

No. _____

In The
Supreme Court of the United States

NORMA L. SLONE, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

**On Petition For A Writ Of Certiorari
To The United States Court Of Appeals
For The Ninth Circuit**

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether a court of appeals may reverse a fact-dependent ruling of the tax court without articulating any standard of review, finding that any of the tax court's factual findings were clearly erroneous, identifying which of the tax court's detailed factual findings with which it disagreed, and identifying facts it relied upon in deciding another issue that the tax court had never reached.

PARTIES TO THE PROCEEDINGS

The Petitioners are Norma L. Slone, Transferee; Slone Family GST Trust, UA Dated August 6, 1998, Transferee, D. Jack Roberts, Trustee; James C. Slone, Transferee; Slone Revocable Trust, UA Dated September 20, 1994, Transferee, James C. Slone and Norma L. Slone, Trustees.

The Respondent is the Commissioner of Internal Revenue.

TABLE OF CONTENTS

| | Page |
|--|------|
| OPINIONS BELOW | 1 |
| JURISDICTION | 1 |
| STATUTORY AND REGULATORY PROVISIONS INVOLVED..... | 1 |
| STATEMENT..... | 3 |
| REASONS FOR GRANTING THE PETITION..... | 10 |
| A. This Court has emphasized the central importance of the clearly erroneous standard | 10 |
| B. The Ninth Circuit based its decision on conclusions directly contradicted by the tax court's findings of fact without deference to the trial court and without any determination that the contrary findings of fact were clearly erroneous..... | 12 |
| CONCLUSION | 19 |

APPENDIX

| | |
|--|---------|
| Court of appeals opinion (July 24, 2018) | App. 1 |
| Tax court supplemental memorandum opinion (June 13, 2016) | App. 13 |
| Court of appeals order and amended opinion (August 28, 2015) | App. 36 |
| Tax court memorandum findings of fact and opinion (March 1, 2012) | App. 57 |
| Court of appeals order denying petition for panel rehearing and petition for rehearing en banc (October 1, 2018) | App. 81 |

TABLE OF AUTHORITIES

| | Page |
|--|--------------|
| CASES | |
| <i>Anderson v. City of Bessemer</i> , 470 U.S. 564 (1985)..... | 10, 11, 16 |
| <i>Comm'r v. Stern</i> , 357 U.S. 39 (1958)..... | 4, 9, 16, 17 |
| <i>Freytag v. Comm'r</i> , 501 U.S. 868 (1991) | 2 |
| <i>Global-Tech Appliances, Inc. v. SEB S.A.</i> , 563 U.S. 757 (2011) | 15 |
| <i>Hongsermeier v. Comm'r</i> , 621 F.3d 890 (9th Cir. 2010) | 3 |
| <i>Inwood Laboratories, Inc. v. Ives Laboratories, Inc.</i> , 456 U.S. 844 (1982)..... | 10 |
| <i>John M. Alterman Trust U/A/D May 9, 2000 v. Comm'r</i> , T.C. Memo. 2015-231 | 14 |
| <i>Julia Swords Trust v. Comm'r</i> , 142 T.C. No. 19 (2014)..... | 14 |
| <i>North Pacifica LLC v. City of Pacifica</i> , 526 F.3d 478 (9th Cir. 2008)..... | 18 |
| <i>Shell Petroleum Inc. v. U.S.</i> , 2008 WL 2714252 (S.D. Tex. July 3, 2008)..... | 14 |
| <i>Silvester v. Harris</i> , 843 F.3d 816 (9th Cir. 2016)..... | 18 |
| <i>Slone v. Comm'r</i> , 788 F.3d 1049 (9th Cir. 2015).... | 3, 4, 9 |
| <i>Slone v. Comm'r</i> , 896 F.3d 1083 (9th Cir. 2018) | 3, 5, 9, 15 |
| <i>Slone v. Comm'r</i> , T.C. Memo. 2012-57 | 3 |
| <i>Slone v. Comm'r</i> , T.C. Memo. 2016-115 | 3, 4 |

TABLE OF AUTHORITIES – Continued

| | Page |
|--|------------|
| <i>Starnes v. Comm'r</i> , 680 F.3d 417 (4th Cir. 2012) | 17 |
| <i>Teva Pharm. USA, Inc. v. Sandoz, Inc.</i> , 574 U.S. ____, 135 S. Ct. 831 (2015)..... | 11, 12, 16 |
| <i>Thomas v. County of Los Angeles</i> , 978 F.2d 504 (9th Cir. 1992)..... | 18 |
| <i>U.S. Bank Nat'l Ass'n v. Vill. at Lakeridge, LLC</i> , ____ U.S. ___, 138 S. Ct. 960 (2018)..... | 11, 16 |
| <i>United States v. Real Estate Boards</i> , 339 U.S. 485 (1950)..... | 11 |

STATUTES AND REGULATIONS

| | |
|--|-----------|
| 26 U.S.C. § 351(a)..... | 14 |
| 26 U.S.C. § 362(a)(1) | 15 |
| 26 U.S.C. § 6213(a)..... | 3 |
| 26 U.S.C. § 6901(a)(1) | 3 |
| 26 U.S.C. § 7482(a)..... | 2 |
| 26 U.S.C. § 7482(a)(1) | 3 |
| 28 U.S.C. § 1254(1)..... | 1 |
| Advisory Committee Notes to Fed. R. Civ. P. 52(a) 1985 Amendment..... | 11 |
| Fed. R. Civ. P. 52(a)(6)..... | 1, 10, 17 |
| Rule 1(b), United States Tax Court Rules of Practice and Procedure..... | 2 |

OPINIONS BELOW

The opinions of the court of appeals (App. 1-12; 36-56) are reported at 896 F.3d 1083 and 810 F.3d 599 respectively. The memorandum findings of fact and opinion and supplemental memorandum opinion of the tax court (App. 57-80; 13-35) are reported at T.C. Memo. 2012-57 and 2016-115 respectively and are available on Westlaw at 2012 WL 691401 (U.S. T.C. Mar. 1, 2012) and 2016 WL 3264397 (U.S. T.C. June 13, 2016) respectively.

JURISDICTION

The judgment of the court of appeals was entered on July 24, 2018. A combined petition for rehearing en banc and petition for panel rehearing was denied on October 1, 2018. App. 81-82. On November 20, 2018, Justice Kagan extended the time within which to file a petition for writ of certiorari to and including January 30, 2019. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The pertinent provision is Rule 52(a)(6), Federal Rules of Civil Procedure:

Rule 52. Findings and Conclusions by the Court;
Judgment on Partial Findings

(a) FINDINGS AND CONCLUSIONS.

(1) *In General.* In an action tried on the facts without a jury or with an advisory jury, the court must find the facts specially and state its conclusions of law separately. The findings and conclusions may be stated on the record after the close of the evidence or may appear in an opinion or a memorandum of decision filed by the court. Judgment must be entered under Rule 58.

* * *

(6) *Setting Aside the Findings.* Findings of fact, whether based on oral or other evidence, must not be set aside unless clearly erroneous, and the reviewing court must give due regard to the trial court's opportunity to judge the witnesses' credibility.

The tax court must give particular weight to the Federal Rules of Civil Procedure to the extent they are suitably adaptable. Rule 1(b), United States Tax Court Rules of Practice and Procedure. Moreover, the tax court "exercises judicial power to the exclusion of any other function" and its decisions "are appealable only to the regional United States Courts of Appeal . . . [which decisions] are reviewed 'in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury. [26 U.S.C.] § 7482(a).'" *Freytag v. Comm'r*, 501 U.S. 868, 891 (1991). The Ninth Circuit reviews the tax court's findings of

fact for clear error. *Hongsermeier v. Comm'r*, 621 F.3d 890, 899 (9th Cir. 2010).

STATEMENT

Two of the Petitioners, the Slone Revocable Trust and the Slone Family GST Trust, are the former shareholders of Slone Broadcasting Corporation, who sold the stock in the corporation in 2001. In 2009, the Commissioner of Internal Revenue sought to hold Petitioners responsible as transferees for an estimated \$15.3 million in taxes that were not paid by the purchaser of the corporation's stock. Petitioners prevailed twice in tax court. *Slone v. Comm'r*, T.C. Memo. 2012-57 ("*Slone I*"); *Slone v. Comm'r*, T.C. Memo. 2016-115 ("*Slone III*"). The tax court had jurisdiction pursuant to 26 U.S.C. §§ 6213(a) and 6901(a)(1). The Commissioner twice appealed to the Ninth Circuit, resulting in two published opinions, as well as a separate partial dissenting opinion. *See Slone v. Comm'r*, 788 F.3d 1049 (9th Cir. 2015), *amended and superseded by* 810 F.3d 599 (9th Cir. 2015) ("*Slone II*"); *Slone v. Comm'r*, 896 F.3d 1083 (9th Cir. 2018) ("*Slone IV*"). The court of appeals had jurisdiction pursuant to 26 U.S.C. § 7482(a)(1). In each opinion, the Ninth Circuit reversed the tax court.

In *Slone II*, the Ninth Circuit held that to assess tax liabilities against a transferee, the finder of fact must determine whether the transferee is substantively liable for the transferor's unpaid taxes because the transferee had actual or constructive knowledge

that the transaction had no purpose other than tax avoidance. The court further held that the Commissioner had the burden of establishing liability under two separate and independent federal and state law prongs in accordance with *Comm'r v. Stern*, 357 U.S. 39 (1958). Under the federal law prong, the court remanded for findings as to whether the shareholders had a business purpose for entering into the stock purchase transaction other than tax avoidance, or whether the stock purchase transaction had economic substance other than shielding the Slone Broadcasting shareholders from tax liability. App. 51. Under the state law prong, the court remanded for findings as to whether the shareholders were substantively liable under state law (the Arizona Uniform Fraudulent Transfer Act), including whether they had actual or constructive notice of the purchaser's entire tax evasion scheme. App. 51-52. The *Slone II* court directed the tax court to make the requisite findings of fact in the first instance. App. 52.

In *Slone III*, the tax court incorporated by reference its factual findings in *Slone I*, making credibility determinations as to each witness appearing before it and further making factual findings based on witness testimony, documentary evidence, and stipulations of the parties. App. 14, 58-70. The tax court affirmatively found that the Slone shareholders did not have either actual or constructive knowledge required by *Slone II* under the state law prong of *Stern*, *i.e.*, that the Slone shareholders lacked actual or constructive notice that the transaction had no purpose

other than tax avoidance. Having found for the Petitioners on the state law prong based on its detailed factual findings and credibility determinations, the tax court found it unnecessary to decide the federal law prong. On further appeal by the Commissioner, in *Slone IV*, the Ninth Circuit reversed the fact-dependent ruling of the tax court on the state law prong and determined the federal prong notwithstanding that the tax court had made no findings on the federal prong.

The Ninth Circuit employed no deference to the factual findings of the tax court. It failed to articulate any standard of review, to identify which of the tax court's detailed factual findings with which it disagreed, and to identify which facts it relied upon in deciding the federal prong (which the tax court had never reached).

In concluding that the shareholders had neither actual nor constructive knowledge that the transaction lacked any purpose other than tax avoidance, the tax court had found numerous specific subsidiary facts supporting its ultimate factual finding that the Slone shareholders had no reason to suspect "any impropriety" (App. 17, 26, 64):

- The shareholders retained three independent advisers to review and advise them on the transaction: Steven Phillips, a tax attorney who advised the Slone Revocable Trust; D. Jack Roberts, the Slones' accountant; and Gregory Gadarian, a tax attorney who advised the Slone Family GST Trust. App. 61-63, 65.

- The purchaser of the stock, Berlinetta, Inc., an affiliate of Fortrend International, LLC, solicited the Slones regarding the stock purchase. App. 61-64.
- The purchaser informed the Slones that they had a plan to acquire the stock of Slone Broadcasting and redirect the company into a debt recovery business through MidCoast Credit Corp., a corporation engaged in the business of collecting delinquent credit card debt acquired from banks. App. 62-63.
- Mr. Phillips conducted due diligence on the proposed transaction. App. 63-64. He reviewed the projections in the Fortrend/MidCoast business plan and concluded they were reasonable. App. 17, 64. He investigated the reputations of Fortrend and MidCoast together with those of their attorneys and accountant advisers and determined that they were good. *Id.* He contacted a broker in the debt recovery business to inquire about MidCoast and was informed that MidCoast played an active role in the asset recovery industry and had a reputation as a legitimate collector, albeit an aggressive one. App. 26, 63-64.
- Mr. Phillips considered whether there were potential legitimate tax strategies to achieve the tax benefits that Fortrend had claimed. Mr. Phillips prepared a memorandum to Mr. Gadarian, the other independent tax attorney who was representing the Slone Family GST trust. Mr. Phillips's memorandum described the plan to offset the company's income by

contributing high basis/low value assets to the purchaser in an Internal Revenue Code Section 351 transaction and selling those assets at a loss before the end of fiscal 2001. App. 17-18, 78. The memorandum also provided a legal analysis of transferee liability considerations for the selling shareholders, ultimately concluding that the shareholders would not be exposed to such liability. App. 18, 65-66.

- Mr. Gadarian performed his own research and agreed with Mr. Phillips's conclusions. App. 18, 66.
- After Mr. Phillips and Mr. Gadarian completed their analysis that the stock sale could proceed, Slone Broadcasting entered into a stock sale agreement with Berlinetta, the Fortrend affiliate. App. 18, 66.
- In connection with the stock sale, the Slone shareholders obtained a representation from the purchaser that it had not engaged in any transactions that would be deemed a prohibited "listed transaction." App. 26, 65. (A "listed transaction" is a tax avoidance transaction that must be disclosed or registered. App. 40-41.)
- Moreover, both Mr. Phillips and Mr. Gadarian previously had considered whether the transaction was a prohibited "intermediary transaction" tax shelter linked to an earlier sale of assets of the corporation. App. 18, 66. In initiating the proceedings below, the Commissioner contended that the transaction was a prohibited "intermediary transaction" tax shelter,

but later abandoned that argument in the tax court and acknowledged that the IRS notice prohibiting such transactions did not apply. The Commissioner then changed his theory of the case. App. 75.

- Slone Broadcasting and the Slone shareholders had no involvement in the purchaser's financing of the stock sale; after the stock sale closed, the Slones and the Slone shareholders had no knowledge of, or say in, the operation of Slone Broadcasting. App. 18-19.
- The purchaser financed the acquisition of the stock through a combination of loans and equity and held at least \$18,459,360 of equity at the time of closing (App. 66): when added to the Slone Broadcasting's assets, that amount exceeded that company's liabilities, including tax liabilities. App. 64-65.
- In addition, the purchaser had agreed on a restriction that no use would be made of the funds held in Slone Broadcasting's bank account until 10 days after the closing date (App. 66), thereby precluding use of Slone Broadcasting's cash for the purchase of the stock in a circular transaction.

In setting forth its findings, the tax court expressly stated that it had made credibility determinations in favor of the Slones. App. 14, 25, 77. In addition to its affirmative findings that the Slones had neither actual nor constructive notice of a scheme that had no purpose other than tax avoidance, the tax court pointed out that the burden of proof under the state

law prong was on the Commissioner and that the Commissioner had failed to prove essential elements under the Arizona Uniform Fraudulent Transfer Act. The tax court specifically found that the Commissioner had failed to meet his burden of proof to establish the financial condition of the purchaser, an essential element of a fraudulent transfer under the state law prong: “Respondent did not prove that the sum of Slone Broadcasting/Arizona Media’s debts was greater than all of Slone Broadcasting/Arizona Media’s assets at a fair valuation. Nor did he prove that Slone Broadcasting/Arizona Media was not paying its debts as they came due.” App. 33.

In *Slone IV*, the Ninth Circuit did not articulate a standard of review and did not make any determination that the factual findings of the tax court were clearly erroneous. The court of appeals did not hear or see the testimony of Mr. and Mrs. Slone, the shareholders’ advisers (Mr. Roberts, Mr. Phillips and Mr. Gadarian), or the IRS revenue agent (Ms. Brandt). In addition, the Ninth Circuit determined the federal law prong of *Stern* without any findings having been made by the tax court, a determination the Ninth Circuit had previously stated it could not make in *Slone II* because findings under the federal prong were a matter for the tax court in the first instance.

REASONS FOR GRANTING THE PETITION

The Ninth Circuit in this case has departed from this Court’s direction that appellate courts must apply a clearly erroneous standard of review before they may reverse a trial court’s decision dependent upon its factual findings.

A. This Court has emphasized the central importance of the clearly erroneous standard.

The trial court’s findings of fact, whether based on trial testimony, solely on documentary evidence, stipulated facts, or inferences drawn from such evidence are to be reviewed for clear error, not *de novo*. Fed. R. Civ. P. 52(a)(6); *Anderson v. City of Bessemer*, 470 U.S. 564, 574-75 (1985). “The rationale for deference to the original finder of fact is not limited to the superiority of the trial judge’s position to make determinations of credibility. The trial judge’s major role is the determination of fact, and with experience in fulfilling that role comes expertise.” *Anderson*, 470 U.S. at 574.

Deference requires that “[w]here there are two permissible views of the evidence, the factfinder’s choice between them cannot be clearly erroneous.” *Anderson*, 470 U.S. at 574; *see also Inwood Laboratories, Inc. v. Ives Laboratories, Inc.*, 456 U.S. 844, 857-58 (1982) (“An appellate court cannot substitute its interpretation of the evidence for that of the trial court simply because the reviewing court ‘might give the facts another construction, resolve the ambiguities differently, and find a more sinister cast to actions which the District Court

apparently deemed innocent.' *United States v. Real Estate Boards*, 339 U.S. 485, 495 (1950).").

These rules are grounded in the policy of not undermining the legitimacy of trial courts in the eyes of litigants. Advisory Committee Notes to Fed. R. Civ. P. 52(a) 1985 Amendment ("To permit courts of appeals to share more actively in the fact-finding function would tend to undermine the legitimacy of the district courts in the eyes of litigants, multiply appeals by encouraging appellate retrial of some factual issues, and needlessly reallocate judicial authority."). "[T]he parties to a case on appeal have already been forced to concentrate their energies and resources on persuading the trial judge that their account of the facts is the correct one; requiring them to persuade three more judges at the appellate level is requiring too much. . . . [T]he trial on the merits 'should be the main event . . . rather than a tryout on the road.'" *Anderson*, 470 U.S. at 575.

Recently, this Court has recognized the importance of clarifying the standard of review employed by courts possessing specific subject matter expertise and having nationwide reach. *U.S. Bank Nat'l Ass'n v. Vill. at Lakeridge, LLC*, __ U.S. __, 138 S. Ct. 960 (2018) (applying *Anderson* and clarifying clear error standard of review applies to specialized bankruptcy court determination of question of mixed law and fact as to whether a person qualifies as a non-statutory insider that purchased claim in an arm's length transaction). *Teva Pharm. USA, Inc. v. Sandoz, Inc.*, 574 U.S. __, 135 S. Ct. 831 (2015) (applying *Anderson* and clarifying clear error standard of review applies to subsidiary

fact determinations made in the specialized area of patent claim construction). In *Teva*, clarification was needed because the “Federal Circuit reviews the claim construction decisions of federal district courts throughout the Nation.” 135 S. Ct. at 836. Similarly, the tax court is a specialized court of national reach and the standard of review applied to its factual findings has nationwide import.

B. The Ninth Circuit based its decision on conclusions directly contradicted by the tax court’s findings of fact without deference to the trial court and without any determination that the contrary findings of fact were clearly erroneous.

1. The Ninth Circuit’s opinion is based entirely upon its conclusion that “Petitioners were at the very least on constructive notice that the entire scheme had no purpose other than tax avoidance.” App. 5-6. To support this assertion, the Ninth Circuit concluded that Petitioners were on constructive notice by virtue of the nature of the purchaser’s financing structure for the stock sale because the “financing transactions . . . demonstrate that the deal was only about tax avoidance,” that the purchaser/new company “had no assets with which to pay the taxes due from the original asset sale,” and “borrowed the funds to make the purchase” so that after the sale “Slone Broadcasting’s significant cash holdings went immediately out the door.” App. 4, 6-7. The court asserted that the stock sale “left neither Slone Broadcasting nor Berlinetta able to satisfy Slone

Broadcasting's \$15.3 million tax liability." App. 8-9. The tax court's findings of fact squarely contradicted each of these conclusions. In particular, the tax court specifically found that the Slones had no involvement in the purchaser's financing structure and that the purchaser had assets above and beyond the financing with which to pay liabilities:

- "Slone Broadcasting had no involvement in the financing." App. 18, 66. Moreover, "[a]fter the stock sale was closed petitioners had no knowledge or say in the operation of Slone Broadcasting." App. 19.
- "Berlinetta [the purchaser] financed the acquisition of the stock through a combination of loans and equity. . . . Berlinetta also held at least \$18,459,360 of equity at the time of closing." App. 66.

In further support of its conclusion, the Ninth Circuit asserted that Petitioners were on constructive notice because in a lengthy memorandum, the tax counsel retained by the Petitioners (Mr. Phillips) "never analyzed how Berlinetta could legally offset Slone Broadcasting's taxable gain from the [prior] asset sale." App. 11. To the contrary, the tax court made the explicit finding that Mr. Phillips *had* analyzed the potential for offsetting the gain with the contribution of high basis/low value assets to be sold at a loss:

In fact, in Mr. Phillips' memo to Mr. Gadarian dated November 21, 2001, he explains Fortrend's plan to offset the gains from the asset sale by contributing high basis/low value assets

to Berlinetta in a section 351 transaction and selling those assets at a loss before the end of 2001.

App. 78; *see also* App. 17-18. Deference to the tax court's findings of fact within its sphere of expertise applies with particular force.

The tax court's finding that Mr. Phillips undertook a reasonable analysis of the potential for a legitimate section 351 transaction to achieve tax savings is further supported by other reported decisions involving Fortrend as purchaser or having similar fact patterns to this case that have recognized that there were legitimate tax planning strategies at the time that could be employed to reduce or avoid taxes. *John M. Alterman Trust U/A/D May 9, 2000 v. Comm'r*, T.C. Memo. 2015-231 at 58 ("there are legitimate tax planning strategies involving built-in gains and losses" and holding that "it was not unreasonable for the [petitioners] and their advisers to believe MidCoast's [Fortrend's manager's] business plan was viable"); *Julia Swords Trust v. Comm'r*, 142 T.C. No. 19 at 53 (2014) ("This Court has acknowledged that there are legitimate tax planning strategies involving built-in gains and losses and that it was not unreasonable, in the absence of contradictory information, for the representatives to believe that the buyer had a legitimate tax planning method."); *see also Shell Petroleum Inc. v. U.S.*, 2008 WL 2714252, **13, 27 (S.D. Tex. July 3, 2008) (holding that a section 351 transaction was proper, and that the adviser in that case knew "as any knowledgeable tax lawyer would have," that under 26 U.S.C. §§ 351(a) and

362(a)(1) there was an ability to transfer an asset and for the receiver of the asset to have a built-in loss from the asset received; “the law in effect at the time of the underlying events permitted the transferor’s basis in the transferred property to be carried over to become the transferee’s basis in the property, even if that basis exceeds the fair market value of the property”).

2. The Ninth Circuit did not even articulate a standard of review in *Slone IV*. Nor did the Ninth Circuit identify any of the tax court’s detailed findings with which it disagreed regarding the reasonableness of the Slones’ advisers’ due diligence and analysis of potential legitimate tax strategies supporting the tax court’s findings that the Slones’ advisers “made a reasonable inquiry as to the actions Berlinetta would take to achieve the tax savings,” and, ultimately, that the Petitioners had no reason to suspect “any impropriety.” App. 17, 26, 64.

3. In *Slone IV*, the Ninth Circuit further predicated its reversal on its own determination that Petitioners had engaged in “willful blindness.” App. 11. But the court reached this determination without first finding that it was clearly erroneous for the tax court to find just the opposite—that Petitioners did not have any reason to suspect any impropriety. Willful blindness consists of two elements: “(1) the defendant must subjectively believe that there is a high probability that a fact exists and (2) the defendant must take deliberate actions to avoid learning of that fact.” *Global-Tech Appliances, Inc. v. SEB S.A.*, 563 U.S. 757, 769

(2011). The subjective belief of the Slones was a matter of fact for determination by the tax court. The tax court explicitly found that “[t]here was no reason for Mr. Roberts or Mr. Phillips [the Slones’ advisers] to suspect any impropriety” and that “Petitioners had no reason to believe that Fortrend’s methods were illegal or inappropriate.” App. 17, 78. The appellate court did not hear or see the testimony of the Slones or their three advisers (Mr. Roberts, Mr. Phillips, and Mr. Gadarian). By contrast, the tax court assessed the Slones’ subjective beliefs and purposes, determining that neither the Slones nor their advisers had any knowledge—actual or constructive—of an illegitimate tax scheme and had no reason to suspect any impropriety.

4. By affording no deference to the tax court’s findings of fact on the state law prong of *Stern*, the Ninth Circuit failed to apply the holdings and rationale of *Anderson*, *Teva*, and *U.S. Bank*. The tax court had tools to determine the facts necessary to decide actual or constructive notice. The tax court judge had the ability to question witnesses, including the professionals with expertise in tax law. The tax court sat through the entire trial, assessed whether Petitioners and their advisers had acted in earnest, and made specific credibility determinations in their favor. Yet the Ninth Circuit’s opinion did not apply *Anderson*, afforded no deference to the factual findings of the tax court, and did not articulate any standard of review other than that it disagreed with the ultimate decision of the trial court. The reported Ninth Circuit opinion, if left to stand, will no doubt be used by unsuccessful parties in

the tax court to appeal decisions of that court on the basis of mere disagreement, subverting what the Advisory Committee found to be the *raison d'etre* of Fed. R. Civ. P. 52(a)(6): to avoid a multiplicity of appeals premised upon appellate retrial of factual issues thereby needlessly reallocating judicial authority. *See* discussion, *supra* at 11.

Moreover, the approach of the Ninth Circuit to the state law prong of *Stern* conflicts with the decision of the Fourth Circuit in another case involving the same issues and one of the same parties, *MidCoast. Starnes v. Comm'r*, 680 F.3d 417, 435-36 (4th Cir. 2012) (tax court findings of fact reviewed for clear error):

This evidence certainly supports the Commissioner's position in this litigation. But they do not persuade us that the Tax Court was *clearly erroneous* in finding that, under the circumstances shown by the evidence, the Former Shareholders lacked constructive knowledge that [the company they sold to be re-engineered into an asset recovery business] was unlikely to pay its 2003 taxes. To the contrary, there was ample countervailing evidence to that relied on by the Commissioner supporting the lower court's finding that the admittedly limited inquiry by the Former Shareholders did little to bolster the Commissioner's case. Properly viewed, as we suggest above, the Tax Court clearly found that the Former Shareholders would not have learned through further inquiry so much more of MidCoast's

intentions to justify the court's imposition of constructive knowledge.

(Emphasis added.)

5. The Ninth Circuit's departure here from the clearly erroneous standard cannot be characterized as an idiosyncratic aberration; the same Circuit has failed to defer to the factual findings of trial courts in several other cases as well. *See, e.g., Silvester v. Harris*, 843 F.3d 816, 828 (9th Cir. 2016) (setting aside the district court's factual findings as to several expert reports without identifying the standard of review or finding clear error); *North Pacifica LLC v. City of Pacifica*, 526 F.3d 478 (9th Cir. 2008) (reversing district court judgment and reinterpreting factual findings of trial court regarding sufficiency of requisite knowledge for discriminatory treatment); *Thomas v. County of Los Angeles*, 978 F.2d 504 (9th Cir. 1992) (rejecting the district court's factual findings without identifying the standard of review or finding clear error).

CONCLUSION

The petition for writ of certiorari should be granted to ensure that federal appellate courts apply the correct standard of review of the tax court's findings of fact in this and other cases.

Respectfully submitted,

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