THE INCONSISTENT POSITION: SECTION 1311(b)(1)

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INTRODUCTION[1]

The intention of Congress in introducing the predecessor[2] of sections 1311 to 1315 into the Internal Revenue Code was to obviate in specified situations[3] the unfair benefit which could be obtained by assuming an inconsistent position and then taking shelter behind the statute of limitations.[4] Judicial doctrines such as estoppel,[5] recoup-

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1. Much has already been written on Sections 1311 to 1315. See Maguire, Surrey and Traynor, *Section 820 of the Revenue Act of 1938*, 48 YALE L.J. 509, 719 (1938), Rothe, *A Comparison of the Basis Provision of the 1939 Code Section 3801 with the 1954 Law*, 35 TAXES 97 (1957); Kent, *Mitigation of the Statute of Limitations in Federal Tax Cases*, 27 CALIF. L. REV. 109 (1939); Landman, *Tax Relief from the Statute of Limitations*, 5 TAX L. REV. 547 (1950); Burford, *Basis of Property after Erroneous Treatment of a Prior Transaction*, 12 TAX L. REV. 365 (1957); Holland, *Tax Consequences of Inconsistent Positions—A Review of Section 3801*, N.Y.U. 10TH INST. ON FED. TAX 807 (1952); Goetten, 3801 *Brought up to Date*, N.Y.U. 13TH INST. ON FED. TAX 1119 (1955); Maguire and Zimet, *Hobson's Choice and Similar Practices in Federal Taxation*, 48 HARV. L. REV. 1281 (1935); Plumb, *The Problem of Related Taxpayers—A Procedural Study*, 66 HARV. L. REV. 225 (1952); Comment, *Mitigation of the Statute of Limitations in Federal Taxation*, 1 U.C.L.A. L. REV. 60 (1953); Note, *Recent Cases*, 70 HARV. L. REV. 1483 (1957); Note, *Section 820: Equity in the Administration of the Revenue Act*, 39 COLUM. L. REV. 460 (1939); Comment, *Mitigation of Effect of Statute of Limitations under the Income Tax Laws*, 27 TEXAS L. REV. 818 (1949); Note, *The Emerging Concept of Tax Estoppel*, 40 VA. L. REV. 313 (1954); Note, *Relief from the Statute of Limitations in Tax Cases under §3801*, 40 VA. L. REV. 773 (1954); Note, *Recoupment in Federal Taxation: When Does It Apply?*, 44 VA. L. REV. 981 (1958); Austin, Surrey, Warren, and Winokur, *The Internal Revenue Code of 1954; Tax Accounting*, 68 HARV. L. REV. 257 (1954); Annotation, 54 A.L.R.2d 538; Note, *Sections 1311-15 of the Internal Revenue Code: Some Problems in Administration*, 72 HARV. L. REV. 1536 (1959); Note, *Problems Arising from Changes in Tax-Accounting Methods*, 73 HARV. L. REV. 1564 (1960); Mullock, *A Change in Accounting Method*, 38 TAXES 607 (1960); Mullock, *The Overlap of Section 481 and Sections 1311 to 1315*, 39 TAXES 207 (1961).
2. INT. REV. CODE OF 1939, §3801.
3. INT. REV. CODE OF 1954, §1312.
4. S. REP. NO. 1567, 75th Cong., 3d Sess. 49 (1938); 1939-1 CUM. BULL. 815. For example, it may be "determined" that an item of expense is properly deductible in, say, the taxable year 1958. If the taxpayer has already claimed the item as a deduction in 1957, which is closed at the time of the determination, he will obviously have obtained an unfair benefit due to the operation of the statute of limitations. Under sections 1311-1315 the bar of the statute of limitations would be lifted to permit assessment of a deficiency for the year 1957 because the determination with respect to the year 1958 would have

ment and set-off[6] had been tried and found wanting.[7] Moreover, they could be asserted only in the District Court or Court of Claims for the Tax Court has no jurisdiction to apply equitable remedies.[8] On the other hand, sections 1311 to 1315 afford relief which can be granted in any federal court including the Tax Court.[9]

In order to bring sections 1311 to 1315 into play there must be (1) a determination as defined in section 1313 (a) which has become final; (2) one of the seven types of error specified in section 1312, in a closed year; and (3) an inconsistent position if the error is described in section 1312 (1), (2), (3) (A), (5), (6), or (7).[10] The purpose of this

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adopted a position maintained by the taxpayer which was inconsistent with the erroneous deduction in 1957.

5. Tax estoppel, for instance, involves a false or malicious concealment of a material fact but not of law by one party and the innocent reliance thereon by another to the latter's detriment. The offending party may thus be barred from changing his position as to a tax item. Since the taxpayer and not the Commissioner is the one usually in possession of the facts, it is only on rare occasions that the taxpayer can avail himself of estoppel. Moreover, it does not open to revision the tax results of inequitous conduct in a prior year; it merely modifies the disposition of the present controversy in which it is successfully invoked. Sections 1311-1315, however, were enacted to lift the bar of the statute of limitations to the extent necessary to correct error in a closed year predicated upon a position inconsistent therewith adopted in a determination.
6. Equitable recoupment has been defined as a rule of law which diminishes the right of a party invoking legal process to recover a debt to the extent that he holds money of his debtor to which he has no moral right. The tax refund suit is regarded by the courts as one of *indebitatus assumpsit* for money had and received and thus opens up all common law defenses. The leading case on the application of recoupment to override a statute of limitations in tax controversies is Bull v. United States, 295 U.S. 247 (1935), which established the "same transaction" test. The tax for the closed year sought to be recouped must have arisen out of some feature of the transaction upon which the main action was grounded. But whether the taxpayer is seeking to recoup an overpayment or the Commissioner wants to recoup from A a deficiency resulting from a refund to B, tax must have been paid. Recoupment would thus offer no solution in such circumstances, set out in section 1312, as the double allowance of a deduction or the double exclusion of income.
7. S. REP. No. 1567, 75th Cong., 3d Sess. 49 (1938); 1939-1 CUM BULL. 815; 48 YALE L. J. 509.
8. Commissioner v. Gooch Milling & Elevator Co., 320 U.S. 418 (1943); Amelia J. Taylor, 258 F.2d 89 (2d Cir. 1958), *affirming* 27 T.C. 361 (1956).
9. It should be remembered, however, that the statute supplements rather than overrides these equitable remedies. (But see Note, 72 HARV. L. REV. 1536, 1537 for a contrary view). If the facts cannot be fitted into sections 1311-1315, tax estoppel and recoupment may still be available. For example, although the statute applies only to the income tax, the *Bull* doctrine will still permit recoupment of a barred overpayment of estate tax against an income tax deficiency assessment; recoupment will also be available if there are two related taxpayers involved who do not fall within the definition given in section 1313 (c).
10. In cases falling under section 1312 (3) (B) and (4) the conditions of sections 1311 (b) (2) (A) and (B) respectively must be met rather than the requirement of an inconsistent position as set out in section 1311 (b) (1).

paper is to determine precisely what the statute means by the notion of an inconsistent position.

Sections 1311 to 1315 cannot come into play until there has been a determination which has become final.[11] The determination must result in a set of facts which fit one of the circumstances of adjustment described in section 1312. This section sets out a number of typical error patterns involving a logical inconsistency. The statute rests on the proposition that the determination when final represents truth. It follows from this that if the respective treatments accorded the same item[12] in the determination and in a closed year cannot both be true together then they are contradictories and hence logically inconsistent. Given this inconsistency, the determination must have adopted a position maintained by the party against whom relief is sought.[13] Hence the notion of an inconsistent position. If the determination adopts a position maintained by the party against whom the statute is invoked and this position is inconsistent with the error in the closed year then the statute will apply. Where the taxpayer is seeking relief the determination must have adopted a position maintained by the Commissioner;[14] if the Commissioner seeks relief, a position maintained by the taxpayer.[15]

THE PROBLEM

Does the concept of an inconsistent position require that the party against whom the statute is invoked have *changed* his position? Conversely, does it matter that the party against whom relief is sought treated the item in question consistently from year to year?

11. INT. REV. CODE OF 1954, §1311 (a); §1313 (a).
12. Under sections 1311 to 1315 each item of income, expense, gain or loss and the contention made with respect to it is considered a separate matter for purposes of the statute. Section 1314 (c) clearly states that the adjustment shall not be affected by any item other than the one which was the subject of the error. The statute does not purport to permit of adjustments in closed years for items that are merely similar to those with respect to which a determination has been made for another year; the items must be the same. D. A. MacDonald, 17 T.C. 934 (1951); Est. of A. W. SoRelle, 31 T.C. 272 (1958). For a criticism of this view based on Gooch Milling & Elevator Co. v. U.S., 78 F. Supp. 94 (Ct. Cl. 1948), see 72 HARV. L. REV. 1543-1550. In Gooch, the Court of Claims did take into account—erroneously, it is submitted—the collateral effect of a similar item. The error involved the shifting of gross income from the closed year 1935 to 1936 as a result of the determination correcting the opening 1936 inventory—which, of course, was the same thing as the 1935 closing inventory. This, however, did not mean that the collateral effect of a similar adjustment to the 1935 opening inventory should also be taken into account. In a situation analogous to *Gooch* involving a shift of gross income from 1945 to 1946, the Tax Court refused to take into account a similar correction of the 1945 opening inventory. Est. of A. W. SoRelle, 31 T.C. 272, 276 (1958).
13. INT. REV. CODE OF 1954, §1311 (b) (1).
14. INT. REV. CODE OF 1954, §1311 (b) (1) (A).
15. INT. REV. CODE OF 1954, §1311 (b) (1) (B).

LEGISLATIVE HISTORY

The House Revenue Bill of 1938 contained no provision for mitigating the effect of the statute of limitations. We must look, therefore, to the Senate and Conference Committee Reports. The Senate Report[16] seems to place its emphasis on change of position. But to a considerable extent this can be put down to the use in the report of examples limited to paradigm situations involving change of position. Nevertheless, despite this emphasis, the report contains language indicating a broader scope. For instance, it notes the need to take the profit out of inconsistency whether fortuitous or the result of design and points out that it was never the intention of Congress to sanction active exploitation of the statute of limitations by the beneficiary of the statutory bar.[17] The reference to the beneficiary of the statutory bar is significant because his *position* with respect to the determination could, conceivably, be neither inconsistent with nor contrary even to that, if any, maintained by him in the year of error. For he could be persisting in his error or "snapping up" an advantage made possible by the opposite party's error.

The Conference Committee Report on the Senate amendment is free of ambivalence and states the problem clearly as follows:

> Under the income tax laws it is possible for a taxpayer or the Commissioner, after operation of the statute of limitations . . . prevents correction of an error, to obtain a double advantage by taking a position contradictory[18] to that which caused the error.[19]

Moreover, in explaining how the statute would work, the report explains that there must be a determination "which gives authoritative sanction to the inconsistent position presently maintained by the taxpayer or the Commissioner and indicates that the previous treatment

16. S. REP. No. 1567, 75th Cong., 3d Sess., 1939-1 CUM. BULL. 814-817.
17. *Id.* at 815.
18. The alternating use of "contradictory" and "inconsistent" raises an interesting point of logic. In the formal or classical Aristotelian logic, two propositions can be contradictories if they are neither true together nor false together; and can be contraries if they cannot be true together though they may be false together. The term "inconsistent" is used in a broad sense to denote two statements which are contradictory or from which a contradiction can be deduced. On the other hand, the modern empiricist (*e.g.*, P. F. STRAWSON, INTRODUCTION TO LOGICAL THEORY) sees "inconsistent" as expressive of contradictory in a narrower sense, viz., that of self-contradiction—the application of incompatible predicates to the same person or thing at the same time. To the formal logician, the term "self-contradictory" cannot apply to a single statement for whereas two statements may contradict one another, they cannot be self-contradictory. Thus, neither school regards "inconsistent" as meaning merely what lawyers understand by change of position.
19. H. REP. No. 2330, 75th Cong. 3d Sess., 1939-1 CUM. BULL. 835.

of the item was erroneous."[20] This hardly suggests any restriction to change of position by one of the parties.

THE UNRELATED CONCEPT OF CONSISTENCY

Before considering how the courts have interpreted "inconsistent position" an excursus is justified at this stage in order to examine another, and it is contended, unrelated concept which seems fated to confuse the issue raised by the statute—viz., the "consistency" required of taxpayers in the year to year accounting for their income.

Section 446 provides that taxable income shall be computed under a method of accounting which clearly reflects income. In order clearly to reflect income, all items of gross income and all deductions must be treated with consistency.[21] As the Tax Court has pointed out: "The consistency required of taxpayers in reporting their income and the uniformity shown by the petitioner results . . . in the long range consequences being no different under one system than under the other."[22] Thus, provided the method of accounting is in accordance with the regulations[23] the Commissioner cannot compel the taxpayer to change to another method if the existing method has been used consistently over a period of years. Similarly, if the taxpayer wishes to change his consistently used method he must first secure the consent of the Commissioner.[24]

It is apparent, then, that "consistency" in accounting as a means towards clear reflection of income is meaningful only in terms of a relatively long period of time. "Inconsistent position", on the other hand, looks only to two points in time[25] (or to the same point in time where two related taxpayers are concerned) and focuses on a particular item of gross income, deduction, gain or loss. It follows that the relationship between "consistency" and "inconsistency" is one of contrariety and not contradiction.[26] That is to say, "no consistency" in the

20. *Ibid.*
21. U. S. Treas. Reg. 1.446-1 (a) (2); 1.446-1 (c) (ii).
22. Geometric Stamping Co., 26 T.C. 301, 305 (1956).
23. U. S. Treas. Reg. 1.446-1 (c).
24. INT. REV. CODE OF 1954, §446 (e).
25. This statement must be modified where the error accumulates over more than one year, as for example in H. T. Hackney, 78 F. Supp. 101 (Ct. Cl. 1948) and M. Fine & Sons Mfg. Co., 59-1 U.S.T.C. No. 9106 (Ct. Cl. 1959), vacating and withdrawing 162 F. Supp. 763 (Ct. Cl. 1958).
26. This may be illustrated as follows:
If A says: X is over 6 feet tall (So); and
If B says: X is under 6 feet tall (Su); and
If C says: X is 6 feet tall (Sj),
Then Su=Snot—o.
However, So/Snot—o is not the same as So/Su because whereas Sj is incon-

accounting treatment of an item over a period of years could be inconsistent with both the consistent and inconsistent treatment of the item with respect to the open and closed years. Hence, it cannot be said that "no consistency" is "inconsistency". Statutory recognition of this is implicit in section 1314 (c) which provides that the adjustment under the statute shall not be affected by any item other than the one which was the subject of the error. Unfortunately this point has not always been appreciated.

JUDICIAL INTERPRETATION

In *Heer-Andres Investment Co.*,[27] the Tax Court was clearly of the opinion that lack of year to year consistency on the part of the Commissioner amounted to the statutory vice of inconsistency; that consistency on the part of the taxpayer precluded his position in the determination from being an inconsistent position. The case undoubtedly called for relief to the Commissioner under section 1312 (3) (A);[28] the court, however, felt otherwise. The determination related to an involuntary change in accounting for rental income for the years 1946 and 1947. The Commissioner had moved the rents reported in 1947 and 1948 back to 1946 and 1947 respectively. In eliminating 1946 rent from 1947, however, he did not similarly eliminate 1945 rent from 1946; as 1945 was closed it would otherwise have escaped taxation entirely. On this issue the determination adopted the taxpayer's contention that the Commissioner could not bunch both 1945 and 1946 rents into 1946 merely because 1945 was closed.[29] From the irrelevant fact that the Commissioner had not consistently adjusted each of the open years 1946 and 1947, the court moved to the fallacious conclusion that the Commissioner and not the taxpayer had taken

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sistent with both So and Su yet Sj cannot be inconsistent with both So and Snot—o.
Thus, So and Su are contraries and
So and Snot—o are contradictories.

27. 22T.C. 385 (1954).
28. The facts may be expressed in terms of section 1311 (b) (1) and section 1312 (3) (A) as follows:
    a) A determination by the Tax Court requiring the exclusion of 1945 rent from gross income of 1946.
    b) An omission of 1945 rent from the gross income of 1945.
    c) In contemplation of the statute, (a) represents truth, therefore (b) is erroneous.
    d) The adjustment would be a deficiency for 1945.
    e) The determination adopted a position maintained by the taxpayer, (a), the party against whom relief was sought, which was inconsistent with the error, (b).
29. 17 T.C. 786 (1951).

"inconsistent positions".[30] The taxpayer, on the other hand, had been entirely consistent in his year to year reporting of rental income. In the face of such consistency and absence of change of position on the taxpayer's part, the court lost sight of the material facts, viz., that the determination, in excluding 1945 rent from 1946, adopted a position maintained by the taxpayer which was inconsistent with the exclusion of 1945 rent from the closed year 1945.

The decision is particularly unfortunate in view of the Tax Court's earlier decisions. For example,[31] in *Albert W. Priest Trust*,[32] involving section 1312(5), the determination, in allowing the exclusion of currently distributable income from the beneficiary's taxable income, adopted his position that the estate was still in the course of administration. This was inconsistent with the deduction allowed to the estate by the Commissioner on the ground that the trust was then in existence. In resisting a deficiency adjustment the estate argued that both it and the beneficiary had been consistent because the original returns of both were filed on the basis that the estate was in the process of administration and therefore any inconsistency must spring from the Commissioner's erroneous theory in the first place. The Tax Court replied as follows:

> We do not think there is any requirement that the position of the taxpayer which is adopted in the determination must be inconsistent with a position theretofore maintained by that of (sic) a related taxpayer. The sole requirement of the statute is that the position so adopted be inconsistent with the prior erroneous allowance of the deduction. It does not seem impor-

30. By his determination (3801 deficiency) as to the fiscal year 1945 which is controverted in the instant proceeding, (Commissioner) has placed himself in the same position he occupied in the (determination) with respect to the fiscal year 1946. His position there was inconsistent with his action as to the fiscal year 1947. Likewise, his position here is inconsistent with his action as to that year. To us it appears that (Commissioner) is persisting in an inconsistency which was pointed out to him (query) in the (determination) and which was there held not to be tenable. (Commissioner), not (taxpayer), has taken inconsistent positions. 22 T.C. 385, 390.

And note also the surprising statement by the Second Circuit in Cory v. Comm., 261 F.2d 702 (2d Cir. 1958) that §1311(b) is satisfied by a change of position by the taxpayer in the year of the determination: It is true that the (taxpayer's) 1944 return (year of determination) disclosed in full all the relevant facts surrounding their receipt of the royalties. But the fact remains that in that return they took the position that the entire sum was received in 1944 whereas in the later claim for refund (for 1944) they urged that they did not obtain $30,257 of these royalties until 1945. This is sufficient to bring 1311-15 into play. 261 F.2d 702, 704.

31. See also The First National Bank of Philadelphia, 205 F.2d 82 (3d Cir. 1953) where the court resisted the taxpayer's attempt to inject the notion of consistency in the hope of somehow hiding the patent contradiction. The court refused to be side-tracked.

32. 6 T.C. 221 (1946).

> tant . . . who proposed the allowance of the deduction or upon what theory.[33]

Inconsistency, then, is ascertained by reference to what was actually done in the earlier year rather than to what the taxpayer or the Commissioner may have urged at the time. Nor is it limited to change of position. An unconscionable advantage and misuse of the statute of limitations may obtain just as readily without change of position where the beneficiary of the statutory bar persists in his error or "snaps up" an error, persistent or otherwise, of the opposite party.

CONCLUSION

The notion of "maintaining an inconsistent position" embodies a simple idea. Postulating the truth of the determination, the inconsistency is between (a) a position which was urged by the party against whom relief is sought and adopted in the determination and (b) an error, which must be error because the determination is deemed to represent truth, in a closed year. The difficulty it presents lies principally, it is submitted, in the form in which it is drafted. Given its two constituent propositions as stated, inconsistency exists. Why then bother to state the obvious? Moreover, the Code being what it is, such ponderous and complicated language as that used in section 1311 (b) makes us look for complexities that do not exist. By way of contrast, consider the A.L.I.'s suggested version of section 1311 (b). After all other prerequisites to relief have been stated, the draft concludes as follows:

> If the adjustment is to be by way of refund or credit, no adjustment shall be made unless the Secretary urged the action required by the determination. If the adjustment is to be by way of a deficiency, no adjustment shall be made unless the taxpayer with respect to whom the determination is made urged the action required by the determination.[34]

This says all that is necessary to limit relief to those situations in which the party in whose favor a statutory bar would otherwise operate justifies the adjustment by his active maintenance of a position in the controversy leading up to the determination at variance with the position which he desires to perpetuate by proclaiming the bar. Anything more than this is superfluous; less would not suffice.

33. *Id.* at 226.
34. A.L.I. Fed. Income Tax Stat. S.X. 330 (c).