

THE FEDERAL INCOME TAX STATUTES OF LIMITATION

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Statutes of limitation play a significant part in the administration and enforcement of the federal income tax laws since they fix the period during which the taxing authorities may assess and collect the tax. For the taxpayer they sometimes are of critical importance, determining whether he will be able to take advantage of his right to contest a disputed tax.

The Internal Revenue Code of 1954 was approved by the President on August 16, 1954.¹ It will be the purpose of this article to highlight some of the changes which the new law has made affecting periods of limitation in civil and criminal income tax proceedings.

The provisions of the 1954 Code concerning limitations are, in general, applicable only with respect to taxes imposed by the 1954 Code. The provisions of the 1939 Code will continue to apply to taxes imposed by the 1939 Code.² This means that for a period of several years, until the disputed questions arising under the 1939 Code are disposed of, the tax practitioner will be working with two sets of rules for limitations—one set governing taxes levied under the new Code and the other applying to taxes under the old Code.

While there are many provisions in the Internal Revenue Code prescribing the time within which certain acts must be done,³ we will deal here with the limitations most frequently encountered and which will now be found grouped under one heading, Chapter 66, of the 1954 Code. These provisions concern (1) limitations on assessment and collection, (2) limitations on credit or refund, and (3) periods of limitation in judicial proceedings.

LIMITATIONS ON ASSESSMENT AND COLLECTION

Assessment is the formal administrative act imposing upon a taxpayer a certain tax liability which, in the absence of further action by the taxpayer, becomes final. Under the Internal Revenue Code of 1954, the assessment is made "by recording the liability of the taxpayer in the office of the Secretary (of the Treasury) or his delegate in accordance with rules or regulations prescribed by the Secretary or his delegate".⁴

With certain exceptions to be noted later, an assessment for income taxes must be made within three years after the return was filed.⁵ If it

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¹ Public Law 591, Title 26 United States Code.

² INT. REV. CODE OF 1954, §§7851 (a) (6) and 7851 (d).

³ See, for example, cross references in sections 6501 to 6533 IRC.

⁴ INT. REV. CODE OF 1954, §6203.

⁵ INT. REV. CODE OF 1954, §6501.

is not so made, no proceeding may thereafter be brought against the taxpayer for the collection of the tax. This was the rule under the 1939 Code and continues to be the rule under the 1954 Code.⁶ Under the 1939 Code, the three-year period of limitations applied only to the assessment of income, estate, and gift taxes, whereas for most other taxes the period for assessment was four years.⁷ Under the 1954 Code the three-year period is now uniform for all taxes.⁸

If an income tax return is filed before the due date, the period of limitations begins on the due date, not the date on which the return was filed.⁹ Hence, an early return will be considered as filed on the last day prescribed by the statute or regulations for filing the return. This was the rule for income taxes under the 1939 Code,¹⁰ which has been carried over into the 1954 Code and at the same time extended to most other taxes.

If a return is filed after the due date, the period of limitations begins to run from the date of actual filing not the due date.¹¹ The rule for tardy returns is therefore not the same as that for early ones.

Notice of Deficiency

In the ordinary case where the collection of the tax will not be jeopardized by delay, the Commissioner of Internal Revenue may not make an assessment until after a notice of deficiency has been sent to the taxpayer by registered mail. Within ninety days after the notice of deficiency is mailed the taxpayer may file a petition with the Tax Court for a redetermination of the deficiency.¹² No assessment may be made or collection proceedings begun during the ninety-day period.¹⁴ If a petition is filed with the Tax Court, the period of assessment is then postponed until the decision of the Tax Court has become final.¹⁵ After the notice of deficiency is mailed, the running of the period of limitations is suspended for the period during which the Commissioner is prohibited from making the assessment and for sixty days thereafter.¹⁶

If the taxpayer does not file a petition with the Tax Court within the 90-day period, the deficiency is then assessed and must be paid upon notice and demand.¹⁷

⁶ INT. REV. CODE OF 1939, §275(a), 53 STAT. 86.

⁷ INT. REV. CODE OF 1939, §275(a), 53 STAT. 86; §874(a), 53 STAT. 135; §1016(a), 53 STAT. 153; §1635(a), 64 STAT. 538; §3312(a), 53 STAT. 400.

⁸ INT. REV. CODE OF 1954, §6501(a).

⁹ INT. REV. CODE OF 1954, §6501(b) (1).

¹⁰ INT. REV. CODE OF 1939, §275(f), 53 STAT. 87.

¹¹ INT. REV. CODE OF 1954, §6501(a).

¹² INT. REV. CODE OF 1954, §6213(a).

¹³ *Ibid.*

¹⁴ *Ibid.*

¹⁵ *Ibid.*

¹⁶ INT. REV. CODE OF 1954, §6503(a).

¹⁷ INT. REV. CODE OF 1954, §6213(c).

Jeopardy Assessments

Where, in the opinion of the Commissioner, the assessment or collection of a tax would be jeopardized by delay, the formal notice of deficiency, or 90-day letter, need not be sent. The assessment and demand for payment are then made forthwith; and the notice of deficiency is mailed to the taxpayer within sixty days after the making of the assessment.¹⁸

The jeopardy assessment may be made whether or not the taxpayer has theretofore filed a petition with the Tax Court and the Tax Court has jurisdiction to redetermine the entire amount of the deficiency and of the amounts assessed.¹⁹

Special Five-Year Period of Limitations

Under the 1939 Code, if the taxpayer omitted from gross income an amount properly includible therein which exceeded twenty-five (25) per cent of the amount of gross income shown on the return, the period of limitations for the assessment of the tax was five years instead of three years from the date the return was filed.²⁰ Under the 1954 Code the 5-year period has been extended to six years.²¹

The 1939 Code contained no definition of gross income for the purpose of determining when this particular provision of the law came into play. The Treasury and the Tax Court took the position that overstatement of costs of goods sold constituted an omission from gross income, but one of the United States courts of appeals took a contrary view.²² Under the 1954 Code, the cost of goods sold is no longer a relevant factor in determining the amount of the omission from gross income for the statute now explicitly provides that in the case of a trade or business, the term "gross income" means the total of the amounts received or accrued prior to diminution by the cost of sales or services.²³

If the taxpayer discloses either on his return or in a statement attached to the return the nature and amount of the receipts which he is omitting from gross income, the six-year period of limitations does not apply. This is a new provision added by the 1954 Code.²⁴

No Limitation in Case of Fraud or Failure to File Return

As was true under the 1939 Code, there is no period of limitation for the assessment and collection of tax in case a false or fraudulent return is filed or in case of a failure to file a return where one is required.²⁵

¹⁸ INT. REV. CODE OF 1954 §6861(a) (b).

¹⁹ INT. REV. CODE OF 1954, §6861(c).

²⁰ INT. REV. CODE OF 1939, §275(c), 53 STAT. 86.

²¹ INT. REV. CODE OF 1954, §6501(e).

²² Estate of J. W. Gibbs, Sr., 21TC—No. 55 (1954); Uptegrove Lumber Company v. Comm'r., 204 F. 2d 570 (3rd Cir. 1953).

²³ INT. REV. CODE OF 1954, §6501(c) (1) (A) (i).

²⁴ INT. REV. CODE OF 1954, §6501(e) (1) (A) (ii).

²⁵ INT. REV. CODE OF 1939, §276, 53 STAT. 87; INT. REV. CODE OF 1954, §6501(c) (1) (2) (3).

In these instances the tax may be assessed, or a proceeding in court for the collection of the tax may be begun without assessment, at any time.

The enforcement of the civil liability should be distinguished from criminal prosecutions for violations of the internal revenue laws. While no periods of limitations exist for the assessment and collection of the tax in case of fraud or wilful failure to file returns, there are statutes of limitations governing the institution of criminal prosecutions for these offenses.

Some Other Exceptions

Where the estate of a decedent is in the process of administration or a corporation is in the process of dissolution, it is important to know the exact amount of income tax liability which the taxing authority may assert. If the executor or other fiduciary representing the estate of a decedent or the corporation contemplating dissolution makes a written request for a prompt assessment, the tax must be assessed, or a proceeding for the collection of the tax must be begun, within 18 months from the date of the request. The request must be filed in the manner and form prescribed by the regulations.²⁶

The taxpayer and Commissioner of Internal Revenue may consent in writing to an extension of the statute of limitations for the assessment of the tax. The agreement for the extension must be made before the expiration of the period for assessment; and may be extended by subsequent agreements. There is no change in existing law in this provision.²⁷

Limitations on Proceedings for Collection.

Proceedings for collection may be instituted in court either before or after assessment of the tax.²⁸ The usual procedure is to make the assessment and then begin proceedings for collection.

If the proceedings are instituted before assessment, they must be begun within the same period fixed for making the assessment—in the ordinary case, three years from the date of filing the return.²⁹

Where an assessment has been made within the period fixed by law, the tax may be collected by levy or by a proceeding in court which is begun within six years after the date of the assessment. The six year period may be extended by agreement between the Commissioner and the taxpayer.³⁰ This provision is the same as the old law.³¹

The 1954 Code, however, provides for the suspension of the statute of limitations on collection in two instances not covered by the old law.³² One is the case where the assets of a taxpayer (other than the estate of a decedent or an incompetent) are in the control or custody of any court.

²⁶ INT. REV. CODE OF 1954, §6501(d).

²⁷ INT. REV. CODE OF 1954, §6501(c)(4).

²⁸ INT. REV. CODE OF 1954, §§6501(a) and 6502(a).

²⁹ INT. REV. CODE OF 1954, §6501(a).

³⁰ INT. REV. CODE OF 1954, §6502(a).

³¹ INT. REV. CODE OF 1939, §276(c).

³² INT. REV. CODE OF 1954, §6503(b) and (c).

During this period and for six months thereafter, the running of the statute is suspended.³³ Under the old law the period of limitations was suspended only when the assets were in bankruptcy or receivership; and the suspension applied only to gift and income tax.³⁴ Now the suspension applies to all taxes and is not restricted to bankruptcies and receiverships. The second instance is the case where collection is hindered or delayed because property of the taxpayer is situated or held outside the United States. The statute is now suspended during this period for all taxes. However, the total suspension of time because of this reason may not exceed six years.³⁵

LIMITATIONS ON CREDITS AND REFUNDS

Under the 1954 Code claims for credit or refund of a tax must be filed within three years from the time the return was required to be filed (determined without regard to any extension of time for filing) or two years from the time the tax was paid, whichever of such periods expires the later. If no return was filed by the taxpayer, the period of limitations is two years from the time the tax was paid.³⁶

Under the 1939 Code, a refund claim was timely if filed within three years from the filing of the return³⁷—rather than three years from the original due date of the return as is the rule under the 1954 Code.³⁸ However, the amount of the tax that was recoverable under the 1939 Code was limited to that amount paid during the three years preceding the filing of the claim for refund.³⁹ Hence, if a taxpayer paid a tentative tax on the date a return was required and then filed his return and paid the balance of the tax several months later, a claim for refund filed within three years from the date of the filing of the return but more than three years from the date of the payment of the tentative tax, would be valid only with respect to the balance of the tax paid at the time of filing the return and ineffective to recover the tentative tax. Under the 1954 Code such a refund claim would be totally invalid, since it was filed more than three years after the date the return was required.

After a claim for refund is filed, it is either approved or rejected by the Internal Revenue Service. If the claim is rejected, a suit or proceeding for the recovery of the tax must be begun within two years from the date of the mailing of the notice of disallowance. This was and is the rule under both the 1939 and 1954 Codes.⁴⁰

³³ INT. REV. CODE OF 1954, §6503(b).

³⁴ INT. REV. CODE OF 1939, §274(b), 53 STAT. 86 and §1015(b), 53 STAT. 153.

³⁵ INT. REV. CODE OF 1954, §6503(c).

³⁶ INT. REV. CODE OF 1954, §6511(a).

³⁷ INT. REV. CODE OF 1939, §322(b) (1), 53 STAT. 91 and §322(b) (2), 53 STAT. 92.

³⁸ INT. REV. CODE OF 1954, §6511(a).

³⁹ INT. REV. CODE OF 1939, §322(b) (2), 53 STAT. 92.

⁴⁰ INT. REV. CODE OF 1939, §3772(a) (2), 53 STAT. 465, INT. REV. CODE OF 1954, §6532(a) (1).

The two year period for filing suit after disallowance of the claim may be extended for any period as may be agreed upon in writing between the Commissioner and the taxpayer.⁴¹ Under the 1939 Code the period could be extended only to the date of final decision in one or more specific cases then pending before the courts.⁴²

Under the 1954 Code, if the taxpayer files a written waiver of the requirement that he be sent a notice of disallowance of his claim for refund, the two-year period for filing suit for refund begins to run on the date the waiver is filed.⁴³ There was no such provision in the 1939 Code.

If the Commissioner fails to render a decision on a claim for refund within six months from the date the claim is filed, the taxpayer may then bring suit on the claim at the expiration of the six months period.⁴⁴

Where the Commissioner and the taxpayer enter into an agreement to extend the period within which the income tax may be assessed, the time for filing a claim for credit or refund does not expire until six months after the expiration of the period within which the assessment could be made pursuant to the agreement.⁴⁵

STATUTES OF LIMITATIONS ON CRIMINAL PROSECUTIONS

A criminal prosecution for violation of the internal revenue laws is a proceeding separate and apart from any proceeding involving civil liability for the tax. The outcome of the criminal proceeding does not affect the right of the Government to collect the tax and is not *res judicata* of the civil liability.

The limitations governing criminal prosecutions are found in section 3748 of the Internal Revenue Code of 1939. The counterpart of this section in the 1954 Code is section 6531.

The general rule is that the indictment must be found or the information instituted within three years after the commission of the offense.⁴⁶ To this rule there are important exceptions enumerated in the statute where the period of limitations is six years instead of three years.⁴⁷ Thus, the six year period applies to offenses involving the defrauding of the United States, the offense of wilfully attempting in any manner to evade or defeat a tax, the offense of wilfully aiding or assisting in the preparation of a false return or claim, and other offenses.

The 1954 Code changed the period of limitations for prosecutions of several offenses. Under the 1939 Code the offenses of wilfully failing to pay a tax or to file a return had to be prosecuted within three years.⁴⁸

⁴¹ INT. REV. CODE OF 1954, §6532(a) (2).

⁴² INT. REV. CODE OF 1939, §3774(b) (2), 53 STAT. 466.

⁴³ INT. REV. CODE OF 1954, §6532(a) (3).

⁴⁴ INT. REV. CODE OF 1954, §6532(a) (1).

⁴⁵ INT. REV. CODE OF 1954, §6511(c).

⁴⁶ INT. REV. CODE OF 1954, §6531.

⁴⁷ INT. REV. CODE OF 1954, §6531(1) (2) (3) (4) (5) (6) (7) (8).

⁴⁸ INT. REV. CODE OF 1939, §3748(a), 53 STAT. 461.

Under the new Code these offenses may be prosecuted within six years. The period of limitations was also extended from three to six years for the following crimes: (a) making a false statement in connection with any return or other document under the internal revenue laws, in violation of sections 7206 and 7207 of the 1954 Code; (b) attempting to intimidate or impede an employee of the Internal Revenue Service in the performance of his duties, in violation of 7212(a) of the 1954 Code; and (c) certain offenses committed by United States officials and employees, in violation of section 7214 of the 1954 Code.

The 1954 Code controls the period of limitations for all offenses committed after the date of enactment of the new law. The 1939 Code provisions continue to apply to acts done or offenses committed before enactment of the 1954 Code.⁴⁹

In the case of advance filing of a return or the advance payment of a tax, the period of limitations, under the 1954 Code, starts on the due date of the return or payment rather than on the date of actual filing or payment.⁵⁰ This was not the rule under the 1939 Code. Thus, under the old Code, if a return was filed on February 15, 1950, and the statute of limitations for the offense was six years, the period of limitations would expire on February 15, 1956. Under the new Code, where a return is filed on February 15, 1955, prosecution would not be barred until April 15, 1961—six years from the due date of the return.

Tolling of the Statute

Section 3748(a) of the 1939 Code contains the following provision:

The time during which the person committing any of the offenses above mentioned is absent from the district wherein the same is committed shall not be taken as any part of the time limited by law for the commencement of such proceedings.

The words "absent from the district" were not uniformly construed by the courts.⁵¹ Under the interpretations of some courts, it was possible, for example, that the statute of limitations would never run against some individuals. Thus, a person who lives in the Bronx, New York, which is located in the southern judicial district of New York, is required to file his tax returns with the collector or director in Albany, New York, which is located in the northern judicial district of the state. If the taxpayer simply continued to reside in the Bronx, in the southern district, he would be absent, in the view of some courts, from the northern district where the return was filed or the offense was committed, and thus the statute of limitations would never run against him. It was

⁴⁹ INT. REV. CODE OF 1954, §7851(d).

⁵⁰ INT. REV. CODE OF 1954, §§6513 and 6531.

⁵¹ Compare *United States v. Beard*, 118 F. Supp. 297 (D. C. Md. 1954) and *United States v. Eliopoulos*, 45 F. Supp. 777 (D.C. N.J. 1942), with *United States v. Satz*, 109 F. Supp. 94 (N.D. N.Y. 1952) and *United States v. Udell*, 109 F. Supp. 96 (D. C. Del. 1952).

to remedy this situation that the 1954 Code changed the law. The comparable provision in section 6531 now reads:

The time during which the person committing any of the various offenses arising under the internal revenue laws is outside the United States or is a fugitive from justice within the meaning of section 3290 of Title 18 of the United States Code, shall not be taken as any part of the time limited by law for the commencement of such proceedings.

Section 3290 of Title 18 reads simply: "No statute of limitations shall extend to any person fleeing from justice."

So, instead of the provision in old section 3748(a) that the time during which the person committing any of the offenses is absent from the district where the offense is committed, shall not be taken as any part of the period of limitations, we now have the provision in section 6531 that the statute is tolled when the person committing the offense is outside the United States or is a fugitive from justice.

The second method by which the statute of limitations may be extended is by the filing of a complaint before a commissioner of the United States before the limitations period has expired. Under the old Code if a complaint was properly instituted before the limitation period had expired, the statute was extended until the discharge of the grand jury at its next session within the district.⁵² Under the new Code the period is extended until a date which is nine (9) months after the date of the making of the complaint before the commissioner of the United States.⁵³

When Is A Complaint "Instituted"?

Since the operation of the statute may be tolled by instituting a complaint, it becomes important to determine what "instituting" a complaint means.

A complaint is merely a sworn statement or affidavit filed with a United States commissioner charging a person with the commission of a crime. Rule 3 of the Federal Rules of Criminal Procedure defines a complaint as follows: "The complaint is a written statement of the essential facts constituting the offense charged. It shall be made upon oath before a commissioner or other officer empowered to commit persons charged with offenses against the United States."

The complaint is usually made by a person having some knowledge of the facts, such as the special agent or the revenue agent in a tax case. Does instituting a complaint before a commissioner mean the mere making and filing of the complaint with the commissioner, or does it mean something more? That was the question in *United States v. Dolan*,⁵⁴ which the court answered in this way:

⁵² INT. REV. CODE OF 1939, §3748(a), 53 STAT. 461.

⁵³ INT. REV. CODE OF 1954, §6531.

⁵⁴ 113 F. Supp. 757 (D.C. Conn. 1953).

Thus is raised a question of statutory interpretation which is not as simple as a first glance would indicate. By the *institution* of a complaint does the statute mean merely the presentation to the commissioner of a sworn writing sufficient in content to satisfy the definition of a complaint contained in Rule 3? An interpretation of such scope, I think, should be rejected. It overlooks the fact that not every complaint presented to a commissioner is automatically filed by him and accepted by him as a proper foundation instituting a criminal prosecution.

The court added these words of guidance:

. . . the commissioner should not accept the complaint as instituting a criminal prosecution until by examination under oath of at least one witness he finds probable cause for believing the existence of one or more underlying facts from which in their context the ultimate inference might reasonably be made.

If the commissioner issues a warrant of arrest upon the basis of the complaint, there is a presumption that he has satisfied himself that the complaint was based on probable cause and was validly instituted. Thus in the *Dolan* case, the court ruled that the complaint was effective to toll the statute, since the only showing by the defendant was that the complaint had been filed and a warrant was issued.

The *Dolan* case, however, opens up some areas of inquiry in those cases where an attempt has been made to toll the statute by filing a complaint. If it is actually proved that there was no hearing on the complaint and that no witnesses were examined under oath by the commissioner before the warrant was issued, presumably under the rule of the *Dolan* case the complaint does not toll the statute.

In *United States v. Langsdale*,⁵⁵ a complaint signed by an assistant United States attorney who had no personal knowledge of the facts stated therein was held to be an insufficient basis for the issuance of a warrant and ineffective to toll the statute of limitations.

⁵⁵ 115 F. Supp. 489 (W.D. Mo. 1953).

