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Fifth Circuit Survey: Taxation

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FIFTH CIRCUIT SURVEY: TAXATION

by Michael Hatfield*

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I. FIFTH CIRCUIT TAX ISSUES SURVEY: JUNE 2005-MAY 2006

During the survey period, the Fifth Circuit decided nine federal tax cases. Four of the nine cases were appealed from district courts. The remaining five were appealed from the Tax Court. Three of the Tax Court's five decisions (60%) were affirmed, and three of the four district court decisions (75%) were affirmed. Thus, the Fifth Circuit affirmed most of the lower court decisions (66%). Interestingly, only three of the decisions (33%) favored the taxpayer—EC Term of Years Trust v. United States; Garber Industries, Inc. v. Commissioner; and Estate of Baird v. Commissioner—even though the Fifth Circuit is often known as a taxpayer-friendly circuit.

As usual, the cases covered a broad range of issues from tax protests to family partnership valuation. In Gandy Nursery, Inc. v. United States, the Fifth Circuit reversed an award of post-judgment interest by the Eastern District Court of Texas and remanded the case to determine whether there had been unauthorized collection practices. In Estate of Baird v. Commissioner, the Fifth Circuit reversed the Tax Court for abusing its discretion in determining that the Internal Revenue Service (IRS) had substantial justification for its legal position and remanded the case to determine the

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2. Estate of Baird, 416 F.3d at 442; Strangi, 417 F.3d at 468; Estate of Smith, 429 F.3d at 533; Estate of Baird, 416 F.3d at 442.

3. Deaton, 440 F.3d at 223; Garber Indus., Inc., 435 F.3d at 555; Strangi, 417 F.3d at 468; Estate of Smith, 429 F.3d at 533; Estate of Baird, 416 F.3d at 442.

4. Deaton, 440 F.3d at 223; Garber Indus., Inc., 435 F.3d at 555; Strangi, 417 F.3d at 468.

5. Estate of Years Trust, 434 F.3d at 80; Saldana, 427 F.3d at 298; Simkanin, 420 F.3d at 397.

6. See Howard M. Zaritsky, Why FLPs Remain Useful After Strangi 4, 32 EST. PLAN 56 (2005), available at 2005 WL 2630614 (referring to the "Fifth Circuit's reputation as a circuit of easy virtue in estate tax matters").


amount to be awarded to the estate because the IRS did not have substantial justification. In *Strangi v. Commissioner*, the Fifth Circuit affirmed the Tax Court’s determination that Albert Strangi had impermissibly retained enjoyment of assets contributed to his family limited partnership. This was the fourth case in a series involving the Albert Strangi estate. In *United States v. Simkanin*, the Fifth Circuit affirmed the conviction of a tax protestor in the Northern District Court of Texas. In *United States v. Saldana*, the Fifth Circuit affirmed the convictions and sentences given by the Western Texas District Court to two brothers who filed false statements with the IRS to harass certain individuals. In *Estate of Smith v. Commissioner*, the Fifth Circuit decided that the Tax Court was without jurisdiction and vacated the Tax Court’s judgment that the IRS was precluded from offsetting unpaid interest against the overpayment due to the estate. In *EC Term of Years Trust v. United States*, the Fifth Circuit affirmed the United States Western District of Texas Court’s dismissal of a refund claim when the sole remedy was a wrongful levy action. In *Garber Industries, Inc. v. Commissioner*, the Fifth Circuit affirmed the Tax Court’s application of family attribution rules in a corporate reorganization, which limited the corporation’s deduction for net operating loss carryforwards. Finally, in *Deaton v. Commissioner*, the Fifth Circuit upheld the Tax Court’s determination that remittance filed with an application for a filing extension was a payment of estimated taxes rather than a deposit.

II. UNAUTHORIZED COLLECTION AND POST-JUDGMENT INTEREST: *GANDY NURSERY, INC.*

In *Gandy Nursery, Inc. v. United States*, the Fifth Circuit reviewed a judgment of the United States District Court for the Eastern District of Texas. Gandy Nursery, Inc., Gandy Marketing and Trucking, Inc. (GMT),

11. See id.
15. EC Term of Years Trust v. United States, 434 F.3d 807, 807 (5th Cir. Jan. 2006).
18. Gandy Nursery, Inc. v. United States, 412 F.3d 602, 603 (5th Cir. June 2005). If an agent of the IRS recklessly or intentionally disregards any provision of the Internal Revenue Code (Code) or the Treasury Regulations promulgated under the Code in connection with federal tax collection, Code Section 7433 gives the offended taxpayer the right to sue for actual, direct economic damages sustained by the taxpayer as a proximate result of the reckless or intentional actions of the officer or employee. I.R.C. § 7433 (2000). Except as provided in Code Section 7432, an action under Section 7433 is the exclusive remedy provided by the Code or Treasury Regulations for recovering damages resulting from intentional or reckless disregard by an IRS agent. 5 LAWRENCE F. CASEY, CASEY FEDERAL TAX PRACTICE § 14:77
and Dennis Gandy (appellees) brought an action against the United States seeking a refund for tax penalty assessments and damages for failure to release certain tax liens. The district court had ruled that the government engaged in unauthorized collection practices under section 7433 of the Internal Revenue Code (Code). The appellees were awarded refunds and damages. On appeal, the Fifth Circuit remanded the case. On remand, the district court found that the government violated section 7433 as a matter of law and determined that GMT incurred $100,000 in damages with post-judgment interest. The government appealed. The Fifth Circuit reversed the award of post-judgment interest on the damages and remanded the case to determine whether the IRS was liable under section 7433.

A. Background

In November 1995 the appellees filed an action against the government seeking a refund and abatement of income tax, income tax penalties, and employment tax penalties. The appellees asserted claims for negligent failure to release tax liens under Code Section 7432 and for damages for unauthorized tax collection practices under section 7433. The district court and an advisory jury determined that the appellees were entitled to $11,262.42 for their employment tax refund claims. The court further determined that GMT was entitled to $16,800 under section 7432 because the government failed to release a tax lien filed in 1995.

On appeal, the Fifth Circuit affirmed the tax refunds and the damages awarded under section 7432, but the Fifth Circuit remanded the case to determine whether the government was liable under section 7433 for unauthorized collection actions for its conduct in 1995 when it filed liens against GMT. On remand, the district court concluded that the government was liable and reduced the $388,500 in damages recommended by the jury to


20. Id. at 603.
21. Id.
22. Id.
23. Id.
24. Id.
25. Id. at 609.
26. Id. at 603.
27. Id. If an IRS agent knowingly or negligently fails to release certain liens on a taxpayer’s property, section 7432 enables the offended taxpayer to bring a civil action to recover actual, direct economic damages incurred by the taxpayer that would not have been incurred but for the actions of the IRS, plus the costs of the action. CASEY, supra note 18, § 14:75.
29. Id.
30. Id. at 604.
the statutory cap of $100,000. The district court also awarded costs and attorneys fees to the appellees and ordered the government to pay the interest accrued post-judgment on the $16,800 awarded to GMT in the first trial. The government appealed.

B. Analysis of Legal Issues

The first issue the Fifth Circuit decided was whether the district court erred in finding the government liable as a matter of law under section 7433 for filing the liens in 1995. The Fifth Circuit reviewed this issue de novo. In order for a taxpayer to prevail under section 7433, the taxpayer must establish that the government either recklessly or intentionally disregarded a Code provision in conjunction with the collection of federal taxes.

The court began the analysis by reviewing the district court’s previous orders to evaluate whether there was a determination of liability against the government. The Fifth Circuit determined that the district court did not address the 1995 liens filed against GMT in its first order, and therefore, the district court’s first order could not be read to support a section 7433 liability determination against the government.

The appellees argued that the Fifth Circuit had previously determined liability against the government when the case came up on the first appeal. The Fifth Circuit clarified that it had not made any liability determinations and pointed to the language of its opinion where it specifically stated, “[W]e remand to the district court for further consideration regarding whether the filing of the April 1995 and September 1995 liens may constitute unauthorized collection actions under Code Section 7433.” The Fifth Circuit noted that the district court did make some additional findings of fact and conclusions of law on remand but many of the findings were simply restatements from its first order. Furthermore, in support of its liability determination, the district court simply referred to the language in the Fifth Circuit’s opinion, but the Fifth Circuit noted that the language in the opinion did not establish liability under section 7433.

31. Id.
32. Id.
33. Id.
34. Id.
35. Id.
36. Id. at 605.
37. Id.
38. Id.
39. Id.
40. Id. at 606.
41. Id.
42. Id.
The Fifth Circuit had previously determined that section 7433 was not the appropriate vehicle to recover damages related to improper assessment of taxes in Shaw v. United States. The court in Shaw stated that proof of distinctive facts is required in order to demonstrate an improper assessment of taxes and establish improper collection activities. When claiming improper collection practices, the taxpayer must prove that the IRS did not follow the prescribed procedures of acquiring assets. The court in Shaw also held that a taxpayer is not entitled to damages for an improper assessment of taxes under section 7433. The court further held that a per se violation of section 7433 does not result from filing a tax lien based on an invalid tax assessment.

The Fifth Circuit noted that the district court did not focus on the methods used by the government in attempting to collect on monies, and the reassessments of employment tax penalties were against Dennis Gandy d/b/a Gandy Nursery, rather than GMT. Additionally, the lien filed against GMT in April 1995 related to unpaid interest that GMT owed on prior unpaid employment taxes, not to reassessment of tax penalties, and no evidence that a lien was filed against GMT in September 1995 existed. Therefore, the Fifth Circuit concluded that the district court had not made the necessary findings to support its liability determination under section 7433.

In the second issue, the Fifth Circuit addressed whether the district court erred in awarding post-judgment interest on the $16,800 in damages that it had previously awarded GMT under section 7432. The Fifth Circuit stated that parties cannot recover interest on claims against the government absent a constitutional requirement or express statutory provision. Because Congress has promulgated statutes expressly authorizing parties to recover interest on judgments against the United States, the court presumed that if Congress intended for the government to pay interest under section 7432, the statute would state that intention. There is no express waiver of sovereign immunity in section 7432. Additionally, because Code section 1961(c) allows parties to recover interest against the government only in suits filed in the United States Court of Appeals for the Federal Circuit and the United States Court of Federal Claims, waiver of immunity is not necessary for suits filed in the Fifth

43. Id. at 607 (citing Shaw v. United States, 20 F.3d 182, 184 (5th Cir. 1994)).
44. Id. (citing Shaw, 20 F.3d at 184).
45. Id. (citing Shaw, 20 F.3d at 184).
46. Id. (citing Shaw, 20 F.3d at 184).
47. Id. (citing Shaw, 20 F.3d at 184).
48. Id.
49. Id.
50. Id.
51. Id. at 608.
52. Id.
53. Id.
54. Id.
Therefore, the district court erred in awarding post-judgment interest to GMT on damages recovered under section 7432.\textsuperscript{56} The Fifth Circuit held that the district court did not make the necessary findings to support its liability determination that the government, as a matter of law, recklessly or intentionally filed tax liens against GMT and reversibly erred when it awarded GMT post-judgment damages.\textsuperscript{57} The Fifth Circuit remanded the case so that the district court could provide specific findings as to whether the government recklessly or intentionally violated the Code and thus, whether the government was liable under section 7433 when it filed the 1995 liens.\textsuperscript{58}

**C. Commentary**

*Gandy Nursery* is one more addition to an exceptionally long line of sovereign immunity cases begun by *Gordon v. United States*.\textsuperscript{59} *Gandy Nursery* applies to section 7432’s general rule that post-judgment interest is not recoverable on claims against the United States unless a specific statute, contract, or act of Congress waives immunity of the United States and consents to liability for interest.\textsuperscript{60} Thus, unless the specific statutory requirements are met, the party is not entitled to post-judgment interest.\textsuperscript{61}

**III. Litigation Costs from the Internal Revenue Service: Estate of Baird**

In *Estate of Baird v. Commissioner*, the estate of John L. Baird and the estate of Sara W. Baird appealed the Tax Court’s determination that the estates were not entitled to an award of administrative and litigation costs under Code Section 7430.\textsuperscript{62} The Tax Court held that the IRS was substantially

\begin{footnotes}
\item[55.] Id. at 608-09.
\item[56.] Id.
\item[57.] Id.
\item[58.] Id.
\item[60.] See 77 AM. JUR. 2D United States § 46 (2006); BOELTER, supra note 59, § 4:75; WARREN, supra note 59, § 19.
\item[61.] See 77 AM. JUR. 2D United States § 46 (2006); BOELTER, supra note 59, § 4:75; WARREN, supra note 59, § 19.
\item[62.] Estate of Baird v. Comm’r, 416 F.3d 442, 443-44 (5th Cir. July 2005). In certain situations, a taxpayer’s expense of participating in administrative and judicial proceedings generally can be recovered if the IRS’s position was not substantially justified, meaning, in practical terms, that the IRS’s pursuit of a case was unreasonable because the agents knew or should have known that there was little or no chance of winning. See, e.g., Ridgeley A. Scott, *Suing the IRS and Its Employees for Damages: David and Goliath*, 20 S. Ill. U. L.J. 507, 535 (1996).\end{footnotes}
justified in taking the position that the only discount allowable when valuing the decedents' non-controlling fractional interests in Louisiana timberland was the cost of partitioning the property.\textsuperscript{63} The Fifth Circuit reversed the Tax Court for abusing its discretion in determining that there was substantial justification.\textsuperscript{64} The Fifth Circuit then remanded the case to the Tax Court to determine the amount to be awarded to the estates.\textsuperscript{65}

A. Background

Mr. Baird's estate included a fourteen sixty-fifths undivided interest in a Louisiana trust that held 2,957 acres of timberland in sixteen noncontiguous tracts in Sabine Parish, Louisiana.\textsuperscript{66} Mrs. Baird's estate included a seventeen sixty-fifths interest in the same trust.\textsuperscript{67} In March 1996 Mr. Baird's estate filed an initial estate tax return claiming a 25\% fractionalization discount from the pro rata fair market value of his fourteen sixty-fifths interest in the sixteen tracts held by the trust.\textsuperscript{68} In January 1997 Mrs. Baird's estate filed its initial estate tax return claiming a 50\% fractionalization discount from the pro rata fair market value of her seventeen sixty-fifths interest in the sixteen tracts held by the trust.\textsuperscript{69} Then, in February 1997, Mr. Baird's estate filed an amended estate tax return claiming a 50\% fractionalization discount for the sixteen tracts.\textsuperscript{70}

In June 1998 the IRS issued notices of proposed adjustments and rejected the estates' claimed fractionalization discounts.\textsuperscript{71} The IRS asserted that the only discount should have been the estimated costs of a hypothetical partition in kind.\textsuperscript{72} This position was based on an IRS forester's report.\textsuperscript{73} The report estimated costs resulting in a 3.37\% discount for Mr. Baird's estate and a 3.11\% discount for Mrs. Baird's estate.\textsuperscript{74} In response, the estates filed protest letters and attached expert reports criticizing the IRS forester's use of transactions involving sales of controlling interests and explaining the risks and difficulties in partitioning the sixteen tracts.\textsuperscript{75} The letters also stated that any partitioning would be vigorously resisted.\textsuperscript{76}

\footnotesize
\begin{itemize}
\item 63. Estate of Baird, 416 F.3d at 443.
\item 64. Id.
\item 65. Id.
\item 66. Id.
\item 67. Id. at 444.
\item 68. Id.
\item 69. Id.
\item 70. Id.
\item 71. Id.
\item 72. Id.
\item 73. Id.
\item 74. Id.
\item 75. Id. at 444-45.
\item 76. Id. at 445.
\end{itemize}
Counsel for the estates offered to settle for a 45% fractionalization discount during an appeals conference in Shreveport, Louisiana. The offer was not accepted at that time, so the co-executors sent a letter to the IRS Appeals Office repeating the offer. The IRS did not respond, and in March 1999 the IRS issued notices of deficiency taking the same position. The notices of deficiency reflected additional tax due from each estate based on the forester’s valuation of the tracts.

In March 1999 and May 1999 respectively, Mr. and Mrs. Baird’s estates filed a claim for refund based on increasing the fractionalization discount from 50% to 60%. In May 1999 both estates filed petitions for redetermination of deficiencies. The IRS asserted the same position in its answer that it had asserted in its notices. The IRS attempted to settle the valuation issue, but the estates would not agree to discuss settlement unless the IRS agreed to a minimum 45% discount. The estates later demanded a 70% discount.

The Tax Court held that the estates established that noncontrolling fractional interests in Louisiana timberland were discounted, on average, 55% and that an additional 5% was appropriate due to peculiar circumstances regarding the decedents’ family members. The estates requested an award of reasonable litigation and administrative expenses, but the Tax Court held that the IRS’s position was substantially justified in the proceedings and denied the motion.

B. Analysis of Legal Issues

The issued considered by the Fifth Circuit was whether the Tax Court abused its discretion in determining that the IRS’s position in the administrative and judicial proceedings was substantially justified. Courts may award prevailing parties in a tax case reasonable administrative and litigation costs under section 7430 unless the position of the IRS is substantially justified. The position is substantially justified if it “is justified to a degree that could satisfy a reasonable person.”
According to the record, the IRS maintained the same position throughout the administrative and judicial proceedings. The IRS’s position was that the only allowable discounts were estimated costs of a hypothetical partition in kind as determined in the IRS forester’s report.

The Tax Court based its determination on the argument that the information received by the IRS was insufficient to discredit the position that the partition was a viable alternative. The Fifth Circuit determined that the Tax Court abused its discretion based on the information provided by the estates.

Mr. Baird’s initial estate tax return contained an appraisal report providing an opinion of the fair market value of the sixteen tracts and applying a 25% discount for the fractional interest due to the fact that a minority owner cannot force the sale of the timber and the fact that the difficulty of marketing timberland is compounded by a minority interest. A supplemental statement indicated that an in-kind partition could only be achieved with the unanimous consent of all remaining co-owners and co-trustees of the trust, and the likelihood of this was so remote as to be negligible. A hypothetical purchaser of the fourteen sixty-fifths interest who elected to receive the pro rata share of distributions from timber cutting would likely apply a discount of substantially more than 25% because of the absence of the right to enter timber cutting or other agreements without the consent of the other co-owners. The trust agreement also required that any transfer of trust property be made to a principal or income beneficiary of the trust unless all of the current beneficiaries gave written consent for transfer to a third party.

Mrs. Baird’s estate tax return and Mr. Baird’s amended estate tax return attached a supplemental statement and appraisal asserting that a 50% discount was appropriate given the lack of control and the remote likelihood of an in-kind partition. The statement explained that the appraisal in Mr. Baird’s original return was based on an average of discounts permitted in two previous cases cited in the appraiser’s reports that involved comparable transactions in Louisiana timberland.

The estates filed a protest letter citing a Louisiana statute that prohibits a buyer of timberland from a co-owner or co-heir from removing the timber
without the approval of the co-owners owning at least 80% of the land
interests. Furthermore, the IRS forester’s report failed to recognize that at
the time of Mr. and Mrs. Baird’s deaths, no co-owner had an interest large
enough to secure the legal right to cut with the purchase of either decedent’s
interest. The protest letter discussed case law allowing large
fractionalization discounts and contained letters from the estates’ experts
explaining the difficulties and risks involved in a partition proceeding.

The Fifth Circuit also noted that the Tax Court acknowledged that facts
available to a hypothetical knowledgeable buyer should be factored into a
discount, and these facts indicated that the remaining family members would
resist and cause difficulty for an outside buyer. These facts were also
available to the IRS when it took its position.

The Fifth Circuit concluded that the estates provided sufficient
information to the IRS to alert it that an in-kind partition was not viable, and
the IRS forester’s estimated costs of a hypothetical partition in kind were
speculative and unsupported. The IRS could not rely solely on its expert’s
opinion and should have been aware of relevant legal authorities and of
Louisiana law relating to partition of real property. The Fifth Circuit further
noted that the IRS continued to stick with its position, even after trial.

The Fifth Circuit next addressed the Tax Court’s reasoning that the
estates’ increasing discount claims from 25% to 50%, 50% to 60%, and 60%
to 90%, each supported by expert opinion, were a second justification for
concluding that the IRS was substantially justified in its position. The Fifth
Circuit again held that the Tax Court abused its discretion by relying on the
increases in claimed discounts because the IRS maintained the consistent
position that no discounts were permissible other than the partition costs
estimated in the IRS forester reports. Additionally, the estates provided
explanations for each of the claim increases and supported them with expert
opinions. Also, the estates claimed the 90% discount post-trial, so the claim
had no effect on the IRS’s litigating position. The Fifth Circuit remanded
the case to determine the fees to be awarded to the estates.

101. Id. at 450-51.
102. Id. at 451.
103. Id.
104. Id.
105. Id.
106. Id. at 451-52.
107. Id. at 452-53.
108. Id. at 453.
109. Id.
110. Id. at 454.
111. Id.
112. Id.
113. Id. at 455.
The *Estate of Baird* decision is important from both the estate planning and administration perspectives. From the estate planner's perspective, the Fifth Circuit has confirmed the essential planning principle that a fractional interest in property does not have a fair market value equal to its aliquot share whenever evidence shows that it could not actually be sold to a hypothetical buyer without a discount.\(^{114}\) The position taken by the IRS—discounting only by partitioning costs—is not uncommon, but, fortunately from the planner's perspective, has been undercut by the decision.\(^{115}\) From the estate administrator's perspective, the award of administrative and litigation costs is significant precisely because the IRS's position in the case is not uncommon but is unreasonable.\(^{116}\) The decision should encourage a more realistic and reasonable negotiation between IRS agents and Fifth Circuit estate administrators.\(^{117}\)

### IV. ESTATE VALUATION: STRANGI

Two Tax Court cases and two Fifth Circuit cases have involved Albert Strangi's estate plan.\(^{118}\) The fourth case, *Strangi v. Commissioner*, was the second, and presumably final, Fifth Circuit case.\(^{119}\) In the first Tax Court case, the Tax Court sided with Albert Strangi's estate over the IRS.\(^{120}\) The IRS moved for leave to amend its arguments in order to raise an issue under Code Section 2036(a) that Albert Strangi had retained a life estate in assets transferred to the Strangi Family Limited Partnership (SFLP), but the Tax Court denied the motion.\(^{121}\) The IRS appealed to the Fifth Circuit, and the Fifth Circuit remanded the matter to the Tax Court to consider the IRS's retained life estate argument.\(^{122}\) In the second Tax Court case, the Tax Court determined that Strangi had retained enjoyment of assets transferred into the

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116. See id.

117. See id.

118. Strangi v. Comm'r, 417 F.3d 468 (5th Cir. July 2005); Estate of Strangi v. Comm'r, 293 F.3d 279 (5th Cir. 2002); Strangi v. Comm'r, 85 T.C.M. (CCH) 1331 (2003), aff'd, 417 F.3d at 468; Estate of Strangi v. Comm'r, 115 T.C. 478 (2000), rev'd, 293 F.3d at 279.

119. See Strangi, 417 F.3d at 468.

120. Id.

121. Id.

122. Id.
SFLP, and therefore, the assets were properly included in the estate. In the second Fifth Circuit case, the estate appealed, but the Fifth Circuit affirmed the Tax Court.

A. Background

Upon failing health, Strangi transferred personal assets worth approximately ten million dollars into a family limited partnership. The partnership was created in August 1994 after Strangi’s son-in-law, an attorney, attended a seminar that promoted using limited partnerships as a means of lowering the taxable value of an estate. Strangi’s son-in-law, acting under power of attorney on behalf of Strangi, created the SFLP and Stranco Inc., which was the sole general partner of SFLP. He transferred assets valued at $9,932,967—98% of Strangi’s assets—in exchange for a 99% limited partner interest. He then transferred $49,350 of assets to Stranco in return for 47% of Stranco’s common stock. Strangi’s four children purchased the remaining 53% of Stranco’s common stock. Stranco then purchased its 1% general partnership interest in SFLP with a check.

In the end, under the SFLP partnership agreement, Stranco had sole authority to control SFLP’s business affairs with a 1% general partnership interest, and Strangi had no formal control with a 99% limited partnership interest. Strangi owned 47% of Stranco’s common stock, and each of his children owned a 13% share. Stranco’s articles of incorporation named Strangi and his four children as the initial board of directors, and after meeting, they employed Strangi’s son-in-law as manager of Stranco.

Prior to and after Strangi’s death in October 1994, SFLP made various payments to meet Strangi’s needs and expenses. SFLP distributed $8,000 and $6,000 to Strangi in September and October of 1994 and made proportional distributions to Stranco. In 1994, SFLP also distributed approximately $40,000 to pay for Strangi’s funeral and estate administration.

123. Id. at 472.
124. Id.
125. Id.
126. Id. at 473.
127. Id.
128. Id.
129. Id.
130. Id.
131. Id.
132. Id.
133. Id.
134. Id. at 473-74.
135. Id. at 474.
136. Id.
expenses as well as various personal debts incurred by Strangi.\textsuperscript{137} SFLP distributed approximately $65,000 in 1995 and 1996 to pay for Strangi’s estate expenses and a specific bequest by Strangi.\textsuperscript{138} SFLP also distributed $3,187,800 to the estate in 1995 to pay federal and state inheritance taxes.\textsuperscript{139} Prior to his death, Strangi transferred a house to SFLP but continued to live in the house.\textsuperscript{140} While SFLP charged rent for the two months Strangi lived in the house, it was not actually paid until 1997.\textsuperscript{141}

The IRS issued a notice of deficiency to the estate in December 1998 asserting that the estate owed federal estate tax of $2,545,826 or, alternatively, federal gift tax of $1,629,947.\textsuperscript{142} The IRS determined that Strangi’s interest in SFLP was the actual value of the assets transferred.\textsuperscript{143} The estate challenged the determination of the deficiencies in Tax Court.\textsuperscript{144} The Commissioner moved for leave to amend his answer prior to trial to include the alternative theory that code section 2036(a) required inclusion in Strangi’s taxable estate of the full value of the assets Strangi transferred to SFLP and Stranco.\textsuperscript{145} The Tax Court denied the motion and held for the estate, and the Commissioner appealed.\textsuperscript{146} The Fifth Circuit remanded the case with instructions for the Tax Court to set forth its reason for denying the Commissioner’s motion for leave to amend or reverse its denial.\textsuperscript{147} On remand, the Tax Court found for the Commissioner and upheld the initially assessed estate tax deficiency.\textsuperscript{148} The estate appealed.\textsuperscript{149}

\textbf{B. Analysis of Legal Issues}

The Fifth Circuit first considered whether Strangi retained rights to possess or enjoy the assets transferred to SFLP.\textsuperscript{150} The Fifth Circuit noted that section 2036(a) is meant to prevent the avoidance of the estate tax by employing testamentary substitutes permitting transferors to retain lifetime enjoyment of purportedly transferred property.\textsuperscript{151} The section provides that if the decedent retains either “(1) ‘possession or enjoyment’ of the transferred

\textsuperscript{137} Id.
\textsuperscript{138} Id.
\textsuperscript{139} Id.
\textsuperscript{140} Id.
\textsuperscript{141} Id.
\textsuperscript{142} Id.
\textsuperscript{143} Id.
\textsuperscript{144} Id. at 475.
\textsuperscript{145} Id.
\textsuperscript{146} Id.
\textsuperscript{147} Id.
\textsuperscript{148} Id.
\textsuperscript{149} Id.
\textsuperscript{150} Id. at 476.
\textsuperscript{151} Id.
property; or (2) 'the right . . . to designate the persons who shall possess or enjoy the property . . . ' after the transfer, the decedent's transferred property will be included in the taxable estate. Transferors retain possession or enjoyment if they retain a "substantial present economic benefit" from the property." This benefit can result from either an express or implied agreement at the time of the transfer that the transferor will continue to either possess or enjoy the property.

Because no express agreement existed, the question was whether an implied agreement existed. Whether an implied agreement existed is a finding of fact, and the Fifth Circuit reviewed the Tax Court's decision for clear error. The Fifth Circuit stated that the assurance that assets will be available to pay debts and expenses at the time of death is part of the possession and enjoyment of one's assets, and that assurance is what Strangi retained in this case. SFLP paid for expenses associated with Strangi's funeral and estate administration as well as specific bequests and assorted personal debts. Additionally, Strangi retained possession of a residence after its transfer to SFLP without paying rent until 1997. The deferral of payment provided a substantial economic benefit. Strangi retained assets barely sufficient to meet his own living expenses after creating SFLP, and at the same time, he began receiving substantial monthly payments from SFLP. For these reasons, the Fifth Circuit concluded that the Tax Court did not clearly err in holding that Strangi and his children implicitly agreed that Strangi would have continuing access to his assets, thereby retaining possession or enjoyment.

The second issue the Fifth Circuit considered was whether the transfer of property met the bona fide sale exception in section 2036(a), which provides that a transfer of property constituting a bona fide sale for full and adequate consideration in money or money's worth is excluded from the taxable estate. Because the assets were transferred into a partnership in exchange for a proportional interest therein, the adequate and full consideration requirement was satisfied.

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152. Id. (quoting I.R.C. § 2036(a) (2002)).
153. Id. (quoting United States v. Byrum, 408 U.S. 125, 145, 150 (1972)).
154. Id. (citing Treas. Reg. § 20.2036-1(a) (2006)).
155. Id.
156. Id. at 477.
157. Id.
158. Id.
159. Id.
160. Id.
161. Id. at 478.
162. Id.
163. Id.
164. Id. at 478-79.
The Fifth Circuit, however, held that the bona fide sale requirement was not satisfied.\textsuperscript{165} A bona fide sale is one that, as an objective matter, serves a substantial business or non-tax purpose.\textsuperscript{166} The estate presented five non-tax rationales to justify Strangi's transfer of assets to SFLP.\textsuperscript{167} First, the estate asserted that the transfer deterred potential tort litigation by Strangi's former housekeeper who had sustained an injury on the job, but Strangi paid all of her medical expenses and salary during her absence from work.\textsuperscript{168} No evidence that the housekeeper ever threatened to take any action existed.\textsuperscript{169} The estate also contended that SFLP deterred a will contest by Strangi's second wife's children.\textsuperscript{170} But those children retained counsel prior to the creation of SFLP, and no one ever contacted the estate about Strangi's will or made a claim against the estate.\textsuperscript{171} Third, the estate argued that SFLP deterred the corporate co-executor named in Strangi's will from serving.\textsuperscript{172} The Fifth Circuit noted that a fact-finder could infer a causal relationship between SFLP and the corporate executor's withdrawal, but the Tax Court's decision not to do so was not clearly erroneous.\textsuperscript{173} Fourth, the estate contended that SFLP was a joint investment vehicle for its partners.\textsuperscript{174} But SFLP neither invested nor conducted any active business.\textsuperscript{175} Lastly, the estate argued that SFLP facilitated centralized, active management of Strangi's working interests, but it was undisputed that a majority of the transferred assets did not require active management.\textsuperscript{176}

Finally, the estate argued that the Tax Court abused its discretion by denying the estate's request for leave to amend its petition to apply the doctrine of equitable recoupment to include a computational offset for a time-barred income tax refund.\textsuperscript{177} The doctrine of equitable recoupment arises when the Commissioner brings a timely suit for payment of taxes and the taxpayer tries to offset that amount with a time-barred claim seeking a refund of erroneously imposed taxes.\textsuperscript{178} Thus, the doctrine allows the taxpayer to raise a refund claim that is otherwise time-barred.\textsuperscript{179}
The Fifth Circuit noted that the taxpayer must show that the refund sought is actually time-barred in order to sustain a claim for equitable recoupment. The estate, however, had a separate action pending in which it contended that the disputed refund was not time-barred. The estate simply argued that the Tax Court's decision was inequitable, and it failed to address the underlying merits of the decision. Therefore, the Fifth Circuit held the estate did not prove any abuse of discretion by the Tax Court.

C. Commentary

This fourth and hopefully final Strangi case belongs in the broader context of family limited partnership and estate tax discount planning and litigation. Although the case was a Fifth Circuit victory for the IRS, it has to be viewed as one Fifth Circuit case in a series on the issues and the only one that was favorable to the IRS. Wheeler, Kimbell, and Church had, perhaps, encouraged some estate planners to believe the Fifth Circuit would never side against the taxpayer on these issues. But in some circumstances, we now know, the Fifth Circuit will say no.

As a practical matter, the planning strategies following Strangi are the same as those before, simply with a renewed awareness that following sound operational principles is as important as cautious estate planners have always insisted. Capital accounts should be created and maintained correctly. There should be solid evidence of an objective, non-tax, or other substantial business purpose. Clients should have sufficient substantial assets outside the partnership to maintain their accustomed standard of living and cover their estate administration. The partnership and terms of the agreement should be respected promptly in all events—rent or other payments between partners and the partnership should be made and not merely accrued. Sharing the management power with someone other than the client may be important if one of the primary non-tax purposes of the partnership is reducing the
managing burden on the client. Each of these, however, illustrates the sort of meticulous planning that conservative estate planners have always thought best. In other words, the Strangi decision is unlikely to chill family limited partnership planning so much as provide planners and clients with a useful outline of what to avoid in order to establish good “facts on the ground” with the family limited partnership estate plan.

V. TAX PROTEST: SIMKANIN

In United States v. Simkanin, the taxpayer-appellant appealed his conviction and eighty-four month prison sentence in the Northern District Court of Texas for willfully failing to collect and pay employment taxes, knowingly making and presenting false claims for refund of employment taxes, and failing to file federal income tax returns. The Fifth Circuit affirmed.

A. Background

Richard Simkanin did not file income tax returns for the years 1996 to 2001. In addition, he owned a corporation and failed to collect and pay employment taxes from January 2001 until the dissolution of the corporation in July 2001. Simkanin met with an accountant several times, and on several occasions the accountant advised Simkanin to pay taxes. Simkanin stated that he was not required to pay taxes and that filing tax returns was voluntary. Although the accountant advised Simkanin that filing returns was not voluntary and that Simkanin could get in trouble, Simkanin rejected the advice.

Simkanin was a member of an organization, We The People Foundation for Constitutional Education, which promoted the view that Americans are not required to pay income taxes or employment taxes. In 1996 he mailed a

193. Id.
195. See Zaritsky, supra note 6; Feldman, supra note 194, at 226.
197. Id. at 399.
199. Simkanin, 420 F.3d at 402.
200. Id. at 401.
201. Id. at 400.
202. Id.
203. Id. For information on the continuing life of We The People Foundation for Constitutional Education, see http://www.givemeliberty.org/ (last visited Feb. 3, 2007).
statement to the U.S. Treasury Secretary expatriating himself from the United
States and repatriating to the Republic of Texas.204 He also posted the
statement on his company’s website and vowed to ignore the United States’
laws.205 In 2001 Simkanin appeared in an advertisement for the organization in USA Today that stated the organization’s tax beliefs and requested
donations.206

Simkanin’s first trial ended with the district court declaring a mistrial
when the jury could not reach a unanimous verdict.207 Investigations later
revealed that Simkanin’s supporters had contacted some of the jurors.208

During Simkanin’s second jury trial, he argued that he did not willfully
violate the tax laws because he believed in good faith that he had no obligation
to pay taxes.209 Simkanin was found guilty, and the trial court upwardly
departed from the sentencing guidelines and sentenced him to eighty-four
months imprisonment.210

B. Analysis of Legal Issues

The Fifth Circuit first considered whether the district court erred by
providing an additional jury instruction in response to a jury note.211 Simkanin
testified that he did not pay taxes because his company did not fit into any of
the industries or activities listed in the Code.212 Because his company did not
operate in any of those industries, Simkanin concluded that his workers were
not employees under the Code and that he was, therefore, not required to
withhold taxes.213 During jury deliberations, the jury asked whether it needed
to decide if Simkanin’s employees were in an occupation listed in the Code.214
The district court responded that the jury need not concern itself with that
because the court made a legal determination that Simkanin’s company had
a duty to collect taxes.215 The Fifth Circuit concluded that the district court
did not direct a verdict for the government because the issue for the jury was
whether his tax law violations were willful.216 The district court did not
instruct the jury to disregard Simkanin’s beliefs; the court simply instructed

204. Simkanin, 420 F.3d at 401.
205. Id.
206. Id.
207. Id. at 402.
208. Id.
209. Id.
210. Id. at 403.
211. Id.
212. Id. at 405.
213. Id.
214. Id.
215. Id.
216. Id. at 407.
the jury that Simkanin’s beliefs were incorrect.\textsuperscript{217} Additionally, the Fifth Circuit stated that even if the district court’s response was erroneous, the error was harmless.\textsuperscript{218}

The second issue the Fifth Circuit considered was whether the district court abused its discretion when it refused to include a jury instruction on Simkanin’s good faith defense.\textsuperscript{219} The Fifth Circuit looked at two Supreme Court cases in deciding this issue.\textsuperscript{220} In \textit{Cheek v. United States}, the Supreme Court defined “willfulness” as a “voluntary, intentional violation of a known legal duty.”\textsuperscript{221} In addition, the Supreme Court found that a defendant’s good faith belief that he is acting within the laws negates the willfulness element; however, a good faith belief that the tax laws are unconstitutional or invalid does not negate the willfulness requirement.\textsuperscript{222} The Supreme Court derived its definition of willfulness from \textit{United States v. Pomponio}, when it held that an additional instruction on good faith was unnecessary because the district court instructed the jury as to the definition of willfulness.\textsuperscript{223} Because the district court in this case instructed the jury as to the definition of willfulness under \textit{Cheek} and \textit{Pomponio}, the Fifth Circuit held that the district court did not abuse its discretion when it refused to include a jury instruction on Simkanin’s good faith defense.\textsuperscript{224} The Fifth Circuit noted that the instructions given to the jury substantially covered Simkanin’s requested instruction.\textsuperscript{225}

The Fifth Circuit also considered whether the district court abused its discretion when it excluded evidence regarding Simkanin’s belief about tax laws.\textsuperscript{226} The district court excluded the evidence because it would tend to confuse the jury and was cumulative of Simkanin’s testimony.\textsuperscript{227} The Fifth Circuit held that the district court did not abuse its discretion because the tendency of the evidence to confuse the jury outweighed its probative value.\textsuperscript{228}

The Fifth Circuit also considered whether the district court erred by upwardly departing from the sentencing guidelines.\textsuperscript{229} Among several arguments, Simkanin argued that the district court was not allowed to depart based on his beliefs, but the Fifth Circuit held that Simkanin’s beliefs could be considered if they were sufficiently related to the issues at sentencing.\textsuperscript{230}

\begin{itemize}
\item \textsuperscript{217} \textit{Id.} \\
\item \textsuperscript{218} \textit{Id.} at 408. \\
\item \textsuperscript{219} \textit{Id.} at 409. \\
\item \textsuperscript{220} \textit{Id.} \\
\item \textsuperscript{221} \textit{Id.} at 410 (quoting \textit{Cheek v. United States}, 498 U.S. 192, 201 (1999)). \\
\item \textsuperscript{222} \textit{Id.} \\
\item \textsuperscript{223} \textit{Id.} (citing \textit{United States v. Pomponio}, 429 U.S. 10 (1976)). \\
\item \textsuperscript{224} \textit{Id.} at 411. \\
\item \textsuperscript{225} \textit{Id.} \\
\item \textsuperscript{226} \textit{Id.} at 412. \\
\item \textsuperscript{227} \textit{Id.} \\
\item \textsuperscript{228} \textit{Id.} \\
\item \textsuperscript{229} \textit{Id.} at 414. \\
\item \textsuperscript{230} \textit{Id.} at 417.
\end{itemize}
Simkanin’s sentence was not increased merely because of his beliefs, and his beliefs were directly related to his crimes and demonstrated a likelihood of recidivism.\textsuperscript{231} The Fifth Circuit held that the district court did not abuse its discretion when deciding to upwardly depart from the sentencing guidelines because the court based its reasons on Simkanin’s contempt for the law, radical beliefs, and his likelihood to commit further tax-related crimes.\textsuperscript{232}

The Fifth Circuit also considered Simkanin’s argument that he was entitled to resentencing under \textit{United States v. Booker} because the district court upwardly departed based on facts not admitted by Simkanin or found by the jury.\textsuperscript{233} Because Simkanin did not point to anything in the record suggesting that he would have received a lesser sentence under the post-\textit{Booker} advisory guidelines, the Fifth Circuit held that he was not entitled to resentencing.\textsuperscript{234}

\textbf{C. Commentary}

The \textit{Simkanin} decision can be added to the more than fifteen similar penalty cases since 2004 that are detailed by the IRS in its latest news release on Code Section 6673 penalties.\textsuperscript{235}

In addition, \textit{Simkanin} was one of two tax-related Fifth Circuit cases during the survey period in which the Fifth Circuit upheld an upward departure from the sentencing guidelines.\textsuperscript{236} Commentators have criticized the Fifth Circuit’s reasoning for its upward departure in these cases.\textsuperscript{237} The second upward departure case was \textit{United States v. Saldana}.\textsuperscript{238}

\textbf{VI. IMPEDING ADMINISTRATION OF TAX LAWS: SALDANA}

In \textit{United States v. Saldana}, the defendant-appellants, twin brothers Samuel and Saul Saldana, appealed their convictions in the Western District Court of Texas for corruptly endeavoring to impede the administration of Internal Revenue laws and for filing false statements.\textsuperscript{239} They also claimed that the district court sentenced them in violation of their Sixth Amendment rights in light of the Supreme Court’s \textit{United States v. Booker} decision or,
alternatively, that the sentences were unreasonable.\textsuperscript{240} The brothers were tried and sentenced separately, but they had their cases consolidated for appeal.\textsuperscript{241} The Fifth Circuit affirmed the convictions and the sentences of both brothers.\textsuperscript{242} 

\textbf{A. Background}

The government charged the Saldanas with several counts of filing false tax reports regarding several persons who had some connection with the state or local government for the purpose of triggering IRS audits in order to harass and intimidate these persons.\textsuperscript{243} The same district judge sentenced each brother after separate trials and separate jury convictions.\textsuperscript{244} The Saldanas were convicted of sending false forms 8300, \textit{"Report of Cash Payments over $10,000 Received in a Trade or Business,"} to the IRS.\textsuperscript{245} The brothers stated that they had paid or received payments to or from several individuals identified on the forms, but none of the individuals had ever received money from or given money to either brother.\textsuperscript{246} The Saldanas did not dispute that they had committed these acts; rather, each trial focused on whether the Saldanas had the necessary intent to corruptly obstruct administration of Internal Revenue laws.\textsuperscript{247} Saul Saldana claimed that he filed the forms in good faith after attending a tax course and learning about a redemption process through which persons can receive money from the government for a variety of obscure reasons.\textsuperscript{248} Saul attempted to introduce \textit{"black manuals"} that he claimed to have received in the class into evidence, but the trial court ruled that the manuals were inadmissible hearsay that would confuse the jury.\textsuperscript{249} But Saul testified that he relied on the manuals and described the redemption process.\textsuperscript{250} 

An IRS special agent and the persons named on the forms 8300 testified at each trial.\textsuperscript{251} The IRS special agent testified that the false filings cost the IRS several hundred hours of investigatory manpower.\textsuperscript{252} The persons targeted

\textsuperscript{240.} \textit{Id.}
\textsuperscript{241.} \textit{Id.}
\textsuperscript{242.} \textit{Id.}
\textsuperscript{243.} \textit{Id.}
\textsuperscript{244.} \textit{Id.}
\textsuperscript{245.} \textit{Id.}
\textsuperscript{246.} \textit{Id. at 302.}
\textsuperscript{247.} \textit{Id.}
\textsuperscript{248.} \textit{Id.}
\textsuperscript{249.} \textit{Id.}
\textsuperscript{250.} \textit{Id.}
\textsuperscript{251.} \textit{Id.}
\textsuperscript{252.} \textit{Id.}
by the forms testified that they were concerned about an audit, but none of them had been audited.\textsuperscript{253}

The district court sentenced Saul to twenty-four months of incarceration, a supervised release for three years, and a $1,300 mandatory assessment.\textsuperscript{254} The trial court sentenced Samuel to sixty months of incarceration, a supervised release for three years, and a $1,700 mandatory assessment.\textsuperscript{255}

\section*{B. Analysis of Legal Issues}

The Fifth Circuit considered whether the district court erred in its definition of "corruptly" in its jury instructions when it interpreted Code Section 7212(a), which prohibits "corruptly or by force or threats of force . . . endeavor[ing] to intimidate or impede any officer or employee of the United States acting in an official capacity . . ."\textsuperscript{256} The trial court defined "corruptly" as "to act knowingly and dishonestly with the specific intent to secure an unlawful benefit either for oneself or for another."\textsuperscript{257} The Fifth Circuit reviewed the instruction for plain error because neither brother objected at the trial to the court's jury instruction on the definition of "corruptly."\textsuperscript{258}

The Saldanas argued that "corruptly," under section 7212, means "intentionally endeavoring to gain an advantage or benefit inconsistent with a person's rights and duties under the tax laws."\textsuperscript{259} They relied on \textit{United States v. Reeves}, in which the Fifth Circuit reversed a conviction for violating section 7212 because the district court wrongly interpreted "corruptly" to mean "'with improper motive or bad or evil purpose."\textsuperscript{260} The Fifth Circuit rejected this argument because in its actual holding, it made no reference to benefits or advantages obtained under the tax laws.\textsuperscript{261} The Fifth Circuit noted that other circuits have defined "corruptly" under section 7212 without addressing whether the advantage is confined to benefits under the tax laws.\textsuperscript{262} Because its holding in \textit{Reeves} made no mention of benefits under the tax laws and the language of the statute does not require an intent to procure a benefit under the tax laws, the Fifth Circuit held that the district court did not err in its jury instructions.\textsuperscript{263} The Fifth Circuit did not address whether a defendant must seek a financial advantage or whether section 7212 is directed at any

\begin{itemize}
\item 253. \textit{Id.} at 302-03.
\item 254. \textit{Id.} at 303.
\item 255. \textit{Id.}
\item 256. \textit{Id.}
\item 257. \textit{Id.}
\item 258. \textit{Id.} at 303-04.
\item 259. \textit{Id.} at 304.
\item 260. \textit{Id.} (quoting \textit{United States v. Reeves}, 752 F.2d 995, 998 (5th Cir. 1985)).
\item 261. \textit{Id.}
\item 262. \textit{Id.} at 305.
\item 263. \textit{Id.}
\end{itemize}
activity that seeks to impede government efforts to execute tax laws because the Saldanas sought to do both.\textsuperscript{264}

The second issue considered by the Fifth Circuit was whether the trial court abused its discretion when it excluded the black manuals from evidence.\textsuperscript{265} Under Rule 403 of the Federal Rules of Evidence, a trial court can exclude evidence if "its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay, waste of time, or needless presentation of cumulative evidence."\textsuperscript{266} The Fifth Circuit stated that the manuals' probative value was slight because they were cumulative of Saul's testimony, and they appeared unprofessional and random.\textsuperscript{267} Also, the manuals had a high potential to confuse the jury because they contained inaccurate legal advice and documents unrelated to taxes or to the case.\textsuperscript{268} Therefore, the Fifth Circuit held that the trial court did not abuse its discretion in excluding the manuals from evidence.\textsuperscript{269}

The third issue the Fifth Circuit considered was whether the trial court's sentences were in violation of the defendants' Sixth Amendment rights and whether the sentences were unreasonable.\textsuperscript{270} Both brothers challenged their sentences as violating their Sixth Amendment rights under \textit{United States v. Booker} arguing that the district court raised their sentences beyond the limit the jury authorized in its verdict and that the trial court based its sentences on facts that were not proved to a jury nor admitted by defendants.\textsuperscript{271}

\textbf{1. Saul Saldana's Sentence}

Because Saul did not raise his Sixth Amendment argument before the district court, the Fifth Circuit reviewed the \textit{Booker} claim for plain error.\textsuperscript{272} The Fifth Circuit held that the district court did commit plain error by departing upward on Saul's sentence based on facts not admitted by him or found by the jury; however, Saul could not show that the error affected the outcome of the proceedings.\textsuperscript{273} The Fifth Circuit rejected Saul's \textit{Booker} argument because he could not demonstrate that the district court would have

\begin{itemize}
\item \textsuperscript{264} \textit{Id.} at 305-06.
\item \textsuperscript{265} \textit{Id.} at 306.
\item \textsuperscript{266} \textit{Id.} at 307.
\item \textsuperscript{267} \textit{Id.}
\item \textsuperscript{268} \textit{Id.}
\item \textsuperscript{269} \textit{Id.}
\item \textsuperscript{270} \textit{Id.}
\item \textsuperscript{271} \textit{Id.}
\item \textsuperscript{272} \textit{Id.} at 308.
\item \textsuperscript{273} \textit{Id.}
\end{itemize}
sentenced him differently had it sentenced him under an advisory system rather than a mandatory sentencing system.\textsuperscript{274}

Saul also challenged the court's upward departure arguing that the court relied on impermissible factors and that the magnitude of the departure was unreasonable.\textsuperscript{275} The Fifth Circuit noted that district courts are not bound by the guidelines, but they must still consider them and provide reasons for imposing a sentence outside the sentencing range.\textsuperscript{276} The reasons must be included in its written order of judgment under 18 U.S.C. § 3553(c).\textsuperscript{277} Also, a court does not abuse its discretion in upwardly departing when its reasons advance the objectives set forth in section 3553(a)(2), are authorized by section 3553(b), and are justified by the facts.\textsuperscript{278}

The district court orally explained that it upwardly departed because of the harm Saul caused, his disrespect for the law, the fear he created, and the number of times he committed the crime.\textsuperscript{279} But in its written statement, the court only stated that the sentencing guidelines had not sufficiently addressed the injury caused when the wrongdoing occurred on multiple counts and that Saul's conduct caused "legal stoppage."\textsuperscript{280}

Saul contended that the guidelines provide a method to calculate an offense level for defendants convicted of multiple similar offenses; therefore, the district court could not upwardly depart due to the number of counts of conviction.\textsuperscript{281} The Fifth Circuit stated that the guidelines provide for the sentencing of defendants convicted of multiple counts, but the guidelines permit deviation in unusual circumstances.\textsuperscript{282} The Fifth Circuit also stated that no conflict between the policy reasons behind the guidelines and an upward departure based on multiple counts exists.\textsuperscript{283} Saul was convicted of thirteen separate counts, and the guidelines did not allow for any enhanced punishment based on the degree of harm or the number of counts included.\textsuperscript{284} Therefore, the district court did not abuse its discretion by upwardly departing based on multiple counts.\textsuperscript{285}

Saul's next contention was that the guidelines account for the risk that filing false tax forms can potentially cause aggravation and harm.\textsuperscript{286} The Fifth Circuit stated that the section addressing the base offense levels for section

\textsuperscript{274} Id.
\textsuperscript{275} Id.
\textsuperscript{276} Id. at 310.
\textsuperscript{277} Id.
\textsuperscript{278} Id.
\textsuperscript{279} Id.
\textsuperscript{280} Id.
\textsuperscript{281} Id. (citing U.S. SENTENCING GUIDELINES MANUAL § 3D, introductory cmt. (2005)).
\textsuperscript{282} Id.
\textsuperscript{283} Id. at 311.
\textsuperscript{284} Id.
\textsuperscript{285} Id.
\textsuperscript{286} Id.
7212 was primarily focused on tax evasion and failed to account for harm caused by tax protestors impeding the IRS and using the IRS to harass others. The district court could consider the fact that the degree of harm the victims suffered in this case was greater than the harm normally associated with false tax form cases.

The Fifth Circuit concluded that the decision to upwardly depart was reasonable because the district court’s reasons reflected the severity of the offense, encouraged respect for the law, and provided just punishment. In determining whether the degree of departure was unreasonable, the Fifth Circuit deferred to the district court because the court relied on permissible factors in making its decision. The Fifth Circuit noted that the departure approached the outer boundary of reasonableness because the district court quadrupled the maximum sentence allowed under the guidelines. The extent of departure overstated the harm caused by Saul’s acts. Saul’s acts caused no significant disruptions for the victims and led to no audits. Also, there was no evidence that the IRS spent more hours investigating these false forms than they would have normally spent investigating false forms. Although the Fifth Circuit agreed that the number of counts was an appropriate basis for a greater sentence, the court was not convinced that it justified quadrupling the maximum sentence. Nevertheless, the Fifth Circuit concurred with the district court’s departure because each of the reasons for departing was permissible. Therefore, the Fifth Circuit held that Saul’s sentence was not an abuse of discretion by the district court.

2. Samuel Saldana’s Sentence

Because Samuel did raise his Sixth Amendment argument before the district court, the Fifth Circuit reviewed his Booker claim for harmless error. During the sentencing hearing, the judge stated that if the Booker decision found the guidelines unconstitutional, the court would sentence Samuel to the same punishment in accordance with the substantive statutes.

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287. Id.
288. Id. at 312.
289. Id.
290. Id.
291. Id.
292. Id. at 313.
293. Id.
294. Id.
295. Id.
296. Id. at 312-13.
297. Id. at 313.
298. Id. at 308.
299. Id. at 314.
Therefore, the Fifth Circuit held that although the district court plainly erred, the error was harmless.\textsuperscript{300}

The Fifth Circuit noted that the district court sentenced Samuel and Saul in the same manner.\textsuperscript{301} The district court’s justifications for the upward departure were not unreasonable.\textsuperscript{302} In addition, Samuel only challenged the extent of the departure, not the validity.\textsuperscript{303}

Again, the Fifth Circuit noted that the extent of the departure reached the outer limits of reasonableness.\textsuperscript{304} But, as in Saul’s case, the district court’s reasons for upwardly departing were valid and justified the sentence imposed.\textsuperscript{305} Therefore, the district court did not abuse its discretion in imposing Samuel’s sentence.\textsuperscript{306}

\textbf{C. Commentary}

The \textit{Saldana} decision follows the Eighth and Sixth Circuits in upholding convictions under section 7212 when the defendants had not sought any advantage under the tax laws.\textsuperscript{307} The rule is clear: One does not need to be seeking a tax benefit in order to criminally run afoul of the tax laws.\textsuperscript{308}

\textbf{VII. TAX COURT LITIGATION AND OFFSETS: ESTATE OF SMITH}

In \textit{Estate of Smith v. Commissioner}, the Commissioner of the IRS appealed the Tax Court’s order granting the Tax Court Rule 260 motion by the estate of Algerine Allen Smith.\textsuperscript{309} The Tax Court determined that the Commissioner was precluded from offsetting the unpaid interest against the overpayment due to the estate because the parties’ calculation of Tax Court Rule 155 and stipulation of overpayment of estate tax included the IRS’s claim for additional unpaid interest.\textsuperscript{310} The Fifth Circuit held that the Tax

\begin{itemize}
  \item \textsuperscript{300} \textit{Id}.  \\
  \item \textsuperscript{301} \textit{Id}. at 315.  \\
  \item \textsuperscript{302} \textit{Id}.  \\
  \item \textsuperscript{303} \textit{Id}.  \\
  \item \textsuperscript{304} \textit{Id}. at 316.  \\
  \item \textsuperscript{305} \textit{Id}.  \\
  \item \textsuperscript{306} \textit{Id}.  \\
  \item \textsuperscript{307} \textit{Id}. at 304.  \\
  \item \textsuperscript{308} \textit{See id}.  \\
  \item \textsuperscript{309} \textit{Estate of Smith v. Comm’t}, 429 F.3d 533, 534 (5th Cir. Oct. 2005). A Tax Court Rule 260 motion is a taxpayer’s proceeding to enforce an overpayment determined by the Tax Court. 20A FEDERAL PROCEDURE § 48:1019 (2006).  \\
  \item \textsuperscript{310} \textit{Estate of Smith}, 429 F.3d at 534. After the Tax Court has determined the issues in a case, it may withhold entry of its decision until the parties submit Tax Court Rule 155 computations showing the correct amount of the deficiency, liability, or overpayment to be entered as a result of the court’s determination of the substantive issues. 20A FEDERAL PROCEDURE § 48:1244 (2006).
\end{itemize}
Court was without jurisdiction to review the offset, and therefore, the Fifth Circuit vacated the Tax Court’s judgment.\textsuperscript{311}

\textbf{A. Background}

In July 1991 the estate filed its original tax return and included a $60,164 payment to satisfy the tax due.\textsuperscript{312} The Commissioner issued a notice of deficiency of $663,785 in 1994 and imposed an accuracy related penalty of $132,785.\textsuperscript{313} The estate then filed a petition in Tax Court requesting redetermination of the deficiency.\textsuperscript{314} In February 1998 the Tax Court held that there was a $564,429 deficiency in estate taxes but no accuracy related penalty.\textsuperscript{315}

In March 1998 the estate remitted a payment of $646,325 to cover the estimated tax and interest due.\textsuperscript{316} In May 1998 the Commissioner assessed the estate tax deficiency of $564,429 and $410,848 in underpayment of interest.\textsuperscript{317} In order to satisfy the estate tax deficiency, the Commissioner applied the estate’s March 1998 payment of $501,377 and the estate’s overpayment credit of $63,052 from its 1992 return.\textsuperscript{318} The Commissioner applied the $144,947 balance ($646,325 less $501,377) from the March 1998 payment to the assessed interest.\textsuperscript{319}

In December 1999 the Fifth Circuit reversed the Tax Court’s decision and remanded the case.\textsuperscript{320} In January 2002 after the Tax Court issued its opinion on remand, the parties entered a stipulated computation under Tax Court Rule 155.\textsuperscript{321} The parties agreed to a $385,747 estate tax liability and a $238,847 overpayment.\textsuperscript{322} The Tax Court entered a judgment that the estate

\textsuperscript{311} Estate of Smith, 429 F.3d at 534. The Tax Court’s jurisdiction does not extend to all tax issues despite the court’s name. Federal Tax Coordinator § U-2130 (2d ed. 2006); 20A Federal Procedure § 48:1018 (2006); 630-3rd Tax Management Portfolios § 1 (BNA 2006), available at TMFEDPORT No. 630 § 1 (Westlaw). For example, though clearly related to tax, the Tax Court has no jurisdiction if there has been no notice of deficiency, such as when there has been an overpayment or a rejection of a refund claim. Federal Tax Coordinator § U-2130 (2d ed. 2006); 20A Federal Procedure § 48:1018 (2006); 630-3rd Tax Management Portfolios § 1 (BNA 2006), available at TMFEDPORT No. 630 § 1 (Westlaw).

\textsuperscript{312} Estate of Smith, 429 F.3d at 534.

\textsuperscript{313} Id.

\textsuperscript{314} Id.

\textsuperscript{315} Id.

\textsuperscript{316} Id.

\textsuperscript{317} Id.

\textsuperscript{318} Id.

\textsuperscript{319} Id.

\textsuperscript{320} Id.

\textsuperscript{321} Id.

\textsuperscript{322} Id. at 535.
had a $238,847 overpayment in estate tax. The estate appealed, and the Fifth Circuit affirmed.

The Commissioner adjusted the estate’s accounts in May 2002 to reflect the Tax Court’s judgment. The Commissioner abated $238,847 to the estate’s account to properly reflect the agreed overpayment of tax and abated $180,564 in underpayment interest on the estate’s account. As a result, the estate’s account contained a balance of $85,336 of assessed, unpaid interest. Then, the Commissioner refunded $153,510 ($238,847 less $85,336) to the estate after crediting $85,336 against the assessed, unpaid underpayment of interest owed. Later in May 1992, the Commissioner discovered an error in the interest calculation due to a timing error in the application of the 1992 income tax overpayment to the estate tax liability. The Commissioner abated and refunded $20,341 of the underpayment of interest to correct the error.

In the end, the estate received $173,851 of its $238,847 overpayment, and the Commissioner applied the difference of $64,996 to the balance of assessed, unpaid underpayment of interest.

The estate filed a Motion for Proceeding to Enforce Overpayment Decision pursuant to Code Section 6512(b)(1) and Tax Court Rule 260 seeking $85,336 plus interest from the Commissioner. The Tax Court granted the estate’s motion and ordered the Commissioner to refund the overpayment in full, plus interest, less any previously refunded amounts. The Commissioner moved for leave to file a motion to vacate the Tax Court’s January 2002 decision, but the Tax Court denied the motion.

B. Analysis of Legal Issues

The issue considered by the Fifth Circuit was whether the Tax Court had jurisdiction to review the Commissioner’s decision to offset unpaid interest against the previously established overpayment of tax. "The Tax Court is
an Article I court of limited jurisdiction,” and therefore, “may exercise jurisdiction only to the extent . . . conferred upon it by Congress.”

The Fifth Circuit reviewed the Tax Court’s jurisdiction throughout the case. The Tax Court had jurisdiction to ascertain the amount of overpayment when it determined that there was a deficiency but that there had also been an overpayment. Once that judgment was final, the Commissioner had an obligation to credit or refund the amount to the estate.

The Commissioner argued that it complied by crediting a part of the overpayment to the assessed, unpaid interest and refunding the balance pursuant to Code Section 6402(a). Therefore, the Commissioner argued, the Tax Court would have no jurisdiction to review the offset under section 6512(b)(4).

The Tax Court held that overpayment judgments account for both interest and tax, and therefore, the Commissioner may not offset interest already considered and incorporated into the judgment because this has the effect of decreasing the refund due under the judgment.

The Fifth Circuit concluded that the Tax Court erred in holding that an overpayment of tax always includes any underpayment of interest due. Statutes specifically provide that the Tax Court may make a final determination of tax overpayments without incorporating interest due because there are procedures to account for any overpayment or underpayment of interest related to the original tax deficiency under Code Section 7481. Section 7481 allows the Tax Court to determine any interest overpayment or underpayment after it has determined that there is an overpayment of tax under section 6512(b).

The Tax Court can calculate the amount of overpayment interest through its jurisdiction to determine an overpayment of tax when interest has been assessed and paid. In this case, however, the overpayment decision did not decide the question of underpayment interest. The overpayment computation included in the stipulation and judgment involved only tax assessments, abatements, and payments, not interest.

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337. Id. "The Tax Court . . . shall have such jurisdiction that is conferred on . . . [it] by this title . . . ." I.R.C. § 7442 (2005).
338. Estate of Smith, 429 F.3d at 537.
339. Id.
340. Id.
341. Id.
342. Id.
343. Id.
344. Id. at 538.
345. Id.
346. Id.
347. Id. at 538-39.
348. Id.
349. Id.
that because the Tax Court did not decide the estate's liability for underpayment of interest in determining the estate's overpayment, the Tax Court exceeded its jurisdiction under section 6512(b)(2) when ordering the Commissioner to refund the full amount of the overpayment.\textsuperscript{350} Additionally, the Commissioner acted properly under section 6402 when he offset the unpaid interest against the overpayment of tax.\textsuperscript{351} The Tax Court's actions constituted a review of the offset, which the Tax Court specifically lacked jurisdiction to do under section 6512(b)(4).\textsuperscript{352}

C. Commentary

As a result of Estate of Smith, the IRS will not be prevented from collecting or offsetting underpayment interest in overpayment cases even though the cases are silent on the question of the interest.\textsuperscript{353} Accordingly, at least within the confines of the Fifth Circuit, the IRS seems likely to return to its prior practice of drafting overpayment decisions without calculating the applicable underpayment interest.\textsuperscript{354}

VIII. REFUND CLAIM: EC TERM OF YEARS TRUST

In EC Term of Years Trust v. United States, the trust appealed the United States Western District of Texas Court's dismissal of its refund claim under Code Section 1346.\textsuperscript{355} The district court dismissed the trust's refund claim for lack of subject matter jurisdiction because the trust's sole and exclusive remedy lay in a wrongful levy action under Code Section 7426.\textsuperscript{356} The Fifth Circuit affirmed.\textsuperscript{357}

\textsuperscript{350} Id.
\textsuperscript{351} Id.
\textsuperscript{352} Id.
\textsuperscript{353} Philip N. Jones, Two New Opinions on Jurisdiction Over Interest on Taxes, 104 J. Tax'n 63, 63 (2006).
\textsuperscript{354} Id.
\textsuperscript{355} EC Term of Years Trust v. United States, 434 F.3d 807, 808 (5th Cir. Jan. 2006). The Tax Court is the tribunal for prepayment litigation with the IRS, while the district courts and the Court of Federal Claims are the tribunals for post-payment litigation. See 631-3rd TAX MANAGEMENT PORTFOLIOS § III.A.1 (BNA 2006), available at TMFEDPORT No. 631 § III (Westlaw); 630-3rd TAX MANAGEMENT PORTFOLIOS § II.A (BNA 2006), available at TMFEDPORT No. 630 § II (Westlaw). In other words, the district courts have jurisdiction when a payment has been made and a refund demanded. See 631-3rd TAX MANAGEMENT PORTFOLIOS § III.A.1 (BNA 2006), available at TMFEDPORT No. 631 § III (Westlaw); 630-3rd TAX MANAGEMENT PORTFOLIOS § II.A (BNA 2006), available at TMFEDPORT No. 630 § II (Westlaw).
\textsuperscript{356} EC Terms of Years Trust, 434 F.3d at 808. A person other than the taxpayer who has an interest in property levied by the IRS can file a wrongful levy suit under section 7426(a)(1). CASEY, supra note 18, § 13C:31.
\textsuperscript{357} EC Term of Years Trust, 434 F.3d at 810.
A. Background

After assessing federal income taxes, penalties, and interest against the creators of the trust, Elmer and Dorothy Cullers, the IRS filed transferee tax liens against the trust for the Cullers' tax liability. The IRS seized an account created by the trust to satisfy the amount owed. The trust sought to recover the funds under sections 7426(a)(1) and 1346(a)(1), but the statute of limitations had run on the wrongful levy action. The district court dismissed the claim due to lack of subject matter jurisdiction.

The trust brought suit a second time, seeking a refund under section 1346(a)(1). The district court addressed whether a section 7426 wrongful levy claim remained the sole and exclusive remedy for third parties, such as the trust, after the Supreme Court's decision in United States v. Williams. Williams allows third parties to remove a lien on their property by paying the tax liability of another individual and then bringing a refund action under section 1346(a)(1). The district court distinguished Williams, held that a wrongful levy action was the exclusive remedy for the trust, and dismissed the trust's claim for lack of subject matter jurisdiction again. The trust appealed.

B. Analysis of Legal Issues

The Fifth Circuit reviewed the dismissal de novo. The issue considered was whether a wrongful levy action under section 7426 is the exclusive remedy for innocent third parties when the IRS confiscates their property to satisfy another person’s tax liability.

Historically, the Fifth Circuit has held that section 7426 is the sole and exclusive remedy if it is available to an individual. The court noted also that section 7426 supports the government's strong interest in quickly resolving doubts concerning the status of the taxpayer's account. The short
statute of limitations under section 7426 allows for the prompt resolution of tax liability.\textsuperscript{371}

The trust argued that Williams allows litigants to bring a refund action under section 1346 even if section 7426 was available to them.\textsuperscript{372} The Fifth Circuit distinguished Williams by stating that in that case the Supreme Court did not directly address whether a third party could sue under section 1346.\textsuperscript{373} The Court simply determined that Williams had standing to sue under section 1346 because the statute’s language did not state that only the person assessed may sue.\textsuperscript{374} The Fifth Circuit stated that Williams does not suggest that a section 1346 refund action is available in addition to a section 7426 wrongful levy action.\textsuperscript{375} In Williams, Williams could not have brought an action under section 7426 and would have lacked a remedy without a claim under section 1346.\textsuperscript{376} The Fifth Circuit then held that Williams applies when a remedy under section 7426 is unavailable, which was not the case in EC Term of Years Trust.\textsuperscript{377} Additionally, the Court noted that several other circuits have held that section 7426 is the exclusive remedy for third party wrongful levy claims.\textsuperscript{378}

The Fifth Circuit held that Williams did not alter the rule of exclusivity of the remedy available under section 7426.\textsuperscript{379} When section 7426 is available, it is the sole and exclusive remedy.\textsuperscript{380}

\textbf{C. Commentary}

In finding section 7426 to be the exclusive remedy, the EC Term of Years Trust decision follows the Tenth Circuit decision Dahn v. United States; the Eighth Circuit decision Miller v. Tony and Susan Alamo Foundation; and the Fourth Circuit per curiam, unpublished decision Audio Investments v. Robertson.\textsuperscript{381} The IRS has publicized its agreement with this approach in Revenue Ruling 2005-49.\textsuperscript{382} But future litigation on the availability of section 1346 in this situation seems very likely.\textsuperscript{383}

\footnotesize{\begin{tabular}{l}
\textsuperscript{371} Id.
\textsuperscript{372} Id.
\textsuperscript{373} Id.
\textsuperscript{374} Id.
\textsuperscript{375} Id.
\textsuperscript{376} Id. (citing United States v. Williams, 514 U.S. 527 (1995)).
\textsuperscript{377} Id. at 810.
\textsuperscript{378} Id.
\textsuperscript{379} Id.
\textsuperscript{380} Id.
\textsuperscript{381} Id. (citing Audio Invs. v. Robertson, 67 F. App’x 795, 797 (4th Cir. 2003) (unpublished per curiam decision); Miller v. Tony & Susan Alamo Found., 134 F.3d 910, 916 (8th Cir. 1998); Dahn v. United States, 127 F.3d 1249, 1253 (10th Cir. 1997)).
\textsuperscript{383} 631-3rd TAX MANAGEMENT PORTFOLIOS § VI (BNA 2006), available at TMFEDPORT No. 631 § VI (Westlaw).}

IX. FAMILY ATTRIBUTION: Garber Industries, Inc.

In Garber Industries, Inc. v. Commissioner, the taxpayer-petitioner, Garber Industries Holding Co., Inc. (Garber Industries), appealed an order of the Tax Court limiting a 1998 deduction of net operating loss carryforwards and assessing an income tax deficiency. The issue the Fifth Circuit considered was whether or not a 1998 stock sale from one brother and his wife to another brother resulted in an ownership change under Code Section 382 in light of certain family attribution rules that arguably precluded an ownership change. The Fifth Circuit agreed with the Tax Court that there was such an ownership change and thus, affirmed the Tax Court’s judgment.

A. Background

Garber Industries was incorporated in December 1982. Its two primary shareholders were brothers Charles M. Garber and Kenneth R. Garber. Charles owned about 68%, while his brother owned about 26%. Various other family members—the wives and children of the two brothers—were minority shareholders.

In July 1996 Garber Industries effected a “corporate D reorganization,” under Code Section 368(a)(1)(D). The D reorganization did not change the wives’ and children’s ownership interests in Garber Industries. But Charles’s ownership went from 68% of the corporation to 19%, while Kenneth’s went from 26% to 65%. In April 1998 almost two years after the D reorganization, Kenneth and his wife sold all of their remaining shares to

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384. Garber Indus., Inc. v. Comm’r, 435 F.3d 555, 556 (5th Cir. Jan. 2006). Under Code Section 172, a taxpayer can carry forward a net operating loss twenty years after the year in which the loss occurred and carry back two years from the year in which the loss was incurred. I.R.C. § 172 (2006). This provision reflects the economic realities that most businesses have fluctuating income from year to year, which is not reflected in the annual accounting period rule. See, e.g., United States v. Foster Lumber Co., 429 U.S. 32, 42 (1976). The annual accounting period rule would be especially harsh if businesses were unable to offset income from good years with losses from bad ones. See id.

385. Garber Indus., Inc., 435 F.3d at 556.
386. Id. at 559.
387. Id. at 556.
388. Id.
389. Id.
390. Id.
391. Id.
392. Id.
393. Id.
Charles.\textsuperscript{394} This increased his ownership in the corporation from 19\% to 84\%.\textsuperscript{395} No other Garber Industries stock changed ownership in that year.\textsuperscript{396}

By the end of 1997, the year before Kenneth and his wife sold their shares to Charles, Garber Industries had over $20,000,000 in net operating losses.\textsuperscript{397} The corporation suffered these losses from 1983 to 1989 and also in 1992.\textsuperscript{398} But under Code section 172, net operating losses can be carried forward and deducted in future years.\textsuperscript{399} When the corporation filed its tax return for 1998, the year the shares were sold to Charles, the corporation deducted net operating loss carryovers of $808,935.\textsuperscript{400}

The IRS audited Garber Industries and concluded that the 1998 net operating loss deduction should be substantially reduced because of the ownership change that occurred during that year.\textsuperscript{401} In June 2001 the Commissioner issued a notice of deficiency for the increased tax liability that resulted from reducing the net operating loss carryover deduction that the corporation had claimed in 1998.\textsuperscript{402}

Garber Industries contested the deficiency in the Tax Court.\textsuperscript{403} The Tax Court held in favor of the Commissioner.\textsuperscript{404} The Tax Court concluded that the corporation was not entitled to the full $808,935 net operating loss carryover deduction because the sale between the brothers constituted an ownership change under section 382.\textsuperscript{405} Garber Industries appealed the Tax Court’s determination to the Fifth Circuit.\textsuperscript{406}

\textbf{B. Analysis of Legal Issues}

The section 382 ownership change issue was the sole issue in determining whether or not Garber Industries was entitled to the $808,935 deduction.\textsuperscript{407} In order to prevent trafficking in net operating losses, section 382 limits how much of a net operating loss carryover can be deducted when there has been an ownership change.\textsuperscript{408} An ownership change arises if,

\textsuperscript{394} \textit{Id.}
\textsuperscript{395} \textit{Id.}
\textsuperscript{396} \textit{Id.}
\textsuperscript{397} \textit{Id.}
\textsuperscript{398} \textit{Id.}
\textsuperscript{399} \textit{Id.}
\textsuperscript{400} \textit{Id.}
\textsuperscript{401} \textit{Id.}
\textsuperscript{402} \textit{Id.}
\textsuperscript{403} \textit{Id.}
\textsuperscript{404} \textit{Id.}
\textsuperscript{405} \textit{Id.}
\textsuperscript{406} \textit{Id.} Prior to the Fifth Circuit’s rulings, some commentators had described the Tax Court’s analysis as “Solomonic” and expected that the Fifth Circuit would affirm. Burgess J.W. Raby & William L. Raby, \textit{Stock Ownership Tax Attribution and Siblings}, 106 Tax Notes 675, 678 (2005).
\textsuperscript{407} Garber Indus. Inc., 435 F.3d at 556.
\textsuperscript{408} \textit{Id.} at 557.
immediately after a stock shift, the percentage of stock owned by one or more shareholders owning 5% or more of the corporation—5% shareholder—has increased by more than fifty percentage points over the lowest percentage owned by such persons during the three year period ending on the date of the owner shift.\textsuperscript{409}

Kenneth and Charles Garber were both 5% shareholders.\textsuperscript{410} Without an exception to the above rules, the 1998 sale from Kenneth to Charles caused an owner shift because the sale increased Charles Garber’s ownership by more than fifty percentage points, from 19% to 84%.\textsuperscript{411} If the brothers’ stock could be aggregated or attributed to each other, however, then a sale between them would not cause an ownership change.\textsuperscript{412} In some circumstances, section 382 allows stock held by family members to be combined for purposes of determining if an ownership change occurred.\textsuperscript{413} Whether an ownership change occurred depends on whether ownership of the brothers’ Garber Industries stock can be aggregated or attributed to one another under the ownership rules set forth in sections 382 and 318.\textsuperscript{414}

Unfortunately for Garber Industries, the constructive ownership rules of section 318(a)(1) that allow the aggregation of family members refer to spouses, children, grandchildren, and parents but not siblings.\textsuperscript{415} Section 318(a)(5)(B) has a second rule that prevents double family attribution; that is, application of the family attribution rules may not be applied twice (e.g., a son’s stock attributed to his parents and a parent’s stock then attributed to a child other than the son, which would effectively attribute stock ownership between siblings).\textsuperscript{416} The technical issue was whether or not there was some means by which the double family attribution prohibition could be avoided.\textsuperscript{417}

Garber Industries pointed to section 382(l)(3)(A)(I), which provides that the double family attribution prohibition does not apply in the context of section 382.\textsuperscript{418} Thus, Garber Industries argued that double family attribution should occur, which would mean that Kenneth’s stock should be attributed to the brothers’ parents and then from the parents to Charles.\textsuperscript{419} This would mean that the 1998 sale did not cause an ownership change.\textsuperscript{420}

The Fifth Circuit, however, believed that the plain language of these statutes supported the Tax Court’s decision that the stock owned by Kenneth

\textsuperscript{409} Id.
\textsuperscript{410} Id.
\textsuperscript{411} Id.
\textsuperscript{412} Id. at 556.
\textsuperscript{413} Id. at 557.
\textsuperscript{414} Id. at 556.
\textsuperscript{415} Id. at 558.
\textsuperscript{416} Id.
\textsuperscript{417} See id. at 559.
\textsuperscript{418} Id. at 559.
\textsuperscript{419} Id.
\textsuperscript{420} Id.
could not be attributed to Charles. Section 318(a)(1) does not list siblings as family members whose stock is to be aggregated, and the court rejected Garber Industries' argument that section 382(l)(3)(A)(I) means that the double family attribution prohibition does not apply.

The court read section 382(l)(3)(A)(I) as having two parts. The first part removes the general attribution scheme of section 318(a)(1) and the double family attribution prohibition of section 318(a)(5)(B). But the second part replaces those rules with a different method of determining ownership among family members: An individual and his family members as described in section 318(a)(1) will be treated as a single individual for purposes of applying section 382. The court rejected Garber Industries' argument because it only mentioned removal of the double family attribution rule and not the removal of the general attribution scheme or its replacement with the different attribution scheme, the family grouping model. Under this interpretation, when determining whether family members' stock can be aggregated under section 382, the sole question is whether the parties are members of the same family as described by section 318—an individual and his or her spouse, children, and grandchildren. Nothing in the language of section 382 suggests that the stock ownership of anyone outside the limited list of family members in section 318 can be regarded as owned by those members within the family group.

The court also rejected the argument by Garber Industries that section 382 should be read to allow ownership attribution to and from a parent without regard to whether the parent is also a shareholder of the loss corporation. Garber Industries argued that this provision allowed a family group to aggregate the stock of the brothers around their parents. But the court specifically agreed with the Tax Court that the individuals forming the basis of the ownership analysis must be shareholders of the loss corporation because the purpose is to identify ownership changes relative to 5% shareholders. Such a change of ownership by a shareholder is the only change the statute addresses. Stock owners who are less than 5% shareholders of the corporation are grouped, and their stock is treated as

421. Id. at 558-59.
422. Id. at 559.
423. Id. at 558.
424. Id.
425. Id. at 558-59.
426. Id. at 559.
427. Id.
428. Id.
429. Id.
430. Id.
431. Id.
432. Id.
owned by a single 5% shareholder. Accordingly, the "individual" referred to in the constructive ownership analysis provisions of section 382(l)(3)(A) must be a shareholder. Thus, that individual is the starting point for the formation of a family group, which consists of that individual's spouse, parents, children, and grandchildren but not, as Garber Industries argued, the individual's siblings.

C. Commentary

The Garber Industries case has yet to generate significant commentary or use by other courts. Standard use references have been updated to include the conclusion that a stock sale between siblings does not avoid an ownership change because of family attribution rules. One commentator, however, has noted that if the normal attribution rules of section 318(a)(1) were completely replaced with the family group model, no need for that statute to even refer to the prohibition on double family attribution under section 318(a)(5)(B) would exist.

X. PAYMENT VERSUS DEPOSIT: DEATON

In Deaton v. Commissioner, the taxpayer-petitioners Barbara and Ronny Deaton appealed a judgment of the Tax Court holding that their 1993 remittance was a payment of estimated taxes rather than a deposit. In 1994 the Deatons filed Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, in order to request an extension for filing their 1993 federal income tax return. With the request they remitted $125,000; however, they did not file their 1993 return until 2000. The Deatons petitioned for review of the determination to collect by levy unpaid income taxes assessed for tax years 1994 to 1996. The determination upheld the IRS's denial of their request made in 2000 to apply overpayment

433. Id.
434. Id.
435. Id.
436. See id.
440. Id.
441. Id. at 225.
442. Id. at 226.
of their 1993 taxes to their 1994 to 1996 tax liabilities. The United States Tax Court entered judgment for the IRS, and the Deatons appealed. The Fifth Circuit held that the remittance was payment of estimated taxes, rather than deposit, and affirmed the Tax Court.

A. Background

The Deatons requested time to file their 1993 income tax return by filing Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return. When filing the application, they estimated their tax liability for the 1993 tax year and submitted a check for $125,000 with the application. But the Deatons missed the deadline and did not file their return until almost six years after the due date. They also failed to file their returns timely in 1994, 1995, and 1996. In 2000 when the Deatons did finally file their tax returns for 1994, 1995, and 1996, they requested that the IRS carry forward an overpayment of taxes made in 1993 to the taxes due in 1994, 1995, and 1996.

But the IRS refused to carry forward any amount from 1993 to be applied to the tax liabilities in the later years. The IRS argued that the credit request was barred by Code Section 6511(b)(2)(A). The IRS claimed that this section limited credit claims to amounts paid within three years plus the period of any extension of time for filing the return immediately preceding the filing of the claim for a credit. As there were no payments in the three year period preceding the 2000 return, there was no carryforward credit.

B. Analysis of Legal Issues

The issue for the Fifth Circuit was whether the taxpayers' remittance in 1994 when they filed their Form 4868 was a payment of tax or a deposit. The Supreme Court laid down the general rule in Baral v. United States: As a matter of law, a remittance submitted with a Form 4868 Application for

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443. Id.
444. Id.
445. Id.
446. Id. at 224.
447. Id. at 225.
448. Id.
449. Id. at 226.
450. Id. at 225.
451. Id.
452. Id.
453. Id.
454. Id.
455. Id. at 226.
Automatic Extension should be considered a payment.\textsuperscript{456} The IRS argued that \textit{Baral} controlled the disposition of the Deatons' case.\textsuperscript{457} But the Deatons argued that \textit{Baral} should not apply.\textsuperscript{458} They argued that \textit{Baral} is limited to cases involving "deem paid" remittances under Code section 6315(b) and that their remittance did not fall under that section.\textsuperscript{459} The Deatons argued that because section 6315(b) did not apply to them, neither did \textit{Baral}, which meant that the facts and circumstances test under \textit{Rosenman v. United States} applied.\textsuperscript{460} They argued that under the facts and circumstances test, their remittance should be considered a deposit rather than a payment.\textsuperscript{461}

Even though the \textit{Rosenman} decision had been used by the Fifth Circuit (and other courts) to conclude that remittances made prior to formal assessments of tax were deposits rather than payments, the Fifth Circuit concluded that after \textit{Baral}, it was no longer bound to follow its prior usage of \textit{Rosenman}.\textsuperscript{462} The Fifth Circuit did, however, consider \textit{Rosenman} in the Deatons' case.\textsuperscript{463} In \textit{Rosenman}, in order to secure a two-month estate tax return filing extension, the taxpayer had remitted taxes but had also submitted a letter that said ""[T]his payment is made under protest and duress, and solely for the purpose of avoiding penalties and interest, since it is contended . . . that not all of this sum is legally or lawfully due.""\textsuperscript{464} As a result, the IRS held the funds in a suspense account until the assessment against the estate was finally made.\textsuperscript{465} Unlike the taxpayers in the \textit{Rosenman} case, however, the Deatons had not sent a letter or provided any other notice to the IRS that they were disputing their tax liability for 1993.\textsuperscript{466} Nothing on the document or check that the Deatons submitted showed that they intended their remittance to be a deposit rather than a payment.\textsuperscript{467} Thus, the Fifth Circuit did not need to conclude that, as a matter of law, post-\textit{Baral}, all remittances accompanying a Form 4868 Application for Automatic Extension must be payments.\textsuperscript{468} The Deatons' case did not fit the facts of \textit{Rosenman}, so the Fifth Circuit held that the remittance constituted a payment rather than deposit.\textsuperscript{469} Thus, the Fifth Circuit concluded that the Deatons' remittance was a payment, but the court did not conclude

\begin{thebibliography}{99}
\bibitem{456} Id. at 227 (citing Baral v. United States, 528 U.S. 431, 436 (2000)).
\bibitem{457} Id.
\bibitem{458} Id.
\bibitem{459} Id.
\bibitem{460} Id. (citing Rosenman v. United States, 323 U.S. 658, 662 (1945)).
\bibitem{461} Id.
\bibitem{462} Id. at 229-30.
\bibitem{463} Id. at 228.
\bibitem{464} Id. (quoting \textit{Rosenman}, 323 U.S. at 660).
\bibitem{465} Id.
\bibitem{466} Id. at 232.
\bibitem{467} Id.
\bibitem{468} Id.
\bibitem{469} Id.
\end{thebibliography}
that remittances submitted with Form 4868 Application for Automatic Extension are payments as a matter of law.\textsuperscript{470}

\textbf{C. Commentary}

While the Fifth Circuit declined to hold that the payments accompanying a Form 4868 are payments as a matter of law, the Second Circuit in \textit{Ertman v. United States}, the Sixth Circuit in \textit{Gabelman v. Commissioner}, the Ninth Circuit in \textit{Ott v. United States}, and the Tenth Circuit in \textit{Weigand v. United States} have reached that conclusion.\textsuperscript{471}

\textsuperscript{470} \textit{Id.}

\textsuperscript{471} 14 \textsc{MERTENS LAW OF FEDERAL INCOME TAXATION} § 50:20 (2006); see \textit{Ertman v. United States}, 165 F.3d 204, 206 (2d Cir. 1999); \textit{Ott v. United States}, 141 F.3d 1306, 1309 (9th Cir. 1998); \textit{Gableman v. Comm’r}, 86 F.3d 609, 612 (6th Cir. 1996); \textit{Weigand v. United States}, 760 F.2d 1072, 1073 (10th Cir. 1985).