

THE RELATIONSHIP BETWEEN CIVIL AND CRIMINAL TAX FRAUD AND ITS EFFECT ON THE TAXPAYER'S CONSTITUTIONAL RIGHTS

The Internal Revenue Service (IRS) has the statutory authority to assess both civil and criminal fraud penalties against those who attempt to evade or actually do evade any tax due under the Internal Revenue Code. While the civil and criminal fraud sanctions are theoretically different, they have become closely identified in recent cases involving tax evasion. At present, it is conceivable that the IRS can invoke both sanctions in every case of tax evasion. Indeed, the fusion of these two sanctions has been encouraged by substantial judicial approval. However, in the context of a single case of tax evasion, the possibility of the use of both of these sanctions, with their significantly different consequences, has resulted in considerable confusion and uncertainty regarding the extent of the taxpayer's constitutional rights as compared with those afforded defendants in other types of criminal prosecutions.

This comment will examine the relationship between the civil and criminal sanctions and the role which the doctrines of collateral estoppel and res judicata play in those instances in which the IRS decides to invoke both sanctions. Furthermore, the civil-criminal tax fraud investigation will be examined with a view toward determining the impact of *Miranda* upon that process. Finally, the effect of the fusion of the civil and criminal fraud sanctions on the ability of the IRS to obtain discovery of the taxpayer's books and records within the constitutional requirements of the Fourth and Fifth Amendments will be considered.

I. THE RELATIONSHIP BETWEEN CIVIL AND CRIMINAL TAX FRAUD

A. *Characteristics of Civil and Criminal Tax Fraud*

The civil penalty for fraudulent income tax evasion is contained in Section 6653(b) of the Internal Revenue Code. The primary criminal tax fraud penalty appears in section 7201.¹ The courts that have interpreted these sections have held that the elements of fraud requisite

¹ There are other criminal sanctions in the Internal Revenue Code. See Int. Rev. Code of 1954, §§ 7202-215. Of these, the most significant are § 7203 (making it a misdemeanor for willfully failing to file or pay a tax) and § 7206(1) (making it a felony for submitting a return not believed to be true and correct as to every material matter). The government may also prosecute fraudulent taxpayers for offenses proscribed in Title 18, U.S. Code. The following provisions of Title 18 are potential weapons in the arsenal of the IRS: 18 U.S.C. § 371 (1964) conspiracy; 18 U.S.C. § 2 (1964) aider or abettor; 18 U.S.C. § 1001 (1964) false statements; 18 U.S.C. § 287 (1964) false, fictitious or fraudulent claims on the U.S. Government; 18 U.S.C. § 1612 (1964) perjury. For a comprehensive discussion of these sanctions, see Comment, *Fraud Under Federal Tax Law: A Review of Substantive Offenses*, 1968 U. of Ill. L. F. 431 (1968).

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for the use of both of these provisions are identical.² Section 6653(b), the civil fraud penalty, stipulates that "any part of any underpayment . . . shall be added to the tax [in] an amount equal to 50 percent of the underpayment." The section defines "underpayment" as a deficiency and provides that the fifty percent penalty may be imposed on the entire deficiency even though a part of the deficiency was not due to fraud.³ The fraud contemplated by this section does not presume negligence. Rather, it refers to "actual, intentional wrongdoing, and the intent required is the specific purpose to evade a tax believed to be owing."⁴ Section 7201, the criminal fraud section, makes it a felony for any person willfully to attempt in any manner to evade or defeat any tax imposed by the Internal Revenue Code.⁵ Upon conviction, a fine of up to \$10,000 or five years imprisonment, or both, is authorized. The essential elements of this offense are three.⁶ First, an affirmative act constituting an attempt to evade or defeat taxes must be shown.⁷ Secondly, "willfulness" must be proven.⁸ Finally, an additional tax due and owing is a prerequisite to conviction.⁹

² See, e.g., *Tomlinson v. Lefkowitz*, 334 F.2d 262 (5th Cir. 1964), cert. denied, 379 U.S. 962 (1965).

³ Int. Rev. Code of 1954, § 6653(c); see also *Lipton, The Relationship Between the Civil and Criminal Penalties for Tax Frauds*, 1968 U. of Ill. L. F. 527 (1968) [hereinafter cited as *Lipton*].

⁴ *Mitchell v. Commissioner*, 118 F.2d 308, 310 (5th Cir. 1941).

⁵ Int. Rev. Code of 1954, § 7201 provides:

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 five years, or both, together with the costs of prosecution.

⁶ See generally *Schmidt, Corroboration of Admissions in Criminal Income Tax Prosecutions*, 37 U. Det. L.J. 173 (1959) [hereinafter cited as *Schmidt*].

⁷ *Spies v. United States*, 317 U.S. 492, 498-99 (1943). In *Spies*, the Supreme Court made clear that the "affirmative attempt" required was not bound up with the complexities of the common law crime of attempt. *Id.* at 498. The Court stressed that the attempt alone was the consummated, independent crime, regardless of success or failure of the attempt, and that the affirmative act had to include a positive commission rather than a mere omission. To illustrate its position the Court stated:

By way of illustration, and not by way of limitation, we would think affirmative willful attempt may be inferred from conduct such as keeping a double set of books, making false entries or alterations, or false invoices or documents, destruction of books or records, concealment of assets or covering up sources of income, handling of one's affairs to avoid making the records usual in transactions of the kind, and any conduct, the likely effect of which would be to mislead or to conceal.

Id. at 499.

⁸ The element of willfulness requires some degree of "evil motive and want of justification in view of all the financial circumstances of the taxpayer." *Id.* at 498. See also *United States v. Murdock*, 290 U.S. 389, 394-95 (1933). In addition to the specific intent required, willfulness can only be proven by independent evidence. It cannot be inferred solely from an understatement of income. *Holland v. United States*, 348 U.S. 121, 139 (1954).

⁹ See *Schmidt*, *supra* note 6, at 174. See also *Balter, How to Defend a Tax Evasion Case Before Criminal Charges are Brought*, 19 J. Taxation 162 (1963).

The three elements required under section 7201 are the same elements required for an assessment under section 6653(b).¹⁰ Each statute requires a deficiency—the “underpayment” of section 6653(b); the “tax due and owing” of section 7201. Further, the “willfulness” element of section 7201 is equivalent to the “due to fraud” phrase of section 6653(b).¹¹ Finally, the affirmative attempt necessary for conviction under the criminal statute has as its civil counterpart an “actual, intentional, wrongdoing.”¹² The fact that the concept of fraud and the elements required to prove fraud are identical under both the civil and criminal sanctions of the Code cannot be overemphasized because it has crucial significance with respect to the doctrine of collateral estoppel.¹³ The identity between the two sections has further significance because the imposition of one sanction by the government does not bar the imposition of the other.¹⁴ Conceivably, each penalty might be imposed in every case of tax evasion. This latter possibility gives a tax fraud investigation a dual nature and generates issues concerning the point at which the *Miranda* warnings should attach, and whether or not discovery obtained by means of an administration subpoena issued by the IRS may be used in a criminal prosecution.

*Helvering v. Mitchell*¹⁵ illustrates the choice the government has with regard to the fraud sanctions. In *Helvering*, the taxpayer was acquitted of a criminal evasion charge involving an alleged fraudulent deduction for stock loss and a substantial omission of income. Following acquittal, the Commission assessed the deficiency in tax and the fifty percent civil fraud penalty against the taxpayer. The Commissioner's position was affirmed by the Board of Tax Appeals.¹⁶ The Court of Appeals for the Second Circuit, however, reversed the assessment of the civil fraud penalty on the grounds that acquittal of the criminal fraud charge barred imposition of the civil fraud penalty.¹⁷ The Commissioner's successful appeal to the Supreme Court resulted in a holding that the imposition of the civil penalty for tax fraud was not barred by acquittal in the criminal fraud proceedings.¹⁸ The Su-

¹⁰ See Lipton, *supra* note 3, at 528; Balter, Three New Cases Hold Criminal Tax Conviction “Proves” Civil Fraud, 24 J. Taxation 158, 159 (1966) [hereinafter cited as Balter].

¹¹ Lipton, *supra* note 3, at 528.

¹² *Mitchell v. Commissioner*, 118 F.2d 308, 310 (5th Cir. 1941).

¹³ See p. 1181 *infra*.

¹⁴ *Helvering v. Mitchell*, 303 U.S. 391 (1938); *Spies v. United States*, 317 U.S. 492, 495 (1943), where the Court stated:

The penalties imposed by Congress to enforce the tax laws embrace both civil and criminal sanctions. The former consist of additions to the tax upon determinations of fact made by an administrative agency and with no burden on the Government to prove its case beyond a reasonable doubt. The latter consist of penal offenses enforced by the criminal process in the familiar manner. *Invocation of one does not exclude resort to the other.* (Emphasis added.)

¹⁵ 303 U.S. 391 (1938).

¹⁶ 32 B.T.A. 1093.

¹⁷ *Mitchell v. Commissioner*, 89 F.2d 873 (2d Cir. 1937).

¹⁸ 303 U.S. at 398-400.

preme Court in *Helvering* rejected the taxpayer's arguments based upon res judicata and double jeopardy.¹⁹ The Court held that the res judicata doctrine was not applicable because of the differing burdens of proof involved in criminal and civil tax fraud proceedings.²⁰ Further, the Court stated that double jeopardy cannot occur in the enforcement of a civil sanction and pointed out that Congress clearly intended the fifty percent penalty for fraud to be remedial and civil in nature.²¹ Similarly, it has been held that a conviction does not bar imposition of the civil penalty.²²

While the elements of civil and criminal fraud are identical, there are some differences with respect to the two sanctions. The civil penalty, remedial in character, is intended as a safeguard for the protection of revenue. It is intended to defray the expenses incurred by the government in investigating deficiencies stemming from fraud.²³ The criminal sanction, on the other hand, being primarily penal in nature, has deterrence as one of its primary objectives.²⁴ It is designed to insure prompt compliance with the duties imposed by the Internal Revenue Code.²⁵ Additionally, the burdens of proof on the government differ in civil and criminal fraud cases. In the former, the government must establish its case by "clear and convincing evidence." In the criminal context, the "reasonable doubt" standard is applied. Basically, a greater degree of "evil motive" or "bad purpose" is required under section 7201. Some writers have suggested that this difference is largely theoretical.²⁶ A more practical distinction between the civil and criminal fraud sections exists with respect to the applicable statute of limitations. In cases of criminal fraud, the statute of limitations is six years.²⁷ However, there is no limitation period for civil fraud.²⁸ The civil penalty may even be assessed against the estate of a deceased taxpayer.²⁹

¹⁹ *Id.*

²⁰ *Id.* at 403-04.

²¹ *Id.* at 399.

²² See, e.g., *Tomlinson v. Lefkowitz*, 334 F.2d 262 (5th Cir. 1964), cert. denied, 379 U.S. 962 (1965). See also *Lipton*, supra note 3, at 527.

²³ *Helvering v. Mitchell*, 303 U.S. 391, 401 (1938).

²⁴ See *Lipton*, supra note 3, at 532, quoting IRS Audit Division Manual, ch. 4500, P-4560-3 (1960).

²⁵ See *Spies v. United States*, 317 U.S. 492, 495-97 (1943).

²⁶ See *Lipton*, supra note 3, at 529-30; *Balter*, supra note 10, at 158-59.

²⁷ Int. Rev. Code of 1954, § 6531.

²⁸ Int. Rev. Code of 1954, § 6501(c)(1) and *Lipton*, supra note 3, at 528-30. See also Raby and Ireland, *Rights of the Federal Taxpayer*, 46 *Taxes* 200 (1968). This latter article contains a dramatic illustration of the absence of a limitations period with respect to the civil fraud penalty by making reference to *Silliman v. Commissioner*, 220 F.2d 282 (2d Cir.), cert. denied, 350 U.S. 828 (1955). In *Silliman*, deficiencies were asserted against a former judge of a Hawaii court for the taxable years 1924 and 1926. The deficiencies were asserted in 1952 when the judge was 77 years old. The criminal statute had long since run, but under the civil fraud provision the government was still able to collect a deficiency of \$235,000, a civil 50% fraud penalty of \$117,000, plus interest of \$380,000. Cases of this sort, however, are unlikely to arise frequently because the government will

Assuming there are no statute of limitations considerations, the theoretically easier burden of proof under the civil fraud provision does not result in IRS preference of that sanction to the criminal fraud penalties. In fact, it is the avowed policy of the IRS to give overriding importance to the criminal aspects of a tax fraud investigation, and to hold in abeyance the civil aspects.⁸⁰ In any event, the decision to prosecute is within the discretion of the IRS.⁸¹ The policy behind the decision to prosecute for criminal fraud apparently varies from time to time. In prior years, the IRS attempted to enhance the deterrent effect of the criminal fraud provisions by prosecuting cases involving even small deficiencies.⁸² Also, in former years the element of willfulness was deemphasized.⁸³ In more recent years, however, the practice of the IRS has been to give greater consideration to mitigating factors, such as the smallness of the deficiency, while placing greater emphasis upon the factor of willfulness.⁸⁴ Before prosecuting under the criminal fraud sections, however, the IRS requires that there be sufficient evidence to establish the fraud and a reasonable probability of conviction.⁸⁵ Even where the Service is satisfied that these requirements exist, serious illness of the taxpayer and a voluntary disclosure by him are factors which the IRS would consider in determining whether or not to recommend criminal prosecution to the Justice Department, the agency which makes the final decision and which actually handles the prosecution.⁸⁶ Another facet of the criminal and civil fraud relationship is worthy of mention. Imposition of the civil fraud penalty usually follows the prosecution for criminal fraud.⁸⁷ The reverse situation—criminal prosecution following civil assessment—is unlikely under current IRS policy.⁸⁸

generally lose unless it can place into evidence the return for the year in question. Routine destruction of individual returns after 8 years is currently practiced so that cases similar to Judge Silliman's should be rare. See Lipton, *supra* note 3, at 528 n.6.

²⁹ Estate of Louis L. Briden, 11 T.C. 1095 (1948), *aff'd sub nom. Kirk v. Commissioner*, 179 F.2d 619 (1st Cir. 1950).

³⁰ Lipton, *supra* note 3, at 532.

³¹ *Id.* at 530.

³² See Balter, *How to Defend a Tax Evasion Case Before Criminal Charges are Brought*, 19 J. Taxation 162, 166 (1963).

³³ *Id.*

³⁴ See Lipton, *supra* note 3, at 531.

³⁵ See *Id.*, where the author writes:

The Service has a two-fold standard in deciding whether or not to recommend criminal prosecution. There must be sufficient evidence to establish guilt beyond a reasonable doubt, and there must be a reasonable probability of conviction. Due consideration is given to all the facts and circumstances in determining whether a case warrants a recommendation for prosecution or should be disposed of on the basis of the civil liability only.

³⁶ *Id.*

³⁷ *Id.* at 538. See also Balter, *supra* note 10; Tomlinson v. Lefkowitz, 334 F.2d 262 (5th Cir. 1964), cert. denied, 379 U.S. 962 (1965); Armstrong v. United States, 354 F.2d 274 (Ct. Cl. 1965); Amos v. Commissioner, 360 F.2d 358 (4th Cir. 1965).

³⁸ Lipton, *supra* note 3, at 533-34.

The fact that the civil and criminal tax fraud relationship is characterized by identity of legal concept and factual element is unfortunate for the taxpayer subjected to a tax fraud investigation. This is so because of the tremendous aid furnished the IRS by the doctrine of collateral estoppel in pursuing both the criminal and civil aspects of the fraud investigation.

B. The Doctrine of Collateral Estoppel and the Civil-Criminal Tax Fraud Relationship

The doctrine of collateral estoppel is applicable when an attempt is made to litigate a fact previously litigated in an earlier suit involving a different action.³⁹ The doctrine may be invoked to estop a person from relitigating a fact only if the following conditions are met.⁴⁰ First, the fact at issue in the original suit must have been identical to the fact at issue in the second suit. Secondly, the same legal principles must apply in the second suit. Finally, both parties, or persons in privity with them, must have been participants in the earlier suit: The doctrine applies to both criminal and civil cases.⁴¹

The doctrine of collateral estoppel lurks as a menacing foe to the taxpayer under investigation for tax evasion. The fact that the elements of sections 7201 (criminal) and 6653(b) (civil) have been deemed identical gives the doctrine great vitality in tax fraud cases.⁴² For example, a number of cases have held that conviction for criminal fraud establishes the existence of civil fraud under section 6653(b).⁴³ The taxpayers involved were held to be collaterally estopped from introducing any evidence on the question of fraud in the civil proceedings.⁴⁴ The rationale underlying these decisions was the view that the "willful attempt to evade" under section 7201 included all the elements necessary for civil fraud under 6653(b)—the only difference being the greater burden of proof required in the criminal case.⁴⁵ On the other hand, as previously mentioned,⁴⁶ the prior criminal acquittal of a taxpayer does not allow him to invoke the doctrine of collateral estoppel

³⁹ It should be noted that *res judicata* differs from collateral estoppel. The former doctrine bars relitigation of issues involving the same cause of action. It puts an end to that cause of action, thereby preventing its relitigation on any ground except fraud or lack of jurisdiction. See *Commissioner v. Sunnen*, 333 U.S. 591 (1948).

⁴⁰ See *id.* at 598-99.

⁴¹ *Lipton*, *supra* note 3, at 534.

⁴² Since the doctrine requires identity of factual and legal issues in the second suit, the IRS would probably not succeed in attempting to have it applied in civil proceedings following convictions for criminal tax fraud violations not comprising all the elements of § 6653(b). For example, under § 7203 (failure to file), it is not necessary for the prosecution to prove intent to evade or that a tax was due—both elements are prerequisites to assessment of the civil penalty under § 6653(b).

⁴³ *Tomlinson v. Lefkowitz*, 334 F.2d 262 (5th Cir. 1964), cert. denied, 379 U.S. 962 (1965); *Moore v. United States*, 360 F.2d 353 (4th Cir. 1965); *Amos v. Commissioner*, 360 F.2d 358 (4th Cir. 1965); *Armstrong v. United States*, 354 F.2d 274 (Ct. Cl. 1965).

⁴⁴ *Id.*

⁴⁵ *Balter*, *supra* note 10; *Lipton*, *supra* note 3, at 533-35.

⁴⁶ See p. 1178 *supra*.

in a civil fraud proceeding.⁴⁷ Thus, in a sense, the collateral estoppel doctrine is a "one way street"⁴⁸ in that it aids the government in tax fraud cases but is of no assistance whatsoever to the taxpayer. The only instance where it could possibly be of assistance to the taxpayer would be if he prevailed on the issue of fraud in a civil case and then invoked the doctrine in a subsequent criminal proceeding. However, under current IRS policy, a decision to proceed first with the civil fraud sanction will not be followed with a criminal prosecution.⁴⁹ Thus, the doctrine of collateral estoppel affects the relationship of civil and criminal tax fraud in a way totally beneficial to the government and totally detrimental to the taxpayer.⁵⁰ For this reason, the application of the doctrine to the civil and criminal tax fraud cases has often been criticized.⁵¹

The tax fraud investigation routinely begins as an audit to determine civil liability. The taxpayer may surprisingly learn, however, that the possibility for criminal prosecution has arisen. This dual nature of the tax fraud investigation, coupled with the potency of the collateral estoppel doctrine in favor of the government, makes the constitutional rights of the taxpayer in the non-custodial tax fraud investigation a matter of critical importance.

II. THE *Miranda* WARNINGS IN TAX FRAUD INVESTIGATIONS

For the past several years a controversy has existed among judges and legal writers as to whether, or at what stage, *Miranda* warnings⁵² must be given during a non-custodial tax fraud investigation. It is in this area that the civil-criminal fraud dichotomy becomes increasingly important. In determining civil liability no constitutional warnings are required. However, once the decision to pursue the criminal fraud

⁴⁷ The rationale for denying the acquitted taxpayer the use of collateral estoppel is the fact of the higher burden of proof on the government in the criminal proceeding. The government can fail to meet its burden there yet still may meet its lesser burden in the subsequent civil proceeding. See Balter, *supra* note 10, and Lipton, *supra* note 3, at 534.

⁴⁸ See Balter, note 10 *supra*.

⁴⁹ See text at note 38 *supra*.

⁵⁰ It should be noted that a plea of guilty in a criminal proceeding allows invocation of the doctrine by the IRS in a civil proceeding. A plea of *nolo contendere* will not bar litigation of the civil fraud penalty; however, the Justice Department and IRS normally oppose such a plea and some courts, therefore, will not accept it. In attempted settlements of the civil penalty the IRS will also consider a *nolo* plea tantamount to a guilty plea and will likely be inflexible on this point. See Lipton, *supra* note 3, at 536-38.

⁵¹ See Comment, Collateral Estoppel in Civil Tax Fraud Cases Subsequent to Criminal Conviction, 64 Mich. L. Rev. 317 (1965). Other objections to the application of the doctrine to the civil fraud proceeding are that it deprives the taxpayer of his statutory right to have the Tax Court review the Commissioner's determination, or to have a jury determine the issue in a district court, and that the more rigid rules of evidence in a criminal case might exclude evidence favorable to the taxpayer which would have been admissible in the subsequent civil proceeding but for the doctrine. *Id.*

⁵² These warnings are: (1) the right to remain silent; (2) that any statement made may be used against the person undergoing interrogation; (3) the right to consult and have present an attorney; and (4) the right to have an appointed attorney in the event of indigency. *Miranda v. Arizona*, 384 U.S. 436, 444 (1966).

aspect is made, and the assessment for civil fraud becomes secondary, the *Miranda* issue assumes great significance. The substantial disagreement among courts and commentators as to the accrual of a taxpayer's constitutional rights in a tax fraud investigation makes this issue worthy of reexamination.⁵³

In 1964, in *Escobedo v. Illinois*,⁵⁴ the Supreme Court held that when the process of governmental interrogation shifts from *investigatory* to *accusatory*—when the investigation *focuses* on the accused and the purpose becomes to elicit a confession—the adversary system begins to operate and the accused must be permitted to consult with counsel. In *Escobedo*, the defendant was in the physical custody of the police and was questioned in the police station interrogation room.⁵⁵ Any information obtained under these circumstances, the Court held, could not be admitted into evidence.

In 1966, the constitutional rights of the suspect were further clarified by the Supreme Court in *Miranda v. Arizona*.⁵⁶ In the latter decision, the Supreme Court expanded its *Escobedo* decision by holding that evidence obtained from a person subjected to custodial interrogation is inadmissible unless the suspect was warned of his right to counsel, retained or appointed, and of his privilege against self-incrimination.⁵⁷ The Court explained its decision by stating: "By custodial interrogation we mean questioning initiated by law enforcement officers after a person has been taken into custody or *otherwise deprived of his freedom of action in any significant way*."⁵⁸ (Emphasis added.) *Miranda*, like *Escobedo*, was in police custody and questioned in an interrogation room at the police station. This factual situation is important, as is the italicized portion of the above quoted extract from *Miranda*, for both give leverage, respectively, to either a narrow or broad interpretation of the applicability of the *Miranda* warnings.⁵⁹

Shortly after *Escobedo*, the Ninth Circuit applied its constitutional mandates to a criminal tax fraud investigation. In *Kohatsu v. United States*,⁶⁰ the issue concerned whether the accusatory stage had been reached when a routine civil audit shifted to a criminal investigation owing to the appearance in the case of a special agent from the Intelligence Division of the IRS.⁶¹ Periodically, before the appearance of the special agent, the taxpayer and a revenue agent from the Audit

⁵³ Compare *Kohatsu v. United States*, 351 F.2d 898 (9th Cir. 1965), cert. denied, 384 U.S. 1011 (1966), with *United States v. Dickerson*, 413 F.2d 1111 (7th Cir. 1969).

⁵⁴ 378 U.S. 478 (1964).

⁵⁵ Id. at 490-91.

⁵⁶ 384 U.S. 436 (1966).

⁵⁷ See note 52 *supra*.

⁵⁸ 384 U.S. at 444.

⁵⁹ See, e.g., Note, The Shift of Emphasis Theory: Constitutional Rights of Taxpayers in Criminal Fraud Investigations in Light of *Miranda v. Arizona*, 20 *Syr. L. Rev.* 725, 729-730 (1969).

⁶⁰ 351 F.2d 898 (9th Cir. 1965), cert. denied, 384 U.S. 1011 (1966).

⁶¹ The Intelligence Division of IRS has jurisdiction over criminal investigations. Its investigators are known as special agents.

Division of the IRS had held meetings in which books and records of the taxpayer were examined. For nearly two years after the appearance of the special agent in the case, the taxpayer continued to give information, unaware that the investigation had shifted from civil to criminal, and without having been warned of his constitutional rights. These events occurred before the decision in *Escobedo* was rendered. The taxpayer nonetheless contended that under *Escobedo* the evidence obtained after the investigation had shifted from civil to criminal was inadmissible. At this point, he argued, the investigation *focused on* him and the accusatory stage had been reached. The government countered with the argument that since the function of the revenue agent was to ascertain civil liability, and that of the special agent was to investigate any alleged violations and make recommendations, the accusatory stage, within the meaning of *Escobedo*, had not been reached. The court agreed with the government, holding that the accusatory stage had not been reached and that the focus upon a particular suspect referred to in *Escobedo* was not applicable in this situation.⁶² The court distinguished *Escobedo* by stressing the fact that in *Escobedo* an unsolved crime existed for which the accused had been arrested. The tax fraud investigation differed in the opinion of the Ninth Circuit because, in this situation, the function of the agents was to determine whether in fact a crime had been committed.⁶³ Moreover, the court in *Kohatsu* noted that no arrest or indictment characterized the situation.

The *Kohatsu* distinction between an unsolved crime and a criminal tax fraud investigation, the purpose of which is to determine if a crime has been committed, has been strongly criticized by both legal writers⁶⁴ and judges.⁶⁵ Criticism has been directed at the emphasis the *Kohatsu* court placed upon the exploratory nature of the criminal tax fraud investigation without regard to a determination of whether or not the adversary process had begun.

In another decision on the same issue, *United States v. Turzynski*,⁶⁶ the court viewed the law as requiring a suspect to be warned of his constitutional rights as soon as the investigative machinery of government, with the aim of ultimate conviction, became directed at him. The Court in *Turzynski* found the *Kohatsu* distinction irrelevant to the ascertainment of this event: "What matter if the culprit be known before the crime or the crime before the culprit. In either case the investigator is attempting to develop evidence for the purpose of criminal prosecution and conviction."⁶⁷ The *Kohatsu* distinction was further criticized by reason of the fact that a taxpayer subjected to

⁶² 351 F.2d at 902-03.

⁶³ *Id.* at 901.

⁶⁴ See Lay, Right to Counsel in Criminal Tax Fraud Investigations, 43 Ind. L.J. 69, 73 (1968) [hereinafter cited as Lay].

⁶⁵ See *United States v. Turzynski*, 268 F. Supp. 847, 853 (N.D. Ill. 1967); *United States v. Dickerson*, 413 F.2d 1111, 1115 (7th Cir. 1969).

⁶⁶ 268 F. Supp. 847 (N.D. Ill. 1967).

⁶⁷ *Id.* at 852-53.

a criminal tax fraud investigation is suspected of criminal acts prior to the initiation of the criminal investigation.⁶⁸ As the court in *Turzynski* pointed out, at least by the time the case is referred to the Intelligence Division of the IRS, the taxpayer is suspected of fraud and possible prosecution is contemplated.⁶⁹ The fact that the *Kohatsu* rationale could be extended to other areas of white collar crime, where the identity of the suspect is known but the certainty that a crime has been committed is not, forms the basis of additional criticism. During investigations to prove crimes such as the unauthorized practice of law or attempted bribery, for example, it has been held by the Seventh Circuit, in *United States v. Dickerson*,⁷⁰ that *Miranda* would be erroneously limited by application of the *Kohatsu* rationale.

The implication of *Kohatsu* is that the accusatory stage is not reached until arrest or indictment occurs.⁷¹ However, the necessity for arrest or indictment has been considered quite unjustifiable.⁷² After the investigation has been concluded, the warnings may be worthless since by then the taxpayer may have divulged incriminating information.⁷³ Secondly, arrests prior to and after indictment are virtually unknown in tax fraud cases.⁷⁴ Finally, after the investigation has been completed, the case is processed, for purposes of review, through six different levels of the IRS and the Justice Department before an indictment is entered.⁷⁵ Therefore, it has been suggested that all this review obviously indicates that the accusatory stage has been reached prior to indictment.⁷⁶

Writers⁷⁷ and courts⁷⁸ have agreed that the accusatory stage in a non-custodial criminal tax fraud investigation is reached sometime after the special agent enters the case but prior to the formal accusation. Because of the difficulty in pinpointing the exact time at which the special agent subjectively feels prosecution should be recom-

⁶⁸ Id. at 853.

⁶⁹ Id.

⁷⁰ 413 F.2d 1111 (7th Cir. 1969).

⁷¹ See Lay, *supra* note 64, at 73.

⁷² Weiss, Special Agents Need Not Advise a Taxpayer of His Constitutional Rights, 25 J. Taxation 26, 27 (July, 1966) [hereinafter cited as Weiss].

⁷³ Lay, *supra* note 64, at 73.

⁷⁴ Weiss, *supra* note 72, at 27.

⁷⁵ Id.

⁷⁶ Id.

⁷⁷ Weiss, *supra* note 72, at 27; Lay, *supra* note 64, at 89-90; Comment, Constitutional Rights of the Taxpayer in a Tax Fraud Investigation, 42 Tul. L. Rev. 862, 878 (1968). Because of the rigidity of the "first contact with the Intelligence Division" or "entry of the special agent into the case" approach, and because the revenue agent could merely extend the civil phase of the audit in order to obtain incriminating evidence, a shift of emphasis in the nature of the investigation from civil to criminal has been suggested as the best solution to the time of attachment for the *Miranda* warnings. See Note, The Shift of Emphasis Theory: Constitutional Rights of Taxpayers in Criminal Fraud Investigations in Light of *Miranda v. Arizona*, 20 Syr. L. Rev. 725, 736-37 (1969). This also is the test used in *United States v. Turzynski*, 268 F. Supp. 847 (N.D. Ill. 1967).

⁷⁸ See, e.g., *United States v. Dickerson*, 413 F.2d 1111 (7th Cir. 1969).

mended, the consensus among those asserting that *Miranda* is applicable to non-custodial tax fraud investigations seems to be that entry of the special agent into the case, or the first contact the Intelligence Division has with the case is, practically, the best time to mark the advent of the accusatory stage.⁷⁹ Consequently, it is argued that the *Miranda* rights should attach at this time.

Most of the courts that have passed on the issue of the *Miranda* warnings in tax fraud investigations have placed more emphasis on the factor of *custody* rather than on attempts to ascertain the advent of the accusatory stage.⁸⁰ The majority of the courts have taken a narrow view of *Miranda* and *Escobedo*, reasoning that unless the taxpayer is held in custody, the rationale of those decisions—the compulsion on the suspect to speak arising from his custodial surroundings—is inapplicable to the tax fraud investigation. This was the situation, for example, in *United States v. Squeri*,⁸¹ where the Second Circuit declared that the *Miranda* opinion made clear that it was the custodial surroundings in which the questioning took place that created the necessity for the warnings. "This rationale is relevant only where the questioning is conducted in custody or in circumstances similarly inherently compelling; it does not apply to questioning under other circumstances in which there are no inherently compulsive pressures to be overcome."⁸² In reaching its result, the court in *Squeri* relied to some extent on *Mathis v. United States*,⁸³ a more recent decision of the Supreme Court concerning the *Miranda* warnings.

⁷⁹ *Id.*; see also note 77 *supra*.

⁸⁰ Every court of appeals, except the Seventh Circuit, which has considered this issue has found *Miranda* inapplicable when the investigation is non-custodial: *Morgan v. United States*, 377 F.2d 507 (1st Cir. 1967), *Schlinsky v. United States*, 379 F.2d 735 (1st Cir. 1967), cert. denied, 389 U.S. 920 (1967); *Taglianetti v. United States*, 398 F.2d 558 (1st Cir. 1968); *United States v. Squeri*, 398 F.2d 785 (2d Cir. 1968); *United States v. Browne*, 421 F.2d 48 (4th Cir. 1970); *United States v. Maius*, 378 F.2d 716 (6th Cir. 1967); *Kohatsu v. United States*, 351 F.2d 898 (9th Cir. 1965), cert. denied, 384 U.S. 1011 (1966); *Hensley v. United States*, 406 F.2d 481 (10th Cir. 1968); *Cohen v. United States*, 405 F.2d 34 (8th Cir. 1968), cert. denied, 394 U.S. 943 (1969). A majority of the district courts have also held *Miranda* inapplicable to the non-custodial tax fraud investigation. See cases cited in *United States v. Turzynski*, 268 F. Supp. 847, 851 n.2 (N.D. Ill. 1967).

⁸¹ 398 F.2d 785 (2d Cir. 1968).

⁸² *Id.* at 789.

⁸³ 391 U.S. 1 (1968). The court in *Squeri*, stated:

That the determinative factor is whether the interrogation was custodial, rather than the degree of the government's suspicions, is clearly shown by *Mathis v. United States* . . . where the court held that the IRS agents were required to give *Miranda* warnings . . . even though the interview was merely the initial stage of a routine inquiry by civil agents.

398 F.2d at 790 n.1. The court supported this view of *Mathis* by referring to a footnote in the *Miranda* decision, 384 U.S. at 444 n.4, in which the *Miranda* Court explained that when it spoke of an investigation which focused on the accused in *Escobedo* it really meant custodial interrogation. The *Squeri* court thus reasoned that the "compelling atmosphere of the in-custody interrogation" was really the basis of *Miranda* and *Escobedo*. 398 F.2d at 790 n.1.

For a view that vigorously rejects this narrow interpretation of *Miranda*, see the re-

In *Mathis*, the Supreme Court held that the *Miranda* warnings were required when the defendant was questioned by revenue agents of the IRS while he was in state custody on an unrelated charge.⁸⁴ Mathis had been visited in jail by a revenue agent concerning claims for false tax refunds. During the visits he made oral and written statements to the agent which were later used to convict him on the tax charge. The Supreme Court, in reversing the conviction, held that the incriminating evidence was inadmissible, reasoning that Mathis was "in custody" for purposes of *Miranda*. The Court observed that tax investigations frequently lead to criminal prosecutions and, therefore, such investigations are not immune from the *Miranda* warning requirement where the defendant is in custody.⁸⁵ The Court rejected the government's contention that *Miranda* was not applicable because this was a routine tax investigation and custody was due to a separate offense. The Court further stated that it was immaterial whether the custody was in connection with the case under investigation.⁸⁶ Unfortunately, the Court in *Mathis* was not required to decide whether the *Miranda* warnings should be required at some point during a non-custodial tax fraud investigation. The *Squeri* opinion implies that custody was the crucial factor in *Mathis*.

The Seventh Circuit, in *United States v. Dickerson*,⁸⁷ has read *Mathis* more broadly. In holding that *Miranda* is applicable to non-custodial tax investigations after initial contact with the case by the Intelligence Division of the IRS, the court in *Dickerson* relied on the point stressed by the Supreme Court in *Mathis*, that is, that routine tax investigations frequently lead to criminal prosecutions, in rejecting the *Kohatsu* distinction, and in deemphasizing the factor of custody.⁸⁸ Despite the view taken in *Dickerson*, it has been predicted that the *Mathis* decision is likely to have a limited effect in convincing the majority of circuit courts to deemphasize the significance of the custody factor.⁸⁹ Indeed, this was the rationale in *United States v. Browney*,⁹⁰ where the Fourth Circuit held that a taxpayer is not en-

marks of Judge Will in *United States v. Turzynski*, 268 F. Supp. 847 (N.D. Ill. 1967), contending that the Supreme Court "did not intend the custody standard to be raised to constitutional significance," *Id.* at 853. Judge Will favors interpretation of *Miranda* and *Escobedo* to hold that the warnings are required at "the inception of the adversary process," without regard to custody. *Id.* at 853.

⁸⁴ 391 U.S. at 4-5.

⁸⁵ *Id.* at 4.

⁸⁶ *Id.* at 4-5.

⁸⁷ 413 F.2d 1111 (7th Cir. 1969).

⁸⁸ *Id.* at 1115.

⁸⁹ See Lipton, Supreme Court's Decision in *Mathis* Likely to Have Very Limited Effect, 29 J. Taxation 32 (1968). Cf. Ghent, What Constitutes "Custodial Interrogation" Within the Rule of *Miranda v. Arizona* Requiring that Suspect be Informed of his Federal Constitutional Rights before Custodian Interrogation, 31 A.L.R.3d 565, 657 n.6, (1970), wherein it is submitted that cases following the majority rule, although factually distinguishable, have been weakened as authority by the holding in *Mathis* that tax investigations are not immune from the *Miranda* requirements.

⁹⁰ 421 F.2d 48 (4th Cir. 1970).

titled to be notified of the right to counsel prior to interviews by IRS agents in which the taxpayer is not in custody or deprived of his freedom in any significant way, and where there is no evidence of coercion or intimidation. The Fourth Circuit stated that *Mathis* was not applicable since the taxpayer had not been in custody during the interviews. It stated further that "[t]he *Miranda* decision was intended to apply to interrogation of a suspect then in custody and to prevent coercion by interrogators when a suspect is 'otherwise deprived of his freedom of action in any significant way.'"⁹¹ The court in *Browney* noted that the weight of authority has viewed *Miranda* in this light.⁹²

Although the weight of authority stresses actual, formal custody, and the *Mathis* opinion can be read to support such a limitation, the phrase "otherwise deprived of his freedom of action in any significant way," contained in the *Miranda* opinion, lends support to the argument that the *Miranda* warnings could be constitutionally required in situations where formal physical custody is absent. This view is further strengthened by virtue of the Supreme Court's decision in *Orozco v. Texas*.⁹³ There the defendant was involved in a shooting in a Dallas cafe. He returned to his boarding house bedroom. At four o'clock in the morning the police arrived, questioned him without giving him the *Miranda* warnings, and obtained incriminating evidence later used to convict him of murder. The Supreme Court, rejecting the state's argument that the defendant was in familiar surroundings, held that *Miranda* was applicable. The decision apparently did not require a formal arrest for *Miranda* to apply, and there was nothing to indicate whether the defendant in fact knew he was free to leave.⁹⁴ Therefore, the *Orozco* opinion can be read as requiring the *Miranda* warnings even when no formal custody or arrest exists, so long as there is the appearance that the defendant is deprived of his freedom in any significant way. Arguably, the circumstances of an IRS fraud investigation could qualify as such a deprivation.

The Seventh Circuit, the only court requiring *Miranda* warnings in non-custodial tax fraud investigations, has viewed the *Orozco* case in this light.⁹⁵ In *Dickerson*, a special agent interviewed the taxpayer at the latter's place of business without advising the taxpayer of his constitutional rights or of the fact that the investigation had become criminal.⁹⁶ The court considered the basis of the Supreme Court's decision in *Miranda* to be the opportunity to exercise or waive intelligently one's constitutional rights.⁹⁷ Ignorance of one's rights could not be deemed a valid waiver.⁹⁸ With these premises in mind, the

⁹¹ *Id.* at 51.

⁹² *Id.*

⁹³ 394 U.S. 324 (1969).

⁹⁴ See *United States v. Dickerson*, 413 F.2d 1111, 1114, n.4 (7th Cir. 1969).

⁹⁵ *Id.* at 1114.

⁹⁶ See text at note 90 *supra*.

⁹⁷ 413 F.2d at 1113-114.

⁹⁸ *Id.* at 1114.

court noted that the taxpayer could easily be under a misapprehension in a tax fraud investigation.⁹⁹ If he is not informed that there has been a shift from civil to criminal emphasis, he is likely to believe that he is obligated to supply information on account of a possible civil deficiency.¹⁰⁰ Moreover, when questioned by government agents without being warned of his rights, he is likely to feel restrained from walking out on the investigators or from asking them to leave his home or office.¹⁰¹ Lastly, the average citizen would likely think that only the non-cooperative would be prosecuted.¹⁰² Incriminating statements obtained under such circumstances characteristic of a non-custodial tax fraud investigation, the Seventh Circuit reasoned, would be "equally violative of constitutional protections as a custodial confession extracted without proper warning."¹⁰³ The court, therefore, held that the *Miranda* warnings must be given to the taxpayer by the revenue agent or the special agent at the inception of the first contact with the taxpayer after the case has been transferred to the Intelligence Division.¹⁰⁴

One further point made in *Dickerson* is worthy of mention. The court pointed out that in nearly all the other courts of appeals and district court cases that passed on the *Miranda* issue with respect to the criminal tax investigation, either some form or portion of the *Miranda* warnings were given, or an attorney was present, or the court in question arbitrarily chose the strict physical custody view of *Miranda*.¹⁰⁵ Thus, despite the weight of authority to the contrary, factual distinctions in future cases indicate that more litigation over the accrual of *Miranda* rights in tax investigations is likely. By way of illustration, in *Dickerson*, which held *Miranda* applicable to non-custodial tax interrogations, the taxpayer was indicted on the basis of information obtained during five interviews at which he was not once warned of his rights nor accompanied by counsel.¹⁰⁶ In *Turzynski*, which held similarly, no warnings were given nor was the taxpayer informed that the investigation had shifted to a criminal nature. In contradistinction, in *Squeri* and *Browney*, both of which ruled *Miranda* inapplicable in non-custodial tax fraud cases, there was some form of warnings. In *Squeri*, the taxpayer was informed of his right to remain silent and, moreover, he had his accountant present at the inter-

⁹⁹ Id. at 1116.

¹⁰⁰ Id.

¹⁰¹ Id.

¹⁰² Id.

¹⁰³ Id.

¹⁰⁴ Id. at 1116-117.

¹⁰⁵ Id. at 1114-115 nn.7, 8, 9. See also the cases collected in Ghent, What Constitutes "Custodial Interrogation" Within the Rule of *Miranda v. Arizona* Requiring that Suspect be Informed of his Federal Constitutional Rights before Custodial Interrogation, 31 A.L.R. 3d 565, 647-57 (1970). A review of the tax cases cited therein supports the observation of the *Dickerson* court to the effect that most of the cases following the majority rule are either factually distinguishable or turn solely on the factor of formal custody.

¹⁰⁶ 413 F.2d at 1113.

view.¹⁰⁷ In *Browney*, the taxpayer was informed of his right to silence before all interviews.¹⁰⁸ It seems, therefore, that if no warnings whatsoever are given, and the taxpayer is kept in the dark as to the nature of the investigation after it has shifted to criminal, an argument that *Miranda* should apply has strong merit.

The IRS apparently has indicated, either as a precaution against judicial disfavor or because it too recognizes that there might be some merit to the application of *Miranda*, that some warnings should be given to the taxpayer when the special agent enters the case. Since May, 1967, it has required its special agents to give the first three *Miranda* warnings.¹⁰⁹ The fourth—that an indigent accused is entitled to have counsel appointed—is not required.¹¹⁰ Most of the cases that have reached the appellate courts to date concerned interviews that were conducted before *Miranda* was decided.¹¹¹ To some extent, therefore, the weight of authority on the issue may have been influenced by the fact that the agents did what was proper at the time. Consequently, in balancing the administrative interest with that of the taxpayer, this factor may have been significant. In the future, the recent IRS policy requiring special agents to give a modified *Miranda* warning at first contact with the taxpayer should, as cases come up in which it has been given, probably rigidify the position of those courts which feel *Miranda* is not required in non-custodial tax investigations. However, as was pointed out in *Dickerson*, IRS policy does not obviate the responsibility of the court to render judgment in accordance with its understanding of the intent of *Miranda*.¹¹²

It is submitted that a narrow view of "custody" unjustifiably disregards the taxpayer's interest. The possible misapprehension with respect to criminal possibilities, plus the likelihood of subjective compulsion which may face a taxpayer during a tax fraud investigation, militate against adoption of a narrow standard. The rationale of the First Circuit in *Morgan v. United States*¹¹³ to the effect that "to some extent persons must be prepared to look after themselves,"¹¹⁴ is inappropriate where constitutional rights may be waived through ignorance.

A broader view of *Miranda's* "custodial interrogation" rationale, judicially applied on a case-by-case basis, is more appealing. Such a view would be more equitable and more flexible than the strict, formalistic view of "custody" which necessarily and unjustifiably would not

¹⁰⁷ 398 F.2d at 787.

¹⁰⁸ 421 F.2d at 49-50.

¹⁰⁹ See *United States v. Dickerson*, 413 F.2d 1111, 1117 n.13 (7th Cir. 1969).

¹¹⁰ Query whether the fourth requirement is necessary. How many taxpayers suspected of tax evasion are indigent?

¹¹¹ See, e.g., *United States v. Browney*, 421 F.2d 48 (4th Cir. 1970) which, although decided in 1970, dealt with interviews conducted during the 1963-1966 period.

¹¹² 413 F.2d at 1117 n.13.

¹¹³ 377 F.2d 507 (1st Cir. 1967).

¹¹⁴ *Id.* at 508.

require warnings in cases where high degrees of subjective compulsion could arise even though the taxpayer were not in custody. The test enunciated in *Browney* can be read as affording this broader, more flexible test. In *Browney*, the court held that the *Miranda* rights did not accrue if the defendant were neither in custody, nor deprived of his freedom in any significant way, nor subject to coercion or intimidation.¹¹⁵ Judge Sobeloff, concurring in the result reached in *Browney*, understood the test enunciated by the majority to mean that the *Miranda* rights were not to be confined to deprivations of physical freedom, but would arise in "any set of circumstances that robs a person of freedom of will or independence of judgment."¹¹⁶ Judge Sobeloff recognized and pointed out that such an approach would necessitate case-by-case litigation—a situation which, he noted, the *Dickerson* court through its experience had found unsatisfactory. He felt, therefore, that although the majority had reached the correct result on the facts of *Browney* (owing to the fact that some warnings were given), he nevertheless urged that the Fourth Circuit not foreclose adoption of the *Dickerson* approach at least until a fact situation similar to the latter case arose in the circuit. Judge Sobeloff emphasized the sound reasoning and practicality behind the "first contact with the Intelligence Division or special agent" approach in stating his preference for it over the broader view of applying *Miranda* case by case. It is submitted that the broader view of *Miranda* applied to each case is certainly preferable to the strict custody approach. Moreover, the "flood of litigation" specter or the difficulty of case-by-case determination is exaggerated. But the real issue is whether a loose construction of "custody," applied on a case-by-case basis, is better than the "first contact approach," which *arguably* may facilitate evasion by creating a quagmire of constitutionally unwarranted conditions.

The "first contact with the Intelligence Division" rationale does have some disadvantages. It may balance the equities too far in favor of the taxpayer with the possibility that more fraud may be attempted. Taxpayers may find that it is easier to stymie the IRS. In addition, this approach could engender between the IRS and the courts the same type of antagonism created between the police and the courts as a result of the "in custody" warning requirements. Why should seemingly well educated special agents be required to parrot these warnings at the initial stages of an investigation where merely a possibility of criminality exists? Furthermore, this "first contact" approach may be conducive to the administrative structure of the IRS, but presumably the rationale of such a rule could be extended to other government agencies such as the Securities Exchange Commission or the Federal Trade Commission. Would the courts have to tailor an analogous rule for each government agency that conducts non-custodial investigations which could result in either civil or criminal sanctions?

¹¹⁵ 421 F.2d 48 (4th Cir. 1970).

¹¹⁶ *Id.* at 52.

Despite these and other disadvantages, which arguably are exaggerated, it is submitted that the "first contact" approach as adopted in *Dickerson* is the best guarantee of the taxpayer's rights in the non-custodial fraud investigation. It is easy and practical in application. It relieves the IRS of the difficulty of the subjective determination of *Miranda's* accrual. It informs the taxpayer of the sanctions possibly facing him and guards against his misapprehension with respect to the nature of the investigation. It insures against unwitting waivers of constitutional rights. Even if adoption of this approach goes a bit too far in the taxpayer's favor, it is preferable to the adoption of a less practical approach which is rooted in the fear that a taxpayer's knowledge of his rights is a threat to effective law enforcement. After all, the rationale behind the Fifth Amendment privilege against self-incrimination is that no person should aid in his own conviction. Presently, a strong argument can be made that this is exactly what will occur in a non-custodial criminal tax fraud investigation unless the *Miranda* warnings are required to be given when the criminal investigation begins. Hence, it would be beneficial to the public, to the taxpayer being investigated, and to the IRS if the United States Supreme Court resolves this issue the next time it arises before that Court.¹¹⁷

III. THE ABILITY OF THE INTERNAL REVENUE SERVICE TO OBTAIN DISCOVERY OF THE TAXPAYER'S BOOKS AND RECORDS

The fact that a tax fraud investigation has both civil and criminal possibilities raises an important issue pertaining to the authority of the IRS to obtain discovery of the taxpayer's books and records. The issue is whether an administrative subpoena issued by the IRS may be validly used to obtain evidence for use in the criminal aspect of the fraud case. Another problem in the discovery area is the "required records doctrine." This doctrine concerns the taxpayer's Fifth Amendment rights and is, therefore, related constitutionally to the *Miranda* problem previously discussed. It thus bears indirectly upon the civil-criminal tax fraud relationship. The statutory powers of the IRS in the discovery area will be considered. This analysis will be followed by a close scrutiny of the administrative summons and the problems facing the taxpayer because of the "required records doctrine."

Section 6001 of the Internal Revenue Code requires that every person liable for any tax under the Code "keep such records," "render such statements," or "make such returns" as the Secretary of the Treasury or his delegate may prescribe, in order that his tax liability may be ascertained.¹¹⁸ The regulations prescribed by the Secretary

¹¹⁷ In his dissent from denial of certiorari on this issue in *Thomas v. United States*, 386 U.S. 975 (1967), Justice Douglas said: "This is not an in-custody case, but it is a coercive examination of a taxpayer at a critical preliminary hearing, so to speak, and the question presented apparently is a recurring one." Since a more conservative view in the law enforcement area is apparently developing within the Burger Court, a reconsideration of a future grant of certiorari on this issue is unlikely.

¹¹⁸ Int. Rev. Code of 1954, § 6001.

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require that permanent books of account or records as are sufficient to establish the amount of gross income, deductions or credits be kept by any person subject to tax.¹¹⁹ Less formal records are required in the case of farmers and wage earners.¹²⁰ The records required to be kept must be made available at all times for inspection by IRS personnel.¹²¹ Generally, these required records have to be kept for at least four years after the tax to which the records relate is due or paid—whichever is later.¹²² Anyone who willfully fails to keep the required records, or to supply information, is subject to a \$10,000 fine, a year's imprisonment, or both.¹²³

Section 7602 of the Code gives to the IRS administrative subpoena power for the purpose of ascertaining the veracity of any return, making a return where none has been made, or determining the liability of any person with respect to the payment or collection of any tax.¹²⁴ This statute provides the IRS with authority to examine "any books, papers, records, or other data which may be relevant or material. . . ."¹²⁵ It also enables the IRS to summon a person liable for a tax or its collection, or any officer or employee of such a person having possession or custody of his books of account.¹²⁶ Any other person may also be summoned to produce records, papers, books or other data, or to give testimony under oath relevant to the taxpayer's liability. The taxpayer himself may be summoned to appear and give testimony under oath.¹²⁷ The appropriate United States District Court may enforce an IRS administrative summons by appropriate process if it is ignored.¹²⁸

The dual civil and criminal nature of the tax fraud investigation raises some doubt as to the proper use of the IRS administrative summons. As long as the civil liability is also being investigated, the courts have held that a concurrent criminal investigation does not preclude judicial enforcement of the IRS summons.¹²⁹ But section 7602 contains no language to support such a result. It speaks only of the ascertainment and collection of the civil tax liability.¹³⁰ It makes no mention of criminal investigations. Furthermore, the fact that criminal investigation is the province of the special agents, and that their statutory duties do not include the responsibility for issuing a summons, suggests that

¹¹⁹ Int. Rev. Code of 1954, Regs. § 1.6001-1(a).

¹²⁰ Int. Rev. Code of 1954, Regs. § 1.6001-1(b).

¹²¹ Int. Rev. Code of 1954, Regs. § 1.6001-1(d).

¹²² Int. Rev. Code of 1954, Regs. § 1.6001-1(c)(2).

¹²³ Int. Rev. Code of 1954, § 7203.

¹²⁴ Int. Rev. Code of 1954, § 7602.

¹²⁵ Int. Rev. Code of 1954, § 7602(1).

¹²⁶ Int. Rev. Code of 1954, § 7602(2).

¹²⁷ Int. Rev. Code of 1954, § 7602(3).

¹²⁸ See Int. Rev. Code of 1954, §§ 7604, 7402(b).

¹²⁹ See, Lipton, *The Relationship Between the Civil and Criminal Penalties for Tax Frauds*, 1968 U. of Ill. L. F. 527, 533 (1968) [hereinafter cited as Lipton]; *Wild v. United States*, 362 F.2d 206 (9th Cir. 1966); *United States v. Crespo*, 281 F. Supp. 928 (D. Md. 1968).

¹³⁰ Lipton, *supra* note 129, at 533 n.40.

Congress did not intend the IRS administrative subpoena to be used to gather evidence of criminality.¹³¹ It has been suggested, therefore, that since the subpoena power of the government may be used only to the extent and in the manner permitted by statute, the enforcement of the IRS summons resulting in the procurement of evidence for use in the criminal aspect of the case is error and exceeds the statutory authority.¹³²

The use of the IRS administrative summons during a criminal investigation has also been deemed objectionable because it arguably violates the Fourth Amendment.¹³³ The latter requires probable cause alleged under oath or affirmation before a detached magistrate as a prerequisite to issuance of a warrant. An administrative subpoena issued by the IRS bears no such characteristics. Apparently to rebut this constitutional difficulty, IRS special agents have on occasion testified that the tax fraud investigation has as its main purpose the determination of the correct civil tax liability.¹³⁴ But this assertion is questionable because it is inconsistent with the admitted policy of the IRS to place overriding emphasis on the criminal aspects of the fraud investigation while holding the civil aspect in abeyance.¹³⁵

Because the use of the IRS administrative subpoena in conjunction with a criminal tax fraud investigation may be in excess of statutory authority and is constitutionally doubtful, limitations upon its use have been suggested. One commentator has expressed the view that the enforcement of such a summons should be subject to the condition that any evidence elicited thereby be barred from use in a criminal prosecution.¹³⁶ The evidence obtained via the use of the summons would be admissible only for purposes of determining the civil tax liability. Since, as will be discussed below, it is questionable whether even a court may constitutionally authorize discovery of the taxpayer's books and records for purposes of a criminal investigation, and since the statutory construction argument and Fourth Amendment consideration appear logically and persuasively weighted in favor of the taxpayer, it is submitted that the IRS administrative summons should indeed be limited strictly to civil fraud or civil liability purposes, and that any evidence obtained from the taxpayer by its use should be inadmissible in the criminal aspects of the case. Under the statutory construction issue, it could also be maintained that the use of the IRS summons to acquire evidence of criminality from *persons other than the taxpayer* is unauthorized and should also be restricted. However, because the constitutional issue is not so directly involved as to persons

¹³¹ *Id.*

¹³² *Id.*

¹³³ Lipton, *supra* note 129, at 533 nn.40, 41.

¹³⁴ *Id.* at nn.40-43.

¹³⁵ *Id.*

¹³⁶ Lipton, *Constitutional Rights in Criminal Tax Investigation*, 45 F.R.D. 323, 329 (1968). See also, *Hinchcliff v. Clarke*, 371 F.2d 697 (6th Cir. 1967).

other than the taxpayer (since they are not being summoned with a view to being prosecuted), an argument to limit the use of the summons in this context is less persuasive.

No one would argue that the records required to be kept pursuant to section 6001 could not be subpoenaed for purposes of civil liability—either by administrative summons or judicial process. As has been pointed out, the use of the administrative summons to obtain evidence for the criminal case is of doubtful validity. But even under a judicially granted summons meeting the requirement of probable cause pursuant to the Fourth Amendment, it is still not clear whether the section 6001 records may be constitutionally subpoenaed. At issue is the question of whether the Fifth Amendment privilege against self-incrimination protects these required records or whether the “required records doctrine” excepts the section 6001 records from the protection of the Amendment.

The required records doctrine originated in *Shapiro v. United States*.¹⁸⁷ There, the United States Supreme Court held, by a vote of 5 to 4, that books and records required by law to be kept and maintained under the Emergency Price Control Act became “public” records subject to subpoena, and that the immunity section of the Emergency Price Control Act would not protect the defendant against the use of such records as evidence against him in a criminal proceeding. The Court stated its rationale as follows: “[T]he privilege which exists as to private papers cannot be maintained in relation to ‘records required by law to be kept in order that there may be suitable information of transactions which are the appropriate subjects of governmental regulation and the enforcement of restrictions validly established.’”¹⁸⁸ The Supreme Court has never applied the *Shapiro* required records exception to tax records.¹⁸⁹ Moreover, the Court in *Shapiro* mentioned twenty-six other regulatory statutes to which the doctrine might apply, but it did not include the Internal Revenue Code.¹⁴⁰ Nevertheless, a number of courts have extended the doctrine to tax cases.

In *Falsone v. United States*,¹⁴¹ the IRS served an administrative summons on the taxpayer’s accountant. The latter was directed to appear before an agent to give testimony relating to the tax liability of his client and to bring certain books and records pertaining to the taxpayer’s returns. The accountant refused to produce the records and asked the district court to quash the summons. The request was refused. On appeal, the court of appeals affirmed, holding that the records had to be produced even though a Florida statute considered the accountant-client relationship confidential. The court stated that the

¹⁸⁷ 335 U.S. 1 (1948).

¹⁸⁸ *Id.* at 33.

¹⁸⁹ Pemberton, Tax Fraud Investigations and the Required Records Doctrine, 46 *Taxes* 209, 211 (1968).

¹⁴⁰ 335 U.S. at 6 n.4.

¹⁴¹ 205 F.2d 734 (5th Cir. 1953).

power granted to the Commissioner of the IRS by section 6001 was "inquisitorial in character" and comparable to the power vested in federal grand juries.¹⁴² The court even went so far as to say that the records of a taxpayer, even if in the hands of an attorney for purposes of consultation, cannot be regarded as privileged. Otherwise, the court reasoned, interference with the administration of justice would be effected simply by transferring important papers back and forth between attorney and client.¹⁴³

In *Beard v. United States*,¹⁴⁴ the Fourth Circuit ruled by implication that tax records required to be kept by the Internal Revenue Code fell within the rule enunciated in *Shapiro*. *Beard* involved a prosecution for willful filing of a false return. At the trial, the jury was instructed that it could consider the defendant's failure or refusal to produce his books and records for inspection when requested to do so by IRS agents pursuant to the statute. The defendant, a bookmaker, appealed, contending that the instruction was erroneous on the ground that it violated his Fifth Amendment privilege against self-incrimination. The Court rejected this contention.

In *United States v. Clancy*,¹⁴⁵ the Seventh Circuit held that books and records required by law to be kept and maintained are not private papers which are immune from seizure under a valid search warrant. Here the defendants were licensed gamblers who were charged with evasion of wagering excise taxes in connection with a gambling operation they had established at an unlicensed location. IRS agents acting under a valid, authorized search warrant obtained evidence subsequently used to convict the defendants. It consisted of gambling books, records and other paraphernalia. The defendants contended these were private papers within the protection of the Fourth and Fifth Amendments. The Court held they were not, stating "this exception to the privilege against self-incrimination and searches and seizures, has come to be known as the 'required records exception' and has been recognized in numerous cases."¹⁴⁶

In *Stern v. Robinson*,¹⁴⁷ a United States District Court specifically held that the records of a taxpayer required to be kept and produced by the federal income tax laws were not entitled to Fifth Amendment protection. The court discarded the taxpayer's first contention by stating that *Miranda* and *Escobedo* were limited substantially to in-custody interrogation.¹⁴⁸ The court, although citing it for support, expressly noted that *Shapiro* did not involve a prosecution under the tax laws.¹⁴⁹

¹⁴² Id. at 742.

¹⁴³ Id. at 739.

¹⁴⁴ 222 F.2d 84 (4th Cir. 1955).

¹⁴⁵ 276 F.2d 617 (7th Cir. 1960).

¹⁴⁶ Id. at 631.

¹⁴⁷ 262 F. Supp. 13 (W.D. Tenn. 1966).

¹⁴⁸ Id. at 15.

¹⁴⁹ Id. at 16. The defendant appealed but since this was a pretrial motion, no appel-

Notwithstanding the aforementioned decisions, there is some authority for the proposition that the required records doctrine does not overcome the protection of the Fifth Amendment. In *United States v. Remolif*,¹⁵⁰ defendant-wagering operators moved to suppress evidence obtained by IRS through examination of the defendants' books and records. The issue was whether the Fifth Amendment protected the records even though the tax laws required them to be kept. The government contended that the required records exception of *Shapiro* exempted all records required by law to be maintained by all persons subject to the federal excise tax on wagers. The court distinguished *Shapiro* factually and noted that there the defendant did not assert or insist upon his privilege against self-incrimination.¹⁵¹ The court also rejected *Clancy* as controlling. It stated: "We cannot interpret either of such decisions as abolishing the protection of the Fifth Amendment with respect to a person's books and records merely because one or more of innumerable state and federal laws may require records of that type to be kept."¹⁵²

In addition to *Remolif*, several other courts and legal writers have argued that the required records doctrine of *Shapiro* has no place in the tax field.¹⁵³ The most compelling reasons posited in support of this position have been: (1) that *Shapiro* involved an emergency measure and the national interest required strict enforcement; (2) that notwithstanding the emergency conditions, *Shapiro* was decided only by a 5 to 4 vote; (3) that the Supreme Court has never applied the doctrine to tax cases and did not cite the Internal Revenue Code among the statutes it cited as examples to which the required records doctrine might apply; and (4) that the Supreme Court impliedly recognized limitations on the doctrine when it said in *Shapiro* that the government's power to require the maintenance and production of records for inspection by an administrative agency could be exercised constitutionally only when there existed a sufficient relationship between the activity sought to be regulated and the public concern.¹⁵⁴ This sufficient relationship might exist, the Court implied, where the government could forbid or regulate the basis activity concerned. Thus, the required records doctrine arguably has been properly applied in liquor, narcotics and gambling cases.¹⁵⁵ However, since the tax laws are designed for revenue-collecting purposes, it could be contended that application of the required records doctrine to these laws would be an unwarranted

late jurisdiction existed. *Stern v. Robinson*, 391 F.2d 601 (1967), cert. denied, 390 U.S. 1027 (1968).

¹⁵⁰ 227 F. Supp. 420 (D. Nev. 1964).

¹⁵¹ *Id.* at 423.

¹⁵² *Id.*

¹⁵³ See, e.g., *In the Matter of Daniels*, 140 F. Supp. 322 (S.D.N.Y. 1956); *Blumberg v. United States*, 222 F.2d 496 (5th Cir. 1955); *Lipton, Constitutional Rights in Criminal Tax Investigations*, 45 F.R.D. 323 (1968).

¹⁵⁴ See *Pemberton*, *supra* note 139, at 211.

¹⁵⁵ *Id.*

extension of *Shapiro*. One writer has stated that, although many lawyers and some judges are unaware of the taxpayer's right to withhold tax records in fraud investigations, even the IRS has conceded that such records are privileged.¹⁵⁶

Two recent Supreme Court decisions may be read as further supporting the position that the required records doctrine has no place in the tax area. In *Marchetti v. United States*¹⁵⁷ and *Grosso v. United States*,¹⁵⁸ both 1968 cases, the Court further explained the circumstances under which the doctrine could be applied. In *Grosso*, the Court stated that the purpose of the statute involved must be regulatory, that the records must be the type the regulated party customarily keeps, and further, that the records must have "public aspects" which makes them analogous to public documents.¹⁵⁹ In *Marchetti*, the Court implied that a mere record-keeping requirement does not "stamp information with a public character."¹⁶⁰

A strong argument can be made that tax records do not satisfy the conditions recently enunciated by the Supreme Court. The primary purpose of the revenue laws is revenue collection. Not all the records required by the tax laws would necessarily be customarily kept by taxpayers. Finally, even though the Internal Revenue Service represents society as a whole, it is questionable whether the public at large has a right to see one's tax returns or whether the IRS has a right to divulge a taxpayer's records to any citizen who might so request. Therefore, it is submitted that the required records doctrine should be excluded from use in the area of criminal tax fraud litigation.

CONCLUSION

The civil and the primary criminal tax fraud sanctions are related by identity of concept and factual element. These sanctions are further fused by the doctrine of collateral estoppel. The interrelation between civil and criminal tax fraud gives a tax fraud investigation a dual nature. This duality generates a significant legal issue as to the accrual or attachment of the constitutional rights set forth in the *Miranda* decision. Finally, this duality also contributes to the supposed ability of the Internal Revenue Service to obtain discovery of the taxpayer's books and records via the administrative summons and the required records doctrine.

A thorough examination of the civil-criminal fraud relationship and the characteristics of a tax fraud investigation suggests that without a definite standard for application of the *Miranda* warnings, and without a clarification of the administrative subpoena process and

¹⁵⁶ Lipton, *supra* note 153, at 332-33. Here Lipton directed with particularity his disapproval to the decision in *Stern v. Robinson*, note 149 *supra*.

¹⁵⁷ 390 U.S. 39 (1968).

¹⁵⁸ 390 U.S. 62 (1968).

¹⁵⁹ *Id.* at 68.

¹⁶⁰ 390 U.S. at 57.

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the required records doctrine, the constitutional rights of a taxpayer subjected to the non-custodial tax fraud investigation will continue to be in jeopardy. It is hoped that the Supreme Court will soon consider the weighty issues generated by the civil-criminal tax fraud relationship.

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