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Collateral Estoppel in Civil Tax Fraud Cases
Subsequent to Criminal Conviction

To secure compliance with federal income tax laws, Congress has provided both criminal and civil penalties.1 Fines and imprisonment are imposed under section 7201 of the Internal Revenue Code2 if the Government can prove beyond a reasonable doubt3 a willful

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2. Int. Rev. Code of 1954, § 7201 (formerly Int. Rev. Code of 1939, § 145(b)), reads in full: "Any person who willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, shall be fined not more than $10,000, or imprisoned not more than 5 years, or both, together with the costs of prosecution." Other criminal sanctions are provided for in §§ 7201-7344 of the 1954 Code.

attempt to evade or defeat taxation. Section 6653(b)\textsuperscript{4} authorizes, as a civil sanction, a fifty per cent addition upon findings by the Commissioner of fraudulent underpayment. These findings, if challenged by the taxpayer, need only be sustained by a preponderance of the evidence.\textsuperscript{5} Because of the similarity between the acts condemned by sections 7201 and 6653(b), conviction under section 7201 is frequently followed by a civil addition based on section 6653(b). The successive application of these sections has given rise to collateral estoppel problems.\textsuperscript{6} Although collateral estoppel operates to preclude relitigation of matters of law and fact actually at issue in a prior suit between the same parties and upon which the prior judgment ultimately rested,\textsuperscript{7} the Government's greater burden of proof

\textsuperscript{4} INT. REV. CODE OF 1954, § 6653(b) (formerly Int. Rev. Code of 1939, § 293(b)), reads in part: "(b) Fraud—If any part of any underpayment (as defined in subsection (c)) of tax required to be shown on a return is due to fraud, there shall be added to the tax an amount equal to 50 percent of the underpayment." Additional civil penalties are provided for in §§ 6601-6681 of the 1954 Code. Although more than one ad valorem penalty could be imposed on the same tax liability under the 1939 Code (see Fred N. Acker, 26 T.C. 107 (1956)), only one of the various civil penalties can be imposed under the 1954 Code. For example, if the 50\% fraud penalty is imposed under § 6653(b) of the 1954 Code, the 25\% delinquency penalty of § 6651 cannot also be imposed. See INT. REV. CODE OF 1954, § 6653(d).


\textsuperscript{6} In addition, subjecting the taxpayer to both criminal and civil penalties has raised questions of double jeopardy. Although the civil additions for fraud quite often entail a substantially larger sum than the previously assessed criminal fine for willful evasion (see, e.g., Abraham Teitelbaum, 29 P-H Tax Ct. Mem. 55 (1960); Vincent Cefalu, 27 P-H Tax Ct. Mem. 181 (1959), aff'd, 276 F.2d 122 (5th Cir. 1956); Jolly's Motor Livery Co., 26 P-H Tax Ct. Mem. 886 (1957)), the Supreme Court has held that the fifth amendment's double jeopardy clause is not violated. Helvering v. Mitchell, 303 U.S. 391 (1938). See Kenney v. Commissioner, 111 F.2d 374 (5th Cir. 1940); cf. Inman v. United States, 151 F. Supp. 784 (W.D.S.C. 1957). See generally 1959 DUKE L.J. 146.

\textsuperscript{7} The term "res judicata" embraces two related concepts which are not always clearly distinguished. First, when there is a final judgment on the merits, parties to the suit and their privies are bound in a subsequent suit on the same cause of action as to every matter which actually was or could have been litigated. See McCall v. Commissioner, 312 F.2d 699 (4th Cir. 1963); Hyman v. Regensthein, 258 F.2d 502, 509 (6th Cir. 1958); The Evergreens v. Nunan, 141 F.2d 927 (2d Cir. 1944); The Two branches of this first doctrine are merger and bar. If the plaintiff prevails, the cause of action merges into the judgment and is extinguished. See Commissioner v. Sunnen, 333 U.S. 591 (1948); Filice v. United States, 271 F.2d 782 (9th Cir. 1959), cert. denied, 362 U.S. 924 (1960). If the plaintiff loses, a final judgment on the merits bars any future suit on the same cause of action. See Tait v. Western Maryland Ry., 289 U.S. 620 (1933); Taylor v. Anderson, 303 F.2d 546 (4th Cir. 1962). Since proceedings under §§ 7201 and 6653(b) constitute separate causes of action, merger and bar are unavailable to either the government or the taxpayer in the subsequent civil dispute. See Helvering v. Mitchell, supra note 6; John W. Amos, 43 T.C. 50 (1964); Eugene Vasallo, 23 T.C. 566 (1955).

The second concept embraced by res judicata, commonly termed "collateral estop-
in a section 7201 criminal prosecution prevents the taxpayer from maintaining that an acquittal under section 7201 should preclude a section 6653(b) civil penalty. As the Supreme Court has pointed out, failure to prove a violation beyond a reasonable doubt should not estop the Government to attempt to prove one by a preponderance of the evidence. However, when a taxpayer is convicted in the criminal prosecution, the question of whether collateral estoppel should be applied in a subsequent civil suit has caused a recent split of judicial opinion. Collateral estoppel was applied in *Tomlinson v. Leftowitz* and *John W. Amos,* but not in *Moore v. United States.*

To apply collateral estoppel in a section 6653(b) civil tax fraud case following a section 7201 criminal conviction, it is necessary to establish that proof of a willful attempt to evade or defeat a tax required by section 7201 encompasses proof of fraud within the meaning of section 6653(b). The courts in *Amos* and *Tomlinson* squarely confronted this task, citing considerable authority tending

pel;" is broader in some respects than merger and bar because it applies to suits on a different cause of action. However, in other respects it is narrower than merger and bar since it operates to preclude litigation only of matters of law and fact which were actually at issue in a prior suit and upon which the prior judgment ultimately rested. See *McGill v. Commissioner,* *supra*; *Hyman v. Regenstein,* *supra* at 509-11; The *Evergreens v. Nunan,* *supra.* See generally Branscomb, *Collateral Estoppel in Tax Cases—Static and Separable Facts,* 37 Texas L. Rev. 584 (1959); *Lore, Res Judicata in the Tax Laws,* 34 Taxes 455 (1956); Polasky, *Collateral Estoppel—Effects of Prior Litigation,* 39 Iowa L. Rev. 217 (1954); Note, 35 Iowa L. Rev. 700 (1950).

In the leading case of *The Evergreens v. Nunan,* *supra,* Judge Learned Hand first promulgated the "ultimate fact-mediate datum" test followed by the Restatement of Judgments, § 68. Judge Hand stated that collateral estoppel should apply only to "those facts, upon whose combined occurrence the law raises the duty, or the right, in question [the ultimate facts]." Mediate data—facts "from whose existence may be rationally inferred the existence of [ultimate facts]"—should not call into play collateral estoppel. The *Evergreens v. Nunan,* *supra,* at 926. Judge Hand also maintained that collateral estoppel should apply only to ultimate facts in the second suit as well, because otherwise "what jural relevance facts may acquire in the future... is often impossible even remotely to anticipate." Id. at 929. The latter concept has not been so widely accepted as the former. See United States v. Cathcard, 70 F. Supp. 653 (D. Neb. 1946). The "ultimate fact" doctrine was accepted by the Supreme Court in *Yates v. United States,* 354 U.S. 298, 338 (1957). See generally Polasky, *supra,* at 287-39.

Generally, the United States, the Commissioner, and District Directors of Internal Revenue are considered as one "party" so as to make a decision affecting one binding on all. See *Tait v. Western Maryland Ry.,* 289 U.S. 620 (1933); Edward H. Garcia, 22 B.T.A. 1027 (1931).

For a discussion of the effect of consent judgments in tax cases, see 52 Mich. L. Rev. 303 (1953).


10. 334 F.2d 262 (5th Cir. 1964).


13. See, e.g., *Spies v. United States,* 317 U.S. 492 (1943); *Bloch v. United States,* 221 F.2d 786, 788 (9th Cir. 1955); *Wardlaw v. United States,* 208 F.2d 884, 885 (6th Cir. 1953); *Mitchell v. Commissioner,* 118 F.2d 308 (5th Cir. 1941).
to support their conclusion that the term “willfully” as used in section 7201 had been judicially defined to embrace all of the elements of section 6653(b) fraud. In addition, the Tomlinson court cited cases involving proceedings to deport persons convicted of willful tax evasion which held that the equivalent of an intent to defraud the United States must be proved in section 7201 criminal prosecutions.

The courts applying collateral estoppel could have buttressed their position with three additional arguments. First, section 6653(b) fraud is not common-law fraud, but rather a statutory fraud, inferable from any conduct calculated to mislead or conceal; it is difficult to envision any willful attempt to evade or defeat payment of taxes which would not fall within this broad concept. Second, it has been judicially established that an indictment for willful evasion under section 7201 must allege a specific intent to defraud the Government. Third, it has been held that the intent which

14. "Willfully" within the purview of section 7201, comprehends a specific intent involving the bad purpose and evil motive to evade or defeat the payment of tax." John W. Amos, 43 T.C. 50, 65 (1964). A specific intent involving an evil motive to evade seems equivalent to fraud. See Spies v. United States, supra note 13; Bloch v. United States, supra note 13; Wardlaw v. United States, supra note 13.

The leading case of Spies v. United States, supra note 13, held that a simple failure to file a return did not bring one within § 145(b) (the 1939 Code predecessor of § 7201); some overt act was necessary. The Spies case was followed in United States v. Croessant, 178 F.2d 96 (3d Cir. 1949), cert. denied, 339 U.S. 927 (1950): "There is substance . . . in distinguishing between failing to file a return and knowingly filing a false one. . . . The law has always distinguished between failing to disclose useful information and making a disclosure which is a lie." Id. at 97. Accord, Reynolds v. United States, 288 F.2d 78 (5th Cir. 1961). The essential similarity between the criminal and civil sanctions was further demonstrated when the Spies doctrine was held applicable to civil fraud cases in Cirillo v. Commissioner, 314 F.2d 478, 482 (3d Cir. 1963).

Cohen v. United States, 297 F.2d 760 (9th Cir. 1962), declared that under § 7201 a willful and knowing attempt to evade the payment of tax (such as making certain that money acquired does not go to pay a previously assessed tax) can be different from a willful and knowing attempt to defeat the tax (such as the use of false returns or double books). If that distinction is valid, it is possible that evading payment under § 7201 does not necessarily imply fraud within the purview of § 6653(b).

For cases discussing § 7201 and its predecessors in terms of fraud, see United States v. Palermo, 293 F.2d 872 (5th Cir. 1960); Goun v. United States, 184 F.2d 284 (1st Cir. 1950), cert. denied, 394 U.S. 917 (1951); cf. Blauner v. United States, 293 F.2d 723 (8th Cir. 1961); United States v. Allied Stevedoring Corp., 241 F.2d 925 (2d Cir. 1957).

15. See Tseung Chu v. Cornell, 247 F.2d 929 (9th Cir. 1957); Chanan Din Khan v. Barber, 147 F. Supp. 771, 775 (N.D. Cal. 1957), aff'd, 253 F.2d 547 (9th Cir.), cert. denied, 597 U.S. 925 (1958).

17. See Elwert v. United States, 281 F.2d 928 (9th Cir. 1956), in which the defendant in a criminal prosecution under § 145(b) of the 1939 Code—the predecessor of § 7201—maintained that the indictment was insufficient because it failed to allege a specific intent to defraud the Government. The court held the indictment sufficient because Elwert failed to show that he was prejudiced, although he agreed that a specific intent to defraud must be proved. "The requirement of such a specific intent resulted from an interpretation of the word 'willfully' in Section 145(b) and imposed on the United States a more difficult burden of proof than is normally required in a criminal case."
must be proved to establish section 6653(b) fraud is the "specific purpose to evade." The predecessor in the 1939 Code of section 6653(b) expressly utilized the phrase "fraud with intent to evade tax," and there is no indication that its deletion from the 1954 Code was intended to effect a substantive change.

Before the arguments supporting the application of collateral estoppel could be deemed decisive, however, the court in Amos was forced to distinguish a Supreme Court case, United States v. Scharton, which was heavily relied upon in Moore as authority for holding collateral estoppel inapplicable. In Scharton, the defendant was indicted under a statute essentially identical to section 7201 more than three but less than six years after an alleged willful tax evasion. At issue was the applicability of a clause extending the three-year statute of limitations to six years for "offenses involving the defrauding or attempting to defraud the United States." The Government contended that the statute of limitations should be extended because willful evasion necessarily includes every element of fraud. The Supreme Court never squarely faced this contention, but decided that the extension clause should not apply because it was "an excepting clause and therefore to be narrowly construed." Thus, the Court did not hold in Scharton that the elements comprising willful evasion do not embrace the components of fraud. Moreover, as the Amos court noted, Scharton's restrictive approach to statutory construction has since been rejected by the Supreme Court.

Id. at 931. The court asserted that "this requirement has crystallized only in recent years," thus rendering doubtful prior authority holding it sufficient to frame an indictment in the language of § 145(b). Compare Bloch v. United States, 221 F.2d 786, 788 (9th Cir. 1955), with Capone v. United States, 56 F.2d 927 (7th Cir. 1932), cert. denied, 286 U.S. 553 (1932).

18. Mitchell v. Commissioner, 118 F.2d 308, 310 (5th Cir. 1941); see Powell v. Granquist, 252 F.2d 56, 60 (9th Cir. 1958); Eagle v. Commissioner, 242 F.2d 685, 637 (9th Cir. 1957); In the Matter of Parr, 205 F. Supp. 492 (S.D. Texas 1962).

19. See 10 MERR\*N, op. cit. supra note 1, § 55.09 n.83.5.


21. Language from another distinguishable case, Commissioner v. Sunnen, 333 U.S. 591 (1948), was also relied upon by the dissenters in Amos to support their conclusion that collateral estoppel was inapplicable. In Sunnen, the Supreme Court declared that collateral estoppel "must be confined to situations where the matter raised in the second suit is identical in all respects with that decided in the first proceeding and where the controlling facts and applicable legal rules remain unchanged." Id. at 599-600. This statement, however, viewed in context, is not aimed at formal differences in statutory language. The Court in Sunnen was concerned with the possibility of a prior decision becoming obsolete by an evolution or change in legal doctrine. This justifiable concern is not relevant to an application of collateral estoppel between §§ 7201 and 6653(b) if the sections' constituent elements are deemed identical. The change which concerned the Sunnen Court was a change in substantive law and not legal language. Cf. Jones v. Trapp, 186 F.2d 951 (10th Cir. 1950).


Although the Amos and Tomlinson courts demonstrated that collateral estoppel can be applied in the subsequent action under section 6653(b), in concluding that collateral estoppel should be applied these courts failed to analyze correctly the relevant policy considerations. One of the primary justifications for applying collateral estoppel is the possibility of effecting a marked saving of judicial time. However, application of collateral estoppel in this instance will not accomplish that result. While it is true that proof of fraud or tax evasion can require an exhaustive compilation of the taxpayer's every item of income and expense for an entire year, and that careful consideration of this evidence involves many judicial man-hours, collateral estoppel applies only to findings of fact upon which the prior conviction necessarily rests. While some deficiency must be proved to establish a willful evasion under section 7201, the exact amount need not. Therefore, even though the taxpayer is collaterally estopped to relitigate the issue of fraud in a subsequent section 6653(b) dispute, the exact deficiency to which the fifty per cent penalty will attach is still subject to litigation. Thus, whether or not collateral estoppel is applied, the court must reexamine the voluminous evidence.

A second consideration underlying the doctrine of collateral estoppel is the policy favoring the establishment of certainty in legal relations. Certainty, however, must give way if a party is unfairly burdened. Therefore, the argument by an Amos dissenter that application of collateral estoppel is unfair because it gives the Government the benefit of a "one-way street" is quite persuasive. As noted before, when the taxpayer-defendant is acquitted in a prosecution under section 7201, the difference in burdens of proof prevents his pleading collateral estoppel in a subsequent civil suit. The potential inequities of this one-sided availability are best illustrated by William Hendrick, in which a poorly educated immigrant waiter who failed to report his income from tips pleaded guilty in a criminal prosecution in order to permit prompt conclusion at minimum legal expense. He was fined $250 and put on probation for six months. Subsequently, he was confronted by the Commissioner with an addition of approximately $1500, a sum certainly not in contem-

30. See The Evergreens v. Nunan, 141 F.2d 927 (2d Cir. 1944); Polasky, supra note 7, at 250.
plation when he pleaded guilty. The court, acknowledging the taxpayer's motive for pleading guilty, gave no weight to the prior conviction, and was able to hold that there had been no fraud. Of course, if collateral estoppel had been held applicable, the court would have been precluded from reexamining the prior conviction. Such an application of collateral estoppel would in effect force defendants to engage in expensive criminal litigation even when the anticipated punishment does not merit it. Moreover, even if the defendant prevailed after this otherwise unwarranted expense, he would still be potentially subject to the expense of a civil proceeding. Thus, a defendant situated as was Hendrick would be, in effect, forced to defend twice against the civil addition.\textsuperscript{33}

Finally, the application of collateral estoppel will virtually eliminate the taxpayer's choice of forum. Normally, the taxpayer may elect to contest a civil addition in the Tax Court, the Court of Claims, or a federal district court. This choice will depend on such factors as financial resources, desirability of expert fact-finding, and variances among courts in construction of the Code.\textsuperscript{34}

\textsuperscript{33} This unjust result could be partially mitigated by the free granting of the plea of \textit{nolo contendere} in § 7201 prosecutions. Such a plea would prevent any mention of a § 7201 conviction in a subsequent § 6653(b) civil proceeding. See Mickler v. Fahs, 249 F.2d 518 (5th Cir. 1957) (mention of a former \textit{nolo contendere} plea in a § 6653(b) civil proceeding held prejudicial error requiring reversal of a judgment for the Commissioner); cf. B. Frank Wells, Jr., 27 P-H Tax Ct. Mem. 684 (1958). \textit{But see} Broadhead v. Enochs, 162 F. Supp. 897, 899 (1958) ("[T]he plea of \textit{nolo contendere} has very little, if any, weight."); See generally Hudson v. United States, 272 U.S. 451 (1926). \textit{Fed. R. Crim. P. 1} provides that \textit{nolo contendere} is available only at the discretion of the court; the Department of Justice may be counted upon to resist it. See Ferguson, \textit{Jurisdictional Problems in Federal Tax Controversies}, 48 Iowa L. Rev. 512, 522 (1963). Nevertheless, a liberal approach to its use has been urged. See United States v. Jones, 119 F. Supp. 288 (S.D. Cal. 1954). "Defendants claim a potential of civil litigation based upon the same transactions pleaded in the indictment. They tell the Court that they are willing not to contend against the charges but desire not to create evidence which could be used as an admission in other potential litigation. To avoid exacting an admission which could be so used, is the main, if not only, modern purpose of \textit{nolo contendere}." Id. at 289. \textit{But see} United States v. Bagliore, 182 F. Supp. 714 (E.D.N.Y. 1960), in which the court stated that no other authorities could be found to support the liberal approach of \textit{Jones}.

Even if \textit{nolo contendere} is henceforth readily available, however, the basic concept of mutuality of estoppel would seem to be violated. Strictly construed, the doctrine of mutuality prevents a party from invoking collateral estoppel unless he would have been bound if the prior judgment had gone the other way. See Lawlor v. National Screen Serv. Corp., 349 U.S. 322 (1955). Therefore, when the Government seeks to utilize § 7201 criminal convictions to preclude relitigation of the fraud issue, it would seem that collateral estoppel should not be applied because the defendant could not so utilize an acquittal because of the different burdens of proof. Nevertheless, it is clear that in federal courts collateral estoppel will operate between a criminal conviction and a civil dispute if the parties are the same. See United States v. Rubin, 243 F.2d 900 (7th Cir. 1957); Lentin v. Commissioner, 226 F.2d 690 (7th Cir. 1955), cert. denied, 350 U.S. 934 (1956). See generally 1B Moore, \textit{Federal Practice} § 0.418[1] (2d ed. 1955).

\textsuperscript{34} See Bittker, \textit{FEDERAL INCOME ESTATE & GIFT TAXATION} 934-43 (3d ed. 1964); Ferguson, supra note 33.
lateral estoppel is applied, the taxpayer will, in effect, be limited to the district courts, where the criminal actions are prosecuted. In view of the potential complexities of tax cases, it is indeed arguable that collateral estoppel should not be allowed to preclude a choice available to all other tax litigants. This, coupled with the double burden placed upon the taxpayer in exchange for a negligible saving in judicial time, suggests that collateral estoppel, while technically applicable, should not operate between section 7201 and section 6653(b) proceedings.