No. 17-10676

UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

JOHN FINNEGAN, ET AL.,

PETITIONERS-APPELLANTS,

v.

COMMISSIONER OF INTERNAL REVENUE,

RESPONDENT-APPELLEE.

On Appeal From
the United States Tax Court
(Tax Court Docket No. 8637-13)
Honorable Thomas B. Wells, United States Tax Court Judge

REPLY BRIEF FOR PETITIONERS-APPELLANTS

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CERTIFICATE OF INTERESTED PERSONS AND CORPORATE DISCLOSURE STATEMENT

In accordance with 11TH CIR. R. 28-3 and 11TH CIR. R. 26.1-2(b), it is hereby certified that in addition to the trial judges, attorneys, persons, associations of persons, firms, partnerships, or corporations identified in Petitioners-Appellants' Opening Brief as having an interest in the outcome of this appeal, the following additional person has acquired an interest in the outcome of this appeal:

1. Haungs, Esq., Michael J., Appellate Section, Tax Division, United States Department of Justice, Post Office Box 502, Washington, D.C., 20044.

In accordance with 11TH CIR. R. 28-3 and 11TH CIR. R. 26.1-1, as well as FED. R. APP. P. 26.1(a), it is hereby certified that a Corporate Disclosure Statement is still not required because Appellants are individuals and neither is a nongovernmental corporate entity.

Date: April 11, 2018

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POINT I

THE PROPER INTERPRETATION OF SECTION 6501(c)(1) CANNOT BE, AND WAS NOT, WAIVED

I. The Correct Application of the Law Is Nonwaivable

The Government urges this Court to not decide whether the fraud exception in section 6501(c)(1) applies only when a taxpayer personally intends to evade tax, because the Finnegans did not present that theory to the Tax Court.[1] (R's Br. 18-29).[2] The Government's waiver argument is based upon the flawed premise that a trial court can avoid the application of the correct law by a party's failure to specifically argue it. But, "[w]hen an issue or claim is properly before the court, the court is not limited to the particular legal theories advanced by the parties, but rather retains the independent power to identify and apply the proper construction of the governing law." *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 99 (1991). "Neither party can avoid the application of the correct law to the facts of the case by filing to plead or argue it. That is the province of the Court." *Concord Consumers Hous. Coop. v. Comm'r*, 89 T.C. 105, 126 (1987) (Korner, J.,

[1] Unless otherwise indicated, section references are to the Internal Revenue Code of 1986, as amended ("Code" or "I.R.C."). All capitalized terms have the meaning given in Petitioners-Appellants' Opening Brief.

[2] Citations to Petitioners-Appellants' Opening Brief, Respondent-Appellee's Brief, and Petitioners-Appellants' Appendix are in the form of "(P's Br. __)," ("R's Br. __)," and "(A__)," respectively, with appropriate page numbers inserted.

concurring).

The petition the Finnegans filed below alleged that "[t]he period within which the Commissioner may assess additional taxes or additions to tax expired pursuant to [section] 6501(a)." (A6 at ¶4). The Finnegans maintained that position at trial. (A140; "The tax years are 1994 through 2001. So under [section] 6501(a), that's beyond the three-year statute of limitations."). The Tax Court acknowledged the Finnegans' position in its opinion, stating the Finnegans "contend that the assessments are time-barred by the three-year period of limitations of section 6501(a)." (A242). Since the statute of limitations issue was properly before the Tax Court, it was the Tax Court's duty to apply the correct law to the facts.

Instead, the Tax Court erroneously relied upon *Allen v. Comm'r*, 128 T.C. 37 (2007), despite (a) the Federal Circuit's criticisms in *BASR P'ship v. United States*, 795 F.3d 1338, 1344-47 (Fed. Cir. 2015) ("*BASR II*"), *aff'g*, 113 Fed. Cl. 181 (2013) ("*BASR I*"), and (b) the Finnegans' request that *Allen* be overruled. (A272-A273; A288-A289). As explained in the Finnegans' Opening Brief (P's Br. 12-31) and *infra* at Point II, section 6501(c)(1) is most logically interpreted to mean that it is the taxpayer (not a third-party) who must intend to evade tax to suspend the three-year statute of limitations in section 6501(a). Reversal is appropriate because the Tax Court clearly erred in applying the law to the undisputed facts.

II. The Tax Court Ruled on the Continuing Validity of *Allen* and the Scope of Section 6501(c)(1)

The Government, relying on the faulty premise that applying the correct law can be avoided, asks this Court to sustain the Tax Court's erroneous statutory interpretation because the Tax Court allegedly did not decide whether the fraud exception in section 6501(c)(1) applies only when a taxpayer personally intends to evade tax. (R's Br. 25-26). However, the opinion below demonstrates that the Tax Court considered and ruled on the continuing validity of *Allen*. The Tax Court said:

> **We see no reason to revisit [*Allen v. Comm'r*], 128 T.C. 37 (2007), on account of *BASR P'ship v. United States*, 113 Fed. Cl. 181 (2013), *aff'd*, 795 F.3d 1338 (Fed. Cir. 2015).** In the Court of Appeals for the Federal Circuit's opinion, a persuasive dissent was filed, as well as a concurring opinion that relied on sec. 6229, a provision inapplicable in the instant case. Accordingly, even in cases appealable in the Federal Circuit, it is unclear whether, in the absence of sec. 6229, which interpretation of sec. 6501(c)(1) would prevail.

(A258, n.6) (emphasis supplied). The Tax Court may have stated it saw no reason to revisit *Allen*, but in doing so it revisited that opinion and endorsed its reasoning by evaluating *Allen* given the majority, concurring, and dissenting opinions in *BASR II*. The Tax Court's characterization of Judge Prost's dissent as "persuasive" enforces the point because deliberation was required for that conclusion. Because the Tax Court entrenched in its position that the phrase "with the intent to evade tax" in section 6501(c)(1) refers to the intent of any third-party connected to the

filing of the taxpayer's return, that issue is properly before this Court.

The Government next cites *Arkansas Pub. Emp. Ret. Sys. v. Harman Int'l Indus., Inc.* (*In re Harman Int'l Indus., Inc. Sec. Litig.*), 791 F. 3d 90 (D.C. Cir. 2015), to bolster its waiver argument. (R's Br. 25). This case supports the Finnegans' position, not the Government's. *In re Harman* explained that "on appeal, a party may refine and clarify its analysis in light of the district court's ruling, including citing additional support for his side of an issue *upon which the district court did rule*, much like citing a case for the first time on appeal." *In re Harman*, 791 F.3d at 100 (internal quotation marks and citations omitted) (emphasis supplied). As just explained, the Tax Court revisited *Allen* and decided it was correct notwithstanding the Federal Circuit's opinion in *BASR II*. Because the Tax Court ruled on the *Allen* issue, *In re Harman* supports that this Court may consider the Finnegans' position in this appeal.[3]

The Government also cites, out of context, the colloquy between the Finnegans' counsel and Judge Wells during which counsel stated the Finnegans do not contest *Allen*. (R's Br. 23-24). The Government fails to disclose, however, that counsel prefaced his remarks by stating the tax assessments are time-barred by

[3] Furthermore, *Harman* recognized that an appellate court "has discretion to consider issues raised for the first time on appeal … where there are exceptional or otherwise particular circumstances." *In re Harman*, 791 F.3d at 100-101. As explained *infra* at pages 7 through 13, the exceptional circumstance of this case warrant this Court reviewing the meaning of section 6501(c)(1).

the three-year statute of limitations in section 6501(a). The following dialogue occurred:

> THE COURT: There is no objection as to the statute of limitations in this case; is that correct?
>
> MR. SCHARF: Yes, there is.
>
> THE COURT: There is. And what's the basis of the objection?
>
> MR. SCHARF: The tax years are 1994 through 2001. So under [section] 6501(a), that's beyond the three-year statute of limitations….
>
> THE COURT: Has not the Court decided that issue as to the statute of limitation[s] if there's fraud on behalf of the preparer of the return?
>
> MR. SCHARF: Yes. We admit to the *Allen* case. Right. The Court has decided that. But we're not saying that --
>
> THE COURT: So, you're still objecting?
>
> MR. SCHARF: We're objecting -- we're not conceding that Howell's fraud for his dozens of other clients was also perpetrated in the case of the Finnegans.

(A140-A141). As explained, because the Finnegans preserved the issue that the three-year statute of limitations expired with respect to their 1994 through 2001 tax returns, the *Allen* issue is properly reviewable by this Court.

The Tax Court unfairly faulted the Finnegans for not addressing *BASR I* until their request for reconsideration. (A310-A312). The Tax Court overlooked the rule that trial courts' "decisions, unlike the decisions of States' highest courts

and federal courts of appeals, are not precedential in the technical sense: they have collateral estoppel, *res judicata*, and 'law of the case' effects, but create no rule of law binding on other courts." *ATSI Commc'ns, Inc. v. Shaar Fund, Ltd.*, 547 F.3d 109, 112 & n.4 (2d Cir. 2008) (footnotes omitted). Because *BASR I* was not binding precedent on the Tax Court, it is inconsequential whether the Finnegans cited that case below.

In contrast to *BASR I*, which the Tax Court was not bound to follow under *stare decisis* principles, the Tax Court had to decide the effect of *BASR II* on *Allen* and this case. "At every stage in the proceedings, the court must 'stop, look, and listen' to determine the impact of changes in the law on the case before it." *Naturalist Soc'y Inc. v. Fillyaw*, 958 F.2d 1515, 1520 (11th Cir. 1992) (quoting *Kremens v. Bartley*, 431 U.S. 119, 135 (1977)). *BASR II* is a decision of a Federal appellate court that affects the critical issue to be decided. And, the Tax Court obviously knew of *BASR II* because the Commissioner alerted the Tax Court to it when the Federal Circuit released its opinion. (A312).

More important, the Federal Circuit rejected the holding and reasoning in *Allen* as limited to the text of section 6501(c), unpersuasive, incomplete, uncomforting, and inconsistent with other provisions of the Code. *BASR II*, 795 F.3d at 1346-47. And, neither Judge O'Malley's concurring opinion nor Judge Prost's dissenting opinion in *BASR II* cited *Allen* or its reasoning favorably. *See*

generally BASR II, 795 F.3d at 1350-61 (O'Malley, J., concurring and Prost, J., dissenting). The Tax Court's failure to decide the effect of *BASR II* on *Allen* and this case does not prevent this Court from deciding whether the Tax Court applied the law correctly.

III. This Court Should Decide the *Allen* Issue and the Scope of Section 6501(c)(1)

Even if the Finnegans did not raise with specificity the theory that the fraud exception in section 6501(c)(1) is limited to situations in which a taxpayer personally intends to evade tax, this Court has broad discretion to still decide this issue. *Roofing & Sheet Metal Servs. v. La Quinta Motor Inns, Inc.*, 689 F.2d 982, 989 (11th Cir. 1982) (quoting *Singleton v. Wulff*, 428 U.S. 106, 121 (1976)). It is accepted that an appellate court generally will not consider a legal issue or theory not presented to the trial court. *Roofing*, 689 F.2d at 989 (quoting *Bliss v. Equitable Life Assurance Soc'y*, 620 F.2d 65, 70 (5th Cir. 1980)). However, this general rule is typically reserved for cases in which the issue to be decided requires the development of factual issues. *See Troxler v. Owens-Illinois, Inc.*, 717 F.2d 530, 533-534 (11th Cir. 1983); *Roofing*, 689 F.2d at 990. Here, the facts necessary for this Court to decide whether the Commissioner's tax assessments for 1994 through 2001 are time-barred by section 6501(a)(1) are undisputed. The general rule barring consideration of issues raised for the first time on appeal does not prevent this Court from deciding the issue.

In *Dean Witter Reynolds, Inc. v. Fernandez*, 741 F.2d 355, 360-361 (11th Cir. 1984), this Court articulated five important exceptions to the general rule that an appellate court will refuse to consider an issue not presented to the trial court and raised for the first time on appeal. Relevant here are that this Court may consider: (1) a pure question of law if the refusal to consider it would result in a miscarriage of justice, and (2) an issue first raised on appeal if the issue presents significant questions of general impact or of great public concern. *Dean Witter*, 741 F.2d at 360-361. These exceptions support this Court deciding whether section 6501(c)(1) is limited to situations in which a taxpayer personally intends to evade tax (sometimes, "*Allen* issue").

A. The *Allen* Issue Is a Pure Legal Question and Failing to Consider It Would Result in a Miscarriage of Justice

The issue presented – whether section 6501(c)(1) suspends the period of limitations on tax assessments in the case of a fraudulent return even though a third-party, and not the taxpayer, intends to evade tax – is a pure legal question. The Government does not dispute that the issue presented is purely legal. (R's Br. 27-29). The first prong of the first *Dean Witter* exception is met.

The miscarriage of justice element is also met. "A 'miscarriage of justice' is a 'decision or outcome of a legal proceeding that is prejudicial or inconsistent with the substantial rights of a party.'" *Wright v. Hanna*, 270 F.3d 1336, 1342 n.8 (11th Cir. 2001) (quoting *Black's Law Dictionary*, 999 (6th ed. 1990)) (alterations

omitted). A "substantial right" is "[a]n essential right that potentially affects the outcome of a lawsuit and is capable of legal enforcement and protection, as distinguished from a mere technical or procedural right." *Black's Law Dictionary*, 1324 (7th ed. 1999). An "essential" right is a right that is "basic or fundamental, especially belonging to or forming part of the minimum indispensable body, character, or structure of a thing." Webster's Third New International Dictionary, 777 (1986).

The right at issue is the period of limitations on tax assessments in section 6501(a). "Statutes of limitations are not simply technicalities. On the contrary, they have long been respected as fundamental to a well-ordered judicial system." *Bd. Of Regents of Univ. of N.Y. v. Tomanio*, 446 U.S. 478, 487 (1980); *see Artis v. Dist. of Columbia*, --- U.S. ---, 138 S. Ct. 594, 607-608 (2018); *Rothensies v. Elec. Battery Storage Co.*, 329 U.S. 296, 301 (1946). Statutes of limitations are rights capable of legal enforcement and protection, and they can affect the outcome of a lawsuit. *See, e.g.*, *Colony, Inc. v. Comm'r*, 357 U.S. 28, 38 (1958); *BASR II*, 795 F.3d at 1338-39; *Callaway v. Comm'r*, 231 F.3d 106, 134-35 (2d Cir. 2000) (each holding tax assessments are time-barred by the statute of limitations). Applying the foregoing principles to this case, a miscarriage of justice would result if this Court did not decide the *Allen* issue because the Tax Court's decision below contradicts the fundamental right to closure as reflected in the statute of limitations

provisions of section 6501(a) and taxpayers' "right to finality" in section 7803(a)(3)(F).

The Government glosses over the "substantial rights" element to respond that a miscarriage of justice would not result because the Finnegans would not be prejudiced. (R's Br. 28-29). This is incorrect. A "legal prejudice" occurs when a condition exists that, "if shown by a party, will usually defeat the opposing party's action." *Black's Law Dictionary*, 1198 (7th ed. 1999). If the fraudulent intent of a third-party does not trigger section 6501(c)(1), then the tax assessments are time-barred and the Finnegans prevail. The Finnegans are clearly prejudiced if the correct law is not applied. The first *Dean Witter* exception favors this Court deciding the *Allen* issue.

B. The *Allen* Issue Presents a Significant Legal Question of Broad Impact and Great Public Concern

1. The *Allen* Issue Impacts Victims of Abusive Return Preparers, Identity Thieves, and Unscrupulous Tax Advisors

The next relevant exception under *Dean Witter* is also met given the broad impact the *Allen* issue has on honest, law-abiding taxpayers. Following the Government's logic, *Allen* permits the Commissioner to recover taxes and penalties from victims of abusive return preparers, identity thieves, and unethical tax advisors who fraudulently misstate a taxpayer's tax liability. It is difficult to quantify how many taxpayers are affected by the *Allen* issue, but considering the

following statistics, the total eclipses 18 million taxpayers *per year*:

- During the Government's 2016 fiscal year, U.S. tax authorities initiated 252 criminal investigations against abusive return preparers who prepared an undisclosed number of fraudulent returns for an unknown number of taxpayers.[4]
- During the 2016 calendar year, it is estimated there were 15.4 million U.S. consumers who were victims of identity theft, many of whom were U.S. taxpayers.[5]
- During the Government's 2017 fiscal year, the Commissioner assessed 2,950,000 civil tax fraud penalties resulting in assessments of more than $177 million.[6]

The foregoing statistics belie the Government's claim that the *Allen* issue is not of general impact. (R's Br. 29). When these statistics are considered, it becomes apparent why this Court should not overturn 100 years of tax precedent to adopt

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[4] IRS, *Statistical Data – Abusive Returns Preparers*, https://www.irs.gov/compliance/criminal-investigation/statistical-data-abusive-return-preparers (last visited Apr. 7, 2018).

[5] Insurance Information Institute, *Facts + Statistics: Identity theft and cybercrime*, https://www.iii.org/fact-statistic/facts-statistics-identity-theft-and-cybercrime (last visited Apr. 7, 2018).

[6] IRS, *2017 Internal Revenue Service Data Book*, 42 (Mar. 2018), https://www.irs.gov/pub/irs-soi/17databk.pdf (last visited Apr. 7, 2018) (including civil tax fraud penalties for employment taxes as well as those for individual, corporate, estate, and trust income taxes).

the Government's strained reading of section 6501(c)(1).

2. The *Allen* Issue Disproportionately Affects Low-Income Taxpayers Who Will Not Seek Appellate Review

The public concern element is also met because of the disproportionate effect the *Allen* issue has on low-income taxpayers. Abusive return preparers prey on individuals of limited means. The *modus operandi* of these preparers is generally to file fraudulent returns and abscond with all or a portion of the refund otherwise payable to the taxpayer.[7] Taxpayers are victimized when the fraudulent return is filed and the refund is stolen. *Allen* permits these taxpayers to be victimized again, when the Commissioner issues a notice of deficiency to recover the refund (and related penalties and interest) after the three-year statute of limitations in section 6501(a) has expired.

The refund these low-income taxpayers receive is typically often attributable to a nonrefundable tax credit, like the earned income credit,[8] that the taxpayer never received because the preparer stole it. The money at stake, while significant to the victim, is usually not enough to warrant the cost of an appeal on other than a

[7] *See* IRS, *Examples of Abusive Return Preparer Investigations – Fiscal Year 2016*, https://www.irs.gov/compliance/criminal-investigation/examples-of-abusive-return-preparer-investigations-fiscal-year-2016 (last visited Apr. 7, 2018).

[8] The earned income credit is a governmental subsidy aimed at providing assistance to low-income taxpayers with earned income below a certain threshold amount (*i.e.*, the working poor). *Sutherland v. Comm'r*, 81 T.C.M. (CCH) 1001 (2001).

pro bono basis. Some have observed the Government reserves *Allen*-type arguments for individuals and *pro se* litigants who lack the knowledge or resources to challenge the issue.[9]

Although the *Allen* issue is widespread, the prospects for appellate review are not. The Claims Court hears refund suits. Affluent taxpayers can avail themselves of *BASR's* holdings by paying the tax and suing for a refund in the Claims Court. Thus, appellate courts will not be required to review the issue for taxpayers with means to pay the tax before litigating.

By contrast, the Tax Court is the only prepayment forum available to low-income taxpayers. Approximately 70% of all petitions filed in the Tax Court are filed by *pro se* litigants. Hon. Peter J. Panuthos, *The United States Tax Court and Calendar Call Programs*, 68 TAX L. 439, 440 (Spring 2015). Therefore, most low-income taxpayers will defend against the Commissioner's *Allen* arguments in the Tax Court without the benefit of counsel. Most *pro se* litigants will not recognize the tenuous legal grounds of *Allen* or endure the complexities and cost of an appeal. The public concern related to the *Allen* is overwhelming, and the limited opportunity for appellate review is another ground for this Court to decide the issue under *Dean Witter*.

[9] Jack Townsend, Posting of *Does the Preparer's Fraud Invoke the Unlimited Statute of Limitations* to Federal Tax Procedure blog, http://federaltaxcrimes.blogspot.com/2012/08/does-preparers-fraud-invoke-unlimited.html (Aug. 5, 2012).

IV. The Tax Court's Evidentiary Rulings Require This Court to Decide the *Allen* Issue

Finally, despite whether one or more of the *Dean Witter* exceptions apply, the Government's waiver argument separately fails because the *Allen* issue must be resolved to decide whether the Tax Court abused its discretion by overruling the Finnegans' objections to the testimony of Agent Ashcroft and Robins on relevance grounds. As explained in the Finnegans' Opening Brief (P's Br. 31-33), once *Allen* is rejected, evidence of Howell's habits are inadmissible because they are irrelevant or because the probative value of the testimony is substantially outweighed by issue confusion and prejudice.

POINT II

SECTION 6501(c)(1) REQUIRES "INTENT TO EVADE TAX" BY THE TAXPAYER

I. The Government's Interpretation of Section 6501(c)(1) Finds No Support Textually or Within the Statutory Framework

Section 6501(c)(1) provides that "[i]n the case of a false or fraudulent return with the intent to evade tax, the tax may be assessed ... at any time." The Government contends the statute is not confined to the intent of the taxpayer because "[t]he fraud exception focuses entirely on the fraudulent nature of *the return* – without regard to *who* intended the fraud." (R's Br. 30-31; emphasis in original). The Government's interpretation of section 6501(c)(1) fails because it finds no support textually or within the statutory framework of the Code.

The Government's reading of the statute renders the words "with the intent to evade tax" superfluous and violates the rule of statutory construction "to give effect, if possible, to every clause and word of a statute." *Inhabitants of Montclair Twp. v. Ramsdell*, 107 U.S. 147, 152 (1883). As explained in the Finnegans' Opening Brief (P's Br. 19-22), the phrase "with the intent to evade tax" was added to section 250(d) of the Revenue Act of 1918, Pub. L. No. 54-254, 40 Stat. 1057 ("1918 Act") (now codified in section 6501(c)(1)), to ensure that taxpayers who acted without the intent to defraud the Government were not subject to an unlimited period of assessment. Under the Government's reading of section 6501(c)(1), the statute might as well read "[i]n the case of a false or fraudulent return, the tax may be assessed … at any time." But that is not what the statute says, and the phrase "with the intent to evade tax" was a deliberate inclusion that must be given proper effect.[10]

The Government's interpretation of the statute also ignores that fraud requires specific intent to evade tax by the person liable for the tax. In *McGowan v. Comm'r*, 187 Fed. Appx. 915, 916 (11th Cir. 2006), this Court cited section

[10] The Government claims the juxtaposition of the fraud exception in section 250(b) and 250(d) of the 1918 Act show that if Congress intended for the fraud exception to be limited to the taxpayer, it would have stated so. (R's Br. 42-43). This claim is rebutted in the Finnegans' Opening Brief (P's Br. 19-22), as well as in Bryan T. Camp, *Tax Return Preparer Fraud and the Assessment Limitation Period*, Tax Notes, Aug. 31, 2007, https://ssrn.com/abstract=1008487, and Bryan T. Camp, *Presumptions and Tax Return Preparer Fraud*, Tax Notes, July 14, 2008, http://ssrn.com/abstract=1186582.

6501(c)(1) to explain that there "is no statute of limitations for deficiencies *if the taxpayer acted with the specific intent to evade taxes*." (Emphasis supplied). To say the statute "focuses entirely on the fraudulent nature of the return" contradicts *McGowan* and misses the point.

Documents do not have intent, much less specific intent to evade tax. Rather, "a fraud is only committed via submission of a document when a person acting with an intent to defraud makes a false entry on that document." *BASR II*, 795 F.3d at 1343; *accord McGowan v. Comm'r*, 187 Fed. Appx. at 916. Although section 6501(c)(1) does not specify whose fraud triggers the unlimited statute of limitations, as explained in the Finnegans' Opening Brief (P's Br. 13-14), courts have traditionally interpreted the statute to mean "fraudulent intent on the part of the taxpayer." There is nothing in the statute to suggest the statute of limitations is tolled absent the taxpayer's specific intent to evade a tax believed to be owed. And, outside of *Allen* and its progeny, there is absolutely no precedent to support the Government's radical interpretation of section 6501(c)(1).

The Government's reading of section 6501(c)(1) also causes the term "fraud" to be defined in a way that is inharmonious with other provisions of the Code. As explained in the Finnegans' Opening Brief (P's Br. 18-19; 22-27), Congressional intent that tax fraud is determined by reference to the taxpayer's intent is confirmed by sections 7454(a), 6663(a) and (c), and 6161(b)(3). If the

Government's reasoning is taken to its logical conclusion, then the civil tax fraud penalty may be imposed whenever someone (not necessarily the taxpayer) causes a fraudulent return to be filed. However, courts have repeatedly held that the civil tax fraud penalty requires "intentional wrongdoing *on the part of the taxpayer* with the specific intent to avoid a tax known to be owing." *Conforte v. Comm'r*, 692 F.2d 587, 592 (9th Cir. 1982); *see also Cole v. Comm'r*, 637 F.3d 767, 780 (7th Cir. 2011); *Marretta v. Comm'r*, 168 Fed. Appx. 528, 531 (3d Cir. 2006); *McGraw v. Comm'r*, 384 F.3d 965, 970 (8th Cir. 2004). The Government impliedly conceded the civil tax fraud penalty only applies if the taxpayer intends to evade tax by not asserting that penalty against the Finnegans.

Additionally, section 6501(a) defines the term "return" as "the return to be filed by the taxpayer (and does not include a return of any person from whom the taxpayer has received an item of income, gain, loss, deduction, or credit)." In *Badaracco v. Comm'r*, 464 U.S. 386, 397 (1984), the Supreme Court concluded that the word "return" as defined in section 6501(a) must be consistently applied throughout 6501. And, because section 6501(a) limits section 6501 to a return filed "by the taxpayer," the fraudulent intent referenced in section 6501(c)(1) must by implication be limited to fraud "by the taxpayer." *BASR I*, 113 Fed. Cl. at 192.[11]

[11] The Government urges this Court to review section 6501(c)(1) without

Equally troubling is the Government articulates no limiting principle for its interpretation. Is the unlimited assessment period triggered by the fraud of the return preparers who signs the return? How about individuals who prepare or help to prepare the return but who do not sign it? What about persons who advise regarding reporting positions on the return or who maintain the taxpayer's books and records? Does the fraud of an employee who embezzles monies from an employer-taxpayer trigger the unlimited assessment period? The Government's interpretation leads to ridiculous questions and even more ridiculous answers.

The plainest reading of the statute, and the most logical one, is the Finnegans' reading: "the intent to evade tax" in section 6501(1) refers to the taxpayer's intent and "the tax" in that section means the tax a taxpayer must report on an annual tax return and pay to the Government without assessment or notice and demand for payment under section 6151(a). And, for the reasons set forth in the Finnegans' Opening Brief (P's Br. 16-29), section 6501(c) should be narrowly interpreted in the context in which it stands today: as an exception to the general

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regard to other fraud-related provisions. (R's Br. 45-53). The words of a statute "must be read in their context and with a view to their place in the overall statutory scheme." *Roberts v. Sea-Land Servs., Inc.*, 566 U.S. 93, 101 (2012). Moreover, the determination of fraud for purposes of section 6501(c)(1) is the "same as the determination of fraud for purposes of the penalty under section 6663." *Neely v. Comm'r*, 116 T.C. 79, 85 (2001). Any interpretation of section 6501(c) must be harmonious with other fraud-related provisions of the Code. The Government's reliance on sections 6672 and 7201, (R's Br. 40-41), is irrelevant because those statutes concern "willfulness," not "fraud."

rule.

II. *Badaracco* Confirms the Finnegans' Position

Finding no support textually or within the framework of the Code, the Government next asks this Court to find that section 6501(c)(1) imposes no limitation on who must intend to evade tax for the unlimited period of assessment to apply. (R's Br. 32). The Government cites *Badaracco* for the proposition that statutes of limitations barring the collection of taxes must be strictly construed for the Government. (R's Br. 31). However, presumptions are of no force where, as here, the statute is unambiguous. *McNary v. Haitian Refugee Ctr., Inc.*, 498 U.S. 479, 502-503 (1991). Moreover, "[w]here no fraudulent conduct on the part of the taxpayer is alleged, 'taxing acts, including provisions of limitation embodied therein, are to be construed liberally in favor of the taxpayer.'" *Lauckner v. United States*, No. 93-1594, 1994 WL 837464 (D. N.J. 1993) (quoting *United States v. Updike*, 281 U.S. 489, 496 (1930)), *aff'd*, 68 F.3d 69 (3d Cir. 1995). The presumption in *Badaracco* only applies where "fraudulent conduct on the part of the taxpayer is alleged." And, since the Government does not allege the Finnegans acted with the intent to evade tax, section 6501(c)(1) must be liberally construed in their favor.

III. *Allen* and Its Progeny Contradict 100 Years of Tax Jurisprudence

The Government contends that courts consistently apply the fraud exception

by looking to the fraudulent nature of a return and not the source of the fraud. (R's Br. 35). As explained in the Finnegans' Opening Brief (P's Br. 13-14), this is simply untrue. The Government cites *Richardson v. Comm'r*, 509 F.3d 736 (6th Cir. 2007), and *Ballard v. Comm'r*, 740 F.2d 659 (8th Cir. 1984), to supports its claim. Those cases hold, *in the case of a jointly filed tax return*, section 6501(c)(1) tolls the statute of limitations on assessments against both spouses when they file a joint tax return and one spouse has defrauded the Government. These cases do not advance the Government's cause because their holdings are required by the rules that apply to jointly filed return, not because one person's fraud extends the statute of limitations for another individual.

To appreciate the distinction, it is important to know that section 6013(d)(3) makes spouses jointly and severally liable for each other's tax due regarding a jointly filed return. The *Richardson* and *Ballard* courts had to conclude that the fraud of one spouse tolls the statute of limitations for both spouses because to hold otherwise defeats the purpose of section 6013(d)(3) (*i.e.*, the non-fraudulent spouse may escape joint and several liability for the tax liability owed under 6013(d)(3)). The Tax Court explained this point in *Vannamam v. Comm'r*, 54 T.C. 1011, 1018 (1970): "*the bar of the statute of limitations still is removed* from the deficiencies determined against the wife, and she is liable for the additions to the tax *by virtue of the joint and several liability provisions of section 6013(d)(3)*." (Emphasis

supplied).

The Government superficially discusses *Allen* to embrace its holding, but never addresses the soundness of the underlying reasoning. (R's Br. 37-38). In addition to the reasons stated in the Finnegans' Opening Brief (P's Br. 14-15), *Allen* was wrongly decided because the Tax Court misapplied a plain meaning analysis by focusing on one phrase in section 6501(c)(1) ("false or fraudulent return") without considering the context in which the fraud exception was originally enacted.[12] The Tax Court compounded that error by refusing to consider the effect its definition of "fraud" has on other parts of the Code, including the civil tax fraud penalty under section 6663(a). Finally, the *Allen* court erred by relying on a failed proposal from Congress in 1934 as "legislative *history*" for an Act passed 16 years earlier. *Cent. Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 187 (1994) ("failed legislative proposals are 'a particularly dangerous ground on which to rest an interpretation of a statute.'") (quoting *Pension Benefit Guar. Corp. v. LTV Corp.*, 496 U.S. 633, 650 (1990)).

The Government next points this Court to *City Wide Transit, Inc. v. Comm'r*, 709 F.3d 102 (2d Cir. 2013), which did not endorse *Allen* in the manner the Government suggests. (R's Br. 37-38). In *City Wide*, the taxpayer "concede[d] that … City Wide's returns trigger the tolling provision if [the Court] finds that

[12] The *Allen* court examined the language of section 250(d) of the 1918 Act, but did so out of context because it did not consider section 250(b) of the 1918 Act.

[the return preparer] filed them with the intent to evade City Wide's taxes."). 709 F.3d at 107. In *City Wide*, the Second Circuit confronted only whether the person who prepared the returns acted with the intent to evade taxes. The Second Circuit explained:

> In front of the tax court, City Wide argued that it was not liable for the returns [the return preparer] prepared where "(1) [City Wide] did not know of the preparer's defalcations; [and] (2) [City Wide] did not sign or knowingly allow to be filed a false return…." The Commissioner anticipated these claims on appeal and rebutted them in its opening brief. City Wide, however, conceded these issues in its response brief. Moreover, each member of this panel asked City Wide whether it had intended this concession, and City Wide responded affirmatively to each of us in turn. Accordingly, we accept this concession without deciding whether certain factual situations might arise that sever the tax *payer's* liability from the tax-*preparer's* wrongdoing.

City Wide, 709 F.3d at 107 n.3 (emphasis in original and citations omitted). Despite the Government's contrary suggestion, *City Wide* does not actually address whether the return preparer's intent triggers the unlimited assessment period under section 6501(c)(1). *BASR II*, 795 F.3d at 1347. *Allen*, *BASR I*, and *BASR II* are the only cases deciding whether the fraud exception in section 6501(c)(1) applies only when a taxpayer personally intends to evade tax. And, for the reasons discussed in the Finnegans' Opening Brief, and throughout this Brief, this Court should align itself with the Federal Circuit.

IV. Public Policy Does Not Favor Tolling the Statute of Limitations

The Government argues that the purpose of section 6501(c)(1) is to protect

the public fisc against losing revenue caused by a fraudulent tax return. (R's Br. 32-35; 50-51). The Government's policy arguments are flawed for multiple reasons. First, "[p]olicy considerations cannot override [a court's] interpretation of the text and structure of [an] Act, except to the extent that they may help to show that adherence to the text and structure would lead to a result 'so bizarre' that Congress could not have intended it." *Cent. Bank of Denver*, 511 U.S. at 188 (quoting *Demarest v. Manspeaker*, 498 U.S. 184, 191 (1991)). As explained in the Finnegans' Opening Brief (P's Br. 12-31), the only permissible construction of section 6501(c)(1) is that it is the taxpayer (not some third-party) who must intend to evade tax to toll the three-year statute of limitations in section 6501(a). And, as explained throughout this Brief, policy does not favor the Government because the Commissioner's position leads to bizarre results Congress did not intend.

Second, the Government cites *Badaracco v. Comm'r*, 464 U.S. 386, 398, 400 (1984), to support the theory that section 6501(c)(1) provides the Commissioner unlimited time to assess tax because of the special disadvantage the IRS faces in detecting and investigating a fraudulent return. But, in *Badaracco*, the taxpayer intended to file a fraudulent return, so it was appropriate to construe the statute of limitations strictly for the Government. *Badaracco*, 464 U.S. at 386, 392. The Supreme Court explained: "it seems to us that a taxpayer who has filed a fraudulent return with intent to evade tax hardly is in a position to complain of the

fairness of a rule that facilitates the Commissioner's collection of tax due." *Id.* at 400. No similar policy justification exists where, as here, a taxpayer acts without fraudulent intent. Where no fraud by the taxpayer is alleged, "taxing acts, including provisions of limitation embodied therein, are to be construed liberally in favor of the taxpayer." *Updike*, 281 U.S. at 496; *see Lauckner*, 1994 WL 837464.

Third, Congress enacted specific civil and criminal tax penalties to sanction the conduct of non-taxpayers intending to evade a taxpayer's tax. These penalties include the paid preparer penalty under section 6694(a), failing to be diligent with respect to particular types of tax credits under section 6695(g), conspiracy charges under 18 U.S.C. § 286, aiding or assisting in the preparation or presentation of a false tax return under section 7206(2), and an action to enjoin the preparer from return preparation under section 7407. Because Congress provided the Commissioner with specific devices to recoup taxes from third parties who intentionally violate the law, the conclusion that section 6501(c)(1) facilitates the Commissioner's collection of taxes from third-parties is unfounded. *See BASR II*, 795 F.3d at 1350 n.8.

Fourth, equally strong policy arguments exist to narrowly construe section 6501(c)(1). In addition to the policy concerns discussed *supra* at pages 10 through 13, statutes of limitation are "an almost indispensable element of fairness as well as of practical administration of an income tax policy." *Rothensies v. Elec. Battery*

Storage Co., 329 U.S. 296, 301 (1946). If the fraud of a third-party extends the period of limitations on assessment indefinitely, taxpayers could rarely know with certainty that a tax return is final. Must taxpayers keep records indefinitely to stand ready to potentially defend a return? Must businesses create financial accounting reserves for deferred tax liabilities indefinitely? If the Government's reading of section 6501(c)(1) is endorsed, courts should stand ready to answer similar questions. Also, to construe section 6501(c)(1) as urged by the Government encourages taxpayers to *not* provide evidence against abusive return preparers because the taxpayer's reward is to be subject to an indefinite statute of limitations (and related taxes, penalties, and interest).

Finally, any difficulty the Government faces in collecting taxes allegedly due from the Finnegans is of its own making. The Commissioner first investigated Howell regarding his preparation of fraudulent tax returns during the 1980s and obtained a conviction in 1986. *See United States v. Howell*, 104 F.3d 356 (2d Cir. 1996), *cert. denied*, 484 U.S. 1065 (1988). The Commissioner investigated Howell again from 1999 until in or around 2004, (A255; Trial Transcript at p. 82, lines 9 through 11). Despite the criminal conviction and the second investigation, the Government never sought to enjoin Howell from acting as a return preparer under section 7407. (Whole record).

Despite closing its second investigation into Howell in 2004, and receiving

complete cooperation from the Finnegans throughout, it took the Government almost *nine years* to issue the Notice to the Finnegans. During this time, the Commissioner never solicited from the Finnegans a written agreement to extend the assessment period under section 6501(c)(4). (Whole record). Because of the Finnegans' cooperation, it is reasonable to conclude the Finnegans would have signed agreements extending the statutes of limitation had the Commissioner asked for them.

When the Government closed its second investigation into Howell in 2004, the six-year period of limitations on assessment under section 6501(e)(1) was arguably open for the 1997 through 2001 tax years. The liabilities allegedly due for 1997 through 2001 account for 65% of the total taxes, penalties, and interest purportedly due from the Finnegans for the 1994 through 2001 tax years. (A8). This Court should not reward the Government for sitting on its rights for nearly a decade and not pursuing civil tools available to it that could have prevented any alleged tax loss. *Accord BASR II*, 795 F.3d at 1350 n.8. For the reasons stated in the Finnegans' Opening Brief (P's Br. 30-31), this Court should reverse the Tax Court because the assessments with respect to the Finnegans' 1994 through 2001 tax returns are time-barred by section 6501(a).

POINT III

THE TAX COURT'S EVIDENTIARY RULINGS WERE AN ABUSE OF DISCRETION

I. The Testimony of Agent Ashcroft and Robins Was Irrelevant and Highly Prejudicial

The Tax Court concluded (A244), and the Government agrees (R's Br. 57-58), that the testimony of Agent Ashcroft and Robins regarding Howell's habit was admissible because this testimony makes it more or less probable that Howell prepared the Finnegans' tax returns with the intent to evade tax. This position ignores that section 6501(c)(1) requires "*the taxpayer* [to have] acted with the specific intent to evade taxes." *McGowan v. Comm'r*, 187 Fed. Appx. 915, 916 (11th Cir. 2006). Whether Howell prepared the Finnegans' returns with the intent to evade tax is irrelevant to the Finnegans' specific intent. Despite the Tax Court's conclusion, (A244), the Finnegans' intent is not a fact of consequence because the Government concedes the Finnegans did not act fraudulently. (*See* P's Br. 4-5). Thus, as explained in the Finnegans' Opening Brief (P's Br. 31-33) and herein, the Tax Court abused its discretion by admitting the irrelevant and highly prejudicial testimony of Agent Ashcroft and Robins.

II. Howell's Testimony in Mitts' Criminal Trial and Howell's Affidavit Are Inadmissible Hearsay Not Against Howell's Interest

The Tax Court concluded, (A246), and the Government maintains, (R's Br. 58-62), that Howell's testimony from Mitts' criminal trial and Howell's affidavit

against the Finnegans are admissible under FED. R. EVID. 804(b)(3) because Howell's statements allegedly exposed him to increased civil and criminal liability. As explained in the Finnegans' Opening Brief (P's Br. 33-36), this is untrue. As to the Government's claim of civil liability, Howell testified against Mitts on June 10, 2008, more than six years after the Finnegans' 2001 tax return was filed on April 15, 2002. (A60). The Government identifies no theory by which the Finnegans could recover civil damages from Howell more than six years after the fact, because no such theory exists. *Cf.* N.Y. C.P.L.R. § 214(6) (MCKINNEY 2016) (three-year statute of limitations on malpractice); N.Y. C.P.L.R. § 213(8) (MCKINNEY 2017) (six-year statute of limitations on fraud). Howell's lack of civil culpability supports that his statements were not against his proprietary or pecuniary interest.

As to the Government's claim of criminal culpability (R's Br. 59), Howell's testimony in the Mitts trial occurred on June 10, 2008, after he was indicted and pleaded guilty, (A62-A117), but before sentencing in June 2009, *United States v. Howell*, No. 06-cr-283 (S.D.N.Y. June 30, 2009) (order to surrender). A reasonable person in Howell's position might think implicating someone else (like his clients) would decrease his exposure to criminal liability as it relates to sentencing. Absent trustworthy corroborating circumstances, of which there are none, the Finnegans were deprived of a fair trial because of their inability to cross-

examine Howell about his statements. *See Williamson v. United States*, 512 U.S. 594, 600-605 (1994). For the reasons stated in the Finnegans' Opening Brief (P's Br. 34-36), the Tax Court abused its discretion by finding Howell's statements trustworthy and not against his proprietary or pecuniary interest. If this Court does not reverse the Tax Court because the tax assessments are time-barred, the Tax Court's evidentiary rulings must be reversed, its decision vacated, and this case remanded with instructions.

CONCLUSION

For the foregoing reasons, and those in the Finnegans' Opening Brief, the Tax Court's decision should be reversed or reversed, vacated, and remanded with instructions.

Date: April 11, 2018

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CERTIFICATE OF COMPLIANCE WITH
FED. R. APP. P. 32(g) AND 11TH CIR. R. 28-1(m)

It is hereby certified that:

1. This brief complies with the type-volume limitation of FED. R. APP. P. 32(a)(7)(B) because, excluding the parts of the brief exempted by FED. R. APP. P. 32(f) and 11TH CIR. R. 32-4, this brief contains 6,494 words; and

2. This brief complies with the typeface requirements of FED. R. APP. P. 32(a)(5) and the type style requirements of FED. R. APP. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using the Microsoft Word word processing program in 14 point font size and Times New Roman style.

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CERTIFICATE OF SERVICE

It is hereby certified that on April 11, 2018, I electronically filed the foregoing Reply Brief for Petitioners-Appellants with the Clerk of the Court for the United States Court of Appeals for the Eleventh Circuit using the CM/ECF system. Counsel for the Appellee is a registered CM/ECF user and will be served by the CM/ECF system.

It is further hereby certified that I will mail to the Clerk of the Court of the United States Court of Appeals for the Eleventh Circuit seven paper copies of the foregoing Reply Brief for Petitioners-Appellants.

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