1980

Supplement: Criminal Prosecution - Voluntary Disclosure; History, Revocation and Revival

R. Barrow Blackwell

SUPPLEMENT

The following article is one of the papers submitted by a student in fulfillment of one of the course requirements as a candidate for the degree of Masters in Law and Taxation.

CRIMINAL PROSECUTION—VOLUNTARY DISCLOSURE; HISTORY, REVOCATION AND REVIVAL

R. BARROW BLACKWELL

Almost thirty years ago the Department of Treasury abandoned its longstanding policy of not recommending criminal prosecution to the Justice Department of a taxpayer who, prior to an investigation of his tax status by the then Bureau of Internal Revenue, voluntarily disclosed to proper Bureau officials that he had filed a fraudulent return or had willfully failed to file a return. First announced to the public in 1945, this policy of voluntary disclosure was withdrawn on January 10, 1952.[1] Derived from neither statute nor regulations,[2] the policy was instead a discretionary rule of administration which stemmed from the general supervisory powers of the Commissioner of Internal Revenue in aid of his principal function, the collection of the revenue.[3]

This paper explores the history of the voluntary disclosure policy, its nature and operative effect, the problem of its administration, the reasons for its abandonment and, finally, the attempts to revive it. In doing so, primary focus is directed to the arguments, both pro and con, of voluntary disclosure as a tool of federal tax policy, with comment on its place, if any, in the enforcement of the criminal tax laws.

The voluntary disclosure policy was first made public in a press release on August 21, 1945 by then Secretary of the Treasury Vinson:

> The Commissioner of Internal Revenue does not recommend criminal prosecution in the case of any taxpayer who makes a voluntary disclosure of omission or other misstatement in his tax return or of failure to make a return.[4]

The policy, however, had been formulated and implemented long before its public announcement. In a speech on May 14, 1947, J. P. Wenchel, then Chief Counsel of the Bureau of Internal Revenue, stated:

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[1] Balter, *Tax Fraud and Evasion* (3d Ed.), 1963, Section 4.2, page 4, citing Treas. Dept. Announcement S-2930, Jan. 10, 1952.

[2] Burns and Rachlin, "Should We Penalize Voluntary Disclosures?", 28 TAXES 39, January, 1950.

[3] Letter of the Attorney General of the United States to the Secretary of Treasury regarding voluntary disclosure legislation, dated June 1, 1950.

[4] Winer, "Voluntary Disclosures and Related Federal Tax Fraud Matters," 26 B.U.L.Rev. 1, 16 (Jan. 1946); Burns and Rachlin, 28 TAXES 39.

> There is nothing new in this position. For years the position of the Department has been that where the taxpayer makes a voluntary disclosure of intentional evasion before the investigation has been initiated criminal prosecution will not be recommended.[5]

The policy's historical antecedents are found at least as far back as 1934, and probably as early as 1919. Initially, the policy appears to have been formulated in a confidential mimeograph issued to Bureau personnel on September 8, 1919:

> In cases in which fraud or intentional evasion is discovered thorugh internal revenue officers, or is disclosed after the Bureau has initiated an investigation of tax liability, it will be the policy of the Bureau to impose the maximum civil penalties and institute criminal prosecution . . .
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> In cases in which voluntary disclosure is made of deficiencies thorugh intentional evasions which if discovered by internal revenue officers would be made the basis of criminal prosecution, it will be the policy of the Bureau to impose the maximum civil penalties and to consider offers in compromise of the criminal liability, instead of initiating prosecution and insisting on a jail sentence.[6]

This policy was effectuated by use of statutory compromise agreements pursuant to the forerunners of Section 7122 of the Internal Revenue Code.[7]

In 1934 the voluntary disclosure policy was restated in another confidential Bureau mimeograph:

> Where a violation of the internal revenue laws is deliberate and with the intent to defraud, and is discovered through internal revenue officers, or is disclosed by the taxpayer after the Bureau has initiated an investigation, the criminal liability will in no case be compromised by the Treasury Department. Prosecution will be recommended or not, solely on the basis of whether the evidence is sufficient to afford reasonable grounds for the belief that a conviction can be secured.
>
> In cases in which taxpayers make voluntary disclosures of intentional evasions before investigation by the Bureau has been initiated, the Bureau will not recommend criminal prosecution, but will impose the maximum civil panalties unless there is substantial doubt as to collectibilty.[8]

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[5] Burns and Rachlin, 28 TADES 39.

[6] Paul Lipton, "Prosecutions for Tax Evasions—New Policies and Procedures," 30 TAXES 356, 357-358 (May, 1952).

[7] Lipton, 30 TAXES 358, referring to the predecessors of IRC Section 3761.

[8] *Id.*, at page 358.

This revised statement removed some of the doubt implied by the word "consider" in the 1919 version, a word which had been substituted for "accept" as finally drafted.[9] After 1934 the Bureau's policy was theoretically less discretionary: criminal prosecution would *not* be recommended if the taxpayer's fraud was properly and timely disclosed. Statutory compromise agreements were no longer utilized; thereafter cases were handled on an individual basis as purely an administrative matter.[10] It was substantially in this form that the policy was announced to the public in 1945.

The purpose of the voluntary disclosure policy was to increase tax revenues at a cost which was minimal to the government. In support of the policy, Bureau Chief Counsel Wenchel stated in 1947:

> In excusing the man from criminal prosecution we are merely taking the sensible step to produce the revenue called for by the law with the minimal cost of investigation. The man who makes a voluntary disclosure saves us a lot of money in investigating. In return, we can spare him a term in jail. This is good business from his standpoint and it is good business from the government's standpoint.[11]

Public announcement of the policy, however, coincided with a surging increase in tax evasion during the second world war. The number of evasion cases received by the Commissioner of Internal Revenue nearly tripled between 1942 and 1945 and more than doubled again between 1946 and 1947.[12] These increases were variously attributed to unprecedented increases in the individual income tax rates,[13] as well as to a stiff excess profits tax levied on corporations and the proliferation of black market operations during the war.[14] The Bureau launched a vigorous drive on tax fraud at the end of the war, but faced with manpower shortages, the statutes of limitation and the increasing difficulty of detecting fraud over time,[15] the Treasury Department felt compelled to enlist the aid of practical-minded and conscience-stricken taxpayers. Although then Bureau Chief Counsel Wenchel declared that in the first eighteen months after the policy was announced an addi-

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[9] *Id.*, at page 358.

[10] *Id.*, at page 358.

[11] Burns and Rachlin, 28 TAXES 40.

[12] Turner L. Smith, "Policies and Procedures in Income Tax Fraud Cases," 28 TAXES 761, 762 (August, 1950). The number of income tax evasion cases received from the Commissioner for the eight year period from 1942 to 1949 were as follows:

1942	79	1946	241
1943	93	1947	523
1944	71	1948	691
1945	203	1949	420

[13] Smith, 28 TAXES 762; Lipton, 30 TAXES 358.

[14] Smith, 28 TAXES 762.

[15] Lipton, 28 TAXES 358.

tional $500 million was collected from such disclosures,[16] the Bureau later admitted at the King Subcommittee hearings, which were investigating purported corruption in the Bureau, that it had no statistics to show how much revenue the policy actually had produced.[17]

As described by Mr. Wenchel the policy was a simple one:

> And what is a voluntary disclosure? A voluntary disclosure occurs when a taxpayer of his own free will and accord, and before any investigation is initiated, discloses fraud upon the government . . .[18]

In theory the procedure for accomplishing a voluntary disclosure was equally straightforward:

> The making of a voluntary disclosure is a simple thing. The taxpayer or his legal agent can go before any official of the Bureau of Internal Revenue or any of its field offices—whether it is a Collector, a Deputy Collector, a Revenue Agent, a Special Agent, or any other responsible Treasury officer. There is no special form for making the disclosure. The simple statement that 'I have filed false returns and I want to make the government whole' would constitute a complete disclosure. Of course, it is usually best to present an amended return or other written document as evidence of the disclosure.[19]

In short, the disclosure had to be voluntary, complete,[20] made before the proper Treasury or Bureau representatives, accompanied by the payment of civil penalties eventually imposed, and accomplished before an investigation had been initiated by the Bureau. This latter requirement was critical and "initiation of an investigation" was defined thus:

> The mere record of a name does not mean that an investigation has been initiated. The fact is that examining officers throughout the country have thousands of names or possible leads. To deny the existence of voluntary disclosure merely because we have a name, would be comparable to regarding the telephone book as a dossier of tax evaders.
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> An investigation is initiated when a Special Agent, an Internal Revenue agent, a Deputy Collector, or other Bureau

[16] Burns and Rachlin, 28 TAXES 39.

[17] Lipton, 28 TAXES 358, n.53.

[18] Jones, "Voluntary Disclosure Policy of the Treasury Department," *Note,* 6 Tax L. Rev. 329, 330 (N.Y.U. March, 1951); Burns and Rachlin, 28 TAXES 39.

[19] *Note,* 6 Tax L. Rev. 330.

[20] Where disclosure not complete, no offer of immunity. *Shotwell Mfg. Co.* v. *United States,* 371 U.S. 341 (1963); Mortensen, *Federal Tax Fraud Law,* Section 60, p. 68 (1958).

> officer, is assigned a return for examination, or where an investigating officer has requested the advice of appropriate officers of the Bureau with respect to the filing of a return or the payment of taxes.[21]
>
> The time of disclosure and the time an investigation begins are, therefore, matters which can be ascertained with complete objectivity and certainty, thus protecting both the government and the taxpayer from decisions based on guesswork or other vague circumstances. To assure adherence to this principle, the Bureau stands ready at all times where a dispute may arise as to the time of a disclosure and the time an investigation was initiated to open its records in that regard.[22]

Despite this apparently well-defined policy and procedure, in practice the policy did not work nearly so simply. A major difficulty for the taxpayer was in knowing whether he had timely disclosed his misdeeds. Notwithstanding as declared "openness" of Bureau files,[23] one commentator has stated that this was not true in practice and that "no instruction to that effect was ever issued to the (Bureau's) Field Offices."[24] Moreover, some special agents' offices took the position that if any investigation had been commenced by a governmental authority, not necessarily a federal agency, it was too late to make a voluntary disclosure.[25]

The taxpayer, in inquiring of various Treasury agencies whether an investigation of his tax status had in fact begun, ran the risk of himself triggering an investigation,[26] and his curiosity would doubtless inspire a more comprehensive investigation, if already initiated.[27] Inquiries would have to be directed to several places. It was conceivable that the Agent in Charge of the taxpayer's district would have no knowledge that a Collector or Special Agent in Charge had already assigned the taxpayer's return for examination.[28]

Additionally, it was not always clear when an investigation had begun. Had an investigation of the taxpayer begun where he was only part of a "chain' 'investigation involving his financial dealings with other taxpayers who were under investigation for tax fraud?[29] The problem of determining when a collateral investigation became a primary one as to a particular taxpayer was raised in *United States* v. *Weisman*, 78 F. Supp. 979 (D. Mass. 1948). There, the special agent had conducted a collateral investigation involving Weisman's financial

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[21] *Note,* 6 Tax L. Rev. 330.

[22] Burns and Rachlin, 28 TAXES 39, at page 40.

[23] Volume 12, N.Y.U. *Inst. on Federal Taxation,* "Voluntary Disclosures," page 213, at 215, n.130.

[24] Burns and Rachlin, 28 TAXES at 41.

[25] John Griffin, "Fraud," 28 TAXES 151, 159 (February 1950).

[26] Balter, "Should Your Client 'Cooperate' When Charged with Tax Fraud?", 29 TAXES 290, 295 (April, 1951); Griffin, 28 TAXES 159.

[27] 12 N.Y.U. *Inst. on Fed. Tax.* 215.

[28] *Id.*

[29] Balter, 29 TAXES 294, 295.

transaction with others. Sensing that he would be the target of a further probe, Weisman confessed his misdeeds. His disclosure was not considered timely, however. The investigation had begun with other taxpayers who were involved with Weisman.[30] Thus, Weisman's defense that his confession had been improperly obtained was rejected; he had not been required to divulge the information to Bureau officials.[31]

If a taxpayer was investigated as to a particular year, there was a further problem as to whether his voluntary disclosure would be accepted as to prior and subsequent years.[32] Or, if a taxpayer's return was examined and he was assessed a deficiency which he paid and then disclosed additional information regarding transactions for the period covered by the return which indicated fraud, was the voluntary disclosure timely made?[33] Or, this further problem suggested by one commentator: "whether a voluntary disclosure by a taxpayer as to fraud in his individual tax return will be considered a grant of immunity to a corporation in which the taxpayer is a substantial stockholder and where the corporation itself has defaulted on its taxes by diverting part of its income to the stockholder."[34]

The fact that the initiation of an investigation was unknown to the taxpayer did not help his cause. In *Lapides* v. *United States,* 215 F.2d 253 (2nd Cir. 1954), a taxpayer obtained an order from the district court requiring the United States Attorney to show cause why certain evidence divulged by the taxpayer as part of what he believed was a voluntary disclosure should not be suppressed from being presented to the grand jury. After a hearing, the order was dismissed and the taxpayer was subsequently indicted and found guilty. The taxpayer had voluntarily disclosed that he had not reported specified income for the five years from 1946 to 1950. This disclosure was made on May 15, 1951. Unbeknownst to the taxpayer, a special agent of the Bureau had been assigned to undertake a preliminary investigation of the taxpayer's returns on April 14, 1951, an investigation prompted by state criminal charges against the taxpayer for maintaining a lottery and gambling. The Special Agent consulted with the State's Attorney on April 23, 1951, requisitioned the taxpayer's returns on April 27, 1951, and transferred the investigation to another Special Agent on May 15, 1951.

On appeal, the Second Circuit considered the crucial issue of whether the disclosure had been timely. In holding that it was, the Court stated (p. 256):

> . . . For even if it were so that the appellant, when he made his disclosure on May 15, 1951, did not know, notwithstand-

[30] Burns and Rachlin, 28 TAXES 40-41.

[31] *Id.;* Mortensen, *Federal Tax Fraud Law,* Section 60, p. 68 (Bobbs-Merrill 1958).

[32] Balter, 29 TAXES 294, 295.

[33] 12 N.Y.U. *Inst. on Fed. Tax.* 217.

[34] Balter, 29 TAXES 294-295.

> ing the publicity as to his arrest, that a federal tax investigation had already been initiated, and even if in April, 1953, when he brought the motion initiating this proceeding, he thought that his disclosure had precipitated the departmental investigation, it would not follow that his disclosure was timely. Only if, in fact, no investigation had been begun, was his disclosure timely. United States v. Levy, D.C. Conn., 1951, 99 F.Supp. 529. The mere fact that the Department did not inform him and that he did not know that an investigation had begun was irrelevant. Any holding to the contrary contained in the case of In re Liebster, D.C., E.D. Pa., 1950, we cannot approve.

Support for this holding is at least implicit in *White* v. *United States,* 194 F.2d. 215 (5th Cir. 1952), involving a motion to suppress information obtained by Internal Revenue agents from taxpayers who had disclosed their fraud in the belief that they would be granted immunity from criminal prosecution. The district court held that the Treasury's voluntary disclosure policy was not available to taxpayers after an investigation had been begun, and hence any admissions voluntarily made without inducement or promise were competent evidence in a subsequent prosecution. While the facts of *White* were in dispute as to the knowledge of the taxpayers, the Court on appeal affirmed that the disclosures were not timely, having been made only after the investigation was underway. Accordingly, the taxpayers could not rely on the voluntary disclosure policy even though they contended that they were unaware of the investigation. Their statements were therefore not protected by their privilege against self-incrimination.

A contrary view, expressly rejected by the Second Circuit in *Lapides,* was expressed in *In re Liebster,* 91 F. Supp. 814 (E.D. Pa. 1950).[35] There, the district court accepted the taxpayer's argument that his statement should be suppressed because they were tendered without knowledge of an investigation. The Court held that statements made in the hope of immunity from prosecution where the taxpayer could demonstrate that he had no knowledge of the investigation could not be used against the taxpayer in a later prosecution.

While these cases dealt with the admissibility of statements obtained from allegedly unsuspecting taxpayers, and not with whether the Commissioner was or was not obligated to accept the disclosure as timely made, they nevertheless are authority for materiality of the taxpayer's knowliedge. *In re Liebster* remained a distinctly minority view.

The risks to the taxpayer from an untimely disclosure were less ambiguous. Once the taxpayer approached Bureau officials to make a disclosure, he had to be prepared for an examination of his books and records and to voluntarily answer the Bureau's questions under

[35] This case is discussed at length in *Note,* 6 Tax L. Rev. 329, 331-335.

oath.[36] If an investigation had already commenced, the taxpayer's voluntary disclosure statements constituted a waiver of the taxpayer's constitutional privilege against self-incrimination, and any admissions freely given could be used by the Bureau's agents in making their case against the taxpaper.[37] *United States* v. *Lustig,* 163 F.2d. 85 (2nd Cir. 1947). Moreover, the filing of an amended return based on financial records which were often in disarray and which caused the amended return itself to be false constituted a separate offense.[38]

With the lack of specific rules defining the identifiable event which initiated the investigation, the determination of whether a voluntary disclosure was acceptable was left to the almost unchecked discretion of Bureau officials, on whose integrity the taxpayer was forced to rely. In a letter to the Joint Committee on Internal Revenue Taxation of the Congress, the Bureau stated:

> It should be borne in mind that the policy is entirely an administrative one and in its application the Bureau must be the ultimate judge of the facts. Cases upon cases have of course been disposed of without prosecution under the policy. In the administration of the policy the Bureau attempts in every possible manner, through conferences with taxpayers or otherwise, to determine whether the facts of a particular case come within the voluntary disclosure policy. Where any tax evader is dissatisfied with the Buerau's decision and contends that his confession of deliberate fraud was obtained and is being used against him under circumstances which amount to a snare or delusion, the opportunity exists, just as happened (in *Lustig* and *Weisman*). In the event it is desired to disclose the application of the Bureau's voluntary disclosure policy to the facts of any specific case a conference for that purpose will be arranged on request by the taxpayer.[39]

It is not entirely clear that the taxpayer could actually litigate an adverse decision by the Bureau: he could litigate the propriety of using his statements in a subsequent prosecution.[40] The Bureau's decision not to accept an asserted voluntary disclosure was held to be nonreviewable in *Lustig*.[41] And it was clear that a voluntary disclosure did not entitle a taxpayer to immunity from prosecution under the compromise statute.

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[36] Griffin, 28 TAXES 159.

[37] *Id.*

[38] 12 N.Y.U. *Inst. on Fed. Tax.* 217.

[39] Burns and Rachlin, 28 TAXES 41.

[40] Burns and Rachlin, 28 TAXES 41.

[41] 12 N.Y.U. *Inst. on Fed. Tax.* This article quotes the following form Judge Kennedy in the *Lustig* case, although this writer has not been able to find the quoted portion either in the district court or appellate decisions:

> Now it is my notion of the law . . . that the Secretary of the Treasury and the named officials must assent to the specific compromise in the

In the *Lustig* case,[42] it held that the voluntary disclosure policy was not a blanket promise of immunity which had a binding effect on the Commissioner of Internal Revenue. At most a voluntary disclosure was an offer to compromise. Earlier, the Supreme Court, in *Botany Mills* v. *United States,* 278 U.S. 282 (1928), had held that the Commissioner could only compromise tax claims where the prescribed statutory formalities had been strictly followed and the consent of the Treasury Secretary or his delegate had been given. Informal agreements had no binding effect on the Commissioner unless the statute had been fully complied with.[43] The decision to accept a voluntary disclosure and not to recommend prosecution was purely administrative, not judicially reviewable, and hinged in part on the good faith decision of the Bureau to abide by its word.

The taxpayer, then, had to rely on the integrity of Bureau officials. This seemingly absolute authority of the Bureau could be checked in two possible ways so as to avert prosecution. First, the Department of Justice could reject prosecution if, in its view, the voluntary disclosure had been valid, or the disclosure would likely negative the element of willfulness in the minds of jurors.[44] Thus, even though voluntary disclosure was not a legal defense to criminal prosecution, the Justice Department accorded it weight in assessing the chances for conviction. Secondly, a motion to suppress would be sustained as to statements made by the taxpayer if the disclosure was shown to be bona fide and timely. *United States* v. *Shotwell Mfg. Co.,* 225 F.2d 394 (7th Cir. 1955).

The numerous difficulties which inhered in the administration of a policy lacking in specific guidelines was a major reason for its abandonment of the voluntary disclosure policy on January 10, 1952.[45] In announcing its abandonment, the Treasury Department stated:

> particular case, and if they refuse to compromise, their judgment is not reviewable by any court or jury. . . . Now, therefore, I charge you as a matter of law that neither court nor jury under our system has the right to review policy made by officials of the executive branch, like the Secretary of Treasury, or any administrative decisions made by the Secretary of the Treasury involving the determination of fact. . .

While it is clear that Judge Kennedy was referring to the compromise statute, this holding of law would apply, it would seem, to administrative determinations of whether a voluntary disclosure was in fact voluntary and timely.

[42] 163 F.2d 85 (2nd Cir. 1947).

[43] 278 U.S. at 288-289, referring to Rev. Stat. 3229, which provided in pertinent part:

> The Commissioner of Internal Revenue, with the advice and consent of the Secretary of the Treasury, may compromise any civil or criminal case arising under the internal revenue laws instead of commencing suit thereon; and, with the advice and consent of the said Secretary and the recommendation of the Attorney-General, he may compromise any such case after a suit thereon has been commenced.

[44] Balter, *Tax Fraud and Evasion* (4th Ed. 1976), Section 4.03, p. 4-4.

[45] Treasury Dept. Announcements S-2930, Ja. 10, 1952.

> Litigation in the courts in recent years has illustrated the controversial nature of the question as to what constitutes a true voluntary disclosure in fact. In the administration of the policy it has been difficult and at times impossible to ascertain whether the disclosure was made because the taxpayer realized he was under investigation or whether the disclosure was in fact voluntary and in reliance on the immunity held out by the policy.
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> The intensified enforcement activities of the Bureau's Special Tax Fraud Drive and Racket Squads throughout the country are ferreting out the willful tax evaders, and resulting in recovery of the additional taxes and penalties due the government.[46]

The Treasury Department also emphasized that a voluntary disclosure often held up prosecution; that the Bureau still had to resort to statutory remedies to collect the contemplated civil remedies; that it was felt that black marketeers and racketeers should not be able to utilize the policy;[47] that staffing to enforce the internal revenue laws had improved; and, finally and significantly, the policy was perceived by congressional authorities as having "... furnished an apt vehicle for some corruption in high places."[48]

Whatever the reasons for its abandonment, the voluntary disclosure policy lingers as an apparent informal policy and for ten years after its demise as a formal policy there were efforts to revive it.

Almost immediately after its abandonment the Tax Section of the American Bar Association attempted without success to have the policy reinstated at an administrative level.[49] Thereafter, the Section drafted legislation[50] to be approved by Congress, but in 1961 the House of Delegates of the ABA voted against recommending the proposed legislation.

The proposed legislation was essentially intended to provide the identifiable event by which the timeliness of the disclosure could be objectively determined. Under the Tax Section's proposal a taxpayer would have been exempted by statute from prosecution where a voluntary disclosure was made. A voluntary disclosure would be deemed timely if made both before the date of a written communication to the taxpayer from the Treasury Secretary or his delegate that an investigation of the taxpayer's liability for an indicated taxable period had been initiated and before the taxpayer had knowledge that

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[46] Lipton, 30 TAXES 357, at 358.

[47] *Id.* at 359.

[48] Balter, *Tax Fraud and Evasion,* (4th Ed. 1976), Section 4.02, p. 4-2.

[49] *Id.* at Section 4.05, p. 4-5.

[50] This somewhat lengthy proposal is set forth in full in Balter, *Tax Fraud and Evasion,* (3rd Ed. 1963) at Section 4.5, p. 4-6, n.15. A copy of same is contained in Appendix.

an inquiry or investigation was pending.[51] The burden of proof as to any issue with respect to the mailing of such written communication or of the taxpayer's knowledge was on the Secretary. In 1949 the Bureau had considered a similar, though non-legislative, proposal from the Tax Section to mail notices to taxpayers, informing them of an investigation. This suggestion was rejected because it was believed that honest taxpayers would resent the notice and refuse access to their books and records and that racketeers and "professional" evaders would destroy their records, intimidate prospective witnesses, and otherwise conceal facts which the Bureau could obtain through an unpublicized investigation.[52] Finally, under the proposed legislation the voluntary disclosure would have to be in writing, and if it was not a full disclosure the Secretary could bring a civil action in the district court to have the exemption nullified.

The ABA Tax Section set forth the following justification for a voluntary disclosure policy in a letter to the Commissioner of Internal Revenue:

> Income-tax evasion is a unique crime, in that our system of self-assessment imposes peculiar temptations upon tax-papers, and in that this self-assessment system affects millions of taxpayers widely differentiated as to education, experience, intelligence, emotional stability, social consequences, etc. Hence, the Service already distinguishes among various cases and gradations of income-tax crimes in determining which specific instances should be recommended for prosecution and which should not. The Advisory Group believes that a carefully drafted policy of voluntary disclosure policy would be of assistance to enforcement authorities in making the aforesaid distinction. We submit that voluntary disclosure prior to initiation of investigation in itself affords an adequate for including the taxpayer's case among those which are not to be recommended for prosecution. Such a policy could result in substantial collection of taxes, penalties, and interest from individuals who might never be caught in the enforcement net, or who, if caught, might not be successfully prosecuted because of lack of sufficient evidence.[53]

Congress had long treated income-tax evasion differently from other crimes, as evidenced by enactment of a statutory compromise proce-

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[51] See Section 7216(b) of the proposal. The requirement of written notice was suggested by Burns and Rachlin in their January, 1950, article, cited in footnote 2, at 28 TAXES 39, at 42.

[52] Lipton, 30 TAXES 357, at 360.

[53] Balter, *Tax Fraud and Evasion,* (3rd Ed. 1963), Appendix, page 4.9. This quote was actually a comment from the Advisory Group appointed to assist a Subcommittee of the House Ways and Means Committee in making a study of the administration of the internal revenue laws. It was contained in a letter from William R. Spofford to Commissioner of Internal Revenue Caplin in support of reinstatement of the voluntary disclosure policy.

dure.[54] Moreover, even without a formal policy, a voluntary disclosure often cast doubt on the taxpayer's willfulness and was a factor in assessing the success of prosecution. Revival of the policy, it was argued by proponents, would not encourage taxpayers to file fraudulent returns; no evidence suggested that increases in tax fraud were directly related to the Treasury's voluntary disclosure policy. Nor was the ABA Tax Section convinced that such a policy would spur collusion with Internal Revenue Service officials.[55]

The Tax Section and other commentators contended[56] that most of the difficulties and abuses of the abandoned policy could be cured by adoption of definite standards, particularly with respect to the cut-off event which determined the timeliness of the disclosure. This position was supported by some members of the King Subcommittee, who felt that Internal Revenue had failed to attempt a workable definition of the policy.[57]

Attempts to legislate a voluntary disclosure policy in fact pre-dated its abandonment. A revenue bill considered by the House Ways and Means Committee in 1950 provided:

> The Commissioner of Internal Revenue is hereby authorized to accept voluntary disclosures of underpayments of tax and shall issues rules and regulations which shall set forth the time within which such disclosures may be made, and the procedures which must be followed in making such disclosures. The Commissioner shall not refer to the Department of Justice for prosecution any case in which the taxpayer had made a full and complete disclosure in compliance with such rules and regulations, and proof of such disclosure shall constitute a defense to the person or persons making such disclosure in any criminal prosecution with respect to such underpayment of tax.[58]

This proposal, essentially similar to the proposal of the Tax Section of the ABA, provided a statutory exemption from prosecution, with the marked difference that it left to the Commissioner the formulation of rules and regulations for determining the timeliness of the disclosure.

In a letter dated June 1, 1950,[59] the Department of Justice expressed its opposition to the proposed legislation. In part, the Justice Department felt that a statute was unnecessary because the Commissioner

[54] Letter of Spofford to Commissioner Caplin, reprinted in Appendix to Balter, *Tax Fraud and Evasion*, etc.

[55] *Id.*

[56] See Burns and Rachlin, 28 TAXES at 43.

[57] Lipton, 30 TAXES 361.

[58] Statement on the Proposal Before the Ways and Means Committee for Legislation on "Voluntary Disclosure," undated (Reserve materials), from United States Department of Justice.

[59] See footnote 3.

was presently vested with the power to accept voluntary disclosures, and that regulations promulgated thereunder would "... divert attention from the main issue in many tax prosecutions by injecting another issue involving the construction, interpretation, and legality of such rules and regulations."[60] Perhaps more significantly, Justice expressed the fear that the Commissioner's obligation not to recommend prosecution would raise serious legal questions as to its own jurisdiction and authority in carrying out its mandate to enforce the criminal statutes.

While the Justice Department's opposition was chiefly directed against making voluntary disclosures statutory, thereby elevating the policy to a position where it would be a primary tool of revenue collection instead of its proper role as an incidental function of the Commissioner in collecting the revenues, its reason for challenging the legislative proposal cut to the core of the policy itself. In a position paper outlining its opposition[61] to the proposed statute, several reasons were proffered. First, the Department disagreed with the principal reason advanced for the need of such a policy: to produce more revenue. Justice saw no proof of that theory. Moreover, in its view racketeers and flagrant "tax dodgers" who deliberately concealed their fraud were hardly likely to experience a later change of heart and confess. Indeed, the opposite effect was seen as more probable: encouraged by the open invitation of a voluntary disclosure policy they would be encouraged to conceal until an investigation was believed to be imminent. Secondly, the Justice Department contended that a statutory reduction of punishment for income-tax evasion, that is, an "amnesty to income tax defaulters," would weaken the enforcement of criminal tax sanctions by permitting the tax evader to inject the collateral fact issue of voluntary disclosure into a criminal trial, thereby diverting attention from the main issue of willfulness of intent. Finally, in Justice's view such a statute would have a detrimental effect on honest taxpayers who would perceive their government as "begging" for its tax dollars, thus undermining the nation's voluntary assessment system.

This asserted protection of the "integrity of the tax laws"[62] lies at the heart of the opposition to the voluntary disclosure policy as a legitimate tool of enforcing the revenue laws. As stated by a vice-chairman of the Tax Section's Committee on Procedure in Fraud Cases, "... the voluntary disclosure policy is inconsistent with the role criminal sanctions are expected to fulfill in the tax system,"[63] and the Treasury Department's abandonment of the voluntary disclosure policy is a "re-evaluation of the role which the criminal provisions of the Internal Revenue Code are expected to fulfill."[64]

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[60] *Id.*

[61] See footnote 58.

[62] Lipton, 30 TAXES at page 361, quoting testimony of Richard C. Schwartz, assistant head of the Penal Division, at the King Subcommittee hearings.

[63] Lipton, 30 TAXES at page 361.

[64] *Id.*

In 1960, the Treasury Department finally concluded that it would not re-institute a voluntary disclosure at an administrative level.[65] Although voluntary disclosure as a formal policy or statutory mandate appears to be a dead issue at the present time, there lingers an informal policy of sorts. In August, 1959, then Commissioner of Internal Revenue Dana Latham stated:

> But in any event, it should be borne in mind that in determining whether or not an evader should be prosecuted, the existence of a true voluntary disclosure is an important element taken into consideration by Regional Counsel, Intelligence, and the Department of Justice. The Department of Justice has learned by what may be termed the 'hard way' that evidence of a truly penitent spirit weighs heavily with a jury. . . This does not mean that no evader who has made a voluntary disclosure will not be prosecuted. But it is, nevertheless, a very important element to be considered by you as practitioner. . . .[66]

Clearly, the existence of a voluntary disclousre will no longer formally be stated as the reason for not recommending prosecution, but the Internal Revenue Service, according to one commentator,[67] looks with favor on bona fide disclosures in failure to file cases (although not in cases involving the filing of a fraudulent return), and prosecution may, in fact, be averted by a timely disclosure.[68] Moreover, even where the IRS recommends prosecutions the Justice Department may decline on the ground that the making of a voluntary disclosure may negative the element of willfulness in the minds of the jurors.[69] The fact that one's fraud was disclosed to the IRS may also result in a lighter sen-

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[65] Balter, Tax Fraud and Evasion, (3rd Ed. 1963), Appendix, page 4.9.

[66] Crowley and Manning, "Representing the Taxpayer Before Trial," (PLI 1976), Section 4.2, page 90; also, Balter, *Tax Fraud and Evasion* (3rd Ed. 1963), Section 4.1, at page 4-1. It was also stated by then Commissioner Latham, in a letter to the Taxation Section on March 14, 1961:

> While our present policy does not guarantee immunity in return for disclosure we do not close our eyes to a true act of voluntary disclosure. Our current policy, which is similar to the way we operated from 1919 to 1945, provides that a true disclosure by a taxpayer of intentional evasion will be one of the factors taken into consideration, along with all the other facts and circumstances of the case, in deciding whether criminal prosecution should be recommended. I am sure you will agree that we are being realistic when we weigh the genuine repentance by the taxpayer as disclosed by a true disclosure against the chances for a conviction by a jury. In fact, this is the same consideration that is given by any prosecuting official or defense attorney to similar situations in any case when criminal action is contemplated.

Balter, *supra,* at page 4-12.

[67] Balter, *Tax Fraud and Evasion,* (4th Ed. 1976), Section 4.02, page 4-4.

[68] *Id.*

[69] *Id.* at Section 4.03, page 4-4.

tence after conviction.[70] Defense attorneys must weigh these factors in considering whether to advise their clients to make a voluntary disclosure.

The announcement of a formal voluntary disclosure policy appears to have been occasioned by the seriously overburdened enforcement activities of the then Bureau of Internal Revenue during the second world war. While its principal purpose was to aid the collection of revenue, its earlier genesis suggests perhaps that it should be viewed as the embodiment of a philosophy of tax administration that distinguishes tax evasion from other crimes, and that it is a policy consistent with a public benefit. It is arguable that the delineation of specific guidelines could have possibly rescued the voluntary disclosure policy from the serious administrative problems which arose after its formal announcement. Its abandonment was in large part attributable to the failure of the IRS to address these difficulties. At the same time the controversial nature of the policy called into question the role of criminal sanctions in the federal tax system. In a system of self-assessment which depended on the honesty of taxpayers, the voluntary disclosure appeared both fundamentally unfair and inconsistent with criminal enforcement activities. Perhaps widespread abuse of the voluntary disclosure policy was more illusory than real. Nevertheless, in the minds of many, the voluntary disclosure policy suggested an indifference to willful evasion. It is this inherent weakness in the policy, rather than administrative difficulties, which more probably sounded the death knell of the policy. In the opinion of the writer, it is not likely that it will be resurrected.

[70] *Id.* at Section 4.04, page 4-5. Balter provides the example of the case of *United States* v. *Szabo*, N.2-7203 (S.D. Cal. 1958), in which a taxpayer, after being contacted by a special agent, immediately began a review of his tax situation, hiring accountants and counsel. Within a few months he made a disclosure and filed amended returns, paying some additional $100,000 in taxes and interest. The District Court considered this a voluntary disclosure and fined the defendant only $50 on each of two counts.