the usual burden allocation under the former general rule and a number of the exceptions to it. At the general level, two considerations came into play in this regard, at least historically. First, the modern era of taxation in the United States began with the passage of the Sixteenth Amendment in 1913. For most of the time since then, the dominant tendency of the courts, recognizing the centrality of revenue to the modern state, has been solicitude towards revenue-raising.³⁷⁶ This has been given doctrinal expression in constructional rules which presume that receipts are taxable,³⁷⁷ and that expenditures are non-deductible,³⁷⁸ unless shown to the contrary. The existence of such rules makes arguments for non-taxability or for deductibility disfavored contentions, suggesting, under this traditional factor of burden-of-proof theory, that the burden usually should be on the taxpayer. Second, the courts often have invoked a presumption that actions taken by the Government are correct. In tax law, this presumption of administrative regularity has extended to both the procedural³⁷⁹ and substantive³⁸⁰ aspects of actions by the IRS.³⁸¹ This presumption adds additional weight to viewing an argument that the IRS's determination was wrong as being a disfavored contention.

Both principles can be pushed too far. Courts have varied widely in the extent to which they sought to protect the revenue or to espouse faith in the regularity and correctness of Government actions.³⁸² Still, for many

376. *E.g.*, *United States v. Dalm*, 494 U.S. 596, 604 (1990); *Bull v. United States*, 295 U.S. 247, 259 (1935).

377. *E.g.*, *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 429 (1955) ("This Court has frequently stated that [current I.R.C. § 61] was used by Congress to exert in this field 'the full measure of its taxing power.'" (citations omitted).

378. *E.g.*, *Interstate Transit Lines v. Commissioner*, 319 U.S. 590, 593 (1943) ("[A]n income tax deduction is a matter of legislative grace and . . . the burden of clearly showing the right to the claimed deduction is on the taxpayer."). *But see* Erwin N. Griswold, *An Argument Against the Doctrine that Deductions Should Be Narrowly Construed as a Matter of Legislative Grace*, 56 HARV. L. REV. 1142 (1943) (arguing that it is a function of the court to interpret the statute and resolve doubt).

379. *R.H. Stearns Co. v. United States*, 291 U.S. 54, 61-62 (1934).

380. *E.g.*, *Niles Bement Pond Co. v. United States*, 281 U.S. 357, 361 (1930); *Thomas v. Commissioner*, 223 F.2d 83, 88 (6th Cir. 1955).

381. The same forces that led the courts to this view also caused them to accord similar indulgence to the actions of federal regulatory agencies, for much of the modern period. *See* Steve R. Johnson, Note, *Reasonable Relation Reassessed: The Examination of Private Documents by Federal Regulatory Agencies*, 56 N.Y.U. L. REV. 742, 749-53 (1981) (discussing relaxed restrictions on agency access).

382. Karl Llewellyn's classic pairing of antithetical canons of statutory interpretation, Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to Be Construed*, 3 VAND. L. REV. 395 (1950), has parallels in tax. Opposed to the above

courts, throughout much of our modern chapter of taxation, a desire not to impede revenue collection and tax administration has buttressed other reasons to place the proof burden on taxpayers.

In addition, "disfavored contention" analysis is dynamic, not static. If, as I believe, revenue-protection and presumed-administrative-regularity have often been a "thumb on the scale" in the past, that need not always obtain. Especially since the Reagan Administration and given the recent Republican ascendancy in Congress, many have felt that we need to be protected *from* the government, not by it. Lively controversy now exists as to whether, at this stage in our political evolution, the country is better served by the marginal dollar entering the federal fisc or by its remaining in private hands. Depending on the outcome of this national debate, there may be an inversion in which contentions are disfavored.³⁸³ Indeed, § 7491 may be seen as representing just that inversion, effected legislatively rather than judicially.³⁸⁴

The "disfavored contention" factor of traditional burden-of-proof theory also explains a number of exceptions to the former general rule. It is "un-genteel" to assert that a taxpayer committed fraud,³⁸⁵ or violated applicable non-tax law,³⁸⁶ and it is irregular to assert that normal procedural steps and safeguards must be omitted because of collection exigencies.³⁸⁷ Accordingly, the pre-§ 7491 regime placed the burden of proof on the IRS when its case involved such assertions.

pro-Government precepts are several favoring taxpayers. *See, e.g.,* *Gould v. Gould*, 245 U.S. 151, 153 (1917) (stating that, if the statute's application to a situation is unclear, doubt should be resolved against taxability); *Northville Dock Corp. v. Commissioner*, 52 T.C. 68, 73 (1969), *aff'd*, 427 F.2d 164 (2d Cir. 1970) (stating that deductions and credits should be liberally construed to accomplish their subsidy purposes). However, the pro-revenue maxims have loomed larger in tax jurisprudence than have the anti-revenue maxims.

383. The retrenchment of the formerly high universal reach of federal authority under the Commerce Clause, illustrates that judicial doctrine is not immune from this national ideological debate. *See, e.g.,* *United States v. Lopez*, 514 U.S. 549 (1995) (holding that a statute exceeded Congress's authority under the Commerce Clause).

384. More accurately, § 7491 could have been so seen if it really had altered allocation of the burden in actual cases.

385. For burden reversals as to fraud issues, see I.R.C. §§ 7422(e), 7427 & 7454(a)-(b). Also, I.R.C. § 6902(a) is germane since transferee liability is the tax equivalent of fraudulent conveyance. *See, e.g.,* *Commissioner v. Stern*, 357 U.S. 39, 42-46 (1958).

386. For burden reversals as to such issues, see I.R.C. §§ 162(c)(1)-(2) § 280G(b)(2)(B).

387. For burden reversals as to such issues, see I.R.C. § 7429(g)(1) (discussing jeopardy and termination assessments). *See supra* notes 344-47 and accompanying text (discussing statute of limitations exceptions).

D. PROBABILITY

Another traditional factor in allocating the burden of proof is probability—the party asserting the more unlikely or improbable scenario is more likely to have the burden imposed upon her.³⁸⁸ Viewed categorically (without reference to the particulars of any given controversy), whose contention is less likely to be correct: the IRS's contention that the taxpayer has greater tax liability than reported or the taxpayer's contention that she does not?

We want to believe that taxpayers usually are honest and that the positions they take on their tax returns usually are correct. This desire comports with fact. As far as can be ascertained, the voluntary compliance rate for American taxpayers is high (though dropping).³⁸⁹ From the numbers, one might conclude that the probability factor cuts in taxpayers' favor. But go deeper. Litigated tax controversies do not involve items selected randomly from the universe of tax returns. They involve only items the IRS believes erroneous, and a formidable array of checks are built into the system to cull spurious IRS adjustments before trial. Specifically, most returns are selected for audit by the IRS based on their reporting items significantly divergent from the statistical norm for items of that kind claimed by comparable taxpayers.³⁹⁰ If the taxpayer disagrees with the conclusions of the revenue agent, she may take the matter to the agent's supervisor.³⁹¹ The taxpayer then has the opportunity for administrative review through the IRS Appeals Office, whose very purpose is to resolve cases short of trial.³⁹² If no settlement occurs, a statutory notice of deficiency will be issued, but, in many cases, only after further review by the attorneys in the IRS District Counsel Office.³⁹³ If the taxpayer files a Tax Court petition, the case often is referred back to the Appeals Office for another attempt at settlement.³⁹⁴ If Appeals fails, IRS Counsel often succeeds in settling the case short of

388. *E.g.*, JAMES ET AL., *supra* note 8, at 324.

389. *See, e.g.*, Cohen, *supra* note 276, at 117 (stating the voluntary compliance rate was over 90% in 1964-1968 and is about 80% today).

390. *See, e.g.*, Saltzman, *supra* note 88, at 8-9 to 8-10 (discussing the procedures by which the IRS selects returns for audit).

391. *Id.* at 8-51, 8-96.

392. Typically, 85% or more of the cases handled by the Appeals Office are disposed of by agreement with the taxpayer. *See, e.g.*, INTERNAL REVENUE SERVICE HIGHLIGHTS 1990, at 41 (reporting that 47,446 and 39,845 nondocketed cases were settled by Appeals by agreement in 1989 and 1990, respectively, versus 3,313 and 3,680 unagreed cases).

393. *See* I.R.M. 4469(3)-(9).

394. *See, e.g.*, INTERNAL REVENUE SERVICE HIGHLIGHTS 1990, at 41 (30,604 and 27,017 docketed cases settled by Appeals by agreement in 1989 and 1990, respectively, versus 5432 and 4586 unagreed cases).

trial.³⁹⁵

One may suspect that, if the IRS still thinks there is triable return inaccuracy after all these levels of review, it probably is right more often than not. The fact that the IRS wins many more litigated cases than it loses³⁹⁶ does nothing to diminish this suspicion. Thus, the pre-§ 7491 general allocation of the burden of proof accorded with the probability factor of burden-of-proof theory.

This factor also explains some of the exceptions to the former rule. For instance, I.R.C. § 83 governs taxation of property transferred in connection with the performance of services. The taxpayer's inclusion into income usually is measured by reference to the fair market value of the property.³⁹⁷ However, in the case of property subject to a non-lapse restriction permitting sale of the property only at a price determined under a formula, the statute puts the burden of proof on the IRS to prove that fair market value is different from the formula price.³⁹⁸ This exception reflected a probability judgment, Congress's determination that such a formula price is likely to describe accurately the property's fair market value.³⁹⁹

E. POSSESSION OF PROOF

Traditionally, the extent to which the opposing parties have access to information and evidence as to the transactions at issue in the case, has been an important factor in allocating the burden of proof.⁴⁰⁰ This makes sense in terms of efficiency: it is cheaper for the party already in possession

395. See, e.g., MARSHALL W. TAYLOR ET AL., *TAX COURT PRACTICE* 116-20 (7th ed. 1990) (discussing settling with IRS counsel).

396. Although statistics are not consistently reported, the available information is strongly to this effect. For instance, in the years between 1965 and 1986, the IRS won (partly or completely) between 63% and 78% of district court tax cases and between 83% and 96% of Tax Court cases. Deborah A. Geier, *The Tax Court, Article III, and the Proposal Advanced by the Federal Courts Study Committee: A Study in Applied Constitutional Theory*, 76 CORNELL L. REV. 985, 998 (1991) (summarizing information from various Annual Reports of the Commissioner of the IRS). More recent information reflects generally similar results. See, e.g., INTERNAL REVENUE SERVICE DATA BOOK 1996, at 31; INTERNAL REVENUE SERVICE 1993-94 DATA BOOK, at 67; INTERNAL REVENUE SERVICE HIGHLIGHTS 1990, at 43.

Of course, these figures do not control for the burden of proof. It is impossible to know how much these figures would be depressed under a different allocation of the burden. I suspect the IRS's win rate would remain well over 50%.

397. I.R.C. § 83(a)(1) (1998).

398. I.R.C. § 83(d)(1) (1998).

399. See H.R. REP. NO. 91-413, 91st Cong., 1st Sess., 2 U.S.C.A.N. 1645, 1735-36 (1969).

400. See, e.g., Wigmore, *supra* note 3, at 290 (giving examples of statutes and cases applying this principle and putting the burden of proof on the party with peculiar means of knowledge).

of the evidence to produce it than to compel the other party to get it from him or to replicate it from other sources.⁴⁰¹ Decisional accuracy cuts in the same direction. A decision is only as good as the information on which it rests.⁴⁰² Thus, the burden of proof should be allocated so as to encourage the party in possession of, or with better access to, the relevant information to bring it to the attention of the tribunal.

Typically, the taxpayer, but not the IRS, was a party to the transactions at issue in the case. The taxpayer, but not the IRS, can testify from first-hand knowledge and has kept (or had the chance to keep) documentary or physical evidence of those transactions. This superior knowledge and this superior access to evidence strongly support allocating the burden of proof in civil tax cases to the taxpayer,⁴⁰³ as the former rule generally did.

However, in rare cases, the informational advantage is with the IRS. For example, the Tax Court has the authority to enjoin IRS collection activities in certain circumstances.⁴⁰⁴ The Tax Court has put the main burden of persuasion on the IRS in such cases, reflecting its perception that the IRS is in the better position to explain the nature of, and justification for, its collection activities.⁴⁰⁵ Thus, this traditional factor explains some exceptions to the former rule as well as the former general rule.

In summary of the foregoing, the pre-§ 7491 rule comported well with the factors traditionally governing allocation of the burden of proof.

401. So, as Bentham observed, the burden of proof should be imposed "on whom it will sit the lightest." *THE WORKS OF JEREMY BENTHAM* 139 (John Bowring ed. 1962).

402. As Francis Bacon told us four centuries ago: "knowledge itself is power." *Religious Meditations*, in 7 *THE WORKS OF FRANCIS BACON* 253 (J. Spedding, R. Ellis & D. Heath eds., 1st ed. London 1870) (1597).

403. For greater detail of this idea, see *supra* Part III.B.1.

404. See, e.g., I.R.C. §§ 6213(a), 6863(b) (1998) (describing procedures for filing petitions with Tax Court and listing conditions in case of income, estate, or gift taxes for the stay of collection of jeopardy assessments).

405. See *supra* text accompanying notes 339-43 (describing circumstances in which the IRS has the burden of proving its collection activities were appropriate).