No. 14-5037

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

BASR PARTNERSHIP and WILLIAM F. PETTINATI, SR., Tax Matters Partner
Plaintiffs – Appellees

v.

UNITED STATES,
Defendant – Appellant

ON APPEAL FROM THE JUDGMENT OF THE
UNITED STATES COURT OF FEDERAL CLAIMS
No. 10-244; Judge Susan G. Braden

BRIEF FOR BRYAN T. CAMP AS *AMICUS CURIAE* IN SUPPORT OF APPELLEES FOR AFFIRMANCE

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June 25, 2014

CERTIFICATE OF INTEREST

Counsel for the *amicus* Bryan T. Camp certifies the following

1. The full name of every party or *amicus* represented by me is: Bryan T. Camp.

2. The name of the real party in interest (if the party named in the caption is not the real party in interest) represented by me is: None.

3. All parent corporations and any publicly held companies that own 10 percent or more of the stock of the party or *amicus curiae* represented by me are: None.

4. The names of all law firms and the partners or associates that appeared for the *amicus* now represented by me in the trial court or agency or are expected to appear in this court are: None.

Date: June 25, 2014

Signature of counsel: ____/s/ Bryan T. Camp______________
Printed name of counsel: Bryan T. Camp

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STATEMENT OF *AMICUS* IDENTITY, INTEREST AND AUTHORITY

Pursuant to Rules 47.4 and 29(c)(4), *amicus* is the George H. Mahon Professor of Law at Texas Tech University School of Law. *Amicus* studies the theory and history of tax administration in general and the statutes involved in this case in particular. *Amicus* has no financial or personal interest in the case outcome. The aim of this brief is to educate the Court on the legal history of the statutes involved and to show how the historical and statutory contexts support affirmance. Pursuant to Rule 29(c)(5), *amicus* confirms that (a) no counsel to any party authored this brief in whole or in part; (b) no party or party's counsel contributed money intended to fund preparing or submitting the brief; and (c) no person other than *amicus* and his counsel contributed money intended to fund preparing or submitting this brief.

Pursuant to Rule 29(a) *amicus* states that all parties have consented to the filing of this brief.

STATEMENT OF THE ISSUE

This case is about the burden of proof. To obtain the benefit of §6501(c)(1), must the government prove that the taxpayer intended to evade tax, or need it prove only that a third party somehow involved with the taxpayer's return intended to evade tax? Since 1918, the IRS, taxpayers, courts and commentators have all agreed that the government must show, by clear and convincing evidence, that the taxpayer intended to evade tax. Typically, the government relied on indirect evidence, labeled "badges of fraud," to convince a fact-finder of the taxpayer's fraud. Recently, however, the government has started claiming that it need only prove that someone associated with the taxpayer intended to evade tax. In this case, for example, the government presented evidence to the trial court that the taxpayers' lawyer, Mayer, intended for the taxpayers, the Pettinatis, to evade tax. But it made no attempt to prove that the taxpayers intended to evade tax. It did not seek to use the taxpayer's association with Mayer as a badge of fraud. The government instead claims that Mayer's fraudulent intent "is all the fraud exception requires" it to prove (Gov.'s Br. 37). The correctness of that claim is the issue in this case.

STATEMENT OF THE CASE

Amicus generally relies on the government's statement of the case. *Amicus* notes, however, that the government's enthusiastic use of the words 'fraud' and 'fraudulently' tends to obscure the key fact to remember: the taxpayers did not intend to evade tax. For example, the government states that the taxpayers "hired Mayer to guide them through a variant of a fraudulent tax shelter popularly known as 'Son-of-BOSS.'" (Gov.'s Br. 2). That is not quite true. The government never attempted to prove that the taxpayers here knew or should have known that Son-of-BOSS was a "fraudulent tax shelter." A more accurate statement is that the taxpayers hired Mayer to guide them in minimizing taxes. The taxpayers may have been greedy, venal, or even negligent. But they did not commit fraud. If the government could have genuinely disputed that key fact, Judge Braden would not have granted Summary Judgment.

SUMMARY OF ARGUMENT

The Court of Federal Claims was correct to use the traditional interpretation of §6501(c)(1) as focusing exclusively on the taxpayer's intent: for there to be a fraudulent return the government must prove the taxpayer intended to evade tax, which the government made no attempt to do here.

The traditional interpretation is supported by the statute's plain language. The phrase "intent to evade" most plainly refers to the intent of the taxpayer whose liability is reported on the return. One evades one's obligations. It is a stretch to say that one evades another's obligations.

The traditional interpretation is also supported by the statute's history and relationship with other procedural statutes. First, what is now §6501 was enacted as a statute of repose, promoting a strong congressional policy of closure. Before 1918 the statutory scheme required the Commissioner to assess each taxpayer by each June. Once the assessment was made, the matter was closed; the courts held the Commissioner *functus officio* to correct errors in the absence of a statute granting a power to re-assess. Congress eventually supplied such power, but only for a limited time and only in cases of "a false or fraudulent return." False or fraudulent returns triggered the additional time to re-assess, regardless of whether the taxpayer intended to evade taxes. When Congress overhauled the assessment process in 1918, it created the current unlimited period of time to assess, adding for the first time the "with the intent to evade" language after the phrase "false or fraudulent return" in order to narrow the historically expansive exception. After 1918, courts continued to resolve ambiguities in the new assessment scheme in favor of closure, and Congress enacted additional statutes to favor closure. The government's position conflicts with this strong and consistent policy of closure.

Second, §6501(c)(1) should be read consistently with §6663, which imposes a 75 percent penalty on underpayments due to the taxpayer's fraud. Both sections originated in §250 of the Revenue Act of 1918. The Senate Finance Committee copied the phrase "with intent to evade" from the fraud penalty provision into the assessment provision in order to narrow the latter's scope of operation. Thus, the same conduct that triggered the fraud penalty would trigger the unlimited assessment period, and that conduct was that of the taxpayer, not third parties. Judge Braden's interpretation of §6501(c)(1) as imposing the same burden of proof on the government as does §6663 is correct.

Third, §6501(c)(1) should be read consistently with §7454, which requires the government to bear the burden of proof whenever the issue of "whether the petitioner has been guilty of fraud with intent to evade tax" arises in a Tax Court proceeding. Reading §6501(c)(1) as reaching beyond the intent of the taxpayer creates the anomalous result that taxpayers would bear the burden before the Tax Court to <u>disprove</u> the application of §6501(c)(1) whenever the governmental merely asserts fraud by a third party in its Notice of Deficiency. The history of §7454 shows that Congress did not intend that result but instead intended §7454 to apply when the government sought either the fraud penalty or the unlimited assessment period.

ARGUMENT

I. SECTION 6501(c)(1) HAS TRADITIONALLY BEEN READ AS REFERRING TO TAXPAYER INTENT, NOT THE INTENT OF THIRD PARTIES.

The traditional interpretation of §6501(c)(1) is that "[t]here must be additional evidence, independent of the general presumption of correctness, from which fraudulent intent <u>on the part of the taxpayer</u> can be properly inferred." *Payne v. Commissioner*, 224 F.3d 415, 420-21 (5th Cir. 2000) (emphasis changed). This traditional interpretation is long-standing. *See, e.g.*, *Drieborg v. Commissioner*, 225

F.2d 216, 218 (6th Cir. 1955) (same); *Botwinik Brothers of Mass., Inc. v. Commissioner*, 39 T.C. 988, 996 (1963)(corporate bookkeeper Vera Green's submission of fraudulent corporate returns did not toll the limitation period because "[i]t must be kept in mind at the outset that the fraud to be established is the fraud of petitioner corporation, not that of Vera Green"). Respected treatise-writers have similarly long believed that "[t]he issue is one of fact involving the taxpayer's intent." Michael I. Saltzman, *IRS Practice and Procedure* ¶5.03[1][a], at 5-10 (1981).

From 1918 until 2001, the IRS also agreed with this consensus. For example, Field Service Advice Memorandum 200104006, 2000 FSA LEXIS 207, 2001 WL 63261, discusses why the fraudulent intent of a tax return preparer cannot be used to trigger the §6501(c)(1) exception. Its analysis nicely refutes many of the government's current arguments. Since 2001, however, the government has sought to expand the reach of §6501(c)(1), with mixed success in the courts.

II. THE TRADITIONAL INTERPRETATION IS SUPPORTED BY THE PLAIN LANGUAGE OF SECTION 6501(c)(1).

Section 6501(c)(1) provides:

> In the case of a false or fraudulent return with the intent to evade tax, the tax may be assessed, or a proceeding in court for collection of such tax may be begun without assessment, at any time.

The government urges that "[t]he statute…focuses entirely on the fraudulent nature *of the return* without regard to *who* intended it." (Gov.'s Br. 38). That argument runs into two difficulties. First, it leaves no work to be done by the phrase "with intent to evade tax." The statute might as well read "in the case of a false or fraudulent return, the tax may be assessed…at any time." As explained further below, the Senate Finance Committee inserted the "with intent to evade" language in 1918 to ensure that taxpayers who were not seeking to avoid their taxes would not be subject to an unlimited assessment period.

Second, the very concept of fraud requires intent of a person. To say the statute "focuses entirely on the fraudulent nature *of the return*" is unhelpful because it begs the question of whose intent counts. Documents cannot have intent. So the question is: whose intent matters? The statute does not say. Any answer to that question requires inserting language that does not exist.

The government's interpretation that anyone's intent suffices enjoys no textual support. The government observes that "[n]othing in the plain meaning of the statute suggests the limitations period is extended only in the case of the taxpayer's fraud." (Gov.'s Br. 53 (quoting *Allen v. Commissioner*, 128 T.C. 37 (2007)). That observation, however, is unhelpful as a plain language analysis. One can just as easily say "nothing in the plain meaning of the statute suggests the limitations period is extended ABSENT the taxpayer's fraud." The statute is simply silent. While the statute's silence is a starting point for analysis---it leads to the necessity of examining the statute's history and purpose, taken up below---the government does not explain how it jumps from its initial observation to its preferred interpretation.

Worse, the government articulates no limiting principles for its preferred interpretation. Does the government want to read the statute as requiring "intent by the taxpayer or the taxpayer's attorney to evade"? Or perhaps the government would prefer the words "by the taxpayer or the taxpayer's attorney or the taxpayer's return preparer." Or perhaps the government would prefer the words "by the taxpayer or anyone reasonably associated with the taxpayer." The government's proposed interpretation is simply unbounded.

In contrast, textual analysis supports the traditional interpretation that limits the statute to the intent of the taxpayer. The terms "the tax" and "such tax" must refer to a specific tax, because each uses a definite article. The plainest reading of these terms is that they refer to "the" tax of "the" person submitting the return. After all, it makes little sense---that is, it is <u>far</u> from plain---to attribute to a person an intent to evade something which is not otherwise imposed on him or her. There is nothing to be evaded. The <u>plainest</u> reading of the statute is that "the intent" to evade relates to "the tax" required to be reported on the return which, but for the evasion, would be reported and paid by the person signing and submitting the return. Person A might well intend to <u>help</u> B evade B's tax liability, but while B's action is evasion, A's action of helping is not generally referred to as evasion, but is rather labeled conspiracy, or aiding and abetting, or some such phraseology.

III. THE TRADITIONAL INTERPRETATION IS SUPPORTED BY SECTION 6501(c)(1)'s HISTORY AND RELATIONSHIP WITH OTHER PROCEDURAL STATUTES.

A. Section 6501 was enacted as a statute of repose, and §6501(c)(1) should be interpreted consistently with that purpose.

The legal history of the language presently codified in §6501(a) and (c)(1) strongly supports interpreting ambiguities to favor closure of past tax years. *See e.g. Diamond Gardner Corp. v. Commissioner*, 38 T.C. 875 (1962)(reviewing history of §6501(a)). For a more thorough explanation of the following brief summary, *see* Bryan T. Camp, *Tax Return Preparer Fraud and the Assessment Limitation Period*, 116 Tax Notes 687 (August 20, 2007), available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1008487. This history shows that, if there is any doubt as to the reach of §6501(c)(1), such doubt should be resolved in favor of closure.

Congress first imposed an income tax in 1862 as a temporary measure to pay for the Civil War, and made major modifications to it over the next 10 years. Revenue Act of 1862, ch. 119, 12 Stat. 432; Revenue Act of 1864, ch. 173, 13 Stat. 223; Act of July 13, 1866, ch. 184, 14 Stat. 98 (1866); Act of July 20, 1868, ch. 186, 15 Stat. 124; Act of July 14, 1870, ch. 255, 16 Stat. 260. Congress did not renew it after it lapsed in 1872. *See generally* Edwin R. A. Seligman, *The Income Tax* 435-80 (2d ed. 1914)(describing operation of the early income tax acts). When Congress revived the income tax for individuals in 1913 it used the administrative provisions of the Civil War statutes (often using the same language), but then made significant changes to the assessment procedure in 1918. *See generally* Bryan T. Camp, *Theory and Practice in Tax Administration*, 29 Va. Tax Rev. 227 (2009).

The tax assessment procedure contemplated by the Revenue Act of 1862 was one where the government was expected to make a final determination of liability <u>before</u> making any assessment, and taxpayers had no obligation to pay until they received a bill for the assessed taxes. 12 Stat. 432. By May 1 of each year, taxpayers were required to "make a list or return to the assistant assessor…of the amount of annual income, the articles or objects charged with a special duty or tax [etc.]…according to the forms and regulations to be prescribed." *Id.* §6. Assistant Assessors were required to personally visit noncompliant taxpayers to obtain their return, *Id.* §7, and if the taxpayer did not cooperate, were empowered to make out the return "according to the best information which he can obtain." *Id.* §11. However created, these returns were then reviewed by the Assessors and posted for public viewing for 15 days to allow taxpayers to appeal either the amount or valuation of the items listed. Upon review, the Assessor could increase or decrease the valuations of anyone, but had to give any "party interested" at least five days notice to object to any proposed increase. *Id.* §15. By June, the Assessors were to draw up a final list of who owed what taxes and give it to the Collectors of the districts. *Id.* §16. The Collectors then notified taxpayers of this final assessment and the amount due, and had six months to administratively collect any unpaid balance. *Id.* §23.

This statutory scheme gave Assessors huge powers to examine and unilaterally modify the returns before the final assessment was made, during the period between the receipt of returns and the transmittal of the assessment list to the collectors. And they were expected to evaluate each return before making a final assessment. *See* Camp, *supra*, 29 Va. Tax Review at 229-34. After the final assessment, however, the statutes said nothing about what power Assessors had to re-assess. Courts held that Assessors had no such power; after transmission of the assessment list to the collector, they were *functus officio* because of a need for closure to the taxpayer:

> There should be some limit of time, beyond which this inquisitorial power of the assessor to examine into all the private business transactions of every person, should not be exercised. * * * It appears to me that the assessor should be regarded as to such list functus officio – his power is spent. If he afterwards ascertains that any list or return is false and fraudulent, he may cause the person making it to be indicted and punished therefore under the 15th section; or for perjury under the 42d section of the act.

In re Brown, 4 F. Cas. 330, 332 (N.D.N.Y. 1866).

This lack of power created a problem: the number of returns later discovered to be false gave rise to an impression that "the honest taxpayer almost became the laughing-stock of his fellow citizens." Seligman, *supra*, at 473. Congress responded by giving Assessors the power to re-examine returns, even after the final list was transmitted. But the new power was limited. The re-assessment power could only be exercised when, within 15 months, the Assessor discovered "any omission, or understatement, or undervaluation, or false or fraudulent statement contained in any return or returns made by any persons or parties liable to tax." Revenue Act of 1866, §9. The re-assessment period was the same for all types of erroneous returns, whether the error was innocent (false) or wicked (fraudulent). And the "false or fraudulent statement" had to be "contained in any return or returns made by any persons...liable for tax." *Id.* In sum, since assessments had to be made by each June, the 15-month period in which to re-assess is more accurately understood as a grant of power and not a limitation, triggered by any returns that were simply "false" as well as returns that were "fraudulent." Nothing in the statutes required any intent to evade taxes in order to trigger this additional grant of power.[1]

When Congress re-established the individual income tax in 1913, it carried forward the same "pay after assessment" process used during the Civil War. The Commissioner was still expected to make final assessments by June and evaluate all returns before making the final assessment, only now the re-assessment authority---still triggered by <u>either</u> a false <u>or</u> a fraudulent return---ran for three years. Here is the provision for individuals:

[1] Courts routinely understood a "false" return to be one that was simply incorrect, while a "fraudulent" return was one where the error was intentional. *Eliot Nat'l Bank v. Gill*, 218 F. 600 (1st Cir. 1914)(construing language in 1909 Corporate Tax Act); *Woods v. Lewellyn*, 252 F. 106 (3rd Cir. 1918)(construing the 1913 Act).

> That all assessments shall be made by the Commissioner of Internal Revenue and all persons shall be notified of the amount for which they are respectively liable on or before the first day of June of each successive year and said assessment shall be paid on or before the thirtieth day of June, except in cases of refusal or neglect to make such return and in cases of false or fraudulent returns, in which cases the Commissioner of Internal Revenue shall, upon the discovery thereof, at any time within three years after said return is due, make a return upon information obtained as provided for in this section or by existing law....

§II(E), 38 Stat. at 169.

Importantly, §II(E) also provided that "[n]othing in this section shall be construed to release a taxable person from liability for income tax." 38 Stat. at 171. Thus, a tax liability, once accrued, was not affected by the Commissioner's inability to assess it timely. Even if the Commissioner was *functus officio* for missing the June deadline or the three year deadline for false or fraudulent returns, the government could still sue taxpayers in court, giving the government an unlimited time to sue on the liability. *See United States v. Nashville, C. & St. L. Ry.*, 249 F. 678 (6th Cir. 1918)(collecting cases)(government could maintain an action to recover taxes even when taxes not assessed because assessment was a non-exclusive remedy to collect tax liability). Thus, the limitation periods in the 1913 Act were truly statutes of limitations, not repose.

This all changed in 1918 when Congress replaced the "pay after assessment" scheme with a "pay before assessment" scheme. The Revenue Act of 1918 still required taxpayers to submit returns, and still required that a list of the taxpayers and proposed assessments be transmitted to the Commissioner for assessment. But now taxpayers had to pay their taxes <u>with their returns</u>. §250(a), 40 Stat. at 1082. That is, no longer were taxpayers permitted to wait for the Commissioner to make the final assessment and make demand upon them before being obligated to pay. More importantly, no longer was the Commissioner required to issue final assessments by June. Instead, taxpayers had to pay their liabilities <u>before</u> assessment, and the Commissioner now had to assess "[a]s soon as practicable after the return is filed." *Id.* §250(b). This new scheme left open the question of how long was "as soon as practicable." The statutory answer was given in §250(d):

> Except in the case of false or fraudulent returns with intent to evade the tax, the amount of tax due under any return shall be determined and assessed by the Commissioner within five years after the return was due or was made, and no suit or proceeding for the collection of any tax shall be begun after the expiration of five years after the date when the return was due or was made. In the case of such false or fraudulent returns, the amount of tax due may be determined at any time after the return is filed, and the tax may be collected at any time after it becomes due.

Two features of the 1918 revisions show how Congress moved to a far stronger public policy of closure than previous limitation periods: (1) it dropped the language in §II(E) of the 1913 Act which had provided that nothing in that section would eliminate a taxpayer's liability for tax; and (2) it prohibited both reassessments and any "suit or proceeding" after the limitation period had run, thus bringing closure to both assessment and collection powers after the five-year period.

Of particular relevance here is the ambiguity in the phrase "suit or proceeding" in §250(d). As in this case, the statutory language was arguably ambiguous, and the lower courts were split on how to interpret it. As here, the government argued that the ambiguity should be resolved in favor of preserving the flow of monies into the federal fisc. Specifically, the government wanted the term "proceeding" to be read as meaning court proceedings and not administrative actions like distraint. This position treated the new limitations period still as a statute of limitations affecting the remedy. In *Bowers v. New York & Albany Lighterage Co.*, 273 U.S. 346 (1927), the Supreme Court rejected the government's reading and instead interpreted the statute as one of repose, to promote the policy of closure:

> The purpose of the enactment was to fix a time beyond which steps to enforce collection might not be initiated. The repose intended would not be attained if suits only were barred, leaving the collector free at any time to proceed by distraint.

273 U.S. at 349.[2]

By 1926 Congress had also acted to strengthen its policy of closure by enacting a "we really mean it" statute, now codified as §6401(a), to overturn a Court of Claims decision called *Toxaway Mills v. United States*, 61 Ct. Cl. 363, 372 (1925),

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[2] In 1924, Congress created the current system of two limitation periods, one for assessment and one for collection. Under this arrangement, Congress gave the IRS three years to assess (or file suit without assessment) and then six years to either collect administratively or sue on the <u>assessment</u>. Revenue Act of 1924, ch. 234, §278, 43 Stat. 253, 299-300. Still, no "suits or proceedings" were permitted after three years, except "in the case of a false or fraudulent return with the intent to evade tax or of a failure to file a return." *Id.*

rev'd, 273 U.S. 781 (1927). *Toxaway Mills* involved the problem of waivers. Recall that Congress had directed the Commissioner to examine each return "as soon as practicable" and gave a period of five years to do so. That was not always enough time. "Owing to the inability of the Department to audit all the complicated returns for the years during and after the war period, the Department early instituted a system of waivers of the statute of limitations against the Government." S. Rep. No. 69-52 (1926), *reprinted in* 1939-1 C.B. (Part 2) 357. In *Toxaway Mills*, the Court of Claims held that a waiver signed after the limitations period had run could operate retroactively because the limitations period was simply a statute of limitations, barring only remedies. The Court of Claims decision was issued on December 7, 1925, right in the middle of the Revenue Act of 1926 legislative process. Until that point, there was no provision in either the House or Senate bills that year regarding the limitation period. But after the decision came down, the Conference Committee decided that "amendment is deemed advisable because of an opinion in a recent decision of the Court of Claims." H.R. Rep. No. 69-356 (1926)(Conf. Rep.), *reprinted in* 1939-1 C.B. (Part 2) 380. That amendment became §1106(a) of the Revenue Act of 1926, ch. 27, 44 Stat. 9, and it provided that "the bar of the statute of limitations against the United States and against the taxpayer shall operate to bar the remedy and also extinguish the liability." 44 Stat. at 113. However, in apparent contradiction, the statute went on to say "but no credit or refund shall be allowed unless the taxpayer has overpaid the tax." *Id.*

The confusion caused by the hastily drafted 1926 provision led Congress to change the language in 1928, retroactively, to read almost as it does now in §6401(a): "Any tax…assessed or paid…after the expiration of the period of limitations properly applicable thereto shall be considered an overpayment…." Revenue Act of 1928, ch. 852, 45 Stat. 791, 874. The change in wording did not change the concept: the running of the limitations period extinguished liability and not merely collection of liability. Thus, the Supreme Court described the 1928 statute as providing that "a credit against a liability in respect of any taxable year shall be void if it has been made against a liability barred by limitation." *R. H. Stearns Co. v. United States*, 291 U.S. 54, 60 (1934)(emphasis added, internal quotes omitted). Such has been the judicial construction ever since. *See, e.g., Diamond Gardner Corp.*, 38 T.C. at 881 (reviewing history and interplay of § 6501(a) with § 6401(a)); *accord Hoffman v. Commissioner*, 119 T.C. 140, 144 (2002)("If petitioners' liability for the tax attributable to the cancellation of indebtedness income was eliminated by the expiration of the period of limitations, petitioners cannot be liable for any interest or a penalty.").

The government ignores this historic policy of closure. It argues for an expansive reading of §6501(c)(1) because, it claims, the "fraud exception to the statute of limitations is designed to protect the Government, not to penalize the taxpayer." (Gov.'s Br. 48). Like the government's plain-language argument, this one also begs the question of exactly what the fraud exception is designed to protect against. The traditional interpretation has read the exception as protecting the government from taxpayer fraud. And that reading is supported by the strong policy of closure for taxpayers. Keeping past tax years open is precisely the "penalty" to taxpayers that the policy of closure addresses. It might well be that the policy of protecting the fisc should now trump the policy of closure. But that is up to Congress.

B. The intent requirement in §6501(c)(1) is the same as the intent requirement in §6663.

Section 6663 imposes a 75 percent penalty on underpayments due to fraud. The government agrees that this fraud penalty applies only where the taxpayer committed the fraud, despite the equally ambiguous language in the statute. (Gov.'s Br. 49). Courts have traditionally linked the government's burden under §6501(c)(1) to its burden under §6663: both sections require proof that the taxpayer intended to evade tax. *Pittman v. Commissioner*, 100 F.3d 1308, 1319 n.13 (7th Cir. 1996); *Schaffer v. Commissioner*, 779 F.2d 849, 857 (2nd Cir. 1985); *Asphalt Indus., Inc. v. Commissioner*, 384 F.2d 229, 232 (3rd Cir.1967); *Drieborg v. Commissioner*, 225 F.2d 216, 218 (6th Cir. 1955)(if the government failed to prove taxpayer fraud, then not only were fraud penalties erroneous, but so were any deficiencies for the years barred by the assessment limitations period). *See Neely v. Commissioner*, 116 TC 79, 85 (2001)("the determination of fraud for purposes of the period of limitations on assessment under section 6501(c)(1) is the same as the determination of fraud for purposes of the penalty under section 6663."); *Botwinik Bros. of Mass., Inc. v. Commissioner*, 39 T.C. 988, 996 (1963), *acq.*, 1963-2 C.B. 3.

The government now argues against this traditional interpretation. It suggests that the fraud penalty carries a punitive purpose that distinguishes it from the restitutive purpose of the assessment limitation exception, and these different purposes justify a narrow resolution of the ambiguity in §6663 and more expansive reading of the ambiguity in §6501(c)(1). (Gov.'s Br. 48–49).

The government's argument has three weaknesses. First, it ignores the strong and consistently enforced policy of closure, discussed above. Second, it overstates the difference in purpose. The historic justification for the civil fraud penalty is remedial, not punitive. *See Helvering v. Mitchell*, 303 U.S. 391, 401-05 (1938). It is very similar to what the government claims is the purpose behind §6501(c)(1). *See, e.g., Schachter v. Commissioner*, 255 F.3d 1031, 1034 (9th Cir. 2001)(criminal restitution payments made by taxpayer allowed as credit towards civil fraud penalty because purpose of the civil fraud penalty was "to reimburse the Government for investigation expenses, to cover the monetary loss due to the taxpayer's fraud, and to protect revenue."). Finally, it contradicts the legislative history of these two statutes, which demonstrates that they were legislative twins, born in the same moment and meant to accomplish the same purpose: to impose coordinated consequences for taxpayer misbehavior.

The fraud penalty now codified in §6663 was enacted as part of the Revenue Act of 1918. As with other revenue measures, it started life in the House. H.R. 12863, 65th Cong. 2nd Sess. (as reported by H. Comm. of Ways and Means, Sept. 3, 1918). Recall that §250 of this legislation significantly changed assessment procedure. No longer was the Commissioner required to review all returns and assess by June each year. Instead, taxpayers were required to pay with their returns and the Commissioner was now allowed examine the returns "as soon as practicable" and defer assessment until then.

As sent to the Senate, the House version of §250 consisted of eight unnumbered paragraphs. 63 *U.S. Revenue Acts 1909-1950* at 44-47 (Bernard D. Reams, Jr. ed., 1979). In them, the House created a new penalty for fraudulent understatements of tax, embedded in the middle of a series of contingencies, as follows: First, if the Commissioner's eventual examination revealed an understatement of tax, then "if the return is made in good faith and the understatement...is not due to any fault of the taxpayer, there shall be no penalty." *Id.* at 46. Second, "if the understatement is due to negligence on the part of the taxpayer, but without intent to defraud, there shall be added as part of the tax 5 per centum of the total amount of the deficiency…" *Id.* Third, however, "[i]f the understatement is false or fraudulent with intent to evade the tax, then, in addition to other penalties provided by law…there shall be added as part of the tax 100 per centum of the amount of the deficiency." *Id.* As evidenced by the language "on the part of the taxpayer," the structure of this new fraud penalty scheme focused on the degree of intentionality of the taxpayer, and not third parties.

What is now the §6501(c)(1) assessment limitation exception also came from §250. That part of the the House's undifferentiated eight paragraphs read:

> Except in the case of false or fraudulent returns, the amount of tax due under any return shall be determined and assessed by the Commissioner within five years after the return was due or was made, and no suit or proceeding for the collection of any tax shall be begun after the expiration of five years after the date when the return was due or was made. In the case of false or fraudulent returns, the amount of tax due may be determined at any time after the return is filed, and the tax may be collected at any time after it becomes due.

Id. at 46-47. Notice how this version continued the old phrasing, treating both "false" returns and any type of "fraudulent" return the same: both triggered the new unlimited assessment period. If that language had carried into the final statute, the exception would have completely swallowed the rule. Any error, no matter how innocent, would have defeated closure, per the settled distinction between "false" and "fraudulent" returns. Moreover, any type of fraud associated with the return would trigger the unlimited period, regardless of that fraud's relationship with "the tax" reported on the return.

The Senate Finance Committee re-formatted the House version of §250 into multiple subsections. H.R. 12863, 65th Cong. 3rd Sess., Report No. 617 (as referred to the S. Comm. on Finance, Sept. 21, 1918) at 72-78, *reprinted in* 64 *U.S. Revenue Acts 1909-1950.*[3] In §250(b), it coordinated the new understatement penalty with penalties previously codified in Revised Statutes §3176. In so doing, it did not disturb the series of contingencies that linked the phrase "with intent to evade" with the phrase "on the part of the taxpayer." In §250(d), previously set out on page 14, the Finance Committee fixed the problematic assessment limitation period by inserting the same "intent to evade" language from the new fraud penalty---where we have seen how it referred to the intent of the taxpayer and not third parties.

This history of how the phrase "with intent to evade" came into what is now codified at §6501(c)(1) thus strongly supports the traditional interpretation of §6501(c)(1) as containing the same intent requirement as the equally ambiguous language in §6663. There is absolutely nothing in the legislation process to suggest that the phrase "with intent to evade" had one meaning for the new fraud penalty and another meaning for the fraud exception to the assessment limitations period. On the contrary, these two provisions were inextricably linked; they were legislative twins. They were born at the same time, in the same Committee, as part of the same section of the Code, to deal with the same misbehavior by taxpayers.

[3] The Conference Committee Print is also in Vol. 64, as is the final product.

C. Section 6501(c)(1) should be read in harmony with §7454.

Whenever a taxpayer contests a Notice of Deficiency (NOD) in Tax Court, the taxpayer must overcome a very strong presumption that the NOD is correct. T.C. Rule 142; *United States v. Janis*, 428 U.S. 433, 441-42 (1976); *Welch v. Helvering*, 290 U.S. 111 (1933). Until that presumption is overcome, courts will not examine the basis for the adjustments that have been made, the propriety of the Commissioner's motives, or the administrative policy or procedure used in determining a deficiency. *Zuhone v. Commissioner*, 883 F.2d 1317, 1325 (7th Cir. 1989).

Section 7454 is an exception to this general rule. It provides that "[i]n any proceeding involving the issue whether the petitioner has been guilty of fraud with intent to evade tax, the burden of proof in respect of such issue shall be upon the Secretary." This statute is not limited by its terms to issues involving assertion of the fraud penalty but to any issue involving taxpayer fraud. The Tax Court has long applied this statute when the government seeks to invoke the §6501(c)(1) fraud exception to the three-year assessment limitations period. *McGowan v. Commissioner*, T.C. Memo 2004–146, *aff'd.* 187 Fed. Appx. 915 (11th Cir. 2006); *Willits v. Commissioner*, 36 B.T.A. 294 (1937).

The traditional interpretation of §6501(c)(1) is in harmony with §7454 in that both statutes focus on taxpayer misbehavior. The former creates an unlimited assessment period when taxpayers misbehave and the latter puts the burden on the government to prove the misbehavior.

In contrast, the government's proposed interpretation of §6501(c)(1) creates an anomaly, a gap, a problem. Who bears the burden of proof when the government seeks to extend the limitation period based on the alleged fraud of a third party, such as the taxpayer's CPA, return preparer, bookkeeper, in-house counsel, external counsel, salesperson, head of personnel, fleet manager, loan officer, or anyone else whose fraudulent activities the government decides has caused the taxpayer's return to be erroneous and thus, under the government's view, "evading" a tax? The general presumption of correctness puts the burden on the taxpayer to disprove the fraud of third parties and the plain language of §7454 would not apply. Thus, the government would bear the burden of proof on the taxpayer's fraud, but not the fraud of a third party. Such a result does not appear to be what Congress intended when it created the statutory rule.

The current set of government actors may suggest that common law allocates the burden of proof to litigants who allege fraud. They could certainly cite cases to that effect. Until Congress created the statutory rule, however, an earlier set of government actors argued strenuously that the general presumption of correctness for NOD's overcame the common law and required taxpayers to disprove allegations of taxpayer fraud. The Board of Tax Appeals began to agree. *See*

Desmonds, Inc. v. Commissioner, 15 B.T.A. 738 (1929); *Budd v. Commissioner,* 12 B.T.A. 490 (1928), *rev'd,* 43 F.2d 509 (3rd Cir. 1930); *Humphrey v. Commissioner*, 9 B.T.A. 656 (1927).

It was to correct this practice that Congress enacted what is now codified at §7454, as §601 of the Revenue Act of 1928. 45 Stat. at 871. *Budd v. Commissioner*, 43 F.2d at 512. ("§601...specifically corrected this practice by amending section 907 of the Revenue Act of 1924"); *accord Paddock v. United States,* 280 F.2d 563 (2nd Cir. 1960)(discussing history of §7454 and its application in refund suits).

Section 601 was based on a proposal from the ABA's Committee on Taxation. *Revenue Act of 1928: Hearings on H.R. 1 Before the S. Comm. on Finance*, 70th Cong., 1st Sess. 23-26 (1928) (testimony of Hugh Satterlee).[4] Reflecting the traditional interpretation of §6501(c)(4), the discussion in the Senate Finance Committee hearing shows that the proposal was understood as applying equally to fraud for penalty purposes and for statute of limitation purposes. *Id.*

Even after Congress created the statutory rule, earlier sets of government actors argued strenuously that the rule did not apply in refund cases. *Paddock,* 280 F.2d at 566-67 (reviewing case law from seven circuits). So whatever position the current set of government actors may take, their time on the stage will pass and

[4] The Hearings are reprinted in 8 *U.S. Revenue Acts 1909-1950.*

another set of government actors may come to believe that the strong presumption of correctness given NODs should overcome the general common rule. That is the reason for the statute. And that is why reading §6501(c)(1) as reaching beyond the intent of the taxpayer to evade creates an anomaly, a gap, a problem.

CONCLUSION

Misbehaving tax advisors and return preparers is certainly a serious concern. In the face of Congressional inaction, one can be entirely sympathetic to the tax agency's attempt to address the problem on its own. This is not, however, a new problem. It existed back in the 1920's when the traditional interpretation of §6501(a)(1) was already well-developed. *See* Bryan T. Camp, *'Loving' Return Preparer Regulation*, 140 Tax Notes 457, 469 (2013). And sympathy is not a good reason to re-interpret §6501(c)(1) in the face of a traditional interpretation well-grounded in the text, context, and history of the statute, especially when such re-interpretation will unsettle the law.

Respectfully Submitted,

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Date: June 25, 2014

CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing brief with the Clerk of the Court for the United States Court of Appeals for the Federal Circuit by using the appellate CM/ECF system on this 25th day of June, 2014. I further certify that service of the brief was made on counsel for the appellant and counsel for appellee by CM/ECF.

/s/ Bryan T. Camp

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CERTIFICATE OF COMPLIANCE

With Type-Volume Limitation, Typeface Requirements, and Type Style Requirements

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 6,585 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

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 Microsoft Word 2010 in 14-point Baskerville Oldface.

/s/ Bryan T. Camp

Date: June 25, 2014