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Board of Tax Appeals

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The Board of Tax Appeals *

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Since the passage of the first income-tax statute in 1913, the accountant has played an important part in the administration of the federal tax law. When the war came on and it became necessary to raise additional revenue, and the war revenue acts were passed, which made necessary the determination of invested capital, and carried other provisions with which we had had no experience, the accountant's rôle became still more important. The important part played by the accountant in the administration of the law during these years has had its effect upon the principles involved in the more recent acts. The principles embodied in the present act are the result of knowledge obtained by the treasury department through its administration of the law. Many of the most important changes are those founded upon sound principles of accountancy, many of which have gone into the regulations and subsequently became part of the act itself.

The precise facts are most important in the handling and consideration of any case, and it is in connection with gathering the facts that the technical skill of the accountant has been of untold value. The ability properly to analyze a balance-sheet, with its supporting data, may be more important in determining invested capital than a knowledge, or learned discussion, of the decisions of the courts. The accountant's service has been highly important, and to him belongs a very large share of the credit for the solution of many of the difficult problems with which the government and the taxpayer have been confronted.

The organized accountants took a very active and important part in the discussions which took place while congress had under consideration the section of the revenue act of 1924 providing for the board of tax appeals. The first thing the board did after its organization was to promulgate two rules; one dealing with the manner by which an appeal might be promulgated and the other relating to admission to practice. The United States government, by the rule of the board relating to admission to practice, for the first time recognized accountancy as a profession, and

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thereby recognized the great value of the service which had been performed by the members of that profession in the solution of the problems growing out of the revenue acts.

It is highly fitting, therefore, that you should be unusually interested in what the board has done and is doing to carry out the provisions of section 900 of the revenue act of 1924, which created it.

Prior to the passage of the revenue act of 1924, under the practice of determining and assessing additional taxes, there were certain grave fundamental defects which led the public to feel that it would not receive unprejudiced and equitable treatment. The only appeal that a taxpayer had as to taxes assessed through subordinates of the commissioner of internal revenue, prior to the payment thereof, was an appeal to the commissioner of internal revenue or his subordinates. Taxpayers naturally felt that the commissioner of internal revenue, if zealous in the performance of his duties, would collect as much of the revenue for the government as possible, and accordingly his inclination would be to decide all doubtful questions against the taxpayer, and his subordinates or appointees, whether in the income-tax unit or a disconnected reviewing body, such as the advisory tax board or the committee on appeals and review, would be guided by similar motives.

This attitude on the part of taxpayers brought about discussion which finally resulted in the creation, by the revenue act of 1924, of the board of tax appeals, of which the members are appointed by the president, with the advice and consent of the senate, and which constitutes an independent agency in the executive branch of the government designed to stand impartially between the taxpayer and the bureau of internal revenue.

Prior to the enactment of the act of 1924, the taxpayer before payment of the tax, sought revision in the adjustments made in his taxes by the income-tax unit by taking an appeal to the commissioner. The commissioner personally could not pass upon all the questions, and various methods of review were provided in the bureau of internal revenue for consideration of the questions involved. The advisory tax board functioned prior to October, 1919. The committee on appeals and review was created at that time and remained in existence until the organization of the board of tax appeals. The solicitor of internal revenue also considered many appeals. This machinery merely expressed the

determination of the commissioner as to the amount of tax due. This practice led to a feeling on the part of the public that cases in the bureau were not always decided upon their merits. It was objected that the appeal from the action of the income-tax unit was usually taken to an organization which was a part of the bureau itself, that the person who was to decide the appeal acted both as advocate and judge, since he must both protect the interests of the government and decide the question involved, and that such conditions did not insure impartial decision of the cases. If the decision on the appeal was in favor of the government, the taxpayer only after payment of the tax had the right to protest the correctness of the decision in the courts, but if the decision was in favor of the taxpayer the action of the bureau was final and the decision of the bureau could never be contested in the courts. It was contended that this condition resulted in the decision of many doubtful points in favor of the government.

To meet these objections, congress established the board of tax appeals. Although prior to the passage of the act, the taxpayer might, after payment of his tax, bring suit for the recovery thereof and thus secure a judicial determination of the questions involved, he could not, in view of section 3224 of the revised statutes, which prohibits suits to enjoin the collection of taxes, secure such a determination prior to the payment of the tax. It was felt that the right of appeal after payment of the tax was an incomplete remedy and did little to remove the hardship occasioned by an incorrect assessment. The payment of a large additional tax on income received several years previously and which since its receipt may have been either wiped out by subsequent losses, invested in non-liquid assets or spent, sometimes forced taxpayers into bankruptcy and often caused great financial loss and hardship. These results were not remedied by permitting the taxpayer to sue for the recovery of the tax after payment. It was believed that he was entitled to an appeal and a determination of his liability for the tax prior to its payment.

Under the provisions of the act creating the board, the taxpayer may, prior to the payment of additional tax, appeal to the board and secure an impartial and disinterested determination of the issues involved.

In the consideration of the appeal, both the government and the taxpayer appear before the board to present their cases, with the result that each member of the board sits solely as the judge and

not both as the judge and the advocate. The provision allowing the commissioner to sue in court for the recovery of any taxes thought by him to be due in excess of that decided by the board to be due, relieves the board from the responsibility of finally passing upon questions involving large amounts and removes the necessity for a decision in favor of the government in order to force the issues into court.

The president was empowered, with the advice and consent of the senate, to appoint, solely on the grounds of fairness to perform the duties of the office, not more than twenty-eight members to compose the board. Those first appointed were to serve until two years after the passage of the act, after which it is provided that the board shall consist of seven members appointed for overlapping terms up to ten years.

On July 3, 1924, the senate not being in session, President Coolidge made recess appointments of the first twelve members of the board. The appointees were chosen from all parts of the country and were selected on the basis of their qualifications for the office.

Those appointed met in Washington on July 16, formally organized as a board, elected a chairman and appointed a secretary. The board decided to proceed forthwith to the adoption of rules under which taxpayers could proceed to file their appeals and the commissioner of internal revenue could prepare to defend them. By remaining in continuous session, the board was able to prepare and publish its rules by July 28th, and printed copies were ready for the public by August 6th. On July 30th the first appeal was filed.

On August 15th, approximately thirty days after its organization meeting, the board first sat to hear argument in a motion made by counsel for a taxpayer with respect to the commissioner's pleading in his case, and on August 19th the first appeal was argued before the board, all members being present. The board was ready even before this time to hear appeals, but none was ready for presentation prior to that date. The decision in the first case was handed down on August 27th, and on the same day the board heard argument in the second case.

The board of tax appeals is in effect a judicial tribunal of limited jurisdiction. It has power to review determinations of the commissioner of internal revenue with respect to income and profits taxes, estate taxes and the new gift tax. There are some interest-

ing questions capable of argument on either side as to the extent of the jurisdiction of the board over taxes assessed under past revenue acts. With respect to these, of course, it would not do to express any obiter opinions. It has already been necessary to decide, however, in a litigated case, that the board has no jurisdiction over claims for refund. This necessarily follows from the limited power vested in the board. When the commissioner of internal revenue makes a determination proposing to assess a deficiency tax, the taxpayer may appeal to the board, and, to the extent that he prevails, the commissioner is prohibited from collecting the proposed tax by distraint. He may, however, sue in the courts for the collection of the tax. In that case the findings of the board are prima-facie evidence of the facts found. This constitutes a method of appeal by the commissioner from the determination of the board. The taxpayer has a similar method of appeal by paying such taxes as the board determines to be proper and suing to recover them. If a tax has already been paid, however, the board is vested with no jurisdiction to compel the treasury to refund it, and the taxpayer's remedy is the same as it was before the passage of the 1924 act—by suit in the district court or the court of claims.

The first problem with which the board was confronted was that of determining its policy with respect to rules of practice, including the admission of counsel, evidence and procedure. In the first draft of the revenue act of 1924, commonly known as the Mellon bill, it was provided that the proceedings before the board should be informal, but after several changes, the congress finally decided to substitute for that provision this language: "The proceedings of the board and its divisions shall be conducted in accordance with such rules of evidence and procedure as the Board may prescribe." Obviously congress decided to leave the question of formality of procedure to the judgment of the board. So it became necessary to decide whether to provide for highly informal proceedings, such as those conducted by conferees in the income-tax unit, or strict and technical rules, such as those in force in the courts, or for some intermediate scheme.

The statute leaves no room for doubt as to the solemn nature of the function of the board. It is not merely a newly created higher division of the bureau or even of the treasury department. It is, in the language of the statute, "an independent agency in the executive branch of the government," and as such it is expected to

act independently in all its determinations. This independent character cannot be too firmly emphasized because it seems not to be fully realized, for this is what makes necessary the formal procedure of the board. If the board were within the bureau the entire record in the bureau would be available to it, and all of the administrative aspects of each case would need be considered. The board in the privacy of its chambers would go through the file and with the aid of an additional argument on behalf of the taxpayer would determine whether the unit acted wisely. Thus the taxpayer would be in much the same situation as he has heretofore been before the unit and the committee.

This is very apparently not what congress intended. The reports of the congressional committees and the language of the statute show that what was intended was an entirely independent body with no motive except to apply the law to the facts in each case and reach the correct answer in that case. The board is not to collect the revenue and hence it has no fear of administrative precedents. Its concern is to see on the one hand that the citizen is not unjustly assessed and on the other that in the collection of its just revenue the government is not unduly delayed. The board represents neither party. Both parties are represented by their own advocates who, the board confidently believes, will seek wholeheartedly to give it the proper basis for a correct conclusion.

The provisions of section 900 of the statute are very specific as to how the board shall perform its function. It must hear appeals, giving notice and an opportunity to be heard both to the taxpayer and the commissioner. These hearings shall be open to the public and all the evidence shall be open to public inspection. It must not only decide the ultimate question of liability but it must in all cases make a written report of its findings of fact and decision. In cases where more than $10,000 is in controversy it must write an opinion. Witnesses are to be heard and, if necessary, compelled by subpoena to testify; oaths are to be administered; papers and books introduced in evidence and depositions taken. These are not the attributes of an administrative office. They give us the picture of a judicial tribunal.

We are familiar with the growth in recent years of the special tribunal outside the judiciary. In the federal government the interstate commerce commission and the federal trade commission are well known examples. Such bodies have a composite function to perform, both judicial and legislative. They are largely con-

cerned with the legislative function of prescribing specific rules of conduct for the future—and to that end they determine the facts of the past. Their primary interest is not for the parties but for the public, so that carriers' rates and business practices shall be fair. Their problems are more economic perhaps than legal, and yet these bodies have without exception found it necessary to adopt the forms of litigation in order to determine issues.

This board has no such legislative function and the problems which it solves are only indirectly economic. They are primarily legal. The board must see that a specific statute is correctly applied to a completed and past state of facts and the specific liability of a single person under that statute correctly determined —a purely judicial duty. If a correct determination discloses a wrong economic result for the future the remedy is with congress.

But there is a further matter to be considered. The act provides that in any subsequent proceeding in court, either by the taxpayer to recover the amount paid or by the government to collect the amount abated, "the findings of the board shall be prima-facie evidence of the facts therein stated." This means that in practice the findings of the board shall have judicial effect. While it is true the board has no power directly to enforce its determination, here is a provision which gives the decision a legal sanction in a court of law. I do not wish to express for the board any opinion as to the legal effect of the decision, but this is probably what may be expected to take place: Suppose the government sues in court for a deficiency which the board has held is not due. The taxpayer, relying upon the decision of the board, introduces it in evidence and the findings of fact thus stated constitute, as provided by the statute, prima-facie evidence of the facts therein stated. But a finding of the board cannot be arbitrary and still retain its weight as evidence. Its effect is only prima facie, which means that it may be overcome. The opposing party—in our illustration, the government—may no doubt by countervailing testimony overcome the effect of the findings. But are they in the first instance entitled to prima-facie effect unless they are supported by legal evidence? Will a court respect the findings of the board if made other than in accordance with a legal record? If the record before the board discloses that the finding is unsupported by legal evidence, how can it be justified? It is unfortunate that truth is sometimes elusive and can be captured only by devious methods; but this is a recognized fact and cannot be

ignored. If we act upon what the law of our land has after many years come to recognize as evidence, our feet are upon solid ground. To do otherwise would be to arouse suspicion and incur resentment. This the board hopes to avoid. We want the citizen to feel confident that we will act openly and above board and that the decision will be upon the merits of the case.

Having in mind the provisions of the statute and the general principles to which I have alluded, the board formulated its rules of practice in accordance therewith.

In the actual preparation of the rules, every effort was made to make them as simple as possible, and it is believed the board has succeeded. Anyone who knows the facts in the case and has formulated his reasons as to why he thinks the commissioner has committed error, can prepare his petition on appeal. It probably is not possible, having in mind the provisions of the statute, to have fewer rules than those adopted. The board has already found places where minor changes were desirable and others will undoubtedly occur from time to time as its experience grows.

The statute provides that the board may be divided into divisions by the chairman, that the divisions may sit at any place within the United States, and that the times and places of the meetings of the board and of its divisions shall be prescribed by the chairman with a view to securing reasonable opportunity to taxpayers to appear before the board or any of its divisions, with as little inconvenience and expense to taxpayers as is practicable. These provisions have led some persons to believe that divisions would be permanently assigned to certain cities in different sections of the country. This undoubtedly would be permissible under the statute, but so far it has seemed to us inadvisable. At present it has seemed to the board that if we were to establish divisions, of say three members, in each of a number of cities and keep them there permanently, we should very soon have conflicting rulings coming from the various divisions. Under the statute the decision of a division becomes the final decision of the board thirty days after it is rendered by the division, unless within that period the chairman has directed that such decision shall be reviewed by the board. If the board is scattered all over the country, it cannot very well review decisions of divisions, for reviewing by circulating copies of records and opinions and by requesting written comment and vote by absent members would be highly unsatisfactory. It has therefore seemed much wiser to

arrange hearings outside of Washington in such a way that divisions which go into the field to hold them will return to Washington. No definite arrangements for hearings in the field have yet been made. The number of cases at issue to date hardly justified any such assignments, and it has been highly desirable to be together and get experience, as a board. As the number of cases arising in different parts of the country increases sufficiently to justify sending divisions out, itineraries will be planned and divisions will be sent into the field to sit for stated periods in different places and then to return to Washington for general conference. It is impossible to lay out any definite circuits and to prepare calendars showing when divisions will sit in the various towns on those circuits, for the number of cases arising in the different parts of the country should be the controlling factor, as the whole purpose of sending divisions into the field is to meet the convenience of the taxpayer. Just as a concrete indication of what we have in mind, I might say that the number of pending cases might develop so that it would be decided to send a division to sit for a week at Atlanta, another week at Birmingham, a third week at New Orleans, and then to return. Meanwhile another division might be sent to cover Los Angeles, San Francisco, Portland and Seattle; while a third might cover St. Louis, Kansas City, Dallas, St. Paul and Denver; and a fourth Pittsburgh, Detroit, Cleveland and Chicago. But it is impossible to make any definite plan until the board can get more information as to the number of cases it will have for disposition and some idea as to their geographical origin. It may be that divisions will be sent into the field as early as the first of December.

The statute provides for the publication of findings of fact and decisions in every case, and an opinion in every case involving over $10,000. Under present plans, the findings and decisions in each case, and the opinion in those cases where opinions are rendered, will be mimeographed and will be available to the public shortly after promulgation. While not definitely decided it is possible that reports will be reprinted in pamphlet form for weekly or for monthly distribution, and if this plan is carried out arrangements may be made with the superintendent of documents for subscription to these pamphlets in the same way that the internal-revenue bulletin is now distributed.

All of the members of the board of tax appeals realize the magnitude and the importance of the task which the board has to

perform. It has been recently organized and it is felt that great progress has been made in building up an organization for carrying on its work. It has not had sufficient experience to determine whether or not its existence is justified. The purposes behind its establishment are well known. The board hopes to accomplish everything that has been hoped for it. It is, however, treading on new ground and it will have before it in the future many serious problems. It may be that some of its decisions will be criticized. During the early period of its existence it is hoped that a charitable attitude will be taken and that its mistakes, if any, will be considered in the light of the serious problems it has before it. The board should be given an opportunity to make up its record before final judgment is passed.