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THE *DE NOVO* DOCTRINE: IRRELEVANT TO RELEVANCY IN CIVIL TAX LITIGATION

by

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I. INTRODUCTION

“A tax case is a de novo proceeding and the thoughts, procedures, conclusions, reasoning, or factual findings of Internal Revenue Service employees about a taxpayer’s liability are irrelevant.”

Any attorney who has handled a tax case on a taxpayer’s behalf has likely heard this argument, or a variation of it, during the discovery process, during motion practice, or even in the courtroom when attempting to introduce evidence.¹ Many attorneys from the Internal Revenue Service

1. *See, e.g.,* R.E. Dietz Corp. v. United States, 939 F.2d 1, 4 (2d Cir. 1991) (“The factual and legal analysis employed by the Commissioner is of no consequence to the district court.” (citing Nat’l Right to Work Legal Def. & Educ. Found. v. United States, 487 F. Supp. 801, 805 (E.D.N.C. 1979))); LPCiminelli Interests, Inc. v. United States, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,671, 110 A.F.T.R.2d (RIA) 2012-6631, 6633 (W.D.N.Y. 2012) (“[T]he factual considerations and legal analysis employed by the audit team during their examination . . . must be deemed ‘of no consequence’ to the *de novo* review required in this refund action . . .”); United States v. Nordberg, 96-1 U.S. Tax Cas. (CCH) ¶ 50,295 at 84,085, 77 A.F.T.R.2d (RIA) 96-2158, 96-2160 (D. Mass. 1996) (“In light of the principle that a challenge to a tax determination results in a trial de novo rather than a review by this Court of an existing administrative record, the defendants’ discovery requests fail to satisfy the mandate of Fed. R. Civ. P. 26(b) that information sought to be discovered by relevant or ‘reasonably calculated to lead to the discovery of admissible evidence.’ (citations omitted)); Garity v. United States, 81-2 U.S. Tax Cas. (CCH) ¶ 9599 at 88,005-06, 46 A.F.T.R.2d (P-H) 80-5143, 80-5145 (E.D. Mich. 1980) (“The Court holds that the opinions, impressions, conclusions and reasoning of IRS agents are irrelevant to the validity of the assessment against plaintiff.”); Vons Companies, Inc. v. United States, 51 Fed. Cl. 1, 5-6 (Fed. Cl. 2001) (“We begin with the axiomatic principle that tax refund cases are de novo proceedings. . . . As such, this court’s determination of plaintiff’s tax liability must be based upon the facts and merits presented to the court and does not require (or even ordinarily permit) this court to review findings or a record previously developed at the administrative level.” (citation omitted)); Int’l Paper Co. v. United States, 36 Fed. Cl. 313, 320

(“Service”) or Department of Justice who defend or bring tax cases on the government’s behalf have likely asserted some version of the “*de novo* doctrine.” Indeed, the Service and Department of Justice commonly raise the *de novo* doctrine in an attempt to defeat taxpayers’ requests to discover or introduce into evidence information about the Service’s audit or facts and information gathered by the Service and contained in its audit file.² The asserted ground for withholding such information from taxpayers is that none of it is relevant to the court’s inquiry, which is to determine the merits of taxpayers’ liabilities.

If successful, in this context the *de novo* doctrine is a powerful and broad tool. It is powerful because, if it applies, the *de novo* doctrine thwarts taxpayers’ discovery requests on relevancy grounds, and allows the government to withhold from its adversaries in tax litigation information to which the government has access. The *de novo* doctrine is broad because, unlike the attorney-client privilege and work product doctrines, courts often apply the *de novo* doctrine to shield from discovery purely factual information, as well as information that should not typically be discoverable, such as analysis, reasoning, or the Service’s motives for initiating an examination.³ Moreover, because relevant evidence under the discovery and

(Fed. Cl. 1996) (“[T]he factual findings, if any, underlying the Commissioner’s determination of tax liability are irrelevant and entitled to no evidentiary weight. This position is, of course, fully consistent with the *de novo* nature of tax refund proceedings in the Court of Federal Claims (as well as in the district courts). . .”); *Flamingo Fishing Corp. v. United States*, 31 Fed. Cl. 655, 658 (Fed. Cl. 1994) (“‘The opinions, conclusions and reasoning of government officials are not subject to discovery.’ . . . ‘The opinions, impressions, conclusions, and reasoning of IRS agents are irrelevant. . . .’” (quotations omitted)).

2. *See, e.g.*, Defendant United States of America’s Motion in Limine to Exclude Certain Witness Testimony, Certain Exhibits and All Deposition Testimony Designations as Evidence at 3, *LPCiminelli Interests, Inc. v. United States*, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,671, 110 A.F.T.R.2d (RIA) 2012-6631 (W.D.N.Y. 2012) (No. 09-CV-274) [hereinafter Motion in Limine] (“‘The factual and legal analysis employed by the Commissioner [in the examination of a taxpayer’s return and the assessment of tax] is of no consequence to the district court.’ As a result, any witness testimony or documentary evidence which the plaintiff seeks to introduce concerning the actions of the IRS during the examination of its tax return and the assessment of tax are not relevant to the fact finder.” (citation omitted)); Response of the United States to Panasonic’s Motion to Compel (§ 6103) at 4–5, *Panasonic Comm’n Corp. v. United States*, 99 Fed. Cl. 422 (Fed. Cl. 2011) (No. 09-793T).

3. *See, e.g.*, *R.E. Dietz Corp.*, 939 F.2d at 4 (“The factual and legal analysis employed by the Commissioner is of no consequence to the district court.” (citing *Nat’l Right to Work Legal Def. & Educ. Found. v. United States*, 487 F.Supp. 801, 805 (E.D.N.C. 1979))); *ISI Corp. v. United States*, 503 F.2d 558, 558 n.3 (9th Cir. 1974) (noting the district court refused to require Service’s agent to answer purely factual questions in deposition, such as “[d]id you make any independent

evidentiary rules is defined broadly, any weapon that exempts material from the scope of relevancy can, by its nature, preclude inquiry into a wide range of facts and information.

Despite the doctrine's advantages, breadth, and the fact that it is regularly asserted, the *de novo* doctrine has received little discussion among practitioners and scholars. The goal of this article is to help fill this void by examining the *de novo* doctrine's origins, merits, and vitality as a doctrine of relevancy in tax litigation.

As it turns out, courts often struggle to apply the *de novo* doctrine in a coherent manner and often shield from discovery or introduction factual material that would be otherwise discoverable under any established definition of relevancy. Courts fail to distinguish taxpayers genuinely hunting for information that can prove or disprove the merits of the Service's determination from recalcitrant taxpayers who seek information about the Service's motives or judgment behind initiating an audit or making an adjustment. Moreover, the current articulation of the *de novo* doctrine — as a doctrine of relevancy — has weak historical and precedential footing. The *de novo* doctrine arose in cases that expanded, rather than restricted, the scope of inquiry in tax cases. The first opinions to articulate the *de novo* doctrine did not do so in the relevancy context but, rather, simply explained that in tax cases courts review the merits of the Service's determination, rather than its motives or judgment. At some point, however, what had historically been a well-established and uncontroversial standard of review mutated into a standard of relevancy that shields from discovery or introduction into evidence facts and information that might prove or disprove the merits of the Service's determination.

As explained below, the *de novo* doctrine's underlying premise — that relevancy adequately supports withholding from a taxpayer or a court information the Service has itself deemed relevant to the taxpayer's examination — is suspect given the broad definitions of relevancy under applicable legal rules, the instances where information in the Service's files is directly relevant to issues in tax cases, and well-established notions of fundamental fairness. Finally, the *de novo* doctrine's continued vitality is further undercut by the deference the Service and Department of Justice are increasingly seeking and receiving in tax litigation today. If the Service argues that courts should defer to the Service's thoughts, procedures, conclusions, reasoning, or factual findings about a taxpayer's liability, perhaps taxpayers and courts should have the opportunity to examine in detail those thoughts, procedures, conclusions, reasoning, or factual findings

determination of your own whether the personal property of \$300,000 as allocated in the agreement, was in fact worth \$300,000 at the date of purchase" and "[a]t any time did you review the contract between ISI and Miller for the sale of the personal property, the leasehold and the investor records").

as applied on a case-by-case basis. At the very least, the *de novo* doctrine should not preclude such an examination on relevancy grounds.

To be clear, this article does not suggest that taxpayers or courts should be given wholesale access to materials and information gathered by the Service during an audit or during the pendency of a tax case. The Service and the Department of Justice have in their quivers other privileges to defeat unwarranted disclosures, such as the deliberative process privilege, the attorney-client privilege, and the work product doctrine, each of which stand on stronger precedential and policy footings than the *de novo* doctrine as a relevancy standard.⁴ Nor does this article suggest that the government or courts should be bound by materials and information gathered or created by the Service during an audit, or by statements made by the Service during an audit.⁵ Rather, this article concludes that articulating the *de novo* doctrine as a doctrine of relevancy is misguided based on the cases in which the doctrine arose, well-established evidentiary and discovery principles, and the current state of affairs in tax litigation. In other words, the *de novo* doctrine is not relevant to relevancy.

4. *See, e.g.*, *Procter & Gamble Co. v. United States*, 2010-1 U.S. Tax Cas. ¶ 50,146, 105 A.F.T.R.2d 2010-330 (S.D. Ohio 2009) (determining that documents related to the Service's appraisals of artwork and intellectual property were relevant under FED. R. CIV. P. 26(b)(1) over the Department of Justice's *de novo* objection, but analyzing deliberative process).

5. *See, e.g.*, *Boulez v. Commissioner*, 810 F.2d 209 (D.C. Cir. 1987) (refusing to bind the Service to an oral compromise agreement between the taxpayer and the Service's director of international operations); *Herbert v. United States*, 662 F. Supp. 573, 583 (S.D.N.Y.1987) (stating that the government is not "bound or estopped by a position taken . . . by one of its employees or agents" (citing *Heckler v. Cmty. Health Serv.*, 467 U.S. 51, 59-61 (1984); *Schweiker v. Hansen*, 450 U.S. 785, 788-89 (1981) (per curiam))); *Louderback v. United States*, 500 F. Supp. 575, 579 (D. Colo. 1980) ("[A]n Internal Revenue Service agent does not have authority to make a final determination binding on the government. . . ."); *Order of Dismissal for Lack of Jurisdiction at 2, Maser v. Commissioner*, No. 19497-11S (Nov. 29, 2011) ("The law is clear that erroneous legal advice rendered by employees of the IRS generally is not binding on the Commissioner." (citing *Dixon v. United States*, 381 U.S. 68, 72-73 (1965); *Schuster v. Commissioner*, 312 F.2d 311 (9th Cir. 1962); *Fortugno v. Commissioner*, 41 T.C. 316 (1963), *aff'd* 353 F.2d 429 (3d Cir. 1965))). *See also* *Greene v. Commissioner*, 55 T.C. Memo (CCH) 1374, 1376, T.C. Memo (P-H) ¶ 88,331 at 88-1640 (1988) ("It is well settled that, where a taxpayer relies to his detriment on an Internal Revenue Service publication, the contents of the publication do not bar respondent from collecting tax lawfully due. While petitioner did not point out the specific language he relied on in the publications, to the extent the publications may have been misleading, authoritative tax law is contained in statutes, regulations, and judicial decisions and not in information publication. Internal Revenue Service publications are merely guides published by the Service to aid taxpayers." (citations omitted)).

Part II of this article describes the origins of the *de novo* doctrine in Tax Court and in Federal district courts and the Court of Federal Claims, which suggest it is unwarranted to apply the doctrine to preclude discovery or introduction of facts and information that might prove the merits of a tax case. Part III of this article examines several recent contexts in which courts have struggled to apply the *de novo* doctrine in a coherent, justifiable manner to discovery or evidentiary disputes. Part IV introduces other problems with applying the *de novo* doctrine as a doctrine of relevancy that courts have not addressed, including how to reconcile the doctrine with instances in which the Service asks courts to defer to its litigating position or when the Service assumes a litigating stance that is contrary to the position it took during audit. Part V of this article concludes that courts should return to the *de novo* doctrine's origins and scrap the doctrine as a standard of relevancy in the discovery or evidentiary contexts. An alternative is to establish a principled approach to the *de novo* doctrine as a relevancy standard that avoids the confusion recent cases have engendered. Doing so could prevent costly discovery and evidentiary battles but raises other questions courts should answer.

II. THE WEAK PRECEDENTIAL UNDERPINNINGS OF THE *DE NOVO* DOCTRINE AS A RELEVANCY CONCEPT

The *de novo* doctrine was first articulated as a standard of review whereby courts committed to analyzing anew all of the evidence that illustrated the merits of a taxpayer's tax liability. In the Tax Court, the Federal district courts, and Court of Federal Claims, the doctrine was initially unmoored to any concept of relevancy as a discovery or evidentiary matter and arose in cases that expanded, rather than restricted, the scope of inquiry.

A. *Origins of the De Novo Doctrine in Tax Court*

Less than six months after it was created, the Board of Tax Appeals (the predecessor to the Tax Court) issued what is perhaps its earliest articulation of the *de novo* doctrine.⁶

6. The Board of Tax Appeals was created under the Revenue Act of 1924. See CAMILLA E. WATSON & BROOKES D. BILLMAN, JR., *FEDERAL TAX PRACTICE AND PROCEDURE: CASES, MATERIALS AND PROBLEMS* 67 (2004) [hereinafter WATSON & BILLMAN, *FEDERAL TAX*]. The first members of the Board of Tax Appeals, then an independent agency of the Executive Branch, were sworn in on July 16, 1924. HAROLD DUBROFF, *THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS* 80 (1979) [hereinafter DUBROFF, *HISTORICAL ANALYSIS*].

1. *Barry v. Commissioner*

In *Barry v. Commissioner*, the Board overruled the Service's objection and enabled a taxpayer to raise for the first time an argument the taxpayer did not raise at the administrative level.⁷ The Board stated:

When a taxpayer brings his case before the Board he proceeds by trial *de novo*. The record of the case made in the Internal Revenue Bureau is not before the Board except in so far as it may be properly placed in evidence by the taxpayer or by the Commissioner. The Board must decide each case upon the record made at the hearing before it, and, in order that it may properly do so, the taxpayer must be permitted to fully present any questions relating to his tax liability which may be necessary to a correct determination of the deficiency. To say that the taxpayer who brings his case before the Board is limited to questions presented before the Commissioner, and that the Board in its determination of the case is restricted to a decision of issues raised in the Internal Revenue Bureau would be to deny the taxpayer a full and complete hearing and an open and neutral consideration of his case.⁸

Thus, the *de novo* doctrine encompasses the idea that courts in deficiency cases do not sit in judgment of the record established by and before the Service.⁹ Rather, courts determine taxpayers' liabilities anew based on the evidence introduced by the parties and the merits of the case.

Ironically, in direct opposition to the government's current articulations of the *de novo* doctrine as a standard of relevancy, in *Barry* the Service argued that the only items germane to the Board's determination

7. *Barry v. Commissioner*, 1 B.T.A. 156 (1924).

8. *Id.* at 157.

9. In certain non-deficiency cases, however, the Tax Court's review may be limited to the administrative record established by and before the Service. *See, e.g., Robinette v. Commissioner*, 439 F.3d 455 (8th Cir. 2006) (holding that the Tax Court erred in deciding that it could consider evidence not in the administrative record in its review of a collection due process hearing); *Murphy v. Commissioner*, 469 F.3d 27 (1st Cir. 2006) (holding that Tax Court properly excluded evidence not in the administrative record in its review of a collection due process hearing). *But see Wilson v. Commissioner*, 111 A.F.T.R.2d (P-H) 2013-522, 531 (9th Cir. 2013) ("The text structure, and legislative history of § 6015(e) direct the Tax Court to proceed *de novo* when determining whether a taxpayer is eligible for relief under § 6015(f). The Tax court therefore did not err in holding a trial *de novo* and applying a *de novo* standard of review in this case.").

were those considered at the administrative level. The Board rejected that argument, but *Barry* does not stand for the converse: that facts and materials developed at the administrative level are never germane to the Board's decisions. Rather, like other contemporaneous articulations of the *de novo* doctrine, *Barry* expands the scope of inquiry, rather than contracts it.¹⁰ *Barry* also makes clear that notions of fundamental fairness play a role, as a broad inquiry is necessary to ensure the taxpayer obtains "a full and complete hearing and an open and neutral consideration of his case."¹¹

Most importantly, *Barry*'s creation of the *de novo* doctrine was entirely independent of any notion of relevancy as an evidentiary or discovery concept. This makes sense, in part because *Barry* articulated the *de novo* doctrine as a standard of review in tax cases, and standards of review are questions of law distinct from evidentiary and discovery rules. But it also makes sense because the Board, which Congress renamed the Tax Court in 1942 and designated as an Article I court in 1969,¹² had no formal pretrial discovery procedures until 1974, and thus presumably had limited occasion to grapple with relevancy questions in the discovery context.¹³ However, shortly after the Tax Court adopted its formal pretrial discovery procedures, it articulated what is today arguably its most widely cited iteration of the *de novo* doctrine.

10. See also *Wisconsin Butter & Cheese Co. v. Commissioner*, 10 B.T.A. 852, 854 (1928) ("On many occasions the Board and its Members have had occasion, in decisions and otherwise, to point out that the proceeding before it is *de novo* and that we have before us only such evidence as the parties submit."); *Martin Wunderlich Co. v. Commissioner*, P-H 1952 B.T.A. Mem. Dec. (P-H) ¶ 52,029, at 52-96 (1952) ("The Court admitted into evidence, over objection of respondent, certain documents which petitioner contends represent a binding agreement between the government and petitioners as to the use of the completed contract basis of accounting. This Court is given jurisdiction to determine *de novo* excessive profits, if any, realized by a contractor. Being a *de novo* proceeding, we are not restricted to a review of the administrative steps taken below." (internal citations omitted)); *Caplan v. Commissioner*, B.T.A. Mem. Dec. (P-H) ¶ 40,028 (1940) (quoting *Barry*, 1 B.T.A. at 157).

11. *Barry*, 1 B.T.A. at 157.

12. In 1942, the Board changed its name to the Tax Court of the United States, but maintained a similar jurisdiction and its position as an independent agency within the Executive Branch. See WATSON & BILLMAN, FEDERAL TAX, *supra* note 6, at 67. In 1969, the Board "became an Article I (United States Constitution, Article I, § 8) legislative court of record within the federal judicial system, redesignated the United States Tax Court." *Id.*

13. See DUBROFF, HISTORICAL ANALYSIS, *supra* note 6, at 297-305.

2. *Greenberg's Express Inc. v. Commissioner*

In *Greenberg's Express Inc. v. Commissioner*,¹⁴ the Tax Court stated:

As a general rule, this Court will not look behind a deficiency notice to examine the evidence used or the propriety of respondent's motives or of the administrative policy or procedure involved in making his determinations. . . . The underlying rationale for the foregoing is the fact that a trial before the Tax Court is a proceeding *de novo*; our determination as to a petitioner's tax liability must be based on the merits of the case and not any previous record developed at the administrative level.¹⁵

Greenberg's Express cited the *de novo* doctrine to support its holding that it would decide the validity of the Service's determination on the merits, rather than vitiating the determination based on the petitioners' "allegations of discrimination in their selection as objects of an otherwise legitimate tax audit."¹⁶ The passage above is consistent with the notions espoused in *Barry* and similar cases: each expresses the *de novo* doctrine as a standard of review whereby the Tax Court will itself determine a taxpayer's liability.

But, without elaboration, subsequent cases have cited the aforementioned passage to deny on relevancy grounds taxpayers' discovery requests or attempts to introduce evidence.¹⁷ These cases confuse distinct

14. *Greenberg's Express Inc., v. Commissioner*, 62 T.C. 324 (1974).

15. *Id.* at 328.

16. *Id.* at 327. The Tax Court in *Greenberg's Express* stated that it "has on occasion recognized an exception to the rule of not looking behind the deficiency notice when there is substantial evidence of unconstitutional conduct on respondent's part and the integrity of our judicial process would be impugned if we were to let respondent benefit from such conduct." *Id.* at 328.

17. *See, e.g.*, *United States v. Nordberg*, 96-1 U.S. Tax Cas. (CCH) ¶ 50,295 at 84,085, 77 A.F.T.R.2d (RIA) 96-2158, 2160 (D. Mass. 1996) ("In light of the principle that a challenge to a tax determination results in a trial *de novo* rather than a review by this Court of an existing administrative record, the defendants' discovery requests fail to satisfy the mandate of Fed. R. Civ. P. 26(b) that information sought to be discovered by relevant or 'reasonably calculated to lead to the discovery of admissible evidence.'" (citing *Lewis v. Reynolds*, 284 U.S. 281, 283 (1932); *Ruth v. United States*, 823 F.2d 1091, 1094 (7th Cir. 1987); *Greenberg's Express, Inc. v. Commissioner*, 62 T.C. at 328)); *Avedisian v. Commissioner*, 53 T.C.M. (CCH) 503, 505, T.C.M. (P-H) ¶ 87,176 at 87-839 (1987); *Ramsey v. Commissioner*, 51 T.C.M. (CCH) 1247, 1250, T.C.M. (P-H) ¶ 86,252 at 86-1073 to 86-1074 (1986) ("Specifically, petitioners contend that respondent has not completely disclosed the file compiled by the Inspection Division in connection with its criminal investigation of petitioner's bribe of Agent West nor has he disclosed

aspects of the Tax Court's opinion in *Greenberg's Express*, which, in addition to reiterating a commitment to judging the Service's determinations on their merits, also denied the petitioners' request for an order impounding documents with the Tax Court.¹⁸ However, a close examination of *Greenberg's Express* reveals nothing that supports relevancy objections.

The petitioners in *Greenberg's Express* were the sons of Carlo Gambino, an alleged organized crime boss, and several affiliated entities. They alleged that the Service discriminatorily selected their returns for examination and, to gather evidence to help prove these claims, moved the Tax Court under Tax Court Rule 103(a)(10)¹⁹ to order the Service to gather and deliver a number of documents to the court. This was not an ordinary discovery request for specific items in the Service's administrative file. Rather, the petitioners requested all documents, whether in custody of the Service, the Department of the Treasury, or the Attorney General, and their agents, relating to the audit of the petitioners' tax returns or to any investigation of Thomas and Joseph Gambino by the Department of Justice, the Service, or the Federal Strike Force Against Organized Crime in New York City.²⁰

The Tax Court denied this request. It was unnecessary to issue an impounding order under Rule 103(a)(10) because "[t]he custodians of the documents which petitioners seek are already, by virtue of their offices, obligated to preserve any evidence that they know may be relevant to these cases."²¹ The court also explained that the petitioners chose the wrong mechanism for their documentary request. The Tax Court refused to sanction impoundment as "a device for obtaining access to documents which [taxpayers] might be able to obtain by some other available procedures for the production of documents," such as a request for production or subpoena *duces tecum*.²²

After refusing to grant the petitioners' "blanket coverage" discovery request, the Tax Court also held that, even if such documents revealed

certain receipts, memoranda and cancelled checks relied on by Agent Stephens to prepare his examination report. Petitioners contend that this evidence is necessary to establish the basis for respondent's notice of deficiency. For the reasons stated above, however, this Court will not look behind respondent's deficiency notice, and, therefore, any evidence concerning the basis for respondent's determination is not relevant to the disposition of the instant case.").

18. *Greenberg's Express*, 62 T.C. at 325-27.

19. According to the Tax Court in *Greenberg's Express*, "Rule 103(a)(10) permits the issuance of an order, 'That documents or records be impounded by the Court to insure their availability for purposes of review by the parties prior to trial and use at the trial.'" *Id.* at 326 n.3.

20. *Id.* at 325-26.

21. *Id.* at 326.

22. *Id.* at 327.

discriminatory selection of petitioners' returns for audit, the Tax Court would not have been justified in declaring the Service's determination null and void.²³ Rather, it would examine the merits of the determination. It was in this specific context that *Greenberg's Express* reaffirmed the Tax Court's commitment to deciding tax liabilities *de novo*. However, subsequent courts have confused the two aspects of the opinion in *Greenberg's Express* and cite the *de novo* standard of review as support for denying narrow discovery requests on relevancy grounds. There are several flaws in such an extension of *Greenberg's Express*.

First, in *Greenberg's Express*, the Tax Court did not refuse to issue the impounding order based on relevance. In fact, the converse is true. The court refused to grant the order because (1) the government was otherwise "obligated to preserve any evidence which [it] know[s] *may be relevant* to these cases,"²⁴ and (2) the taxpayers should have requested such evidence by other (recently established) pretrial discovery procedures as opposed to a draconian impounding order.²⁵ The Tax Court presumed the agencies from which the petitioners sought documents had at least some evidence in their files relevant to the determination of the petitioners' tax liabilities and noted that evidence should be preserved even if it might *be* relevant to those determinations. Moreover, perhaps to facilitate future information gathering, the Tax Court even advised taxpayers to "give careful attention to developing a more precise description of the materials which they may seek."²⁶

Second, as noted above, *Greenberg's Express* was decided shortly after the Tax Court adopted its first set of formal, pretrial discovery procedures, which, although not as broad as discovery under the Federal Rules of Civil Procedure, defined relevancy broadly and, according to the Tax Court, liberally.²⁷ It would have been incongruous for the court to enact

23. *Id.*

24. *Id.* at 326.

25. *Id.* at 326–27.

26. *Id.* at 327. In fairness, by characterizing the scope of petitioners' requested order "blanket coverage," the court suggested (but did not decide) that some evidence gathered by the various investigative agencies from which the petitioners sought documents would be irrelevant to determining petitioners' tax liabilities for the years at issue. *Id.* This makes sense, however, because the scope of the requested documents included "any investigation of petitioners Thomas Gambino and Joseph Gambino by the Department of Justice, the Internal Revenue Service, or the Federal Strike Force Against Organized Crime operating in New York City." *Id.* at 32526. It is hard, if not impossible, to imagine how some of the information gathered by these agencies would be relevant to tax liabilities of these and other individuals and affiliated entities for three, specific Federal income tax years.

27. *Zaentz v. Commissioner*, 73 T.C. 469, 471-72 (1979) ("For purposes of discovery, the standard of relevancy is liberal. Rule 70(b) permits discovery of

a liberal standard of relevancy and then immediately curtail that standard in a case where relevancy objections were not at issue. Indeed, relevancy objections were at issue in a case decided the same year as *Greenberg's Express*, and there the Tax Court reaffirmed the breadth of relevancy in the pretrial discovery context.²⁸

Third, *Greenberg's Express* fits comfortably within the Tax Court's prior and well-settled articulations of the *de novo* standard of review, beginning with *Barry*. For *Greenberg's Express* (and *Barry*), the *de novo* doctrine holds that courts in tax cases do not sit in judgment of the record established administratively by the Service but, instead, apply a merit-based determination of taxpayers' liabilities based on the evidence introduced by the parties. Distinguishing between the proper mechanism for obtaining evidence to prove a proper tax liability, on the one hand, and the *de novo* doctrine, on the other, is consistent with earlier cases whose articulations of this standard of review are distinct from any notion of relevancy or other discovery or evidentiary concepts. Moreover, by suggesting that the Service or the taxpayer can place some materials in the Service's administrative files into evidence, *Greenberg's Express* and the Tax Court's earlier cases consistently presume that such materials can be relevant to cases before the court.²⁹ Reading *Greenberg's Express* as a drastic departure from this lineage, as modern cases have, is going too far.

information relevant not only to the issues of the pending case, but to the entire 'subject matter' of the case. We have previously ruled that material which would aid the discovering party in understanding relevant material, or which would lead to admissible evidence, is within the scope of Rule 70(b).") *But see* Estate of Woodward v. Commissioner, 64 T.C. 457, 459 (1975) ("Discovery in the Tax Court is new and, although many of our Rules were adopted from the Federal Rules of Civil Procedure, discovery is not as broad in the Tax Court as it is in the Federal District Courts. For example, discovery depositions are not available in the Tax Court.").

28. P.T. & L. Constr. Co. v. Commissioner, 63 T.C. 404, 413-14 (1974) ("Some of the material respondent has objected to, such as the table of contents to the special agent's report, while not directly relevant to any fact that may be established at trial, would aid the reader in understanding the material that we hold is subject to discovery. As such, it is relevant, albeit in a derivative sense. . . . Finally, we emphasize most strongly that the basic purpose of discovery is to reduce surprise by providing a means for the parties to obtain knowledge of all the relevant facts. What is relevant is the factual information which may either reveal evidence that will be admissible at the trial or lead to the discovery of such evidence.").

29. See *Caplan v. Commissioner*, B.T.A. Mem. Dec. (P-H) ¶ 40,028 (1940) ("The record of the case made in the Internal Revenue Bureau is not before the Board except insofar as it may be properly placed in evidence by the taxpayer or by the Commissioner.").

B. *Origins of the De Novo Doctrine in District Courts and the Court of Federal Claims*

In Federal district courts and the Court of Federal Claims, the *de novo* doctrine appears to have its roots in *Lewis v. Reynolds*,³⁰ a seminal 1932 Supreme Court opinion. However, while *Lewis* is the earliest case these courts commonly cite when discussing the *de novo* doctrine,³¹ *Lewis* does not stand for the proposition that the discovery of, or introduction of, evidence should be restricted. In fact, like *Barry*, *Lewis* expanded the scope of review, rather than restricted it, and said nothing about relevancy in the evidentiary or discovery context.

At issue in *Lewis* was whether the Service could offset a refund, on which the statute of limitations had not expired, with a deficiency from the same year, on which the statute of limitations had expired. In *Lewis*, the Service audited the final tax return of a decedent's estate, disallowed certain deductions, and assessed a \$7,297.16 deficiency. The decedent's estate paid the assessed deficiency and requested a refund. Nearly three years later, the Service refused payment, citing other improper deductions for the same year that, if they had been disallowed in the first instance, would have caused an even bigger deficiency.

In a concise opinion which upheld the Service's refusal to issue a refund, *Lewis* established the rule that:

An overpayment must appear before a refund is authorized.
Although the statute of limitations may have barred the

30. 284 U.S. 281 (1932).

31. See, e.g., *Gen. Motors Corp. v. United States*, 75 Fed. R. Serv. 3d 828 (E.D. Mich. 2009) ("Tax refund cases are *de novo* proceedings." (citing *Lewis*, 284 U.S. at 283)); *United States v. Nordberg*, 96-1 U.S. Tax Cas. (CCH) ¶ 50,295 at 84,085, 77 A.F.T.R.2d (RIA) 96-2158, 96-2160 (D. Mass. 1996) ("In light of the principle that a challenge to a tax determination results in a trial *de novo* rather than a review by this Court of an existing administrative record, the defendants' discovery requests fail to satisfy the mandate of Fed. R. Civ. P. 26(b) that information sought to be discovered by relevant or 'reasonably calculated to lead to the discovery of admissible evidence.'" (citing *Lewis*, 284 U.S. at 283 (1932))); *Armtek Corp. v. United States*, 78 A.F.T.R.2d 96-5266, 96-5268 (W.D.N.Y. 1996) ("It is the Government's position that the opinions and conclusions of the IRS are not relevant to the court's *de novo* determination of the applicable tax. (citing *Lewis*, 284 U.S. at 283)); *Fowler v. United States*, 89 A.F.T.R.2d (RIA) 2002-2736 (Fed. Cl. 2002); *Vons Companies, Inc. v. Commissioner*, 51 Fed. Cl. 1, 6 (Fed. Cl. 2001) ("We begin with the axiomatic principle that tax refund cases are *de novo* proceedings." (citing *Lewis v. Reynolds*, 284 U.S. 281, 283 (1932))). See also *R.E. Dietz Corp. v. United States*, 939 F.2d 1 (2d Cir. 1991); *Litman v. United States*, 78 Fed. Cl. 90, 107 (Fed. Cl. 2007); *Cook v. United States*, 46 Fed. Cl. 110, 116 (Fed. Cl. 2000).

assessment and collection of any additional sum, it does not obliterate the right of the United States to retain payments already received when they do not exceed the amount which might have been properly assessed and demanded.³²

Courts regularly cite *Lewis* for the well-established proposition that a plaintiff seeking a refund of taxes has the burden of proving that she is in fact entitled to a refund (e.g., that an overpayment actually exists in a given tax year).³³

However, in the discovery or evidentiary context, some courts have cited *Lewis* for the proposition that facts developed by the Service are irrelevant in *de novo* proceedings.³⁴ Such an extension of *Lewis* is unwarranted for several reasons. First, *Lewis* expanded the scope of relevant facts in trials of refund actions. Under *Lewis*, courts must look at all of the items in a taxpayer's tax year — even those for which adjustments are barred by the statute of limitations — to determine whether a refund is justified. Second, *Lewis* held nothing about relevancy as a discovery or evidentiary matter. *Lewis* simply established a standard of review in refund actions, much like *Barry* and *Greenberg's Express* did in deficiency cases. Relying on the case to support decisions about relevancy in the discovery or evidentiary context is misguided.

Finally, *Lewis*' only reference to evidence was to a letter from the Service to the petitioners that stated additional deductions had been improperly allowed and provided a revised computation of the petitioners' tax liability for the year at issue. The Supreme Court noted that the letter was "introduced in evidence by [petitioners],"³⁵ noted that the lower courts upheld the Service's determination reflected in the letter, and affirmed the lower courts' decisions. *Lewis* itself thus relied on facts and conclusions that were developed and established at the administrative level and introduced into the evidentiary record. Citing the case to preclude the discovery or introduction of such facts is incongruous.

The historical origins of the *de novo* doctrine in the Tax Court and the Federal district courts and the Court of Federal Claims illustrates the weaknesses in applying the *de novo* doctrine to enable the Service and Department of Justice to withhold information from taxpayers on relevancy grounds. In addition to, and perhaps because of, the *de novo* doctrine's weak precedential underpinnings in the evidentiary and discovery context, courts

32. *Lewis*, 284 U.S. at 283.

33. See, e.g., *Williams-Russel & Johnson, Inc. v. United States*, 371 F.3d 1350 (11th Cir. 1994); *Decker v. Korth*, 219 F.2d 732 (10th Cir. 1955); *Bachner v. Commissioner*, 109 T.C. 125 (1998).

34. See *supra* note 31.

35. *Lewis*, 284 U.S. at 282.

often apply the doctrine inconsistently in those arenas, a problem to which this article now turns.

III. COURTS STRUGGLE TO COHERENTLY APPLY THE *DE NOVO* DOCTRINE

As noted above, the *de novo* doctrine arose as a standard of review courts apply when determining taxpayers' tax liabilities. Specifically, it embodies the idea that courts must base their determinations on all of the facts pertinent to taxpayers' liabilities for the year at issue, rather than "looking behind" the adjustment to miscellaneous factors such as the Service's motives or reasons for initiating an audit or making an adjustment.³⁶ In contrast to facts surrounding the Service's deficiency determination, these miscellaneous factors do not bear on the merits of taxpayers' tax liabilities.

At some point, however, courts began citing the doctrine in the discovery or evidentiary context for the proposition that the factual findings, thoughts, procedures, conclusions, or reasoning of Service employees about a taxpayer's liability are irrelevant.³⁷ To say that facts, thoughts, reasoning, or conclusions obtained or reached by the Service are privileged and not discoverable is one thing. To say that such information is irrelevant is an entirely different matter, especially because the standard of review in tax cases is distinct from other legal questions such as the discovery or admissibility of evidence. As noted below, courts often fail to draw these distinctions and, as a result, apply the *de novo* doctrine inconsistently.

36. It is worth noting that even this well-established rule has exceptions. See *Clapp v. Commissioner*, 875 F.2d 1396, 1402 (9th Cir. 1989) ("Only where the notice of deficiency reveals on its face that the Commissioner failed to make a determination is the Commissioner required to prove that he did in fact make a determination." (citing *Campbell v. Commissioner*, 90 T.C. 110 (1988))); *Scar v. Commissioner*, 814 F.2d 1363 (9th Cir. 1987); *Frazier v. Commissioner*, 91 T.C. 1, 9-10 (1988) ("Where, however, there is substantial evidence of unconstitutional conduct by respondent in connection with the deficiency determined, we have, as an exception on occasion, 'looked behind the notice of deficiency.'" (citations omitted)).

37. See, e.g., *R.E. Dietz Corp. v. United States*, 939 F.2d 1, 4 (2d Cir. 1991) ("The factual and legal analysis employed by the Commissioner is of no consequence to the district court." (citing *Nat'l Right to Work Legal Def. & Educ. Found. v. United States*, 487 F.Supp. 801, 805 (E.D.N.C. 1979))); *United States v. Nordberg*, 96-1 U.S. Tax Cas. (CCH) ¶ 50,295, 77 A.F.T.R.2d (RIA) 96-2158 (D. Mass. 1996); *Katz v. United States*, No. 91-5623, 1992 U.S. Dist. LEXIS 7394, at *2-3 (E.D. Pa. May 6, 1992); *Garity v. United States*, 81-2 U.S. Tax Cas. (CCH) ¶ 9599, 46 A.F.T.R.2d (P-H) 80-5143 (E.D. Mich. 1980); *Flamingo Fishing Corp. v. United States*, 22 Cl. Ct. 625, 629 (1991).

A. *LPCiminelli Interests, Inc. v. United States*

LPCiminelli Interests, Inc. v. United States,³⁸ a 2012 decision of the federal district court for the Western District of New York, illustrates the difficulties courts face in applying the *de novo* doctrine. In *LPCiminelli*, the Service examined a corporation's 2004 consolidated income tax return for compliance with the consolidated return rules' excess loss account ("ELA") provisions and with the Code's cancellation of indebtedness ("COD") provisions. During the audit, the Service found the corporation complied with the ELA provisions but found that the corporation had \$3.5 million of unreported COD income.³⁹

After *LPCiminelli* paid the additional tax and sued for a refund, the Department of Justice determined that the Service's position was erroneous, conceded that the corporation had no COD income, and argued that *LPCiminelli* failed to report an equivalent amount of income from its ELA.⁴⁰ During litigation, *LPCiminelli* deposed David Thom, one of the Service's agents, and obtained several emails, draft notices of proposed adjustments, "and other documents pertaining to the facts considered and matters pursued by the audit team, which included Mr. Thom's supervisor Kathleen Oswald and IRS Attorney Matthew Root."⁴¹ When *LPCiminelli* sought to introduce pieces of this evidence at trial, the Service filed a motion *in limine* to preclude such evidence arguing that "any testimony or documentary evidence concerning the actions of IRS employees involved in the audit is of no relevance to the court in its role as the finder of fact as to the propriety of the tax assessment."⁴²

The court agreed with the Service, holding that "[t]he factual and legal analysis employed by the Commissioner is of no consequence to the district court"⁴³ and that "trial courts called upon to conduct *de novo* review of the Commissioner's assessment of tax liability have declined, on relevance grounds, to consider evidence regarding IRS agents' underlying opinions, impressions, conclusions, and reasoning for their administrative

38. *LPCiminelli Interests, Inc. v. United States*, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,671, 110 A.F.T.R.2d (RIA) 2012-6631 (W.D.N.Y. 2012).

39. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,220, 110 A.F.T.R.2d (RIA) at 6633.

40. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,220-21, 110 A.F.T.R.2d (RIA) at 6633.

41. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,221, 110 A.F.T.R.2s (RIA) at 6633.

42. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,221, 110 A.F.T.R.2d (RIA) at 6633-34.

43. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,222, 110 A.F.T.R.2d (RIA) at 6634.

determinations.”⁴⁴The court granted the Service’s motion *in limine* on relevancy grounds and refused to consider “the factual considerations and legal analysis employed by the audit team. . . .”⁴⁵

To determine the merits of the case, however, the court relied heavily on a document “which was prepared by the IRS [in] connection with the audit of LPCiminelli’s 2004 tax return, [and provided] an accurate summary of [LPCiminelli’s subsidiary’s] assets, liabilities, income, and expenses during the period from 1999 through 2003.”⁴⁶ This document was not subject to the Service’s motion *in limine*, despite the fact that it contained the Service’s underlying factual and legal analysis.⁴⁷ Moreover, in support of its conclusion that LPCiminelli did not violate the ELA anti-avoidance rule or recognize ELA income, the court stated “the IRS examined the matter and chose not to assess tax based on any realized ELA income. Instead, the IRS directed LPCiminelli to pay tax on COD income for tax year 2004.”⁴⁸

Thus, at the same time the court was rejecting evidence as irrelevant because it included factual considerations and legal analysis employed by the audit team, the court was accepting as relevant and relying on factual considerations and legal analysis employed by the audit team. *LPCiminelli* is devoid of any apparent legal justification for such a distinction. Additionally, the court and parties considered the factual considerations and legal analysis employed by the audit team relevant for purposes of discovery, as LPCiminelli deposed the Service’s agent assigned to the case and obtained emails, draft notices, and other documents from the Service’s audit team. But the court did not distinguish relevancy for purposes of Federal Rules of Civil Procedure 26(b)(1) (“FRCP”), which governs discovery, from relevancy for purposes of Federal Rules of Evidence 401, which governs trial

44. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,222, 110 A.F.T.R.2d (RIA) at 6634.

45. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,222, 110 A.F.T.R.2d (RIA) at 6634.

46. *Id.* 2012-2 U.S. Tax Cas. (CCH) at 87,224, 110 A.F.T.R.2d (RIA) at 6636.

47. The Service and LPCiminelli apparently stipulated that the document and its factual and legal analysis were admissible. *See id.* However, “it is axiomatic that the litigants cannot stipulate the court into error” with respect to evidentiary matters. *See Exxon Corp. v. United States*, 45 Fed. Cl. 581, 692 (Fed. Cl. 1999). *See also Kaminer Constr. Corp. v. United States*, 488 F.2d 980, 988 (Ct. Cl. 1973); *Dillon, Read & Co., Inc. v. United States*, 875 F.2d 293, 300 (Fed. Cir. 1989). Thus, the fact that the parties stipulated the document was relevant (and admissible) does not control whether it was in fact. The court’s reliance on the document in *LPCiminelli* suggests it determined the document was relevant and otherwise admissible.

48. *LPCiminelli Interests, Inc.*, 2012-2 U.S. Tax Cas. (CCH) at 87,225, 110 A.F.T.R.2d (RIA) at 6637.

admissibility. Moreover, for better or worse, courts have applied the *de novo* doctrine as a doctrine of relevancy for both discovery and evidentiary purposes,⁴⁹ so *LPCiminelli*'s application appears to be a misapplication of a misguided doctrine.

B. Other Cases

LPCiminelli is not alone in its confusing application of the *de novo* doctrine as a relevancy standard. Other cases inconsistently apply the *de novo* doctrine when faced with discovery or evidentiary disputes. Some cases deny on relevancy grounds taxpayers' attempts to discover⁵⁰ or introduce⁵¹ factual materials in addition to materials containing the Service's thoughts, impressions, or opinions. Other cases, however, have allowed taxpayers to discover⁵² or introduce⁵³ materials contained in the Service's administrative file.

49. See *infra* notes 50–51.

50. See, e.g., *ISI Corp. v. United States*, 503 F.2d 558 (9th Cir. 1974) (noting that district court may have erred in refusing to require Service's agent to answer purely factual questions in deposition); *United States v. Nordberg*, 96-1 U.S. Tax Cas. (CCH) ¶ 50,295, 77 A.F.T.R.2d (RIA) 96-2158 (D. Mass. 1996); *Garity v. United States*, 81-2 U.S. Tax Cas. (CCH) ¶ 9599 at 88,005; 46 A.F.T.R.2d (P-H) 80-5143, 5145 (E.D. Mich. 1980) (refusing to require production of "documents relating to the assessment or collection of Federal withholding taxes;" although taxpayer argued that the reasoning of the Service was relevant to whether the assessment was an abuse of discretion, the court did not address the fact that the documents may have contained factual data relevant to the amount of the assessment itself); *Flamingo Fishing Corp. v. United States*, 22 Cl. Ct. 625, 629 (1991).

51. See, e.g., *Katz v. United States*, No. 91-5623, 1992 U.S. Dist. LEXIS 7394, at *2–3 (E.D. Pa. May 6, 1992).

52. See, e.g., *Big Ernie's Inc. v. United States*, 104 A.F.T.R.2d (RIA) 2009-6218 (E.D. Va. 2009); *Beresford v. United States*, 123 F.R.D. 232, 235 (E.D. Mich. 1988) ("[I]nformation relied upon by the government in making its valuation is directly relevant to plaintiff's ability to challenge that valuation in this proceeding."); *Simons-Eastern Co. v. United States*, 55 F.R.D. 88 (N.D. Ga. 1972); *Timken Roller Bearing Co. v. United States*, 38 F.R.D. 57, 62 (N.D. Ohio 1964) (holding that the discovery rules permit "discovery of a defensive claim as well; the requested items may relate to the defense which the government may offer"); *Memorandum for Counsel, Black and Decker Corp. v. United States*, 219 F.R.D. 87 (D. Md. 2004) (No. WDQ-02-2070) (enabling depositions of two Service officials because the Service took a position allegedly inconsistent with public pronouncements it made); *Jade Trading, LLC v. United States*, 65 Fed. Cl. 487 (Fed. Cl. 2005).

53. See, e.g., *Hudspeth v. Commissioner*, 914 F.2d 1207, 1214 (9th Cir. 1990) (holding that Tax Court's determination that Service's agent's data was irrelevant was erroneous; evidence was relevant and admissible to show bias); *D'Angelo v. United States*, 2009-1 U.S. Tax. Cas. (CCH) ¶ 50,273, 103 A.F.T.R.2d

Still other cases discuss the *de novo* doctrine in a manner that closely adheres to the doctrine's origins; these cases are difficult to reconcile with other modern views of the doctrine as a relevancy standard.⁵⁴

C. *Cook v. United States*

For instance, in *Cook v. United States*, the Service lost all but select portions of the taxpayer's administrative file.⁵⁵ Regarding the standard of review it should apply to the Service's assessment, the court stated that "[i]n tax refund suits, factual issues are tried *de novo* in this court, with no weight given to subsidiary factual findings made by the Service in its internal administrative proceedings."⁵⁶

It is worth noting that *Cook's* precise language — that factual findings made by the Service are given no *weight* by trial courts — is separate from a comment on the discoverability or admissibility of such factual findings.⁵⁷ A fundamental precept of evidentiary rules is that the weight of evidence is distinct from the admissibility of that evidence.⁵⁸ Thus, *Cook's* recitation of the *de novo* doctrine says nothing about whether the court would admit into the trial record the Service's administrative factual findings. In fact, *Cook* suggests that the Service's administrative files are generally subject to discovery on relevancy grounds. The court admonished

(RIA) 2009-1296 (S.D. Fla. 2009) (denying motion *in limine* to preclude calling Service witnesses at trial to question their administrative determination); *Haag v. Commissioner*, 88 T.C. 604, 622 n.14 (1987) (admitting into evidence over the Service's objection a thirty day letter and revenue agent's report to identify the basis for the Service's deficiency determination), *aff'd*, 855 F.2d 855 (8th Cir. 1988); Order: The Court Directs the Parties to Confer and Attempt to Reach Agreement Regarding the Form of a Judgment Consistent with the Determinations in this Order and Trinity I, *Trinity Indus., Inc. v. United States*, No. 3:06-CV-00726, at 6 n.2 (N.D. Tex. May 11, 2012) ("It appears to the Court that the RAR is admissible evidence under the party opponent exception to the hearsay rule. Thus, while certainly not binding on the Government, the RAR statement is competent evidence and the Court has considered it as such.")

54. *See, e.g.*, *Litman v. United States*, 78 Fed. Cl. 90, 107 (Fed. Cl. 2008); *Cook v. United States*, 46 Fed. Cl. 110 (Fed. Cl. 2000).

55. *Cook*, 46 Fed. Cl. at 110.

56. *Id.* at 113.

57. *See, e.g.*, *Builders Steel Co. v. Commissioner*, 179 F.2d 377, 380 (8th Cir. 1950) (reversing Tax Court's opinion for failure to allow evidence and noting "[w]e think that the trial judge in this case confused the question of the admissibility of evidence with its weight. Evidence as to value may be admissible, although of little weight."); *Gilford v. Commissioner*, 88 T.C. 38, 54 n.18 (1987) ("The facts presented by these documents go to the weight of the evidence, not its admissibility."). *See also* *Ziskie v. Mineta*, 547 F.3d 220, 225-26 (4th Cir. 2008).

58. *See supra* note 57.

the Service for its inability to locate the taxpayer's administrative file, and stated "this court believes that the Service has a particular responsibility to ensure that files needed for litigation are preserved and timely made available to the Justice Department and, upon proper discovery request, to plaintiffs."⁵⁹

Although relevancy was not at issue in *Cook*, the court, like *Barry*, *Greenberg's Express*, and *Lewis*, implied that documents in the Service's administrative file would be responsive to a taxpayer's discovery request.

The distinctions between these cases do not appear to be founded on a principled, or even an identifiable, application of a relevancy standard to each case's unique circumstances. Nor do these cases routinely distinguish facts the Service has gathered from taxpayers and third parties that might support or contradict the Service's assessment, from materials that purely reflect the Service's thoughts, impressions, opinions, or motives for beginning an examination or making an adjustment.⁶⁰ Trial courts, tasked with judging the merits of deficiencies *de novo*, generally do not consider the latter, which might also be shielded from discovery on grounds such as work product, attorney-client privilege, or deliberative-process privilege. It is difficult to see how the former, however, would be irrelevant under even the most restrictive definition of relevancy in the discovery and evidentiary contexts.

The inconsistent manner in which courts have applied the *de novo* doctrine as a standard of relevancy suggests that courts should either dispose of the *de novo* doctrine as a relevancy standard or articulate a more principled, clear, and uniform approach. Either option would help eliminate costly discovery and evidentiary battles and facilitate the speedy, inexpensive, and extrajudicial determination of tax controversies, which are goals of courts' discovery rules to begin with.⁶¹ Either way, courts should be mindful of several additional problems with the *de novo* doctrine as a standard of relevancy.

59. *Cook*, 46 Fed. Cl. at 120.

60. *But see Big Ernie's*, 104 A.F.T.R.2d at 2009-6218; *Armtek Corp. v. United States*, 78 A.F.T.R.2d 96-5266, 5267-68 (W.D.N.Y. 1996); *Simons-Eastern Co. v. United States*, 55 F.R.D. 88 (N.D. Ga. 1972).

61. TAX CT. R. 1(d) ("The Court's Rules shall be construed to secure the just, speedy, and inexpensive determination of every case."); FED. R. CIV. P. 1 ("[These rules] should be construed and administered to secure the just, speedy, and inexpensive determination of every action and proceeding.").

IV. ADDITIONAL PITFALLS WITH THE *DE NOVO* DOCTRINE AS A RELEVANCY STANDARD

Part II discussed the fundamental problem with articulating the *de novo* doctrine as a relevancy standard: such an articulation has no apparent legal justification. None of the cases to first articulate the *de novo* doctrine were cases in which relevancy was at issue, and they either expanded the scope of inquiry or presumed information obtained by the Service or other government agencies was relevant to the issues at hand. Part III explained that courts inconsistently apply the *de novo* doctrine as a relevancy concept and have failed to draw important, principled distinctions that might facilitate extrajudicial resolution of future discovery disputes.

As noted below, there are other problems with reading the *de novo* doctrine as a standard of relevancy such as a fundamental inconsistency with the broad scope of relevancy in the discovery and evidentiary context.

A. *The De Novo Doctrine Violates Well-Settled Discovery and Evidentiary Rules*

FRCP 26(b)(1) establishes the scope of discovery for tax refund suits in district courts. Under FRCP 26(b)(1), unless otherwise limited by a court order:

Parties may obtain discovery regarding *any* nonprivileged matter that is relevant to any party's claim or defense — including the existence, description, nature, custody, condition, and location of any documents or other tangible things and the identity and location of persons who know of any discoverable matter. For good cause, the court may order discovery of any matter relevant to the subject matter involved in the action. Relevant information need not be admissible at the trial if the discovery appears reasonably calculated to lead to the discovery of admissible evidence.⁶²

Although the 2000 amendments to FRCP 26(b)(1) narrowed the scope of discovery from its prior focus on relevance to the subject matter of the suit to encompass material relevant to the claims or defense of any

62. FED. R. CIV. P. 26(b)(1) (emphasis added). The corollary in the Rules of the United States Court of Federal Claims, R. CT. FED. CL. 26(b)(1), parallels the structure and content of FRCP 26(b)(1). See R. CT. FED. CL. 26(b)(1); R. CT. FED. CL. 26 rules committee notes, 2002 revision.

party,⁶³ federal district courts still “must employ a liberal discovery standard in keeping with the spirit and purpose of the discovery rules,”⁶⁴ which are to be “construed and administered to secure the just, speedy, and inexpensive determination of every action and proceeding.”⁶⁵

Unlike the FRCP, the Tax Court’s rules enable discovery of any information relevant to the subject matter of the case. Tax Court Rule 70(b) states that:

The information or response sought through discovery may concern any matter not privileged and which is relevant to the subject matter involved in the pending case. It is not ground for objection that the information or response sought will be inadmissible at the trial, if that information or response appears reasonably calculated to lead to discovery of admissible evidence, regardless of the burden of proof involved. If the information or response sought is otherwise proper, it is not objectionable merely because the information or response involves an opinion or contention that relates to fact or to the application of law to fact.⁶⁶

Under FRCP 26(b)(1) and Tax Court Rule 70(b), the basic purpose of discovery is to reduce surprise and enable the parties to evaluate and resolve their dispute by providing a means for the parties to obtain knowledge of all the relevant facts.⁶⁷ In determining whether evidence is relevant, which party bears the burden of proof in the matter is of no consequence, since parties may obtain discovery of matters relating to any party’s claim or defense.⁶⁸ Hence, a claim that factual material obtained by

63. See 6 JAMES WM. MOORE ET AL., *MOORE’S FEDERAL PRACTICE* ¶ 26.41(6)(c) (3d ed. 1999).

64. *Wrangen v. Pa. Lumbermans Mut. Ins. Co.*, 593 F. Supp. 2d 1273, 1278 (S.D. Fla. 2008) (citing *Graham v. Casey’s Gen. Stores*, 206 F.R.D. 251, 253 (S.D. Ind. 2002); *White v. Kenneth Warren & Son, Ltd.*, 203 F.R.D. 364, 366 (N.D. Ill. 2001)).

65. FED. R. CIV. P. 1.

66. Tax Ct. R. 70(b).

67. *Ersine v. Consol. Rail Corp.*, 814 F.2d 266, 272 (6th Cir. 1987); *Nutt v. Black Hills Stage Lines, Inc.*, 452 F.2d 480, 483 (8th Cir. 1971) (“The federal discovery rules were designed to provide each party with the fullest pre-trial knowledge of the facts and to clarify and narrow the issues to be tried.”); *P.T. & L. Construction Co. v. Commissioner*, 63 T.C. 404 (1974) (discussing discovery under Tax Court Rule 70(b)). See also 6 MOORE ET AL., *supra* note 63, at ¶ 26.02.

68. FED. R. CIV. P. 26(b)(1). See also TAX CT. R. 70(b)(1) (“It is not ground for objection that the information or response sought will be inadmissible at the trial,

the Service is irrelevant because taxpayers must prove the Service's determination is incorrect or prove their entitlement to a refund is unfounded.

Nor is information irrelevant for discovery because it would be inadmissible at trial.⁶⁹ Thus, information may be discoverable even if, under the Federal Rules of Evidence, it would be cumulative, would waste time or might mislead the jury,⁷⁰ is hearsay,⁷¹ describes compromise offers or negotiations,⁷² is evidence of insurance against liability,⁷³ cannot be authenticated,⁷⁴ or is irrelevant under the Federal Rules of Evidence.

Like its counterpart in the discovery rules, the definition of relevancy under evidentiary rules is itself a broad standard. The Federal Rules of Evidence govern the admissibility, rather than the discovery, of evidence in federal civil trials and in the Tax Court.⁷⁵ Under Federal Rule of Evidence 401:

Evidence is relevant if: (a) it has *any* tendency to make a fact more or less probable than it would be without the evidence; and (b) the fact is of consequence in determining the action.⁷⁶

In tax cases, trial courts are given significant discretion to determine the scope of relevancy, and regularly interpret the term broadly.⁷⁷

if that information or response appears reasonably calculated to lead to discovery of admissible evidence, *regardless of the burden of proof involved.*" (emphasis added).

69. FED. R. CIV. P. 26(b)(1); TAX CT. R. 70(b)(1).

70. See FED. R. EVID. 403.

71. See FED. R. EVID. 802.

72. See FED. R. EVID. 408(a).

73. See FED. R. EVID. 411.

74. See FED. R. EVID. 901.

75. The Tax Court follows the Federal Rules of Evidence as adopted by the U.S. District Court for the District of Columbia for non-jury trials. TAX CT. R. 143(a); I.R.C. § 7453.

76. FED. R. EVID. 401 (emphasis added).

77. See, e.g., *Kalo v. Commissioner*, 98-2 U.S. Tax Cas. ¶ 50,514, 85,142-43, 81 A.F.T.R.2d 98-2266, 2269-71 (6th Cir. 1998); *Robinette v. Commissioner*, 123 T.C. 85, 103-04 (2004), *rev'd*, 439 F.3d 455 (8th Cir. 2006); *Estate of Gilford v. Commissioner*, 88 T.C. 38, 53-54 (1987); *Karme v. Commissioner*, 73 T.C. 1163, 1178-80 (1980). See also *Procter & Gamble Co. v. United States*, 2010-1 U.S. Tax Cas. ¶ 50,146, 83,196, 105 A.F.T.R.2d 2010-330, 332 (S.D. Ohio 2009) (construing FED. R. CIV. P. 26(b)(1)); *Vons Cos., Inc. v. United States*, 51 Fed. Cl. 1, 19 (2001) ("Indeed, the language establishing what is 'relevant evidence' under the Federal Rules of Evidence is quite different and certainly much broader than the 'directly related' language in section 6103(h)(4)(B) — a difference which the legislative history of the latter provision indicates should not be overlooked.").

However, in contravention of the broad scope of relevancy under these rules, applying the *de novo* doctrine as a standard of relevancy potentially exempts from discovery or introduction into evidence a wide range of facts gathered and developed by the Service. Such an application of the *de novo* doctrine also contravenes the Tax Court's rules, which, in addition to purely factual information, allow discovery of information that "involves an opinion or contention that relates to fact or to the application of law to fact."⁷⁸ As noted below, the Service regularly obtains such information from sources other than the taxpayer, and discovery requests are often the quickest and least expensive way for taxpayers to obtain such information.

B. The De Novo Doctrine Enables the Service to Withhold from Taxpayers Materials it Has Gathered from Third Parties and Deemed Relevant to Taxpayers' Examinations

The Service regularly contacts and obtains information from third parties as part of its examination process, both informally and using the summons process.⁷⁹ Taxpayers are generally entitled to notice of this information gathering when summons are issued,⁸⁰ and in the third-party contact context, when the contact: "(1) Is initiated by [a Service] employee; (2) Is made to a person other than the taxpayer; (3) Is made with respect to the determination or collection of [a] tax liability of [the] taxpayer; (4) Discloses the [taxpayer's] identity . . . ; and (5) Discloses the association of the [Service] employee with the [Service]."⁸¹ In other contexts, however, taxpayers are not entitled to notice that the Service has gathered materials from third parties to assist the Service in its examination.⁸² In addition, the Service occasionally gathers or obtains information about *other* taxpayers to be used as evidence that might prove or disprove issues to be decided in the taxpayer's case.⁸³

78. TAX CT. R. 70(b).

79. See I.R.C. § 7602; IRM 4.11.57 (Jan. 15, 2005).

80. I.R.C. § 7609(a)(1).

81. Reg. § 301.7602-2(b).

82. For instance, the Service is not required to give notice to the taxpayer if its third-party contacts are outside of any of the four criteria noted above. See Reg. § 301.7602-2(b). The Service also need not give notice to any contacts authorized by the taxpayer "if the [Service] determines for good cause . . . that such notice would jeopardize collection of any tax" or "involve reprisal against any person," or "with respect to pending . . . criminal investigation[s]." See I.R.C. § 7602(c)(3). The Service also need not provide taxpayers with notice of its service of third-party summonses in various instances. See I.R.C. § 7609(c)(2).

83. See, e.g., I.R.C. § 7491(b) (allocating to the Service the burden of proof with respect to individuals' incomes that are reconstructed by the Service "solely

Use of the summons or examination process itself is contingent on the information sought by the Service being “relevant or material to such inquiry.”⁸⁴ Additionally, in the context of maintaining taxpayer confidentiality, the Code defines taxpayer “return information” to encompass any information received by, collected by, or furnished to the Service “with respect to the determination of the existence, or possible existence, of [the taxpayer’s] liability.”⁸⁵ Thus, in each of these situations, the material the Service’s third-party inquiries yield is relevant to the Service’s examination of the taxpayer.⁸⁶ To then argue that, under the *de novo* doctrine, such facts and information are not relevant because they were gathered by (and found relevant by) the Service makes no sense, especially because the *de novo* doctrine’s origins provide no justification for doing so.

Moreover, in some instances a discovery request might be the only reasonable manner in which the taxpayer can access the facts and information gathered by the Service.⁸⁷ In the third-party contact context, the regulations typically entitle taxpayers to pre-contact notice of potential third party contacts and post-contact reports of the individuals contacted, but not to information “such as the nature of the inquiry or the content of the third party’s response.”⁸⁸ In other instances, taxpayers are not entitled to notice that the Service has gathered materials from third parties. Absent a discovery request in these instances, it could be nearly impossible for the taxpayer to obtain information that might be used to support or rebut its position at trial.

through the use of statistical information on unrelated taxpayers”); I.R.S. Legal Mem. 2012-50-020 (Dec. 14, 2012) (“[P]attern evidence from other participants showing that all the arrangements were designed, implemented, and operated identically can be used to demonstrate that the arrangement was not designed with a specific taxpayer’s business needs in mind and therefore lacked a bona fide business purpose other than tax benefits.”).

84. I.R.C. § 7602(a)(1)-(3). Notably, the standard of relevancy in the summons context is also relaxed, as documents are generally considered relevant if they “have the potential to shed some light on any aspect of [a taxpayer’s] income.” 2121 Arlington Heights Corp. v. I.R.S., 109 F.3d 1221, 1224 (7th Cir. 1997) (citing *United States v. Arthur Young & Co.*, 465 U.S. 805, 814-15 (1984)).

85. I.R.C. § 6103(b)(2).

86. *See Vons Cos., Inc. v. United States*, 51 Fed. Cl. 1 (2001) (“Indeed, the language establishing what is ‘relevant evidence’ under the Federal Rules of Evidence is quite different and certainly much broader than the ‘directly related’ language in section 6103(h)(4)(B) — a difference which the legislative history of the latter provision indicates should not be overlooked.”).

87. While taxpayers can submit Freedom of Information Act requests for materials gathered by the Service, such requests are cumbersome and impose time, monetary, and administrative burdens on both the taxpayer and the Service that simple, direct discovery requests do not. *See* 5 U.S.C. § 552; 5 U.S.C. § 552a; Reg. § 601.702. *See also* I.R.C. § 6110(a).

88. Reg. § 301.7602-2(e)(2)(i).

Indeed, the discovery process provides a means for obtaining helpful and harmful facts and materials gathered by the Service during the examination, which narrows issues for trial and encourages a quick and inexpensive resolution of litigated matters. Applying the *de novo* doctrine as a restrictive standard of relevancy thwarts these purposes.

C. *What Occurred During the Examination, and the Service's Thoughts, Procedures, Conclusions, Reasoning, or Factual Findings Is Often the Central Issue to be Decided*

Another problem with applying the *de novo* doctrine as a standard of relevancy in tax cases is that in many instances — when the Service or taxpayer might argue estoppel or when the Service might argue the doctrine of variance, for example — the Service's thoughts, procedures, conclusions, reasoning, or factual findings are directly at issue. As a practical and policy matter, the strength of the *de novo* doctrine as a discovery or evidentiary concept is undercut by the various instances where it should not apply.⁸⁹

89. The examples below are only several that might commonly occur. There are other instances when the Service's thoughts, procedures, conclusions, reasoning, or factual findings might be directly at issue in a given case. *See, e.g.*, *United States v. Powell*, 379 U.S. 48, 57-58 (1964) (holding that, to defeat a petition to quash a summons or to enforce a summons, the government must establish that (1) "the investigation will be conducted [for] a legitimate purpose," (2) the material being sought is relevant to that purpose, (3) "the information sought is not already in the [Service's] possession," and (4) the Service complied with all the administrative steps required by the Code); *William Bryen Co. v. Commissioner*, 89 T.C. 689, 707 (1987) ("Respondent may rely on a particular theory [at trial] if he has provided petitioner with 'fair warning' of his intention to proceed under that theory." (citing *Schuster's Express, Inc. v. Commissioner*, 66 T.C. 588, 593 (1976); *Rubin v. Commissioner*, 56 T.C. 1155, 1163 (1971))). Cases in which the Service attempts to penalize taxpayers pose an especially thorny issue because reasonable cause and good faith based on "all the facts and circumstances, including the uncertain state of the law," is a defense to penalties. *See, e.g.*, *Patel v. Commissioner*, 138 T.C. No. 23, 39 (2012) ("Given all the facts and circumstances, including the uncertain state of the law, we find that petitioners acted with reasonable cause and in good faith. Therefore, we hold that they are not liable for any penalty under section 6662."). Arguably, the Service's views on the state of the law and the Service's treatment of other similarly situated taxpayers might be relevant to whether a taxpayer acted reasonably in a given case. *See Allison v. United States*, 80 Fed. Cl. 568, 582 (2008) ("There is no record showing whether the Commissioner at all investigated the actions of each individual taxpayer or any explanation about the standard of care expected and the reason each taxpayer was found to fall short of this standard. . . . As a consequence, the taxpayers are in the position of needing to prove that they were not negligent without the benefit of knowing why the Commissioner thought that they were.").

1. Estoppel

Claims of estoppel by or against the Service generally require that (1) there be a false representation or wrongful misleading silence, (2) the error originate in a statement of fact and not in an opinion or statement of law, (3) the person claiming the benefit of estoppel must be ignorant of the true facts, and (4) the aggrieved party must be adversely affected by the acts or statements of the person against whom estoppel is claimed.⁹⁰ As noted above, relevant evidence is that which is relevant to the claim or defense of any party.⁹¹ Thus, in instances where the Service alleges the taxpayer should be estopped, the Service's detrimental reliance and ignorance of the true facts are directly at issue and can only be proven or disproven by the Service's thoughts, conclusions, reasoning, and factual findings. Conversely, in instances where the taxpayer alleges the Service should be estopped, whether the Service made a false representation or was wrongfully silent, and whether the error arose out of a statement of fact and not opinion or law are directly at issue and can only be proven or disproven by the Service's thoughts, conclusions, reasoning, and factual findings. The *de novo* doctrine should not apply to claims of estoppel because, if it did, taxpayers would be unable to access the evidence to prove or disprove such a claim or defense.

2. Variance

In tax refund actions, the doctrine of variance prevents taxpayers from raising issues at trial that vary from those it asserted in its administrative refund claim.⁹² A well-established exception to the doctrine of variance, however, states that:

90. See *Whitney v. United States*, 826 F.2d 896 (9th Cir. 1987) (citing *Lignos v. United States*, 439 F.2d 1365 (2d Cir. 1971)); *Stair v. United States*, 516 F.2d 560 (2d Cir. 1975); *Van Antwerp v. United States*, 92 F.2d 871, 875 (9th Cir. 1937) (citing *United States v. F.S. Scott & Sons*, 69 F.2d 728 (1st Cir. 1934)). See also *Botany Worsted Mills v. United States*, 278 U.S. 282, 288 (1929) (holding that an agreement which does not comply with the statutory requirements for compromises cannot be binding on the taxpayer or the Service).

91. See *supra* notes 62, 66. The Tax Court's rules apply a slightly broader rule, enabling discovery of information "relevant to the subject matter involved in the pending case." *Supra* note 66.

92. *Union Pac. R.R. Co. v. United States*, 389 F.2d 437 (Ct. Cl. 1968) (citing *United States v. Felt & Tarrant Mfg. Co.*, 283 U.S. 269 (1931); *Real Estate-Land Title & Trust Co. v. United States*, 309 U.S. 13, 17-18 (1940); *Int'l Curtis Marine Turbine Co. v. United States*, 56 F.2d 708 (Ct. Cl. 1932); *The Midvale Co. v. United States*, 138 F. Supp. 269 (Ct. Cl. 1956); *Williamson v. United States* 292 F.2d 524 (Ct. Cl. 1961)). Variance stems from section 7422, which states that suits for recovery of taxes cannot be maintained in any court until a claim for refund or

[A]n item raised in litigation but not specifically adverted to in the claim might be permitted if it is found that the taxpayer adequately alerted the Service to the fact that the item is a ground for refund, or that the Commissioner considered that unspecified ground in reaching his decision on the items for which a refund was requested.⁹³

Thus, what the Service knew and considered with respect to the items for which a refund was requested are relevant to whether variance applies to issues raised in litigation that a claim for refund did not expressly include.⁹⁴ Moreover, the purpose of the variance doctrine is to “prevent surprise and to give adequate notice to the Service of the nature of the claim and the specific facts upon which it is predicated, thereby permitting an administrative investigation and determination.”⁹⁵ Whether the Service undertook an administrative investigation and determination with respect to the claim and its underlying facts is directly relevant to whether the defense applies. The *de novo* doctrine should not apply when variance might be at issue because, if it did, taxpayers would be unable to access the evidence to disprove such a claim or defense.

3. *Shifting the Burden of Proof as to Factual Matters*

Finally, the taxpayer’s cooperation with the Service’s reasonable requests during its examination is a statutory prerequisite to shifting from the taxpayer to the Service the burden of proof on certain factual issues in tax litigation.⁹⁶ Under section 7491(a), if the taxpayer introduces credible evidence with respect to any factual issue in any court proceeding, the Service will bear the burden of proof on that factual issue, but only if the

credit has been duly filed, and from regulations which require a refund claim to “set forth in detail each ground upon which a credit or refund is claimed and facts sufficient to apprise the Commissioner of the exact basis thereof.” I.R.C. § 7422(a); Reg. § 301.6402-2(b)(1).

93. *Union Pac.*, 389 F.2d at 442 (citing cases). See also *Herrington v. United States*, 416 F.2d 1029, 1032 (10th Cir. 1969) (“Thus, if the claim fairly apprises the Service of the ground on which recovery is sought or if the Service actually considers the ground later sought to be raised the claim will be held adequate for . . . bringing suit under § 7422.”); *Garvey, Inc. v. United States*, 1 Cl. Ct. 108 (1983).

94. See *Computervision Corp. v. United States*, 445 F.3d 1355, 1370 (Fed. Cir. 2006); *Dillon, Read & Co., Inc. v. United States*, 15 Cl. Ct. 246, 251-52 (1988), *vacated*, 875 F.2d 293 (Fed. Cir. 1989).

95. *Union Pac.*, 389 F.2d at 442.

96. I.R.C. § 7491(a)(2)(B).

taxpayer meets certain conditions, including cooperating with the Service's examination.⁹⁷

The legislative history to section 7491(a) states:

[T]he taxpayer must cooperate with reasonable requests by the Secretary for meetings, interviews, witnesses, information, and documents (including providing, within a reasonable period of time, access to and inspection of witnesses, information, and documents within the control of the taxpayer, as reasonably requested by the Secretary). Cooperation also includes providing reasonable assistance to the Secretary in obtaining access to and inspection of witnesses, information, or documents not within the control of the taxpayer (including any witnesses, information, or documents located in foreign countries). A necessary element of cooperating with the Secretary is that the taxpayer must exhaust his or her administrative remedies (including any appeal rights provided by the IRS). The taxpayer is not required to agree to extend the statute of limitations to be considered to have cooperated with the Secretary. Cooperating also means that the taxpayer must establish the applicability of any privilege.⁹⁸

Section 7491(a) places directly at issue facts the Service requested and received, and events that occurred, at the administrative level, and whether those facts and circumstances were reasonable. Courts "consider all the surrounding facts and circumstances of [a] case in deciding whether [the Service's] request for witnesses, information, documents, meetings, and interviews is reasonable."⁹⁹ Moreover, "[w]hether the taxpayer cooperated with reasonable requests by the Commissioner for witnesses, information, documents, meetings, and interviews is based on all the surrounding facts and circumstances of the case."¹⁰⁰

Broadly applying the *de novo* doctrine as a standard of relevancy contradicts section 7491(a), which itself places at issue the facts gathered by

97. I.R.C. § 7491(a).

98. S. REP. NO. 105-174, at 45 (1998) (internal footnotes omitted).

99. *Polone v. Commissioner*, 86 T.C. Memo. (CCH) 698, 707, T.C. Memo. (RIA) ¶ 2003-339, 1957 (2003), *aff'd on other issue*, 449 F.3d 1041 (9th Cir. 2006). *See also* *Long Term Capital Holdings v. United States*, 330 F. Supp. 2d 122 (D. Conn. 2004), *aff'd on other issue*, 150 F. App'x 40 (2d Cir. 2005); *Southgate Master Fund, L.L.C. v. United States*, 651 F. Supp. 2d 596 (N.D. Tex. 2009), *aff'd on other issue*, 659 F.3d 466 (5th Cir. 2011).

100. *Polone*, 86 T.C. Memo. (CCH) at 707, T.C. Memo. (RIA) at 1957.

the Service and the general nature of its examination. Of course, one could argue that taxpayers have access to facts that prove whether or not they cooperated with the Service's examination, so the application of the *de novo* doctrine as a relevancy standard would do them no harm. But purely internal statements of Service employees regarding the audit and the taxpayer's and Service's conduct would also tend to prove whether or not the taxpayer cooperated with the Service and applying the *de novo* doctrine as a relevancy standard would preclude access to that information.

Noting a few examples where the Service's thoughts, procedures, conclusions, reasoning, or factual findings are directly at issue does not, by itself, doom the *de novo* doctrine's vitality as a standard of relevancy in other contexts. However, these examples illustrate the standard is not unconditional and generally undercut the doctrine's vitality as a relevancy standard. They also illustrate the broader implications of applying the *de novo* doctrine as a standard of relevancy in an unprincipled manner. Specifically, they raise the specter that the Service could seek to apply the *de novo* doctrine in a manner that enables it to withhold information harmful to the Service's claims or defenses, but disclose information beneficial to the Service's claims or defenses or harmful to taxpayers' claims or defenses, a matter of fairness to which this article now turns.

D. The De Novo Doctrine as a Standard of Relevancy Is Inimical to Well-Established Notions of Fundamental Fairness

In the tax realm, considerations of fundamental fairness are central to the government's mission.¹⁰¹ Fundamental fairness is also central to the discovery and evidentiary rules discussed above,¹⁰² so courts hold fairness

101. See The IRS Mission, <http://www.irs.gov/uac/The-Agency,-its-Mission-and-Statutory-Authority> (last updated Aug. 2, 2012) (stating that the Service's mission is to "[p]rovide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all"); United States Department of Justice Tax Division, Mission Statement, <http://www.justice.gov/tax/> (last visited Jan. 9, 2012) ("The Tax Division's mission is to enforce the nation's tax laws fully, fairly, and consistently, through both criminal and civil litigation, in order to promote voluntary compliance with the tax laws, maintain public confidence in the integrity of the tax system, and promote the sound development of the law.").

102. See, e.g., FED. R. CIV. P. 1 ("[These rules] should be construed and administered to secure the *just*, speedy, and inexpensive determination of every action and proceeding." (emphasis added)); TAX CT. R. 1(d) ("The Court's Rules shall be construed to secure the *just*, speedy, and inexpensive determination of every case." (emphasis added)); *Campbell Jr. v. Eastland*, 307 F.2d 478, 485 (5th Cir. 1962) ("It ought not to be necessary to resort to discovery against the Government . . . [T]he Government litigates with its citizens and ought to be frank and fair and

plays a role in disputes between taxpayers and the Service regarding the applicability of those rules.¹⁰³ Indeed, with respect to the discovery rules in tax cases, the Service is often “treated like any other litigant.”¹⁰⁴ However, reading the *de novo* doctrine as a standard of relevancy contradicts these principles and violates well-established notions of fundamental fairness.

The Service and Department of Justice regularly call as witnesses or deponents Service employees, including examining agents. On the other hand, and sometimes in the same cases,¹⁰⁵ the Service and Department of

disclose all facts.” (quoting Statement of William D. Mitchell, FEDERAL RULES OF CIVIL PROCEDURE, PROCEEDINGS OF THE INSTITUTE AT WASHINGTON, D.C., OCT. 6, 7, 8, 1938 AND OF THE SYMPOSIUM AT NEW YORK CITY OCT. 17, 18, 19, 1938 (Edward H. Hammond ed., 1939)).

103. *See* *Angelus Milling Co. v. Commissioner*, 325 U.S. 293, 297 (1945) (“Even tax administration does not as a matter of principle preclude considerations of fairness.”); *Eastland*, 307 F.2d at 485 (“Usually, when the taxpayer is seeking a refund or resisting payment of a tax deficiency assessed against him the United States is just another litigant. In such cases we start with the feeling that fundamental fairness to both sides — the Government starts with a great advantage in investigative resources — requires recognition of the taxpayer’s right to pre-trial discovery of the reports of the Internal Revenue Agents who examined the taxpayer’s books and records.”); *Beresford v. United States*, 123 F.R.D. 232, 233 (E.D. Mich. 1988) (“[I]t is apparent that Congress enacted [section 6103] as a shield to protect taxpayers from improper disclosure by the government of the information they were required to provide to it by law. The government now seeks to use this statute as a sword to avoid telling the taxpayer seeking a refund the information utilized in determining the tax. . . . While the government may not be able to introduce the return information at trial absent disclosure, it has already received the advantage of that information.”); *Peterson v. United States*, 52 F.R.D. 317, 321-22 (S.D. Ill. 1971) (“The Government, through its objections to Interrogatories Nos. 6 and 8, is seeking a favored position under the discovery rules. In a tax refund case, however, it should be treated as any other litigant.”); *Frazier v. Phinney*, 24 F.R.D. 406, 410 (S.D. Tex. 1959) (requiring the Service to produce various materials in its administrative files because “there is a sufficient necessity for the production of these documents and that denial of production would unduly prejudice the preparation of plaintiffs’ case. . . . Plaintiffs are entitled to know what defendant’s claims and contentions may be”).

104. *Peterson*, 52 F.R.D. at 321-22. *See also Eastland*, 307 F.2d at 485; *Barry v. Commissioner*, 1 B.T.A. 156, 157 (1924) (“To say that the taxpayer who brings his case before the Board is limited to questions presented before the Commissioner, and that the Board in its determination of the case is restricted to a decision of issues raised in the Internal Revenue Bureau would be to deny the taxpayer a full and complete hearing and an open and neutral consideration of his case.”).

105. *See, e.g., ISI Corp. v. United States*, 503 F.2d 558 (9th Cir. 1974); *LPCiminelli Interests, Inc. v. United States*, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,671, 110 A.F.T.R.2d (RIA) 2012-6631 (W.D.N.Y. 2012); *Panasonic Communications*

Justice often invoke the *de novo* doctrine and argue they (or their witnesses or deponents) may withhold from taxpayers or courts, on relevancy grounds, facts the Service gathered and analyzed during an examination. In these cases, the *de novo* doctrine can apply to prevent disclosure of information that the Service has already obtained the advantage of reviewing in contravention of the fundamental premise that litigants be fairly treated for discovery purposes absent a countervailing privilege.¹⁰⁶ Moreover, this type of selective disclosure of information is precluded in other discovery and evidentiary contexts such as when litigants attempt to use privileges as a “shield and a sword.”¹⁰⁷ Fairness suggests that facts and analysis the Service deems relevant to the examination of a taxpayer should likewise be relevant when the taxpayer seeks to challenge the merits of the Service’s adjustments in litigation. At a minimum, fairness should play a role when courts are asked to decide whether to give taxpayers access to facts and analysis used by the Service in making a determination.

Unfortunately, courts that articulate the *de novo* doctrine as a standard of relevancy have not analyzed the impact their articulations of the doctrine have on notions of fundamental fairness. But these notions should have a role and be considered when the Service asks courts to withhold information from its adversaries in litigation. While there may be countervailing concerns that would favor maintaining the *de novo* doctrine as a standard of relevancy despite its impact on fundamental fairness, courts should articulate such concerns and principles so that they too can become as ingrained in the discovery process as notions of fairness.

E. Courts are Regularly Asked to, and Increasingly Do, Decide Cases Based on Deference to the Service’s Thoughts, Procedures, Conclusions, Reasoning, or Factual Findings

Courts have long deferred to agencies when deciding cases, assuming the agency’s determination is reasonable. Broadly, deferring to agency decisions is justified by principles of encouraging uniformity and consistency in regulation, facilitating efficient administration of industry

Corp. v. United States, 99 Fed. Cl. 422 (Fed. Cl. 2011), vacated sup nom. In re United States, 669 F.3d 1333 (Fed. Cir. 2012).

106. See *Beresford*, 123 F.R.D. at 233 (requiring production where, “[w]hile the government may not be able to introduce the return information at trial absent disclosure, it has *already received the advantage of that information*” (emphasis added)).

107. See, e.g., *New Phoenix Sunrise Corp. v. Commissioner*, 408 Fed.App’x 908, 919 (6th Cir. 2010) (quoting *In re Lott*, 424 F.3d 446, 454 (6th Cir. 2005)). See also *Glenmede Trust Co. v. Thompson*, 56 F.3d 476, 486 (3d Cir. 1995); *In re G-I Holdings, Inc.*, 218 F.R.D. 428, 433 (D.N.J. 2003).

developments, and agency expertise.¹⁰⁸ Typically, courts apply such deference to the Service's regulations¹⁰⁹ although courts have deferred to the positions the Service takes in its Revenue Rulings¹¹⁰ and even in its litigation briefs with respect to individual taxpayers.¹¹¹ A recent case from the Second Circuit illustrates that the Service has increasingly been seeking — and receiving — deference from courts with respect to its expertise.

In *Union Carbide Corp. v. Commissioner*, the Service challenged Union Carbide's entitlement to research and development tax credits for supplies Union Carbide used in the conduct of qualified research.¹¹² At issue was whether Union Carbide's costs for the supplies used during the research, which would have been used in Union Carbide's manufacturing process regardless of any research, were "amount[s] paid or incurred for" supplies used in the conduct of qualified research.¹¹³ In its appellate brief, the Service argued that supply costs are not eligible for the credit if they would have been incurred regardless of any research activities.¹¹⁴ The Second Circuit agreed, stating that:

We ordinarily give deference to an agency's interpretation of its own ambiguous regulations, even if that interpretation appears in a legal brief. The interpretation advanced here does not fall into any of the enunciated categories where we would withhold such deference as it is not "plainly erroneous or inconsistent with the regulation," does not "conflict with prior interpretation" of the same regulation, and is not merely a "convenient litigating position" or a

108. See, e.g., Michael Hall, *From Muffler to Mayo: The Supreme Court's Decision to Apply Chevron to Treasury Regulations and Its Impact on Taxpayers*, 65 TAX LAW. 695, 702–06 (2012).

109. See, e.g., *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704 (2011).

110. See, e.g., *Bob Jones Univ. v. United States*, 461 U.S. 574 (1983).

111. See, e.g., *Union Carbide Corp. v. Commissioner*, 697 F.3d 104, 109 (2d Cir. 2012) ("We ordinarily give deference to an agency's interpretation of its own ambiguous regulations, even if that interpretation appears in a legal brief." (citing *Auer v. Robbins*, 519 U.S. 452, 461–62 (1997))); *Deweese v. Commissioner*, 870 F.2d 21 (1st Cir. 1989) ("For one thing, the Tax Court was obligated to give some deference to the Commissioner's view of the application of the sham in substance doctrine, and the 'for profit' language, to the facts of this case." (citing cases)).

112. *Union Carbide*, 697 F.3d at 105.

113. *Id.* at 106 (quoting I.R.C. § 41(b)(2)(A)(ii)).

114. *Id.* at 108–09.

“*post hoc* rationalization advanced by an agency seeking to defend past agency action against attack.”¹¹⁵

As *Union Carbide* suggests, in deciding whether to defer to the Service’s interpretation during litigation of its own ambiguous regulation, courts engage in an examination of the facts surrounding the interpretation itself. Whether the Service’s position is merely a “convenient litigating position” or a “*post hoc* rationalization” requires a detailed comparison of the Service’s institutional, administrative position with respect to an issue to the Service’s articulation of its position on the facts of a given case.¹¹⁶ More broadly, whether the Service’s position is reasonable requires an analysis of the facts and circumstances of the Service’s interpretation.¹¹⁷ The Service’s thoughts, procedures, conclusions, reasoning, or factual findings are relevant to such an inquiry because courts regularly cite them in upholding or overturning the Service’s actions. Applying the *de novo* doctrine as a standard of relevancy to preclude consideration of the Service’s thoughts, procedures, conclusions, reasoning, or factual findings ignores these issues, especially in cases where the Service claims its position with respect to a specific taxpayer in litigation is entitled to deference.¹¹⁸

These considerations acquire additional significance when the government in litigation seeks to use the *de novo* doctrine as a relevancy standard to distance itself from a contrary position the Service took

115. *Id.* (citations omitted).

116. See *Christopher v. SmithKline Beecham Corp.*, 132 S. Ct. 2156, 2166-69 (2012) (citing cases).

117. See *Mayo Found. for Med. Educ. & Research v. United States*, 131 S.Ct. 704, 714-16 (2011).

118. Moreover, the Service’s thoughts, procedures, conclusions, reasoning, or factual findings are relevant to whether deference to the Service’s position with respect to a specific taxpayer is supported by the policy rationale for deference in the first instance. A key reason why courts defer to agencies is because agencies are presumed to have “a body of experience and informed judgment to which courts and litigants may properly resort for guidance.” *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944). As the Supreme Court stated: “[T]he judgments about the way the real world works that [inform an agency’s] policy are precisely the kind that agencies are better equipped to make than are courts. This practical agency expertise is one of the principal justifications behind *Chevron* deference.”

Pension Benefit Guar. Corp. v. LTV Corp., 496 U.S. 633, 651-52 (1990). If the Service’s judgment — the informed thoughts, procedures, and reasoning its employees have developed over time — is relevant to whether a court should defer to that judgment as it is applied to all taxpayers through regulations, the Service’s judgment might also be relevant to whether a court should defer to that judgment as it is applied to individual taxpayers on a case-by-case basis. Nonetheless, a strict application of the *de novo* doctrine as a relevancy standard would preclude an informed inquiry into such judgment.

administratively while examining the taxpayer. For instance, in *LPCiminelli*, the Department of Justice argued that:

While the United States agrees that the IRS agents came to that conclusion, it asserts in this refund suit proceeding that the IRS agents were wrong. The United States contends in this motion that the fact that IRS agents came to an incorrect conclusion is irrelevant within the meaning of Fed. R. Evid. 402 and that therefore the proposed testimony and documents are inadmissible.¹¹⁹

The *LPCiminelli* opinion noted that “the notice of tax deficiency carries a presumption of correctness, requiring the taxpayer to demonstrate that the deficiency is incorrect,”¹²⁰ despite the fact that the Department of Justice argued in the same case that the Service’s stated ground for claiming a deficiency was incorrect.

LPCiminelli and *Union Carbide* raise two interesting questions that bear on the *de novo* doctrine as a relevancy standard. First, if courts should defer to the Service’s institutional expertise or litigating position on a case-by-case basis, why not provide support for such expertise to the taxpayers whose liabilities are being decided? And second, if the Service’s institutional expertise is correct in some instances but erroneous in others, how should the *de novo* doctrine as a relevancy standard apply when both instances allegedly occur at different phases of the same case?

A full discussion of how deference should apply in these circumstances is beyond the scope of this article (and is a briar patch *LPCiminelli* did not enter). Nonetheless, applying the *de novo* doctrine as a relevancy standard to preclude consideration of the Service’s factual findings, thoughts, reasoning, and conclusions conflicts with arguing courts should rely on those factual findings, thoughts, reasoning, and conclusions to decide cases. Moreover, situations like *LPCiminelli*, in which the government assumes a litigating stance contrary to a prior agency determination in the same case and then argues that a court should not rely on the Service’s factual findings, thoughts, reasoning, and conclusions, highlight this problem.¹²¹

119. Motion in Limine, *supra* note 2, at 2–3

120. *LPCiminelli Interests, Inc.*, 2012-2 U.S. Tax Cas. (CCH) ¶ 50,671, at 87,221, 110 A.F.T.R.2d (RIA) 2012-6631, 6634 (W.D.N.Y. 2012), (quoting *R.E. Dietz Corp. v. United States*, 939 F.2d 1, 4 (2d Cir.1991)).

121. This might especially be true when penalties are at issue, and courts must grapple with questions of whether substantial authority or a reasonable basis exists for a position or whether a taxpayer acted with reasonable cause and good faith. See I.R.C. § 6662(d)(2)(B)(i)-(ii)(II); Reg. § 1.6664-4(b)(1). In other words,

Unfortunately, however, courts that articulate the *de novo* doctrine as a standard of relevancy have not examined the impact their articulations of the doctrine might have on the deference the Service increasingly requests and receives. Nor have they examined how the *de novo* doctrine should operate in situations when the Service requests deference, but only to its litigating position and not to an allegedly erroneous position advanced during its examination of the taxpayer.

V. CONCLUSION

Historically, the *de novo* doctrine was not a standard of relevancy in the discovery or evidentiary context. It merely encompassed the idea that courts decide tax cases on the merits of taxpayers' liabilities for the year at issue, rather than on miscellaneous factors such as the Service's motives or reasons for initiating an audit or making an adjustment. Today, however, the doctrine is commonly and unjustifiably cited for the proposition that the Service may withhold from taxpayers on relevancy grounds information the Service gathered during its examination, even though the cases in which the doctrine arose do not stand for such a proposition.

Moreover, recent cases that have applied the doctrine have done so inconsistently, which encourages additional costly discovery and evidentiary disputes. Contemporary courts also fail to draw clear distinctions between taxpayers who genuinely seek factual and other information that might prove the merits of a tax case from intransigent litigants who merely want to argue that the Service's motives or reasons for initiating an audit or making an adjustment are improper. Applying the *de novo* doctrine as a standard of relevancy also contrasts with the broad scope of relevancy in the discovery and evidentiary contexts, is hostile to notions of fundamental fairness, fails to account for instances in which information in the Service's administrative files is directly relevant to claims or defenses of the parties, and raises thorny policy issues regarding deference in today's litigating environment.

All of these factors suggest the *de novo* doctrine is not relevant to relevancy. Courts should dispense with the *de novo* doctrine as a relevancy concept and return to the doctrine's simple, uncontroversial roots. Concerns that doing so would give litigants free access to the Service's administrative files are unjustified because well-established privileges — attorney-client privilege, work product, and deliberative process — would continue to apply to prohibit unwarranted disclosures. Alternatively, courts could articulate a principled, uniform approach to the doctrine as a relevancy standard that litigants can easily apply without court intervention. In so doing, however,

the fact that the Service examined but did not adjust an item might be relevant to whether a taxpayer should be penalized if the Service reverses course and makes an adjustment during litigation.

courts should address the additional concerns mentioned above, which have escaped judicial analysis to date.

FLORIDA TAX REVIEW

ARTICLE

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ALLOCATION RULES

Emily Cauble



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