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Must the Reports of Tax Court Special Trial Judges Be Disclosed?

by Leandra Lederman

PREVIEW of United States Supreme Court Cases, pages 131-135. © 2004 American Bar Association.

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Editor's Note: PREVIEW's deadline precluded discussion of arguments made in petitioners' reply briefs.

ISSUES

Is disclosure of a Special Trial Judge's report in a case heard under Tax Court Rule 183 required by the Due Process Clause of the Constitution, the right to effective Article III appellate review, or federal statutes?

Does Tax Court Rule 183 require Tax Court judges to uphold Special Trial Judges' findings of fact and credibility judgments unless they are clearly erroneous?

FACTS

Burton W. Kanter was a well-known tax lawyer, as well as an adjunct professor of law and a businessman. Claude Ballard and Robert Lisle were real estate executives for Prudential Life Insurance Co. of America (Prudential). The Internal

Revenue Service (IRS) alleged that Messrs. Kanter, Ballard, and Lisle had an arrangement under which individuals seeking to do business with Prudential made payments to corporations controlled by Kanter, which were then distributed to Kanter, Ballard, and Lisle or entities they controlled. Kanter, Ballard, and Lisle did not report the payments on their individual returns. The IRS therefore asserted deficiencies in their taxes and subsequently alleged that their actions were fraudulent.

In the United States Tax Court (Tax Court), the cases were consolidated and assigned to Special Trial Judge Couvillion, who conducted a trial that lasted almost five weeks. Special Trial Judges (STJs) are judicial officers appointed by the chief

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*BALLARD ET UX. V. COMMISSIONER
OF INTERNAL REVENUE*

AND

*ESTATE OF KANTER ET AL. V.
COMMISSIONER OF INTERNAL
REVENUE*

DOCKET NOS. 03-184 AND
03-1034

ARGUMENT DATE:
DECEMBER 7, 2004

FROM: THE ELEVENTH AND THE
SEVENTH CIRCUITS

Case at a Glance

Special Trial Judges (STJs), judicial officers appointed by the chief judge of the United States Tax Court, are authorized by statute to hear but not to decide cases involving large tax deficiencies. An STJ who conducts the trial in such a case submits a report to the chief judge, who then assigns the case to a regular judge. In these cases, which involved both tax deficiencies and fraud penalties, the taxpayers are seeking disclosure of the STJ's report.



judge of the Tax Court. Under 26 U.S.C. § 7443A, the STJ did not have the authority “to make the decision of the court” in the consolidated cases because the tax deficiencies in dispute exceeded \$50,000. Therefore, as required by Tax Court Rule 183, after trial, the STJ submitted a report to the chief judge of the Tax Court. The chief judge reassigned the matter to Judge Dawson. In 1999, Judge Dawson issued an opinion finding the taxpayers liable for millions of dollars in tax deficiencies and penalties, including fraud penalties. See *Investment Research Assocs. v. Commissioner*, T.C. Memo. 1999-407. As is typical in cases decided under Tax Court Rule 183, the Tax Court’s opinion states that “[t]he Court agrees with and adopts the opinion of the Special Trial Judge, which is set forth below.”

In April and May 2000, the taxpayers filed motions seeking “all reports, draft opinions, or similar documents” prepared by the STJ in their cases or, in the alternative, to have the Tax Court include the original STJ report in the record sent to the Courts of Appeals. The second motion sought to have the report placed under seal for the Courts of Appeals’ review. The Tax Court denied the motions. In August 2000, the taxpayers made a motion for reconsideration that was accompanied by an affidavit. The affidavit, signed by one of the attorneys for the Kanters, Randall Dick, stated that two Tax Court judges had informed him that the STJ’s original report had found that the taxpayers were not taxable on payments made by certain individuals seeking to do business with Prudential and that the fraud penalty did not apply. On August 30, 2000, the Tax Court denied the motion for reconsideration, stating, in part, “Judge Dawson states and Special Trial Judge Couvillion agrees, that, after a metic-

ulous and time-consuming review of the complex record in these cases, Judge Dawson adopted the findings of fact and opinion of Special Trial Judge Couvillion. ...” *Tax Court Order Denying Request for Access to STJ Report*, 2001 TNT 23-30. Each of the three taxpayers filed petitions for writs of *mandamus* in their respective circuits, which were denied. The taxpayers subsequently appealed to those circuits.

In *Ballard v. Commissioner*, the Eleventh Circuit affirmed the Tax Court’s decision. With respect to the issue of the STJ report, the court stated “the record as presented to us clearly reveals that the report adopted by the Tax Court is Special Trial Judge Couvillion’s report. This critical fact is exhibited in the August 30, 2000 Order signed by Special Trial Judge Couvillion, Judge Dawson and the Chief Judge of the Tax Court.” *Ballard*, 321 F.3d 1037, 1042 (11th Cir. 2003). The Eleventh Circuit also held that “[e]ven assuming Dick’s affidavit to be true and affording Petitioners-Appellants all reasonable inferences, the process utilized in this case does not give rise to due process concern.” The taxpayers in *Ballard* petitioned for *certiorari* on issues relating to disclosure of the STJ’s report.

In *Estate of Kanter v. Commissioner*, the Seventh Circuit affirmed the Tax Court on all but one of the eight issues it considered, a tax deduction issue. With respect to the STJ’s report, the court stated that “[t]he Tax Court’s final opinion clearly states that it ‘agrees with and adopts the opinion of the Special Trial Judge.’ ... The Chief Judge of the Tax Court, Judge Dawson, and Special Trial Judge Couvillion himself all signed the [Tax Court’s] final opinion, and we take their statement at face value. Therefore, notwithstanding Kanter’s attorney’s declaration, we accept as

true the Tax Court’s statement that the underlying report adopted by the Tax Court was in fact Special Trial Judge Couvillion’s.” *Estate of Kanter*, 337 F.3d 833, 840-41 (7th Cir. 2003). The Seventh Circuit also found that a “purportedly quasi-colaborative [judicial deliberation] process would not offend our notions of fundamental fairness, nor would due process require the inclusion of the report in the appellate record to preserve the fairness of our review.” Judge Cudahy dissented on the issue of the STJ’s report, arguing that the report must be included in the record on appeal for the Court of Appeals to review. As in *Ballard*, the taxpayers in *Estate of Kanter* petitioned for *certiorari* on issues relating to disclosure of the STJ’s report.

In *Estate of Lisle v. Commissioner*, which is not before the Supreme Court, the Fifth Circuit reversed the Tax Court on the fraud issue, which resulted in one of the tax years being barred by the statute of limitations and eliminated liability for any fraud penalty. On the issue of the STJ’s report, the court stated, “[w]e find the reasoning of the Seventh and Eleventh Circuits direct and persuasive, and adopt it here. We hold that the application of Rule 183 in this case did not violate Appellants’ due process rights.” *Estate of Lisle*, 341 F.3d 364, 384 (5th Cir. 2003). Neither party petitioned for *certiorari* in *Estate of Lisle*.

CASE ANALYSIS

The Internal Revenue Code provides the Tax Court with the authority to promulgate its own rules of practice and procedure. Tax Court Rule 183(b), which applied to the consolidated Tax Court proceeding, provides that the STJ “submit[s] a report, including findings of fact and opinion, to the Chief Judge” and the



chief judge assigns the case to a reviewing judge. The reviewing judge “may adopt the Special Trial Judge’s report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.” Tax Ct. R. 183(c).

This rule does not provide for disclosure of the report, unlike a prior version of the rule. Until 1983, the last line of former Tax Court Rule 182(b) provided, “[a] copy of the report shall forthwith be served on each party.” In addition, former Tax Court Rule 182(c) provided, in part, “[w]ithin 45 days after service of the Special Trial Judge’s report, a party may file with the Court a brief setting forth any exceptions of law or fact to that report.”

In their briefs, the taxpayers argue that the Due Process Clause of the Fifth Amendment to the Constitution, the right to meaningful review by an Article III court, and/or federal statutes require disclosure of the STJ’s report. The taxpayers make due process arguments both with respect to the Tax Court proceeding and with respect to appellate review of the Tax Court’s decision. In addition, the taxpayers argue that Tax Court Rule 183 requires deference to the STJ’s report.

In its brief, the government both responds to these arguments, as discussed below, and counters with an argument of its own. The government first contends that the taxpayers’ principal arguments for disclo-

sure of the STJ’s report “are not properly presented in these cases” because, it argues, STJ Couvillion’s “final report” was adopted by the Tax Court and therefore was disclosed in the Tax Court’s opinion. The government further argues that any “original” report submitted by STJ Couvillion is part of his confidential deliberative processes and litigants cannot compel disclosure of these processes. The government maintains that suggestions that the reviewing judge improperly influenced the STJ or that the reviewing judge and STJ collaborated are not sufficient to warrant disclosure of the STJ’s report. It also argues that judges are presumed to have discharged their responsibilities.

With respect to due process in the Tax Court proceeding, the taxpayers contend that they are entitled to see the STJ’s report because they are entitled to know the basis of the court’s decision. In addition, the taxpayers emphasize that the STJ was the one who presided over the trial and had the opportunity to observe the witnesses. They cite cases such as *United States v. Raddatz*, 447 U.S. 667 (1980), in which the Supreme Court expressed concern about the prospect of a judge who did not observe the witnesses rejecting the credibility determinations made by a magistrate judge who did.

The government counters that the Constitution does not compel disclosure of the STJ’s credibility assessments. It argues that *Raddatz* is not applicable because that case involved a criminal proceeding. In addition, the government argues that, in *Raddatz*, the Court found that the Constitution did not preclude *de novo* review of credibility determinations so long as the court could rehear evidence if it so chose, and Tax Court Rule 183 permits the reviewing judge to “receive further evidence” or direct the parties to file additional briefs.

The taxpayers also contend that all other areas of modern federal law provide for routine disclosure of initial factual findings, so that the Tax Court’s process is at odds with established norms and presumptively violates the Due Process Clause. The government responds that the full range of procedural protections applicable in proceedings governed by Article III of the Constitution is not required for tax cases. It also argues that the Tax Court’s nondisclosure practice in the Rule 183 context is not unique, pointing both to 26 U.S.C. § 7460(b), which provides that the report of a judge in a case in which the chief judge directs its review by the full Tax Court “shall not be a part of the record,” and to a non-tax example involving boards of contract appeals established by administrative agencies.

The taxpayers also argue that disclosure of the STJ’s report is supported by the balancing test of *Mathews v. Eldridge*, 424 U.S. 319 (1976). In identifying what due process requires, *Mathews* considered (1) the nature of the private interest involved; (2) the likely reduction in the risk of an erroneous deprivation that the procedural safeguards sought would provide; and (3) the government’s interest, including the burdens that the procedural safeguards sought would impose. In *Ballard* and *Estate of Kanter*, the taxpayers assert the importance of the interests of taxpayers in tax fraud cases, the necessity of disclosure of the report for accurate decision making, and the lack of burden in disclosing a report that is already required to be prepared. The taxpayers maintain that, in fact, disclosure of the STJ’s report would provide a benefit by increasing the accountability of the Tax Court.

The government responds that because the taxpayers received

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extensive process in the Tax Court, the taxpayers' interest in disclosure of the STJ's original report is insignificant. By contrast, the government argues, its interest in maintaining the current procedure is substantial because of its interest in considered and confidential decision making, the additional time that would be required for review were the STJ's report disclosed, and the government's interest in tax collection more generally.

With respect to due process on appeal, the taxpayers argue that, in order to conduct proper review, a court of appeals must have a complete record that includes the original findings of fact. The taxpayers in *Estate of Kanter* emphasize the "clearly erroneous" standard of review that courts of appeals must apply to Tax Court decisions, which they contend requires access to the initial factual findings. The taxpayers in both cases argue that this access is particularly important when the factfinder makes credibility judgments.

The taxpayers in *Ballard* also contend that they have a right to meaningful review by an Article III court. They argue both that once Congress has granted the right to seek review of a decision in an Article III court, the Tax Court cannot effectively eliminate that right, and that Supreme Court precedent allows decision making by Article I courts only when the parties in those cases have a right to appeal to an Article III court. The government counters that disclosure of the original report of an STJ is not required for effective appellate review. The government argues that, by statute, in tax cases of this type, only a Tax Court judge, not an STJ, can make the decision of the court, and only that decision is subject to appellate review.

The taxpayers in both *Ballard* and *Estate of Kanter* also argue that the

appellate review statute, 26 U.S.C. § 7482(a)(1), requires disclosure of the STJ's report in order for an appellate court to review a Tax Court's decision "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury," as the statute provides. They argue that the reports and recommendations of magistrate judges, special masters, and bankruptcy judges are all included in the record on appeal and are necessary for meaningful review of district court decisions, so that failure to provide the STJ's report to a reviewing court violates the statutory requirement.

The government contends that the Internal Revenue Code does not require disclosure of the STJ's report. It argues that "Congress did not intend the 'in the same manner' language of Section 7482(a)(1) to import the standards or procedural rules applicable to proceedings before a magistrate judge. ..." but merely responded to the Supreme Court's decision in *Dobson v. Commissioner*, 320 U.S. 489 (1943), which had curtailed appellate review of Tax Court decisions.

The taxpayers in *Estate of Kanter* also argue that 26 U.S.C. § 7461(a), which provides that "all reports of the Tax Court and all evidence received by the Tax Court ... shall be public records open to the inspection of the public" and 26 U.S.C. § 7459(b), which requires the Tax Court to "report in writing all its findings of fact, opinions, and memorandum opinions," mandate disclosure of STJ reports. The taxpayers contend that § 7461 does not limit the type of report subject to its disclosure requirement. They further argue that if STJ reports are not "reports" within the meaning of the statute, the reports are "evidence" within the meaning of § 7461(a) because the reports are

considered by the Tax Court in making its decisions. The taxpayers contend that the disclosure statutes should be construed against the background of the common-law right of access to judicial documents and the concern about secrecy in tax proceedings that Congress manifested when it enacted these disclosure provisions.

The government counters that these statutes apply only to "reports adopted by the Tax Court" and that reading the statutes to cover STJ reports would "lead to absurd results," including requiring official publication of STJ reports "for public information and use" under 26 U.S.C. § 7462. The government further argues that STJ reports do not constitute "evidence" under the disclosure provisions; the STJ is not a party to the proceeding but rather "operates within the adjudicative body itself. ..." The government also contends that no "common-law" right of access extends to STJ reports" and that that question is not properly before the court.

The taxpayers also make an argument that Tax Court Rule 183 itself requires deference to the STJ's report. In *Stone v. Commissioner*, 865 F.2d 342 (D.C. Cir. 1989), an appeal from a 1983 Tax Court decision, the U.S. Court of Appeals for the D.C. Circuit interpreted former Rule 182(d) as imposing a "clearly erroneous" standard of review. Former Tax Court Rule 182(d) provided, in part, that "[d]ue regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." The same language appears in current Tax Court Rule 183(c). Accordingly, the taxpayers argue that the reviewing judge must provide deference to the STJ's



report and, under *Stone*, may reject the STJ's findings of fact only if they are clearly erroneous.

The government responds that because "STJ Couvillion's final report was adopted in full by the Tax Court, disclosed to the parties, and included in the record of this case," the "case does not present any question concerning the proper degree of deference to be given an STJ's recommendations. ..." The government also counters that the Tax Court's elimination of the prior provisions for service of the STJ's report on the parties and the opportunity to file exceptions made clear that the Tax Court "does not contemplate any sort of appellate-style review of STJ reports." Thus, the government argues that the *Stone* decision, which found that a "clearly erroneous" standard applied to the Tax Court's review of the STJ's report, is inapposite.

In *Estate of Kanter*, the taxpayers also argue that the case warrants exercise of the Supreme Court's supervisory power over lower federal courts because the process involved "departed from the accepted and usual course of judicial proceedings" as provided in Supreme Court Rule 10(a). The government responds that the Supreme Court has never used that power to alter the rules of an Article I court that has the power to prescribe its own rules and that it would not be appropriate for the Court to do so here. The government also contends that this issue is not included in the questions before the Court.

SIGNIFICANCE

These cases present important issues about transparency in adjudication, particularly with respect to factfinding by judicial adjuncts. The Supreme Court will have the opportunity to decide to what extent initial findings of fact must be trans-

parent to reviewing courts and litigating parties. If the Court decides the case on constitutional grounds, its reasoning will likely extend beyond the Tax Court to other judicial processes, as well as to quasi-judicial administrative processes.

These cases may also have broad significance for the Tax Court as an institution. The Tax Court is neither an Article III court nor an administrative agency, but rather is a court created by Congress under Article I of the Constitution. The Supreme Court will have the opportunity to decide the extent to which statutes or the Constitution require Tax Court procedures and review of Tax Court decisions to parallel those of Article III courts. The Court's opinion also could address the nature and extent of the Tax Court's rule-making power, as well as the role of the Tax Court in the federal system more generally. Depending on the scope of the Court's rationale for its decision, the decision might impact other Article I courts, as well.

At a more basic level, these cases are significant for the Tax Court and its litigants because of the likely impact of the decision on the Tax Court's use of STJs. The chief judge of the Tax Court has discretion to assign large cases to STJs. In the past, the Tax Court has used STJs in cases governed by Rule 183 with some frequency. For example, in his separate opinion in the Seventh Circuit's decision in *Estate of Kanter*, Judge Cudahy stated that he had found more than 880 opinions in such cases since 1983. A holding for the taxpayers in the current cases would inevitably occasion changes in Tax Court practice in these large cases.

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