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THE REVOCABILITY OF FEDERAL TAX ELECTIONS

EDWARD YORIO*

I. INTRODUCTION

EACH year every American individual income taxpayer faces a choice when he fills out his Form 1040: whether to elect the so-called standard deduction or to take the option of itemizing his personal deductions. Making this choice is relatively simple, for a taxpayer usually need only compare his allowable personal deductions to the amount of his standard deduction. If the total of his deductions exceeds the amount of the standard deduction, he will choose to itemize his deductions; otherwise, he will generally elect the standard deduction.

There are at least one hundred and sixty-seven other elections available to taxpayers under the Internal Revenue Code, but few are as simple or clear-cut as the standard deduction. Before a taxpayer makes a Code election, he should analyze at least three critical factors: (1) the tax effects of the election; (2) the method of making the election; and (3) the time period within which the election must be filed. Of these by far the most difficult is determining the tax consequences of a given election. One problem is that many elections affect an individual's tax situation for many years subsequent to the

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1. The taxpayer makes this election on line 45 of Internal Revenue Service Form 1040.
3. Id. § 63(a).
4. Since it is usually much simpler to elect the standard deduction, occasionally a taxpayer will elect the standard deduction even though it results in a higher tax simply to avoid the increased difficulty inherent in itemizing personal deductions.
5. In rare instances a taxpayer will choose to itemize even though his personal deductions are less than the standard deduction because certain tax credits are not available to a taxpayer who elects the standard deduction. The credit for income taxes imposed by foreign countries is probably the most important example. See Int. Rev. Code of 1954, §§ 33, 36.
7. The analysis in notes 1-5 supra and accompanying text on the standard deduction is an elementary example.
8. The literature on factors which are important in making elections under the Code is extensive. A few of the leading articles are Little, Saving Taxes by Proper Elections, 18 Tul. Tax Inst. 613 (1959); Meyer, Making and Rescinding Tax Accounting Elections, N.Y.U. 30th Inst. on Fed. Tax. 1691 (1972); Stine, Some Important Factors in Making Elections Under the Internal Revenue Code, 16 U. So. Cal. 1964 Tax Inst. 635.
year of the election. Consequently, whether or not to make the election will depend to some extent on the individual's projected future income flow. Some elections may be unwise because they preclude the taxpayer from securing other advantages under the Code. Occasionally the advisability of a tax election depends on economic conditions other than the taxpayer's own projected income flow; at other times an election will be advantageous only if tax rates remain constant. In short, to make a wise election a taxpayer must add to the skills of the tax expert the science of an economist and the prescience of a prophet.

A taxpayer must be very careful, too, that he conform to the prescribed method for making a Code election, since these methods vary considerably. Filing a return with one's spouse, for example, constitutes an election to file a joint return. Filling in the appropriate line on Form 1040 is an election between the standard deduction and itemized deductions. For some elections the taxpayer must file a special form; at other times he must attach a statement to his tax return. Equally important is that the taxpayer file his election on time. While many elections must be made at the time the taxpayer's return is filed, the requirements are by no means uniform. In some instances the Code itself specifies a time period for making the election; more commonly, regulations issued by the Internal Revenue

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9. An example is the choice between depreciating an asset on the straightline basis or on an accelerated basis. Int. Rev. Code of 1954, § 167(b).
10. See note 5 supra.
11. In National Lead Co. v. Commissioner, 336 F.2d 134 (2d Cir. 1964), cert. denied, 380 U.S. 908 (1965), the taxpayer made an election, the wisdom of which depended on rising zinc prices. Zinc prices fell, and the taxpayer sought and succeeded in revoking his election before the time period for the original election had expired. Id. at 137-38.
12. In Stewart v. United States, 100 F. Supp. 221 (D. Neb. 1951), the taxpayer's failure to elect to include an item in income for 1942 resulted in a considerable tax loss when the item had to be included in his 1943 income after federal income tax rates had risen steeply. Id. at 226.
15. See note 1 supra.
17. See, e.g., Treas. Reg. § 1.248-1(c) (1956) (election to amortize organizational expenses).
19. The elections to file a joint return, to take the standard deduction, and to depreciate on the straightline or on an accelerated basis are three of the most common examples.
20. See, e.g., Int. Rev. Code of 1954, § 333(d) (election must be made within 30 days after the adoption of a plan of liquidation of a corporation); id. § 1372(c)(1) (election to be taxed as a Subchapter S corporation must be made during the first month of the corporation's taxable year or during the month preceding).
Service prescribe the permissible period.\textsuperscript{21} Most laymen are ill-equipped to make an election, even if they are aware that it is available. Even with tax advice from an accountant or lawyer, often the wrong choice is made or the proper choice is made incorrectly.\textsuperscript{22} Given these obstacles, it would seem that relief should sometimes be given to a taxpayer who, by mistake or inadvertence, has made an unwise election. Yet prominent authority, including a Supreme Court\textsuperscript{23} case and a leading treatise,\textsuperscript{24} suggests that, with rare exceptions, an election once made will be binding. The aim of this Article is to determine under what circumstances a taxpayer should be allowed to revoke, to change or to make a late federal income tax election.\textsuperscript{25}

II. EARLY DEVELOPMENTS

With the ratification of the sixteenth amendment on February 25, 1913, and the enactment of the Revenue Act of 1913 a few months later,\textsuperscript{26} American courts faced for the first time the problem of interpreting a national individual income tax on a continuing basis.\textsuperscript{27} Faced with a statute without a case law tradition of its own, the courts

\begin{itemize}
\item \textsuperscript{21} See, e.g., Treas. Reg. § 1.446-1(e)(3)(i), T.D. 7073, 1970-2 Cum. Bull. 98, 100 (election to change method of accounting must be filed within 180 days after the beginning of the taxable year).
\item \textsuperscript{22} The instances of improper tax election advice from a lawyer or an accountant are legion. Some of the more egregious reported examples are: Youngblood v. United States, 388 F. Supp. 152 (W.D. Tex. 1974), aff'd per curiam, 507 F.2d 1263 (5th Cir. 1975) (installment election by agent valid though unknown to taxpayer); Kiesling v. United States, 171 F. Supp. 314 (S.D. Tex. 1958) (accountant's misadvice regarding community property; refiling permitted); see Mamula v. Commissioner, 346 F.2d 1016 (9th Cir. 1965) (taxpayer allowed to elect installment method under section 453 after an audit uncovered a mistake by a certified public accountant).
\item \textsuperscript{23} J.E. Riley Inv. Co. v. Commissioner, 311 U.S. 55 (1940). See notes 45-53 infra and accompanying text.
\item \textsuperscript{25} The Code itself makes some elections revocable for a certain period. See, e.g., Int. Rev. Code of 1954, § 901(a) (election to take foreign tax credit). Also, some sections authorize the Secretary to prescribe regulations governing a change of election. See, e.g., id. § 144(b); Treas. Reg. § 1.144-2(a), T.D. 6792, 1965-1 Cum. Bull. 69, 85 (election to take standard deduction). The Service has issued rulings authorizing taxpayers to revoke an election or to make a late election. See, e.g., Rev. Rul. 65-297, 1965-2 Cum. Bull. 152. The Commissioner can give advance approval to a taxpayer wishing to revoke even without an authorizing Code section, regulation, or ruling. See Stine, Some Important Factors in Making Elections Under the Internal Revenue Code, 16 U. So. Cal. 1964 Tax Inst. 635, 645.
\item \textsuperscript{26} This Article will focus on cases involving revocations which the Service resists, and for which the taxpayer can find no explicit authority in either the Code, regulations, or rulings.
\item \textsuperscript{27} Act of Oct. 3, 1913, ch. 16, 38 Stat. 114.
\item \textsuperscript{28} While the Civil War income tax first enacted in 1862 continued in effect until 1873, Congress repeatedly reduced its incidence. E. Seligman, The Income Tax 430-81 (1914). The 1894 tax was found unconstitutional soon after its effective date. Pollock v. Farmers' Loan & Trust Co., 158 U.S. 601 (1895).
\end{itemize}
sometimes borrowed precedents from older areas of the law, and in the interpretation of income tax elections this conscious borrowing was common. In an early decision, *McIntosh v. Wilkinson*, in which a taxpayer had sought to revoke an income tax election made by mistake, the court assumed that the governing rules for elections under the income tax were the same as the principles developed for elections in the courts of equity. One important authority for the court, therefore, was Pomeroy's treatise on equity which states that an election in equity is revocable when the election has been made under mistake of fact.

Other courts, following the lead of *McIntosh*, have held that an election was revocable only if made under a mistake of fact and that a mistake of law would not suffice. A simple example illustrating this dichotomy might involve the standard deduction. A taxpayer adds up his personal deductions, but forgets that he has made a substantial charitable contribution to his local church. As a consequence, he elects the standard deduction. This election, grounded on a mistake of fact, would be revocable. By contrast, if the taxpayer failed to add the contribution in the belief that charitable contributions were not deductible, his election would not be revocable since his mistake was an improper interpretation of the law.

It is hard to understand why the taxpayer's mistake of fact in the above example would allow him to revoke his election, but his mistake of law would not. While an occasional court has questioned the wisdom of the dichotomy, courts still refuse to permit a taxpayer to revoke an election for a mistake of law. Neither *McIntosh* nor any

28. See Ross v. Commissioner, 169 F.2d 483 (1st Cir. 1948) (on equitable principles, unpaid salary held to constitute constructive receipt, not taxable in later year); Bennet v. Helvering, 137 F.2d 537 (2d Cir. 1943) (on equitable principles, failure to declare an item as income in prior year found not to prevent allowance of loss on same item as deduction in later year).

29. 36 F.2d 807 (E.D. Wis. 1929).


32. It should be noted that, since an election of the standard deduction is revocable pursuant to Treas. Reg. § 1.144-2(a), T.D. 6792, 1965-1 Cum. Bull. 69, 85, this example has more academic than practical interest.

33. Richardson v. Commissioner, 126 F.2d 562, 569-70 (2d Cir. 1942). See Clift & Goodrich, Inc. v. United States, 56 F.2d 751, 752 (2d Cir.) (L. Hand, J.), cert. denied, 287 U.S. 617 (1932) ("[T]he old notion that a mistake of law will not serve . . . still prolongs its discreditable life . . . . ").

34. Estate of Darby v. Wiseman, 323 F.2d 792 (10th Cir. 1963); Raymond v. United States, 269 F.2d 181, 183 (6th Cir. 1959); Rosenfield v. United States, 254 F.2d 940 (3d Cir.), cert. denied, 358 U.S. 833 (1958); Aaron Cohen, 63 T.C. No. 49 (Feb. 3, 1975). It should be pointed out that the McIntosh case itself arguably involved a mistake of law, in that the taxpayer's
other decision has explained why mistakes of fact are accorded preferential treatment. Since there is no satisfactory policy reason for the distinction, and since the Supreme Court has never adopted the language of *McIntosh*, it is time for courts to drop the distinction.

Some other early decisions pursued a different and much more generous course. These courts adopted the view that a relief provision enacted by Congress should be liberally construed in favor of the taxpayer. Thus, revocation of a mistaken election was permitted whenever the election provision had been enacted to provide relief to the taxpayer. The Supreme Court, in *Pacific National Co. v. Welch* and *J.E. Riley Investment Co. v. Commissioner*, rejected this argument. Since every election is arguably a relief provision enacted by Congress for the taxpayer's benefit, to allow a taxpayer freely to revoke an election for that reason alone would "impose burdensome uncertainties upon the administration of the revenue laws."1

Other courts went too far in the opposite direction, reasoning that since an election is afforded as a matter of legislative grace the taxpayer must comply strictly with its requirements. Thus, an election once made should be binding once and forever. Given the uncertainties and difficulties in making many elections, it would be Draconian to hold taxpayers to such high standards. Many elections would become traps for the unwary and only those taxpayers with the best tax advice would be secure.

In addition, simply because Congress is not required to offer an election, it does not necessarily follow that an election, once enacted, should be construed strictly against the taxpayer. If Congress, with the power to decide tax policy, adopts a certain election, it would be

original imprudent election resulted from his acceptance of incorrect tax advice from an agent of the Internal Revenue Service.

35. The Supreme Court cases are *J.E. Riley Inv. Co. v. Commissioner*, 311 U.S. 55 (1940), *Haggar Co. v. Helvering*, 308 U.S. 389 (1940), and *Pacific Nat'l Co. v. Welch*, 304 U.S. 191 (1938), none of which alludes to the mistake of fact-law dichotomy.
37. *304 U.S. 191 (1938).*
41. See notes 6-21 supra and accompanying text.
42. This argument recalls the adage that deductions, as manifestations of congressional beneficence, are to be strictly construed against the taxpayer. In the context of deductions this view has been persuasively criticized. Note, *An Argument Against the Doctrine that Deductions Should Be Narrowly Construed As a Matter of Legislative Grace*, 56 Harv. L. Rev. 1142, 1146-47 (1943).
more reasonable for a court to allow a taxpayer to retract a mistaken election whenever his mistake thwarts the policy behind the election so long as a retraction would do no violence to any other important tax policy.\footnote{43}

The preceding discussion should show that early court decisions on the revocability of tax elections went astray in two respects. In some instances courts relied on established equitable principles which could not thrive as transplants in the field of income taxation. In other cases courts mistakenly tried to formulate a general rule to cover all cases, and in an area as complex and diverse as tax elections, a broad-brush approach had to fail.

The failure of the lower courts in these early decisions to resolve the problems arising from mistaken elections resulted in Supreme Court intervention. The last of these Supreme Court opinions,\footnote{44} \textit{J.E. Riley Investment Co. v. Commissioner},\footnote{45} represents the high-water mark of opposition to taxpayer attempts to revoke an election or to make a late election. The taxpayer was a corporation engaged in mining in Flat, Alaska. Because the winter mail service between Flat and Tacoma was uncertain and slow, the taxpayer customarily filed its tax returns early on a form for an earlier year in order to avoid a delinquency assessment. On January 2, 1935, the taxpayer executed his return for calendar year 1934 on a 1933 form. At that time the taxpayer was unaware of the provision in the 1934 Revenue Act allowing percentage depletion and, since the taxpayer had no basis for cost depletion, it did not deduct any depletion for calendar year 1934. About eight months later the taxpayer first learned of the statutory provision for percentage depletion, and some months thereafter it filed an amended return upon which a deduction for percentage depletion was taken and a refund was claimed.\footnote{46} The Commissioner refused to accept the amended return and the Supreme Court upheld the Commissioner's ruling.

The Court gave two reasons to support its holding, one based on the statute, the other on administrative policy. The 1934 Revenue Act read, in relevant part, as follows:

\begin{quote}
A taxpayer making his first return under this title in respect of a property shall state whether he elects to have the depletion allowance for such property for the taxable year for which the return is made computed with or without regard to percentage depletion . . . . If the taxpayer fails to make such statement in the return, the depletion
\end{quote}

\footnote{43} "The Legislature has the power to decide what the policy of the law shall be, and if it has intimated its will, however indirectly, that will should be recognized and obeyed." \textit{Johnson v. United States}, 163 F. 30, 32 (1st Cir. 1908) (Holmes, J.) (construing federal evidence statute).

\footnote{44} See note 35 supra.

\footnote{45} 311 U.S. 55 (1940).

\footnote{46} Id. at 56-57.
allowance for such property for such year shall be computed without reference to percentage depletion.\textsuperscript{47}

The Supreme Court concluded that the taxpayer's return executed on January 2, 1935 was its "first return" within the meaning of the statute. Since the taxpayer had not elected percentage depletion on that return, it was barred from computing depletion on that basis in its amended return filed on March 3, 1936.\textsuperscript{48} This interpretation is not an unreasonable reading of the statute although less than one year earlier the Supreme Court had itself expanded the meaning of "first return" to embrace an amended return which was filed before the original period for filing a return had elapsed.\textsuperscript{49} Considering the plight of the taxpayer in \textit{Riley}, the Court could have easily gone one step further to include within the definition of "first return" an amended return filed within the statutory limitation period of three years.

The Court also offered a policy reason to support its holding:

If petitioner's view were adopted, taxpayers with the benefit of hindsight could shift from one basis of depletion to another in light of developments subsequent to their original choice. It seems clear that Congress provided that the election must be made once and for all in the first return in order to avoid any such shifts.\textsuperscript{50}

Although it is true that as a general rule taxpayers should not be allowed to change tax elections with the benefit of hindsight,\textsuperscript{51} the taxpayer in \textit{Riley} was clearly not shifting to percentage depletion for such a reason. Since at the time he filed his original return he had no basis on which to deduct cost depletion, his only sensible choice, if he had known about the new provision, would have been percentage depletion. The Court offered a convincing reason for not allowing a revocation in certain cases, but it was a reason which was inapposite to the case before it.

Many subsequent lower court opinions have cited \textit{Riley} for the proposition that an election once made is irrevocable.\textsuperscript{52} It is submitted that the reasoning of the Court in \textit{Riley} was incorrect except for its arguably sound statutory interpretation. In any event, since the Supreme Court has not reviewed this issue in thirty-five years, the \textit{Riley} case should not be taken as a talisman.\textsuperscript{53}

\textsuperscript{48} 311 U.S. at 57-59.
\textsuperscript{49} Haggar Co. v. Helvering, 308 U.S. 389 (1940).
\textsuperscript{50} 311 U.S. at 59.
\textsuperscript{51} See notes 145-51 infra and accompanying text.
\textsuperscript{52} See, e.g., Estate of Darby v. Wiseman, 323 F.2d 792, 794 (10th Cir. 1963); Keeler v. Commissioner, 180 F.2d 707, 710 (10th Cir. 1950); Schall & Co. v. United States, 129 F. Supp. 137, 140 (S.D.N.Y. 1954).
\textsuperscript{53} In addition, since the Court in \textit{Riley} relied on the peculiar language of the Revenue Act of 1934, any later case may be distinguished from it.
III. SOME PRELIMINARY MATTERS

A. Burden of Proof

Many courts place the burden of proving certain issues on the taxpayer seeking to revoke a tax election.54 Usually the taxpayer must establish: (1) that the election (or failure to make an election) was the result of a mistake;55 and (2) that the mistake was a mistake at the time of the election.56 Placing the burden of proof on the taxpayer seems reasonable since the taxpayer, having had his chance and muffed it, is asking the court to allow him to repudiate it and to upset the normal workings of tax administration. Since "the idea of repose in tax matters is genuinely important,"57 the taxpayer should be required to present a convincing case before a court tampers with the status quo.

B. The Statute of Limitations

For the same reasons that statutes of limitations have been enacted to bar actions after a particular time,58 there should be a limitation period after which a taxpayer will not be allowed to revoke an election no matter how compelling his case. The usual limitation period for claiming a refund or credit under the federal income tax is three years,59 and a similar period might be appropriate for revoking a tax election. While one authority60 has argued that in cases of mistake the statute of limitations should be tolled until the taxpayer discovers or should discover his mistake,61 the Service would have a persuasive

54. See, e.g., Estate of George Stamos, 55 T.C. 468 (1970) (taxpayer failed to prove that he had made a mistake of fact); Sam Goldman, 9 CCH Tax Ct. Mem. 936 (1950) (taxpayer failed to offer evidence of his own intent when making an election).
55. Occasionally a taxpayer makes an election the wisdom of which depends on an optimistic view of the tax effect of an unrelated transaction in the hope that his election may be revoked if his view is found to be incorrect. Such conduct is not entirely innocent and perhaps is not even a mistake. It is unclear whether the taxpayer should be entitled to relief. See notes 143-44 infra and accompanying text.
56. An election which turns out to be ill-advised because of subsequent events should not be revocable. See notes 145-51 infra and accompanying text.
61. Id. The authors rely on the apparent old rule that when money is paid under mistake the statute of limitations begins to run when the claimant discovered or should have discovered the mistake. See J. Lightwood, The Time Limit for Actions 239 (1909). Some modern statutes reject this rule. See, e.g., N.Y. C.P.L.R. § 213(6) (McKinney 1972). The Internal Revenue Code itself generally rejects this approach. Int. Rev. Code of 1954, § 6511.
argument for a more stringent rule since a change in a tax election could affect the returns and tax liability of a taxpayer for many years.\textsuperscript{62} To protect the Service against delayed revocations which could severely burden tax administration, a limitation period of three years from the date the election is made might be advisable.\textsuperscript{63}

Congressional action would be necessary to establish an absolute statute of limitations for revocations, but even without a statute, courts have imposed their own informal limitation period. Some courts have denied relief to taxpayers whose revocations were filed too late\textsuperscript{64} and one court distinguished an earlier pro-taxpayer decision by pointing out that in the earlier case, the taxpayer revoked within one year after his original election, while in the case before the court, the taxpayer's attempt to revoke came more than four years after his election.\textsuperscript{65} Even in the absence of congressional action, therefore, courts should weigh the timeliness of a revocation in deciding whether to grant relief to the taxpayer.

C. Revocations Within the Time Period for the Election

The converse of a delayed revocation is a revocation made before the period for the original election has elapsed. \textit{National Lead Co. v. Commissioner}\textsuperscript{66} involved an election provision which gave taxpayers a one year period to select between inventory methods. The taxpayer filed his election, but sought to revoke the election before the expiration of the one year period. The Second Circuit, reversing the Tax Court, held in favor of the taxpayer on the grounds that the government would in no way be prejudiced by a revocation before the end of the election period.\textsuperscript{67}

This holding is no doubt sound since a different result would trap those unwary taxpayers who make elections too soon, while the response of the wise taxpayer would be simply to wait until the latest possible moment before committing himself to an election. One Supreme Court decision supports this result.\textsuperscript{68} Though the argument of

\textsuperscript{62} See note 9 supra.

\textsuperscript{63} At least one supporter of a more liberal revocation policy in general is willing to accept a three year limitation period. Stine, Some Important Factors in Making Elections Under the Internal Revenue Code, 16 U. So. Cal. 1964 Tax Inst. 635, 655.

\textsuperscript{64} See, e.g., Momsen-DunneGAN-Ryan Co. v. Helvering, 68 F.2d 754, 755 (D.C. Cir. 1933).


\textsuperscript{66} 336 F.2d 134 (2d Cir. 1964), cert. denied, 380 U.S. 908 (1965), rev'g 40 T.C. 282 (1963).

\textsuperscript{67} Id. at 139.

\textsuperscript{68} Haggar Co. v. Helvering, 308 U.S. 389 (1940). The revocation in McIntosh v. Wilkinson,
the Court turned mainly on a narrow point of statutory interpretation, the Court did emphasize the policy argument that "no interest of the Government would have been harmed had the Commissioner . . . accepted the petitioner's amended declaration." If the government allows a certain time for making an election, it is unlikely that any interest of tax administration would be hurt by allowing a retraction of the election within that same time period.

IV. SITUATIONS IN WHICH COURTS FAVOR THE TAXPAYER

A. Scrivener's Errors and the Like

Occasionally a taxpayer intending to make one election mistakenly fills in the opposite on his return. If the taxpayer's calculations on the same return indicate his actual intent, a court will allow the taxpayer to correct his return. Even when the return itself does not reveal the error, a court should allow a taxpayer to change his election if he can prove that he (or his agent) filled out the return incorrectly.

A bit more difficult are those cases in which a taxpayer deliberately elects one alternative, but calculations on the same return or on a later return indicate that he misunderstood the effect of the election. In Rosenfield v. United States, an attorney incorrectly advised an executor that the election of the optional valuation date for estate tax purposes allowed the estate to value each asset at the date of death value or on the alternate valuation date, whichever was lower. Based on this advice the estate elected the optional valuation date valuing the assets as the lawyer had instructed. When the Service assessed a deficiency against the estate, the executor sought to revoke the election and to value all the estate's assets as of the date of death.

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36 F.2d 807 (E.D. Wis. 1929), also occurred before the expiration of the election period, but the court apparently did not rely on that fact in finding for the taxpayer. See notes 29-30 supra and accompanying text.

69. 308 U.S. at 394-95.
71. Closely analogous are those cases in contract in which courts, by reforming a written instrument which contains a scrivener's error, enforce the contract in accordance with the parties' actual intent. See 3 A. Corbin, Contracts § 614 (1960); 13 S. Williston, Contracts §§ 1547-49A (3d ed. W. Jaeger 1970).
73. Election of the alternate valuation date generally allows an estate to value all of its assets as of that date; the election does not give the estate a choice of valuation dates for each asset. Int. Rev. Code of 1954, § 2032.
74. The executor also argued that since the alternate valuation date had been applied to only
The Third Circuit affirmed the decision of the lower court, which stated that once "an election has been made, it cannot be revoked to secure tax advantages after the time for filing the tax return has passed."

The lower court's argument is puzzling, for it seems to confuse the executor's dilemma with those very different situations in which taxpayers try to revoke elections when subsequent non-tax events make the elections disadvantageous. The court is quite right that taxpayers should not be allowed to revoke elections on the basis of hindsight, but in Rosenfield hindsight could not have been a factor in the revocation because the executor, had he understood the election, would have known at that time everything he needed to know to make the more advantageous choice. The executor was therefore motivated to revoke not by a view of events subsequent to his election, but simply because of his misconstruction of the effects of the original election. The Rosenfield opinion might make some sense, however, if the court really suspected that the executor deliberately misread the statute and, when the Service caught the discrepancy, wanted to revoke. But if a taxpayer's treatment of an election on his return indicates that he misunderstood the election, and the taxpayer proves a portion of the assets of the estate (the favorable portion), this action, since it was contrary to the statute, was not a true election. The executor urged, therefore, that the date of death values must be used. 156 F. Supp. at 782. The district court rejected the argument: "In the present case the decision of the estate upon the advice of counsel to elect the optional valuation was an unwise decision, but certainly it was a real decision and the election of the optional valuation date was a real election."

The taxpayer's argument finds some support in the field of remedies. Where a plaintiff sues for an unavailable remedy and is denied relief on that basis, some authorities argue that his "election" of a remedy that is not available is not an election at all and, for that reason, he should not be barred from suing for another remedy. See Restatement of Judgments § 65, Comment a (1942); D. Dobbs, Remedies § 1.5, at 20 (1973). However, this technical approach should not be adopted in income tax cases where there are often substantial policy reasons for allowing (or refusing to allow) a taxpayer to change his "election."

The taxpayer's example might be a taxpayer who elects straightline depreciation. If he later determines that his gross income is higher than expected, he might want to shift to accelerated depreciation to offset that income.

At the time of the election (which was subsequent to the alternate valuation date) the taxpayer could have determined the value of the estate's assets both as of the date of death and as of the alternate valuation date. That was the only information he required to minimize the estate tax, though the income tax effects of later sales might vary with the valuation date.

There is no indication that this was the case. Indeed, the lower court clearly accepted the taxpayer's version of the events leading to his election. 156 F. Supp. at 782.

The burden of proof becomes crucial. The mere fact that the taxpayer's calculations are inconsistent with his election may not in itself be sufficient to prove that the misinterpretation was innocent. See notes 54-57 supra and accompanying text.
that his apparent misunderstanding was real, he should be allowed to revoke.

B. Mistakes Caused by Advice from a Government Officer or Agent

Two relatively early cases\(^\text{81}\) involved taxpayers who alleged that their mistaken elections were caused by incorrect legal advice from an employee of the Internal Revenue Service. As already noted,\(^\text{82}\) the court in McIntosh held for the taxpayer primarily on the grounds that a similar mistaken election would have been revocable in a court of equity. The court apparently did not rely on the agent’s misinformation in deciding against the government, though it is conceivable that the court weighed this fact in the taxpayer’s favor. In John D. Biggers,\(^\text{83}\) the Board of Tax Appeals held against the taxpayer, over a strong dissent, for three principal reasons: (1) his mistake was a mistake of law which supposedly does not excuse an incorrect election;\(^\text{84}\) (2) a taxpayer cannot succeed in a suit against the government by relying on the advice of a government agent;\(^\text{85}\) and (3) representations made by an agent of the Service are not binding against the government.\(^\text{86}\)

The Board’s second argument seems to be an evidentiary one, for the court emphasized that “[n]either the official status of the person advising petitioner, nor that of his consultants, is disclosed.”\(^\text{87}\) To be sure, if a taxpayer simply alleges that an agent gave him bad advice, but offers no evidence as to the identity of the agent nor presents any other proof that he had in fact received incorrect advice from the Service, his claim should be dismissed unless he presents some other facts to support his revocation. Again, the burden of proof is critical.\(^\text{88}\) A court should demand that the taxpayer present evidence not only that a specific agent advised him incorrectly, but that he relied on the advice in making his election.

Let us assume, however, that the taxpayer establishes that an agent gave him an incorrect opinion on which he relied to his detriment. This raises the court’s third argument that representations of a government agent do not bind the government, and that as a “general rule . . . estoppel can not apply against the Government . . . .”\(^\text{89}\) It is

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82. See notes 29-30 supra and accompanying text.
83. 39 B.T.A. 480 (1939).
84. See notes 29-35 supra and accompanying text.
85. 39 B.T.A. at 486.
86. Id.
87. Id.
88. See notes 54-57 supra and accompanying text.
89. 39 B.T.A. at 486.
true that many cases hold that the government may not be estopped by the acts of its agents. The rationale for the rule is that each agent, as but one of thousands representing the government, has limited power. Where conflicts of opinion between various agents are common, it would be illogical for each to be able to bind the government.

On the other hand, some cases present strong equitable arguments for the taxpayer. In Biggers, the taxpayer alleged that he was told by an agent that he could not file separate returns, but had to file jointly with his wife. Wishing to comply, the taxpayer filed a joint return. Later, realizing the agent's mistake, he tried to revoke and file separately as he was originally entitled to do. It is submitted that under these facts a court ought to allow the taxpayer to revoke his original election for reasons of fairness without, however, adopting a general rule that the government may be estopped by the acts of its agents.

Other situations may be less compelling for the taxpayer. Suppose in the Biggers situation, for example, that the agent advises the taxpayer (correctly) that he could file either a joint return or a separate return, but (incorrectly) that a joint return would result in less tax. The taxpayer who files a joint return unwisely has a less persuasive claim to relief, for no longer can he argue that the agent's advice left him no choice, but only that the advice induced him to make the wrong choice. The taxpayer has not been coerced into a mistake; he has only been coaxed into it, and that may be a crucial distinction for a court balancing the equities of his case. Yet, since the taxpayer's tax loss is no less real, a court might allow him to revoke anyway.

C. When an Election Appears To Be Unavailable or Inconsequential

Occasionally a taxpayer will file his tax return without making an election because under his view of the facts or the law an election is unavailable or inconsequential. Since the regulations provide in some situations that failure to elect precludes election at a later date without the Commissioner's consent, the consequences of such failure can be disastrous.


91. For an excellent discussion of estoppel as it relates to federal tax controversies see Maguire & Zimet, supra note 57, at 1293-1318.

92. See notes 155-62 infra and accompanying text.

When, however, the taxpayer's failure to make an election results from ignorance that an election is available, the taxpayer has a strong claim for amending his return. In an early case, a corporate taxpayer had apparently sold a subsidiary corporation to a third party reporting its income for three years on a separate basis. When a court later determined that the sale of a subsidiary was ineffective, the taxpayer moved to revoke its separate returns and to file on a consolidated basis with the subsidiary for the three years during which the taxpayer had thought it no longer owned the subsidiary. The Commissioner resisted the taxpayer's amendment on the basis of the 1921 Revenue Act, which provided that a taxpayer who filed on a separate basis for any year was precluded from amending his return to file on a consolidated basis for that year.

The court held for the taxpayer. Since the taxpayer did not know that it still owned the subsidiary, the court reasoned that its initial separate returns did not constitute an election against filing on a consolidated basis. Despite the holding of J.E. Riley Investment Co. v. Commissioner, it is unfair to bind a taxpayer to an unconscious election when, under his view of the facts or law, no election was available.

A more complicated problem arises when the taxpayer is aware that he has an election, but thinks the election is inconsequential because he has no taxable income for the year of the election. As a result he may neglect to make the required election or he may make a hastily considered election which proves to be unwise. The response of the courts to a subsequent attempt by the taxpayer to make the proper election has sometimes been unfavorable, but more often has been generous to the taxpayer. The language of one opinion is fairly typical:

96. 23 B.T.A. at 235-36.
98. In Richardson v. Commissioner, 126 F.2d 562 (2d Cir. 1942), a taxpayer failed to take a specific gift exemption because he did not know that a certain transfer constituted a gift. He was allowed to amend his gift tax return and claim the exemption after the Commissioner successfully characterized the transfer as a gift. The court rejected the Commissioner's argument that a mistake of law would not serve to excuse the taxpayer. Id. at 569. See notes 29-35 supra and accompanying text.
99. This is another ground for criticizing the holding against the taxpayer in John D. Biggers, 39 B.T.A. 480 (1939). See notes 83-85 supra and accompanying text.
Where no tax is assessed and none assessable, no matter how the expenses be treated, and where the initial return is filed upon incomplete knowledge of the material facts . . . it seems to us that the initial return may properly be regarded as tentative in its nature, and as not constituting an election.102

This reasoning overlooks the fact that an election may have important tax ramifications for years before and after the election is made. Consider, for example, this common factual situation:103 a taxpayer incurs research and experimental costs in a given taxable year which under the Code he may deduct entirely in that year or amortize and deduct over a five year (or greater) period.104 Since he has no taxable income for the year, he believes that an election for that year is unnecessary and hence he makes none. But whether he elects to deduct or to amortize the expenses may have a profound effect on his tax liability for later or earlier tax years. If he deducts the costs, he will have a net operating loss in the year of the deduction which, subject to limitations of section 172,105 may be carried back to offset income in earlier years or may be carried forward to offset income in later years. If, on the other hand, he amortizes the costs, only a ratable part of the expenses will be deductible in the first year, resulting in a much smaller net operating loss for that year. The remainder (and bulk) of the expenses, however, will be deductible over the amortization period. Depending on the choice he makes the tax consequences for subsequent years may be considerably different.106

If the taxpayer was unaware of the importance of the election when he made his choice (or had his choice made for him by default), it is understandable that a court would want to rescue him from an unwise election or from an election by default. But a court should hesitate to grant relief after the due date of the original election because the taxpayer's choice becomes much easier if he can make the election knowing his taxable income for subsequent years.107 Hence, a court

are Pittston-Duryea Coal Co. v. Commissioner, 117 F.2d 436 (3d Cir. 1941), and Kehoe-Berge Coal Co. v. Commissioner, 117 F.2d 439 (3d Cir. 1941). In the former the court held for the taxpayer specifically because he had no taxable income and an election was, according to the court, meaningless; in the latter the court held against the taxpayer because he had taxable income.

103. Both Lucas v. Sterling Oil & Gas Co., 62 F.2d 951 (6th Cir. 1933) and Estate of Richard R. Wilbur, 43 T.C. 322 (1964) involved tax situations similar to this example.
105. Id. § 172. Generally a taxpayer may carry back a net operating loss to each of the three preceding taxable years and may carry forward a net operating loss to each of the five succeeding taxable years. Id. § 172(b).
106. At least one court has lucidly analyzed the importance of such seemingly meaningless tax elections. Estate of Richard R. Wilbur, 43 T.C. 322, 330 (1964).
107. In the example under discussion if the taxpayer's income is high for the years im-
which allows a subsequent election or permits a change in a prior
election may be shifting the risk of his future income flow from the
taxpayer to the government. In the ordinary case this risk is on the
taxpayer. There seems to be no reason to shift the risk to the
government simply because the taxpayer regarded the election as
meaningless.

A similar argument for denying relief could be made in the case of a
taxpayer whose failure to elect is due to ignorance that an election is
available. Here again the taxpayer who is allowed to elect late has the
benefit of hindsight. Yet courts allow such late elections on the ground
that it is unfair to penalize a taxpayer for failing to make an election if
he was not aware that he had a right to make an election.\textsuperscript{108} When,
however, the taxpayer knows he has an election and still ignores it, his
claim to relief is less convincing, though even here, a compromise
solution allowing the taxpayer to make a late election might be
appropriate. This would allow the taxpayer to make a late election if
he can prove that he would have made the same choice on his original
return, had he realized the importance of making an election at that
time.\textsuperscript{109} But a court should not allow a late election if the taxpayer's
choice is motivated by later events which he could not know of at the
time of the original election. There is no reason to give the taxpayer
who neglects an election an advantage over the taxpayer who elects on
time and at the risk of future events.

V. SITUATIONS IN WHICH COURTS DO NOT FAVOR
THE TAXPAYER

A. Penalty for Failing to File a Return on Time

Occasionally, courts have refused to allow a taxpayer to make an
election when the taxpayer's return on which the election would
normally be due was not filed until after the filing time specified in the
Code.\textsuperscript{110} The motive of the courts seems to be to punish taxpayers
who fail to file their tax returns on time:

\addcontentsline{toc}{section}{V. SITUATIONS IN WHICH COURTS DO NOT FAVOR THE TAXPAYER}
[T]axpayers voluntarily filing returns and making timely election are bound by their choice. To allow a choice where the taxpayer sits supinely by until by the diligence of the Government it is discovered that a tax is due would put a premium on inertia that certainly is not within the spirit of our system of taxation. If any class of taxpayers is entitled to claim a preference, it consists of those who have complied with the statute.111

There are a number of answers to this argument. First, one major premise of the court's reasoning is clearly unsound since courts do in fact allow taxpayers on occasion to revoke elections made on a timely filed return.112 It would not necessarily be inconsistent or unfair to allow a taxpayer who failed to file a timely return to make a late election. Second, the Internal Revenue Code imposes a penalty for failing to file a return on time113 and it is arguable that courts should not impose an additional judicial penalty by refusing to allow a taxpayer to make an election which he is entitled to make simply because he has filed his return after the due date.

Certain sections of the Code and the regulations impose a time limit for making elections. Under section 248 of the Code, for example, the taxpayer must elect the benefits of that section "not later than the time prescribed by law for filing the return for such taxable year . . . ."114 Similarly, under Treasury Regulation 1.453-8(a)(1), the taxpayer must elect the installment method "on an income tax return for the taxable year of the election, filed on or before the time specified . . . for filing such return."115 In cases where such a refusal by the Service to accept an election on a late return has firm statutory or regulatory116 support, a court should not upset the Service's decision.

But other cases are more promising for the taxpayer. Consider, for example, a taxpayer who files a late return on which he wishes to elect an accelerated depreciation method for a certain asset.117 Such an election should be made on the return for the first taxable year for

111. Sarah Briarly, 29 B.T.A. 256, 259 (1933).
112. See notes 70-71, 94-96 & 101 supra and accompanying text.
114. Id. § 248(c). See note 20 supra.
which the taxpayer claims a depreciation deduction for the asset. However, since neither the Code nor the regulations specifies that a taxpayer must make his election on a return which is duly filed, the taxpayer's election on a late return ordinarily should be accepted by the Service or, if the Service refuses, by a court. As with other late elections, however, the taxpayer who wishes to file an election on a late return must demonstrate that he would have made the same choice had he filed his return on time, and that his choice of a particular alternative is not due to subsequent events.

B. Revocations in Response to an Audit by the Internal Revenue Service

When a taxpayer makes an election under the Code, his choice is often determined by his opinion of the tax consequences of transactions entirely distinct from the one involving the election. If the Internal Revenue Service upon audit succeeds in attacking the taxpayer's opinion of these other transactions, the taxpayer's election may turn out to be disastrous. The question then arises as to whether the taxpayer may revoke or change his election in response to the changes in his tax situation caused by the audit.

The courts have generally been antagonistic to taxpayer revocations in response to tax audits. Some courts base their refusal to allow a

118. Failure to adopt an accelerated method of depreciation mandates the use of the straightline method. Treas. Reg. § 1.167(b)-1(a) (1956).
120. See note 152 infra and accompanying text.
121. An example is the election by a shareholder to be taxed in a liquidation under section 333 of the Code, which provides generally that a shareholder does not recognize gain on a liquidation pursuant to that section. Int. Rev. Code of 1954, § 333(a). Under section 333(e), however, if the corporation has earnings and profits at the time of the liquidation, a non-corporate shareholder will be taxed on his ratable share of such earnings and profits as a dividend, i.e., as ordinary income. Id. §§ 333(e), 301(c)(1). Since gain on a liquidation is ordinarily capital gain, see § 331(a)(1), the shareholder would be badly advised to elect section 333 if the corporation has considerable earnings and profits, since the election would simply convert capital gain to ordinary income. See B. Bittker & J. Eustice, Federal Income Taxation of Corporations and Shareholders, ¶¶ 11.20-.24 (3d ed. 1971) [hereinafter cited as Bittker & Eustice]. Often the shareholder elects section 333 believing that the corporation has little if any earnings and profits, a belief which the IRS may prove erroneous on audit. The question then becomes whether the taxpayer may revoke his section 333 election and be taxed under the normal rules for corporate liquidations.
122. Of the eleven cases which squarely present this question, three went in favor of the
revocation on the traditional mistake of fact and mistake of law dichotomy, but this distinction is no more satisfactory a ground for deciding these specific cases than it is for deciding revocation cases generally. Other courts rely on either of two leading Supreme Court opinions disallowing revocations, but neither of these Supreme Court cases involved a taxpayer who was seeking to revoke an election in response to a tax audit. At least one court has denied relief to the taxpayer on the grounds that the attempted revocation was the result of hindsight which "cannot... destroy the binding effect of an election..." This too misses the mark, for the type of hindsight which should preclude a taxpayer from revoking an election is a knowledge of non-tax events which subsequently make the election less favorable than the taxpayer thought at the time of his election. It is the risk of future non-tax events which the taxpayer assumes when he makes an election, not the risk that he misconstrued the tax effect of transactions already completed at the time of his election.

Perhaps the most common argument raised against the taxpayer is that problems of tax administration would increase considerably if, in response to an audit, a taxpayer could revoke an election which was already examined as one part of the audit. Although problems of tax administration increase somewhat whenever a taxpayer is allowed to change an election, it is hard to see how the presence of a tax audit makes administration any more difficult. In fact, while the taxpayer's entire return is subject to scrutiny, it would be convenient for both the taxpayer and the Service to make changes in the return, including a

taxpayer; eight against him. For the taxpayer: Manula v. Commissioner, 346 F.2d 1016 (9th Cir. 1965); Meyer's Estate v. Commissioner, 200 F.2d 592 (5th Cir. 1952); Gentsch v. Goodyear Tire & Rubber Co., 151 F.2d 997 (6th Cir. 1945). Against the taxpayer: Estate of Darby v. Wiseman, 323 F.2d 792 (10th Cir. 1963); Raymond v. United States, 269 F.2d 181 (6th Cir. 1959); Jacobs v. Commissioner, 224 F.2d 412 (9th Cir. 1955); Aaron Cohen, 63 T.C. No. 49 (Feb. 3, 1975); Estate of George Stamos, 55 T.C. 468 (1970); Estate of Richard R. Wilbur, 43 T.C. 322 (1964); M. Pauline Casey, 38 T.C. 357 (1962); Frank T. Shull, 30 T.C. 821 (1958), vacated and remanded on other grounds, 271 F.2d 447 (4th Cir. 1959).

123. Estate of Darby v. Wiseman, 323 F.2d 792, 794 (10th Cir. 1963); Raymond v. United States, 269 F.2d 181, 183 (6th Cir. 1959); Aaron Cohen, 63 T.C. No. 49 (Feb. 3, 1975).
124. See notes 29-35 supra and accompanying text.
128. See notes 145-51 infra and accompanying text. On appeal in Manula the Court of Appeals recognized that hindsight was not a factor in the revocation. 346 F.2d at 1018.
revocation of a tax election, especially if the taxpayer originally made the election on the very return (or returns) being audited.\textsuperscript{130}

It is, however, important to recognize that certain tax elections in themselves increase the burdens of tax administration. The election by a shareholder to be taxed in a corporate liquidation under section 333 is a good example.\textsuperscript{131} In the usual corporate liquidation the earnings and profits of the liquidating corporation are generally irrelevant to the tax consequences of the liquidation, since the shareholders' gain (or loss) is computed without reference to the corporation's tax history.\textsuperscript{132} When, however, a shareholder elects to be taxed in a liquidation under section 333, the corporation's earnings and profits become vitally important,\textsuperscript{133} and consequently the Service may have to examine the corporation's entire tax history to determine its earnings and profits at the time of the liquidation.\textsuperscript{134} If the Service increases the corporation's earnings and profits and thereby increases the shareholder's dividend income, the shareholder may seek to revoke his section 333 election. These facts present the Service's strongest argument against a revocation,\textsuperscript{135} for a taxpayer should perhaps be estopped from revoking an election when it was only \textit{because} of the election that the Service made an otherwise unnecessary tax examination.\textsuperscript{136}

\begin{itemize}
  \item \textsuperscript{130} Some elections, for example installment sales under section 453 of the Code, may have been made years before the tax audit; here the administrative argument has more force, especially if the statute of limitations for the year of the election has already run. See Int. Rev. Code of 1954, § 6511 and notes 58-65 supra and accompanying text.
  \item \textsuperscript{131} See note 121 supra.
  \item \textsuperscript{132} See Bittker & Eustice, supra note 121, at ¶ 11.01, .03.
  \item \textsuperscript{133} See note 121 supra.
  \item \textsuperscript{134} Under section 333(e) the taxpayer is taxed on his ratable share of the corporation's earnings and profits accumulated after February 28, 1913. Int. Rev. Code of 1954, § 333(e).
  \item \textsuperscript{135} Curiously none of the four cases involving elections under § 333 (or its predecessor in the 1939 Internal Revenue Code) presents the argument of administrative burden in this, its most forceful aspect. See cases cited in note 121 supra.
  \item \textsuperscript{136} Despite this argument the taxpayer still ought to prevail if he presents a convincing case that it would be manifestly unjust to bind him to his election. In Aaron Cohen, 63 T.C. No. 49 (Feb. 3, 1975), the taxpayer-shareholders elected to be taxed under section 333 of the Code in the belief that a sale of corporate assets at a profit was made by the shareholders and not by the liquidating corporation. The Commissioner argued that the corporation had made the sale and that gain on the sale was therefore taxable to the corporation. See Commissioner v. Court Holding Co., 324 U.S. 331 (1945). Under section 337 of the Code, gains on sales pursuant to certain liquidations are not taxable to the liquidating corporation, but section 337 is not applicable to a section 333 liquidation. Int. Rev. Code of 1954, § 337(c)(1)(B).
  \item The consequences to the shareholders of a finding in favor of the Commissioner in Aaron Cohen could hardly be more disastrous, for there would be a tax at the corporate level on the gain, and the gain attributed to the corporation would increase the corporation's earnings and profits, thereby increasing the amount of dividend income to the shareholders on the section 333 liquidation. Id. § 333(e). Faced with this impending catastrophe the shareholders sought to
One subtle and often unexpressed reason underlying a decision against the taxpayer is that he was not blameless in the error that led to his election. Two opinions against the taxpayer, for example, emphasize that the taxpayer offered no evidence to justify the tax error behind his election. And in two decisions in favor of the taxpayer, both courts relied heavily on the finding that the taxpayer's mistake was innocent, and that there was no evidence of fraud or understatement in the original return. In short, by exercising this power to deny or allow a revocation, courts seem to punish those taxpayers who cannot prove their innocence, and to reward those who can.

As with the problem of failing to file a return, the punitive approach to revocations in response to tax audits cannot be justified. Suppose, for example, that a taxpayer-shareholder makes a section 333 election knowing that the liquidating corporation has deliberately understated its earnings and profits. While a tax statute might provide that an election in these circumstances should be irrevocable, the present Internal Revenue Code does not contain such a provision, but rather relies on other harsh and specific penalties for a taxpayer guilty of tax fraud. Given these rather specific penalties a court should not create its own penalty of refusing to allow the taxpayer to revoke his election. Nonetheless, a decision against a taxpayer might be justifiable not on punitive grounds, but simply because the taxpayer has failed to meet his burden of proof that the election was a mistake at all.

When the mistake on the taxpayer’s return is the result not of fraud, but of negligence, he should be allowed to change his election. Again revoke their election under section 333, apparently hoping for the following tax consequences: (1) that they would receive the usual capital gain treatment under section 331, rather than dividend treatment, on their gains realized on the liquidation; and (2) that the corporation would escape tax on the gain by virtue of section 337.

Despite the taxpayers' plight the Tax Court refused to allow them to revoke their elections. An appeal by some of the shareholders to the Second Circuit has been dismissed; an appeal by the other shareholders to the Third Circuit is still pending. An interesting situation may arise if the Third Circuit allows a revocation. As a result the eighty percent shareholder approval requirement for a section 333 election may no longer be satisfied. Id. § 333(c)(1). The shareholders in the Second Circuit will then have a strong argument that, since one of the requirements for a section 333 election is no longer satisfied, they should be taxed under the usual rules for corporate liquidation.


138. Meyer’s Estate v. Commissioner, 200 F.2d 592, 596 (5th Cir. 1952); Gentsch v. Goodyear Tire & Rubber Co., 151 F.2d 997, 999 (6th Cir. 1945).

139. See notes 110-20 supra and accompanying text.

140. Both civil and criminal penalties are imposed for fraud. See Int. Rev. Code of 1954, §§ 6653(b), 7201, 7206, 7207.

141. See notes 54-57 supra and accompanying text.
the Code provides specific penalties for negligence, and thus a court should not impose its own. Furthermore, a showing by the taxpayer that his misstatement was not deliberate will satisfy his burden of proving that a mistake has in fact occurred.

A more common situation involves a taxpayer who is guilty neither of fraud nor negligence, but who submits a return which puts the best possible light on the transactions which it reports. When the taxpayer makes an election on his return, he knows that the election will become disadvantageous if his own view of the tax consequences of the transactions reported on the return proves to be incorrect. He may even be aware that it is unlikely that his own view will prevail. Though this is a closer case, this taxpayer too should probably be allowed to revoke his election unless, as a consequence of the election, the Service had to undertake a tax examination which, but for the election, would have been unnecessary.

C. Hindsight Revocations

This Article in discussing the problem of the late election concluded in part that a taxpayer ought not to be allowed to make a late election when his choice results from a knowledge of events subsequent to the filing deadline for the original election. It should not be surprising that a similar issue arises when taxpayers attempt to revoke elections already made.

Perhaps the simplest example is that of a taxpayer who, in a duly filed election, elects to depreciate an asset on the straightline basis. A few years later he decides that, because his income was unexpectedly high for the years immediately following his acquisition of the asset, he would have been better off from a tax point of view under an accelerated method of depreciation. This would allocate a greater share of the deductions for depreciation to the earlier taxable years to offset his unusually high income. Under these facts a court should reject an attempt by the taxpayer to revoke his original election. Like many other elections, an election of straightline depreciation is, quite simply, a gamble in which the taxpayer is betting against

142. Int. Rev. Code of 1954, § 6653(a) imposes a civil penalty for "negligence or intentional disregard of rules and regulations."

143. The government may argue that no mistake occurred which would entitle the taxpayer to relief. The taxpayer may argue, however, that the government should receive, as a result of the audit, no more revenue than it would receive on a corrected tax return which would include all the proper elections to which the taxpayer is entitled.

144. See notes 131-36 supra and accompanying text.

145. See notes 107 & 120 supra and accompanying text.

146. Examples may be found in Int. Rev. Code of 1954, §§ 173, 174, 248, and 453.
unusually high income in the first years after his acquisition of the asset. Further, it is a gamble in which the Code and Regulations contemplate that the risk of unforeseen events will be on the taxpayer. To allow the taxpayer to shift that risk to the government would be unwise from both a policy and a practical standpoint. A number of cases explicitly follow this reasoning, and it is quite likely that a few other decisions rejecting taxpayer attempts to revoke elections are implicitly grounded in the courts' unexpressed realization that it was hindsight alone which motivated the taxpayers to discard elections which later proved to be unprofitable.

A more debatable question arises when the taxpayer can prove that his election was a mistake even when made. Suppose in the example under discussion that the taxpayer establishes that he did not know at the time he adopted straightline depreciation that accelerated depreciation was allowed by the Code, and that, had he been aware of this alternative, he would have depreciated the asset on that basis. Assuming further that subsequent events made accelerated depreciation even more attractive, a court faces the question of whether to allow a taxpayer to revoke an election which, though originally based on a mistake, has been proven by hindsight to be even more unwise.

On the side of the taxpayer is the argument that, as a general rule, an election mistaken in its inception should be revocable within a reasonable time so long as wisdom acquired by hindsight is not the inducement for the revocation. If the taxpayer proves that but for the

147. A taxpayer may choose straightline depreciation for two other reasons. One is simplicity, since it is quite easy to compute the allowable amount of straightline depreciation on an asset by dividing the cost of the asset less its salvage value by its useful life. A second reason would be to avoid the possible recapture as ordinary income of depreciation in the event the property is sold in a later taxable year when the taxpayer's income may be high. Int. Rev. Code of 1954, §§ 1245, 1250. Even if the taxpayer elected straightline depreciation for either of these reasons, he should still be precluded from revoking the election.

148. The Code explicitly provides that a taxpayer may shift at any time from declining balance depreciation to straightline depreciation. Id. § 167(e)(1). This suggests that a shift from straightline to accelerated depreciation is not permissible in the absence of the usual circumstances justifying the revocation of an election by a taxpayer.

149. See note 50 supra and accompanying text.


151. Pacific Nat'l Co. v. Welch, 304 U.S. 191 (1938); Boone County Coal Corp. v. United States, 121 F.2d 988 (4th Cir. 1941); Youngblood v. United States, 388 F. Supp. 152 (W.D. Tex. 1974), aff'd per curiam, 507 F.2d 1263 (5th Cir. 1975); Estate of E.P. Lamberth, 31 T.C. 302 (1958).

152. This is not very likely since the very subsection in the Code which authorizes straightline depreciation also authorizes accelerated methods of depreciation. Int. Rev. Code of 1954, § 167(b).
initial mistake he would have made a different election, his case has some merit. For the government, the practical argument is that to allow a taxpayer to revoke when hindsight may be a motivating factor for the revocation would open a Pandora's box of claims by taxpayers, disgruntled by unforeseen events, that their elections were mistaken from the start. Choosing between these opposing positions is difficult, but in an area as riddled with complications as tax elections, perhaps courts ought to favor, in any close case, the fairness argument of the taxpayer over the fear that the floodgates will be opened to spurious claims. If the fear proves in practice to be well-founded, Congress or the courts can always close the locks.

VI. CONCLUSION

The struggle between taxpayers and the Commissioner regarding the revocation of tax elections and the filing of late elections basically involves two important and conflicting issues of tax policy. On the side of the taxpayer is the policy that a taxpayer should not have to pay more in taxes than the Code requires simply because he misconstrued, or failed to make, a tax election. On the side of government is the argument that the burdens of tax administration should not be increased by accommodating a taxpayer who, through his own fault, made an incorrect tax election.

Many of the early opinions fail to analyze, or even to recognize, these basic issues of tax policy, but instead focus on an inapposite rule borrowed from equity that a mistake of fact serves to excuse an election, but a mistake of law does not. This distinction is hardly a plausible theory for deciding cases which involve an important policy conflict between the fairness arguments of the taxpayer and the practical arguments of the government.

Following the nearly universal demise of this mistake of fact-mistake of law dichotomy, the trend of the majority of decisions has been toward accepting the government's argument that the burdens of tax administration would become too severe if taxpayers were free to revoke or change tax elections. It is surprising that many courts have embraced the government's position without question, even though the practical difficulties on the taxpayer's side in making a wise and proper election are considerable. The government rarely has been able to

153. See notes 29-35 supra and accompanying text.
154. The courts have held for the government in the vast majority of cases reported in the past quarter century. In nearly all these decisions in favor of the government the courts relied, at least in part, on the government's "burdens of administration" argument.
155. See notes 6-22 supra and accompanying text.
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point to a *specific* problem in tax administration which would become significantly more acute if the court decided in favor of the taxpayer. 156

On the other hand, courts should not blindly grant relief to any taxpayer who claims that it would be unfair to hold him to a mistaken election. Since it is the taxpayer who is at fault, however innocently, he should prove the major elements of his case before a court accedes to his revocation. 157 Furthermore, the taxpayer should be required to move within three years to revoke an unwise election, for any delay in such cases is likely to magnify the problems of tax administration. 158

Once the taxpayer meets these basic procedural hurdles, however, his claim to relief is strong. No longer should the government prevail simply by alluding to amorphous administrative burdens, or by alleging its supposed discretion to reject amended returns. 159 Instead, the taxpayer should prevail unless the government establishes either (1) that a specific administrative burden would increase by permitting the revocation; 160 or (2) that the taxpayer's revocation or late election is motivated by a knowledge acquired through hindsight of events subsequent to the date for his original election. 161 But if the gov-

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156. The only cases in which the government established a specific administrative reason to support its position are Pacific Nat'l Co. v. Welch, 304 U.S. 191, 194 (1938) (revocation would affect a number of taxable years, not just the year for which taxpayer claimed a refund); Youngblood v. United States, 388 F. Supp. 152 (W. D. Tex. 1974), aff'd per curiam, 507 F.2d 1263 (5th Cir. 1975) (revocation after four years, arguably too long a period to permit a revocation); Estate of Richard R. Wilbur, 43 T.C. 322, 330-31 (1964) (change from capitalizing to deducting certain expenses likely to affect a number of tax years, not just the year under audit); M. Pauline Casey, 38 T.C. 357, 386 (1962) (administrative problems would "vastly increase" if taxpayers were permitted to change "their method of taking depreciation every time a change in basis or estimated useful life was determined.").

157. See notes 54-57 supra and accompanying text.

158. See notes 58-65 supra and accompanying text.

159. An occasional court has held against the taxpayer partly on the grounds that, since the acceptance of an amended return is within the discretion of the Commissioner, a court should not upset his decision unless he was "arbitrary and capricious" in refusing to accept the amendment. Youngblood v. United States, 388 F. Supp. at 155; see Keeler v. Commissioner, 180 F.2d 707, 710 (10th Cir. 1950). It is true that, as a matter of procedure within the Internal Revenue Service, the Commissioner is not required to accept an amended return whether the amendment involves a change of election or a simple miscalculation on the original return. Miskovsky v. United States, 414 F.2d 954, 955 (3d Cir. 1969); Kunkel & Co., 3 B.T.A. 133, 137 (1925). But the taxpayer is not without a remedy if the Commissioner rejects the amended return. He can bring a jurisdictionally proper action either in a district court or in the Tax Court to convince the court that the amended return (including the change of election) represents a correct statement of his tax obligations. Miskovsky v. United States, 414 F.2d 954, 956 (3d Cir. 1969); Morrow, Becker & Ewing, Inc. v. Commissioner, 57 F.2d 1, 2-3 (5th Cir. 1932). Once an action has been brought, of course, the decision whether to allow the change of election is with the court.

160. See notes 131-36 & 156 supra and accompanying text.

161. See notes 145-51 supra and accompanying text.
ernment simply presents evidence that hindsight may have been a motivating factor in the revocation or late election, the taxpayer should prevail if he is able to refute the government's evidence by demonstrating that he would have chosen the same alternative even without the benefit of hindsight.\textsuperscript{162}

It will be difficult to reverse the pro-government trend in the decisions since \textit{Riley}. In the meantime the issue will continue to produce uncertainty and litigation. Rather than await the results of the judicial process, it may be advisable for Congress to enact legislation governing the revocability of elections. The main difficulty, however, is that a statutory rule which would be satisfactory with respect to certain elections might produce havoc when applied to other elections. Some elections are much easier with the advantage of hindsight; others are not. Some elections or revocations produce administrative burdens for the Internal Revenue Service; others do not. Congress could simply prohibit all revocations and late elections or it could simply allow all revocations for a limited period. The former would be too harsh on taxpayers, the latter too generous.

Probably the best alternative is for Congress to enact a statute explicitly prohibiting revocations after a statutory limitation period of three years.\textsuperscript{163} The implication of such a provision would be that revocations within the three year period are permissible. However, Congress could make clear in the committee reports that a revocation or late election should not be allowed even within the limitation period if the revocation would create a specific administrative problem or if the revocation is motivated by hindsight. Individual taxpayer problems should still be decided on a case-by-case basis, but at least Congress will have provided useful guidance to taxpayers, to the Service, and to the courts.

\textsuperscript{162} See notes 109, 120 & 152 supra and accompanying text.

\textsuperscript{163} See notes 58-65 supra and accompanying text.