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The Tax Court as a Conscientious Objector in *Daubert*'s War Against Bad Science.

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Introduction

Since the Tax Court does not utilize juries, Tax Court judges feel comfortable hearing most evidence, despite being bound by the Federal Rules of Evidence.[2] In general, the trial judge accepts just about all offered evidence, before retiring to chambers to render a decision based on what the judge concludes constitutes admissible evidence.[3]

Specifically, the court announced that:

> The Court has broad discretion to evaluate the cogency of an expert's analysis. Other times, he or she will not. Aided by our common sense, we weigh the helpfulness and persuasiveness of an expert's testimony in light of his or her qualifications and with due regard to all other credible evidence in the record. We may embrace or reject an expert's opinion in toto, or we may pick and choose the portions of the opinion to adopt. We are not bound by an expert's opinion and will reject an expert's opinion to the extent that it is contrary to the judgment we form on the basis of our understanding of the record as a whole.[4]

This "common sense" approach is in direct conflict with the way that the rest of the judiciary analyzes expert testimony, and it substantially reduces a litigant's ability to seek review of a trial court's decision as to what constitutes valid expert testimony. The

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[2] I.R.C. § 7453 (West 2002), Tax Ct. R. 143(a).

[3] Judge Tannenwald took the position that judges, by virtue of their expertise, have the ability to weigh evidence without strictly adhering to the rules of evidence. Specially, he writes:

> … Nor does the absence of a jury excuse sloppiness on the judge's part. It does, however, permit the judge to be knowledgeably flexible, and counsel should keep this in mind in deciding how far he should attempt to insist on full observance of all the technicalities of the rules of evidence.

Theodore Tannenwald, *Tax Court Trials: An Updated View from the Bench*, 47 Tax Law. 587, 597 (1994).

most heinous result occurs when the Tax Court decides to receive otherwise inadmissible evidence (before applying its "common sense" approach) thereby lowering the standard of review a court of appeals will apply to its decision.[5] Specifically, when a matter hinges on an issue of valuation, the decision of the Tax Court may be insulated from appeal when it finds as a matter of fact that expert testimony as to an item's value was not credible instead of finding as a preliminary matter that it was not based on a logical theory, or that the expert did not rigorously apply the underlying theory to the facts he or she analyzed. The Tax Court seems more than willing to conduct a trial when faced with evidence that is inadmissible, even if the party bearing the burden of persuasion has no other evidence to support its position. In other courts this situation would often result in summary judgment.

Despite the Tax Court's reliance on trial proceedings, its rules require that reports of expert witnesses be submitted well ahead of any trial.[6] The submission of these reports often serves as a basis for settlement, or to afford the opposing party the ability to rebut offered evidence.

Most other courts grant summary judgment based on Fed. R. Civ. P. 56 or its state-law counterparts if 1) the party bearing the burden of proof requires expert testimony to prove an element (or elements) of its case; and 2) no admissible expert

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[4] Caracci v. Commissioner, 118 T.C. No. 25, 118 T.C. 379, 383-394 (2002) (citations omitted).
[5] *See infra* p. 19.
[6] Reports are not required where a witness intends to testify about industry practice. Tax Ct. R. 76. Similarly, the court may waive the requirement for good cause. Tax Ct. R. 143(f)(1). *See*, *also*, Thrower v. Commissioner, T.C. Memo. 2003-139, 2003 WL 21107675 (2003) (after petitioner sought expert testimony from IRS witness that was qualified as expert, court noted that it was not properly introduced, and but concluded that it did not comport with Fed. R. Evid. 702 but did not state whether or not, as a threshold matter, it was admissible).

testimony is offered that could, drawing all inferences in favor of the non-moving party, tend to prove such a material fact.[7]

Typically, during pre-trial proceedings, to better position itself for summary judgment, a party might raise a "*Daubert*-type motion" asserting that that offered expert testimony fails the tests for admissibility[8] as articulated by the United States Supreme Court in *Daubert v. Merrell Dow Pharmaceuticals*[9] or the newly revised Fed. R. Evid. 702,[10] and that the proponent of the evidence must prove its admissibility.[11] The most

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[7] Anderson v. Liberty Lobby, 477 U.S. 242, 247-48, 252 (1986) (presence of material fact determined by substantive law); Celotex Corp. v. Catrett, 477 U.S. 317, 324 (1986) (non-moving party must show that there is an issue of material fact using any of the following: depositions, answers to interrogatories, admissions on file, affidavits, or admissible evidence) *cited in* Young v. C.I.R., T.C. Memo.2003-6, 2003 WL 60472 (2003); Sokaogon Chippewa Community v. Exxon, 805 F.Supp. 680, 711 (E.D. Wis. 1992) (speculation about what an expert might say insufficient to defeat motion for summary judgment), *aff'd,* 2 F.3d 219 (7th Cir. 1993) *cert. denied*, 510 U.S. 1196 (1994).

[8] The eleventh circuit required that the party seeking a *Daubert* hearing include, in its motion, some evidence that there is conflicting literature or offered testimony. United States v. Hansen, 262 F.3d 1217, 1232-3 (11th Cir. 2001). But in the Sixth Circuit, a failure to hold a *Daubert* hearing or conduct *Daubert* analysis, in the face of conflicting evidence about scientific validity, will be an abuse of discretion. U.S. v. Smithers, 212 F.3d 306, 314, 315 (6th Cir. 2000) (noting that a trial court judge's interest "to see what a jury will do" was "gamesmanship at its worst and reveals a troubling disregard for this Defendant's rights, relegating those rights to mere abstractions.")

[9] 509 U.S. 579 (1993). Initially, Daubert extended only to scientific testimony. However, in Kumho Tire Co. v. Carmichael, 526 U.S. 137 (1999) the Supreme Court held that non-scientific expert evidence including opinions based on personal experience must be scrutinized under *Daubert*.

[10] Fed. R. Evid. 702 now reads:

> If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of **reliable principles and methods**, and (3) the witness has applied the principles and methods reliably to the facts of the case.

(emphasis added). At the time of Daubert, rule 702 read simply

> If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise

Fed. R. Evid. Rule 702 (modified 2000). Although the new rule appears to encapsulate much of Daubert, and the advisory committee admits that this revision is in response to Daubert, future litigation may draw out any differences. So far, only the Fourth Circuit has explicitly determined that Daubert jurisprudence should be applied to new rule. Cooper v. Smith & Nephew, 259 F.3d 194 n. 1 (4th Cir. 2001). Surprisingly, no other circuit has weighed in on this question.

[11] Bert Black, *Products Liability Expert Evidence In The Wake Of The Daubert-Jones-Kumho Tire Trilogy*, SE01 ALI-ABA 125, 163 (1999) (Texas law). *But cf.* U.S. v. Starzecpyzel, 880 F.Supp. 1027, 1031 (S.D.N.Y. 1995) ("In the spirit of Daubert, this Court concludes that the inquiry conducted pursuant

common grounds for such a motion would be a claim that the offered evidence is not "good science" or that there is no circumstance in which the theory underlying an expert's testimony could be proven false, or that that there is no set of facts that could disprove the theory to which the expert wishes to testify to. In the words of Karl Popper, the theory would not be considered good science if it were "non-falsifiable."[12] Should the court find that an expert's testimony fails this test and that there is no other admissible evidence to support the non-moving party's claim, a motion for summary judgment would be properly granted.[13]

Nowhere in tax jurisprudence is this problem as great as in valuation issues, where a party, usually the Petitioner, must prove how much an item would sell for (otherwise known as its "fair market value") based on observations of the selling prices of similar items.[14]

Although it is quite possible that the Tax Court's *ad hoc* review of all evidence may reach the same result as a court that openly embraces *Daubert* and *Kumho Tire* there is no guarantee that this would actually happen. I argue first that since the Tax Court

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to Fed. R. Evid. 104(a) represents primarily a legal question for the court, rather than a factual one for the parties.") Starzecpyzel, however, may have been overruled by General Elec. Co. v. Joiner, 522 U.S. 136, 143 (1997). *See infra* note 70.

[12] For a more complete description of Daubert's prongs *see infra* p. 16.

[13] The admissibility of expert testimony is governed by the same rules, whether at trial or on summary judgment. First Financial v. U.S.F. & G. Co., 96 F.3d 135, 136 (5th Cir. 1996). *See also* Nadler v. Baybank Merrimack Valley, 733 F.2d 182, 184 (1st Cir. 1984) (affidavit declaring simply that opposing expert in affidavit was "'low priced furniture' man" and that contested issues of valuation should be resolved in affiant's favor was properly disregarded in determining whether question of fact existed); Merit Motors, Inc. v. Chrysler Corp., 417 F.Supp. 263, 272 (D.D.C. 1976) (Failure of expert to provide basis for assumptions and means by which he determined elasticity of demand in markets rendered affidavit inadmissible). Likewise, the "factual predicate" of the expert's report must also be found in the record. Novartis Corp. v. Ben Venue Laboratories, 271 F.3d 1043, 1051 (Fed. Cir. 2001) (undocumented source code of simulation did not provide a factual basis for computer simulation, and therefore the court could not determine whether a simulation was probative).

[14] *See infra* p. 24 for a description of the situations where a taxpayer might not bear the burden of persuasion.

evades summary judgment, it effectively denies both the Service[15] and the taxpayer explicit *Daubert* scrutiny of scientific or non-scientific expert testimony. This dodge results in a lower standard of review and no guidance to future litigants as to which methodologies experts could employ to prove their case. Likewise, despite the Tax Court's love of "gentlemanly" tax trials followed by scathing denunciations of experts it finds incredible, it appears that some trials may be unnecessary. The outcome of some trials may be a forgone conclusion if one party's evidence is based entirely on inadmissible expert testimony. Furthermore, this "wait and see" approach to expert testimony leaves a key philosophical question regarding the burden shifting provisions of § 7491 dangling: must expert testimony pass *Daubert*-style scrutiny to be deemed credible? For purposes of § 7491, is expert evidence judged by another definition of credibility such as the *Frye* standard, or a yet another standard that the court has yet to adopt or articulate?

Power Of The Court To Consider Motions *In Limine*

Though the Tax Court has limited jurisdiction, it is capable of determining which testimony it may hear.[16] Therefore, the Tax Court may not only determine whether offered testimony should be barred because the Federal Rules of Evidence require its suppression, but the court has the power to determine whether offered testimony would

[15] For the purposes of this paper, "Service," "Commissioner," and "IRS" are used interchangeably.
[16] Utilicorp United v. C.I.R., 104 T.C. 670, 675 (1995) (Even though Tax Court could not decide whether report offered by non-licensed testimony would constitute a criminal offense under state law, it has inherent power to determine whether it may receive offered testimony; "[w]e conclude that we have jurisdiction to determine the admissibility of the report and any testimony… that may be offered in support of it.")

result in a violation of the Petitioner's Constitutional rights, as long as the dispute arises from the Petitioner's disputed tax deficiency.[17]

Role of Summary Judgment in the Tax Court

Officially, the Tax Court embraces summary judgment as a means to decide a legal issue "if the pleadings, admissions, and other materials, including affidavits, demonstrate that no genuine issue exists as to any material fact and a decision may be rendered as a matter of law."[18] However, admission of expert testimony is not a question of fact, but a question of law,[19] and this legal question must be determined before tackling the question of whether summary judgment should be granted.[20]

Although most cases docketed by the Tax Court are resolved by stipulation, the vast majority of the cases that go to trial are resolved after a trial in which a judge weighs the credibility of offered evidence and testimony. Even though the Tax Court may decide cases where there is no material issue of fact without a trial,[21] the vast majority of Tax Court decisions are made after a trial. Pleas for summary judgment, in which a party claims that expert testimony that supports the argument of one party is inadmissible, and there remain no issues of material fact, are consistently ignored.

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[17] *See, e.g.,* Garcia v. C.I.R., 1979 WL 3231, 38 T.C.M. (CCH) 666 (1979).
[18] Tax Ct. R. 121(b). Rule 121 is derived from Fed. R. Civ. P. 56.
[19] General Elec. Co. v. Joiner, 522 U.S. 136, 143 (1997).
[20] Viterbo v. Dow Chemical Co., 646 F.Supp. 1420 (E.D. Tex. 1986), *aff'd*, 826 F.2d 420 (5th Cir. 1987); Elliott v. Massachusetts Mut. Life Ins. Co., 388 F.2d 362 (5th Cir. 1968).
[21] In addition to summary judgment, if all facts (or at least the existence of documentary evidence) are stipulated, the parties may submit the case for decision without a trial if there are no matters to be determined that are outside the pleadings. Tax Ct. R. 122(a). If there are matters to be determined that are outside the pleadings, the Court should treat such a request as a motion for summary judgment. Tax Ct. R. 122(b).

The Tax Court's approach is, at best, inconsistent. The trial judge determines whether the expert is credible and then assesses the methodology that the expert employed, provided that the judge actually believes what the expert testifies to. However, most of the time it is unclear from the written opinion which part of the analysis the judge undertook first. This procedure stands in stark contrast to the pattern that trial court judges elsewhere in the country follow under *Daubert*, or its state-law counterparts. In these courts, expert testimony based on methodology that fails *Daubert* scrutiny will never be heard during a trial and will be disregarded for summary judgment purposes. In exercising the trial court judge's job as "gatekeeper" (as directed in *Daubert*), the judge analyzes the methodology that the expert employed in reaching the result, and evidence is excluded based on either unscientific methodology or improper application of a sound methodology.[22]

In the summary judgment context, the Tax Court has shown reluctance to closely scrutinize an expert's affidavits or report. Most notably, in *Seagate Technology, Inc. v. C.I.R.*[23] Judge Gerber stated, "Even though an expert's opinion may be hearsay (i.e., not based on the expert's personal knowledge but on his perception of the operative facts of a case), courts may rely on the expert's affidavits in denying motions for summary judgment."

In *Seagate*, a dispute arose as to whether the cost of stock options granted to employees that were issued at an exercise price pegged to the market value on the issue date actually were a "cost" – which would have to allocated in a cost-sharing pool

[22] *See infra* note 27.
[23] T.C. Memo. 2000-388; 2000 WL 1899311 (2000).

between Petitioner and its foreign subsidiaries.[24] Seagate argued that the stock options were "costless" and that their cost need not be allocated. Seagate claimed that the Commissioner's expert was merely expressing a contrary opinion in the affidavits attached to the motion for summary judgment, based on no reasoning, but rather his "subjective" belief that the options were valuable.

While the parties may have inadequately briefed the issue and the Tax Court may have been correct in claiming that it was premature to decide the issue even though the experts had submitted their reports, the Tax Court appears to have sidestepped the key question in *Daubert*: is the offered testimony "good science?"[25] Or, as the Ninth Circuit, stated, on remand:

> This means that the expert's bald assurance of validity is not enough. Rather, the party presenting the expert must show that the expert's findings are based on sound science, and this will require some objective, independent validation of the expert's methodology.[26]

Fed. R. Evid. 702, and *Daubert* require that a trial court analyze the offered testimony to determine its underlying methodology, its application,[27] and whether it is actually good science.[28]

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[24] Treas. Reg. 1.482-2(b)(5)(ii) (1992).
[25] Daubert, 43. F.3d 1311, 1315 (9th Cir. 1995).
[26] *Id.*; The Supreme Court was somewhat more terse, saying "the trial judge must determine … whether the expert is proposing to testify to (1) scientific knowledge that (2) will assist the trier of fact to understand or determine a fact in issue." Daubert, 509 U.S. at 592.
[27] The Court "must scrutinize not only the principles ... used by the expert, but also whether those principles ... have been properly applied to the facts of the case". Fed. R. Evid. 702 advisory Committee's note to 2000 amendments. *See also* Cummins v. Lyle Indus., 93 F.3d 362, 367 & n. 2 (7th Cir. 1996) (applying Daubert's general reliability requirement in the context of "as applied" scientific problems).
[28] There is a subtle split of authority at the moment, as to whether or not Daubert principles apply only to "case-specific" information. The majority view holds that not only must the conclusions of the expert as they relate to the matter before the court be falsifiable, but so must the data that the expert relied on in drawing his conclusion. The minority holds that only the "case-specific" data, or whatever is before the court, and not the data that underlies the expert's assumptions be falsifiable. See Edward J. Imwinkelried, *Developing a Coherent Theory of the Structure of Federal Rules of Evidence 703*, 47 Mercer L. Rev. 447,

However, *Daubert*, when correctly applied, requires that a court disregard any evidence that does not meet the *Daubert* threshold for reliability before it may even begin to consider which party's evidence is more worthy of belief.[29] If the testimony offered in a report submitted under Tax Ct. R. 76 does not meet this test, then there is no real issue of fact and the party opposing the admission of the report and testimony by the expert may be entitled to summary judgment. In fact, even absent *Daubert*'s guidance, the First Circuit held that in order to defeat a motion for summary judgment, expert testimony must be more than conclusory assertions about ultimate legal issues.[30]

The Petitioners in *Seagate* asked the court to conduct such an analysis. The court refused.[31] Instead, the Court took the Service's expert's word that his conclusions conflicted with the petitioner's expert, thereby implying that his methodology was sound. In failing to scrutinize this claim, the Tax Court placed itself in conflict with the rest of the country's understanding of the role of expert testimony in the summary judgment context.[32]

Meanwhile, in refund suits in United States District Courts, it is acknowledged at summary judgment that: 1) the factual and theoretical basis for the conclusion for an expert must be disclosed; and 2) the court must determine that the expert's proposed

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454 (1996). Tax Court and the United States District Court for the District of Columbia appear not to have taken sides on this issue.

[29] *See infra* p. 24 for a description of how "believeability" relates to Daubert.

[30] Haynes v. Douglas Dynamics, 8 F. 3d 88, 92 (1st Cir. 1993) *cert. denied* 511 U.S. 1126 (1994). *See also* cases cited *supra* n. 13.

[31] The Seagate court sidestepped the issue by saying:

> We do not conclude that respondent's determination is or is not well founded. Likewise, we do not, in the context of this opinion, accept, agree with, or disagree with respondent's expert's opinion. We must however, observe that for better or for worse, expert witnesses have become the prognosticators and the bane of transfer pricing cases. Both parties may rely on expert advice/opinions in reaching their conclusions and/or defending their positions.

testimony must satisfies *Daubert*, if the party seeking summary judgment claims that absent the expert testimony, no other evidence would tend to prove the non-moving party's claim.[33]

The Tax Court's Handling of Expert Testimony

Tax Court judges give various reasons for finding that evidence was incredible. Roughly they can be grouped into two types of rationalizations: 1) a *Frye*-like analysis employed before *Daubert*, in which the Tax Court found that the expert's findings were not generally accepted;[34] and 2) a *Daubert*-like analysis where the Court attacked the scientific method of the expert.[35] No matter which methodology the Court uses, it seems to relish the idea of not admitting that it is doing so.[36]

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[32] *See* cases cited *supra* n. 13.

[33] *See, e.g*., Van Camp & Bennion, P.S. v. U.S., 2002 WL 373358 (E. D. Wash. 2002) *citing* Rebel Oil Co. v. Atlantic Richfield Co., 51 F.3d 1421, 1435 (9th Cir. 1995). As well, outside the world of tax law, in determining "lost profits" damages in breach of contract cases, District Courts question whether or not an expert's determination of just how much money the Plaintiff lost can be falsified or whether it has survived rigorous attempts at falsification. *See, e.g*., Otis v. Doctor's Associates, 1998 WL 673595, *4 (N.D.Ill. 1998).

[34] Jacobson v. Commissioner, 58 TCM (CCH) 645, 650 (1989); Mathis v. Commissioner, 57 TCM (CCH) 519, 524-26 (1989). *See* Frazee v. Commissioner, 98 TC 554, 577-78 (1992) (expert's inability to explain wide disparity gave appearance that expert was "merely acting as an advocate"); Sundstrand Corp. v. Commissioner, 96 TC 226, 370 (1991) (same); Estate of Newhouse v. Commissioner, 94 TC 193, 244 (1990). *See also* Neeley v. Commissioner, 85 TC 934, 945 (1985) (evidence that taxpayer had "shopped" for an appraiser who could provide the desired price range); Coleman v. C.I.R., 87 T.C. 178 n. 2. (1986) ("This figure inexplicably differs from Petitioners' expert's figure").

[35] In other cases, the Court found fault with an expert who refused to reveal the sources of his underlying data. Seagate Tech. v. Commissioner, 102 TC 149, 265, 271 (1994). However, this reluctance may justly be termed an attack on the credibility of a witness – and not on the credibility of his employed method. This case involved a different issue than was discussed in Seagate's later trip to the Tax Court discussed elsewhere in this work.

[36] The Tax Court does, however, take judicial notice of distance calculations, which on some level could be viewed as an acceptance of whatever methodology revealed that cities were a certain distance apart. *See, e.g.,* Armstrong v. C.I.R., T.C. Memo.2002-224 n. 12, (2002) (distance between Denver and Orem, Utah); Johnson v. C.I.R., 115 T.C. No. 16, 115 T.C. 210 (2000) (distance between Whidebey Island and Tacoma, Washington). Nevertheless, the court does not hesitate to take judicial notice of other things facts that it might find in an encyclopedia. Coward v. C. I. R., T.C. Memo. 1997-198, 1997 WL 211299 (1997) ("average gestation period for cattle is 284 days, with a variation range of 260-300").

Into the *Frye*-ing Pan

It is commonly required that "*Frye* courts" decide whether to admit expert testimony[37] based on whether the methodology that produced it had obtained "general acceptance" in the "relevant scientific community." Technically speaking, in order to evaluate the credibility of testimony offered in a *Frye* court, a trial judge would have to determine the general acceptance of the methodology.[38] To its credit, the pre-*Daubert* Tax Court meticulously followed this dictate. In cases like *Conti*[39] the Tax Court inquired first which scientific field would be competent to determine the validity of the scientific methodology, and second whether the methodology was "generally accepted."

Nevertheless, in some instances, the Court opted to mechanically apply a prior decision of the circuit regarding admission of scientifically questionable evidence.[40] Even under the *Frye* standard, the Court did not grant summary judgment to the moving party, even if the party that bore the burden of production was unable to produce

[37] All scientific evidence is, at its heart "testimony." Although an expert may produce a report, diagram, model or model, its admission hinges on the sworn statement of the expert, and the availability of the expert to be cross-examined.

[38] United States v. Yee, 134 F.R.D. 161, 197 (N.D. Ohio 1991), *aff'd sub nom.* United States v. Bonds, 12 F.3d 540 (6th Cir. 1993) (trial court must not confuse scientific reliability with extent of acceptance); Barry C. Scheck, *Scientific Evidence After the Death of Frye DNA and Daubert*, 15 Cardozo L. Rev. 1959 n. 3 (April 1994) (In counting the 'noses' of the scientists who generally accept a scientific methodology, a court *must* admit scientific literature or testimony as not as to the reliability of the scientific technique, but as to the "*acceptance vel non* in the scientific community.") *See, e.g.* Conti v. C. I. R., 99 T.C. 370 & n. 1 (1992) (listing courts experience with *Frye*-type valuation of polygraph evidence).

[39] Conti, 99 T.C. at 373-375.

[40] For years, polygraph evidence seems to have fit into this category. *See, e.g.,* Barnier v. Szentmiklosi, 810 F.2d 594 (6th Cir. 1987). *See also* Wolfel v. Holbrook, 823 F.2d 970 (6th Cir. 1987), *cert. denied,* 484 U.S. 1069 (1988). It should be noted that even after Daubert, the fourth circuit rejected polygraph evidence outright, without leaving it to the discretion of the trial court judge. United States v. Sanchez, 118 F.3d 192, 197 (4th Cir. 1997). This has not been retested after United States v. Scheffer, 523 U.S. 303 (1998) in which the Supreme Court found that a court's *per se* rule of excluding polygraph evidence, even if offered by a criminal defendant, did not offend the defendant's fifth or sixth amendment rights.

evidence that satisfied the *Frye* test.[41] In these cases, however, the moving party may have been able to produce additional non-expert testimony that tended to support what the expert would testify to.[42]

***Daubert*-Style Analysis Termed Credibility Judgment**

At trial, the Court determines whether or not to believe an expert witness, and usually gives a reason. A common excuse for discrediting an expert witness is to declare that his or her testimony did not exhibit "detached neutrality" but is really "advocacy."[43] At first, one is left to wonder which expert witnesses before the Tax Court are not "advocates" for particular points of view.[44] From a common philosophical perspective, it is not a foregone conclusion that "advocacy" for a particular viewpoint constitutes "bad science." On the contrary, many philosophers of science point out that in formulating theories, scientists will draw upon such sources of inspiration as dreams and religious teachings in a "context of discovery" separate from the "context of justification" that determines good science.[45] What difference does it make if the impetus behind some

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[41] For years, polygraph evidence has been the most controversial form of scientific evidence. The Tax Court, like most courts, has determined it to be unreliable – usually when asked to determine whether expert testimony based on the results of a polygraph test was offered to show that a taxpayer was telling the truth was admissible. *See, e.g.* Conti, 99 T.C. at 371. Whatever the case, in most cases, just because a taxpayer thinks they are truthful does is not dispositive of the overall issue.

[42] For example, in Conti, and probably all polygraph cases, the petitioner was willing to testify under oath to the things that he stated when he was hooked up to a polygraph machine.

[43] Physicians Ins. Co. of Wisconsin, Inc. v. C.I.R., T.C. Memo. 2001-304 (2001). For a pre-Daubert example, *see* Estate of Halas v. Commissioner, 94 T.C. 570, 577-579 (1990).

[44] See, e.g., David S. Caudill, *Ethnography and the Idealized Accounts of Science in Law*, 39 San Diego L. Rev. 269, 270 (Spring, 2002) ("rhetoric and persuasion are inevitable features in the production of scientific knowledge"). Professor Caudill also writes, "[g]reed, ambition, persuasion, or economic interests might produce the best science, while institutional gatekeeping, theoretical paradigms, and models may at times lead scientists astray." *Id.* at 277.

[45] James Ladyman, Understanding the Philosophy of Science 75 (2002); Caudill, *supra* n. 44, at 277.

research is an attorney for the service or a petitioner?[46] Philosophers, like most litigators, respond that while conceiving a theory in the "context of discovery," one need not employ <u>any</u> mode of critical analysis.[47] However, in testing and determining if the theory is a good one (the "context of justification); the scientist should make a serious attempt to prove his or her theory incorrect.[48]

During a trial, a party may cross-examine experts, to decide whether their observations were credible, or whether they had rigorously attempted to falsify their conclusions. However, in the Tax Court, where just about every witness is a hired gun, it does little good to ask the witnesses where they got the idea to analyze the data given to them, since the inevitable answer to the critique of their "context of discovery" is that "one of the lawyers paid me to do it."

Specifically, in *Physicians*,[49] a dispute arose as to the size of unpaid losses of an insurance company specializing in medical malpractice policies that could only be resolved by reference to "actuarial science."[50] The Court found that the "general tenor" of one report was "adversarial" toward the other actuary since it accused its rival of "consciously violating various actuarial precepts." The Court goes on to call those accusations "unsupported," and therefore gave "their opinions little weight in this

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[46] Critics of falsification point out, that the ability to test an hypothesis is only as good as the social setting in which the testers sit. *See, e.g.,* Margaret G. Farrell, *Scientific Evidence After the Death of Frye* Daubert v. Merrell Dow Pharmaceuticals, Inc.*: Epistemology and Legal Process*, 15 Cardozo L. Rev. 2183, 2204 (April 1994) (Compliance with the Daubert factors only demonstrates that the methodologies in question conform to the prevailing scientific paradigms, constructed by the conventions of, and for the purposes of, specialized scientific communities.)

[47] Ladyman, *supra* n. 45.

[48] Kola Abimbola, *Abductive Reasoning In Law: Taxonomy And Inference To The Best Explanation*, 22 Cardozo L. Rev. 1683 & n. 1 (2001).

[49] *See supra* n. 43.

[50] For these purposes, the Court assumed that the question of whether actuaries really are scientists is moot, since all parties agreed that the only way to determine what constitutes "appropriate and reasonable" estimates is via actuarial calculations.

regard." While discrediting one actuary may be the correct result in the end, the Court did not actually decide whether or not the "adversarial" report was based on bad science. Although the Court accorded the report absolutely no weight because it thought it was more adversarial than analytical, had it followed *Daubert*, it would have found the expert's report (and therefore his testimony) inadmissible, rather than having less credibility than the "neutral" report. And, if the Court had found the report inadmissible, this actuary would never have entered the courtroom in the first place. Here, it seems, the Court applied *Daubert*, but refused to say so.

The Tax Court applied a similar analysis in *Thrower*.[51] Here, without complying with the rules for offering expert testimony,[52] the respondent sought expert testimony from one of the service's witnesses, a former police officer, as to what would be a reasonable amount of income for a marijuana dealer. The court stated that it was "considering the testimony as expert testimony" that the testimony was not "based upon 'sufficient facts or data' or upon 'reliable principles and methods' applied 'reliably to the facts' of this case, as required by rule 702 of the Federal Rules of Evidence." However, the court appears not to have actually applied *Kumho Tire* or *Daubert*. Instead it discounts the credibility of this expert witness since earlier proceedings failed to authenticate a ledger which most of the IRS's case was based upon. While arguably the court's analysis appears scrutinize the methodology of this witness, the courts conclusion overlooks *Daubert* entirely, and decides that its analysis does not render the former

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[51] *See supra* n. 6.
[52] *See supra* n. 6 and accompanying text.

police officer's testimony inadmissible, but only that it is entitled to "little or no weight."[53]

While such opinions may be easy to read, they do not actually address the underlying questions: were the experts' reports 1) good science; or 2) were their assumptions less credible or relevant than the opposing party's expert's assumptions? Likewise, they do not explain why the actuary's justifications were good enough science to be admissible as expert testimony, but the application was so flawed as to cause it to be accorded absolutely no weight. As well, as we explore later, a mere declaration that an actuary is an "advocate" and not that his methodology was flawed, substantively reduces the scope of review that the Court of Appeals may exercise over the matter.[54]

Daubert At The Tax Court

Karl Popper sought a demarcation between science and pseudo-science,[55] or "to define the concepts of 'empirical science' and 'metaphysics' so that one could tell about a given system of statements whether or not its closer study is the concern of empirical science."[56] To a court that follows Popper, and the adoption of his tenets by *Daubert*, such analysis separates the credibility of an individual scientist from the credibility of a scientific method. Therefore, in most other courts other than the Tax Court, a second level of credibility analysis is undertaken at trial, where a judge or jury evaluates whether an expert witness is telling the truth after determining whether his theories underwent

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[53] The holds in the alternative that even as lay testimony the parties had not established a correct "factual predicate" for the opinion testimony. Thrower at n. 12.
[54] See *infra,* p. 21.
[55] Adina Schwartz, *Dogma Of Empiricism Revisited: Daubert V. Merrell Dow Pharmaceuticals, Inc. And The Need To Resurrect The Philosophical Insight Of Frye v. United States*, 10 Harv. J.L. & Tech. 149, 164 (Winter 1997).
[56] Karl R. Popper, The Logic Of Scientific Discovery 37 (1968).

serious attempts to prove them wrong – otherwise known as "rigorous attempts at falsification."[57] While a fact-finder may determine that the scientific method is not credible (or at least less credible than a competing scientific theory), this second analysis is undertaken separately from basic inquiry into whether or not the offered theory is indeed "good" science.

Unlike with the *Frye*-type analysis, the Tax Court does not seem particularly keen on embarking on a voyage charted by *Daubert*. Instead, the Tax Court views *Daubert* as requiring "minimal logical relevance" to be admissible.[58] At its heart, this is not a completely erroneous view of *Daubert*, since a non-falsifiable statement would not tend to prove or disprove an asserted deficiency.

If the Tax Court were to follow *Daubert*, it would initially determine whether there are any circumstances under which the underlying theory that the appraiser relied on would be untrue or *falsified*. In addition, it would also weigh whether 1) the proffered scientific theory or technique can be (and has been) empirically tested (i.e., whether the scientific method is falsifiable and refutable); 2) whether the theory or technique has been subject to peer review and publication; 3) whether the known or potential error rate of the theory or technique is acceptable, whether there are standards that control the technique's operation, and whether they were maintained; and 4) whether the theory or technique has attained general acceptance. Even if the offered theory is not "science" *per se*, even non-expert testimony must be scrutinized under the same criteria.[59]

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[57] *See* Sean O'Connor, *The Supreme Court's Philosophy Of Science: Will The Real Karl Popper Please Stand Up?*, 35 Jurimetrics J. 263, 271 & n. 25 (1995) (rigorous falsification, in Popper's view, would not necessarily require a lot of tests of a theory, but tests that were aimed at exposing a theory's "weakest spot").
[58] Barrister Equipment Associates Series #115 v. C.I.R., T.C. Memo. 1994-205 (1994).
[59] *See supra* n. 9.

Although the final two prongs of *Daubert* were not derived from Popper's philosophy of science, the Tax Court's "minimal logical relevance" view only partially adopts Popper's teachings. It is true that a non-falsifiable statement is logically irrelevant, since it cannot prove or disprove the validity of the Commissioner's proposed deficiency; it merely restates the Commissioner's position and says that under all circumstances it would be true.[60]

In many cases before the Tax Court, the Commissioner and the Petitioner present experts who make a prediction as to the "fair market value" of a tangible or intangible. In these cases, the dueling experts claim that based on a number of observations, they can predict what the item would sell for, if the Petitioner attempted to sell it,[61] provided that the Court does not think that any of the experts are misrepresenting their observations, in determining which expert to believe. In Popper's terms, the court is really making a judgment as to which rival theory has undergone more rigorous attempts at falsification. Popper saw that more attempts at falsification made a theory better, because each successive observation which did not contradict the theory, *corroborated* the scientist's initial hypothesis. For its part, the Court seems to view a lack of samples that tend to

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[60] To illustrate the testimony of a non-falsifiable expert: One can envision a situation where an expert on the length of time it takes vegetables to decay (thereby losing their salability) testifies that a carrot will rot in two weeks. When asked whether a frozen carrot would behave the same way, the expert would reply in the affirmative. When asked whether, carrots with a different chemical composition (perhaps made entirely of gold) would also rot, he would also reply in the affirmative.

[61] In defining what constitutes fair market value, the definition of fair market value commonly used by the courts is

> … [i]n absence of arm's-length sales… [a] price that hypothetical willing buyer would pay hypothetical willing seller, both persons having reasonable knowledge of all relevant facts and neither person compelled to buy or sell, the views of both hypothetical seller and buyer are considered, due to implicit assumption that both buyer and seller would aim to maximize profit and/or minimize cost in the setting of a hypothetical sale.

Estate of Leichter v. C.I.R., T.C. Memo.2003-66 (2003) (citations omitted). *See, e.g.,* Treas. Reg. 20.2031-1(b).

confirm the expert's theory as tantamount to logical irrelevance.[62] In the face of few attempts as falsification, a trier of fact cannot even guess at how much weight to accord the offered theory.[63]

Finding that a theory is logically irrelevant or "of little use" to the court is probably akin to finding that under *Daubert*, it would not be methodologically sound and/or falsifiable. For example, in *Hudson v. C.I.R.*[64] a dispute arose between two experts as to the proper value of master audiotapes. The Court concluded that the testimony of an expert who normally valued businesses, but did not analyze all of the tapes at issue, was "of little use" and gave it no weight. Again, the Court followed *Daubert*, but called it a credibility judgment. Such a decision would be reviewed under a lower standard of review than would a decision to exclude the expert's testimony.

Courts are required to do more than acknowledge that, on the face of a report, it says "something" – they must inquire as to whether or not there actually was *some* scientific experimentation that would aid them in their determination of a fact, as well as

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[62] *See, e.g.,* Mark F. Grady, A Positive Economic Theory Of The Right Of Publicity, 1 UCLA Ent. L. Rev. 97, 113 & n. 55 (1994) *citing* Stephen W. Hawking, *A Brief History Of Time* 9-10 (Bantam ed. 1988) ("a good theory is characterized by the fact that it makes a number of predictions that could in principle be disproved or falsified by observation").

[63] It should be noted that Popper did not think that a theory should ever be believed. Instead, he thought that rigorous falsification made a theory better. Popper, *supra* n. 56 at 265-269. Unlike scientists, courts do not see this as too much of a problem, since they need only ascertain "truth" to within a probability. So, at the Tax Court need only be confident that whoever is tasked under the substantive law with a burden of persuasion is correct to within a "preponderance of evidence." Interestingly enough, the Court has never addressed the issue of whether or not evidence that is offered for the purpose of showing what an item is likely to sell for "by a preponderance" of the evidence is admissible. Instead it opts to declare that "…valuation necessarily involves an approximation, the figure at which we arrive need not be directly traceable to specific testimony if it is within the range of values that may be properly derived from consideration of all the evidence." McCord v. Commissioner, 120 T.C. 13 (2003) *citing* Silverman v. Commissioner, 538 F.2d 927, 933 (2d Cir.1976) (Tax Court's independent analysis of the record was based on "substantial evidence"). At the moment there is little guidance as to the admissibility of an expert's report that explains how a pricing model reveals a 51% likelihood of an item selling at a given price, and has rigorously attempted to falsify that conclusion, but admits that they have not rigorously attempted to falsify the conclusion that it absolutely would sell at that price.

[64] 103 T.C. 90 (1994).

whether it comports with some articulated standard for scientific methodology.[65] The Court in *Hudson* and *Physicians* did none of this.

Appeals of Tax Court Decisions

Under 28 USC § 1292, a litigant may seek interlocutory review of a grant of partial summary judgment or a motion *in limine*, upon the certification of the judge under Tax Ct. R. 193. Likewise, after a final decision is rendered, a litigant in any matter other than an S-case may appeal to the circuit court of appeals.

In reviewing factual findings, courts of appeal analyze the decisions of the Tax Court under the deferential "clearly erroneous" doctrine.[66] Just like reversals of bench trials, reversals of the Tax Court by a court, referrals on the grounds of "clear error" are rare, but not unheard of.[67]

At the moment, at least two circuits take the view that when there is not an actual trial, a lower degree of deference is shown to the determinations of the Court. The Third and Ninth Circuits hold that where the Tax Court has not actually weighed evidence and observed the demeanor of witnesses, it exercises a higher (yet unnamed) standard of review.[68] On the other hand, the Fifth Circuit takes the opposite view.[69] At least in

[65]Erica Beecher-Monas, *A Ray Of Light For Judges Blinded By Science: Triers Of Science And Intellectual Due Process*, 33 Ga. L. Rev. 1047, 1119 & n. 367 (Summer 1999) (Courts can and do exclude evidence on the basis of a lack of corroboration of a causal relationship).
[66] United States v. United States Gypsum Co., 333 U.S. 364, 395 (1948) ("A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed").
[67] *See, e.g.,* Payne v. C.I.R., T.C. Memo. 1998-227, 1998 WL 341843 (Tax Court 1998) *rev'd* 224 F.3d 415, 423 (5th Cir. 2000) (intent to defraud the IRS cannot be inferred from mere failure to report income where there is some evidence of intent to defraud the IRS and several other parties); Estate of Kaplin v. C.I.R., 815 F.2d 32, 34 (6th Cir. 1987) (in valuation case, holding that fully depreciated property was worthless in face of contrary tax-assessed value was clear error).
[68] Demirjian v. C. I. R., 457 F.2d 1, 4 (3d Cir. 1972) ("However, in cases such as the instant action, where the facts have been fully stipulated and no testimony was taken, the Court of Appeals may, within certain

circuits that choose to follow the Third and the Ninth circuit's view, the Tax Court now has unfettered discretion to change the reviewing court's standard of review, simply by deciding not to grant summary judgment based pre-trial scrutiny of expert evidence, and deciding to term an expert "incredible."

That said, if the court actually holds a trial, review of a decision to admit expert testimony is based on an "abuse of discretion" standard.[70] In *Zervos v. Verizon*,[71] Judge Cabranes explained that this standard encompasses the *de novo* standard of review as to whatever questions of law its ruling hinges on, as well as clearly erroneous review. In other words, the lower court's decision "though not necessarily the product of a legal error or a clearly erroneous factual finding--cannot be located within the range of permissible decisions."[72] The Tenth Circuit, for its part, termed this standard "substantial deference." *Hollander v. Sandoz Pharmaceuticals*.[73]

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limits, substitute its factual conclusions and inferences for those of the Tax Court."); Pacific Vegetable Oil Corp. v. C.I.R., 251 F.2d 682 (9th Cir. 1957) ("The rule that we are bound by a finding of fact if not clearly erroneous does not carry the same impact in the instant case as it ordinarily does because here the evidence consists entirely of stipulated facts and documentary evidence from which we are free to draw our own inferences.").

[69] Kramertown Co., Inc. v. C. I. R. 488 F.2d 728, 729 (5th Cir. 1974) ("Although it is based on facts that were mainly stipulated, this ultimate factual conclusion is binding if it is a permissible inference even though this court might have reached a contrary result had it been the trier of fact").

[70] Joiner, 522 U.S. at 146; Snap-Drape, Inc. v. C.I.R., 98 F.3d 194 (5th Cir. 1996); Hudspeth v. C.I.R., 914 F.2d 1207 (9th Cir. 1990). *Cf.* U.S. v. Hurst, 228 F.3d 751, 756 (6th Cir. 2000) (suppression of evidence based on constitutional grounds reviewed under *de novo* standard of review), and *FDIC v. Providence College*, 115 F.3d 136, 140 (2d Cir. 1997) (applications of facts to draw conclusions of law is reviewed *de novo*).

[71] 252 F.3d 163, 168-169 (2001).

[72] *See, also,* Henry J. Friendly, *Indiscretion About Discretion*, 31 Emory L.J. 747, 745-755 (Fall 1982). In addition to a discussion as to the meaning of "abuse of discretion" Judge Friendly recognized that the phrase may have two meanings. In addition to Judge Cabranes' view, Judge Friendly pointed out that some consider the discussion to center on the question of whether …

> [A]s a normative matter, it is wise for lawmakers to insist on rigid rules in the interest of certainty, no matter how harshly these may operate in some cases, and whether it is not better to prescribe accordion-like standards that afford the courts some dispensing powers to accomplish what they perceive to be justice.

In his article, Judge Friendly cites numerous other definitions of how appellate courts define "abuse of discretion" leading to the conclusion that the standard seems to be somewhat flexible. Although a number

After the Tax Court enters a final decision, the parties may appeal to the relevant courts of appeals "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." I.R.C. § 7482. Naturally, conclusions of law are reviewed *de novo*.[74] In holding that Fed. R. Civ. P. 52(a) limits the review of the Tax Court factual findings, the Supreme Court in *Commissioner v. Duberstein*[75] found that in determining a party's subjective intent, deference should be shown to the Tax Court in determining questions of state of mind.

Courts of appeals are more willing to set aside a decision when the findings are not really findings, but are actually an "extended discussion of factual materials terminating in a conclusion that is based upon a subjective judgment about the weight of the various materials considered often gives the illusion of a process of reasoning."[76] Nevertheless, the Sixth Circuit claims that it takes pains to construe recitations of facts by a lower court as judgments if at all possible.[77]

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of rulings concentrate on the issue of just how "pejorative" the term is, Judge Cabranes' more recent holding appears to be closest to a consensus as to substantively, what the term encompasses.

[73] 289 F.3d 1193, 1204 (2002).

[74] *See also*, Helvering v. National Grocery Co., 304 U.S. 282, 293 (1938) (Court of appeals not authorized to independently review Board of Tax Appeals findings of fact).

[75] 363 U.S. 278, 289 (1960). Specially, the court held:

> Decision of the issue presented in these cases must be based ultimately on the application of the fact-finding tribunal's experience with the mainsprings of human conduct to the totality of the facts of each case. The nontechnical nature of the statutory standard, the close relationship of it to the date of practical human experience, and the multiplicity of relevant factual elements, with their various combinations, creating the necessity of ascribing the proper force to each, confirm us in our conclusion that primary weight in this area must be given to the conclusions of the trier of fact.

See, e.g., Madison Recycling Associates v. C.I.R., 295 F.3d 280, 285 (2d Cir. 2002) ("[W]e owe no deference to the Tax Court's statutory interpretations, its relationship to us being that of a district court to a court of appeals, not that of an administrative agency to a court of appeals").

[76] 14 Mertens, Law of Fed. Income Tax'n § 51:24 (2003). *See, e.g,* Johnson v. U.S., 256 F.2d 849, 850-851 (5th Cir. 1958) (remand to district court in tax refund case where the government proposed several alternative grounds to deny the refund district court did not state the grounds upon which its decision rested).

[77] The Sixth Circuit stated its view as:

This deferential standard only goes as far as the Courts "application" of *Daubert* criteria, and not the interpretation of the Supreme Court and relevant court of appeals' current implementation of *Daubert*. The decision as to whether or not to apply *Daubert*, and the analytical process that the Court engaged in (as set fourth by *Daubert*), in deciding whether evidence is admissible is accorded a lesser degree of deference.[78] Thus, if the Tax Court refuses to explain why challenged evidence that is not falsifiable is still admissible under *Daubert*, it will be held to have abused its discretion.

Effect of Statutory Burden-Shifting

One final question is raised by the Tax Court's *Daubert*-blindness. In general, the burden of persuasion in all civil actions rests with the party that seeks to convince a trier of fact that they acted in conformity with or refrained from acting in conformity with a "predetermined pattern of conduct."[79] The Internal Revenue Code provides a few exceptions. Section 7522 provides that the Commissioner must first satisfy its burden of showing that it has actually determined a deficiency, its amounts, and the basis for its determination. In other words, it bears the initial burden of production. Meeting this

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> We instead adhere to "a liberal standard for reviewing the adequacy of the [trial court's] findings." As a result, "findings are to be liberally construed in support of a judgment, even if the findings are not as explicit or detailed as might be desired.

Zack v. CIR., 291 F.3d 407, 412 (2002) (citations omitted). However, in some in earlier cases, the Second Circuit has held that so long as a trial court does not abuse its discretion, or is in the "if it is within the range of figures that may properly be deduced from the evidence" it will uphold the trial court's determination even if there is some doubt as to the methodology that the trial court applied in reconciling the testimony of dueling experts. Silverman, *supra* n. 63. On the other hand, the Second Circuit has reversed cases where the Tax Court did not state any grounds for coming to its decision, holding that its determination was "clearly erroneous." *See*, *e.g.*, Sullivan v. C.I.R., 985 F.2d 704, 707 (2d. Cir. 1993).

[78] Smithers 216 F.3d at 315.

[79] Leo P. Martinez, *Tax Collection and Populist Rhetoric: Shifting the Burden of Proof in Tax Cases*, 39 Hastings L.J. 239, 244 (1988) *citing* C. Chamberlayne, A Treatise on the Modern Law of Evidence § 931, at 1093 (1911).

burden of producing some "predicate evidence" is rather simple,[80] since the Service need only demonstrate that it actually made a calculation, and validly communicated that calculation to the taxpayer, which is evident on the face of a statutory notice of deficiency. After it has met this burden, the taxpayer shoulders the burden of persuasion, unless some other statutory or rule-based shifting of the burden enters the picture.[81]

It should be noted that in determining whether the Service has met its preliminary burden of showing that the notice of deficiency is valid and that it made a calculation, a court need not abide by the Federal Rules of Evidence, and anything that *Daubert* may have added to them, because such a preliminary determination is specifically outside the scope of the Federal Rules of Evidence.[82] Therefore a court need not inquire into whether or not the service used "bad science" in issuing a notice of deficiency, unless the service made its determination using solely statistical evidence gathered from unrelated taxpayers. In this situation, it would not only bear the burden of persuasion at trial, but the service would have to prove that the analysis and the conclusions drawn from the materials withstood *Daubert* analysis.[83]

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[80] See *Portillo v. Commissioner*, 932 F.2d 1128, 1133 (5th Cir. 1991), *affg. in part, revg. in part and remanding* T.C. Memo. 1990-68.

[81] The only remaining unsettled question in this area involves whether or not the Service is entitled to the burden of proof as to the entire amount of the proposed deficiency. In Estate of Simplot v. C.I.R. 249 F.3d 1191, 1193 (9th Cir. 2001), the court of appeals held that the service was entitled to this assumption only insofar as it could offer evidence since the service's two valuation experts came to widely different conclusions. Other circuits have not directly addressed this question.

[82] Fed. R. Evid. 104, 1101(d)(1).

[83] Technically, the service bears the initial burden of producing evidence that it actually calculated a proposed deficiency. This burden is, in most cases, quite easy to meet, since it need only demonstrate that it made some calculation. *See* Anastasato v. C.I.R., T.C. Memo. 1985-101, 1985 WL 14732 (1985). Section 7491(b) provides that in the case of individuals, where the service's assessment is based on statistical evidence from unrelated taxpayers, the burden of persuasion automatically shifts to the service. § 7491(b). Therefore, this provision essentially vitiates any presumption of correctness if the Service intends to meet its burden solely by introducing statistical evidence.

The § 7491(a) Paradox

Apart from the above caveat, a taxpayer bears the burden of persuasion and production when petitioning for a redetermination. However, Congress carved out some exceptions to this. In general, under § 7491, the service may be shouldered with the burden after the taxpayer[84] demonstrates that they complied with the substantiation requirements of the Internal Revenue Code; properly maintained records; cooperated with requests for documentary evidence and witness testimony; and presented "credible evidence… [that a court] would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted".[85]

In effect, § 7491(a) shifts the burden of persuasion away from a party that has met a burden of production.[86] Even so, some complain that § 7491 is a paradox as it only shifts the burden of proof once it has been met.[87] Some observe that § 7491 has the

[84] Partnerships and corporate taxpayers must not have a net worth exceeding $7,000,000 in that tax year may not avail themselves of this benefit. § 7491(2)(c). Likewise revocable trusts are excluded.
[85] Credible evidence is usually defined as "'the quality of evidence which, after critical analysis, the court would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted." H.R. Rep. No. 105-832, at 5 (1998).
[86] Section 7491 does not specify whether it shifts the burden of persuasion or the burden of production. However, it seems to specify which party must convince a trier of fact that their evidence outweighs their opponent's evidence. *See* Nathan E. Clukey, *Benefits of Shifting the Burden of Proof to the IRS are Limited*, 82 Tax Notes 683, 689-95 (1999) ("The IRS has already taken the position that the statute will shift only the burden of persuasion, and that the statute will have a minor effect on litigation, particularly in light of the legislative history's definition of the credible evidence requirement.") On the other hand, if the statute is read so that it does shift the burden of production, it would mean that once the service is determined to bear the burden of proof, it is required to make a *prima facie* case.
[87] *See, e.g.,* Adriana Wos-Mysliwiec, *The Internal Revenue Restructuring And Reform Act Of 1998: Does It Really Shift The Burden Of Proof To The IRS*, 14 St. John's J. Legal Comment. 301, 314, 321 (Fall 1999) ("Despite the years it took to pass the ideals of taxpayer protection embodied in this bill, the final push though Congress may have damaged a very popular theoretical idea by engrafting requirements eviscerating the effectiveness of the rights granted. This effort seems to have failed entirely… One may even go so far as to say that the language of Section 7491 conceals the continued existence of the presumption of correctness."); Steve R. Johnson, *The Dangers Of Symbolic Legislation: Perceptions And Realities Of The New Burden-Of-Proof Rules*, 84 Iowa L. Rev. 413, 414 (March 1999) ("…even when burden shifting is theoretically available, the limiting conditions imposed render such a shift, as a practical matter, largely worthless to taxpayers. Thus, § 7491 is without substance.")

ultimate effect of forcing the Service to concede cases in which an expert witness's fee would be too high for the Service's budget.

From pre-*Daubert* case law, it appears that § 7491 refers to the weight, and not the credibility of evidence. However, we are still left with an unanswered question: in seeking to shift the burden under § 7491, must the taxpayer introduce evidence that can withstand *Daubert* scrutiny? Although the court will determine whether the burden under § 7491 shifts at a preliminary hearing, it does so by inquiring as to whether or not the evidence is "credible." The Court has taken to defining "credible" by referring to the legislative history that reads

> Credible evidence is the quality of evidence which, *after critical analysis*, the court would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted (without regard to the judicial presumption of IRS correctness)[88]

In the end, if the Tax Court were to determine that the phrase "critical analysis" implies *Daubert*, and any other philosophical baggage that it dragged into the Federal Rules of Evidence, it would appear that the Court must, in evaluating a request under § 7491, make a substantive (not evidentiary) determination of whether or not the evidence is "good science" and whether it is factually "plausible." Then the Court must undertake *Daubert*-style analysis of any evidence offered to shift the burden under § 7491.[89] Interestingly enough, such analysis need not adhere to the Rules of Evidence *per se,* but need only use them as a guide for determining what is credible. Naturally, should the Court decide that "critical analysis" refers not to *Daubert* and Popper, but instead to

[88] Conf. Rept. 105-599, at 240-241 (1998), 1998-3 C.B. 747, 994-995 *quoted in* Lutz v. C.I.R., T.C. Memo. 2002-89, 2002 WL 506881 n. 8 (2002) (emphasis added).
[89] *Id.* (not quoted in Lutz).

some other form of critical analysis (such as a determination of whether any offered scientific testimony is "generally accepted") there would be a different result.

Conclusion

Ten years after *Daubert*, the Tax Court has not explored the evidentiary and substantive effects of the Supreme Court's direction that courts must inquire into the logic employed by proposed expert witnesses. Although this has the practical effect of keeping the Tax Court's decisions relatively well insulated from disturbance on appeal, it does little to develop any judicial scrutiny of scientific methodologies, and may actually allow relatively flawed methodologies to convince the service of the veracity of a its position or of a taxpayer's position.

There may be reasons for shunning *Daubert* analysis and summary judgment at the Tax Court. However, each of these rationales seems to rely on purely ceremonial or symbolic grounds. For example, litigants may feel as if they are denied a day in court and a trial or they may be unable to attend a Tax Court session in a distant city for arguments before trial.

However, a court is not in the business of making the parties feel good, or holding civil trials when there is no possible way that a party can prevail – in fact, that is the reason that summary judgment exists.[90] Likewise, most cases in which summary judgment is requested involve highly sophisticated litigants whose experts may charge even more to be ultimately discredited by the Tax Court – not *pro se* "S-type" cases that do not need to have their egos massaged by being permitted to cross-examine witnesses,

or their legal fees kept to a bare minimum by conserving airfare expenses. In fact, argument on summary judgment need not be oral, and when oral argument is requested, the parties may participate telephonically.[91]

Therefore, to spare both the Service and taxpayer the indignity of a futile trial, and taxpayers as a whole the injustice of taxes calculated by bad science, the Tax Court should pre-screen scientific expert testimony and, if necessary, grant summary judgment if it fails *Daubert*'s standards for admissibility.

[90] *See*, *e.g.*, Curtis v. Campbell-Taggart, 687 F.2d 336, 338 (10th Cir. 1982).
[91] Tax Ct. R. 50(c).