**UNITED STATES TAX COURT**
**WASHINGTON, DC 20217** **PA**

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| HECTOR BACA & MAGDALENA BACA, | ) | |
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| Petitioner(s), | ) | |
| | ) | |
| v. | ) | Docket No. 11459-15. |
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| COMMISSIONER OF INTERNAL REVENUE, | ) | |
| | ) | |
| Respondent | ) | |
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**O R D E R**

This case was tried in El Paso, Texas in October 2016, and the parties finished briefing about a year ago. The Commissioner now moves to reopen the record to admit a penalty-approval form that he says shows he complied with I.R.C. § 6751(b)(1) for the accuracy-related penalties that he determined against the Bacas. The Bacas couldn't tell the Commissioner whether or not they objected to his motion and, although we gave them a chance to respond, they never did.

This is another in a long line of *Chai* ghouls. *See Chai v. Commissioner*, 851 F.3d 190 (2d Cir. 2017), *aff'g in part, rev'g in part* 109 T.C.M. 1206, and *Graev v. Commissioner* (*Graev III*), 149 T.C. ___ (Dec. 20, 2017), *supplementing* 147 T.C. 460 (2016).

**Background**

We'll start, as we usually do, with a timeline:

> January 29, 2015 -- The Commissioner determined tax deficiencies and accuracy-related penalties under I.R.C. § 6662 against the Bacas for their joint 2012 and 2013 tax years.

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November 1, 2016 -- Trial. At the trial the Commissioner did not introduce evidence of his compliance with § 6751(b)(1) for the penalties; the parties also never stipulated to his compliance.

November 30, 2016 -- We issued *Graev v. Commissioner* (*Graev II*), 147 T.C. 460, 476-85 (2016), where we held that compliance with § 6751(b)(1) is not ripe for review in a preassessment deficiency case because the penalty has not yet been "assessed".

January 30, 2017 - March 16, 2017 -- The parties filed their seriatim opening and answering briefs; up to this point, neither party had said anything about the Commissioner's compliance (or lack thereof) with § 6751. The briefs didn't say anything about it either.

March 20, 2017 -- The Second Circuit held in *Chai*, 851 F.3d at 218-23, that we were wrong in *Graev II* and that the Commissioner had to show that he complied with § 6751(b)(1) as part of his burdens of production and proof on penalties under § 7491(c) in deficiency cases.

April 5, 2017 - The Bacas filed their seriatim reply brief -- they didn't say anything in it about the Commissioner's compliance (or lack thereof) with § 6751.[1]

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[1] Not only did the Bacas fail to raise § 6751 at trial or in their briefs, they failed even to challenge the accuracy-related penalties at any stage in the proceedings -- not in their petition, amended petition, at trial, or on brief. We were therefore tempted to say here that we didn't need to consider whether the Commissioner has met his burden of production on penalties, *see Swain v. Commissioner*, 118 T.C. 358, 364-65 (2002), and that his penalty-approval form would have no impact on the outcome of the case, *see Butler v. Commissioner*, 114 T.C. 276, 287 (2000), *abrogated on other grounds by Porter v. Commissioner*, 132 T.C. 203 (2009). But we think the Commissioner has the burden of production for the accuracy-related penalties here for another reason: Both parties' pretrial memorandums said that the penalties were at issue, and it seems that that means the issue of the Bacas' liability for accuracy-related penalties was submitted by implied consent for our decision. *See El v. Commissioner*, 144 T.C. 140, 149 (2015) (holding that penalties at issue by implied consent because Commissioner's answer and pretrial memorandum said they were at issue, but not clarifying whether answer and pretrial memorandum were equally important); *see also* Tax Court Rule 41(b). So

December 20, 2017 -- We adopted the Second Circuit's holding in *Chai* as our own in *Graev III*, 149 T.C. at ___ (slip op. at 13-15).

April 13, 2018 -- The Commissioner moved to reopen the record.

The Commissioner wants to add to the record a penalty-approval form for the § 6662(d) (substantial understatement) penalties that he determined against the Bacas for their 2012 and 2013 tax years.[2] In support of his motion, he submitted a declaration from IRS Tax Specialist Alecia Glenn to authenticate the penalty-approval form and show how she came to approve a penalty determination made by IRS Tax Specialist Ruben Paez. Ms. Glenn says in her declaration that she was "Acting Supervisory Internal Revenue Agent/Group Manager for Group Manager Aundra Fusilier" when she signed the penalty-approval form and, at that time, she "was designated by Group Manager Fusilier to review cases and/or act as the immediate supervisor for Tax Specialist Ruben Paez." The penalty-approval form was signed on November 18, 2014; lists R. Paez as the examiner; and does appear to be signed by "A. Glenn for A. Fusilier." In her declaration, Ms. Glenn also says that, as the designated acting supervisor of Mr. Paez, she signed the form to approve the § 6662(d) (substantial understatement) penalties that Mr. Paez proposed in this case.

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the Commissioner has the burden of production for the accuracy-related penalties here, s*ee El*, 144 T.C. at 149, and he must therefore show compliance with § 6751(b)(1), *see Graev III*, 149 T.C. at ___ (slip op. at 13-15).

[2] The Commissioner concedes any § 6662(c) (negligence or disregard) penalties for 2012 and 2013 because the only penalty-approval form he could provide is one for the § 6662(d) (substantial understatement) penalties.

Should we reopen the record to admit this additional evidence? The Bacas don't argue that we shouldn't, but we'll go through the usual analysis anyway.

**Analysis**

The decision to reopen the record to admit additional evidence is within our discretion. *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 401 U.S. 321, 331 (1971); *see also Garcia v. Woman's Hosp. of Tex.*, 97 F.3d 810, 814 (5th Cir. 1996) ("The court's decision 'will not be disturbed in the absence of a showing that it has worked an injustice in the cause'" (quoting *Gas Ridge, Inc. v Suburban Agric. Props., Inc.*, 150 F.2d 363, 366 (5th Cir. 1945))).

But our discretion is not unbounded. We won't reopen the record unless the evidence that the Commissioner seeks to add to the record is not merely cumulative or impeaching, is material to the issues involved, and probably would change the outcome of the case. *Butler v. Commissioner*, 114 T.C. 276, 287 (2000), *abrogated on other grounds by Porter v. Commissioner*, 132 T.C. 203 (2009); *see also Garcia*, 97 F.3d at 814 (trial court should consider "*the importance and probative value of the evidence*, the reason for the moving party's failure to introduce the evidence earlier, and the possibility of prejudice to the non-moving party") (emphasis added).

Even if the evidence is material and would change the outcome of the case, we still need to weigh the Commissioner's diligence (or lack thereof) against any possible prejudice to the Bacas if we were to grant the motion to reopen the record. *See Snuggery-Elvis P'ship v. Commissioner*, 64 T.C.M. 1128, 1132 (1992) (citing *Zenith Radio Corp.*, 401 U.S. at 332-33; *Purex Corp. v. Procter & Gamble Co.*, 664 F.2d 1105, 1109 (9th Cir. 1981); *Mayer v. Higgins*, 208 F.2d 781, 783 (2d Cir. 1953); *Glagola v. Commissioner*, 59 T.C.M. 321 (1990)); *see also Cloes v. Commissioner*, 79 T.C. 933, 937 (1982) ("[p]roper judicial administration demands that there be an end to litigation and that bifurcated trials be avoided"); *Markwardt v. Commissioner*, 64 T.C. 989, 998 (1975) (it is our Court's "policy . . . to try all issues raised in a case in one proceeding and to avoid piecemeal and protracted litigation"). And "prejudice" in this context focuses on whether the submission after trial prevents the nonmoving party from examining and questioning the evidence as it would have during the proceeding. *Estate of Freedman v. Commissioner*, 93 T.C.M. 1007, 1013 (2007); *Megibow v. Commissioner*, 87 T.C.M. 987, 991 (2004).

We'll first consider whether the penalty-approval form is admissible and, if so, whether it passes the first test for reopening the record.

We've found in other cases that penalty-approval forms are admissible under the business-records exception to hearsay, *see* Fed. R. Evid. 803(6), and it's possible that exception would apply here as well -- that is, if we thought the penalty-approval form was hearsay. But it seems that the Commissioner wants the penalty-approval form in as evidence of a verbal act -- admitted to show that the supervisor approved the penalty, not that the penalty was justified or even what the supervisor was thinking when she approved it. As the notes to FRE 801(c) state: "If the significance of an offered statement lies solely in the fact that it was made, no issue is raised as to the truth of anything asserted, and the statement is not hearsay." Fed. R. Evid. 801(c) advisory committee's note; *see also, e.g.*, *Gen. Tire of Miami Beach, Inc. v. NLRB*, 332 F.2d 58, 60-61 (5th Cir. 1964) (statement is nonhearsay verbal act if "inquiry is not the truth of the words said, merely whether they were said"). We think the form is nonhearsay, and the Commissioner has also properly authenticated it -- Ms. Glenn says in her declaration that she has personal knowledge of the IRS's recordkeeping system and that the form was taken from the IRS's administrative file for petitioners. *See* Fed. R. Evid. 901(b)(7)(B) (authentication requirement met by evidence that "a purported public record or statement is from the office where items of this kind are kept"); *see also* Fed. R. Evid. 901(b)(7) advisory committee's note ("[p]ublic records are regularly authenticated by proof of custody, without more"). So the penalty-approval form is admissible.

We can also find that it passes the first test for reopening the record. The Commissioner has the burden of production on the accuracy-related penalties, and he must therefore show compliance with § 6751(b)(1) under *Graev III*. The parties didn't stipulate to his compliance with that section, however, and the Commissioner hasn't to date introduced any evidence of his compliance. Accordingly, we can't say that the penalty-approval form is merely cumulative or impeaching; and it is material and could change the outcome of the case, because it tends to prove that the IRS complied with § 6751. *See Butler*, 114 T.C. at 287; *Garcia*, 97 F.3d at 814. It therefore passes the first test for reopening the record.

We still need, however, to consider diligence and prejudice. The question of the Commissioner's diligence when it comes to *Chai* ghouls is always a little muddled. I.R.C. § 6751 has been in the Code for almost twenty years, and the trial in this case concluded before *Graev II*, *Chai*, or *Graev III*. But the Commissioner argues that he "has not previously had the opportunity to supplement the record to

respond to a section 6751(b) challenge," and it would therefore "be in the interests of justice to reopen the record for the submission of evidence of satisfaction of the requirements of section 6751(b)(1)" in this case. We are not immediately persuaded by this argument: Our decision in *Graev III* didn't create new law; it interpreted a section of the Code that was in effect at the time of the trial in this case, which we then applied to the parties before us in that case. *See Harper v. Va. Dept. of Taxation*, 509 U.S. 86, 97 (1993) (when the Court applies a rule of federal law to the parties in a case, that rule "must be given full retroactive effect in all cases still open on direct review and as to all events, regardless of whether such events predate or postdate . . . announcement of the rule").

But we do think the Commissioner might have had less reason to anticipate the importance of § 6751 in this case than in many other cases. Although *Graev III* didn't create new law, it is true that it and *Chai* are the first cases to *clarify* that § 6751(b) and § 7491(c) combine to place the burden of production on the Commissioner to show that he complied with § 6751(b) in cases where he wants a penalty. And unlike other cases where *Chai* ghouls have appeared, § 6751 never came up here in pretrial motions or discovery; indeed, the Bacas failed to even challenge the accuracy-related penalties in their petition, amended petition, at trial, or on brief. So there is some excuse for the Commissioner's lack of diligence here. *See Garcia*, 97 F.3d at 814 (need to consider the "reason for the moving party's failure to introduce the evidence earlier").

We are also not convinced that the Bacas would be prejudiced if we reopened the record to admit the penalty-approval form. It is evidence that we would have admitted at trial -- just as we are doing now -- and the Bacas haven't told us how they might be prejudiced if we admitted the form now without giving them a chance to examine and question the evidence as they would have during the proceeding. We therefore can't conclude that the Bacas would be prejudiced.

The penalty-approval form is material and could change the outcome of the case; and while we do think the Commissioner could've been more diligent, we also are not convinced that the Bacas would be prejudiced if we reopened the record now to admit the form.

It is therefore

ORDERED that respondent's April 13, 2018 motion to reopen the record is granted to the extent it seeks the admission of the penalty-approval form attached to his declaration. It is also

ORDERED that the Clerk of the Court is to detach the Civil Penalty Form and file it as a separate document.

**(Signed) Mark V. Holmes**
**Judge**

Dated: Washington, D.C.
July 12, 2018