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INTRODUCTION TO THE INTERNAL REVENUE CODE OF 1954

AND

THE ROLE OF THE TAX PRACTITIONER IN THE PRACTICE OF LAW*

SEYMOUR S. MINTZ**

The program instructs me to begin on an historical note, so let me comply at once, with at least some plausible relevance, however, to what is now going on in the world about us.

We have a federal internal revenue system which currently is collecting at the rate of some 70 billions of dollars annually. What can we do, individually and collectively, in the face of this octopus?

Firstly, we could, of course, take up arms and revolt, as did our forbears in the early Whiskey Rebellion, in response to the enactment in 1791 of our *very first* internal revenue statute.¹ But today the remedy of armed insurrection is manifestly impractical.

Secondly, there is the more mundane solution of "voting the rascals out." If we harken back 154 years, we find that when the Federalists were removed from office in 1800, all the internal revenue taxes were repealed except the one on salt. I doubt that we consume enough salt today to bear our entire burden of Government, and, even if we were to add "sugar and spice and everything nice", I am afraid that the solution of 1800 still would be unavailable.

Thirdly, we could, as in the past, honorably attempt to take refuge in the Constitution. This failed in respect of the tax on carriages in 1794, but it was effective to knock down the 1894 income tax, thereby requiring the adoption of the Sixteenth Amendment, which permits the income tax to be levied without apportionment among the states according to population.

As recently as two months ago a strong-minded taxpayer appeared in the federal courts suing the United States for an income tax

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1. The historical references in the text paragraph and the two paragraphs succeeding it may be found in Bruton and Bradley's *CASES AND MATERIALS ON FEDERAL TAXATION*, 1954 Ed., Pamphlet No. 1, p. 1, (West Publishing Co.).

refund on the ground that the income tax is unconstitutional because it places taxpayers in a position of involuntary servitude, contrary to the Thirteenth Amendment. The Circuit Court for the Tenth Circuit found taxpayer's claim to be far-fetched, frivolous, unsubstantial and without merit.² I think we must sadly conclude that constitutional defences today are rarely come by.

More seriously, all of you know that there has been tremendous pressure behind a proposed Constitutional amendment to limit federal income tax rates to 25 per cent. Present indications are that this will not be adopted, at least in the foreseeable future.

Fourthly, there is available for taxpayers the unilateral and dangerous road of outright fraud, that is, the filing of false and fraudulent returns, or none at all; obviously this is a highly personalized solution, with not much to recommend it.

Nevertheless, within the past year, a former Commissioner of Internal Revenue, a former assistant internal revenue agent in charge, a former special agent of the F. B. I., and many other citizens, have been charged with tax fraud. A number of these were professional men, like the doctor who was caught with bank deposits which were in excess of his reported income. He was tried and was acquitted of criminal tax evasion. The experience, however, taught him a lesson; thereafter he was careful not to deposit everything he received. He began keeping two sets of books, one for morning receipts which he deposited in the bank, and one for afternoon receipts which he did not deposit and which he did not report as income. The rather arbitrary AM and PM division did not appeal to the court, and this time he was convicted.³

As to the special problems of doctors, lawyers and other professionals, a Prince Georges County (Maryland) Circuit Court judge last week held that the crime of income tax evasion is not one involving moral turpitude, justifying the revocation of a doctor's license. The judge is reported to have stated:

While it may be said that the violation of any law is immoral and upon conviction a person may be lowered in the estimation of his fellows, it does not follow that in the case of a doctor his ability to serve the public is in any way diminished because of his conviction of the violation of his tax laws.⁴

Despite this finding, few professional men will be attracted to

2. Porth v. Broderick, 1954 CCH FED. TAX SERV. par. 9552.

3. Case reported in Kiplinger Tax Letter, July 10, 1954.

4. Washington Post and Times-Herald, Sept. 23, 1954.

tax evasion as a career collateral to their main one. Moreover, the Internal Revenue Service has for the fiscal year 1955 obtained additional appropriations of \$7,750,000 with which to hire 800 more revenue agents and 455 more special agents, the latter being for fraud work. All in all, the filing of an honest return still seems the best policy, whether viewed from a moral or a practical point of view.

Since neither recourse to the Constitution nor the ballot-box, nor the extra-legal procedures of insurrection and fraud, are appropriate alternatives, we turn, fifthly and finally, to a course founded upon the mature realization that our Government's needs, obligations and expenditures are unlikely to lessen drastically in the coming years, that our federal revenue structure must therefore remain highly productive, and that we must do all we can not only to keep it so, but also to improve it administratively, to make it more understandable, to make it more equitable, and at the same time to attempt to lessen any unnecessary adverse effect upon business, family and other transactions. That is the course adopted in the Internal Revenue Code of 1954; and our meeting here together today is part of that very same process, the process of doing the best with what we have, of understanding and applying it, and of improving it when we can.

Comments on Internal Revenue Code of 1954
Spirit in which this review should be
undertaken.

What I have just said suggests the spirit in which I think our two-day review of the new Code should be undertaken: a spirit of "cold-eyed humility", a phrase employed by John Fischer, the editor of Harpers Magazine, in a recent Kenyon College address which had nothing whatsoever to do with taxation but which nevertheless contained some wise advice applicable to this field as well as others.⁵ In discussing our current ideological conflicts, particularly those with the Russians, Mr. Fischer referred to what he termed the "American heresy", which is implicit in the placard sometimes found hanging in offices in this country, reading:

The difficult we do today;
the impossible will take a little longer.

This boast is an understandable one, since, as a people, there are few problems which we have not mastered. But despite our successful

5. *Ibid.*, p. 18.

history, some things cannot be quickly achieved. One of these is the solution of the Russian problem and another is the writing of a wholly satisfactory tax law. If we approach the new Internal Revenue Code of 1954 in the expectation that it gives us the inevitable happy ending to the American success story, the "and they lived happily ever after" theme, we shall be disappointed, and our disappointment may blind us to some of the solid accomplishments of the new tax law.

This recommended attitude of "cold-eyed humility" is particularly appropriate for any of us who may try to explain to you what the new tax Code means in its substantive provisions.

Firstly, it will take many years of interpretation by taxpayers, by the Revenue Service and by the courts before we fully understand the new law's effects in every situation, assuming we can ever do so.

Secondly, we know that in the meantime the new law will produce many results not intended by its draftsmen, results which will in some instances be pointed out to the experts either gleefully or sorrowfully by general practitioners who may never before have cracked open the Internal Revenue Code with anything more than mild curiosity.

Background of New Tax Code.

The real work on this tax bill, as with other tax bills, was not done on the floor of Congress. For example, while it has been estimated that $\frac{1}{2}$ million man-hours of work went into the new Code, the House of Representatives passed the bill with only 4 hours of debate.

Our federal tax laws are written in committee, and the committee reports are of tremendous assistance to practitioners in construing the new law. The three tax committees of Congress are the House Ways and Means Committee, the Senate Finance Committee and the Joint Committee on Internal Revenue Taxation. The latter committee maintains a staff of exceptionally able technicians who assist all three committees. In addition, the committees receive considerable help from the Legal Advisory Staff of the Treasury, the economists of the Treasury, members of the Legislation and Regulations Division of the Internal Revenue Chief Counsel's office, and from technical planning personnel on the staff of the Commissioner of Internal Revenue.

Further, the Congressional committees in this instance received a great deal of help from the American Bar Association, the American Institute of Accountants, and other professional organizations, especially the American Law Institute, which for many years has been working on a model Internal Revenue Code.

The work of the American Law Institute has been particularly significant because it represents an attempt to produce for Congress an initial or model draft of a tax law removed from the terrible pressures to which Congress is necessarily subject, pressures of time, of special interest groups, of cries by constituents, of log-rolling, of insufficient expert personnel, and of over-reaching and over-zealous claims by taxpayers and sometimes by the administration itself. When we realize the tremendous handicaps under which our Congress has to work, the things it is able to accomplish become particularly noteworthy.

In the present instance, what Congress has produced is the first comprehensive tax law revision since 1876, comprising almost 1,000 pages, renumbering every section except one (§ 32), and making over 3,000 technical changes in the law.

As stated by Russell Train, clerk of the Ways and Means Committee, in a speech to the Federal Bar Association in Washington in September:

Our objectives in undertaking this tremendous task of revision were twofold: first, to rearrange the existing law in order to place its provisions in a more logical sequence, delete obsolete material, and to try to express them in a more understandable manner; and secondly, to make substantive changes and fit them within the framework of the rearranged Code.

As further stated by Mr. Train, "one of the most important accomplishments of the rearrangement has been to bring together wherever possible the provisions dealing with the same general subject. For example, all of the provisions relating to banking institutions can now be found in a special subchapter, Subchapter H of Chapter One. Moreover, all of the provisions dealing with natural resources are now brought together in Subchapter F".

The administrative provisions have all been centralized, so that, for example, if you want to know about filing a return, whether pertaining to income, estate, gift or excise taxes, the place to look is Chapter 61.

This approach has permitted a great deal of consolidation. One illustration relates to interest, which was covered by some 50 differ-

ent provisions in the 1939 Code. In the 1954 version there is only one basic interest provision.

The largest single job accomplished by the rearrangement is in the income tax. Section 1 now starts right out, as it should, by imposing the tax, instead of throwing at you initially a frightening hodge-podge of cross-references and such like.

The Table of Contents in the official copy of the new Code runs to 38 pages. It shows that the new law is broken down into seven Subtitles, as follows:

- Subtitle A. Income Taxes
- Subtitle B. Estate and Gift Taxes
- Subtitle C. Employment Taxes
- Subtitle D. Miscellaneous Excise Taxes
- Subtitle E. Alcohol, Tobacco, and Certain Other Excise Taxes
- Subtitle F. Procedure and Administration
- Subtitle G. The Joint Committee on Internal Revenue Taxation

These seven Subtitles in turn are broken down into a total of 92 chapters. For the purpose of determining the structure of the Act, we might concentrate for a moment on Subtitle A, pertaining to income tax, since for most of us this is the more important one.

The income tax Subtitle contains six chapters as follows:

- Chapter 1. Normal Taxes and Surtaxes
- Chapter 2. Tax on Self-Employment Income
- Chapter 3. Withholding of Tax on Nonresident Aliens and Foreign Corporations and Tax-Free Covenant Bonds
- Chapter 4. Rules Applicable to Recovery of Excessive Profits on Government Contracts
- Chapter 5. Tax on Transfers to Avoid Income Tax
- Chapter 6. Consolidated Returns

Of these, most of the substantive items we will be looking for will be found in Chapter One, entitled "Normal Taxes and Surtaxes". Of the 928 pages comprising the new Code, 350 pages (or about 37%) is contained within this single Chapter One. This Chapter has 19 Subchapters, each devoted to a major income tax area. Each Subchapter is divided into smaller income tax areas, called Parts, and each Part, in turn, is broken down into sections.

In an appendix to the new Code there are contained three tables of cross-references from the 1939 Code section numbers to those of

the 1954 Code, from the 1954 Code to the 1939 Code, and various cross-references within the 1954 Code itself.

The men who will follow me this afternoon, tonight and tomorrow will, of course, give you the technical features in certain major areas of the new Code.

The Role of the Tax Practitioner in the Practice of Law.

The tax practitioner is first of all a lawyer, that is, a practitioner of the law in its fullest sense. In support of this, I read you a paragraph from a statement submitted to the Secretary of the Treasury in September by the American Bar Association on the subject of tax practice:

There can be no question but that tax law is *law* in the most vivid sense of the word. It has been suggested by some that tax law is a field of law separate and apart from the general body of law. To the contrary, tax law is a part of the seamless web of the law. It is not in any sense a unique or isolated topic. It cuts across virtually all branches of substantive law and necessarily weaves in their principles. The general law of the respective 48 States is inextricably a part of the body of federal tax law in that tax law interrelates the law of corporations, partnerships, trusts, wills and estates, gifts, future interests, real and personal property, divorce and a variety of other fields of substantive law.

Turning now to the specific role of the tax practitioner: One of his essential functions is to assist his clients to so plan their transactions as to produce the least tax. There is nothing morally wrong in this course. Judge Learned Hand has stated:

Everybody does so, rich or poor, and all do right, for nobody owes any public duty to pay more than the law demands; taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals, is mere cant.⁶

On the other hand, the tax practitioner must be extremely cautious in his evaluation of tax minimization and tax avoidance schemes in order to determine as precisely as possible whether these are likely to succeed.

As you know, some taxpayers have a horror of overpaying taxes

6. *Comm'r v. Newman*, 159 F. 2d 848, 850-51 (2d Cir. 1947). (Cited in Paul, *The Lawyer as a Tax Adviser*, 25 ROCKY MOUNT. L. REV. 4 (1953).

almost akin to a fear of being buried alive. Eventually they may develop a loophole-complex, which feeds on golf-club and luncheon table rumor as to what "the other chap is getting away with." Their tax consultants necessarily act as a buffer between such clients and a potential chain of events terminating in the fraud sections of the statute. There may be many tax minimization steps which the consultant might permit to be taken by a client who is insistent on tilting with the revenues. But if the matter turns out badly, inevitably the client forgets that he was permitted to take the action subject to stern warnings. Even when his files disclose this, he is likely to say: "You should not have let me do it." In the long run it is sounder procedure to try to change his personality to a more conservative one, and, if you fail in this, as you will, thereupon conclude that you and he will live more happily apart.⁷

There may be rare instances where, even though you are convinced that the particular tax minimization plan will work, you decide for public relations or other reasons that it would be better for the client not to go forward with it. A few years ago, for example, many taxpayers who knew that they could avoid the transportation tax on United States shipments if they paid the freight bill in Canada turned their backs on this loophole.

The tax practitioner remembers that, in a measure, he must act as the conscience of his client. Tax law is so diffuse, and, to the layman, so much a combination of fiction and fact, that the average client can scarcely be expected to know the difference between right and wrong in anything approaching a borderline transaction. To what extent, and under what circumstances, can the taxpayer have business dealings with his wife or with his wholly-owned corporation, a creature which he has created out of thin air. Sometimes in the case of the controlling stockholder of a company, who wishes to deal with it on his own behalf, problems not merely of tax conscience, but also of business ethics and fiduciary obligations arise in connection with minority stockholders. How can he honor these obligations and at the same time accomplish the business result which he desires? These are problems into which the tax consultant is thrown whether he desires to be or not. He should be broad gauged enough to see these problems, to point them out to the client, and to help him solve them. Sometimes it is necessary to remind part-

7. This paragraph and a number of others in this paper are almost exact quotations from an earlier lecture delivered by the author, entitled *Personality Aspects in Tax Determinations*, N.Y.U. 7TH ANNUAL INSTITUTE ON FEDERAL TAXATION p. 1063 (1949).

ners, for example, that they cannot deal with each other as strangers and that they have almost trusteeship responsibilities to one another. So complex are the relationships among people in our society that no tax adviser can perform his function without taking materially into account matters of ethics, conscience, and moral obligation, for eventually these merge into matters of law.

This suggests still another function of the tax practitioner: the prognostication of the future. In tax planning, it is not sufficient to know what the law is today. The important question is: What will be the state of the law when this transaction is in controversy, two, three, five or more years in the future. In estate planning this projection forward may even extend into several generations. This justifiable worry about the future is always particularly acute in transactions which are close to the borderline of tax avoidance, because of the constant fight which the courts, the Treasury and the Congress are waging to close "loopholes." Neither clients nor their tax counsel have a vested interest in the perpetuation of loopholes. As one practitioner has stated it: "The tax bar is in a constant state of disappointment."

Tax counsel should remain keenly aware of the philosophical battle which has been raging for years on the question whether the Treasury, the judiciary or the legislature constitutes the instrumentality best equipped to close so-called loopholes. It is probable that this battle will continue to rage throughout our lifetimes; that the Treasury from time to time will exercise its regulatory powers to the utmost in a legislative sense in a particular area, as in the regulations issued after the Supreme Court decided the *Clifford*⁸ and *Hallock*⁹ cases; that the courts will continue to legislate when they are so minded; and that the Congress will amend the tax laws only when it finds time to do so, that is, in general, when the pressure for revenue and legislative reform becomes rather overwhelming. It is incumbent upon tax counsel to decide whether the current tax interpretation, which he wishes to have available to his client upon future audit of the transaction, will at that time still be followed, or whether such interpretation is likely to be disturbed by the Treasury, by the courts, or by the Congress. If the latter, he might be willing to go forward with the transaction, upon the theory that the Congressional enactment would not have retroactive effect, whereas he could not assume so readily that a new Treasury attitude or a new court

8. *Helvering v. Clifford*, 309 U.S. 331 (1940).

9. *Helvering v. Hallock*, 309 U.S. 106 (1940).

decision would be applied non-retroactively by the Treasury, although it has the power to do so, and often exercises that power.

In the final analysis, no tax plan is perfectly secure. Every step involves some risks, and it is a function of the tax adviser to evaluate those risks wisely and realistically, in the light of the current law and the future possibilities, so as not unduly to impede proper business transactions, and so as not to encourage other transactions whose tax dangers are too great.

Still another function of tax counsel involves a sort of self-abnegation or self-denial. His advice should take such form that the tax phase does not unnecessarily dominate every other aspect of the family or business relationship. We all know how difficult it is to follow such a policy in a period of high tax rates. Despite the obvious difficulties, the tax lawyer should do what he can to prevent clients from taking unwise business or family action purely for tax reasons.

Sometimes the proper performance of his duties places the tax practitioner in the odd position of giving divergent advice or opinions to X and Y on identical problems and yet feeling himself to be "right" in each instance. The divergence may be based on an evaluation of each client's particular personality, background, reputation, prior tax controversies, and so on. Let us assume a concrete case:

X is the chairman of the board of a large oil company. His reputation is excellent, partly due to the public relations of his company. Y is the owner of a retail store which almost continuously runs "removal" and "going out of business" sales. As a result, the community's faith in Y's truthfulness has been somewhat shaken. X and Y both desire to buy, and to operate as businesses, farms on which they plan to live. They approach the same tax consultant for the purpose of determining whether the farm losses, if any, will be deductible. All other things being equal, the tax adviser, knowing the importance of X's and Y's own reputation, demeanor and testimony in the ultimate evaluation of their respective profit-making intentions, might well advise X that he could safely rely on getting the deduction and Y that he could not.

Thus the practitioner consciously or subconsciously may frequently ask himself the question: "Is my client the kind of man (or corporation) whom people customarily believe?" The reputation and appearance of truth unfortunately are sometimes more effective than truth itself. Expressed differently: What you *are* (or seem to be) speaks louder than what you say. While, as one writer has expressed it, actually there is no truthfulness as great as the "truthfulness of

a tired liar",¹⁰ his clergyman probably is much more ready to respect his conversion than is the Internal Revenue Service.

The problem of the "flighty" client provides yet another illustration of divergent advice based on the taxpayer's personality and background. There are many instances in which the nature of the advice which the tax consultant wishes to give is such that he must have assurance that the taxpayer will carry out the plan precisely as outlined. This may relate to the substance of the plan or merely to matters of record-keeping. If his knowledge of the taxpayer is such that he believes the taxpayer cannot be controlled to this extent, the tax consultant may well hesitate to give advice which requires exact compliance, particularly compliance over a period of time.

We might draw from what has just been said the further and broader implication that the tax adviser must have a great deal more knowledge regarding the client than may be acquired at one sitting, including information as to phases of the client's activities and background which initially appear little related to the immediate tax problem. In a sense this may be merely another aspect of Justice Brandeis' belief, voiced as a practicing lawyer in Boston: — that one who desires to advise a client as to particular business problems should try to know more about *all* of the client's business than does the client himself.

The matter of advising and supervising the keeping of necessary records for tax purposes has already been mentioned. Good records sometimes keep a tax controversy from developing; and, of course, the best way to win a tax case is to keep it from ever arising.

But in building up a record which will contemporaneously and honestly reflect the facts, and which will be available in the event of a review of the transaction years later, the parties presumably attempt to act "normally", that is, they attempt to keep records and conduct their transactions in the manner characteristic of persons whose actions are business-motivated rather than tax-motivated. Again the concept of normality must be related to the particular taxpayer's business personality and to the community in which that personality operates. If a closely-held corporation keeps only very sketchy minutes on every subject except dividend policy, as to which it maintains voluminous and virtually exact extracts from conversations at board of directors meetings indicating why the directors did not declare a dividend, there may be some basis for suspicion that such

10. Phrase used by the Austrian writer, Arthur Schnitzler, as quoted by Dr. Theodore Reik, in *LISTENING WITH THE THIRD EAR: THE INNER EXPERIENCE OF A PSYCHO-ANALYST* (Farrar, Straus and Co., 1948).

corporate minutes are merely self-serving documents intended for the eyes of the Internal Revenue Service and are not to be accorded the weight which the courts normally give contemporaneously-written business records.

A further comment we might make is that the tax lawyer, like every other lawyer, if he is to be successful, must be bold enough to place himself on record by giving his client definite advice, instead of making the client guess his own way through various difficult problems conjured up by the lawyer. If it is impossible to decide which is the *best* course, the tax lawyer should at least suggest the course "with the *least undesirable* set of consequences."¹¹

Another important role of tax counsel is that of acting as taxpayer's advocate before the Internal Revenue Service.¹²

We might start out in this area with homely maxim No. 1: That Internal Revenue employees have neither horns nor wings. The practitioner sometimes looks upon the personnel of the Internal Revenue Service as arbitrary, unfair, unsympathetic and grasping. Actually, they are no more and no less so than are the taxpayers and counsel with whom they deal. The Internal Revenue men have a particularly difficult role to play because they are at one and the same time the Government's investigator, its advocate, and the judge of the controversy. They have superiors to satisfy, work-loads to carry, reports to write, deadlines to meet, and wives to explain to, just like many of the rest of us. Thus it should be possible for us to envision ourselves in their position. Once this is done a long step has been taken toward resolution of the controversy with the Government.

Maxim No. 2 is that one should not underestimate the examining agent. This advice is applicable in respect of all the individuals in the audit and settlement hierarchy of the Internal Revenue Service, but the warning may be particularly necessary as to examining agents. The fact that the agent's work is subject to review may lead an inexperienced practitioner to conclude that time spent with an agent is wasted, and that the taxpayer's fire should be held until he sees the whites of the group chief's eyes. In the normal case, this would be a grave error, for the examining agent in many respects is the most important man in the Internal Revenue Service. If he fails

11. Merle Miller, *What Makes a Successful Tax Lawyer*, 7 TAX L. REV. 1, 16 (1951).

12. The remainder of this paper consists largely of extracts from a prior address presented by the author under the title of *Negotiations and Settlements at the Administrative Level*, THIRD ANNUAL, TULANE TAX INSTITUTE (1954). (Matthew Bender & Co., Inc.).

to raise an issue, ordinarily it remains undisturbed. Accordingly, if he accepts a return as filed, it usually stays that way. His findings of fact favorable to the taxpayer customarily are approved by his reviewers; and his findings of fact adverse to the taxpayer create a written record against which the taxpayer must work throughout the life of the case.

If convenient, the practitioner should, I think, be present at the very first interview by the agent and at all subsequent conferences. I doubt, as some have feared, that the early appearance of the practitioner makes the agent suspicious that something is wrong, or provokes him to a more thorough examination than he would otherwise undertake, although this is a possibility. In any event, the early presence of the practitioner makes it unnecessary for the client to pass on to his tax man what the agent first said or asked for, and to garble it in the process. Moreover, because of the production schedule which examining agents attempt to maintain and the consequent stringent time limitations under which they operate, they need and welcome work papers, financial statements and all the other help they can get.

How about bringing the client and the agent together? As the Circuit Court of Appeals for the 9th Circuit has said: A conference with a Treasury agent is "no social conversation".¹³ With good reason, therefore, many practitioners think that clients and revenue agents should be kept physically as far apart as possible. For one thing, some clients complicate the investigation by volunteering irrelevant information. Furthermore, a client generally will come away from a conference with an impression totally different from that of the tax practitioner as to what the examining agent said, asked and did, thereby producing misunderstandings and conflicts of judgment between client and practitioner. There have been instances where the emotional gap between the client and the agent is so great that the client has drawn from a relatively innocuous series of remarks the conclusion that he has been called a liar and a crook, and that the agent has asked for a bribe; none of which happened.

A high-bracket client has so much at stake that his presence even at a routine examination may be harrowing enough to shatter his equilibrium. Furthermore, he often feels that the practitioner is too casual about the whole thing and he lets the practitioner know it, in words which are neither few nor well-chosen. Quite naturally, thereafter, the client's presence has a disruptive effect at conferences, in so far as the practitioner consciously or unconsciously may feel

13. *Cohen v. U. S.*, 201 F. 2d 386 (9th Cir. 1953), *cert. denied*.

it necessary to indulge in some hell and thunder histrionics, sometimes in the form of table-pounding, intended to keep his client happy, but with little advantage otherwise to the case. Conversely, the agent, restive perhaps under the fixed and somber stare of the taxpayer, occasionally reacts as if he were a vigorous participant on the television show "Treasury Men in Action". For the foregoing reasons, it appears better to have the meetings with agents viewed as being technical in nature and hence to be attended only by lawyers and accountants, and other trained personnel, wherever possible.

The human interaction among the parties is important only as it affects the agent's work. If he is made reasonably (but not lavishly) comfortable, if appointments arranged with him are kept, if the information he needs is promptly supplied, if he has no reason to believe his inquiries are being evaded or to question the sincerity of the replies to such inquiries, if, in summary, the reception accorded him shows that both he and his job are respected, he is unlikely to become over-zealous and prosecutive at your client's expense. Of course, he may be satisfied as to all the foregoing and still come up with a proposed deficiency of such handsome proportions as to be of interest to the Bureau of the Budget and the foreign aid program; but, for what it is worth, you will have the satisfaction of knowing that such a proposed deficiency was produced by a clash on issues and not by a crash of personalities.

The initial function of the agent is to find out what happened. Most of the controversies in the world, other than those between a man and a woman, are won on the facts. Once the facts are established in a tax case, the applicable rule of law usually becomes obvious. No matter how fugitive, ethereal or obscure the facts are, the practitioner must relentlessly search them out. He cannot depend on the agent to do it for him. He cannot even wholly depend for this purpose upon the client, who may be too busy, too forgetful, or too interested in winning the case. Sometimes, also, the client is embarrassed by some past event, and, to avoid telling about it, convinces himself of its unimportance. But, as his dealings with human beings accumulate, the practitioner seems to achieve an alertness and an awareness of the specific areas in which he must probe for more information.

Maxim No. 3, therefore, is that, almost to the close of a case, the practitioner should be alive to the possibility that somewhere there is an undiscovered fact which will simplify or win the controversy for him. His perseverance, plus his instinct and intuition, will help him ferret out that hidden fact, if it exists.

There is next the job of assembling the facts. Since the world is a welter of facts, it is a real task to segregate those few which are pertinent to the particular tax problem. Too many facts may be as bad as too few, bearing in mind that the employees and officials of the Internal Revenue Service are busy people who read as they run.

Necessarily the functions of ascertaining and assembling the facts must be kept separate from the function of pleading the facts, that is, separate from the function of presenting the facts in their best light. The latter is a vital activity, perhaps the most important one performed by an advocate. But the man who starts the process of pleading or arguing his facts before he *knows* his facts may find he is riding what the Chinese call a "paper tiger" instead of a real one that can bite in the way that honest facts bite. In other words, never having subjected himself to the discipline of the real facts of the case, he is the first victim of his own propaganda. The moral here is: know the weaknesses and strengths of your actual facts, before you try to dress them up in their Sunday-go-to-meetin' clothes.

The final step in presenting the facts to the Revenue Service is proving them. The nature and effectiveness of your proof will vary depending on the level of the Revenue Service at which you present it. At the agent's level, the most persuasive evidence is simple and tangible.

Regardless of the Internal Revenue level at which you are presenting the matter, however, your own mental attitude profitably may be that this is a case which eventually will be tried in court. This approach will help you in collecting your evidence, and incidentally will suggest to the people on the other side of the table the seriousness of your intentions. Furthermore, you may conclude, for any one of a number of reasons, that the evidence gathered by the Government is legally inadmissible in a trial and you may therefore be able to convince the tax officials that for this reason the issue raised by them should be abandoned.

We might chat for a moment about attempts to settle with the agent. While the agent's function is supposed to be primarily investigative, in practice he frequently initiates, or lets the taxpayers initiate, settlements of the issues which he has raised. Generally, it is good policy to reach an agreement with the agent, if this can be done on a reasonable basis. It may save the client a considerable amount in interest, fees and other costs. It may also avoid a contest as to new and very serious issues which might be brought out in the event of higher review. The agent, moreover, being understandably

desirous of improving his production record of closed cases, particularly one in which his own audit has produced a money issue for the Government, may be more willing to make appropriate concessions than is a conferee handling at his leisure a formidable written record which the agent has worked up against the taxpayer. On the other hand, sometimes the agent is so enthralled by the theories and arguments which he has developed that he lacks objectivity regarding them. The taxpayer then must take his case elsewhere for settlement.

But the agent may be rightfully resentful if you habitually close cases with the group chiefs or appellate division conferees on precisely the same basis which the agent had offered you. Under these circumstances, he may conclude that he is wasting his time in trying in good faith to negotiate with you.

There may be some misunderstanding about *equitable arguments*. Contrary to popular impression, taxpayer arguments addressed to the equities are, it seems to me, more likely to be sympathetically listened to by the agent than by anyone else in the settlement process. The agent knows as well as you do that the equities are not necessarily determinative of tax issues. On the other hand, he frequently must "shoot from the hip", and, lacking both a well-equipped law library and the leisure to enjoy it, he is impelled at times to indulge the assumption that the equities and the law go hand in hand.

One writer has said that —

"Professor T. R. Powell occasionally tells his classes at the Harvard Law School that in many cases the reasoning of the courts is bottomed upon a major premise of 'My God!' "¹⁴

Revenue Agents act like this, too. Conversely, if their instinctive emotional reaction tells them the case is "all right", they are likely to end up still thinking that way.

By what ethical standards is the practitioner guided in presenting his case to the Internal Revenue Service? Clearly a practitioner is acting improperly if he withholds from the tax authorities a fact which is determinative of the issue before them. An illustration by one commentator is that of a dispute as to a depreciation deduction taken on the tax return for a building which, the practitioner later discovers, was torn down prior to the year in question. Obviously he must impart such information to the agent or conferee.

14. Ivins, *The Business Purpose Rule in Corporate Recapitalizations*, N.Y.U. 7TH ANNUAL INSTITUTE ON FEDERAL TAXATION, 1161 (1949).

The more difficult question is whether the practitioner is required to offer wholly unsolicited information which is adverse to the client's position but which is not determinative of the tax issue. Opinions differ on this. The practitioner may attempt to escape the dilemma by rhetorically asking himself why the taxpayer's representatives should be expected to supply a strongly prejudiced Government man with a weapon with which to assail a sound position maintained by the taxpayer? But this response is too glib, based as it is on two easy assumptions dear to the hearts and minds of many practitioners (1) that the taxpayer's position is always sound and (2) that the Government man is always strongly prejudiced. Frequently he is only mildly partisan.

If the practitioner rather deliberately purports to give "the facts of the case", as distinguished from "the facts upon which the taxpayer relies", it seems clear that he should set forth all the facts which are material to the determination, including those which are adverse to the taxpayer. Some practitioners by their demeanor and by their presentation make so frankly clear their partisanship that the agent or conferee is not misled into believing that their factual account is either objective or complete, and the Government is thereby placed on notice that further factual inquiry must be made. The demeanor and presentation of other practitioners, however, may be such as to lead the agent or conferee to the reasonable belief that he is being advised as to all the material facts known to the practitioner. In the latter event, the withholding of pertinent information obviously is improper and, if discovered, at the least will adversely affect the practitioner's relations with the Internal Revenue representative on this and all future cases.

The practitioner must make up his mind, therefore, as to what his relationship with the Internal Revenue Service is to be. If both sides know that this relationship is one of wholly arm's length dealing (and frequently there are advantages, both legally and morally defensible, in this), the advocate's obligations of disclosure will be considerably less than those of the practitioner who prefers not to deal at arm's length. The latter course has much in its favor, but carries with it responsibilities not usually assumed by the advocate in a controversy between two private parties.

These comments are not intended to be definitive, but merely to set out some of the facets of the problem. Those of you who want to delve into this provocative subject of ethics in tax representation

should begin by reading the growing literature on it.¹⁵ You will find, however, that you have to supply many of the answers yourselves.

Closely allied to the problem just mentioned is whether a tax practitioner need "believe in every argument he presents," a question fascinatingly raised, discussed, and answered in the negative, by Randolph Paul in a recent issue of the *Rocky Mountain Law Journal*.¹⁶

As all of you know, if you cannot settle the case with the agent, or with his immediate superior, the group chief, the taxpayer receives a letter giving him 30 days within which to file protest and to request assignment of the case to the Appellate Division of the Internal Revenue Service. If the taxpayer elects to file neither a protest nor a Form 870 (or its equivalent) agreeing to the agent's proposals, a statutory notice of deficiency will be forthcoming, upon the basis of which a petition may be filed with the Tax Court within 90 days.

The Appellate Division of the Internal Revenue Service has jurisdiction of cases docketed in the Tax Court as well as protested cases referred to the Division in the pre-Tax Court stage. Should the taxpayer take his case to the Appellate Division via the protest route or through the Tax Court petition route?

The protest route has two advantages: (1) It gives the taxpayer two bites at the apple, that is, two settlement opportunities at the Appellate Division level, one before and one after issuance of the statutory notice of deficiency. Internal revenue lawyers, acting for the Appellate Counsel, ordinarily do not participate in the first settlement phase in the Appellate Division but do in the second, so that the second go-round there is not necessarily an unsuccessful repetition of the first. (2) The protest route leaves the taxpayer free, until the last moment, to pay the proposed deficiency and ultimately sue in a federal district court or the Court of Claims, if the late trend of decisions in either of these tribunals is more favorable to the taxpayer than the trend in the Tax Court on the issue in question.

On the other hand, the considerations in favor of the Tax Court petition route to the Appellate Division, in lieu of the protest route, are as follows:

15. *Ethical Problems of Tax Practitioners*, 8 TAX L. REV. 1 (1952); Paul, *The Responsibilities of the Tax Adviser*, PROCEEDING OF THE TAX INSTITUTE, UNIVERSITY OF SOUTHERN CALIFORNIA SCHOOL OF LAW 1 (1950); Darrell, *Some Responsibilities of the Tax Adviser in Regard to Tax Minimization Devices*, N.Y.U. 8TH ANNUAL INSTITUTE ON FEDERAL TAXATION 983 (1950); Miller, Robert N., *The Successful Tax Lawyer—His Character and Personal Relationships*, 7 TAX L. REV. 9 (1951); Miller, Merle H., *Morality in Tax Planning*, N.Y.U. 10TH ANNUAL INSTITUTE ON FEDERAL TAXATION 1067 (1952); Paul, *The Lawyer as a Tax Adviser*, 25 ROCKY MT. L. REV. 1 (1953); Curtis, *The Ethics of Advocacy*, 4 STAN. L. REV. 3 (1951).

16. Paul, *The Lawyer as a Tax Adviser*, 25 ROCKY MT. L. REV. 1, 20 (1953).

(1) There is less delay, if one of the settlement attempts is eliminated. Moreover, the Appellate Division accords precedence to cases docketed in the Tax Court.

(2) More certainty attaches to the settlement of a docketed case, since it has the sanction and finality of a Tax Court judgment.

(3) An early appeal to the Tax Court tends to evidence the taxpayer's confidence in his case and his readiness to litigate it.

(4) If a protest is filed and it later becomes necessary for the Government to send a statutory notice of deficiency, this will be prepared and issued by the Appellate Division. On the other hand, if no protest is filed, the statutory notice will be prepared and issued by the District Director's office. In general, the statutory notices emanating from the District Director's office are not as carefully prepared (either in respect of issues or amounts) as those drafted by the Appellate Division, which has the benefit of added consideration of the case and of review by the Appellate Counsel. While the Commissioner may, with the consent of the Tax Court, amend the statutory notice, this consent is not automatically given, and, even when it is given, the Commissioner has the burden of proof as to amounts added to the deficiency. Hence, there is some advantage to the taxpayer in having the statutory notice drawn early in the case, and by the District Director's office.

What we have been discussing is, of course, closely related to the question as to which court you want to have try the case. Generally you will pick the court in which you have the best chance of winning, on the basis of the comparative trend of decisions among the several forums: The Tax Court, Federal district court, or the Court of Claims.

Sometimes you will want a jury trial, which means that you must pay the tax, make claim for refund, and then file suit in federal district court within two years from the time the refund claim is denied.

If you want to go to the Court of Claims, which takes testimony and evidence through Commissioners, you must also pay the tax, then make a claim and thereafter file suit. As you know, there is no intervening level of appellate court between the Court of Claims and the Supreme Court. Thus, there is no assured appeal from the Court of Claims, although review may be sought by petition for certiorari to the Supreme Court. On the other hand, there is an appeal as a matter of right from the Tax Court and the federal district courts to the several circuit courts of appeal.

The major advantage of taking your case to the Tax Court is that you need not pay the tax in advance. In addition, your case is there

heard by specialists who are particularly well versed in tax law because they hear only tax cases. You may or may not view this as an advantage, but the specialized character of the court doubtless will be taken into consideration by you in exercising your election to go there or elsewhere. If you have a case which is weak technically but which is strong on human appeal, I suppose you would ordinarily want to avoid the Tax Court and choose the district court, in order to avail yourself of the jury privilege.

Another element to take into account is that the Revenue Service's own lawyers argue the cases in the Tax Court, whereas those in the Court of Claims are handled by lawyers from the Tax Division of the Department of Justice in Washington, and the cases in the federal district courts are handled either by the local district attorney's staff, or by men sent out from the Justice Department's tax division in Washington, or by both.

Of course, the courts are your last resort, and before going there normally you will have many settlement opportunities within the Revenue Service itself. If his settlement attempts are to be persuasive, the advocate must bear in mind that, like other people, members of the Internal Revenue Service are guided by emotions and by past individual experience as well as by logic and reason. Frequently the emotional forces are dominant. If the practitioner knows what these forces are, he can appreciate their role in inter-personal relations and can take account of the unspoken way in which they affect decisions. People are unlike in the degree to which past experience and other factors have caused them to be envious or satisfied, cynical or trusting, self-seeking or unselfish, grasping or fair, biased or objective, and so on through the ranges of human conduct. On the other hand, most people are alike in certain desires: they want to be respected and not made to feel small, to do a good job which will be properly recompensed, and to maintain their integrity as individuals instead of being unrecognized cogs in a population of 160 millions. The Internal Revenue practitioner, like the jury lawyer, will do better in his cases if he remains conscious of all these things.

In a Tax Law Review discussion two years ago, Chief Justice Arthur T. Vanderbilt of the Supreme Court of New Jersey made the following oral observation:

I have often tried, as I watched my adversaries — and taking a licking now and then — to find out what is the distinguishing trait that makes some men just have that little plus-factor that makes them win the doubtful case. Sometimes it is knowledge

of the law. More often it is likely to be a grasp of the facts. Sometimes it is this element of persistence, but I am inclined to think, fundamentally, the thing that distinguishes the true advocate from the just-so advocate is a sort of semi-instinctive knowledge of the well-springs of human nature, the things which really control people, and make them reach the decisions on which they act.¹⁷

This quotation sums up, better than anything else I have read, the element which marks the successful practitioner before the Internal Revenue Service.

17. 7 TAX L. REV. 1, 12 (1951).