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Discovery in Summary Assessment Proceedings

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When the collection of tax could be imperiled by going through the usual deficiency procedures, the IRS may make a jeopardy assessment or a termination assessment (hereinafter sometimes called "summary assessment") and proceed immediately to collection.[1] To prevent the misuse of this power, section 7429 provides affected taxpayers expedited administrative and judicial review. The IRS has made tens of thousands of jeopardy and termination assessments over the years, and there are hundreds of court decisions in litigated section 7429 cases.

The unique nature of jeopardy and termination assessments makes section 7429 proceedings very different from typical tax litigation. This article addresses a significant difference — the extent to which taxpayers may be allowed discovery of the basis of the IRS's summary assessment. Part I sets the context by describing jeopardy and termination assessments and section 7429 review. Part II examines a number of judicial decisions foundational to discovery incident to section 7429. Part III considers special factors that likely will incline a court to expand or contract discovery available to taxpayers in such cases. The conclusion that will emerge from these parts is that only limited discovery typically is permitted in section 7429 cases, although special factors may alter the permitted extent of discovery. This pattern deviates from the generally more liberal discovery usually available in federal district courts. Part IV asks whether such deviation is consistent with rules of civil procedure and concludes that it is.

I. Context

Summary assessment "is a singular weapon in the Service's armamentarium."[2] Typically, when the IRS believes income tax has been underpaid, it must seek to establish the underpayment through the deficiency procedures, involving the issuance of a statutory deficiency notice followed by the opportunity for Tax Court review.[3] The IRS cannot assess the additional tax until the deficiency procedures have run their course, and it cannot engage in enforced collection activities until after assessment. This creates an obvious concern, however. The deficiency procedure may take years. If the taxpayer conceals or dissipates her assets during this time, the assessment — when it finally comes — would be an empty measure in revenue terms.

Consequently, due to fiscal necessity, our tax system has had expedited means of assessment as long as it has permitted prepayment challenges to the IRS's determinations.[4] At present, the principal avenues of expedited assessments are sections 6851, providing for termination assessments, and 6861, providing for jeopardy assessments. These mechanisms are triggered similarly but have different effects.

Both types of summary assessments are activated when collection of tax may be imperiled by delay. The regulations identify three risk situations. They are:

- the taxpayer is or appears to be planning to leave the United States quickly or to conceal himself or herself;
- the taxpayer is or appears to be planning to place his or her property beyond the effective reach of the IRS by removing it from the country, or concealing, dissipating, or transferring it; and
- the taxpayer's financial solvency is or appears to be in peril (not taking into account the tax liabilities being considered).[5]

There is disagreement among the courts as to whether these indicia are exclusive grounds for summary assessment. Additional factors, however, are often taken into consideration, either as independent triggers or as items bearing on the existence of the three main triggers.[6]

The difference between termination and jeopardy assessments lies in the tax years affected. Termination assessments are made when there exists a revenue peril as to liabilities for a tax year not yet concluded or for which the return is not yet due. When a termination assessment is made, it ends the tax year immediately. Conversely, jeopardy assessments are made when there exists a revenue peril involving a prior tax year, one that is already concluded and for which the return already was filed or the return filing date has passed.

After either type of summary assessment is made, the IRS immediately gives notice and demands payment from the taxpayer. In the event of nonpayment, the IRS engages in enforced collection, including filing notice of lien and levying on the taxpayer's property.[7] The summary assessment does not eliminate the IRS's obligation to issue a deficiency notice nor does it cut off the taxpayer's right to challenge the notice in the Tax Court. However, any Tax Court review will be

[1]The taxpayer against whom the summary assessment is made must be given an opportunity — however brief — to pay. *E.g., Mettenbrink v. United States*, 71 AFTR2d Par. 93-3642 (D. Neb. 1991), *91 TNT 103-28*. If payment is not made, the IRS may seize the taxpayer's property, but may sell the property only under statutorily prescribed conditions. *See* sections 6331(a), 6863(b), and (c); *LaRosa v. United States*, 841 F.2d 544, 545 (4th Cir. 1988), *98 TNT 138-72*.

[2]*Revis v. United States*, 558 F. Supp. 1071, 1073 (D.R.I. 1983).

[3]*See generally* sections 6211-6215.

[4]For the historical evolution of summary assessments, see William D. Elliot, *Federal Tax Collections, Liens, and Levies*, section 3.02 (2d ed. 1995).

[5]Reg. sections 1.6851-1(a)(1), 301.6861-1(a).

[6]*See, e.g., Bean v. United States*, 618 F. Supp. 652, 658 (N.D. Ga. 1985), *85 TNT 127-15*, (distilling many factors); *Prather v. United States*, 54 AFTR2d Par. 84-5909 (M.D. Pa. 1984).

[7]The normal collection due process hearing rules are relaxed in summary assessment situations. Section 6330(f).

post-assessment and perhaps post-collection. It will not be prepayment as normal.[8]

Although it is necessary to the integrity of the system that the IRS possesses summary assessment powers, the exercise of those powers can sometimes be problematic. Congress and the courts have long recognized that prepayment assessment and collection procedures can exact a high price from taxpayers.[9] Before 1976, the taxpayer's sole recourse — apart from normal refund litigation — was to seek an injunction under the extremely narrow *Williams Packing* exception to the Anti-Injunction Act.[10]

In 1976, however, in section 7429, Congress enacted a considerably better remedy. That statute provides for expedited post-assessment review. The main requirements of section 7429 are:

- Within five days of the summary assessment, the IRS is required to provide to the taxpayer a written statement outlining the information on which the assessment was founded and determined to be necessary;
- Within 30 days, the taxpayer may obtain an administrative review of the assessment through the IRS's Appeals Office;
- Within 90 days of the earlier (i) the date the IRS Appeals Office notifies the taxpayer of its determination or (ii) the 16th day after the taxpayer made the request for administrative review, the taxpayer may bring an action in federal district court challenging the summary assessment. The Tax Court also has jurisdiction but only in cases in which the IRS summarily assesses after it has issued a deficiency notice for the tax year and the taxpayer has petitioned the Tax Court for a redetermination as to that notice;
- In the district court — or Tax Court — proceeding, the IRS bears the burden of proof as to whether the making of the assessment was reasonable. If the IRS meets that standard, the burden then is on the taxpayer as to whether the amount of the assessment was reasonable. The court determines these questions *de novo*, and it is required to render its decision within 20 days after the proceeding is started.[11] Under section 7429(f), the trial court's "determination" is final, conclusive, and nonappealable. Some circuits have read "determination" narrowly, however, thus allowing appeal of alleged procedural or constitutional errors although not of alleged errors as to the substantive merits.[12]

II. Foundational Cases

The information outlined makes clear that in section 7429 cases, the government must have an effective summary assessment power, but the exercise of the power can be heavily burdensome on the taxpayer.[13] In the discovery context, this has led courts to permit limited discovery, calibrated to permit effective taxpayer participation in the process but not to seriously inhibit revenue protection.

The foundation of this approach was laid in the review regime preceding section 7429: taxpayer suit for injunction under the *Williams Packing* rule. The key case was *Commissioner v. Shapiro*.[14] Samuel Shapiro, an Israeli citizen, had engaged in substantial transactions in the United States and had substantial assets here. A final order for his extradition to Israel, to face trial on criminal fraud charges, had been issued, as a result of which he was scheduled to leave the United States on December 9, 1973. Three days before that, the IRS made jeopardy assessments exceeding $92,000 against him for the tax years 1970 and 1971. The IRS believed Shapiro had failed to report income from drug trafficking in those years and that his imminent departure along with his assets in New York — consisting of items in his bank accounts and safe-deposit boxes — jeopardized the collection of tax on that income. The IRS also served levy notices on the banks.

In response, Shapiro filed suit to enjoin the jeopardy assessments and levies. The case eventually reached the Supreme Court, where the issue turned on section 7421(a), the Anti-Injunction Act. It provides, with enumerated statutory exceptions, that no suit to restrain tax assessment or collection may be brought. None of the exceptions applied, so Shapiro relied on the narrow judicial exception to the act established by the *Williams Packing* case. To come within that exception, Shapiro had to show both that (i) without an injunction, he would have no adequate remedy at law and (ii) even under the view of the facts and the law most favorable to the IRS, it could not prevail on the merits of the case.

Arguably, the first requirement was met by Shapiro's need for his bank funds as bail money in Israel. It is the second requirement that interests us now. Shapiro argued, and the Court agreed, that

> unless the Government has some obligation to disclose the factual basis for its assessments, either in response to a discovery request or on direct order of the court, the [*Williams Packing*]

[8] Sections 6851(b), 6861(b), and (c).

[9] *E.g.*, *Vernon v. United States*, 586 F. Supp. 115, 116 (W.D. Pa. 1984), H.R. Rep. No. 94-658, at 302, reprinted in 1976 *U.S. Code Cong. & Ad. News* 2897, 3198.

[10] *See generally Commissioner v. Shapiro*, 424 U.S. 614 (1976); *Enochs v. Williams Packing Co.*, 370 U.S. 1 (1962).

[11] The 20-day period may be extended for not more than 40 additional days if the taxpayer so requests and reasonable grounds exist. Section 7429(c). The government cannot request an extension. District courts often fail to meet the 20-day requirement. Courts typically hold that this failure does not invalidate the assessment, especially if the taxpayer has failed to apprise the court of the required expedition. *E.g.*, *United States v. Doyle*, 660 F.2d 277, 280 (7th Cir. 1981).

[12] *E.g.*, *Morgan v. United States*, 958 F.2d 950, 951-52 (9th Cir. 1992), *92 TNT 62-26*; *Schuster v. United States*, 765 F.2d 1047, 1049 (11th Cir. 1985), *85 TNT 144-37*.

[13] *See, e.g.*, *Meadows v. United States*, 665 F.2d 1009, 1011 (11th Cir. 1982).

[14] 424 U.S. 614 (1976).

> exception . . . is meaningless. The taxpayer can never know, unless the Government tells him, what the basis for the assessment is and thus can never show that the Government will be unable to prevail.[15]

Accordingly, the government was directed to come forward with proof sufficient to establish a factual foundation for its assessments. The government attempted to do so through deficiency notices in response to Shapiro's interrogatories and through a detailed affidavit by the revenue agent who handled the case. In concept, the Court held, this could be sufficient.

> The Government may defeat a claim by the taxpayer that its assessment has no basis in fact and therefore render applicable the Anti-Injunction Act without resort to oral testimony and cross-examination. Affidavits are sufficient so long as they disclose basic facts from which it appears that the Government may prevail.[16]

Several subsequent injunction cases applied the principles set forth in *Shapiro*.[17] Although the injunction remedy fell into disuse after enactment of section 7429 in 1976, the limited discovery approach of *Shapiro* continued to be influential, as we shall see.

Discovery is a balance between accommodation and opposition, varying in every case. The government is not uniform in the degree to which it opposes or accedes to taxpayer discovery requests. For example, in one case arising fairly shortly after enactment of section 7429, the parties engaged in some voluntary discovery after the taxpayer filed his complaint for jeopardy assessment review. The taxpayer deposed an IRS special agent who had developed the case, and the government answered the taxpayer's interrogatories and attached documents to its answers. The government, however, failed to respond to the taxpayer's request for production. Instead, it submitted the files compiled by the IRS agents for *in camera* inspection by the district court. On inspection, the court ordered the government to produce a memorandum by the IRS. In doing so, the court concluded the delay in the taxpayer's receipt of the memorandum was not severely prejudicial and the government's failure to produce the other documents was substantially justified.[18]

An interesting analogy, and justification for limited discovery, was offered in *United States v. Doyle*.[19] In that case, the court opined:

> A [section] 7429(b) proceeding is similar to a preliminary examination for probable cause in a criminal proceeding. While such an examination addresses the same basic issue as will be addressed at trial, and although the defendant is faced with a lesser standard of proof and limited discovery, the preliminary examination serves as a means of screening those cases which are obviously without merit and freeing those persons who have been charged without probable cause. Similarly, a [section] 7429 proceeding is designed to provide relief from those assessments which are clearly unreasonable.[20]

Some other courts have cited *Doyle* for this analogy,[21] but it has not been a major influence in shaping section 7429 discovery.

Perhaps the most instructive section 7429 discovery case is *Hohman v. United States*.[22] The taxpayers moved for leave to take depositions, contending this move was necessary to permit them to prepare for the hearing. Opposing the motion, the government noted that section 7429 requires a judicial determination within 20 days but does not shorten the normal time for discovery. This, the government contended, gave rise to an inference that Congress did not contemplate discovery in section 7429 cases. The government also maintained that the taxpayer had other available remedies, including the right to challenge the deficiency notice in the Tax Court.

The court rejected the government's contention. While agreeing "section 7429 contemplates a summary procedure," the court noted the statute's "purpose is to grant immediate relief in those cases where the IRS may have overstepped the bounds of reasonableness."[23] Thus, the section 7429 hearing

> is not pro forma; it is designed to afford the taxpayer an opportunity to initiate a meaningful challenge to the assessment. This contemplates that the taxpayer will be fully informed of the underlying reasons for the making of the assessment; that is, why a jeopardy assessment instead of a regular assessment, and the reasonableness of the amount of the assessment.[24]

On the other hand, the taxpayer will not be allowed open-ended discovery. The taxpayer's need for information must be balanced against the IRS's interests. Discovery is conditional, not absolute, and supervised, not unrestricted. The taxpayer

> is entitled to limited discovery if he demonstrates that he requires discovery in order to participate meaningfully in the hearing. . . . The fact that the proceedings are summary and a determination expedited requires the Court to exercise firm control over discovery and to allow only such discovery as may be necessary for the narrow question before the Court.[25]

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[15] *Id.* at 626-27. This is a variation of the idea that it is difficult to prove a negative. For further discussion of this idea, see Steve R. Johnson, "The Dangers of Symbolic Legislation: Perceptions and Realities of the New Burden-of-Proof Rules," 84 *Iowa L. Rev.* 413, 491 (1999).

[16] 424 U.S. at 633.

[17] *E.g., Schildcrout v. McKeever*, 580 F.2d 994 (9th Cir. 1978); *James v. United States*, 542 F.2d 16 (6th Cir. 1976).

[18] *Bremson v. United States*, 459 F. Supp. 121, 124 (W.D. Mo. 1978).

[19] 482 F. Supp. 1227 (E.D. Wis. 1980).

[20] *Id.* at 1229.

[21] *E.g., Hirschhorn v. United States*, 662 F. Supp. 887, 890 (S.D. N.Y. 1987).

[22] 535 F. Supp. 1218 (D. D.C. 1982).

[23] *Id.* at 1220.

[24] *Id.*

[25] *Id.* at 1221.

In particular, the *Hohman* court struck a balance between the needs of the taxpayer and those of the government. Specifically, the IRS was required to designate an agent to answer the taxpayer's questions as to how the amount of the assessment was computed. It was also required to provide copies — in the form of microfilm accompanied by a compatible viewing machine — of the records seized from the taxpayer.

Of course, the particular type and extent of discovery ordered varies from case to case. But, in general, the limited discovery approach used by Shapiro under the injunction regime and by Hohman under the section 7429 regime is now common in judicial review of summary assessments.[26]

III. Special Factors

We have observed that the precise contours of permitted discovery vary, depending on the situation. As noted previously, the central dynamic in section 7429 proceedings is the clash between the taxpayer's need to participate effectively in the hearing through access to information and the government's need to protect the revenue in circumstances of peril. So, any factor diminishing the former or underscoring the latter will incline the court to restrict discovery by the taxpayer. The reverse will incline the court to broaden allowable discovery. There can be multiple factors, of course. By way of illustration, we examine below five elements that have appeared in a number of cases.

A. Sufficiency of the IRS's Statement

Under section 7429(a)(1)(B), the IRS is required, within five days after making the summary assessment, to "provide the taxpayer with a written statement of the information upon which [it] relied in making such assessment." This statement "serves primarily to alert the taxpayer to any basis for contesting the assessment."[27]

To fulfill this purpose, the written statement should be detailed and comprehensive, and it should recite specific facts, and not general conclusions. Sometimes, though, as a result of inattention, time pressure, or inadequate internal communications, this goal is not achieved. At the worst — and, regrettably, this happens often — the written statement is purely conclusory, providing no information helpful to the taxpayer's preparation for the section 7429 hearing.

What should be the remedy for such dereliction? Taxpayers often have contended that inadequacy of the written statement requires invalidation of the summary assessment. The courts, however, have almost uniformly rejected this contention.[28] Taking a purpose-based approach, the courts have held, as long as the taxpayer is made aware of the factual underpinning of the assessment in a reasonable and timely fashion, the taxpayer is not prejudiced and the inadequacy of the written statement is inconsequential. Discovery, of course, is one such fashion. Thus, the extent of discovery a court grants in a section 7429 proceeding depends in part on the quality of the written statement. Thus, the less detailed and informative the statement, the more discovery the court likely will permit.

An example is *Fidelity Equipment Leasing Corp. v. United States*.[29] The operative portion of the written statement was as follows:

> Under section 6861 of the Internal Revenue Code, you are notified that I [the District Director] have found you to be designing quickly to place your property beyond the reach of the Government either by removing it from the United States, by concealing it, by transferring it to other persons, or by dissipating it, thereby tending to prejudice or render ineffectual collection of income tax for the taxable years ended as shown below.[30]

The above statement does not provide any facts. Beyond revealing which of the three predicate conditions in the regulations the IRS thought applicable to the situation, this statement has not provided any significant information apart from the fact that the jeopardy assessment had been made. Thus, the court correctly concluded that the written statement provided in the case failed to satisfy section 7429(a)(1)(B).

What was the remedy in this case? Instead of invalidating the jeopardy assessment as requested by the taxpayer, the court granted the taxpayer "full use of the discovery process." The court said, "Through the process of discovery the taxpayers have been informed of the information relied upon by the Government. Any deficiency in the notice issued by the Government is now immaterial."[31] Thus, a special factor influencing section 7429 discovery is the quality of the written statement. Many cases have confronted this issue, and typically they have taken the same approach as Fidelity *Equipment Leasing*.[32]

B. Responsiveness to Informal Prior Requests

This factor extends the first factor to a later point in the process. If the written statement is insufficient, the gaps may be filled by information later exchanged on a voluntary basis between the IRS and the taxpayer. The parties' behavior during this subsequent period will influence the extent to which the court will grant formal discovery.

For example, in one case, the IRS's written statement was terse. It consisted of a single paragraph, with little detail. After receiving the statement the taxpayer made "numerous" attempts to obtain additional information

[26] *See, e.g., Lindholm v. United States*, 808 F. Supp. 1 (D.D.C. 1992), *92 TNT 222-22* (relying on both *Shapiro* and *Hohman* in granting limited discovery to taxpayer in section 7429 case).

[27] *Loretto v. United States*, 440 F. Supp. 1168, 1175 (E.D. Pa. 1977).

[28] *But see Walker v. United States*, 650 F. Supp. 877, 855 (E.D. Tenn. 1987), *87 TNT 73-15* (invalidating jeopardy assessments because of inadequate written statement).

[29] 462 F. Supp. 845 (N.D. Ga. 1978), *vacated in part and new order entered* 47 AFTR2d Par. 81-1117 (N.D. Ga. 1981).

[30] 462 F. Supp. at 848.

[31] *Id.*

[32] *E.g., Evans v. United States*, 672 F. Supp. 1118, 1124-25 (S.D. Ind. 1987), *87 TNT 235-26; Hohman v. United States*, 535 F. Supp. 1218, 1222 (D. D.C. 1982) ("The more complete the factual statement, the less likely there will be a need for discovery."); *De Lauri v. United States*, 492 F. Supp. 442, 444 (W.D. Tex. 1980).

from the IRS. These included informal requests and a Freedom of Information Act filing, which turned into a suit under the same act. These efforts met with little success. As a result, the court granted the taxpayer expedited, limited discovery before the section 7429 hearing.[33] Presumably, this factor could also cut the other way as well. That is, a failure by the taxpayer to informally request information from the IRS would undercut any attempt by him to secure formal discovery.[34]

C. Reliability of the Government's Computation

If the government establishes that a condition of jeopardy exists, the remaining issue is the amount of the assessment. Under section 7429(g)(2), the taxpayer bears the burden of proof on this issue.[35] Because the available information may be fragmentary, the IRS may have to act quickly. As a result, the amount summarily assessed by the IRS is all too often a general estimate based on scarce information.

Clearly, that is undesirable. Sometimes, courts have reduced the amount of the assessment when, by the time of the hearing, better information had been developed.[36] Indeed, in extreme cases, assessment and collection sometimes have been restrained as a result of the looseness of the IRS's estimate. For example, in a pre-section 7429 injunction case, the Second Circuit granted an injunction against a $280,000 jeopardy assessment against an illegal bookmaker when the IRS used a three-day average of wagers received, to make an extrapolation of income over five tax years.[37]

For several reasons, though, courts typically do not restrain or invalidate jeopardy assessments based on possibly excessive amounts. First, the taxpayer usually is to blame for the imprecision, because of his or her failure to maintain, and provide to the IRS, accurate and complete records.[38] Second, if more information exists, the taxpayer usually is the party that possesses it, and should be encouraged to bring it forth. Third, the taxpayer will have the opportunity for full review of the merits in a later Tax Court or refund trial.[39] Fourth, if all the taxpayer does is to attack the IRS's computation without adducing affirmative proof, that person has not shouldered the burden of proof under section 7429(g)(2).[40]

Consequently, instead of invalidating the summary assessment, some courts grant the taxpayer greater latitude in discovery to compensate for the Service's foundational looseness in computing liability. For example, in another illegal bookmaking case, the IRS agent had available one day's worth of betting slips, from which he extrapolated the taxpayer's income for a whole year. Yet, disagreeing with the Second Circuit case described above, the court did not hold the assessment unreasonable in amount. Instead, it granted the taxpayer's motion for expedited discovery, during the time of which collection on the jeopardy assessment was stayed.[41] Additional discovery tends to be granted when the facts — and therefore the IRS's computations — are complex.[42]

D. The IRS's Use of After-Acquired Information

The legislative history to section 7491 states that the court reviewing the summary assessment is not limited to the information available as of the date the assessment was made. The court's determination is independent of the IRS's, and the court may take into account all relevant information, whether initially relied on by the Service or not.[43] The courts have uniformly followed this approach.[44]

However, we need to consider a number of questions. First, what if the IRS seeks to use after-acquired evidence to sustain its summary assessment? Second, should that affect discovery available to the taxpayer?

A case raising these questions is *Lace v. United States*.[45] The IRS made termination assessments against two illegal-drug traffickers. Shortly before the start of the section 7429 hearing, the IRS made two changes to its computation of income tax liability. The changes were based on newly obtained information. The infor-

[33] *Lindholm v. United States*, 808 F. Supp. 1, 3 (D. D.C. 1992), *92 TNT 222-22*.

[34] *Cf. Branerton Corp. v. Commissioner*, 61 T.C. 691 (1974) (same as to discovery in Tax Court deficiency litigation).

[35] This is not altered by section 7491, the new burden of proof provision enacted in 1998. That section purports to shift the burden of proof to the IRS generally in civil tax cases, but it contains so many conditions and exceptions that the shift rarely will occur. As relevant here, section 7491 does not come into play "if any other provisions of [the code] provides for a specific burden of proof with respect to such issue." Section 7491(a)(3). That's precisely what section 7429(g) does.

[36] *E.g., Harper v. United States*, 769 F. Supp. 362, 367 (M.D. Fla. 1991); *Nichols v. United States*, 43 AFTR2d Par. 79-835 (E.D. Cal. 1978), *appeal dismissed* 633 F.2d 829 (9th Cir. 1980).

[37] *Pizzarello v. United States*, 408 F.2d 579 (2d Cir. 1969), *cert. denied* 396 U.S. 986 (1969).

[38] *E.g., Jones v. Commissioner*, 903 F.2d 1301, 1303 (10th Cir. 1990), *90 TNT 115-13; Adamson v. Commissioner*, 745 F.2d 541, 548 (9th Cir. 1984).

[39] A section 7429 hearing does not determine the taxpayer's ultimate tax liability. The section 7429 proceeding is substantively and procedurally unrelated to any subsequent trial on the merits, and the section 7429 determination has no binding or persuasive effect in the subsequent trial. *E.g., Pals v. United States*, 867 F.2d 1162, 1163 (8th Cir. 1989); S. Rep. No. 94-938, at 365, reprinted at 1976 *U.S. Code Cong. & Ad. News* 2897.

[40] *E.g., Robinson v. Boyle*, 46 AFTR2d Par. 80-5078 (E.D. Va. 1980).

[41] *Lucia v. United States*, 447 F.2d 912, 916-19 (9th Cir. 1971) (pre-section 7429 injunction case); *see also Lindholm v. United States*, 808 F. Supp. 1, 3 (D. D.C. 1992) (similar approach in section 7429 case).

[42] *See Hedrick v. United States*, 702 F. Supp. 280, 281 (N.D.Ga. 1988), *89 TNT 13-22* ("Generally, discovery is not permitted in proceedings under section 7429. . . . Limited discovery may be allowed in actions involving extremely complex factual situations and computations.").

[43] S. Rep. No. 94-938, at 364-65, reprinted in 1976 *U.S. Code Cong. & Ad. News* 3439, 3793-94.

[44] *E.g., Erath v. United States*, 43 AFTR2d Par. 79-1192 (S.D. Cal. 1979); *Nichols v. United States*, 43 AFTR2d Par. 79-835 (E.D. Cal. 1978).

[45] 45 AFTR2d Par. 80-367 (D. Vt. 1979).

mation was somewhat contradictory. One piece of information increased liability, while the other decreased it. Considered on a net basis, the computed liability decreased.

However, the taxpayers objected on the grounds of inadequate notice and argued that they had been thereby prejudiced. As a remedy, they sought additional discovery. In response, the government moved for a protective order against such discovery. Then, the court admitted the after-acquired evidence and granted the protective order.

However, "the extent of discovery [in a section 7429 case], and indeed whether any discovery is necessary at all, must be determined based upon the facts of each case."[46] Several facts were probably significant in *Lace*. First, there already had been a substantial exchange of information between the parties. The written statement provided facts, and not just conclusions. The government's answer to the complaint included various documents and sworn declarations. The taxpayers had been allowed to take several depositions. Second, the new information addressed the "amount" issue, not the "condition of jeopardy" issue, and, on balance it helped the taxpayers. Third, the court granted alternative relief. The government had sought to establish its case based only on affidavits from the IRS agents.[47] The court, however, required the IRS agents to give testimony in court. In the process, the court gave the taxpayers the opportunity to cross-examine the agents on all matters, including the new information.

So, *Lace* would not appear to close the door. A section 7429 case involving a different prior information exchange and new information could well result in the taxpayer being granted additional discovery in response to the IRS's use of newly acquired information. This is especially likely if the 20-day determination deadline does not impinge or if the taxpayer is prepared to extend that period in exchange for the opportunity for further discovery.

E. Effect on Criminal Tax Investigation

Discovery can be used in an abusive fashion, whether for delay or otherwise. Courts are sensitive to this possibility in section 7429 proceeding.[48] Particular concern exists in the criminal context. Most — though not all — summary assessments are made against taxpayers engaged in criminal activities. Thus, a special factor bearing on the availability and extent of section 7429 discovery is the likely effect on the government's criminal and tax investigations.

The concern manifests itself in two ways. The first involves the disclosure of sensitive information. Too liberal discovery in the section 7429 case could undercut law enforcement. The *Hohman* case, discussed previously, is an example. Although recognizing the availability of limited discovery generally, the court expressed conviction that Congress "did not contemplate wide reaching discovery which would go beyond the taxpayers' need to address the narrow issues raised in Section 7429 proceedings. In no event is the taxpayer entitled . . . to discovery of the Government's criminal investigation."[49] By way of illustration, the court suggested:

> In those rare cases where, for example, discovery would jeopardize an investigation or identify an informant, the submission at the hearing may be *in camera*. Under these circumstances IRS would not include the information in its [written statement] but should make its *in camera* submission once the Section 7429 action is filed, or at least no later than the taxpayer's initial request for discovery.[50]

The other concern involves the diversion of time. This is illustrated by *United States v. Morgan Guaranty Trust Co.*,[51] a summon enforcement case. Summons enforcement is analogous to jeopardy and termination assessment review since both are summary proceedings, preliminary to determination of tax liability, conducted under deferential — to the IRS — standards. Indeed, *Morgan Guaranty* has been cited in section 7429 cases.[52] The court in *Morgan Guaranty* observed:

> The specific discovery sought by the [taxpayers] illustrates the drastic impact on IRS's investigations that the granting of such requests would create. Taxpayers asked that the court "order the IRS agents involved in this investigation to appear for depositions . . . prior to the hearing, with all . . . documents relative to the issue of the purpose for the issuance of the summons and the nature of the investigation of the taxpayers." . . . . Such discovery would seriously delay not only criminal but civil investigation. . . . [I]t is thus clear that the taxpayer must make a substantial preliminary showing before even limited discovery need be ordered.[53]

IV. Consistency With Rules of Procedure

The conclusion that emerges from the preceding parts is that taxpayers cannot expect substantial access to discovery in section 7429 cases. A showing of need must be made, and, even then, discovery typically will be limited, although special factors may expand — or contract — discovery possibilities.

But isn't this curious? Section 7429 cases generally are heard by the district courts, and we are accustomed

[46] *Hohman v. United States*, 535 F. Supp. 1218, 1222 (D. D.C. 1982).

[47] The affidavits would have been hearsay if used by the government, of course, but that would not have been a problem. Many cases have held that the usual rules of evidence do not apply in section 7429 hearings and that, in particular, hearsay is admissible in them. *E.g., Dickerson v. United States*, 65 AFTR2d Par. 90-963 (C.D. Cal. 1990); *Guerra v. United States*, 645 F. Supp. 775, 781 (C.D. Cal. 1986).

[48] *See, e.g., Melton v. United States*, 77 AFTR2d Par. 96-2108 (D.Colo. 1996), *96 TNT 93-17*.

[49] 535 F. Supp. at 1221.

[50] *Id.*

[51] 572 F.2d 36 (2d Cir. 1978).

[52] *E.g., Lace v. United States*, 45 AFTR2d Par. 80-367 (D. Vt. 1979).

[53] 572 F.2d at 42 n.9.

to think of district court practice under the modern Federal Rules of Civil Procedure as featuring broad, not narrow, discovery.[54] Against that backdrop, is the limited discovery approach characteristic of section 7429 hearings legitimate? Yes.

The Federal Rules of Civil Procedure do apply to summary tax proceedings in district court.[55] However, the discovery standards reflect "full recognition of the fact that the rigid application of the rules . . . may conflict with the summary determination desired. . . . [The rules are] drawn so as to permit application of any of the rules in the proceedings whenever the district court deems them helpful."[56]

The decision of a district court to limit discovery constitutes an exercise of discretion.[57] Given the remarkably short time frame to make decisions that Congress chose to impose and the importance of summary assessments to protection of the national fisc, the limited discovery approach crafted by the courts in section 7429 cases is a reasonable exercise of that discretion.[58]

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[54]Broad discovery remains the norm despite some retrenchment in recent years, including the December 2000 amendments to the Federal Rules of Civil Procedure. *See generally* Jeffrey W. Stempel, "Ulysses Tied to the Generic Whipping Post: The Continuing Odyssey of Discovery 'Reform,'" 64 *Law & Contemporary Problems* 197 (2001); Jeffrey W. Stempel & David F. Herr, "Applying Amended Rule 26(b)(1) in Litigation: The New Scope of Discovery," 199 *F.R.D.* 396 (2001).

[55]*See Bremson v. United States*, 459 F. Supp. 121 124 (W.D. Mo. 1978).

[56]*United States v. Morgan Guaranty Trust Co.*, 572 F.2d 36, 42-43 n.9 (2d Cir. 1978) (quoting 1946 Report of Advisory Committee on Rules of Civil Procedure, 3 Legislative History of Rules of Civil Procedure 161 (1947 Amendments)).

[57]*E.g., United States v. Wright Motor Co., Inc.*, 536 F.2d 1090, 1093-94 (5th Cir. 1976); *United States v. White*, 326 F. Supp. 459, 463 (S.D.Tex. 1971), *aff'd* 477 F.2d 757 (5th Cir. 1973), *adhered to per curiam on rehearing* 487 F.2d 1335 (5th Cir. 1973), *cert. denied* 419 U.S. 872 (1974).

[58]*Cf. Donaldson v. United States*, 400 U.S. 517, 528-29 (1971) ("the Civil Rules are not inflexible" and were "not intended to impair a summary enforcement proceeding" as long as the taxpayer's rights are protected); *United States v. Lask*, 703 F.2d 293, 300-01 (8th Cir. 1983), *cert. denied* 464 U.S. 829 (1983) (summons enforcement proceedings).

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