RULE 11 AND THE NONDEDUCTIBILITY OF MONETARY SANCTIONS IMPOSED UPON ATTORNEYS

Arthur W. Andrews*

INTRODUCTION

The 1983 amendments to the Federal Rules of Civil Procedure responded both to perceived abuses of the litigation process and to the need to make that process speedier and more efficient.[1] The need to expedite was addressed, in part, by trying to ensure more effective judicial case management, scheduling and control.[2] Abuses of the litigation process were addressed in rules dealing with excessive discovery and the evasion of reasonable discovery,[3] as well as rules against the filing of frivolous claims, defenses and motions.[4] Amended

---

* Professor of Law, University of Arizona College of Law; Visiting Professor of Law, University of Iowa College of Law, Fall Semester, 1989; B.A. 1959, University of Iowa; L.L.B., 1963, L.L.M. (in Taxation), 1964, New York University. Member of the Arizona, Iowa and New York bars. I wish to thank my colleagues, Professors Charles E. Ares, Roger C. Henderson, and Theodore J. Schneyer, for their very helpful comments and suggestions on various portions of this Article. I also wish to acknowledge the valuable research assistance of Mr. Thomas Piccioli, then a third-year law student.

1. *See generally* Letter by Walter R. Mansfield, Chairman, Advisory Committee on Federal Civil Rules to Judge Gignoux, Chairman, Standing Committee on Rules of Practice and Procedure (March 9, 1982), *reprinted in* 97 F.R.D. 190 (1983) [hereinafter Letter of Mansfield]; FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198 (1983). One commentator has questioned whether Rule 11 is valid under the Rules Enabling Act, 28 U.S.C. § 2072. Burbank, *Sanctions in the Proposed Amendments to the Federal Rules of Civil Procedure: Some Questions About Power*, 11 HOFSTRA L. REV. 997 (1983). *See* Thomas v. Capital Sec. Serv., Inc., 836 F.2d 866, 884 n.25 (5th Cir. 1988) (en banc); Donaldson v. Clark, 819 F.2d 1551, 1559 n.9 (11th Cir. 1987) (en banc). But, "it seems clear that the Supreme Court would ultimately uphold the new provisions as proper exercises of the rulemaking power . . . ." C. WRIGHT & A. MILLER, 5 FEDERAL PRACTICE & PROCEDURE: CIVIL § 1334, at 179 (Supp. 1986); Burbank, *Hold the Corks: A Comment on Paul Carrington's "Substance" and "Procedure" in the Rules Enabling Act*, 1989 DUKE L.J. 1012, 1041 ("[T]he Court has never invalidated a Federal Rule of Civil Procedure.");Gaiardo v. Ethyl Corp., 835 F.2d 479, 483 (3d Cir. 1987).

2. *See* FED. R. CIV. P. 16 (amended 1983); Letter of Mansfield, *supra* note 1. *See also* Schwarzer, *Sanctions Under The New Federal Rule 1—A Closer Look*, 104 F.R.D. 181, 204 (1985).

3. *See* FED. R. CIV. P. 26 (amended 1983); Letter of Mansfield, *supra* note 1.

4. *See* FED. R. CIV. P. 11 (amended 1983); Letter of Mansfield, *supra* note 1. Although Rule 26 applies to discovery generally, amended Rule 11 deals with the filing of discovery motions. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D 198, 201 (1983).

Rule 11 specifically focused on the problem of pleadings and motions that are frivolous or otherwise improper.[5]

This Article has two different, but interrelated, purposes. The most important is to consider whether monetary sanctions imposed solely upon an attorney under amended Rule 11[6] are deductible for federal income tax purposes as ordinary and necessary business expenses pursuant to section 162 of the Internal Revenue Code. This depends on whether, if such payments are otherwise deductible under section 162(a), they are nonetheless specifically disallowed by section 162(f) which forbids the deduction of "any fine or similar penalty paid to a government for the violation of any law." It is appropriate first to present an overview of the more significant elements and aspects of Rule 11. This is due to the direct relevance of much of this material to our later consideration of the tax deductibility issue.

In other words, we need to know what we are talking about before we can deal with its tax consequences. Thus, any analysis of those effects is necessarily predicated upon a basic knowledge of the general scope and purpose

---

5. Amended Rule 11 has generated a wealth of literature as to its construction, application, consequences and wisdom. Some of the more significant include: S. BURBANK, RULE 11 IN TRANSITION: THE REPORT OF THE THIRD CIRCUIT TASK FORCE ON FEDERAL RULE OF CIVIL PROCEDURE 11 (1989); G. JOSEPH, SANCTIONS: THE FEDERAL LAW OF LITIGATION ABUSE 33-310 (1989); G. JOSEPH, P. SANDLER & C. SHAFFER, JR., SANCTIONS: RULE 11 AND OTHER POWERS (1988) [hereinafter SANCTIONS], S. KASSIN, AN EMPIRICAL STUDY OF RULE 11 SANCTIONS (1985); Cavanagh, *Developing Standards Under Amended Rule 11 of the Federal Rules of Civil Procedure*, 14 HOFSTRA L. REV. 499 (1986); Levin & Sobel, *Achieving Balance in the Developing Law of Sanctions*, 36 CATH. U.L. REV. 587 (1987); Nelken, *Sanctions Under Amended Federal Rule 11—Some "Chilling" Problems in the Struggle Between Compensation and Punishment*, 74 GEO. L.J. 1313 (1986); Parness, *More Stringent Sanctions Under Federal Civil Rule 11: A Reply to Professor Nelken*, 75 GEO. L.J. 1937 (1987); Schwarzer, *Rule 11 Revisited*, 101 HARV. L. REV. 1013 (1988); Vairo, *Rule 11: A Critical Analysis*, 118 F.R.D. 189 (1988); Wade, *On Frivolous Litigation: A Study of Tort Liability and Procedural Sanctions*, 14 HOFSTRA L. REV. 433 (1986); Note, *Plausible Pleadings: Developing Standards for Rule 11 Sanctions*, 100 HARV. L. REV. 630 (1987); Note, *The Dynamics of Rule 11: Preventing Frivolous Litigation By Demanding Professional Responsibility*, 61 N.Y.U. L. Rev. 300 (1986) [hereinafter *The Dynamics of Rule 11*]. For further reference materials, see S. BURBANK, *supra*, at 101-04.

6. The question whether monetary sanctions are deductible by the payor where imposed upon both the client and the attorney, jointly and severally, is beyond the scope of this Article. The reason is that the basis for allocation of sanctions separately between the attorney and client may not be clear, although it may be obvious that a violation of Rule 11 has occurred. *See* Eastway Constr. Corp. v. City of New York, 637 F. Supp. 558, 569 (E.D.N.Y. 1986), *modified*, 821 F.2d 121 (2d Cir.), *cert. denied*, 484 U.S. 918 (1987); Schwarzer, *supra* note 2, at 203. If that is the situation, the court may decide to assess the sanction against both the attorney and client, jointly and severally, leaving them to sort it out. *Id.* In such a case where the allocation of fault or responsibility for the violation is not specifically determined by the court the issue of deductibility raises additional considerations beyond those where the lawyer is clearly paying his or her sole obligation.

In addition, the question whether monetary sanctions imposed solely upon clients (or *pro se* litigants) under Rule 11 are deductible is likewise beyond the scope of this Article. The client's expenditure may or may not be arguably generated in a trade or business. Thus, it might arise, for example, in connection with a personal injury suit unconnected with a business, so that it could be considered a non-deductible personal, living or family expense. *See* I.R.C. § 262 (1986).

This Article is concerned, therefore, with those monetary rule 11 sanctions for which the attorney bears the sole responsibility so that the expense can be plausibly regarded as arising in the trade or business of being a lawyer. This can occur where the monetary Rule 11 sanction is imposed *only* upon the attorney either in its entirety or a certain part thereof. In either case it is assumed that the amount paid by the lawyer is not reimbursable by the client.

of Rule 11, the standard utilized and the factors considered by the courts in determining whether a violation has occurred, and the types of conduct coming within its proscription.

Beyond that, and of great importance to the tax portion of this article, is the Rule 11 sanctioning power including its ultimate purpose, the range of sanctions available as a means of enforcement, and the factors taken into account by the court in fixing the particular penalty. In addition, such things as the different types and amounts of potential monetary sanctions, are of obvious relevance to the deduction side. For example, whether the sanction is in the form of a fine payable to the court or of costs and attorney fees payable to the other party is important. In the latter case, the issue whether the amount can include costs and attorney fees on appeal is also important.

A second purpose of this Article relates to the general practitioner who engages in some litigation. Due to the comparative newness of the Rule, the fact that the lawyer's litigation experience may be primarily geared to state rather than federal court, or for whatever reason, the practitioner may not be fully aware of the current scope, construction and application of federal Rule 11. The recent increase in the amount of federal appellate court decisions in this area makes this more important. This overview is a modest attempt to remedy that situation, but its importance to the state court practitioner does not stop there because several states have adopted civil rules or statutes that are either identical, or substantially similar, to federal Rule 11. Therefore, the federal Rule interpretations are also of likely significance in state court practice.

Accordingly, this overview includes some material designed to produce a more rounded and complete presentation of Rule 11. For example, this summary briefly covers such topics as the procedures utilized by courts in the sanctioning process, appellate court standard of review, and the persons against whom sanction awards can be made, including *pro se* litigants and the government. It should be noted that many of these areas are also of importance to the deductibility issue. Thus, several of the cases in the *pro se* litigant topic graphically illustrate the ultimate purpose of Rule 11 sanctions. Likewise, the area involving sanctions against the government is of great importance to one specific prerequisite for nondeductibility.

Nonetheless, no attempt has been made to go into all the intricacies of its construction and operation. It should be realized that the federal courts are still engaged in sorting out the proper interpretation and application of many aspects of the Rule. With these admonitions in mind, it is now time to turn to Rule 11 itself.

PART I: AMENDED RULE 11: AN OVERVIEW

Rule 11 and the Duty Imposed

Amended Rule 11 currently provides, in relevant part, that:

> Every pleading, motion, or other paper of a party represented by an attorney shall be signed by at least one attorney of record in the attorney's individual name. . . . A party who is not represented by an attorney shall sign the party's pleading, motion or other paper. . . . The signature of an attorney or party

> constitutes a certificate by the signer that the signer has read the pleading, motion or other paper; that to the best of the signer's knowledge, information, and belief formed after a reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. . . . If a pleading, motion or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon . . . [the signer], a represented party, or both, an appropriate sanction, which may include an order to pay to the other party . . . the amount of the reasonable expenses incurred because of the filing of the pleading, motion or other paper, including a reasonable attorney's fee.[7]

Under this language an attorney or party signing any pleading, motion or other paper filed in the federal district court is certifying that, to the best of the signer's knowledge, information and belief formed after reasonable inquiry, the paper: (1) is well grounded in fact, (2) is warranted by existing law or it represents a good faith argument for the extension, modification or reversal of existing law; and (3) is not filed for any improper purpose.[8] In general, *conduct* that does not meet each one of these three standards constitutes a violation of Rule 11.[9]

---

7. FED. R. CIV. P. 11 (amended 1983, 1987). The 1987 amendments to Rule 11 were only technical and not substantive. *See* FED. R. CIV. P. 11 advisory committee notes, 1987 amendment, 113 F.R.D. 280, 281 (1987). The United States Tax Court also has a rule which was revised in 1986 to parallel the 1983 amendment to the federal civil Rule 11. *See* R. PRAC. & P. OF THE UNITED STATES TAX COURT, Rule 33(b) (1986). The federal court interpretations of Rule 11 are considered by the Tax Court in construing its own rule. Versteeg v. Commissioner, 91 T.C. 339, 342 (1988). As to other sanctions available in the Tax Court for maintenance of frivolous or groundless positions as well as unreasonably and vexatiously multiplying proceedings, see I.R.C. § 6673 as enacted by the Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7731(a) (1989).

In addition, a number of states have civil procedure rules which are either identical or substantially similar to federal Rule 11. *See, e.g.*, ARIZ. R. CIV. P. 11(a); ARK. R. CIV. P. 11; COLO. R. CIV. P. 11; DEL. SUPER. CT. CIV. R. 11; D.C. SUPER. CT. CIV. R. 11; IDAHO R. CIV. P. 11(a)(1); IOWA R. CIV. P. 80(a); KY. R. CIV. P. 11; ME. R. CIV. P. 11; MICH. CT. R. 2.114(E); MINN. R. CIV. P. 11; MISS. R. CIV. P. 11; MO. R. CIV. P. 55.03; MONT. R. CIV. P. 11; NEV. R. CIV. P. 11; N.D.R. CIV. P. 11; ORE. R. CIV. P. 17; S.D.R.P. CIR. CT. 15-6-11(a) & (b); UT. R. CIV. P. 11; VT. R. CIV. P. 11; WASH. SUPER. CT. R. 11; WYO. R. CIV. P. 11.

Finally, some states have directly enacted statutory provisions which are either identical or substantially similar to federal Rule 11. *See, e.g.*, CAL. CIV. PROC. CODE § 447 (West Cum. Supp. 1989) (applicable only to Riverside and San Bernadino Counties from July 1, 1988 to Jan. 1, 1991 on experimental basis); ILL. ANN. STAT. ch. 110, ¶ 2-611 (Smith-Hurd 1986); KAN. STAT. ANN. § 60-211 (1986); N.C. GEN. STAT. 1A-1 (1986); OKLA. STAT. ANN. § 2011 (1987); VA. CODE ANN. § 8.01-271.1 (1987). *See also supra* note 428.

8. It is obvious that by the very terms of Rule 11 the signer of the paper is also certifying that the signer has read it. The failure of the signer to read the paper is, *ipso facto*, a violation. *See* Zaldivar v. City of Los Angeles, 780 F.2d 823, 830 (9th Cir. 1986). This aspect of Rule 11 will not be discussed further.

9. *See, e.g.*, Unioil, Inc. v. E.F. Hutton & Co., Inc., 809 F.2d 548, 557 (9th Cir. 1986); Golden Eagle Distrib. Corp. v. Burroughs Corp., 801 F.2d 1531, 1536 (9th Cir. 1986). Rule 11 obviously focuses on the *conduct* of the signer in regard to the reasonable pre-filing inquiry. The issue is whether it also focuses on the *product* of the signer and requires that *paper*

From this certification it is clear that, in addition to being directed against the use of filing for improper purposes such as a weapon for personal or economic harassment, the Rule addresses the problem of frivolous filings—where the paper in question is filed without a reasonable pre-filing inquiry into either the facts or the law, and it is subsequently determined to be so deficient in either respect as to merit the imposition of sanctions.[10] Consequently, it has been stated that the Rule includes "a duty to look before leaping and may be seen as a litigation version of the familiar railroad crossing admonition to 'stop, look, and listen.'"[11]

A. The Standard of Objective Reasonableness

The original, pre-1983 unamended version of Rule 11[12] required a showing of subjective bad faith on the part of an attorney before sanctions

---

to be objectively reasonable at the time that it is filed. The product approach has its source in the notes to Rule 11 where the Advisory Committee stated that:

> what constitutes a reasonable inquiry may depend upon such factors as . . . *whether the . . . paper was based upon a plausible view of the law* . . . [and that] [t]he rule does not require a party or an attorney to disclose privileged communications or work product in order to show that the signing of the . . . paper *is substantially justified.*

FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199 (1983) (emphasis added).

The product approach draws further support from the comments of the Advisory Committee to Rule 26(g) which was amended at the same time as Rule 11 and deals with a similar certification by the signer of a discovery request, response or objection. There the Advisory Committee said that

> [t]he duty to make a 'reasonable inquiry' is satisfied if the investigation undertaken by the attorney *and the conclusions drawn therefrom* are reasonable under the circumstances. *It is an objective standard similar to the one imposed by Rule 11.*

FED. R. CIV. P. 26 advisory committee notes, 97 F.R.D. 216, 219 (1983) (emphasis added).

In any event, the product approach has been "widely embraced." S. BURBANK, *supra* note 5, at 14. Consequently, many courts require not only that the signer's conduct be objectively reasonable, but also that the results thereof meet that standard, in order to avoid a Rule 11 violation. *Id. See, e.g., Zaldivar*, 780 F.2d at 830-31; Eastway Constr. Corp. v. City of New York, 762 F.2d 243, 254 (2d Cir. 1985). A recent extensive report on Rule 11 in the Third Circuit has stated cogent arguments as to why the product approach is dubious based upon the language and drafting history. *See* S. BURBANK, *supra* note 5, at 14-18. It makes a difference if the product approach is espoused by a court because, among other things, a pre-filing inquiry into the law which is extensive, thorough, and otherwise objectively reasonable will not save the signer of a complaint from sanction where the signing attorney was simply stupid in believing that it was warranted in law. *Id.* at 18-19; *Zaldivar*, 780 F.2d at 831 ("Extended research alone will not save a claim that is without legal . . . merit from the penalty of sanctions."). *See also* Schwarzer, *Rule 11 Revisited*, 101 HARV. L. REV. 1013, 1018-19, 1021, 1024-25 (1988).

10. *See, e.g.*, Greenberg v. Sala, 822 F.2d 882, 885 (9th Cir. 1987); *Zaldivar*, 780 F.2d at 830; FED. R. CIV. P. 11 Advisory Committee Notes, 97 F.R.D. 198 (1983) ("discourage dilatory or abusive tactics and help to . . . . [lessen] frivolous claims or defenses"); Letter of Mansfield, *supra* note 1, 97 F.R.D. at 192 ("[A] duty of reasonable inquiry . . . would reduce frivolous claims, defenses or motions by leading litigants to stop, think and investigate more carefully before serving and filing papers.").

11. Lieb v. Topstone Indus., Inc., 788 F.2d 151, 157 (3d Cir. 1986).

12. The original, pre-1983 unamended Rule 11 provided as follows:

> Every pleading of a party represented by an attorney shall be signed by at least one attorney of record in his individual name, whose address shall be stated. A party who is not represented by an attorney shall sign his pleading and state his address. Except when otherwise specifically provided by rule or statute, pleadings need not be verified or accompanied by affidavit. The rule in equity that the averments of an answer under oath must be overcome by the testimony of

could be imposed.[13] This was due to the requirement in the Rule that the violation be "willful."[14] One of the consequences of this subjective bad faith requisite was that the Rule was not effective in deterring abuses;[15] for example, a mere eleven proven instances of Rule 11 violations occurred between 1938 to 1976.[16]

Under the current amended Rule 11 there is a general consensus that subjective bad faith is no longer required for a violation to be shown;[17] in other words, a "pure heart but empty head" is no longer a defense.[18] Instead, the new Rule imposes an objective standard of reasonableness under the circumstances for the testing of conduct.[19] In the words of the Advisory Committee, "[t]his standard is more stringent than the original good-faith formula and thus it is expected that a greater range of circumstances will trigger its violation."[20]

In applying this general objective standard of reasonableness under the circumstances, the so-called "reasonable person" against whom the conduct in question is to be tested is that of a competent attorney admitted to practice before the district court.[21] Some courts have typically included, however, such additional general admonitions that Rule 11 should be "used with the utmost care and caution"[22] and should be "reserved only for exceptional circumstances"[23] as it is "an extraordinary remedy."[24] Likewise, with respect

---

two witnesses or of one witness sustained by corroborating circumstances is abolished. The signature of an attorney constitutes a certificate by him that he has read the pleading; that to the best of his knowledge, information, and belief there is good ground to support it; and that it is not interposed for delay. If a pleading is not signed or is signed with intent to defeat the purpose of this rule, it may be stricken as sham and false and the action may proceed as though the pleading had not been served. For a willful violation of this rule an attorney may be subjected to appropriate disciplinary action. Similar action may be taken if scandalous or indecent matter is inserted.

FED. R. CIV. P. 11.

13. *E.g.*, Badillo v. Central Steel & Wire Co., 717 F.2d 1160, 1166 (7th Cir. 1983); Nemeroff v. Abelson, 620 F.2d 339, 350 (2d Cir. 1980).

14. *See* Burkhart Through Meeks v. Kinsley Bank, 804 F.2d 588, 589 (10th Cir. 1986).

15. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198 (1983).

16. *See* S. KASSIN, *supra* note 5, at 2.

17. *E.g.*, Robinson v. National Cash Register Co., 808 F.2d 1119, 1126-27 (5th Cir. 1987); *Zaldivar*, 780 F.2d at 829; *Eastway Constr. Corp.*, 762 F.2d at 253-54.

18. Zuniga v. United Can Co., 812 F.2d 443, 452 (9th Cir. 1987); Thornton v. Wahl, 787 F.2d 1151, 1154 (7th Cir.), *cert. denied*, 479 U.S. 851 (1986); Schwarzer, *Sanctions Under The New Federal Rule 11—A Closer Look*, 104 F.R.D. 181, 184 (1985).

19. *E.g.*, *Thomas*, 836 F.2d at 873; *Donaldson*, 819 F.2d at 1556; *Golden Eagle Distrib. Corp.*, 801 F.2d at 1536; Stevens v. Lawyers Mut. Liab. Ins. Co. of N.C., 789 F.2d 1056, 1060 (4th Cir. 1986). *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198 (1983). A Rule 11 violation may occur where, for example, there is a failure to have a good faith argument for the extension, modification or reversal of existing law. Despite the "good faith" terminology, the standard for testing this type of conduct is that of objective reasonableness. *Id.*

20. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198-99 (1983).

21. *Zaldivar*, 780 F.2d at 830. *See* Brown v. Federation of State Medical Bds of the United States, 830 F.2d 1429, 1436 (7th Cir. 1987); Oliveri v. Thompson, 803 F.2d 1265, 1275 (2d Cir. 1986).

22. Federal Deposit Ins. Corp. v. Tefken Constr. & Installation Co., 847 F.2d 440, 444 (7th Cir. 1988).

23. Mary Ann Pensiero, Inc. v. Lingle, 847 F.2d 90, 99 (3d Cir. 1988).

24. Operating Eng'rs Pension Trust v. A-C Co., 859 F.2d 1336, 1344 (9th Cir. 1988).

to various specific aspects of Rule 11, some courts have stated that it "is violated only when it is 'patently clear that a claim has absolutely no chance of success'"[25] and that "sanctions should not . . . [be] imposed where a 'plausible . . . argument can be made.'"[26] It is unclear whether such admonitions have had the practical effect of diluting the objective reasonableness standard.

In the application of this objective standard of reasonableness under the circumstances, a number of different factors are relevant in determining whether a Rule 11 violation has occurred. With regard to the pre-filing inquiry, the Advisory Committee has suggested the following: (1) the time available to the signer for investigation; (2) whether the signer had to rely on the client for information about the facts underlying the paper; (3) whether the paper was based upon a plausible view of the law; and (4) whether the signer relied upon forwarding counsel or another member of the bar.[27] Depending upon the particular circumstances, a non-exclusive listing of additional factors suitable to be considered by the courts includes: (5) the factual and legal complexity of the issues involved; (6) the time available to the signer to prepare the document; (7) the extent to which development of the factual circumstances underlying the claim requires discovery; and (8) the *pro se* status of the litigant.[28]

With respect to the application of these various factors in determining the adequacy of the pre-filing inquiry, it is probably well to remember that, as a general matter,

> It is not permissible to file suit and use discovery as the sole means of finding out whether you have a case. Discovery fills in the details, but you must have the outline of a claim at the beginning. . . . The amount of investigation required by Rule 11 depends on both the time available to investigate and on the probability that more investigation will turn up important evidence; the Rule does not require steps that are not cost-justified. . . . Inquiry that is unlikely to produce results is also unnecessary.[29]

B. Improper Purpose

It is with respect to the third category of violations--"improper purpose" filings—that the question whether subjective intent should be the appropriate standard is presented in full force. The very words "improper purpose" at least arguably support the idea that subjective intentional impropriety should be the standard for testing this type of conduct.[30] On the other hand, the utilization of a subjective intent test would re-introduce into the amended Rule 11 one of the infirmities of the original version and endanger its effectiveness.[31] Most of the courts considering the issue have indicated that, like the standard applicable to

---

25. *Oliveri*, 803 F.2d at 1275. *See* SANCTIONS, *supra* note 5, at 4.
26. *Golden Eagle Distrib. Corp.*, 801 F.2d at 1541.
27. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199 (1983).
28. *Thomas*, 836 F.2d at 875-76; *Brown*, 830 F.2d at 1435. *See also* SANCTIONS, *supra* note 5, at 3-6.
29. Szabo Food Serv., Inc. v. Canteen Corp., 823 F.2d 1073, 1083 (7th Cir. 1987), *cert. dismissed*, 495 U.S. 901 (1988).
30. *See Zaldivar*, 780 F.2d at 831 n.9; Nelken, *supra* note 5, at 1320 & n.51.
31. *See* Schwarzer, *supra* note 2, at 195-96 (1985); S. KASSIN, *supra* note 5, at 2-4.

the pre-filing inquiry into the facts and the law, an objective standard should be utilized in testing for an improper purpose filing.[32]

The Seventh Circuit, however, apparently disagrees, at least to some extent. In *Brown v. Federation of State Medical Boards*,[33] the court stated:

> whether a party or attorney acted with an improper purpose is based upon an objective standard. However, we have noted that subjective bad faith or malice may be important when the suit is objectively colorable. . . . 'The Rule effectively picks up the torts of abuse of process (filing an objectively frivolous suit) and malicious prosecution (filing a colorable suit for the purpose of imposing expense upon the defendant rather than for the purpose of winning). . . .' Subjective bad faith is relevant in situations involving malicious prosecution of claims, although not . . . where a party has repeatedly pursued implausible claims.[34]

Thus, in the Seventh Circuit subjective intent is applied in testing for improper purpose at least where the filing is not frivolous—that is to say, where it is adequately grounded in fact and law for Rule 11 purposes.[35]

Of the courts espousing the objective improper purpose standard, some, like the Ninth Circuit, have gone even further by indicating that the filing of a nonfrivolous initial complaint cannot violate Rule 11 as a matter of law, even where it was done to harass the defendant, a conceded improper purpose.[36] Under this view, where an initial complaint is concerned, the reasonable pre-filing inquiry into the facts and law requirement of Rule 11 has swallowed up the improper purpose prong.[37] The apparent rationale for this position is that the law gives the plaintiff certain rights, and the filing of a nonfrivolous complaint is necessary in order to be able to vindicate those rights in court.[38]

---

32. *See, e.g.*, INVST Financial Group, Inc. v. Chem-Nuclear Sys., Inc., 815 F.2d 391, 401-02 (6th Cir. 1987); *Stevens*, 789 F.2d at 1060; *Lieb*, 788 F.2d at 157; *Zaldivar*, 780 F.2d at 830-31 n.9.

33. 830 F.2d 1429 (7th Cir. 1987).

34. *Id.* at 1436.

35. The Seventh Circuit may have even gone beyond that and adopted a completely subjective standard in testing improper purpose although this is not clear. *See* Local 232, Allied Indus. Workers of Am., AFL-CIO v. Briggs & Stratton Corp., 837 F.2d 782, 789 n.5 (7th Cir. 1988). *See also Szabo Food Serv., Inc.*, 823 F.2d at 1083.

36. *Zaldivar*, 780 F.2d at 832. *Accord*, National Ass'n of Gov't Employees, Inc. v. National Fed'n of Fed. Employees, 844 F.2d 216, 223-24 (5th Cir. 1988). *See* Aetna Life Ins. Co. v. Alla Medical Serv., Inc., 855 F.2d 1470, 1476 (9th Cir. 1988). Presumably, this means that an initial complaint adequately grounded in fact and law can never violate Rule 11 despite the fact that it was filed for an improper purpose tested against either an objective or subjective standard. *See id.*; *Golden Eagle Distrib. Corp.*, 801 F.2d at 1538. On the other hand, if the complaint is frivolous so that it does violate the reasonable pre-filing inquiry requisite of Rule 11, a court obviously can consider whether it was also filed for an improper purpose. *See* Hudson v. Moore Business Forms, Inc., 827 F.2d 450, 456 n.4 (9th Cir. 1987). This would be relevant, for example, to the issue of the appropriate sanction to be imposed, the existence of an improper purpose, in addition to the lack of an adequate pre-filing inquiry, presumably justifying a more severe sanction. *See, e.g., Eastway Constr. Corp.*, 637 F. Supp. at 573, *modified to increase sanction*, 821 F.2d 121, 123, 124 (2d Cir. 1987).

37. *See Aetna Life Ins. Co.*, 855 F.2d 1475-76, *Zaldivar*, 780 F.2d at 832.

38. *See National Ass'n of Gov't Employees, Inc.*, 844 F.2d at 224.

This principle seemingly has been limited, however, to the filing of the initial complaint and has not been applied to other filings.[39] Thus, in the Ninth Circuit subsequent motions and other papers following the complaint can violate Rule 11 if filed for an improper purpose, tested objectively, despite the fact that they are nonfrivolous.[40]

C. The Signing of Papers, the Issue of Continuing Duty, Removal Cases, and Some Random Examples of Violative Conduct

By its very terms Rule 11 applies to "a pleading, motion or other paper." This not only includes the initial complaint and the answer, but also generally any other pleadings, motions or papers.[41] And, under Rule 11, it is the person's signature that constitutes certification that certain representations about that paper and its filing are true to the best of the signer's knowledge, information and belief formed after reasonable inquiry. If the paper "is signed in violation of this rule," the signer is to be sanctioned.

Accordingly, the focus of the Rule is on the signing of the paper in question with the signer's conduct being tested "by inquiring what was reasonable to believe at the time the pleading . . . was submitted."[42] In this process the use of hindsight is to be avoided.[43] Because of this emphasis on the signing and filing of a paper, it is fair to conclude that, although very important, Rule 11 is limited in scope and "is not a panacea intended to remedy all manner of attorney misconduct occurring before or during the trial of civil cases."[44]

Related to this is the question whether there is any continuing duty to reassess claims or papers already filed based upon information subsequently obtained. For example, is there a violation by a plaintiff's attorney who fails to dismiss the case after the defendant's attorney submits solid evidence to him that the suit is barred by *res judicata*? Most of the courts considering this general issue believe that Rule 11 does not impose such a continuing duty applicable to the period following the act of signing and filing the document in question[45] because "[l]ike a snapshot, Rule 11 review focuses upon the instant when the picture is taken—when the signature is placed upon the document."[46] But there is not unanimity on this point, the Sixth Circuit having espoused the contrary

---

39. *See Zaldivar*, 780 F.2d at 832 n.10; *National Ass'n of Gov't Employees, Inc.*, 844 F.2d at 224.

40. *Aetna Life Ins. Co.*, 855 F.2d at 1476-77. *See also* Cohen v. Virginia Elec. & Power Co., 788 F.2d 247, 249 (4th Cir. 1986) (motion for leave to amend complaint to add new state law counts was sanctionable since filed for an improper purpose although it had a legal basis).

41. It does not, however, apply to discovery papers the certification of which is governed by Rule 26(g), although it does encompass discovery motions. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 201 (1983). *See Zaldivar*, 780 F.2d at 830.

42. Teamsters Local Union No. 430 v. Cement Express, Inc., 841 F.2d 66, 68 (3d Cir. 1988); *Thomas*, 836 F.2d at 874-75; *Oliveri*, 803 F.2d at 1274-75.

43. *See supra* note 42.

44. *See Zaldivar*, 780 F.2d at 829-30.

45. *E.g., Thomas*, 836 F.2d at 874-75 & n.9; *Gaiardo*, 835 F.2d at 484; Pantry Queen Foods, Inc. v. Lifschultz Fast Freight, Inc., 809 F.2d 451, 454 (7th Cir. 1987); *Oliveri*, 803 F.2d at 1274-75. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199 (1983).

46. *Thomas*, 836 F.2d at 874.

view.[47] Moreover, there are a few apparently conflicting decisions even in some of the circuits purportedly following the "no continuing duty" position.[48]

In any event, the effect of no continuing duty tends to be overstated since most cases require a series of filings. To illustrate, knowledge gained after the first filing and before the second filing should be reflected in that second filing, although there is no continuing duty with respect to the first. Consequently, the usual effect of a series of filings is to require updating even under Rule 11.[49] Finally, it seems appropriate to note that other protections can be used against abusive litigation tactics not involving the signing of papers within the scope of Rule 11. These would include, for example, the statutory remedy for an attorney's unreasonable and vexatious multiplication of proceedings[50] and Rule 26(g) dealing with discovery requests, responses and objections.[51]

Another issue related to the limited focus of Rule 11 involves cases removed from state court to federal court.[52] There is near agreement among the appellate courts considering this general issue that Rule 11 does not apply to filings occurring in state court prior to removal.[53] The underlying rationale is, again, that the Rule is directed to the act of signing and filing at which time the Federal Rules of Civil Procedure generally do not apply because the act took place in state court.[54]

---

47. Herron v. Jupiter Transp. Co., 858 F.2d 332, 336 (6th Cir. 1988).

48. *Compare* Flip Side Prod., Inc. v. Jam Prod., Ltd., 843 F.2d 1024, 1036 (7th Cir. 1988) *with Pantry Queen Foods, Inc.*, 809 F.2d at 454; *compare* City of Yonkers v. Otis Elevator Co., 844 F.2d 42, 49 (2d Cir. 1983) *with Oliveri*, 803 F.2d at 1274-75.

49. *See Thomas*, 836 F.2d at 875; *Gaiardo*, 835 F.2d at 484; *Pantry Queen Foods, Inc.*, 809 F.2d at 454.

50. 28 U.S.C. § 1927 (1980).

51. FED. R. CIV. P. 26(g). In addition, *see* FED. R. CIV. P. 56(g) (affidavits with summary judgment motions); Hall v. Cole, 412 U.S. 1, 15 (1973) (inherent power of district court). *See generally Thomas*, 836 F.2d at 870 n.3, 875 & n.12.

52. For the provisions applicable to removal, see generally 28 U.S.C. §§ 1441-52 (1984 & Supp. 1989).

53. *E.g.*, Hurd v. Ralphs Grocery Co., 824 F.2d 806, 808-09 (9th Cir. 1987); Stiefvater Real Estate, Inc. v. Hinsdale, 812 F.2d 805, 809 (2d Cir. 1987); Kirby v. Allegheny Beverage Corp., 811 F.2d 253, 256-57 (4th Cir. 1987). Of course, Rule 11 does apply to filings in federal court following removal. *Id.*

54. *Stiefvater Real Estate, Inc.*, 812 F.2d at 809, *Kirby* , 811 F.2d at 256-57. *See* FED. R. CIV. P. 1 & 81(c).

The situation in the Fifth Circuit, however, is not totally clear. In Robinson v. National Cash Register Co., 808 F.2d 1119 (5th Cir. 1987), involving a removed action dismissed upon res judicata grounds, that court affirmed the imposition of a Rule 11 sanction against an attorney for plaintiffs who had signed the complaint filed in state court. *Id.* at 1121 & n.2, 1124-25, 1131. The decision seemed to assume the applicability of Rule 11 to complaints filed in proceedings that are later removed. *See* SANCTIONS, *supra* note 5, at 87. It should be noted, however, that the plaintiff had filed in federal district court a motion to remand the case to state court. The district court had treated this motion as a sham, describing its allegations as "nonsense." *See* Bookkeeper Tax Serv., Inc. v. National Cash Register Co., 598 F. Supp. 336, 338 (E.D. Tex. 1984). Moreover, the appellate court did not specifically consider the pre-removal filing issue in its Rule 11 discussion. Although the Fifth Circuit, en banc, subsequently rejected or accepted various other aspects of its Robinson panel, the pre-removal filing issue was not mentioned. *See Thomas*, 836 F.2d at 871-75 (rejecting), 876-77 (accepting).

More recently, however, the Fifth Circuit has stated in dictum, in the process of ordering a remand for reconsideration of sanctions in light of its *Thomas* decision, that:

> Rule 11 should not countenance sanctions for pleadings filed in state court in a case later removed to federal court unless, their deficiency having been promptly brought to the attention of the pleader after removal, he (or she) refuses to modify

We have seen the three general categories of conduct covering the multitude of litigation sins condemned by Rule 11. Before considering some specific random examples, it should be noted that it is easily conceivable for a particular act by an attorney or party to come within more than one of these categories at the same time. Consequently, there is the possibility of some overlapping among these otherwise distinct areas of conduct.[55] Moreover, in assessing whether there has been a violation of the requirement of a reasonable pre-filing investigation of both the facts and the law, the analysis is two-fold. The initial issue is whether the filing was actually so deficient that it was not well-grounded in fact or not warranted by law (or a good faith argument for its extension, modification or reversal). If so, the second issue is whether the pre-filing inquiry with respect thereto was not objectively reasonable under the circumstances.[56] Only if the answer is affirmative as to both is there a violation of Rule 11.

With those propositions in mind the following specific random examples are offered to present some of the flavor of a Rule 11 violation. The first category as to the underlying facts has been held to include such conduct as the filing of a RICO counterclaim[57] on the basis of unverified hearsay,[58] the filing of a complaint knowing that it lacked a factual foundation for subject matter jurisdiction,[59] and suing the wrong person of the same name where the only inquiry involved looking in the area telephone book.[60] In addition, an inadequate factual inquiry into such things as the existence of perjury in an action to set aside a jury verdict[61] and a claim of improper affixing of a party's signature to documents in a copyright infringement case[62] have been held to come within this type of proscribed conduct.

The second category dealing with the law encompasses such actions as plaintiff's attorney seeking removal to federal court of plaintiff's own state court suit,[63] the frivolous assertion of either a claim barred by the statute of limitations[64] or the statute of limitations as a defense,[65] as well as a suit clearly barred by either *res judicata*[66] or collateral estoppel.[67] It also applies to such

---

them to conform to Rule 11. Rule 11 does not apply to conduct that occurred in state court before removal.

Foval v. First Nat'l Bank of Commerce in New Orleans, 841 F.2d 126, 130 (5th Cir. 1988).

55. *See* United States v. Milam, 855 F.2d 739, 742 (11th Cir. 1988).

56. *See* Calloway v. Marvel Entertainment Group, 854 F.2d 1452, 1470 (2d Cir. 1988), *rev'd in part on other grounds, sub nom.*, Pavelic & LeFlore v. Marvel Entertainment Group, 110 S. Ct. 456 (1989). *See also* Hudson v. Moore Business Forms, Inc., 827 F.2d 450, 456-58 (9th Cir. 1987).

57. Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. § 1961 (1970).

58. Chapman & Cole v. Itel Container Int'l B.V., 865 F.2d 676, 685 (5th Cir. 1989).

59. Orange Prod. Credit Ass'n v. Frontline Ventures Ltd, 792 F.2d 797, 800 (9th Cir. 1986).

60. Callahan v. Schoppe, 864 F.2d 44 (5th Cir. 1989).

61. Cleveland Demolition Co., Inc., v. Azcon Scrap Corp., 827 F.2d 984, 987-88 (4th Cir. 1987).

62. *Calloway*, 854 F.2d at 1470-73.

63. Ballard's Serv. Center v. Transue, 865 F.2d 447 (1st Cir. 1989).

64. Napier v. Thirty or More Unidentified Federal Agents, 855 F.2d 1080, 1087-88, 1091 (3d Cir. 1988).

65. *Milam*, 855 F.2d at 740-41, 743-45.

66. Robinson v. National Cash Register Co., 808 F.2d 1119, 1121, 1124-25, 1131 (5th Cir. 1987).

conduct as an inadequate legal inquiry in a suit for breach of an employment contract where the employment was terminable-at-will under state law.[68]

The final type of Rule 11 violation is that of filing for an improper purpose. In citing *Browning Debenture Holders' Committee v. DASA Corp.*,[69] the Advisory Committee indicated that this category "recognizes that the litigation process may be abused for purposes other than delay."[70] Presumably this could include those actions condemned by the *Browning Debenture* court, such as a misleading motion to add parties, motion for reargument made almost one-half year after denial of summary judgment, and the issuance of dragnet subpoenas, in addition to delay for discovery never undertaken.[71]

Filings for purposes of delay are obviously within this type of proscribed conduct. Thus, where a defendant, solely for purposes of delay, had filed a motion to set aside a stipulation dismissing a debt collection suit, Rule 11 sanctions were properly imposed.[72] Likewise, the government's motion to remand to the Secretary of Health and Human Services for further administrative review of a social security disability benefits claim was sanctionable where it deliberately misstated the applicable law and was probably filed for purposes of delay.[73]

The requisite improper purpose has also easily been found to exist where the purpose behind the filing included harassment of the opposing party. Thus, it has been applied to a suit obviously barred by *res judicata* where filed to harass the defendants.[74] Likewise, the requisite improper purpose was found to exist as to the inflated damages clause portion of a counterclaim filed in order to harass and retaliate against the plaintiff and to deter similar suits from being brought.[75] Also, a legally baseless motion for Rule 11 sanctions filed to harass plaintiff's counsel has itself been sanctioned.[76] Even more serious in nature, the filing of a section 1983 claim[77] against a judge by an attorney in order to compel that judge to recuse himself in other litigation where that attorney was representing a party has been sanctioned under the improper purpose prong of Rule 11.[78]

Finally, the "improper purpose" category could be applied to such miscellaneous type conduct as the filing of a motion for summary judgment where the movant knew from prior discovery that a genuine issue of material

---

67. Heuttig & Schromm, Inc. v. Landscape Contractors Council, 790 F.2d 1421, 1426-27 (9th Cir. 1986).

68. Ring v. R.J. Reynolds Indus., Inc., 597 F. Supp. 1277 (N.D. Ill. 1984), *aff'd without opinion*, 804 F.2d 143 (7th Cir. 1986).

69. 560 F.2d 1078 (2d Cir. 1977).

70. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198 (1983).

71. *Browning Debenture Holders' Comm.*, 560 F.2d at 1088-89. *See generally*, SANCTIONS, *supra* note 5, at 6-7.

72. Chevron, U.S.A., Inc. v. Hand, 763 F.2d 1184 (10th Cir. 1985). *See also* Ahern v. Central Pac. Freight Lines, 846 F.2d 47, 49-50 (9th Cir. 1988).

73. Larkin v. Heckler, 584 F. Supp. 512, 513-14 (N.D. Cal. 1984).

74. Cannon v. Loyola Univ. of Chicago, 784 F.2d 777 (7th Cir. 1986), *cert. denied*, 479 U.S. 1033 (1987).

75. *Hudson*, 827 F.2d at 456, 458.

76. Bygott v. Leaseway Transp. Co., 637 F. Supp. 1433, 1447-48 (E.D. Pa. 1986).

77. *See* 42 U.S.C. § 1983 (1989).

78. Chu By Chu v. Griffith, 771 F.2d 79 (4th Cir. 1985); Steinle v. Warren, 765 F.2d 95 (7th Cir. 1985).

fact existed,[79] and other filings involving a deliberate misrepresentation of law to,[80] or lack of factual candor with,[81] the court. Having dealt with some of the more significant aspects of the violation side of Rule 11, it is now time to turn our attention to the sanction side and how the Rule is to be enforced.

The Sanction Under Rule 11

Rule 11 provides that, if a paper is signed in violation of the rule, "the court, upon motion or upon its own initiative, shall impose . . . an appropriate sanction . . . ."[82] From this language it is clear that the court can take action under Rule 11 upon the motion of either party or *sua sponte*. In addition, based upon the words "shall impose," there is general agreement that sanctions are mandatory. A court must impose some type of sanction if it has determined that a violation has occurred.[83] This is in accordance with the Advisory Committee's comments that the words "shall impose" are there to "focus the court's attention on the need to impose sanctions for pleading and motion abuse"[84] and "to reduce the reluctance of courts to impose sanctions . . . by emphasizing the responsibilities of the attorney and reinforcing those obligations by the imposition of sanctions."[85]

Although the theories of punishment and compensation (or cost-shifting) have each been advanced as the rationale for amended Rule 11,[86] there is now a growing consensus that the primary or principal purpose, if not punishment,[87] is at least *to deter* attorneys and parties from engaging in litigation abuse.[88]

---

79. *See* Goka v. Bobbitt, 862 F.2d 646, 650-51 (7th Cir. 1988). This also violates the factual prong of Rule 11. *Id. See supra* text accompanying note 55. For a consideration of the proper relationship of summary judgement to Rule 11, see Note, *A Genuine Ground in Summary Judgement for Rule 11*, 99 YALE L.J. 411 (1989).

80. *See* Jorgenson v. County of Volusia, 846 F.2d 1350, 1351-52 (11th Cir. 1988). This could likewise violate the legality prong of Rule 11. *See supra* text accompanying note 55.

81. *See* Blackwell v. Dep't of Offender Rehabilitation, 807 F.2d 914, 915 (11th Cir. 1987), *aff'g*, 609 F. Supp. 772, 775 (S.D. Ga. 1985).

82. FED. R. CIV. P. 11.

83. *E.g., Thomas*, 836 F.2d at 876; Cabell v. Petty, 810 F.2d 463, 466 (4th Cir. 1987); *Unioil, Inc.*, 809 F.2d at 559; Albright v. Upjohn Co., 788 F.2d 1217, 1221-22 (6th Cir. 1986); Westmoreland v. CBS, Inc., 770 F.2d 1168, 1174-75 (D.C. Cir. 1985); *Eastway Constr. Corp.*, 762 F.2d at 254 & n.7. *But see* Brown v. Capitol Air, Inc., 797 F.2d 106, 108 (2d Cir. 1986); Mossman v. Roadway Express, Inc., 789 F.2d 804, 806 (9th Cir. 1986).

84. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983).

85. *Id.* at 198.

86. *Compare, e.g.*, Schwarzer, *supra* note 2, at 185, 201 (emphasizing punishment) *with* Miller & Culp, *Litigation Costs, Delay Prompted the New Rules of Civil Procedure*, Nat'l Law Journal, Nov. 28, 1983, at 34, col. 2 (cost-shifting); Sifton, *Response to a Practitioner's Commentary on the Actual Use of Amended Rule 11*, 54 FORDHAM L. REV. 28, 29-31 (1985) (cost-shifting). The Seventh Circuit originally adopted the latter cost or fee-shifting theory and has persisted in that view. *See* Borowski v. DePuy, Inc., 876 F.2d 1339, 1342-43 (7th Cir. 1989); Hamer v. County of Lake, 871 F.2d 58, 60 (7th Cir. 1989); Hays v. Sony Corp., 847 F.2d 412, 419 (7th Cir. 1988). Other purposes include education in regard to professional responsibility. *See* S. BURBANK, *supra* note 5, at 38.

87. A number of courts have at times indicated that punishment and deterrence are both purposes behind Rule 11 without concluding as to which has primacy. *See, e.g., Oliveri*, 803 F.2d at 1281; *Westmoreland*, 770 F.2d at 1180. In addition, the Advisory Committee notes state that "[t]he detection and *punishment* of a violation of the signing requirement, encouraged by the amended rule, is part of the court's responsibility. . . ." FED. R. CIV. P. advisory committee notes, 97 F.R.D. 188, 200 (1983) (emphasis added).

88. *See, e.g.*, Doering v. Union County Bd. of Chosen Freeholders, 857 F.2d 191, 194 (3d Cir. 1988); Mihalik v. Pro Arts, Inc., 851 F.2d 790, 794 (6th Cir. 1988); Stewart v.

Indeed, the Advisory Committee has specifically stated that the use of the word "sanctions" in the caption to Rule 11 "stresses a *deterrent* orientation in dealing with improper pleadings, motions or other papers."[89] Thus, whatever the effect of the sanction in a particular case—whether it be considered punishment of the offender or compensation to the victim for costs incurred (cost-shifting)--its ultimate purpose is *deterrence* of the misuse and abuse of the litigation process by lawyers and parties.[90] That the principal purpose is not to compensate is supported by the fact that the amount of a monetary sanction payable to the victim can be either lesser or greater than the reasonable actual costs incurred in defending against the offending paper in question.[91] The Supreme Court has now ratified that growing consensus by apparently accepting the view that the purpose of Rule 11 is punishment, retribution and/or deterrence, instead of reimbursement.[92]

Where a violation has occurred, the Rule requires the court to determine "an appropriate sanction, which may include an order to pay to the other party . . . the amount of the reasonable expenses incurred because of the filing . . . including a reasonable attorney's fee."[93] It is not surprising that, with this specific language of authorization, the most common type of sanction imposed is that of costs, including attorney fees, in some amount.[94] Consequently, it appears that Rule 11 constitutes another important exception to the traditional

---

American Int'l Oil & Gas Co., 845 F.2d 196, 201-02 (9th Cir. 1988); *Thomas*, 836 F.2d at 877; *Brown*, 830 F.2d at 1438; *Donaldson*, 819 F.2d at 1556; *In re* Yagman, 796 F.2d 1165, 1184 (9th Cir.), *as amended*, 803 F.2d 1085 (9th Cir. 1986), *cert. denied*, 484 U.S. 963 (1987); *Westmoreland*, 770 F.2d at 1179-80; S. BURBANK, *supra* note 5, at 12; Schwarzer, *supra* note 5, at 1020 & n.31; Levin & Sobel, *supra* note 5, at 593; Nelken, *supra* note 5, at 1325; S. KASSIN, *supra* note 5, at ix, x, 26-27, 29, 31, 45-46; *The Dynamics of Rule 11*, *supra* note 5, at 328-29. *See also* Fauber v. Kem Transp. & Equip. Co., Inc. 876 F.2d 327, 333 (3d Cir. 1989); Dobbs, *Ending Punishment in "Punitive" Damages: Deterrence-Measured Remedies*, 40 ALA. L. REV. 831, 839-40 & n.25 (1989).

89. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199-200 (1983) (emphasis added). See Letter of Mansfield, *supra* note 1, at 192 ("A healthy deterrent against costly meritless maneuvers. . . .").

90. *See Thomas*, 836 F.2d at 877; *Donaldson*, 819 F.2d at 1556.

91. *Compare, e.g., Stewart* , 845 F.2d at 201-02 (lesser amount of one-half the reasonable fees); Taylor v. Prudential-Bache Sec., Inc., 594 F. Supp. 226, 228-29 (N.D.N.Y. 1984), *dismissed without opinion*, 751 F.2d 371 (2d Cir. 1984) (reducing reasonable and realistic request by 50%) *with* Doyle v. United States, 817 F.2d 1235 (5th Cir.), *cert. denied sub nom.*, Vanya v. United States, 484 U.S. 854 (1987) (award of 25 times the actual attorney fees and costs incurred by the government in defending frivolous *pro se* taxpayer class action type suit). *See* Frantz v. United States Powerlifting Fed., 836 F.2d 1063, 1066 (7th Cir. 1987); *Eastway Constr. Corp.*, 821 F.2d at 122-23; SANCTIONS, *supra* note 5, at 92.

92. *See* Pavelic & LeFlore v. Marvel Entertainment Group, 110 S. Ct. 456, 459, 460 (1989).

93. FED. R. CIV. P. 11.

94. *See, e.g.*, Gagliardi v. McWilliams, 834 F.2d 81, 82 (3d Cir. 1987); Donaldson, 819 F.2d at 1557; S. KASSIN, *supra* note 5, at 39-40; Joseph, *The Trouble With Rule 11*, 73 A.B.A. J. 87, 90 (1987); Nelken, *supra* note 5, at 1333. This may include not only the costs and attorney fees incurred by the victim in defending against the offending filing, but also in obtaining the Rule 11 award. *See, e.g.*, K.W. Thompson Tool Co., Inc. v. United States, 656 F. Supp. 1077, 1086 (D.N.H. 1987), *aff'd*, 836 F.2d 721 (1st Cir. 1988) (Rule 11 sanction not appealed). *See also infra* notes 132-39 and accompanying text. As to whether attorneys can insure against such potential liability for monetary Rule 11 sanctions, see Note, *Insuring Rule 11 Sanctions*, 88 MICH. L. REV. 344 (1989).

American rule that parties to litigation pay their own respective attorney's fees regardless of the outcome of the case.[95]

But, as the Rule refers to an "appropriate" sanction that "may" include attorney's fees, it is clear that this is not exclusive and the potential range of sanctions is quite broad. Thus, other approved monetary Rule 11 sanctions have included fines paid directly to the court[96] as well as lost interest that would have accrued on a state court judgment but for the defendant having filed a frivolous last-minute removal petition.[97]

Likewise, the possible nonmonetary sanctions are many and varied, including an oral reprimand in private or in open court,[98] a written reprimand that is either published[99] or unpublished,[100] circulation of a written reprimand among the offender's law partners or associates,[101] consulting with a skilled attorney or attendance at court sessions,[102] or requiring attendance at continuing legal education seminars.[103] Less frequently utilized nonmonetary sanctions have consisted of deeming allegations admitted,[104] striking of the

---

95. For discussions of the American Rule and the exceptions to it, see Alyeska Pipeline Serv. Co. v. Wilderness Soc'y, 421 U.S. 240, 247-68 (1975); Schwarzer, *supra* note 2, at 205-06. Because the most common Rule 11 sanction requires the offending party to pay part or all of the victim's reasonable actual attorney fees does not mean that merely being on the losing side, without more, creates such an obligation. Under the Rule a sanction is mandated only where there is a signing and filing of a paper in violation of the Rule 11 certification. Thus, being on the losing side is not enough. *See* Teamsters Local Union No. 430 v. Cement Express, Inc., 841 F.2d 66, 68 (3d Cir. 1988). If it were, the American rule on the federal level would be turned on its head. Beyond that, Rule 11 sanctions do not depend upon who is the prevailing party as to the underlying merits of the case; instead, Rule 11 is blind to such considerations. *See* SANCTIONS, *supra* note 5, at 3. Thus, Rule 11 sanctions can be imposed even upon the ultimate winner in the litigation. *See* Sheets v. Yamaha Motors Corp., U.S.A., 657 F. Supp. 319, 321, 328 (E.D. La. 1987), *aff'd and rem'd in part*, 849 F.2d 179 (5th Cir. 1988); Perkinson v. Houlihan's/D.C., Inc., 108 F.R.D. 667, 674-77 (D.D.C. 1985), *aff'd, rev'd & remanded in part, sub. nom.* Perkinson v. Gilbert/Robinson, Inc., 821 F.2d 686 (D.C. Cir. 1987).

96. *E.g., Milam*, 855 F.2d 739; *Jorgenson*, 846 F.2d 1350. *See Frantz*, 836 F.2d at 1066. According to a 1982 study, the cost to the government (and, hence, to the taxpayer) of one hour spent by a federal judge in a tort case was nearly $600. Levin & Collier, *Containing the Cost of Litigation*, 37 RUTGERS L. REV. 219, 226-27 (1985). Some courts have imposed sanctions in the form of fines based upon this $600 per hour cost for wasting judicial resources in baseless litigation, in addition to other Rule 11 sanctions. *E.g.*, Harris v. Marsh, 679 F. Supp. 1204, 1324-25, 1387-89, 1392 (E.D.N.C. 1987); Thiel v. First Fed. Sav. & Loan Ass'n, 646 F. Supp. 592, 598 (N.D. Ill. 1986), *dismissed & aff'd in part without opinion*, 828 F.2d 21 (7th Cir. 1987); Robinson v. Moses, 644 F. Supp. 975, 982-83 (N.D. Ind. 1986); Dominguez v. Figel, 626 F. Supp. 368, 374 (N.D. Ind. 1986); Advo System, Inc. v. Walters, 110 F.R.D. 426, 433 (E.D. Mich. 1986).

97. Davis v. Veslan Enterprises, 765 F.2d 494, 497, 501 (5th Cir. 1985) (almost $33,000 in lost interest).

98. *See Eastway Constr. Corp.*, 821 F.2d at 125 (Pratt, J., dissenting).

99. *See In re* Disciplinary Action Against Mooney, 841 F.2d 1003, 1006 (9th Cir. 1988); *In re* Disciplinary Action Against Curl, 803 F.2d 1004, 1007 (9th Cir. 1986).

100. *See* Allen v. Faragasso, 585 F. Supp. 1114, 1119 (N.D. Cal. 1984) (copy of written reprimand placed in the attorney's court file in addition to appearing in a published opinion); Schwarzer, *supra* note 2, at 202.

101. *E.g.*, Larkin v. Heckler, 584 F. Supp. 512, 514 (N.D. Cal. 1984): Heuttig & Schromm, Inc. v. Landscape Contr. Council, 582 F. Supp. 1519, 1522-23 (N.D. Cal. 1984), *aff'd*, 790 F.2d 1421 (9th Cir. 1986).

102. *See Eastway Constr. Corp.*, 637 F. Supp. at 566.

103. Stevens v. City of Brockton, 676 F. Supp. 26, 27 (D. Mass. 1987).

104. *See* Johnson v. Secretary, Dep't of Health & Human Serv., 587 F. Supp. 1117, 1121 (D.D.C. 1984).

offending paper,[105] dismissal with prejudice,[106] and injunctions,[107] as well as the temporary barring of an attorney from appearing in court,[108] or other discipline.[109]

A. Factors Considered in the Determination of Sanctions

As a general matter, the district court has great flexibility in determining the type of sanction to impose and the amount thereof.[110] Such determinations are reviewed by appellate courts under an abuse of discretion standard.[111] In addition, many courts have espoused the view that the district court should generally select the least severe sanction that is adequate to carry out the goal of Rule 11.[112]

Keeping those basic propositions in mind, there is a wide variety of specific factors that can be relevant to these determinations. Although subjective bad faith is no longer required in order for there to be a violation of Rule 11,[113] it is an important element is assessing what the sanction should be,[114] and the Advisory Committee itself has endorsed this consideration.[115]

Other factors that could be considered, some of which are obviously more appropriate to monetary than to nonmonetary sanctions, include the following: (1) the ability to pay;[116] (2) the financial resources of the respective

---

105. National Ass'n of Radiation Survivors v. Walters, 111 F.R.D. 595 (N.D. Cal. 1986).

106. American Inmate Paralegal Ass'n, Inc. v. Cline, 859 F.2d 59 (8th Cir.), *cert. denied*, 109 S. Ct. 565 (1988) (civil rights suit by *pro se* prison inmates based upon no access to typewriter dismissed with prejudice where there was voluminous filing of frivolous documents which were all typed).

107. Farguson v. MBANK Houston, N.A., 808 F.2d 358, 360 (5th Cir. 1986); Van Sickle v. Holloway, 791 F.2d 1431, 1437 (10th Cir. 1986). This sanction is particularly appropriate where a party has filed a multiplicity of suits to vex and harass the defendant and is either judgment proof or otherwise unamenable to monetary sanctions. *See Farguson*, 808 F.2d at 360; *Van Sickle*, 791 F.2d at 1437. *See also In re* Martin—Trigona, 737 F.2d 1254, 1262-64 (2d Cir. 1984). The court imposing such a sanction, however, should take care not to cut off totally the access of the offender to the federal court. *See Van Sickle*, 791 F.2d at 1437 n.6.

108. *See* Schwarzer, supra note 2, at 204; Note, *Plausible Pleadings: Developing Standards For Rule 11 Sanctions*, 100 HARV. L. REV. 630, 634-35 n.19 (1987).

109. *See Donaldson*, 819 F.2d at 1557 n.7 (suspension or disbarment); Schwarzer, *supra* note 2, at 204.

110. *See Thomas*, 836 F.2d at 876-78; *Eastway Constr. Corp.*, 821 F.2d at 122; *Donaldson*, 819 F.2d at 1557; *Unioil, Inc.*, 809 F.2d at 559; *Westmoreland*, 770 F.2d at 1174, 1175 . The Advisory Committee comments confirm this flexibility. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983) ("The court . . . retains the necessary flexibility to deal appropriately with violations of the rule. It has discretion to tailor sanctions to the particular facts of the case. . . ."). *See* Cavanagh, *supra* note 5, at 501.

111. *E.g., Thomas*, 836 F.2d at 871-73; *Eastway Constr. Corp.*, 821 F.2d at 122; *Unioil, Inc.*, 809 F.2d at 557; *Westmoreland*, 770 F.2d at 1178.

112. *E.g., Thomas*, 836 F.2d at 878; *Brown*, 830 F.2d at 1437; Cabell v. Petty, 810 F.2d 463, 466-67 (4th Cir. 1987); *Eastway Constr. Corp.*, 637 F. Supp. at 565. *See* S. BURBANK, *supra* note 5, at xv, 97-98; Schwarzer, *supra* note 2, at 201.

113. *See supra* text accompanying notes 17-19.

114. *See, e.g., Cabell*, 810 F.2d at 466; *Eastway Construction Corp.*, 637 F. Supp. at 573, 578.

115. FED. R. CIV. P. 11 Advisory Committee Notes, 97 F.R.D. 198, 200 (1983).

116. Doering v. Union County Board of Chosen Freeholders, 857 F.2d 191, 195-96 (3d Cir. 1988). *See Oliveri*, 803 F.2d at 1281. This is in accordance with deterrence being the primary goal of Rule 11 instead of compensation. Thus, in the case of a monetary award, the

parties[117] and the need of the victim for compensation;[118] (3) whether one is a first offender;[119] (4) the experience and training (or lack thereof) of the offender and the need for expertise in the area of law in question;[120] (5) the gravity, or degree of frivolousness, of the violation;[121] (6) whether the offender has diminished responsibility;[122] (7) *pro se* status[123] and any other factors bearing upon what is a suitable tailoring of the sanction to the violation in the particular case.[124] Overall, it is well to remember, insofar as lawyer violations are concerned, that

> a violation may stem from a variety of causes: inexperience, incompetence, neglect, wilfulness or deliberate choice. The need for punishment and deterrence is a function of the cause of the violation. In assessing the cause, the judge should consider not only the circumstances of the particular violation but also the factors bearing on the reasonableness of the conduct, such as experience and past performance of the lawyer and his firm, and the general standard of conduct of the bar of the court.[125]

In the case of a monetary sanction encompassing costs and attorney fees in some amount, there is an additional factor to be taken into account—the duty of the offended person to mitigate the incurrence of such expenses. This duty is implicit in the language of Rule 11 which permits a sanction consisting of "the *reasonable* expenses incurred *because of the filing* of the . . . paper, including a *reasonable* attorney's fee."[126] Thus, the actual expenses must be both reasonable and caused by the filing.[127]

Most courts applying this duty of mitigation have indicated that it has at least two aspects: (1) the need to correlate the response to the degree of frivolousness of the offending paper (presumably, the greater the frivolousness, the lesser the response necessary);[128] and (2) the need to bring the violation to the attention of the offender and the court as soon as possible, utilizing the least expensive and most efficient means.[129] The first element exists to ensure that

---

amount may be less than the reasonable actual costs incurred by the victim, due to this factor of ability to pay, among others. *See supra* text accompanying notes 86-92.

117. *See Calloway*, 854 F.2d at 1478; *Brown*, 830 F.2d at 1440.

118. *Eastway Constr. Corp.*, 637 F. Supp. at 574.

119. *Id.* at 573.

120. *See Calloway*, 854 F.2d at 1479 n.11; *Brown*, 830 F.2d at 1439; *Eastway Constr. Corp.*, 637 F. Supp. at 573.

121. *See Calloway*, 854 F.2d at 1476; *Eastway Constr. Corp.*, 637 F. Supp. at 574-75.

122. *See Calloway*, 854 F.2d at 1477.

123. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983) ("When a party is not represented by counsel, the absence of legal advice is an appropriate factor to be considered.").

124. *See Doering*, 857 F.2d at 194-97 & n.6. *See generally* Schwarzer, *supra* note 2, at 200-04; S. BURBANK, *supra* note 5, at 40.

125. Schwarzer, *supra* note 2, at 201.

126. *Id.* at 202 (emphasis added).

127. *Id.* For the view that there should be no formal duty of mitigation, see S. BURBANK, *supra* note 5, at 40.

128. *See, e.g., Thomas*, 836 F.2d at 879; INVST Fin. Group, Inc. v. Chem-Nuclear Sys., Inc., 815 F.2d 391, 404 & n.6 (6th Cir. 1987).

129. *See, e.g.*, Dubisky v. Owens, 849 F.2d 1034, 1037-39 (7th Cir. 1988); Mary Ann Pensiero, Inc. v. Lingle, 847 F.2d 90, 99-100 (3d Cir. 1988). *See also* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983).

the offended person does not take advantage of the situation by "overlawyering" the problem, thereby unnecessarily increasing attorney fees.[130] The second element not only helps to reduce the expenses of responding but also is a recognition of the need to conserve judicial resources and to deter future violations.[131]

A few courts considering the issue have held that a Rule 11 monetary sanction may include attorney fees incurred on appeal with respect to success in defending an award,[132] or overturning its denial,[133] by the district court under Rule 11. The basis for this under the Rule is that, in such a situation, the appellate expenses were "incurred because of the filing of the paper . . . ."[134] The underlying policy reason is that, if it were otherwise, there might be insufficient incentive to defend, or to seek to overturn the denial of, such an award if the appellate expenses would nearly cancel out or exceed the amount of any district court award.[135] But there are substantial arguments against including these appellate expenses within the Rule 11 monetary sanction[136] such as, *inter alia,* potential inconsistency with Federal Rule of Appellate Procedure 38 under which damages, costs and attorney fees may be awarded for a frivolous appeal.[137] Moreover, what little empirical evidence there is does not support the lack of sufficient incentive argument.[138] The Supreme Court will consider this issue, and likely resolve it, in the near future.[139]

B. Monetary Sanctions Against Whom?

Rule 11 provides that the sanction for filing the offending paper may be imposed against "the person who signed it, a represented party, or both . . . ." The Advisory Committee's comments indicate that, although the attorney signed the paper in question, the court should have the discretion to sanction either, or both, the attorney and client, and that it was the drafters' intention thereby to bring "Rule 11 in line with practice under Rule 37 . . . ."[140] In addition, the court can sanction an unrepresented party who signed the document.[141]

The courts have not hesitated in carrying out this mandate, assessing monetary sanctions solely against either the attorney[142] or the client,[143]

---

130. *See INVST Fin. Group, Inc.*, 815 F.2d at 404 & n.6; *Oliveri*, 803 F.2d at 1280.
131. *See supra* note 129.
132. Danik, Inc. v. Hartmarx Corp., 875 F.2d 890, 897-898 (D.C. Cir. 1989), *cert. granted sub. nom.* Cooter & Gell v. Hartmarx Corp., 110 S. Ct. 275 (1989); Muthig v. Brant Point Nantucket, Inc., 838 F.2d 600, 607-08 (1st Cir. 1988). *See* Hays v. Sony Corp. of Am., 847 F.2d 412, 419-20 (7th Cir. 1988).
133. *Westmoreland*, 770 F.2d at 1179-80. *See The Dynamics of Rule 11*, *supra* note 5, at 331-32.
134. *See supra* notes 132-33.
135. *See supra* note 133.
136. *See* S. BURBANK, *supra* note 5, at 49-52.
137. *Id.* at 52.
138. *Id.* at 50-51.
139. *See Cooter & Gell*, 58 U.S.L.W. 3252-53.
140. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983).
141. *Id.*
142. *E.g.*, Jorgenson v. County of Volusia, 846 F.2d 1350 (11th Cir. 1988); *Unioil, Inc.*, 809 F.2d 548; Blackwell v. Department of Offender Rehab., 807 F.2d 914 (11th Cir. 1987); Dalton v. United States, 800 F.2d 1316, 1318, 1320 (4th Cir. 1986).
143. *E.g.*, Chevron, U.S.A., Inc. v. Hand, 763 F.2d 1184, 1187 (10th Cir. 1985). *See* SANCTIONS, *supra* note 5, at 136.

imposing joint and several liability,[144] or some combination.[145] In this process of allocating sanctions, the court is, of course, engaged in fixing the responsibility or blame for the violation.[146]

Where the violation is only that of a professional dereliction by the attorney in which the client did not knowingly participate or authorize, it would seem appropriate to sanction only the attorney and to prevent reimbursement by the client.[147] In any event, attorneys practicing in federal court are held to the minimum standards of competence necessary to comply with Rule 11.[148] Therefore, in the usual situation it would appear that the lawyer should at least be included in the sanctioned group except where, for example, the client lied to the attorney[149] or otherwise misrepresented the facts, and this was not discoverable from a reasonable pre-filing inquiry in the particular circumstances.[150] In addition, the allocation of blame may at times be difficult and unclear. In such a context it may be appropriate for a court simply to assess the monetary sanction against both the lawyer and client, jointly and severally, leaving them to sort it out.[151]

In the case of unrepresented parties, the court has some discretion to consider the special circumstances frequently arising from that *pro se* status. Such circumstances could include the lack of legal skills, or the absence of legal advice, in determining, respectively, the existence of a Rule 11 violation[152] or the nature and severity of any sanction to be imposed.[153] The range of potentially effective sanctions, however, is not as broad as those applicable to an attorney since many of the possible sanctions are peculiarly related to the legal profession.[154] Consequently, the courts emphasize monetary sanctions in this

---

144. *E.g.*, Robinson v. National Cash Register Co., 808 F.2d 1119, 1121, 1132 & n.22 (5th Cir. 1987); Kendrick v. Zanides, 609 F. Supp. 1162, 1173 (N.D. Cal. 1985); Florida Monument Builders v. All Faiths Memorial Gardens, 605 F. Supp. 1324 (S.D. Fla. 1984).

145. *E.g., Eastway Constr. Corp.*, 821 F.2d at 124. *See Calloway*, 854 F.2d at 1476-77.

146. *See, e.g., Calloway*, 854 F.2d at 1477; *Eastway Constr. Corp.*, 637 F. Supp. at 569. *See generally* Braley v. Campbell, 832 F.2d 1504, 1514 (10th Cir. 1987) (en banc) ("[T]he determination to impose sanctions on an attorney . . . involves . . . placing the blame.").

147. *See Calloway*, 854 F.2d at 1474-75; Schwarzer, *supra* note, at 203; *The Dynamics of Rule 11*, *supra* note 5, at 331 n.228. Non-exclusive examples of this could include the filing of a motion for summary judgment although knowing from prior discovery that a genuine issue of material fact existed. *See* Goka v. Bobbitt, 862 F.2d 646, 650-51 (7th Cir. 1988). It could also apply to a misstatement or misrepresentation of the law. *See Jorgenson*, 846 F.2d 1350; Thornton v. Wahl, 787 F.2d 1151, 1154 (7th Cir.), *cert. denied*, 479 U.S. 851 (1986).

148. *Calloway*, 854 F.2d at 1474.

149. *See* Friedgood v. Axelrod, 593 F.2d 395, 397-98 (S.D.N.Y. 1984).

150. It has been recommended by the Third Circuit Task Force on Rule 11 that courts should adopt a presumptive rule that Rule 11 sanctions will be imposed on the lawyer signing the violative paper. S. BURBANK, *supra* note 5, at xv, 98. Under this recommended presumption, reimbursement by the client would be forbidden where the lawyer's primary responsibility is clear, but otherwise leaving any re-allocation to private ordering. *Id.* at 98. This approach would reduce satellite litigation as well as lessen the dangers of the Rule to the attorney-client relationship such as conflict of interest. *Id.* at 30-31, 41-42.

151. *See Eastway Constr. Corp.*, 637 F. Supp. at 569; Schwarzer, *supra* note 2, at 203 . *See also Thornton*, 787 F.2d at 1154 ("Ordinarily we impose attorneys' fees on the party leaving party and lawyer to settle accounts.").

152. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199 (1983).

153. *See supra* note 152, at 200.

154. *See supra* text accompanying notes 93-109.

area.[155] It is true, nonetheless, that courts tend to be more lenient in their treatment of *pro se* litigants.[156] But they are not exempt from the duties of Rule 11,[157] and, particularly in more recent taxpayer protest cases, the courts have been quick to impose sanctions.[158]

For example, in *Doyle v. United States*,[159] some twenty-five employees had filed Forms W-4 claiming exemption from all income tax withholding. The Internal Revenue Service responded by directing the employer to disregard the invalid forms and imposed a $500 penalty against each employee.[160] These employees then filed a frivolous *pro se* class action suit against the Service requesting, *inter alia*, injunctive relief and huge compensatory and punitive damages. The total government expense incurred in getting the suit dismissed was $1,554.88 in costs and attorney's fees. The district court awarded a Rule 11 monetary sanction of $1,554.88 against *each* of the twenty-five employees, or a total amount to the government of $38,872.[161] In affirming the award, the Fifth Circuit clearly accepted both the punishment and deterrence purposes of Rule 11.[162] The appellate court indicated that this resolution, which required each *pro se* litigant to pay the cost of one's own frivolous conduct as if he or she had filed an individual law suit, achieved an appropriate balance. It avoided the danger of too severe a punitive sanction while at the same time eliminating "the incentive to huddle together in mass *pro se* lawsuits in order to minimize the costs of adverse attorney's fee awards."[163]

Whether the United States government as a party and its attorneys can be sanctioned under Rule 11 raises additional problems. There is nothing, however, either in the language of the Rule or in the Advisory Committee Notes, that would prevent its application in such case. But there is a question whether the doctrine of sovereign immunity would prohibit a monetary sanction. There is not much authority on point, but the few appellate courts considering this issue have held or indicated that a Rule 11 sanction of costs and attorney fees may be awarded against the government.[164]

One persuasive reason for this result is that sovereign immunity from attorneys' fee awards has been expressly waived by the Equal Access to Justice Act (EAJA).[165] That Act provides that the United States shall be liable for costs and attorney fees "to the same extent that any other party would be liable . . . under the terms of any *statute* which specifically provides for such an

---

155. *See* S. BURBANK, supra note 5, at 42.
156. Maduakolam v. Columbia Univ., 866 F.2d 53, 56 (2d Cir. 1989). *See* Cheek v. Doe, 828 F.2d 395, 397-98 (7th Cir.), *cert. denied*, 484 U.S. 955 (1987); *Farguson*, 808 F.2d at 359-60; United States v. Tarver, 642 F. Supp. 1109, 1112 (D. Wyo. 1986); SANCTIONS, *supra* note 5, at 60, 125, 166.
157. *See Cheek*, 828 F.2d at 397.
158. *Id.* at 397-98; Itz v. United States Tax Court, 60 A.F.T.R.2d 87-5113 (W.D. Tex. 1987).
159. 817 F.2d 1235 (5th Cir.), *cert. denied, sub nom.* Vanya v. United States, 484 U.S. 854 (1987).
160. *See* I.R.C. § 6682(a) (as amended by the Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 721, Aug. 13, 1981).
161. *Doyle*, 817 F.2d at 1236, 1237.
162. SANCTIONS, *supra* note 5, at 91-92.
163. *Doyle*, 817 F.2d at 1237-38.
164. Adamson v. Bowen, 855 F.2d 668, 670-72 (10th Cir. 1988). *See* United States v. Gavilan Joint Comminity College Dist., 849 F.2d 1246, 1247, 1250-51 (9th Cir. 1988).
165. 28 U.S.C. § 2412(b) (1981).

award."[166] Because the Federal Rules of Civil Procedure have the force of a federal statute,[167] the EAJA is broad enough to constitute a waiver of sovereign immunity for Rule 11 purposes.[168]

There was likewise sparse, but conflicting, appellate court authority as to whether the law partnership of which the signing attorney is a member should be liable, in addition to the signer, for monetary sanctions awarded as the result of a Rule 11 violation. In *Robinson v. National Cash Register Company*[169] monetary sanctions had been imposed by the lower court against not only the parties and the signing attorney but also against his non-signing partner, jointly and severally.[170] The non-signer's only connection with the case was an appearance at a pre-trial conference in which he did not participate meaningfully.[171] The Fifth Circuit reversed the sanction as to the non-signing attorney essentially on the basis that the text of the Rule and the Advisory Committee Notes both indicate that it is the signer who bears the entire responsibility for the violative paper.[172] In support of this position the court reasoned that a contrary view would require further inquiry into the relative culpability of non-signing attorneys who were somehow involved in the case.[173] This would create the very satellite litigation about which the drafters of Rule 11 were concerned.[174]

The Second Circuit reached a contrary conclusion in *Calloway v. Marvel Entertainment Group*[175] where it affirmed the imposition of Rule 11 monetary sanctions against not only the signing attorney but also his law partnership.[176] The reasons given for this result included, in addition to traditional partnership law principles, the fact that more than one person in the firm may have participated in the background research and preparation of the document even though only one signed it. Moreover, the signer may be only a junior attorney carrying out the instructions of his superior.[177] Finally, the Second Circuit thought that this would serve the underlying policy in that creating law firm responsibility would likely produce increased internal monitoring with resulting fewer violations.[178] By granting certiorari in the *Calloway* case,[179] the Supreme Court resolved this conflict. Emphasizing the plain language under which the sanction is to be imposed "upon the person who signed it" in the context of Rule 11 in its entirety, the Court held that the sanction could only

---

166. *Id.*
167. Sibbach v. Wilson & Co., 312 U.S. 1 (1941).
168. *Adamson*, 855 F.2d at 671, 672.
169. 808 F.2d 1119 (5th Cir. 1987).
170. *Id.* at 1121, 1125, 1131-32 & n.21.
171. *Id.* at 1125 & n.11, 1131.
172. *Id.* at 1129, 1131-32. This holding of Robinson has apparently been accepted by the Fifth Circuit sitting en banc. *See Thomas*, 836 F.2d at 875 & n.13.
173. *Robinson*, 808 F.2d at 1129.
174. *See supra* note 173; FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 201 (1983).
175. 854 F.2d 1452 (2d Cir. 1988).
176. *Id.* at 1478-81, 1483.
177. *Id.* at 1479. *See* Schwarzer, *supra* note 2, at 185-86.
178. *Calloway*, 854 F.2d at 1479-80.
179. *Sub. nom.* Pavelic & LeFlore v. Marvel Entertainment Group, 109 S. Ct. 1116 (1989).

be imposed upon the signing attorney and not also upon the law partnership for which he signed.[180]

It would seem that, where both sides in the litigation have engaged in violative conduct, the mandatory nature of Rule 11 sanctions would require that each side be independently penalized.[181] But any award of costs and attorney fees incurred by each side in defending against the other's offending paper might tend to wash out. This would, in effect, leave both sides unpunished and undeterred in the future. It has been suggested that this would be an appropriate occasion to sanction each side by a fine payable directly to the court as recompense for the wasting of judicial resources.[182] Another possible solution is for the court to consider nonmonetary sanctions, at least where the offenders are attorneys, in the form of reprimands or, perhaps, requiring both attorneys to attend remedial continuing legal education courses.[183]

In addressing this problem the Seventh Circuit has indicated that, ideally, competing violations should be independently sanctioned because the misconduct of one party does not do away with the interest in penalizing the opponent's separate violative act. Instead, only if the two actions deserve roughly equal treatment should they offset or cancel each other.[184] But other courts appear to take a "plague upon both your houses" type of approach in not sanctioning either side.[185]

C. The Procedures in Sanctioning

An extensive consideration of the procedures applicable to the imposition of sanctions is clearly beyond the scope of this Article. A few important aspects, however, are relevant and ought to be mentioned. First, except for the provision allowing the court to impose a sanction "upon motion or upon its own initiative," there is nothing in Rule 11 itself about the procedures to be utilized by the court. The Advisory Committee comments take up some of the slack by manifesting the idea that, although due process requisites must be satisfied, the sanction proceedings should be limited to the record, if possible; thus, discovery should be allowed only in extraordinary circumstances. This view of the Committee was based upon the perceived need to reduce satellite litigation over sanctions as well as the reality that, in most cases, the facts are already before the court due to the judge's participation in the main case.[186]

It seems clear, as stated in the Advisory Committee notes, that procedural due process is applicable to the imposition of sanctions.[187] It is not so clear,

---

180. Pavelic & LeFlore v. Marvel Entertainment Group, 110 S. Ct. 456, 458-60 (1989).
181. *See supra* text accompanying notes 82-85.
182. *See The Dynamics of Rule 11*, *supra* note 5, at 331. *See generally supra* note 96.
183. *See* Stevens v. City of Brockton, 676 F. Supp. 26, 27 (D. Mass. 1987).
184. *See In re* Central Ice Cream Co., 836 F.2d 1068, 1074 (7th Cir. 1987).
185. Woodcrest Nursing Home v. Local 144, Hotel, Hosp., Nursing Home & Allied Serv. Union, 788 F.2d 894, 897, 899 (2d Cir. 1986). *See* Mossman v. Roadway Express, Inc., 789 F.2d 804, 806 (9th Cir. 1986).
186. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 201 (1983).
187. *E.g., Donaldson*, 819 F.2d at 1558-59. *See Thomas*, 836 F.2d at 878 & n.17.

however, just what process is due. The general tenor of the Advisory Committee comments minimizes that constitutionally required procedure.[188]

In any event, it is fundamental that, absent extraordinary circumstances, procedural due process requires notice and an opportunity to be heard before any governmental deprivation of a property interest.[189] Attorneys and clients come within this protection when facing potential Rule 11 sanctions.[190] Some courts have determined that the due process notice requirement is satisfied, insofar as lawyers are concerned, by the mere existence of Rule 11 itself, at least where the complaint constitutes the violative filing due to the alleged lack of any basis in fact.[191] It has also been indicated that due process does not necessarily require a separate hearing[192] and that criminal contempt procedures are not generally applicable before monetary sanctions are awarded.[193] On the other hand, due process may require an evidentiary hearing in a particular case,[194] as, for example, when the imposition of a sanction depends upon facts genuinely in dispute.[195]

The Ninth Circuit has recently held, however, in *Tom Growney Equipment Corp., Inc. v. Shelley Irrigation Development, Inc.*[196] that due process requires specific notice be given of the court's intention to impose sanctions or that sanctions are being considered.[197] Thus, under this view the general notice created by Rule 11 is not enough. This seems to be the preferable position because it enables the potential sanctionee to better prepare a more focused defense or explanation of the questioned conduct. Moreover, the *Tom Growney* decision seemed to assume that the hearing prior to the imposition of any sanctions was to be an evidentiary one, where the document in question was a counterclaim for fraud and breach of contract allegedly filed without a reasonable pre-filing factual inquiry.[198] At the very least, it ordinarily would be improper as a matter of due process for a court to impose a Rule 11 sanction without any prior notice and without affording some opportunity to explain.[199]

Related to the due process notice element is the independent notice element apparently required under Rule 11. Although that Rule says nothing

---

188. The due process minimization approach of the Advisory Committee has been roundly criticized recently by the Third Circuit Task Force on Rule 11. *See* S. BURBANK, *supra* note 5, at 25-36. The report of the Task Force also asserted that this minimization view of the Advisory Committee "is entitled to little weight because it does not inform the interpretation of any provision of the Rule." *Id.* at 26.

189. Boddie v. Connecticut, 401 U.S. 371, 379 (1971).

190. *Donaldson*, 819 F.2d at 1558.

191. *E.g., id.* at 1560. *See* Lepucki v. Van Wormer, 765 F.2d 86, 88 (7th Cir. 1985).

192. *See Donaldson*, 819 F.2d at 1560 & n.12, 1561; Rogers v. Lincoln Towing Serv., Inc., 771 F.2d 194, 205-06 (7th Cir. 1985).

193. *Donaldson*, 819 F.2d at 1559 & n.10. *See* FED. R. CRIM. P. 42(b). *Contra*, Cotner v. Hopkins, 795 F.2d 900, 903 (10th Cir. 1986) (relying upon panel decision of *Donaldson*, 786 F.2d 1570).

194. *See Donaldson*, 819 F.2d at 1561.

195. *See Eastway Constr. Corp.*, 637 F. Supp. at 568.

196. Tom Growney Equip. Corp., Inc. v. Shelley Irrigation Dev., Inc., 834 F.2d 833 (9th Cir. 1987).

197. *Id.* at 836 & n.5. *See Thomas*, 836 F.2d at 881.

198. *See Tom Growney*, 834 F.2d at 836 & n.6.

199. *Id.* at 835-36. *See* Sanko Steamship Co., Ltd. v. Galin, 835 F.2d 51, 53-54 (2d Cir. 1987); S. BURBANK, *supra* note 5, at 31-35. *See also* Cleveland Board of Education v. Loudermill, 470 U.S. 532 (1985).

specifically about notice, the comments of the Advisory Committee state that, "[a] party seeking sanctions should give notice to the court and the offending party promptly upon discovering a basis for doing so."[200] The courts have generally approved this procedure with some specifically mandating such early notice.[201]

Intertwined with the early notice feature of Rule 11 is the specific timing of the sanction determination. The Advisory Committee Notes indicate that, although this is discretionary with the trial court, normally the determination with respect to pleadings should occur at the conclusion of the litigation while, in the case of motions, at or near the time the motion is decided.[202] This guideline tends to ignore, at least partially, one aspect of the primary purpose of Rule 11—that of specific deterrence of the offender from further abuse of the litigation process in the very case where it first occurs.[203] In the case of pleadings, the delay of the sanctions determination until the end of the litigation may result in the stacking of further violations in the interim, so that any ultimate sanction has had no specific deterrent effect in that case.[204] Consequently, some courts, while recognizing the general validity of the Advisory Committee's guidance, have indicated their approval of earlier determination in some situations or at least early notice of potential sanctions.[205]

Additionally, neither the Rule nor the Advisory Committee Notes say whether the district court should make specific findings and give reasons in connection with sanction determinations.[206] Such a requirement would greatly aid appellate review, however.[207] Even though specific findings and conclusions are generally not necessary in all Rule 11 cases,[208] the trend appears to be that they should be required at least where the sanction awarded is inherently substantial in amount, or it is substantial either in relation to the offense or in its general effect.[209]

---

200. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983).

201. E.g., Mary Ann Pensiero, Inc. v. Lingle, 847 F.2d 90, 99 (3d Cir. 1988) ("We will henceforth require prompt action by a litigant whenever a Rule violation appears."); *Thomas*, 836 F.2d at 880. *See* Dubisky v. Owens, 849 F.2d 1034, 1037-39 (7th Cir. 1988); *Yagman*, 796 F.2d at 1183-84. In the *Pensiero* case, the Third Circuit also adopted a supervisory rule for the circuit requiring litigants' motions for Rule 11 sanctions to be filed in the district court before the entry of a final judgment. 847 F.2d at 100.

202. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200-01 (1983).

203. *See supra* text accompanying notes 86-92. Specific deterrence refers to deterrence of a particular offender in the instant situation and in the future. General deterrence refers to deterrence of others in the future. *See* S. BURBANK, *supra* note 5, at 38, 43-45.

204. *See Yagman*, 796 F.2d at 1183.

205. *E.g., Thomas*, 836 F.2d at 881; *Yagman*, 796 F.2d at 1183-84. Monetary sanctions can be made payable immediately, even before the end of the litigation. Ortho Pharmaceutical Corp. v. Sona Distrib., 847 F.2d 1512, 1514-15, 1517-18 (11th Cir. 1988). In that event, care must be taken to ensure that the effect is not to preclude access to the courts in any significant way. *See Thomas*, 836 F.2d at 882 n.23.

206. *See INVST Financial Group, Inc.*, 815 F.2d at 401 n.4.

207. See Albright v. Upjohn Co., 788 F.2d 1217, 1222 (6th Cir. 1986) (Guy, J., dissenting).

208. *E.g., Thomas*, 836 F.2d at 883. *But see Sanko S.S. Co., Ltd.*, 835 F.2d at 52, 53.

209. *See Thomas*, 836 F.2d at 883; *In re* Ruben, 825 F.2d 977, 990-91 (6th Cir. 1987), *cert. denied*, 485 U.S. 934 (1988); *Yagman*, 796 F.2d at 1184. *Compare Szabo Food Serv., Inc.*, 823 F.2d at 1084 *with Brown*, 830 F.2d at 1438-39.

Finally, as to the applicable standard of appellate court review,[210] the situation can be summed up with the statement that the courts of appeal have been hopelessly split. On one end of the appellate review spectrum is the position, setting up a three-tiered standard, that findings of fact are subject to a clearly erroneous review, the legal conclusion that a particular set of facts does or does not constitute a Rule violation is subject to *de novo* review, while the nature and amount of any sanction is only reviewed for abuse of discretion.[211] At the other end of the spectrum is a single, across-the-board, type of review standard. Under this position everything is reviewable only for abuse of discretion,[212] perhaps with an addendum that findings of fact, if not clearly erroneous, will not be considered an abuse of discretion.[213]

In between these two poles are a number of standards constituting variations of the extremes,[214] some of which have been characterized as "hard to understand."[215] Because the various circuits widely differ with respect to the proper standard of appellate review, it has been suggested that the straight abuse of discretion approach is preferable due to the fact-intensive nature of Rule 11 determinations as well as its minimization of incentives to appeal, thereby reducing satellite litigation.[216] The Supreme Court has granted certiorari and will likely resolve this conflict in the near future.[217] This article will is now focus on the requirements for the federal income tax deduction of Rule 11 monetary sanctions imposed solely upon attorneys.

PART II: THE DEDUCTION OF BUSINESS EXPENSES

The Threshold Issue of the Rule 11 Monetary Sanction as an "Ordinary" and "Necessary" Expense

Section 162(a)[218] of the Internal Revenue Code[219] generally permits a taxpayer to deduct for federal income tax purposes "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any

---

210. There is a disagreement about whether an order imposing Rule 11 monetary sanctions solely against a nonparty attorney prior to the end of the litigation is immediately appealable. *Compare* Aetna Life Ins. Co. v. Alla Medical Serv., Inc., 855 F.2d 1470, 1472-73 (9th Cir. 1988) (immediately appealable) *with* Click v. Abilene Nat'l Bank, 822 F.2d 544, 545 (5th Cir. 1987) (not immediately appealable). *See* SANCTIONS, *supra* note 5, at 13-14.

211. *E.g.*, Equal Employment Opportunity Comm. v. Milavetz & Associates, P.A., 863 F.2d 615 (8th Cir. 1988); *Zaldivar*, 780 F.2d at 828.

212. *E.g., Thomas*, 836 F.2d at 872-73; EBI, Inc. v. Gator Indus., Inc., 807 F.2d 1, 6 (1st Cir. 1986); Stevens v. Lawyers Mut. Liab. Ins. Co., 789 F.2d 1056, 1060 (4th Cir. 1986); Lieb v. Topstone Indus., Inc., 788 F.2d 151, 157 (3d Cir. 1986).

213. *See Adamson*, 855 F.2d at 673.

214. *See, e.g., Donaldson*, 819 F.2d at 1556-57 (whether factual, dilatory or bad faith reasons exist to impose sanction—abuse of discretion; legal sufficiency of pleading or motion—de novo; type of sanction: abuse of discretion); *Westmoreland*, 770 F.2d at 1174-75 (to same effect as *Donaldson*); *Eastway Constr Corp.*, 762 F.2d at 254 n.7 (whether pleading groundless—de novo; determining specifics of sanction—abuse of discretion).

215. *See* S. BURBANK, *supra* note 5, at 46. This disagreement as to the proper standard of appellate review has occurred even within a single circuit where different configurations have been utilized from time to time. *See* Insurance Benefit Admin'rs, Inc. v. Martin, 871 F.2d 1354, 1358-59 & n.4 (7th Cir. 1989).

216. *See* S. BURBANK, *supra* note 5, at xvi, 98; SANCTIONS *supra* note 5, at 15.

217. *See Cooter & Gell*, 110 S. Ct. 275, 58 U.S.L.W. 3252-53.

218. I.R.C. § 162(a) (1982).

trade or business." Where a licensed attorney engaged in the active practice of law has been monetarily sanctioned under Rule 11, the threshold issue concerning deductibility can usually be narrowed to whether the payment can be considered "ordinary and necessary."[220]

A. The Requisite of "Ordinary"

With regard to the requisite that the expense be "ordinary" the Supreme Court has said that its principal function "is to clarify the distinction, often difficult, between those expenses that are currently deductible and those that are in the nature of capital expenditures, which, if deductible at all, must be amortized over the useful life of the asset."[221] Rule 11 monetary sanctions incurred in a representative capacity would not normally come within the definition of a capital expenditure[222] because such payment would not usually be made in connection with the acquisition of an asset[223] nor for its creation or enhancement.[224]

Other judicial definitions of an "ordinary" expense include "normal, usual, or customary"[225] and "normal or habitual,"[226] with the caution that it can encompass even once-in-a-lifetime type expenditures.[227] The reason for this is, despite the rarity of occurrence in the lifetime of a single taxpayer, the payment

---

219. Internal Revenue Code of 1986, Pub. L. No. 99-514, 99th Cong., 2d Sess. (1986).

220. It is assumed that the attorney is engaged in the full-time, active practice of law and the provision of legal services to others for a livelihood, so that there is no issue that such activity constitutes a trade or business. *See* Commissioner v. Groetzinger, 480 U.S. 23, 27 n.7, 32-35 (1987). For some instances where the amount of activity as a licensed attorney did not attain the level of a trade or business, see Sloan v. Commissioner, 55 T.C.M. (CCH) 1238 (1988); Cohen v. Commissioner, 48 T.C.M. (CCH) 5 (1984). It is also assumed that the attorney was sanctioned in his or her representative capacity, and not as a *pro se* party, so that the attorney was engaged "in carrying on" the trade or business of providing legal services to others when sanctioned.

221. Commissioner v. Tellier, 383 U.S. 687, 689-90 (1966). *See* I.R.C. §§ 167, 168, 263, 263A. *See also* I.R.C. § 262.

222. If a monetary Rule 11 sanction were imposed upon a *party* in a suit involving either his or her acquisition of a business asset, or defending or perfecting title to such an asset, the payment could plausibly be a capital expenditure and, if so, not deductible under section 162(a) without regard to section 162(f). *See* Treas. Reg. § 1.263(a)-2(a) & (c) (1960); Woodward v. Commissioner, 397 U.S. 572 (1970); United States v. Hilton Hotels Corp., 397 U.S. 580 (1970).

223. *See* Treas. Reg. § 1.263(a)-2(a) (1960); *Tellier*, 383 U.S. at 690. This would be true at least where the attorney fee was not to be an in-kind asset.

224. *See* Commissioner v. Lincoln Sav. & Loan Ass'n, 403 U.S. 345, 354 (1971). It has been noted that a consequence of the imposition of a Rule 11 sanction upon an attorney can be to bring "the sanctioned lawyer new business as a certified hard-nosed litigator." *Nelken*, *supra* note 5, at 1325 & n.76. Although such action would be reckless in the extreme, it is at least conceivable that the incurrence of a Rule 11 sanction for such a purpose might make a capital expenditure out of its payment, akin to costs for the development of reputation and good will. *See* Welch v. Helvering, 290 U.S. 111, 115-16 (1933); Brown v. Commissioner, 29 T.C.M. (CCH) 1126, 1133-34 (1970). Such an argument by the Service in order to deny deductibility, however, would seem to turn the assumption behind Rule 11 about what is acceptable lawyer performance on its head. As to the amortization issue, if the argument succeeded without regard to section 162(f) also being applicable, see Sharon v. Commissioner, 66 T.C. 515 (1976), *aff'd*, 591 F.2d 1273 (9th Cir. 1978), *cert. denied*, 442 U.S. 941 (1979).

225. Deputy v. Du Pont, 308 U.S. 488, 495 (1940).

226. *See* Raymond Bertolini Trucking Co. v. Commissioner, 736 F.2d 1120, 1124 (6th Cir. 1984).

227. *Welch*, 290 U.S. at 114.

is nonetheless within the norms of conduct, under the circumstances in question, in the business community of which the taxpayer is a part.[228] Thus "ordinary" has a broad reach, generally covering the operating expenses of a business but excluding capital expenditures. Indeed, it has been held that a business expense "is ordinary if it is a current expense"[229] as distinct from a business capital expenditure. Accordingly, the Sixth Circuit has included within its scope kickbacks made by a company to keep profitable construction subcontracts, the kickback practice not being illegal under state law.[230] Given this legal environment, it would seem that the sanctioned attorney's payment of a Rule 11 monetary award should qualify as "ordinary."

B. The Requisite of "Necessary"

Whether such a payment qualifies as a "necessary" expense, however, is a slightly more difficult matter. Traditionally, the term "necessary" has not been construed to demand very much. It has been treated generally "as imposing only the minimal requirement that the expense be 'appropriate and helpful' for the 'development of the . . . business.'"[231] Almost any type of business expense could arguably come within the lenient standard of being merely "appropriate and helpful." The Supreme Court has specifically labled as "necessary," the legal costs paid by an underwriter in connection with the unsuccessful defense of criminal securities fraud charges.[232] The Service has similarly ruled where the taxpayer was sued for breach of contract and fraud in the ordinary conduct of its business activities and paid an amount, including punitive damages, to satisfy the civil judgment.[233]

The standard does have some content, however. This is illustrated by employees who pay business expenses that are reimbursable by the employer but for which the employees do not seek reimbursement. Whether the failure to seek reimbursement is due to, for example, negligence, primarily a personal rather than a business reason, or even unawareness of the reimbursability, the answer is the same. Such expenses are not deductible because they are not "necessary."[234]

The Service has extended this principle outside the employer-employee area to an attorney's payment to a client arising from malpractice which is covered by insurance. In Revenue Ruling 78-141[235] the Service held that such a

---

228. *See supra* note 227; M.L. Eakes Co., Inc. v. Commissioner, 686 F.2d 217, 221 & n.3 (4th Cir. 1982). Mr. Justice Cardozo, who authored the opinion in *Welch*, then went on to make his famous statement in regard to the "ordinary" standard set out in the statute:

> One struggles in vain for any verbal formula that will supply a ready touchstone. The standard setup by the statute is not a rule of law; it is rather a way of life. Life in all its fullness must supply the answer to the riddle.

Welch, 290 U.S. at 115

229. *Raymond Bertolini Trucking Co.*, 736 F.2d at 1123.

230. *Id.* at 1121-22, 1125-26.

231. *Tellier*, 383 U.S. at 689 (quoting *Welch*, 290 U.S. at 113).

232. *Id.* at 689-90, 695.

233. Rev. Rul. 80-211, 1980-2 C.B. 57. *See* Ostrom v. Commissioner, 77 T.C. 608 (1981).

234. *E.g.*, Orvis v. Commissioner, 788 F.2d 1406 (9th Cir. 1986); Stolk v. Commissioner, 326 F.2d 760 (2d Cir. 1964); Heidt v. Commissioner, 274 F.2d 25 (7th Cir. 1959). An alternative ground for nondeductibility is that, as the expenses were reimbursable by the employer, they were employer, not employee, expenses. *See DuPont*, 308 U.S. at 493-94.

235. 1978-1 C.B. 58.

payment to the client was not deductible under section 162(a) where the attorney filed no claim with his professional liability insurer due to the fear that it might cause either a premium increase or outright cancellation of the policy.[236] In these employer reimbursability and business insurance coverage situations the problem is not the necessity of the expense in and of itself, but, instead, whether it was "necessary" to the person claiming the deduction. Obviously related to this is the issue of the expense itself being avoidable in the first place.

1. Hoover Motor Express and the problem of general avoidability

In *Hoover Motor Express Co., Inc. v. United States*[237] the issue was whether fines paid by a trucking company for inadvertent violation of state highway maximum weight laws were deductible as ordinary and necessary business expenses. These fines were mostly attributable to exceeding the allowable axleweight limits rather than violating the overall truck weight limitations. The Supreme Court held that, as in the companion case of *Tank Truck Rentals, Inc. v. Commissioner*,[238] the deduction should be disallowed because it would otherwise frustrate sharply defined state policy by reducing the "sting" of the state penalty.[239] Additionally, the Court commented that the violations in question had occurred due to load shifting in transit and incorrect weights being stated in the bills of lading where the truckers had picked up loads in communities having no weighing facilities. These factors likewise precluded deductibility, acording to the Court, because both types of violations could have been prevented by, respectively, tying down the load or compartmentalizing the truck, and carrying a scale.[240]

This seems to be an indication that an expense is not "necessary" and, hence, not deductible where its incurrence could have been avoided by the taking of various further steps or precautions. But the maximum requisite degree of reasonableness of such steps or precautions was not defined.

Applying this principle to Rule 11 sanctions imposed because of the attorney's failure to make a reasonable pre-filing inquiry into either the facts or the law or because of an improper purpose, it seems clear that such sanctions could have been avoided. Thus, the payment would not be a "necessary" expense based upon this interpretation of *Hoover Motor Express*. But the Supreme Court itself has subsequently ignored this avoidability aspect of *Hoover*. For example, in *Commissioner v. Tellier* an underwriter was allowed to deduct the legal costs paid in connection with the unsuccessful defense of criminal securities fraud charges,[241] even though it is clear that the expense could have been avoided by simply refraining from the illegal activity itself.[242] In addition, the denial of deductibility in *Hoover* has been construed to properly depend upon the public policy factor, regardless of whether the violation was

236. *But see* Waxler Towing Co., Inc. v. United States, 510 F. Supp. 297 (W.D. Tenn. 1980).
237. 356 U.S. 38 (1958).
238. 356 U.S. 30 (1958).
239. *Hoover Motor Express*, 356 U.S. at 40. *See Tank Truck Rentals*, 356 U.S. at 35-37.
240. *Hoover Motor Express*, 356 U.S. at 39-40.
241. *See supra* notes 231-32 and accompanying text.

deliberate, as in *Tank Truck Rentals*, or merely inadvertent.[243] Thus, the Sixth Circuit has said that the insertion into the *Hoover* opinion of the avoidability comment was really just a contrary response to the contention of the company that it had done everything practicable to avoid violations.[244] Accordingly, it would appear that mere avoidability of the expense itself by the Rule 11 sanctioned attorney—for example, by having made a reasonable pre-filing inquiry—does not prevent its deductibility as a "necessary" expense.

2. The problem of negligence, gross negligence, recklessness and intentional impropriety

Also implicated in, and inextricable from, the problem of general avoidability as such, is the more specific issue of whether an expense is "necessary" where it is caused by an action ranging from mere negligence to intentional impropriety with stops in between these two poles at gross negligence and recklessness. Alternatively, the issue might be stated as being whether the expenses in such cases were incurred in pursuit of, or were directly connected with, or were proximately related to, the business.[245] In any event, under either statement of the issue it is clear that the presence of mere negligence does not prevent the expense from being both "necessary" and proximately related to the business.[246] It is not so obvious, however, that Rule 11 imposes a mere negligence standard upon attorneys for purposes of determining whether a violation has occurred.

It may well be true that such is the import of testing conduct under the Rule according to the standard of objective reasonableness under the circumstances,[247] utilizing as the "reasonable person" a competent attorney admitted to practice before the district court.[248] But this fails to take account of the additional admonitions typically issued by many courts that Rule 11 should be "used with the utmost care and caution," and is "reserved only for exceptional circumstances" as it is "an extraordinary remedy," and that, in certain cases, a violation exists "only when it is patently clear that a claim has absolutely no chance of success."[249] If the objective reasonableness test otherwise establishes a negligence standard, it may be that these additional guidelines dilute it in the sense that it will be more difficult for a violation to occur. The consequence of such additional admonitions may be that Rule 11

---

242. *See* Mason & Dixon Lines, Inc. v. United States, 708 F.2d 1043, 1045 (6th Cir. 1983).

243. *Id.*

244. *Id.*

245. *See* Kornhauser v. United States, 276 U.S. 145, 153 (1928).

246. *E.g.*, Anderson v. Commissioner, 81 F.2d 457, 460 (10th Cir. 1936); Dancer v. Commissioner, 73 T.C. 1103, 1105, 1108 (1980).

247. The Seventh Circuit apparently believes that the Rule establishes a negligence standard. That court stated "[I]n effect it imposes a negligence standard . . . for negligence is a failure to use reasonable care. . . . Restating the standard in negligence terms helps one to see that Rule 11 defines a new form of legal malpractice." Hays v. Sony Corp. of Am., 847 F.2d 412, 418 (7th Cir. 1988).

248. *See supra* note 21 and accompanying text.

249. *See supra* notes 22-26 and accompanying text. As already noted, the Seventh Circuit has expressed the view that Rule 11 establishes a negligence standard. *Supra* note 247 and accompanying text. That court has also admonished, nonetheless, that Rule 11 "is a tool that must be used with the utmost care and caution." Federal Deposit Ins. Corp. v. Tefken Constr. & Installation Co., Inc., 847 F.2d 440, 444 (7th Cir. 1988).

may require more than mere negligence, or the reasonable person might be a *minimally* competent attorney admitted to practice before the court.

Although there is no generally accepted meaning for gross negligence, it probably means more than ordinary negligence but less than conscious indifference to the consequences.[250] Contrariwise, recklessness would encompass the latter.[251] Whether this objective reasonableness standard as amplified by the typical guidelines has the effect of importing either of these tort concepts into Rule 11 is not clear. It is not the purpose of this Article, however, to resolve this issue. The point being made is simply that, if the Rule 11 sanctioned conduct is mere negligence, the payment could still be regarded as "necessary" and proximately related to the lawyer's business. But as the sanctioned conduct ranges higher up the scale of culpability and anti-social behavior to gross negligence and beyond, the Service has an ever stronger case for denying deductibility under section 162(a), without regard to section 162(f), because the payment becomes less "necessary" and less proximately related to the business of providing legal services.

The treasury regulations themselves contain an example of the distinction. Under the casualty loss provision, such a loss is said to occur to the taxpayer's automobile when the damage results from his or her faulty driving, but not when it is the result of a willful act.[252] Perhaps this can be best illustrated by one of the most flagrant Rule 11 violations. Assume that an attorney is monetarily sanctioned for filing a factually baseless section 1983 claim against a judge in order to compel that judge to recuse himself or herself from other litigation being handled by that attorney.[253] It would be hard, indeed, to argue that such a payment would be "appropriate" and, hence, "necessary" as well as being proximately related to the business of lawyering, given the Rule 11 certification, not to mention ethical considerations and the rules of professional responsibility. Of course, this is intentional impropriety, the highest point of egregiousness on our scale,[254] but similar difficulties could be encountered by lesser conduct that is, nonetheless, more than mere negligence.

---

250. PROSSER & KEETON ON TORTS § 34, at 212 (5th ed 1984) [hereinafter PROSSER & KEETON].

251. *Id.* at 213. *See also* Report on Punitive Damages of the Committee on Special Problems in the Administration of Justice 10-13 (March 3, 1989; American College of Trial Lawyers; Prof. Roger C. Henderson, Reporter) [hereinafter Report on Punitive Damages]. Recklessness includes willful and wanton conduct. *See* PROSSER & KEETON, *supra* note 250, at 212-14.

252. Treas. Reg. § 1.165-7(a)(3)(i) (amended 1977). In addition to referring to willful act, that regulation utilizes the term "willful negligence." This latter phraseology is a contradiction in terms, at least under orthodox usage in tort law, as negligence involves the absence of willful injury. *See* Anderson v. Commissioner, 81 F.2d 457, 460 (10th Cir. 1936); Report on Punitive Damages, *supra* note 251. The basic distinction of the regulation, however, remains valid for tax purposes. *See* Farber v. Commissioner, 57 T.C. 714, 718 (1972); White v. Commissioner, 48 T.C. 430, 435 (1967); Heyn v. Commissioner, 46 T.C. 302, 308 (1966).

253. *See supra* notes 77-78 and accompanying text.

254. It would seem that a subjective bad faith filing would violate both the old and the new versions of Rule 11. *See Yagman*, 796 F.2d at 1186. For a pre-1983 example of intentional impropriety causing an expense not to qualify as an ordinary and necessary business expense, but, instead, converting it into a nondeductible personal expense, see Meredith v. Commissioner, 47 T.C. 441 (1967); I.R.C. § 262 (stating that "no deduction shall be allowed for personal, living, or family expenses").

There is some fairly recent judicial support for this approach. In *Oden v. Commissioner*,[255] the Tax Court denied an ordinary and necessary business expense deduction for legal expenses incurred in unsuccessfully defending against, and compensatory damages paid pursuant to a judgment in, a defamation suit against the taxpayer arising from poor recommendations given with respect to a former employee. The Tax Court concluded that, despite the business context, the presence of actual malice in the making of the slanderous statements precluded deductibility.[256] In so holding the Tax Court was compelled to distinguish *Commissioner v. Tellier*[257] where the Supreme Court had held that legal expenses incurred by an underwriter in the unsuccessful defense of criminal securities fraud charges were deductible business expenses. The Tax Court did so on the ground that in *Tellier* the criminal charges involved securities fraud occurring directly in the actual conduct, and in furtherance, of the defendant's underwriting business. But, in *Oden*, the false statements about the former employee could not be said to be in pursuit of the taxpayer's florist business, particularly when made with actual malice.[258]

Therefore, it is plausible that, as the sanctioned conduct rises above the level of mere negligence on our scale of increasing culpability, the Commissioner may gain another arrow for the Service's quiver of weapons for attacking the deductibility of any monetary payment—that it is neither "necessary" nor proximately related to the business of being an attorney engaged in the proper rendering of legal services to others. Regardless of this threshold issue, however, there is another more persuasive reason for denying the deductibility of monetary Rule 11 sanctions imposed solely upon attorneys. Moreover, this reason would apply whatever the level of conduct sanctioned, be it mere negligence, gross negligence, recklessness, or intentional impropriety. Accordingly, this Article next considers the effect of section 162(f).

The Elements of Section 162(f)

A. Section 162(f) as a Codification of the Public Policy Doctrine

Since its enactment in 1969[259] up to the present, section 162(f) has provided: "(f) Fines and Penalties. No deduction shall be allowed under subsection (a) for any fine or similar penalty paid to a government for the violation of any law."[260] As a foundation stone for our consideration of the meaning of section 162(f), it should be clear from this language that a payment within its terms will not be deductible despite the fact that it would otherwise be regarded as an ordinary and necessary business expense under section 162(a).

This was true under the case law, prior to the enactment of the Tax Reform Act of 1969, which permitted the disallowance of deductions upon public policy grounds despite the fact such expenses would have been otherwise

---

255. 56 T.C.M. (CCH) 851 (1988).
256. *Id.* at 853.
257. 383 U.S. 687 (1966).
258. *Oden*, 56 T.C.M. (CCH) at 853. *See also* Commissioner v. Heininger, 320 U.S. 467, 471 (1943) (allowing deduction of legal fees incurred in unsuccessful defense against Post Office fraud order arising in connection with the taxpayer's mail order business, but noting possible exception for bad faith defenses); Car-Ron Asphalt Paving Co., Inc. v. Commissioner, 758 F.2d 1132 (6th Cir. 1985).
259. Tax Reform Act of 1969, Pub. L. No. 91-172, § 902(a), 83 Stat. 710.
260. I.R.C. § 162(f) (1982).

allowable as deductions.[261] In *Tank Truck Rentals*,[262] the Supreme Court applied the public policy doctrine to deny deductibility under section 162(a) of fines paid for the deliberate violation of state highway maximum weight laws.[263] These fines were imposed under penal statutes designed to protect highways from damage as well as the safety of their users. It was uncontested, however, that the particular state's weight limits were so low in relation to other states that, for this and other industry-related reasons, it was not possible for truckers to operate profitably in compliance with those limitations. Consequently, the fines were the product of the deliberate choice of the taxpayer to take the chances of being detected and caught.[264]

In discussing the public policy doctrine, the Court indicated the deduction should be disallowed "if allowance of the deduction would frustrate sharply defined national or state policies proscribing particular types of conduct, evidenced by some governmental declaration . . ."[265] where such frustration would occur "in severe and direct fashion by reducing the 'sting' of the penalty prescribed . . . ."[266] Here, in the view of the Court, permitting federal deduction of the fines would so frustrate the expressed state policy by increasing the likelihood that truckers would be willing to violate the law and run the risk of getting caught.[267]

Faced with some uncertainty in the application of this judicially-created public policy doctrine, and pressures in connection with antitrust treble damage payments, Congress took action in the Tax Reform Act of 1969 (TRA 1969) to substantially codify that public policy, insofar as it applied to section 162.[268] Consequently, it enacted new section 162(f) dealing with the topic of fines and similar penalties. As part of the same process, it also enacted new section 162(g) denying deductibility under certain circumstances for the punitive two-thirds portion of antitrust treble damage payments. In addition, Congress amended section 162(c) dealing with illegal payments to government officials and others.[269]

In other business contexts, however, Congress apparently felt that public policy was not sufficiently fixed and delineated to justify the denial of otherwise allowable business deductions. Consequently, the legislative history to TRA 1969 indicated that those specific codifications of public policy were intended to be all-inclusive.[270] Therefore, an otherwise deductible section 162(a) payment of a fine or penalty not within the scope of the section 162(f) prohibition can

---

261. *See* Taggart, *Fines, Penalties, Bribes, and Damage Payments and Recoveries*, 25 TAX L. REV. 611, 612-14 (1970).

262. 356 U.S. 30 (1958).

263. Alternatively, the decision could be interpreted as a holding that the business expense was not "necessary" if the allowance of the deduction would frustrate public policy. *See* Taggart, *supra* note 261, at 612-13.

264. *Tank Truck Rentals*, 356 U.S. at 32-35.

265. *Id.* at 33-34.

266. *Id.* at 36.

267. *Id.* at 35. The Court also noted that the fines were punitive in nature, not constituting a mere toll for the use of the highways. *Id.* at 34.

268. *See* S. REP. NO. 552, 91st Cong., 1st Sess., *reprinted in* 1969 U.S. CODE CONG. & ADMIN. NEWS 2027, 2310-11; Taggart, *supra* note 261, at 612-14, 616-18.

269. *See* S. REP. NO. 552, *supra* note 268, at 2311; Rev. Rul. 77-126, 1977-1 C.B. 47.

270. S. REP. NO. 552, supra note 268, at 2311.

not be disallowed upon independent public policy grounds.[271] In other words, section 162(f) has preempted the public policy doctrine in this area,[272] and the treasury regulations so provide.[273]

The effect of this proposition in the Rule 11 context is clear. Assume that a monetary Rule 11 sanction is imposed solely upon an attorney, and that this would constitute an otherwise allowable deduction under section 162(a). If the sanction could not be brought within the scope of section 162(f), then deductibility could not be denied for public policy reasons. Given that principle, the question remains whether section 162(f) encompasses monetary Rule 11 sanctions. Accordingly, it is time to focus on the initial issue in this context—whether section 162(f) applies only to fines and penalties of a criminal nature as opposed to encompassing also those on the civil side.

B. Criminal and Civil Fines and Penalties

This issue is raised because of, *inter alia*, the "cryptic and somewhat ambiguous" legislative history to that section in TRA 1969.[274] The Senate Finance Committee report only stated that "[t]his provision is to apply in any case in which the taxpayer is required to pay a fine because he is convicted of a crime (felony or misdemeanor) in a full criminal proceeding in an appropriate court. This represents a codification of the general court position in this respect."[275] That this statement was internally conflicting or at least ambiguous is seen from that fact that it speaks only of a criminal fine yet says that it "represents a codification of the general court position in this respect." Court decisions prior to TRA 1969, however, had denied deduction under the public policy doctrine of payments that represented, in effect, civil penalties.[276]

---

271. Taggart, *supra* note 261, at 646.

272. *See Mason & Dixon Lines, Inc.*, 708 F.2d at 1046 ("[the public policy] exception is no longer available to the Commissioner as it has been subsumed into 'specific legislation.'"). The judicially-created public policy doctrine as an independent basis for disallowing otherwise deductible items remains in being outside the section 162 business expense area, however. Thus, it has been applied to deny a deduction under section 165 for a loss resulting from a scam counterfeiting scheme. Mazzei v. Commissioner, 61 T.C. 497 (1974). To similar effect, see Wood v. United States, 863 F.2d 417 (5th Cir. 1989) (disallowing loss under section 165 resulting from forfeiture of assets acquired with marijuana sales proceeds); Holmes v. Commissioner, 69 T.C. 114 (1977) (disallowing loss under section 165 resulting from forfeiture of automobile used in transporting marijuana); Holt v. Commissioner, 69 T.C. 75 (1977), *aff'd per curiam*, 611 F.2d 1160 (5th Cir. 1980) (disallowing loss under section 165 resulting from forfeiture of truck and horse trailer utilized in marijuana trafficking); Rev. Rul. 77-126, 1977-1 C.B. 47 (disallowing loss under section 165 resulting from forfeiture of gambling devices). *See* Rev. Rul. 81-24, 1981-1 C.B. 79. The public policy doctrine is also available to deny otherwise allowable deductions under section 212. Treas. Reg. § 1.212-1(p) (amended 1975).

Recently, the Tax Court has applied the considerations involved in section 162(f) to deny the deduction of restitution payments under section 165(c)(2). Although it recognized that section 162(f) did not control by its terms, the Tax Court nonetheless believed that its public policy codification should be extended to transactions entered into for profit. *See* Stephens v. Commissioner, 93 T.C. 108 (1989).

273. Treas. Reg. § 1.162-1(a) (1975).

274. *See* Southern Pac. Transp. Co. v. Commissioner, 75 T.C. 497, 651 (1980). *See generally* Taggart, *supra* note 261, at 646-50.

275. S. REP. NO. 552, *supra* note 268, at 2311-12.

276. *E.g.*, McGraw-Edison Co. v. United States, 300 F.2d 453, 455-57 (Ct. Cl. 1962) (disallowing on public policy grounds the deduction of a payment in settlement of claims for

Subsequent legislative history to the amendment of a related provision—section 162(c)--by the Revenue Act of 1971[277] attempted to clear up this problem. The Senate Finance Committee report contained a statement with respect to section 162(f) indicating that it had meant to preclude deductions for sanctions imposed under civil statutes serving the same purposes as a fine exacted under a criminal statute. On the other hand, the report said that the Committee had not contemplated disallowing penalties imposed to promote prompt compliance with such things as filing requirements which are, in essence, more in the nature of late filing or interest charges than fines. The report concluded that the Committee had not intended "to liberalize the law in the case of fines and penalties."[278]

Taken at face value, that Senate Finance Committee report clearly indicates the intent of Congress in TRA 1969 to make section 162(f) applicable not only to criminal fines and penalties but also to those civil fines and penalties that serve the same purposes. The problem with this is that it constitutes the view of a later Congress as to what was meant by an earlier Congress. It is almost a given that such subsequent legislative history is not controlling.[279] In any event, the Treasury proceeded to promulgate final regulations in 1975 that specifically included within the scope of section 162(f) payments of civil penalties as well as payments in settlement of potential liability for such penalties.[280]

Despite the fact that subsequent legislative history is not generally controlling, it can nonetheless be considered where clearly relevant.[281] In addition, there are some further specific circumstances present here giving greater significance to this subsequent legislative history. First, in the Revenue Act of 1971 Congress did, in fact, amend section 162(c), a provision related to section 162(f) representing a portion of the codification of the public policy doctrine.[282] But Congress did not change section 162(f) even though it was aware of the Treasury's proposed regulation applying it to civil penalties.[283] That tended to support the 1971 Senate Finance Committee statement.[284] In addition, the contemporaneous but cryptic 1969 Senate Finance Committee report had indicated that section 162(f) represented the general court position. Since the court decisions prior to the enactment of TRA 1969 were consistent with the subsequent 1971 legislative statement, that further supported the

---

breach of contractual provision, pursuant to the Walsh-Healey Act, prohibiting the use of child labor). *See* Adolf Meller Co. v. United States, 600 F.2d 1360, 1362 (Ct. Cl. 1979).

277. Pub. L. No. 92-178, § 310(a), 85 Stat. 525 (1971).

278. S. REP. NO. 437, 92 Cong., 1st Sess., *reprinted in* 1971 U.S. CODE CONG. & ADMIN NEWS 1918, 1978-80.

279. *See, e.g.*, Haynes v. United States, 390 U.S. 85, 87 n.4 (1968).

280. Treas. Reg. § 1.162-21(b)(1)(ii) & (iii) (1975). *See* T.D. 7345, 1975-1 C.B. 51, 54; T.D. 7366, 1975-2 C.B. 64.

281. *E.g.*, Johnsen v. Commissioner, 794 F.2d 1157, 1163 (6th Cir. 1986); First State Bank v. United States, 599 F.2d 558, 563 n.3 (3d Cir. 1979), *cert. denied*, 444 U.S. 1013 (1980); Walt Disney Prod. v. United States, 480 F.2d 66, 68-69 (9th Cir. 1973), *cert. denied*, 415 U.S. 934 (1974).

282. *See supra* notes 269, 277 and accompanying text; Rev. Rul. 77-126, 1977-1 C.B. 47.

283. *See supra* notes 277-78 and accompanying text; Notice of Proposed Regulation § 1.162-21, 36 Fed. Reg. 9638-39 (1971).

284. *See Adolf Meller Co.*, 600 F.2d at 1363.

accuracy of the latter.[285] Consequently, the regulation has been held to be valid, and section 162(f) can apply to civil, as well as criminal, fines and penalties.[286]

Given that general principle, the question remains what type of civil penalty is encompassed by section 162(f)? In other words, what is the tax test for determining whether a particular civil penalty comes within the scope of that provision? This requires us to turn our attention to the specific elements of section 162(f), the first of which is the "fine or similar penalty" language.

C. "Any Fine or Similar Penalty"

In order to further the process of analyzing the specifics of section 162(f), it seems appropriate at this time to define generally, albeit tentatively, the terms "fine" and "penalty" as used in that provision as well as the word "sanction" as it appears in Rule 11. In this regard it should be remembered that the Supreme Court itself has not neglected the use of a dictionary.[287] Accordingly, the dictionary meaning of "fine" includes a "sum . . . imposed as punishment for a crime" as well as "a forfeiture or penalty paid to an injured party in a civil action."[288] Likewise, the term "penalty" encompasses, *inter alia*, "a fine or mulct imposed as . . . a punishment" in addition to "a sum of money made recoverable in a civil action by the state . . . for the less serious offenses not mala in se."[289] Finally, the meaning of "sanction" includes "the detriment, loss of reward, or other coercive intervention that is annexed to a violation of a law as a means of enforcing the law . . . ."[290] Although these general dictionary definitions are obviously neither conclusive as to their meaning in the federal taxing statute nor the Federal Rules of Civil Procedure, they can serve at least as starting points in assessing their specific meanings under these provisions.[291]

The task of fixing the boundaries of "any fine or similar penalty" also requires the attribution of some content to the word "similar;" otherwise, Congress could simply have settled on the phrase "any fine or penalty."[292] It has been said that a "fine would ordinarily be thought of as only imposed at the conclusion of a criminal proceeding, whereas a penalty has a civil

---

285. *See Southern Pac. Transp. Co.*, 75 T.C. at 652 n.177

286. True, Jr. v. United States, 894 F.2d 1197, 1201-04 (10th Cir. 1990); *Adolf Meller Co.*, 600 F.2d at 1362-63; Tucker v. Commissioner, 69 T.C. 675, 679 n.4 (1978); Shapiro v. Commissioner, 43 T.C.M. (CCH) 136 (1981); Colt Industries, Inc. v. United States, 11 Cl. Ct. 140, 58 A.F.T.R. 2d 86-6057 (1986), *aff'd*, 880 F.2d 1311 (Fed. Cir. 1989); Rev. Rul. 76-130, 1976-1 C.B. 15.

287. *E.g.*, National Muffler Dealers Ass'n v. United States, 440 U.S. 472, 480 n.10 (1979).

288. WEBSTER'S THIRD NEW INTERNATIONAL DICTIONARY 852 (1976 ed. Merriam) [hereinafter WEBSTER'S]. *Accord*, BLACK'S LAW DICTIONARY 569 (5th ed. 1979) [hereinafter BLACK'S].

289. WEBSTER'S , *supra* note 288, at 1668. *See* BLACK'S, *supra* note 288, at 1020 ("An elastic term with many different shades of meaning; it involves ideas of punishment, corporeal or pecuniary, or civil or criminal, although its meaning is generally confined to pecuniary punishment.").

290. WEBSTER'S, *supra* note 288, at 2009. "Sanction" has also been defined as "[t]hat part of a law which is designed to secure enforcement by imposing a penalty for its violations. . . . For example, Fed. R. Civ. P. 37 provides for sanctions for failure to comply with discovery orders." BLACK'S, *supra* note 288, at 1023.

291. *See Southern Pac. Transp. Co.*, 75 T.C. at 650 & n.175.

292. *See* Taggart, *supra* note 261, at 649.

connotation."[293] If that is true, it helps to explain the meaning of "similar" in relationship to both "fine" and "penalty." As already shown, the 1971 subsequent legislative history statement by the Senate Finance committee had indicated that this language "would disallow deductions for . . . sanctions . . . imposed under civil statutes but which in general terms serve the same purpose as a fine exacted under a criminal statute."[294] In any event, the courts have apparently accepted this legislative history in concluding that, in order for a civil penalty to be "similar" to a fine and, hence, come within the coverage of section 162(f), it must generally serve the same purposes as a criminal fine.[295]

Probably the leading Tax Court case setting out the applicable test for determining what is a "similar penalty" is *Middle Atlantic Distributors, Inc. v. Comissioner*.[296] Here, the taxpayer corporation was engaged in the business of distributing wines and liquors and operating a United States Customs bonded warehouse that held imported liquors prior to distribution. Under applicable law, imported liquor could be withdrawn from such a bonded warehouse pursuant to permits issued by the Customs Service, free of imported duties and alcohol taxes, if it was for the use of foreign military personnel on duty in the United States.[297]

In this case, apparently without the knowledge of the taxpayer or its employees, a Turkish embassy official had secured the withdrawal of liquor from mid-1957 to mid-1962 by using forged permits and had then transferred it to unauthorized persons for sale within the commerce of the United States. The government subsequently sued the taxpayer and others to recover the full value of the fraudulently withdrawn liquor as a "penalty against goods," as permitted by statute,[298] in the amount of approximately $500,000. The case was eventually settled by the payment of $100,000 as "liquidated damages" pursuant to a stipulation of compromise. The taxpayer then deducted the payment for income tax purposes as an ordinary and necessary business expense, but the Commissioner disallowed the deduction under section 162(f).[299]

The Tax Court first noted that the regulation, insofar as here applicable, distinguished between two types of payments. On the one hand, payments in settlement of potential liability for a civil penalty imposed by federal law came within the prohibition.[300] On the other hand, amounts paid as compensatory damages did not.[301] Accepting the validity of the subsequent 1971 legislative history to section 162(f), the Court concluded that because a criminal fine or penalty "is . . . imposed to punish and/or deter," a civil penalty must do

293. *Id.* at 647.
294. *Compare supra* text accompanying notes 275-76 *with* text accompanying notes 277-78.
295. *E.g., Southern Pac. Transp. Co.*, 75 T.C. at 651-52; *True, Jr.*, 894 F.2d at 1203.
296. 72 T.C. 1136 (1979).
297. *Id.* at 1137-38.
298. 19 U.S.C. § 1592 (1930). *See Middle Atl. Distrib.*, 72 T.C. at 1138 n.3.
299. *Middle Atl. Distrib.*, 72 T.C. at 1137-38, 1141.
300. *Id.* at 1142; Treas. Reg. § 1.162-21(b) (1)(iii) (1975).
301. *See Middle Atl. Distrib.*, 72 T.C. at 1142; Treas. Reg. § 1.162-21(b)(2) (1975).

likewise, in order to come within that proscription.[302] But where the civil penalty is only remedial or compensatory in nature, it does not.[303]

Having established this basic distinction, the Tax Court still had to deal with the fact that the payment at issue was for "liquidated damages" pursuant to a settlement of a suit rather than of a civil penalty itself. The Court quickly disposed of this problem by citing *United States v. Gilmore*[304] for the proposition that the character of the payment is governed by the origin of the liability giving rise to it. Consequently, the resolution of the ultimate issue depended upon the nature of the claim being asserted by the United States.[305]

Applying the basic distinction via the *Gilmore* origin of the claim standard to the facts of the case, the Tax Court determined that, at least during the entire settlement negotiation, the United States had sought to obtain reimbursement only for lost revenue and other damages, and that, in fact, was what it had obtained as "liquidated damages." Consequently, the claim of the United States was not based upon an intent to punish or to deter. Accordingly, the payment in settlement was not a "fine or similar penalty" and was, therefore, deductible.[306]

Middle Atlantic Distributors stands for the proposition that, for a civil payment to come within the "similar penalty" language of section 162(f), it must have its source in a statutory scheme that is designed to punish or to deter. But where the purpose is only remedial or compensatory, the payment is not within the prohibition. This basic formulation in the application of section 162(f) has been substantially followed in subsequent Tax Court decisions[307] as

---

302. *Middle Atl. Distrib.*, 72 T.C. at 1143.
303. *Id.* at 1143.
304. 372 U.S. 39 (1963).
305. *Middle Atl. Distrib.*, 72 T.C. at 1144-45.
306. *Id.* at 1145.
307. *See, e.g.*, Waldman v. Commissioner, 88 T.C. 1384, 1387-88 (1987) (restitution payments made to victims as a condition for stay of prison sentence for conviction of conspiracy to commit grand theft held not deductible, applying punishment/enforcing the law/deterrence versus remedial/compensation distinction); Huff v. Commissioner, 80 T.C. 804, 824 (1983) (payment of civil penalties under section 17536, California Business and Professions Code (West. Supp. 1972) held not deductible, applying punishment/enforcing the law versus encouraging prompt compliance/remedial/compensation distinction); *Southern Pac. Transp. Co.*, 75 T.C. at 646-52 (payment of penalties under the Safety Appliance Act and the Twenty- Eight Hour Act held not deductible, applying punishment/enforcing the law versus encouraging prompt compliance/remedial/compensation distinction).

All these statements of the standard mean essentially the same thing. Thus, enforcing the law and deterrence as purposes operate with punishment on one side while encouraging prompt compliance goes with remedial and compensatory on the other side. As to deterrence being part of the punishment side, see generally United States v. Halper, 109 S. Ct. 1892, 1901-02 (1989); Kelly v. Robinson, 479 U.S. 36, 49 n. 10 (1986). As to enforcing the law, see also *supra* note 290 and accompanying text. The "encouraging prompt compliance" aspect of the other side arises from the 1971 subsequent legislative history. The Senate Finance Committee had said that:

> It was not intended that deductions be denied in the case of sanctions imposed to encourage prompt compliance with requirements of law. Thus, many jurisdictions impose 'penalties' to encourage prompt compliance with filing or other requirements which are really more in the nature of late filing charges or interest charges than they are fines. It was not intended that this type of sanction be disallowed under the 1969 action.

S. REP. NO. 437, *supra* note 278, at 1980.

well by other courts.[308] In addition, the Internal Revenue Service has used this standard in its rulings.[309]

Moreover, a recent discussion of punishment in the context of the Double Jeopardy Clause by the United States Supreme Court is instructive in this regard. In *United States v. Halper*,[310] the defendant had previously been convicted on 65 counts of violating the criminal false claims statute[311] in connection with medicare reimbursement claims for which he had been sentenced to two years imprisonment and fined $5,000. The government then filed the instant case against him under the civil False Claims Act.[312] Although the total actual overcharge to the government from the false claims had been only $585, Halper appeared to be liable for an amount in excess of $130,000 under the civil act. This was because the concededly remedial provision of the statute provided for "a civil penalty of $2,000, an amount equal to 2 times the amount of damages the government sustains because of the act of that person, and costs of the civil action . . . ." for each of the 65 violations.[313]

The district court in *Halper* concluded that the imposition of a $130,000 penalty against the defendant under this civil remedial statutory provision would constitute "punishment" since it was more than 220 times the government's measurable loss. Consequently, in view of Halper's previous criminal conviction and sentence, it would violate the Double Jeopardy Clause's prohibition of multiple punishments. The district court then limited the judgment in favor of the government to double damages of $1,170 plus costs.[314]

The Supreme Court agreed that the disparity between the district court's approximation of the government's costs and the statutory liability of $130,000 was sufficient to make that sanction a second "punishment" in violation of the Double Jeopardy Clause.[315] In the process of reaching that conclusion the Court said the following about civil sanctions as "punishment:"

> a civil as well as a criminal sanction constitutes punishment when the sanction as applied in the individual case serves the goals of punishment.
>
> . . .
>
> . . . punishment serves the twin aims of *retribution* and *deterrence* . . . . [which] are not legitimate *nonpunitive* governmental objectives. From these premises, it follows that a civil sanction that cannot fairly be said

---

308. *See, e.g., True, Jr.*, 894 F.2d at 1204; *Waldman*, 850 F.2d 611; *Mason & Dixon Lines, Inc.*, 708 F.2d at 1046-48.

309. Priv. Ltr. Rul. 87-08-004 (March 3, 1987); Priv. Ltr. Rul. 87-04-003 (Feb. 2, 1987). *See* Rev. Proc. 88-46, 1988-1 C.B. 76; Rev. Rul. 78-196, 1978-1 C.B. 45. Private letter rulings issued by the Service may not be used or cited as precedent. I.R.C. § 6110(j)(3) (1988); Treas. Reg. § 301.6110-7(b) (1990) (T.D. 7524, 1978-1 C.B. 426). The Supreme Court has indicated, however, that they can serve as evidence of the administrative position of the Service. Rowan Cos., Inc. v. United States, 452 U.S. 247, 261 n.17 (1981). They are offered in this article as some evidence of the position of the Service concerning the interpretation of section 162(f).

310. 109 S. Ct. 1892 (1989).

311. 18 U.S.C. § 287 (1969).

312. 31 U.S.C. §§ 3729-3731 (1982 ed. Supp. IV).

313. *Halper*, 109 S.Ct at 1895-96.

314. United States v. Halper, 664 F. Supp. 852, 854-55 (S.D.N.Y. 1987). *See Halper*, 109 S.Ct at 1897.

315. *Halper*, 109 S.Ct at 1904. The Supreme Court vacated and remanded, however, in order to allow the government the opportunity to prove greater actual costs in dealing with Halper's fraud. *Id.* at 1903-04.

> *solely* to serve a remedial purpose, but rather can be explained only as also serving *retributive* or *deterrent* purposes, is punishment, as we have come to understand the term.[316]

Certainly, the *Middle Atlantic Distributors* standard for testing a payment under section 162(f) is consistent with this recent Supreme Court essay on punishment.[317]

As already noted, *Middle Atlantic Distributors* had applied the origin of the claim doctrine of *Gilmore*[318] in the process of reaching its conclusion concerning the deductibility of the liquidated damages settlement payment under section 162(f). In *Gilmore* the taxpayer separately owned the controlling stock interest of three General Motors automobile dealership corporations in California. In addition to serving as president and principal manager of these companies for which he received salaries totalling about $67,000 per year, Gilmore also derived some $83,000 annually on dividends from the stock. His wife commenced divorce proceedings against him on the basis of marital infidelity, and claimed a community property interest in the stock.[319]

The taxpayer was very much concerned about this for two basic reasons. First, he feared that, if he lost the controlling stock interests, it might jeopardize the retention of his corporate offices which produced his principal means of livelihood. Second, due to his wife's sensational allegations of infidelity, General Motors Corporation might exercise its right to cancel the dealership franchises held by his three corporations, if the court granted her the divorce. Accordingly, the taxpayer cross-claimed for divorce and incurred some $41,000 in legal expenses in successfully defending his sole ownership of

---

316. *Id.* at 1901-02 (emphasis added).

317. The 100 percent penalty of section 6672 imposed upon responsible officers of an employer for failure to withhold and pay over is not deductible due to section 162(f). Medeiros v. Commissioner, 77 T.C. 1255 (1981); Patton v. Commissioner, 71 T.C. 389 (1978); Snedeker v. Commissioner, 47 T.C.M. (CCH) 279 (1983); Reid v. Commissioner, 42 T.C.M. (CCH) 1741 (1981). The reason given is a statement in the 1971 subsequent legislative history which said that "[Section 162(f)] . . . was intended to apply, for example, to penalties provided for under the Internal Revenue Code in the form of assessable penalties (subchapter B of chapter 68) . . . ." S. REP. NO. 437, *supra* note 278, at 1980. *See Adolf Meller Co.*, 600 F.2d at 1363; *Southern Pac. Transp. Co.*, 75 T.C. at 652 n.177; *Colt Indus., Inc.*, 58 A.F.T.R. 2d at 86-6060. The section 6672 penalty is found in subchapter B of Chapter 68.

The punishment/deterrence versus remedial/compensation distinction is not wholly satisfactory in dealing with the section 6672 penalty under section 162(f). As the Second Circuit has said "the nature of the penalty imposed, which is an assessment equal to the amount of tax not paid, shows that § 6672 is simply a means for ensuring that the tax is paid." Botta v. Scanlon, 314 F.2d 392, 393 (2d Cir. 1963). *Accord*, Newsome v. United States, 431 F.2d 742, 745 (5th Cir. 1970). Thus, it is really a tax collection device. This is reinforced by the fact that it is the government's policy to collect the section 6672 penalty only once. *See* United States v. Sotelo, 436 U.S. 268, 279 n.12 (1978). Accordingly, if amounts are recovered from the entity owing the taxes in the first instance, or from other responsible persons, such amounts paid will reduce the penalty sought from any remaining responsible persons. Note, *Voluntary Payment of Trust Fund Taxes Under a Bankruptcy Plan of Reorganization*, 31 ARIZ. L. REV. 159, 161-62 & n.25 (1989). Because it is essentially a tax collection device, it would seem to be more on the side of being remedial or compensatory to make up for otherwise lost taxes, rather than on the side of punishment or deterrence. *See, e.g.*, I.R.C. § 31(a)(1); Treas. Reg. § 1.31-1(a) (1960). Nonetheless, the courts seize on the 1971 subsequent legislative history statement to hold such payments nondeductible under section 162(f).

318. 372 U.S. 39 (1963).

319. *Id.* at 41-42.

the stock, as well as being granted the divorce on his cross-claim with no alimony obligation.[320]

On his individual federal income tax return for the years in question the taxpayer deducted about 80 percent of the legal costs under section 212 and its substantially identical predecessor.[321] That section permits a deduction to an individual for the "ordinary and necessary expenses" paid "for the management, conservation or maintenance of property held for the production of income."[322] Thus, the taxpayer believed that at least 80 percent of the total legal fees were spent in protecting or "conserving" his sole stock ownership interests which directly produced the annual dividend income.[323] The Commissioner disallowed the deduction as a personal or family type expense,[324] but the Court of Claims agreed with the taxpayer on the ground that the *consequence* of the wife's success in the divorce suit would have been to deprive the taxpayer of the income-producing stock itself, as well as the means of earning a livelihood.[325]

The Supreme Court, however, held that the taxpayer's expenditures in resisting the claims of his wife were not deductible.[326] In so holding, the Court accepted the principle that it is "*the origin and character of the claim with respect to which an expense was incurred*, rather than its potential consequences upon the fortunes of the taxpayer [that] is the controlling basic test of whether the expense . . . is deductible . . . ."[327] Here, of course, the wife's claims based upon community property stemmed entirely from the marital relationship, and not from any income-producing activity of the taxpayer.[328]

Although *Gilmore* dealt with a type of expense currently subject to the requisites of section 212(2),[329] the application of the origin of the claim doctrine extends beyond those limits, and clearly includes section 162.[330] In the milieu of section 162(f), *Middle Atlantic Distributors* applied it in determining whether the liquidated damages settlement payment had its origin in the claims of the government for a civil penalty, the purpose of which was to punish or to deter. Thus, the origin of the claim doctrine can be directly relevant to a determination whether a payment is a "fine or similar penalty" under section 162(f). The doctrine is also relevant, perhaps even more so, to another specific requisite for the invocation of that provision—that of being "paid to a government," to be discussed later in this Article.[331]

Monetary sanctions under Rule 11 come generally in either of two basic formats: fines paid directly to the court, or amounts paid to the other party to cover, in whole or in part, the reasonable actual expenses incurred in defending

---

320. *Id.* at 42.
321. *See* Gilmore v. United States, 290 F.2d 942, 944, 947 (Ct. Cl. 1961); *Gilmore*, 372 U.S. at 40 & n.3.
322. I.R.C. § 212(2) (1975).
323. See *Gilmore*, 290 F.2d at 944, 947-48.
324. *Gilmore*, 372 U.S. at 42. *See* I.R.C. § 262 (1988).
325. *Gilmore*, 290 F.2d at 947, *Gilmore*, 372 U.S. at 43-44.
326. *Gilmore*, 372 U.S. at 52.
327. *Id.* at 49 (emphasis added).
328. *Id.* at 51-52.
329. *Supra* note 322.
330. *Tellier*, 383 U.S. at 689.
331. *See infra* text accompanying notes 385-407.

against, and caused by, the offending filing.[332] As we have already seen, the latter type, with its concededly compensatory flavor insofar as its effect on the victim is concerned, is the most common Rule 11 sanction.[333] Initially, it might be thought that a distinction could be made between these two types of monetary sanctions on the basis of this compensatory effect. Under this reasoning, because the latter type of payment to the victim clearly possesses such a compensatory attribute, it should be deductible without more. On the other hand, the payment of a fine directly to the court would seem to partake, at least on the basis of common usage, more of the aura of punishment;[334] hence, it should be nondeductible.

This argument should fail on at least two different levels. First, compensatory effect itself is no valid basis for distinguishing these two types of payments. The reason is that the consequence of the imposition of a fine payable to the court is likewise compensatory; only the victim has changed. Thus, instead of compensating the other party, it is the government (and the taxpayers who support it) who are reimbursed for the wasting of scarce judicial resources.[335] Second, the giving of controlling weight to the compensatory effect of the payment on the victim ignores the *Middle Atlantic Distributors* test for deductibility under section 162(f). That standard establishes the nondeductible effect of the punishment or deterrence purpose, as opposed to the otherwise deductible consequence of the remedial or compensatory goal, depending upon which is the *ultimate objective of the statute in question.* The mere compensatory effect on the victim is not controlling.

It is clear that, in the view of the drafters of Rule 11, its ultimate purpose, if not punishment, was at least to deter attorneys and parties from engaging in the misuse and abuse of the litigation process. The Advisory Committee comments specifically stated that "[t]he word 'sanctions' in the caption . . . stresses a deterrent orientation," and that "[t]he detection and punishment of a violation . . . is part of the court's responsibility . . . ."[336]

Moreover, the effects upon the sanctioned attorney can be quite severe. The courts and the commentators have referred to these consequences time and again. They include not only the economic damage from a monetary award, but also the harm to professional reputation and future business, as well as the general stigma and humiliation almost inherently attached to any such sanction.[337] The Seventh Circuit has said that "[e]ven where . . . the monetary penalty is low, a Rule 11 violation carries intangible costs for the punished lawyer or firm. A lawyer's reputation for integrity, thoroughness and competence is his or her bread and butter."[338] Taking into account the intent of

---

332. *See supra* notes 93-97, 126-27, and accompanying text. A court may impose both a fine payable to the court and costs including attorney fees payable to the victim in a particular case. *E.g.*, Edwards v. Marsh, 644 F. Supp. 1564, 1573 (E.D. Mich. 1986); Robinson v. Moses, 644 F. Supp. 975, 982-83 (N.D. Ind. 1986). *See Cheek*, 828 F.2d at 398 n.5.

333. *See supra* note 94 and accompanying text.

334. *See supra* note 288 and accompanying text; Priv. Ltr. Rul. 84-45-051 (Nov. 14, 1984).

335. *See Edwards*, 644 F. Supp. at 1573 & n.5; *supra* note 96.

336. FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199-200 (1983). *See supra* note 89.

337. *E.g., Oliveri*, 803 F.2d at 1280; *Golden Eagle Distrib. Corp.*, 801 F.2d at 1540; S. BURBANK, *supra* note 5, at 27-28; Schwarzer, *supra* note 2, at 201.

338. *Federal Deposit Ins. Corp.*, 847 F.2d at 444.

the drafters of Rule 11, as well as the severity of these tangible and intangible consequences to the sanctioned attorney, it is difficult not to view the ultimate purpose of that Rule as being at least deterrence. In any event, as already noted, that is clearly the general consensus.[339]

Not giving controlling weight to the compensatory effect on the victim in the determination of whether a payment is a "penalty" or not can be seen in other nontax areas of the law. In this connection, a look at an analogous provision of the federal bankruptcy law, as recently construed by the Supreme Court, may be helpful. That portion of the bankruptcy act is section 523(a)(7) under which there is no discharge of an individual from any "debt" that is for "a fine, *penalty* or forfeiture payable to and for the benefit of a governmental unit, and *is not compensation for actual pecuniary loss* . . . ."[340]

In *Kelly v. Robinson*,[341] the bankrupt person, Carolyn Robinson, filed a voluntary petition under Chapter 7 listing one of her debts as a restitution obligation. This obligation had arisen from her earlier second degree larceny conviction based upon the wrongful receipt of $9,932.95 in welfare benefits from the Connecticut Department of Income Maintenance.[342] Although the state court had sentenced her to a one-to-three year prison term, that sentence had been suspended and Robinson placed on probation for five years. As a condition of probation, however, the court ordered Robinson to make restitution in the total amount of $9,932.95 to the state's Office of Adult Probation at the rate of $100 per month.[343] This was done under the authority of a state statute that gave the court discretion to impose any of eight specific conditions of probation (in addition to any other condition reasonably related to rehabilitation)[344] including requiring the defendant to "make restitution of the fruits of his offense or make restitution, in an amount he can afford to pay or provide in a suitable manner, *for the loss or damage caused thereby* and the court may fix the amount thereof and the manner of performance."[345]

Although duly notified of the filing of Robinson's voluntary petition, neither the probation office nor the income maintenance department filed any proof of claim or objection to discharge, presumably in the belief that the bankruptcy would have no effect upon the conditions of probation. Accordingly, these agencies did not share in the bankruptcy estate distributions. And, after having paid a total of only $450 in restitution, Robinson was subsequently granted her discharge in bankruptcy. Thereafter, she made no further payments as her attorney had informed the probation office by letter of his opinion that the discharge had voided that probation condition. Following an unexplained hiatus of almost three years, the probation office informed Robinson that it considered the restitution obligation nondischargeable, and that it intended to enforce it to the fullest extent possible. Robinson then filed an

339. *See supra* notes 88, 90, 92 and accompanying text.
340. 11 U.S.C. § 523(a)(7) (1978) (emphasis added).
341. 479 U.S. 36 (1986).
342. *Id.* at 38-39.
343. *Id.* at 38-39 & n.2.
344. *Id.* at 52.
345. CONN. GEN. STAT. § 53a-30(a)(4) (1985) (emphasis added).

adversary proceeding in the bankruptcy court seeking declaratory and injunctive relief.[346]

Relying upon its opinion and decision in a virtually identical earlier case,[347] the bankruptcy court concluded that the discharge had had no effect upon Robinson's restitution obligation because it was a "penalty" under section 523(a)(7), and that relief should be denied.[348] This proposed disposition was then accepted without change by the federal district court for Connecticut.[349]

The Second Circuit, however, took a different view.[350] After first determining that the restitution obligation was a "debt" within the meaning of the bankruptcy act,[351] the appellate court focused on the language of the state probation statute under which the restitution condition was imposed.[352] That statute allowed restitution "for the loss or damage caused" by the offense.[353] The court then noted that the probationary restitution obligation was in a total amount exactly equal to the wrongfully received welfare benefits and was to be paid, ultimately, to the victim—the state income maintenance department—through the probation office. Because of these factors the court of appeals thought that it was designed to be "compensation for actual pecuniary loss."[354] The Second Circuit concluded, therefore, that the restitution debt was dischargeable despite section 523(a)(7).[355]

On appeal, the Supreme Court reversed the Second Circuit.[356] The Court initially expressed "serious doubts" that the probationary restitution obligation constituted a "debt" in the first place, for purposes of the bankruptcy law, based upon the traditional view that bankruptcy courts could not discharge criminal judgments.[357] But the Court declined to decide the case on that issue, instead specifically holding that the obligation was nondischargeable under section 523(a)(7).[358]

In reaching this conclusion, the Court agreed that monetary restitution is similar to a judgment for the benefit of a victim because, unlike a typical fine, the amount is ultimately paid to the victim and may be determined by reference to the amount of harm caused by the wrongdoer.[359] Nonetheless, the Court emphasized that the court of appeals had focused too heavily upon only the restitution portion of the state probation statute instead of its entirety.[360] There were other factors and considerations present that tended to negate this similarity.

The Supreme Court first noted generally that the criminal justice system is operated primarily for the benefit of society as a whole rather than for

346. *Kelly*, 479 U.S. at 39-40; *In re* Robinson, 776 F.2d 30, 32 (2d Cir. 1985).
347. *In re* Pellegrino, 42 Bankr. 129 (Bankr. Conn. 1984).
348. *In re* Robinson, 45 Bankr. 423, 424-25 (Bankr. Conn. 1984).
349. *Id.* at 425.
350. *In re* Robinson, 776 F.2d 30.
351. *Id.* at 33-39.
352. *In re* Robinson, 776 F.2d at 40.
353. *See supra* text accompanying note 345.
354. *See supra* text accompanying note 340.
355. *In re* Robinson, 776 F.2d at 40-41.
356. *Kelly*, 479 U.S. 36.
357. *Id.* at 50.
358. *Id.*
359. *Id.* at 51-52.

individual victims. Thus, the main concerns are the punishment and rehabilitation of the wrongdoer. Accordingly, the issue whether to impose a restitution obligation is generally not governed by the injury of the victim but, instead, by the penal and rehabilitative goals of the state and the situation of the offender. Consequently, the victim usually has no control over either the decision to award restitution or the amount thereof.[361] These general facets of the criminal justice system were evidenced in the entire state probation statute which gave the court discretion to impose any of eight specific conditions of probation as well as any other that is "reasonably related to . . . rehabilitation."[362] Moreover, the restitution portion made it clear that the amount set could be less than the loss suffered in view of its reference to an amount the offender "can afford to pay or provide in a suitable manner."[363] It was, therefore, a flexible probation condition designed to fit the wrongdoer's particular situation.[364]

The Supreme Court concluded that "[b]ecause criminal proceedings focus on the State's interests in rehabilitation and punishment, rather than the victim's desire for compensation, . . . restitution orders imposed in such proceedings operate 'for the benefit of' the State. Similarly, they are not assessed 'for . . . compensation' of the victim."[365] Accordingly, the restitution obligation was nondischargeable under section 523(a)(7) because it was part of the criminal sentence and was "not compensation for actual pecuniary loss."[366]

Similar reasoning can be applied to a Rule 11 monetary payment to the other party by the sanctioned attorney for purposes of section 162(f). One might, indeed, regard the Court in *Robinson* as having had the harder task in reaching its result in view of the statutory language of section 523(a)(7) that the debt not be "compensation for pecuniary loss." Contrariwise, section 162(f) itself contains no such specific language.

It is obvious, of course, that the meaning of the word "penalty" for purposes of nondischargeability under the bankruptcy act cannot automatically be imported into the meaning of that word for purposes of nondeductibility under the income tax law. That is because the two statutes are directed at different problems.[367] Therefore, the drawing of analogies between the bankruptcy and revenue laws can, no doubt, be risky. Nonetheless, to acknowledge the absence of automatic controlling force is not to say that certain aspects of the method of analysis by the Supreme Court in *Kelly v. Robinson* are of no importance in our Rule 11-section 162(f) context.

To recapitulate, the Court in *Robinson* had noted that the overall focus of state criminal proceedings and the state probation statute was on the wrongdoer

---

360. *Id.* at 43, 52.
361. *Id.* at 52.
362. *Id.* These other specific discretionary probation conditions included, *inter alia*, requiring the defendant to: (a) work at suitable employment or education; (b) undergo medical or psychiatric treatment; (c) support his or her dependents and meet other family obligations; (d) not violate any criminal law; and (e) reside in a halfway house and contribute to its costs. *See In re* Pellegrino, 42 Bankr. at 136 n.13; CONN. GEN. STAT. § 50a-30(a)(1)-(3), (7), (8) (1985).
363. *Kelly*, 479 U.S. at 52-53.
364. *Id.* at 53.
365. *Id.*
366. *Id.* at 50, 53.

with the goals being both punitive and rehabilitative. Because of that, the decision to award restitution did not depend upon the victim's injury, but, instead, upon the penal goals of the state and the particular situation of the wrongdoer. Thus, the victim had no control over either the issue of whether restitution was to be ordered or the amount thereof.[368] Consequently, the statute provided a flexible remedy tailored to the wrongdoer's circumstances, and the restitution order was not primarily to compensate the victim.[369]

Such analysis seems equally appropriate in the Rule 11 context. The major concerns behind the 1983 amendments to Rule 11 were widely acknowledged dilatory and abusive pretrial tactics by attorneys including the filing of frivolous pleadings, motion and other papers, and the need for streamlining litigation.[370] Because of this, the focus of amended Rule 11 is on the wrongdoer with the primary goal of its available sanctions being at least to deter the violator.[371]

Once the court has determined that a violation has occurred, then Rule 11 mandates the imposition of a sanction.[372] The particular sanction to impose is, however, a matter of discretion with the court,[373] the potential sanctions being very broad in scope.[374] We have seen that the most commonly encountered type of sanction is that of the costs and legal fees incurred by the opposing party.[375] But even when this sanction is chosen by the court, the amount awarded may be greater or lesser than the reasonable actual costs incurred by the victim.[376] As noted by the Advisory Committee, this allows the court "the necessary flexibility to deal appropriately with violations" and gives it "discretion to tailor sanctions to the particular facts of the case . . . ."[377]

This makes the Rule 11 situation very much akin to the state probation statute in *Kelly v. Robinson.* Both the restitution obligation in *Robinson* and payment of the other party's costs and attorney fees in the typical Rule 11 sanction have a compensatory flavor insofar as the victim is concerned; but, both were only one of a number of probation conditions and possible Rule 11 sanctions. In addition, the decision to award restitution or the other party's costs and attorney fees is determined by the penal and rehabilitative goals of the state or the punishment/deterrence objective of Rule 11, not by the need to compensate for losses suffered. Thus, as with the restitution ordered in *Robinson*, the victim of a Rule 11 violation does not control either the decision to award costs and attorney fees or the amount.

---

367. *See* Patton v. Commissioner, 71 T.C. 389, 390-91 (1978); Misbin v. Commissioner, 50 T.C.M. (CCH) 131, 134 (1985).
368. *Kelly*, 479 U.S. at 52.
369. *Id.* at 53.
370. *See Donaldson*, 819 F.2d at 1556; *Golden Eagle Distrib. Corp.*, 801 F.2d at 1536; *Zaldivar*, 780 F.2d at 829.
371. *Supra* notes 87-92 and accompanying text.
372. *Supra* notes 82-85 and accompanying text.
373. *See supra* notes 110-11 and accompanying text.
374. *See supra* notes 96-109 and accompanying text.
375. *Supra* note 94 and accompanying text.
376. *Supra* note 91 and accompanying text. *See* Advo Sys., Inc. v. Walters, 110 F.R.D. 426, 431 (E.D. Mich. 1986); *In re* Itel Sec. Litig., 596 F. Supp. 226, 234 (N.D. Cal. 1984), *aff'd*, 791 F.2d 672 (9th Cir. 1986); Heimbaugh v. City & County of San Francisco, 591 F. Supp. 1573, 1577 (N.D. Cal. 1984).
377. FED. R. CIV. P. 11, advisory committee notes, 97 F.R.D. 198, 200 (1983).

Therefore, the method of analysis utilized by the Court in *Kelly v. Robinson* seems reasonably transferable to our Rule 11—section 162(f) situation. It demonstrates that the mere compensatory effect of a payment to the victim of proscribed conduct is not, of itself, necessarily controlling as to whether or not it is a "penalty." Subsequent to *Kelly*, the Supreme Court again recognized, at least implicitly, this principle. More importantly, the high court has done this in a Rule 11 case in which it expressed the view that its purpose was punishment and deterrence rather than compensation.

In *Pavelic & LeFlore v. Marvel Entertainment Group*[378] the Supreme Court held that a Rule 11 monetary sanction could only be imposed upon the attorney who actually signed the offending paper and not also upon the law partnership or firm for which he had signed.[379] In reaching that conclusion the Court emphasized the nondelegable nature of the Rule 11 duty imposed upon the signer personally, to ascertain reasonably the factual and legal basis of the filed paper. The Court stated:

> Where the text establishes a duty that cannot be delegated, one may reasonably expect it to authorize *punishment* only of the party upon whom the duty is placed. We think that to be the fair import of the language here. . . . [To hold the law partnership accountable for its attorney's violation] would, to be sure, better guarantee reimbursement of the innocent party for expenses caused by the Rule 11 violation . . . . *The purpose of the provision in question, however, is not reimbursement but 'sanction'*; and the purpose of Rule 11 as a whole is to bring home to the individual signer his personal, nondelegable responsibility. It is at least arguable that these purposes are better served by a provision which makes clear that . . . it will visit upon him personally—and not his law firm—its *retribution* for failing in that responsibility. . . . Moreover, . . . there will be *greater* economic *deterrence* upon the signing attorney, who will know for certain that the district court will impose the sanction entirely upon him and not divert part of it to a partnership . . . .[380]

With this rationale for its decision it seems apparent that the Supreme Court has accepted the growing consensus of the lower courts and commentators[381] that the primary purpose of Rule 11 is not to compensate the victim, but, instead, is to punish, visit retribution on, and/or deter the offender.

We have seen (1) the language of the punishment essay by the Supreme Court in *United States v. Halper*,[382] (2) the fact that in nontax contexts the compensatory effect of a payment to the victim is not necessarily controlling on the issue whether that payment is a "penalty" as illustrated by *Kelly*, and, finally, (3) the rationale of the high court in *Pavelic & LeFlore*. From these it should be clear that a monetary sanction imposed upon an attorney under Rule 11 is a penalty intended to carry out the goals of punishment and/or deterrence.

---

378. 110 S. Ct. 456 (1989).
379. *See supra* text accompanying notes 169-80.
380. *Pavelic & LeFlore*, 110 S. Ct. at 459-60 (emphasis added).
381. *See supra* text accompanying notes 86-92.
382. *See supra* text accompanying note 316.

This is true even though the consequence or effect may be to compensate the victim.

In the light, then, of the *Middle Atlantic Distributors* test, such a monetary sanction comes within the "any fine or similar penalty" language of section 162(f).[383] This is simply a recognition of the fact that "deterrence through punishment (or discipline) is the stated goal of the Rule and that expense-shifting is one of many means to effect that goal."[384]

D. "Paid to a Government"

The fact that a monetary Rule 11 sanction, whether in the form of a fine paid to the court or in the form of legal costs paid to the victim, comes within the concept of a "fine or similar penalty" does not end our inquiry under section 162(f). An additional condition of that provision is that it must be "paid to a government." There is, of course, no problem under this element with a fine paid directly to the court.[385] But, at least initially, it would seem to present something of a sticking point with respect to legal costs paid to the other party.

---

383. Whether monetary payments made by the attorney pursuant to a nonmonetary Rule 11 sanction should come within section 162(f) is another matter. Assume, for example, that the court imposed upon an attorney a nonmonetary sanction requiring attendance at a continuing legal education program. *See* Stevens v. City of Brockton, 676 F. Supp. 26 (D. Mass. 1987). The sanctioned attorney then pays a registration fee plus meals and lodging costs in attending this program in another city. Would such derivative monetary payments be regarded as part of the sanction for Rule 11 purposes? If so, would they come within section 162(f)? The derivative monetary payment in this case has not been directly ordered by the court. The court has only commanded that the attorney attend a CLE program. Thus, the payment, although necessarily made to comply with the order, is at least one step removed. Accordingly, it can plausibly be regarded as not part of the sanction. Even if it were construed to be part of the sanction, however, query whether it should fall into the section 162(f) trap. It might be deemed to fail the next requisite of section 162(f) that it be "paid to a government," because the court did not, at least directly, command any payment. This requisite will be discussed in the following section of this Article. Normally, payments made by a licensed practicing attorney to attend CLE programs, even mandatory ones, would clearly be regarded as deductible business education expenses. *See* Treas. Reg. § 1.162-5(b)(3)(ii)(Ex. 3) (1967); Coughlin v. Commissioner, 203 F.2d 307 (2d Cir. 1953). It would seem to be bad policy to extend section 162(f) in this context in order to deny the deduction here. *Cf.* Treas. Reg. § 1.162-21(c) (Ex. 3) (1975) (section 162(f) does not prevent deductibility of amount paid to remedy nonconformity).

384. *See* S. BURBANK, *supra* note 5, at 26-27. A Rule 11 monetary sanction against an attorney solely may include not only the costs and attorney fees incurred by the victim in defending against the offending filing but also those related to obtaining the Rule 11 award. *Thompson*, 656 F. Supp. 1077. The regulation to section 162(f) provides, in part, that:

> The amount of a fine or penalty does not include legal fees and related expenses paid or incurred in the defense of a prosecution or civil action arising from a violation of the law imposing the fine or civil penalty, nor court costs assessed against the taxpayer, or stenographic and printing charges.

Treas. Reg. § 1.162-21(b)(2)(1975).

Under this regulation one might argue that the costs and attorney fees incurred by the victim to obtain, and made part of, the Rule 11 award would be deductible when paid by the sanctioned attorney, although he or she could not deduct when paid those legal expenses of the victim simply related to defending against the offending filing. But the better answer would seem to be that none are deductible. The reason is that, in this context, the regulation refers to expenses paid "in defense of" the Rule 11 motion. Thus, the offending attorney could deduct his or her own legal costs in unsuccessfully defending against the Rule 11 motion. This is simply a regulatory recognition of the doctrine of the *Tellier* case. See *Tellier*, 383 U.S. 687. But the legal costs of the other side — the successful Rule 11 movant — are not "defense" costs in any direct sense. They are at least one step removed, being the consequence of the attorney having lost on the Rule 11 motion.

385. *See supra* notes 96, 335 and accompanying text.

Neither the Service nor the courts, however, have construed the "paid to a government" element literally, one of the reasons being the origin of the claim doctrine—that the character of a payment is to be determined by the origin of the claim giving rise to it.[386]

One example of the application of this doctrine by the Service is where the taxpayer seeks to deduct under section 162 a reimbursement payment made to a third party who had previously paid a fine to the government. In Revenue Ruling 81-151,[387] the taxpayer was the chairman and chief executive officer of a corporation that had made illegal contributions to a political campaign committee with the taxpayer's approval. After a criminal information was filed against the corporation, it pleaded guilty and paid a fine.[388] Subsequently, a shareholders' derivative suit was filed against the taxpayer and others, asserting that they caused the corporation to engage in criminal acts. The taxpayer entered into a court-approved settlement under part of which he made a payment to the corporation to reimburse it for a portion of the fine.

The Service held that the taxpayer's partial reimbursement payment here was not deductible due to the proscription of 162(f), on the basis of the origin of the claim doctrine. In the Service's view the reimbursement to the corporation retained the original underlying character of the expense to which it related—the fine.[389] Such a holding can not be very controversial, particularly where something had, in fact, been "paid to a government," and the taxpayer's reimbursement thereof to the corporation could logically be seen as assuming that "paid to a government" flavor.

The Service has also applied section 162(f) to deny deductibility to a payment made by a taxpayer directly to a third party in lieu of the taxpayer's own potential liability for payment of a fine to the government. In Revenue Ruling 79-148,[390] the taxpayer was a manufacturer convicted of violating a federal criminal law restricting the sale of certain products to a particular country. Before the federal district court imposed any sentence, however, the taxpayer offered to make a contribution to a charity located in the town where the taxpayer had manufactured the illegally sold products. The amount of the offered contribution equalled the maximum fine that the court could impose for this violation. The court accepted the offer, suspending the sentence, placing the taxpayer on two years probation, and directing the taxpayer to pay the offered amount to the charity.

The taxpayer did so, and then deducted that amount on its federal income tax return as an ordinary and necessary business expense. The Service disallowed the deduction on the basis of the regulation to section 162(f) which includes within the term "fine or similar penalty" amounts "[p]aid in settlement of the taxpayer's actual or potential liability for a fine or similar penalty."[391]

---

386. *See supra* text accompanying notes 304-06, 318-31.
387. 1981-1 C.B. 74.
388. *See* 2 U.S.C.§ 441(b) (1976).
389. *Accord*, Priv. Ltr. Rul. 80-31-078 (Aug. 13, 1980); Priv. Ltr. Rul. 80-21-015 (June 4, 1980). *See also* Priv. Ltr. Rul. 80-31-098 (Aug. 13, 1980) (applying origin of the claim doctrine under section 162(c)).
390. 1979-1 C.B. 93.
391. Treas. Reg. § 1.162-21(b)(1)(iii) (1975).

The Service concluded that the amount paid to the charity was in lieu of having to pay that amount *to the government* as a fine.[392]

At least in the particular circumstances of this case, the effect of the ruling is to piggy-back on to the satisfaction of the "fine or similar penalty" element the "paid to a government" requisite. In other words, the application of the origin of the claim doctrine to payments made directly to third parties can have the result of automatically bootstrapping in the satisfaction of the "paid to a government" element, so long as the "fine or similar penalty" language has been met.

This view of the Service is consistent with a more recent Sixth Circuit decision. In *Bailey v. Commissioner*,[393] the taxpayer was a shareholder, officer and director of a corporation, receiving dividends, salary and bonuses in those various capacities and including them in his federal income tax returns. In 1971 the taxpayer had entered into a consent decree with the Federal Trade Commission under which he agreed, individually and as a corporate officer, not to operate the corporation's business in a deceptive or fraudulent manner or in violation of federal law.[394]

In 1976 a federal district court in California determined that the taxpayer had violated the consent decree and imposed a civil penalty of $1,036,000.[395] But the California federal court granted the taxpayer's request that his payment thereof be applied as restitution to private litigants in the settlement of a multidistrict class action suit against the corporation and its officers then pending in a Florida federal court. The California federal court's order provided that such use of the payment did not change its status as a civil penalty.[396]

In his 1977 federal income tax return the taxpayer utilized the benefits of the claim-of-right provision of the Code to obtain a substantial tax reduction attributable to this $1,036,000 payment.[397] Among its requisites, the claim-of-right section provides that the payment itself must be deductible. The Tax Court sustained the Service's denial of the claim-of-right treatment on the ground that the payment was not deductible due to section 162(f).[398]

On appeal, the taxpayer contended that section 162(f) did not apply because the payment was not made to the government, but, instead, went to private litigants as restitution.[399] The Sixth Circuit nonetheless affirmed on the basis of the origin of the claim doctrine and the fact that the "fine or similar penalty" test of *Middle Atlantic Distributors* had been met.[400] Admittedly, the *Bailey* decision is bolstered by the fact that the California federal court had

---

392. *Accord*, Priv. Ltr. Rul. 86-02-002 (Jan. 23, 1986) (also construing Rev. Rul. 79-148 as an application of the origin of the claim doctrine). In addition, the Service determined that the payment was not a deductible charitable contribution because it was not made voluntarily, but, instead, solely to avoid a potential fine. *See* I.R.C. § 170.

393. 756 F.2d 44 (6th Cir. 1985).

394. *Id.* at 45-46.

395. *See* 15 U.S.C. § 45(l) (1988) (civil penalty payable to United States for each violation of the Federal Trade Commission's final orders).

396. *Bailey*, 756 F.2d at 46.

397. *Id. See* I.R.C. § 1341 (1989).

398. *Bailey*, 756 F.2d at 46.

399. *Id.*

400. *Id.* at 46-47.

explicitly stated that the civil penalty status of the payment was not changed by its subsequent use as restitution for private litigants. But a bootstrapping effect was still present, akin to that of Revenue Ruling 79-148.

There is an alternative method of analysis in dealing with payments to third parties for purposes of the "paid to a government" requirement of section 162(f) producing the same ultimate result as the origin of the claim doctrine. This approach is illustrated by the Tax Court's decision in *Waldman v. Commissioner*.[401]

In *Waldman* the taxpayer had been charged with some twenty-nine counts of conspiracy to commit grand theft in connection with his operation of a loan brokerage business in California. In return for his plea of guilty to one count, the remaining twenty-eight counts were dismissed. The state court sentenced him to a prison term of one-to-ten years but stayed execution of that sentence on condition that he pay specified amounts of restitution to his victims. During the tax year in question, he paid some $28,500 in restitution, and deducted that amount on his federal income tax return. The Service denied that deduction due to, among other reasons, section 162(f), and the Tax Court sustained that disallowance.[402] With respect to the "paid to a government" element, the Tax Court said:

> *The State . . . exercised complete control over the ultimate disposition of petitioner's payments.* The court ordered petitioner to pay specified amounts of restitution to specified victims and informed him that '[i]f the court and the victims are not satisfied that things are going along as they should be . . . I will simply dissolve the stay of execution and you will be committed to State Prison.' *We do not believe that a Government must actually 'pocket' the fine or penalty to satisfy the 'paid to a government' requirement* of section 162(f). Petitioner's 'fine or penalty' was 'paid to a government' and is not deductible.[403]

Waldman espouses a standard requiring only that the court control where the monetary payment is to be made, with the precise actual destination being largely irrelevant. This reasoning has received the apparent approval of the Ninth Circuit.[404]

Under either the origin of the claim doctrine with its bootstrapping effect or the *Waldman* control test, it is clear that when a court has ordered an attorney to pay the other party's legal costs as a monetary Rule 11 sanction, it falls within the "paid to a government" requisite of section 162(f).[405] This would also seem to be good policy. To allow deductibility to turn on where the court requires the monetary payment to be made would be to exalt mere form

---

401. 88 T.C. 1384 (1987), *aff'd, substantially for the reasons stated below*, 850 F.2d 611 (9th Cir. 1988).
402. *Id.*
403. *Id.* at 1389 (emphasis added). The Tax Court has subsequently applied *Waldman* and the other considerations of section 162(f) in order to deny the deductibility of restitution payments under section 165(c)(2). *See* Stephens v. Commissioner., 93 T.C. 108, 113 (1989).
404. *Waldman*, 850 F.2d 611.
405. *Cf. Kelly*, 479 U.S. at 52-53, 56 n. 3.

over substance.[406] That is particularly true because the same ultimate goal of punishment or deterrence is being served by either type of monetary sanction, whether it be in the form of a fine payable to the court or a payment to the victim to cover legal costs incurred. Finally, it might tend to negate the federal district court's "flexibility to deal appropriately with violations . . . [and] to tailor sanctions to the particular case. . . ."[407]

E. "For the Violation of any Law"

The last requirement for the application of section 162(f) is that the payment be made "for the violation of any law." The issue becomes, then, whether amended Rule 11 of the Federal Rules of Civil Procedure constitutes a "law" for purposes of that provision. Its resolution will not detain us long. At the threshold of this area we are faced with the fact that section 162(f) was enacted by the Tax Reform Act of 1969 while Rule 11 was amended into its present form only as recently as 1983. Consequently, it might be argued that Congress could not have contemplated and, hence, did not intend, its application to Rule 11.

The Tenth Circuit confronted this issue recently in a case dealing with the availability of monetary Rule 11 sanctions against the government, a topic considered earlier in this Article.[408] In *Adamson v. Bowen*[409] the plaintiff had appealed the denial of social security disability benefits by the Secretary of Health and Human Services to the federal district court. That court reversed, finding the plaintiff to be totally disabled. In addition, the court imposed a monetary Rule 11 sanction upon the Secretary in the amount of about $1,775, consisting of the plaintiff's attorney fees in that court. The basis for the sanction was that the Secretary's defense was so lacking in evidentiary support that the government should have conceded the merits of plaintiff's claim.[410]

On appeal, the Secretary contended that sovereign immunity prevented the imposition of monetary sanctions against him. This position, in turn, raised the issue whether the Equal Access to Justice Act (EAJA) constituted a waiver of the immunity.[411] The relevant portion of EAJA generally provides that the United States shall be liable for attorney fees "to the same extent that any other party would be liable under the common law or *under the terms of any statute* which specifically provides for such an award."[412]

In the process of examining that question the Tenth Circuit initially dealt with the fact that the EAJA was enacted in 1980, prior to the 1983 amendment to Rule 11. The court held that this did not prevent its applicability for Rule 11 purposes.[413] Noting that the legislative history to the EAJA supported that view as well as the lack of any specific statutory limitation to law in existence at the

406. *See* Helvering v. Gregory, 69 F.2d 809, 810-11 (2d Cir. 1934) (Hand, J.), *aff'd*, 293 U.S. 465, 468-70 (1935).
407. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 200 (1983); *see supra* notes 181-83 and accompanying text.
408. *See supra* text accompanying notes 164-68.
409. 855 F.2d 668 (10th Cir. 1988).
410. *Id.* at 670, 674.
411. *Id.* at 670.
412. 28 U.S.C. § 2412(b) (1982) (emphasis added).
413. *Adamson*, 855 F.2d at 671-72.

time of enactment,[414] the court said that "Congress, in referring simply to the 'common law' and 'statutes' undoubtedly understood the shifting nature of both bodies of law and intended to encompass current law and subsequent changes."[415]

That is unquestionably the situation with respect to section 162(f) also. The codification of the public policy doctrine by TRA 1969 was intended, admittedly, to be all-inclusive of that concept so that doctrine could not be subsequently invoked to disallow business deductions *outside* of those specific statutory provisions.[416] But section 162(f) was one of those provisions, and its terms are very broad, indeed. It was obviously designed to encompass not only existing law but also any laws in the future.

That is the very thrust of such language as "or *similar* penalty paid to *a* government for the violation of *any* law."[417] Likewise, the legislative history indicates that it was the congressional intent to disallow civil sanctions that "in general terms serve the same purpose" as a criminal fine, without giving any hint of its being limited to the law already in existence.[418] The reasoning of *Adamson* with respect to the EAJA seems equally applicable to section 162(f).

Having disposed of that threshold problem, the question remains whether Rule 11 is a "law" for purposes of section 162(f). The *Adamson* decision is also of importance here. The Tenth Circuit ultimately concluded that the EAJA did constitute a waiver of sovereign immunity for purposes of Rule 11.[419] In so holding, the court construed the reference in the EAJA to "any statute"[420] as being broad enough to include Rule 11 because the Federal Rules of Civil Procedure have the force of a federal statute.[421]

The fact that the federal civil rules have such force does not seem realistically subject to much debate.[422] The words "any law" in section 162(f) appear to be intrinsically at least as far ranging, if not broader, than the words "any statute" in EAJA. Based upon the statutory equivalence of the federal civil rules and the reasoning of *Adamson*, Rule 11 comes within the meaning of "law" in section 162(f). Having established the satisfaction of all the specific elements for the invocation of section 162(f) the ineluctable conclusion is that monetary sanctions imposed solely upon attorneys under federal Rule 11 are not deductible.[423]

---

414. *Id.*
415. *Id.* at 672.
416. *See supra* text accompanying notes 268-73.
417. I.R.C. § 162(f) (1989) (emphasis added).
418. *See* S. REP. NO. 437, *supra* note 278, at 1980.
419. *Adamson*, 855 F.2d at 672.
420. *See supra* text accompanying note 412.
421. *Adamson*, 855 F.2d at 671.
422. *E.g., Sibbach*, 312 U.S. at 13; United States ex rel. Tanos v. St. Paul Mercury Ins. Co., 361 F.2d 838 (5th Cir. 1966); Laker Airways, Ltd. v. Pan Am. World Airways, 103 F.R.D. 42, 49, 50 n.19 (D.D.C. 1984). *See* 28 U.S.C.A. § 2072 (1982 & Supp. 1989); Griffith Co. v. National Labor Relations Bd, 545 F.2d 1194, 1197 n.3 (9th Cir. 1976), *cert. denied*, 434 U.S. 854 (1977).
423. As previously noted, a number of states have civil procedural rules, or statutes, identical or substantially similar to federal Rule 11. *See supra* note 7. Generally, to the extent that a state court construes such rule or statute in the same manner that the federal courts have construed Rule 11, then monetary sanctions imposed solely upon attorneys under such equivalent state law should likewise be nondeductible for federal income tax purposes due to

CONCLUSION

The 1983 amendments to the federal civil rules were, in large part, a response to abuses of the litigation process by both attorneys and parties. The changes to Rule 11 were specifically directed to pleadings, motions or other papers that were either frivolous or filed for an improper purpose.

The first portion of this Article discussed the fundamentals of amended Rule 11 in the form of an overview of its more significant elements and aspects in the light of recent federal appellate court decisions. In addition to its general scope, this included such things as the duties it imposes upon attorneys, the standard by which conduct is to be judged in determining the existence of violations, and some specific types of prohibited activity. The Rule 11 survey portion then proceeded to deal with the sanctioning power and such topics as its purpose, the range of potential sanctions available to the court, and the factors taken into account in the determination of a specific sanction.

In the second portion of this Article these various aspects of Rule 11 were then tied into the consideration of the question whether monetary sanctions imposed upon attorneys are deductible for federal income tax purposes. The initial issue in this connection is whether such payments constitute "ordinary and necessary" business expenses within the meaning of section 162(a). The general conclusion reached was that a payment by a sanctioned attorney has a lesser, but still substantial, chance of surviving this requisite, particularly the "necessary" aspect, as the violative conduct ranges up the scale of culpability from gross negligence to intentional impropriety.

On the other hand, if Rule 11 does impose only a negligence standard upon attorneys, then a payment by a sanctioned attorney based upon mere negligence is likely to qualify as an "ordinary and necessary" business expense. Regardless of the precise standard of care or duty imposed by Rule 11 and the payment of the monetary sanction being otherwise ordinary and necessary, the core feature of the tax deductibility issue is whether such a payment is nonetheless disallowed as a "fine or similar penalty" which is "paid to a government" for the "violation of any law" within the meaning of section 162(f).

Utilizing the general consensus that the principal purpose of Rule 11 is *to punish or deter* attorneys and parties from engaging in that type of litigation abuse, I ultimately conclude that section 162(f) applies to deny deductibility. Thus, monetary Rule 11 sanctions imposed solely upon attorneys without reimbursement by the client are not deductible for federal income tax purposes. This should be true whether the sanction is in the form of a fine payable directly to the court or legal costs and attorney fees paid to the other party.

As a matter of policy, this conclusion makes good sense. Surely, it is inappropriate to lessen the "sting" of a Rule 11 monetary sanction by permitting the sanctioned attorney to be given a subsidy in the form of a federal income tax deduction as a reward for his or her misconduct. Such a deduction would

---

section 162(f). This conclusion is supported by the legislative history to that provision. The Senate Finance Committee report stated that "[i]t was also intended that [section 162(f)] should apply to similar type payments under the laws of a State or other jurisdiction." S. REP. NO. 437, *supra* note 278, at 1980.

seem to make the sanction less likely to deter the attorney from litigation abuse in the future, an effect similar to that condemned by the Supreme Court in *Tank Truck Rentals*.[424]

The drafters of amended Rule 11 were concerned about the potential consequences of its new sanctioning power. These included the danger that it "could chill an attorney's enthusiasm or creativity in pursuing factual or legal theories," and the risk that it would produce unnecessary "satellite litigation."[425] These concerns have been echoed by the commentators.[426] Such fears can only be heightened by the apparent increasing frequency of Rule 11 controversies in the federal court system.[427]

There is at least some evidence that these dangers may be real.[428] For example, a Third Circuit Task Force study of Rule 11 cases has found that plaintiffs and/or their attorneys in civil rights cases were sanctioned at a rate in excess of five times that of plaintiffs and/or counsel in non-civil rights cases.[429] Moreover, there are sad examples of burgeoning satellite litigation over Rule 11 sanctions.[430]

The answer, if it is first determined that a serious problem exists for which a solution is required, is not to woodenly and narrowly construe section 162(f). Pretty clearly, that section presently precludes a federal income tax deduction for monetary Rule 11 sanctions. For the reasons already stated, it would be bad policy to permit any such deduction for conduct violative of that Rule. Beyond that, to reinterpret the federal taxing statute in order to deal with a problem that is essentially one of sound federal judicial administration would seem to be both inefficient and unwise. It is inefficient because it does not directly confront either the potential chilling effect of a monetary sanction or consequential satellite litigation; instead, it attacks these problems only indirectly by hoping to lessen their incidence with a tax deduction. Such an approach ignores the fact that in allowing a deduction the general effect would be to permit the sanctioned attorney to recover only a relatively minor portion of the monetary payment in tax saved.[431] It is questionable whether that would

---

424. *Tank Truck Rentals*, 356 U.S. at 35.

425. *See* FED. R. CIV. P. 11 advisory committee notes, 97 F.R.D. 198, 199, 201 (1983). With respect to satellite litigation, Professor Arthur R. Miller, Reporter, Advisory Committee on the Federal Rules of Civil Procedure, has said that he has had a "recurrent Kafkaesque dream" concerning a war of sanction motions between opposing attorneys. Annual Judicial Conference of the Second Judicial Circuit of the United States, 101 F.R.D. 161, 200 (1984). In the Rule 11 context, this dream has been realized. *E.g.*, Bygott v. Leaseway Transp. Corp., 637 F. Supp. 1433, 1447-48 (E.D. Pa. 1986).

426. *See, e.g.*, SANCTIONS, *supra* note 5, at 2; Levin & Sobel, *supra* note 5, at 601; Nelken, *supra* note 5, at 1338-43.

427. *See* SANCTIONS, *supra* note 5, at 1-2; Levin & Sobel, *supra* note 5, at 592 & n.24, 600 & n.78. Perhaps some courts have gone too far in their enthusiasm for the new Rule. *See* Dreis & Krump Mfg. Co. v. International Ass'n of Machinists & Aerospace Workers, Dist. No. 8, 802 F.2d 247, 255-56 (7th Cir. 1986) ("The rules . . . are being . . . enforced in this circuit to the hilt . . . . Lawyers practicing in the Seventh Circuit, take heed!").

428. *See* SANCTIONS, *supra* note 5, at 2.

429. *See*, S. BURBANK, *supra* note 5, at 69; Geyelin, *Rule to Curb Frivolous Lawsuits Found to be Used Most in Civil Rights Cases*, Wall St. J., Jun 1, 1989, at B7, col. 2. *See also* S. KASSIN, *supra* note 5, at 39.

430. *E.g., Brown*, 830 F.2d at 1440; *Golden Eagle Distrib. Corp.*, 801 F.2d at 1541.

431. The top current individual tax rate is generally 28%. See I.R.C. § 1 (1986).

be enough to thaw any "chill" otherwise created by the sanction or to make satellite litigation over the sanction any less likely.

It is unwise because section 162(f) includes within its scope many other payments in addition to Rule 11 monetary sanctions, and its meaning and application is fairly well understood. Any judicial reinterpretation of its elements in order to exclude Rule 11 from its coverage might have unforeseen collateral consequences. Hence, it seems better to leave changes in section 162(f), if deemed necessary, to the wisdom of Congress. Accordingly, it is not appropriate for a court to determine that section 162(f) does not apply to Rule 11 sanctions for the reason that, if it did, it would exacerbate the potential chilling and satellite litigation effects of that Rule.

Being a problem of sound federal judicial administration, if the courts were to follow their own cautionary admonitions that Rule 11 is to be "used with the utmost care and caution" and is "reserved only for exceptional circumstances" as it is "an extraordinary remedy," then much of the threat to legitimate advocacy and the danger of excessive satellite litigation would likely disappear.[432] The Ninth Circuit has attempted to deal with this issue by warning that "the inappropriate imposition of sanctions in this case is not an isolated occurrence. . . . District courts simply must use more restraint than was employed here."[433] In a word, if the courts were to exercise more "restraint," that would help greatly in the resolution of any alleged problems.[434]

It has been suggested further that greater use should be made of nonmonetary sanctions with respect to attorneys.[435] If that were done, generally reserving monetary sanctions for the more serious violations, it would likewise probably result in less satellite litigation and constitute less of a threat to zealous advocacy. It should not be forgotten that nonmonetary sanctions can carry their own "sting" for lawyers and their professionalism,[436] and, in many cases, will adequately carry out the ultimate deterrence purpose of Rule 11. In any event, monetary Rule 11 sanctions imposed upon attorneys seem to fit easily within both the letter and spirit of the section 162(f) proscription. And, that proscription marches hand-in-hand with, and serves the underlying primary goal of, Rule 11—to deter attorneys from abuse of the litigation process.

---

432. *See supra* notes 22-26, 246-49, and accompanying text.

433. Operating Eng'rs Pension Trust v. A-C Comp., 859 F.2d 1336, 1344-45 (9th Cir. 1988).

434. It has been suggested that emphasis on the punishment rationale for Rule 11 would produce more sparing use of sanctions. Schwarzer, *supra* note 5, at 1013, 1020 n.31. It is interesting to note that compensation (or cost shifting) oriented judges take a more expansive view of Rule 11 and are more likely to impose monetary sanctions than punishment-deterrence oriented judges. *See* S. BURBANK, *supra* note 5, at 9, 10; S. KASSIN, *supra* note 5, at 29, 31.

435. *See* S. BURBANK, *supra* note 5, at xv, 37-40, 97-98. *See also* Schwarzer, supra note 2, at 201-02. *See generally supra* notes 98-109 and accompanying text.

436. *See* Schwarzer, *supra* note 2, at 201-02 ; *supra* notes 337-38 and accompanying text.