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By Hugh C. Bickford

The suggestion has been made that the jurisdiction of the board of tax appeals be enlarged to enable it to pass upon suits for the recovery of taxes, in addition to its present power to review determinations of deficiencies as made by the commissioner of internal revenue. The thought has a parental wish. Obviously, the wish is that there be some judicial body with authority to review decisions of the commissioner in cases where his view is considered erroneous and it is found, due to the particular status of the case, that the board does not have jurisdiction.

The suggestion should be carefully weighed. When one finds a tribunal with over twenty thousand unheard cases on its docket and learns, as a result, that his case, when filed, must wait for several years before it is tried, and even longer before it is decided, one must express some doubt as to the wisdom of increasing the business of that tribunal and further submerging its functions beneath the flood of a new class of cases. The fact remains, however, that this board can not review many decisions of the commissioner, such as rejections of claims for refund, and that these decisions are as likely to require review and correction as those which result in deficiencies and may, therefore, be carried to the board. The fact which is too generally ignored is that there is ample opportunity of reviewing the commissioner's actions on refund claims without going to the board. The writer refers to review by the federal courts. This right existed before the board was established and if it had been resorted to more frequently probably would have made unnecessary the creation of the board in the first instance.

Before the creation of the board there was not one case in many thousands which reached the courts. Yet, at that time, the commissioner was handing down the same decisions which are being made today, with the same, if not a greater degree of inaccuracy than that which now prompts the filing of so many petitions with the board. True, there was no mode of obtaining relief until after the tax was paid but even this relief was not often sought because of the generally prevailing hesitancy to go into court.

The effect of the creation of the board upon tax practice has been marked in many respects, but in none so plainly as in the effect upon those who represent taxpayers. They now unhesitatingly turn to the board for the courtlike relief which it affords, and, in so doing, they have learned the magic of sworn testimony and documentary proof, properly presented, and of logical argument, timely made. They have learned that public decisions based upon a public record are rather less arbitrary and infinitely more satisfactory in ultimate result. Strangely, however, there is still the same hesitancy to seek the relief which the courts afford and still the same ungrounded fear of suits for recovery.

One sometimes wonders if the hesitancy was or is caused by the fact that tax representatives, generally, are not trial lawyers, and reach the conclusion that if the case is carried into the courts it will mean that they will have to relinquish its control. The thought is too repugnant to bear emphasis. Surely, no professional man, whether he be an accountant or office lawyer, would be guilty of restricting the rights of his clients to the limits of his own capabilities.

The writer does not wish to enter the dog-eared discussion as to which is best qualified to handle a tax case—the accountant or the lawyer. He sometimes thinks that one must be both; and, likewise, an economist, a statistician, a paragon of patience, yea, even a psychologist, for else how could one know just the proper time to admire the cravat of the conferee? Undoubtedly, however, there is need at times for the British system of the divided sphere of solicitor and advocate. When the solicitor has conducted, out of court, all negotiations and conferences seeking to obtain for his client a just settlement, and has failed, it is his duty, in a proper case, to recommend trial and to arrange for the advocate, or barrister, to conduct the trial of the case. So, in tax cases, when the accountant, or office lawyer, has exhausted all proper means before the department and has failed to obtain that which it is honestly believed his client is justly entitled to, it is his duty to advise his client of his right to recover by court action and to bring to that proceeding, in an advisory capacity, the knowledge and experience which he has derived from the negotiations before the department. Otherwise, the representative has failed to apprise his client of his full remedy and has subjugated the rights of the cause to his own limitations.

For example, some months ago there was a case pending before the treasury department involving the valuation of a patent. The inventor had conducted the business of manufacturing the patented article as a sole proprietorship for seven years. His inventive genius was far superior to his business sagacity and the company lost money in virtually every year. Finally, a corporation (let us steal the department's custom and call it the M Company) was formed and the patent, together with all other assets of the business, was paid in for capital stock. Stock having a par value of two million dollars was issued for the patent, and the M Company subsequently claimed as deductions from gross income the amortization of that amount. The department applied its well known formula, based solely upon earnings, and held the patent to be worthless with the result that the entire deduction was disallowed. Affidavits were obtained from several nationally known experts in the art who testified that in their opinion the patented article was the best of its kind in the world—a distinct and highly valuable contribution to commerce and to science. Hundreds of original letters were exhibited which contained orders for the article which had not been filled because of the limited facilities of the business as it had been conducted. Finally, several business men of the community executed affidavits that several months before the incorporation of the business they had offered one million dollars for the patent and had been turned down by the proprietor, and, further, that they had agreed among themselves to pay two million if they could get the patent. Spokesmen of the unit said they "didn't know these men; they didn't know whether they *had* two million dollars; they didn't know whether they would have given it if they had had it." (Any tax representative knows the rest of their answer.) Affidavits were filed by prominent bankers testifying that the men making the offer were the wealthiest and best type of men in the community (character witnesses). Finally, letters were filed from members of congress from that locality testifying to the honesty and reputation of the bankers and of the offering syndicate. The unit continued to point out that the patent had never produced any actual profits, but finally yielded sufficiently to allow a value of one million dollars. The case was carried into court. There the same witnesses were called. Their testimony was convincing and the government offered no rebuttal. It was not necessary there to bring in a second group of witnesses to

prove that the first witnesses were not liars and a third group to prove that the second were honest. The two-million-dollar valuation was allowed. A hesitancy to go into court in this case would have cost the clients many thousands of dollars.

Still another illustration. A partnership claimed special assessment under section 210 of the revenue act of 1917. The partnership was a commission house and argued that it had done over six million dollars' worth of business for its clients on a capital of only $16,000. It kept no books of the total business handled but only of the net commissions received. By consistent rule of the trade such commissions were paid at the rate of one and one-quarter per cent. of the business handled and amounted to $75,000 for the taxable year. Capitalizing this amount, the figure of $6,000,000 was easily obtained. The department refused to believe that $75,000 in commissions meant a total business handled amounting to $6,000,000. One representative in the department went so far as to intimate that inasmuch as that figure was not on the books, somebody must be fabricating. Affidavits, briefs, protests, photostats of the books and all other evidence requested were filed with the department, but the claim was rejected. The case was carried into court where the same evidence was presented which had been exhibited to the department. The government's arbitrary opinion was not competent evidence. The court specially found the facts without question. A hesitancy to go into the courts in this case would have cost the client considerable in taxes which he did not legally owe. The illustrations could be presented ad infinitum. The point is that there should be no such indecision, in a proper case, to claim a right which the law gives. The answer in such cases lies in the courts.

To place one in the proper position to advise court action and to arrange for its commencement, it is necessary to know the remedies provided. The principal class of cases will be those in which the taxes have been paid and claims for refund rejected. Before suit may be brought for the recovery of such taxes all of the prerequisites established by law must have been observed. It must be borne in mind that the sovereign may not be sued without its consent, and, if it has attached purely formal conditions to its consent to be sued, these conditions must be complied with. As Mr. Justice Holmes has stated: "Men must turn square corners when they deal with the government." The conditions to be fulfilled before suit may be commenced are contained in section

1113 of the revenue act of 1926, amending section 3226 of the *Revised Statutes*. Briefly stated, they are:

1. The tax must have been paid.
2. Within the statutory period of limitations a proper claim for refund must have been filed.
3. The claim for refund must have been rejected, or, if not rejected, must have been pending before the commissioner for at least six months.
4. The suit must be brought within five years from the date the tax was paid or within two years after the claim was rejected.

Numerous decisions have been made involving these conditions, the most important of which are to the effect that the claim which forms the basis for the suit must be a proper claim for refund or credit. A claim for abatement or an informal claim is not sufficient. Likewise, the claim must have been based upon the same grounds which form the basis of the suit. A suit upon one ground may not be founded upon a claim for refund stating entirely different grounds.

These steps should be taken during the pendency of the motion before the department with the definite thought in mind that a proper foundation shall be laid for future court action. Otherwise, due to the statute of limitations, it may be too late to lay the proper foundation after the department has made its rejection. In this respect the negotiations before the department are similar to a trial in the lower court. The foundation for the appeal must be laid during the trial. It is too late when the trial court has entered its judgment.

The preliminary conditions having been fulfilled, it is necessary to consider the nature of the suit to be brought and the court in which it should be brought. There are two branches of the judiciary in which the suit may be filed. The action may be brought in a federal district court, of which there are now over eighty sitting in the various federal judicial districts of the United States. On the other hand, suit may be filed in the United States court of claims at Washington. We will consider the classes of actions to be brought in each of these courts.

As stated above, a sovereign state may not be sued without its consent. At common law, however, the judges found a mode for avoiding the stringency of this rule in cases where taxes had been illegally collected. They permitted suits, sounding in

assumpsit, to be brought against the collector to whom the taxes were paid, provided the taxpayer had paid the taxes under duress or protest and had thus put the collector on notice that the taxes were considered illegal and that suit for their recovery would be instituted. In the absence of such a protest there was no way at common law for recovering taxes which had been illegally paid. This common-law right to sue the collector was adopted by the federal courts of this country and is recognized today. However, section 1116 of the revenue act of 1926 has relieved taxpayers of the necessity of paying the taxes under protest. The suit against the collector may be brought in any amount and must be filed in the district in which the defendant, the collector, is a resident at the time the suit is filed.

The rigor of the common-law inhibition against suits against the sovereign was relaxed by the enactment, in 1887, of the Tucker act, which made it possible to sue the United States directly for "claims not exceeding $10,000 founded upon the constitution of the United States or any law of congress, or upon any regulation of an executive department." Suits for the recovery of taxes illegally collected have been held to be included within this definition. Further, the revenue act of 1921 amended the Tucker act to allow suits for taxes to be brought against the United States "even though the claim exceeds $10,000, if the collector by whom such tax, penalty, or sum was collected, is dead or not in office at the time the suit or proceeding is commenced." This obviates the necessity of proceeding against collectors long since gone from office, or against the personal representatives of deceased collectors. Where the United States is named as defendant, the Tucker act requires that the petition must be filed in the district in which the plaintiff resides.

In all such cases in the federal courts the rules of practice and procedure are the same as in other civil suits. The "Rules of decisions" act of 1789 has been held to require the district courts to follow the rules of evidence enforced by the state courts of the state in which the district court sits. The conformity act of 1872 requires that the practice, pleadings and form and mode of proceeding in the federal courts shall conform to like practice in the state courts. These statutes apply to suits to recover taxes.

Summarizing, we find that in the district courts the practice in tax suits is largely the same as in any other civil suit. If the amount sued for is less than $10,000 the action for recovery

may be brought either against the collector or against the United States. If, however, the taxes total more than that amount, the action must be brought against the collector to whom the taxes were paid, unless he is dead or out of office, and in that event the United States may be named as defendant. Only one class of suit is permitted; the taxpayer may not join both the collector and the United States as defendants.

Suits in the court of claims will be found more acceptable in many respects. The action there may be brought in any sum and regardless of the status of the collector to whom the taxes were paid. In that court the United States is always named as defendant. Another important advantage is that the docket of the court is not so crowded as in many of the district courts. More important, however, is the manner of taking testimony and conducting the hearing.

The taking of oral testimony before the court of claims at a formal hearing is a rare occurrence. Under statutory authority there have been appointed a number of commissioners of the court whose duty it is, under the law and the rules of the court, to take testimony and making findings of fact. Virtually all of the testimony in cases pending before the court is taken under the jurisdiction of these commissioners. The rules provide that where convenient the testimony shall be taken in the county in which the witness resides. The rules likewise provide for the taking of testimony on deposition before a notary public or other officer authorized to certify to such testimony. When the petition is filed with the court and answer made by the government (usually a general traverse, or denial) the case is assigned to one of the commissioners for a report of the facts. Arrangements can then be made with the commissioner to produce the witnesses before him or to take depositions before a duly authorized officer of the locality in which the witnesses reside. In some instances the testimony is taken both by deposition and orally before the commissioner. At the conclusion of the testimony the parties will be permitted to file with the commissioner suggested findings of fact based upon the testimony adduced. The commissioner then makes his report to the court and the parties are allowed thirty days within which to object to his findings. These objections will be passed upon by the court. Briefs are then filed by the parties and in due course the case is set down for oral argument before the court itself. Thus, in the usual case, the only actual

appearance before the judges of the court is to make oral argument on the basis of findings of fact as reported by the commissioner and the printed briefs already filed.

It will readily be seen that the procedure before the court of claims is likely to be more convenient and expeditious in tax cases. It is certain that the procedure there is no more difficult and the rules of pleading and evidence no more stringent than those which are enforced by the board of tax appeals, and there should be no more hesitancy, in a proper case, in seeking the relief which this court affords than there now is in petitioning the board of tax appeals for a redetermination of a deficiency.

In all probability, if a case has justified the expense and inconvenience of a long and vexatious litigation before the treasury department, court action is likewise justified. At all events, it is certainly the duty of the representative of the taxpayer, when he believes that an erroneous decision has been rendered by the department, to apprise his client of the further possible relief by an appeal to the courts and to place before him the full facts of the matter so as to enable him independently to reach a decision whether or not to proceed with the case.