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## Shifting the Burden of Proof: A Reckless Experiment

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The IRS restructuring bill (H.R. 2676) now pending in Congress contains a provision that would shift the burden of proof from taxpayer to IRS in most civil tax cases. The idea of burdening one's adversary is always appealing and there is little doubt that many Americans feel that the IRS is a blameworthy opponent. But present law places the burden of proof where it belongs in tax cases. The proposal to change the long-standing rule in civil tax litigation is misguided. It would add to the cost and complexity of tax disputes for taxpayer and IRS alike and yet is unlikely to enhance the fairness of tax law or tax administration. Indeed, the proposed change is more likely to harm honest taxpayers than it is to improve the functioning of either the IRS or of the Internal Revenue Code.

The Internal Revenue Code firmly and appropriately places the burden of proof on the IRS in criminal and civil tax fraud cases.

Similarly, where the IRS seeks extraordinary penalties in connection with tax evasion, it has the burden of proof. But in ordinary civil tax cases, there is a refutable presumption that the government's position is correct and the taxpayer has the burden of proving that the IRS is wrong.

Placing the burden of proof on taxpayers in civil tax cases is appropriate and necessary. The taxpayer is the party in possession of the facts at issue. In civil cases outside the tax area, the courts have ordinarily assumed that the burden of proof should be borne by the party in possession of the facts, which is the party most likely to be able to sustain the burden. The inherent logic of this view in non-tax litigation is reinforced in tax cases by the structure of the controversy. The IRS and taxpayer are not parties to a common transaction of which each has firsthand knowledge. The IRS has nothing to do with the taxpayer's affairs. The taxpayer asserts its view of the facts in its possession and its understanding of the law in filing its return. The IRS responds to the filing of (or failure to file) the

return. Typically, it is the taxpayer's own assertions in its own tax return that present law requires the taxpayer to prove.

H.R. 2676, which passed in the House of Representatives in October 1997 and is now awaiting action in the Senate Finance Committee, would assign to the IRS the burden of proof "in any court proceeding with respect to any factual issues relevant to ascertaining the income tax liability of a taxpayer," providing certain conditions are satisfied. The bill provides that the burden of proof shifts to the IRS only if the taxpayer "fully cooperated" with the Service with respect to the issue. Full cooperation is described as "including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer" that are "reasonably requested" by the IRS. The new rule would apply to more than 90% of individuals and businesses.

The preconditions for placing the burden of proof on the IRS in the trial phase of the controversy are apparently intended to leave the burden with the taxpayer in the

audit and administrative appeals phases, which account for the vast majority of taxpayer interactions with the IRS. The bill apparently envisions a new pretrial proceeding in which someone, probably the trial court, will determine whether the burden of proof is to shift to the IRS for the trial. While it is not clear how this new phase of tax controversies is to be implemented, it is very clear that it will be contentious and costly.

But an even more serious problem is that this change in law will needlessly disrupt tax collection for years to come. The numerous ambiguities in the bill's language and purpose will have to be clarified by the courts. It could well take a decade of appellate litigation before the law interpreting this new provision will be settled. What is to happen to tax collection in that decade?

Dishonest taxpayers will see this new system as an invitation to withhold information while they test the meaning of "full cooperation" and see what standards of proof are imposed on the IRS. Ambiguities in the proposed statute con-

cerning the requirement to substantiate items of income and expense may be seen as an encouragement to destroy records and falsify reporting. Tax evaders will have a field day for years as the courts struggle to develop meaningful standards.

Honest taxpayers may well be hurt also. Some may infer incorrectly that they no longer need to retain records since it will be up to the government to keep track of everything. They will be in for a rude shock when they discover that this is not the case.

If confusion over the burden of proof issue results in even a 1% fall-off in compliance, approximately \$10 billion in tax revenues would be lost annually. Pressure will inevitably grow to increase tax rates to make up the difference, tempting more taxpayers to cut corners and take their chances in court. As compliance drops, the efficacy and fairness of tax administration will inevitably diminish. But something even more valuable may be lost in the process: the noteworthy U.S. habit of voluntary tax compliance.

What impact shifting the bur-

den of proof will have on outcomes at trial is an open question. Many observers have noted that few cases are now won or lost on burden of proof issues alone. But this could change. It is not unusual for the testimony of the taxpayer to be the most relevant, if not the only, evidence of occurrences. Under present law, the courts can hold for the IRS where they find the taxpayer not to be a credible witness in such a case. But if the IRS has the burden of proof, the court's judgment that the taxpayer is lying may not be enough to carry the day for the government if it has no affirmative evidence to present. If affirmative evidence is required of the IRS, unscrupulous taxpayers will have all the more incentive to destroy records or simply never create them. Such behavior will increase the tax burden on honest taxpayers, make the IRS more aggressive at the audit stage and further fray at the fabric of voluntary compliance.

The idea that taxpayers should be encouraged to engage in paperless cash transactions or operate without meaningful records at this point in the development of infor-

mation technology seems particularly anomalous. It is easier than ever before for taxpayers to substantiate expenses and track income in managing their business and personal affairs. Why create a tax incentive to reverse this useful process?

The proposal to shift the burden of proof has been taken up by bipartisan Congressional leadership eager to make its mark against the IRS, even if it cannot figure out how to tackle the Internal Revenue Code. While it may not be intended to do so, the idea of shifting the burden of proof sends a confusing message to taxpayers, suggesting that henceforth they will not have to pay tax until the IRS proves what they owe. Confusion on this point could not come at a worse time. As the United States engages in an intense debate of the relative merits of the current income tax and fundamental tax reform, it is important to maintain our strong tradition of voluntary tax compliance. Whether we end up with a progressive income tax, a consumption tax, or a flat tax, we will need to collect it. Experimenting with the burden of proof is a reckless idea.