No. _____

In the
Supreme Court of the United States

BOCILLA ISLAND SEAPORT, INC., formerly
HIGHPOINT TOWER TECHNOLOGY, INC.,
Petitioner,

v.

COMMISSIONER OF THE INTERNAL REVENUE SERVICE,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

PETITION FOR WRIT OF CERTIORARI

DAVID D. AUGHTRY
Counsel of Record
CHAMBERLAIN, HRDLICKA,
WHITE, WILLIAMS & AUGHTRY
191 Peachtree Street, 46th FL
Atlanta, Georgia 30303-1747
Phone: (404) 659-1410
david.aughtry@chamberlainlaw.com

Attorney for Petitioner

Becker Gallagher · Cincinnati, OH · Washington, D.C. · 800.890.5001

QUESTIONS PRESENTED

This Tax Court partner-level penalty jurisdiction case raises these four interrelated issues:

1) Should "each partner's outside basis [in his partnership interest]... be adjusted at the partner level *before* the [basis-specific] penalty can be imposed" under the implicated statutes Justice Scalia reconciled in *United States v. Woods*, 571 U.S. 31, 42 (2013)?

2) Should a partner's cost basis in Euros (which the partnership proceeding deemed that the partner acquired directly) "be adjusted at the partner level *before* the [basis] penalty can be imposed"?

3) Does the "plain meaning" of the implicated statutes reverse that sequence (imposition of basis penalty *before* determination of basis) and require separate additional proceedings, despite the reading of those statutes in *Woods*, the acknowledged algebraic absurdity, and the overarching legislative purpose of eliminating duplicative proceedings?

4) Where, as here, a separate partner-level Tax Court deficiency proceeding is required to address the impact of partner-level facts on the partner's basis in the Euros reported solely on the partner's return, does that jurisdiction permit the partner-level reasonable cause facts that preclude the IRS imposing the partner-level, basis-specific penalty?

RULE 14(b) STATEMENT

The parties to the proceeding are Petitioner/ Appellant, Bocilla Island Seaport, Inc., formerly Highpoint Tower Technology, Inc., and Respondent/ Appellee, the Commissioner of the Internal Revenue Service.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Bocilla Island Seaport, Inc., formerly Highpoint Tower Technology, Inc., is wholly owned by Bokeelia Realty, LLC, a limited liability company formed under the laws of the State of Florida.

PROCEEDINGS BELOW

A list of all proceedings in trial and appellate courts directly related to this case is as follows:

Highpoint Tower Technology, Inc. v. Commissioner of the Internal Revenue Service, United States Tax Court, Docket No. 2828-16 (July 17, 2017)

Highpoint Tower Technology, Inc. v. Commissioner of the Internal Revenue Service, United States Court of Appeals for the Eleventh Circuit, No. 18-10394-BB (July 24, 2019)

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PETITION FOR A WRIT OF CERTIORARI

Bocilla Island Seaport, Inc., formerly Highpoint Tower Technology, Inc. ("Highpoint"), respectfully petitions for a writ of certiorari to review the opinion and judgment of the United States Court of Appeals for the Eleventh Circuit.

OPINIONS BELOW

The opinion of the Eleventh Circuit is published at 931 F.3d 1050 (11th Cir. 2019), and is reproduced in the Petition Appendix A ("Pet. App.") at pp. App. 1-App. 32. The November 2, 2017 Order of the United States Tax Court is unpublished. It was entered at Docket No. 2828-16 on November 2, 2017 and is reproduced at Pet. App. B, pp. App. 33-App. 36. The July 17, 2017 Order of the United States Tax Court is unpublished. It was entered at Docket No. 2828-16 on July 17, 2017 and is reproduced at Pet. App. C, pp. App. 37-App. 40.

JURISDICTION

The Opinion of the Eleventh Circuit was entered on July 24, 2019. This Court has jurisdiction pursuant to 28 U.S.C. § 1254.

STATUTES OR OTHER PROVISIONS INVOLVED

The following statutes are located in the Appendix at Appendix D:

26 U.S.C. § 6213(a)

26 U.S.C. § 6214(a)

26 U.S.C. § 6230(a)

26 U.S.C. § 6330(a)-(d)

26 U.S.C. § 6662 (1999)

26 U.S.C. § 6664(c) (1999)

INTRODUCTION

Twenty years ago, Highpoint's advisors persuaded the company to acquire a set of Euro options. Highpoint contributed the purchased option to Arbitrage, which traded in currency derivatives. When the Euro declined, Highpoint withdrew from Arbitrage, received Euros in redemption of its partnership interest, and then sold those Euros.

Highpoint reported the loss on those Euros on its return based on the advice of its long-time lawyer and CPA who relied on the exhaustive research performed by an international tax law firm headquartered in New York City, Curtis Mallet-Prevost. That research turned on what the Court of Claims and Federal Circuit determined in the lead case to be the then prevailing authority on the treatment of basis.[1] However, those courts then disregarded the transactions based on the economic substance doctrine. After the final appeal in the lead case, Arbitrage accepted the result, conceded the partnership issues, and explicitly reserved the partner-level defenses for its partners. In the partnership proceeding, Arbitrage was disregarded and Highpoint was deemed to have directly acquired the Euros distributed to it.

The IRS then issued a Partner-Level Deficiency Notice to Highpoint – disallowing its Euro basis and resulting loss, asserting a deficiency, and applying the basis-specific penalty to its reported Euro basis.

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[1] *Jade Trading LLC v. United States*, 80 Fed. Cl. 11, 34 (2007), *aff'd in part, rev'd in part and remanded*, 598 F.3d 1372, 1380 (Fed. Cir. 2010), *and supplemented*, 98 Fed. Cl. 453, 463 (2011), *aff'd*, 2012 WL 178382 (Fed. Cir. Jan. 12, 2012).

Highpoint petitioned that Deficiency Notice to the Tax Court. Four days later, the IRS assessed and demanded payment of the deficiency and basis-specific penalty, even though they were still pending in Tax Court. Highpoint moved to restrain that collection. The IRS and Tax Court agreed the deficiency should be restrained because proof of the partner-level basis facts required the pending Tax Court partner-level proceeding. But the IRS persuaded the Tax Court and the Eleventh Circuit that the Tax Court lacked partner-level jurisdiction over the partner-level, basis-specific penalty in the same partner-level proceeding that would determine that same basis.

The Eleventh Circuit agreed with Highpoint that the sequence of imposing a basis-specific penalty before determining the basis rendered an algebraic absurdity. The Court, however, concluded that the algebraic absurdity was acceptable under the "plain meaning" doctrine and pointed to Highpoint's ability to file a Collection Due Process case in Tax Court where Highpoint could ultimately press its partner-level reasonable-cause defense to the basis-specific penalty in that new case. Like the Tax Court plenary jurisdiction statutes and those instances when the IRS asserts partner-level penalty jurisdiction, the CDP response once again heralds that Tax Court partner-level penalty jurisdiction. Rather than *start* a new duplicative CDP administrative proceeding and ultimately the further delayed CDP Tax Court proceeding, Highpoint badly needs to finally resolve this 20 year old dispute over the inextricably intertwined basis and basis-specific penalty once and for all in this one partner-level proceeding under the practical sequence embraced by Justice Scalia.

STATEMENT OF THE CASE

On November 6, 2015, the Commissioner of the Internal Revenue Service issued his Notice of Deficiency ("Partner-Level Notice") to Highpoint alleging a tax deficiency and penalty that dated back to its taxable year ended December 31, 1999. That Notice asserted that Highpoint owed more than $5 million in tax plus a penalty of more than $2 million for a transaction that occurred nearly 16 years before. With interest, the government sought more than $20 million from Highpoint. Because of the significant losses Highpoint suffered in the 2008 Recession, it did not have the financial ability to pay the entire deficiency, interest, and penalty, and pursue a claim for refund in the United States District Court as contemplated by 28 U.S.C. § 1346(a)(1). Highpoint's only remedy was to pursue litigation in the prepayment forum offered by the United States Tax Court.

During the taxable year ended December 31, 1999, Highpoint's professional advisors had encouraged the company to invest in foreign currency options. As part of that transaction, Highpoint purchased a Euro option from AIG International ("AIGI") while simultaneously selling a Euro option to AIGI. Highpoint then contributed both options to Arbitrage Trading, LLC ("Arbitrage") along with $62,500.00 in cash. In accordance with the then prevailing law, Highpoint reported its basis in its partnership interest in Arbitrage ("outside basis") based on its cash contribution and the fair market value of the purchased Euro option while disregarding the potential obligation under the Euro option it sold to AIGI as a contingent liability.

During 1999, Highpoint withdrew from Arbitrage and received a distribution of Euros in redemption of its partnership interest. Highpoint attributed its outside basis in Arbitrage to those Euros in accordance with 26 U.S.C. § 732(a). Highpoint confirmed with both its longtime trusted lawyer and CPA, as well as a sophisticated international law firm and CPA firm that its computation of both its outside basis in Arbitrage and its consequent basis attributed to the Euros it received in redemption of its interest was the proper treatment. Highpoint sold the Euros it received from Arbitrage and reported a loss on its U.S. Corporation Income Tax Return ("Form 1120") for the taxable year ended December 31, 1999.

On October 13, 2005, the IRS issued a Notice of Final Partnership Administrative Adjustments ("FPAA") to Arbitrage asserting that it lacked economic substance, was a sham for federal income tax purposes, and that "all transactions engaged in directly by the partnership … are treated as engaged in directly by its purported partners." Arbitrage challenged the adjustments in the FPAA as part of a partnership-level proceeding in the United States Court of Federal Claims. That partnership-level proceeding was resolved via an Amended Judgment filed by the Clerk of Court on October 3, 2014.[2]

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[2] The results of *Jade Trading, LLC v. United States*, 98 Fed. Cl. 453 (2011); *aff'd*, 2012 WL 178382 (Fed. Cir. Jan. 12, 2012), were dispositive on the adjustments at issue in the partnership-level proceeding for Arbitrage. The only remaining issue was the accuracy-related penalties asserted on those adjustments. That issue was resolved by *United States v. Woods*, 571 U.S. 31 (2013).

The October 3, 2014 Amended Judgment sustained all of the adjustments contained in the FPAA issued to Arbitrage for the taxable year 1999, and all explanations contained in Exhibit A to the FPAA were conceded to be correct. Additionally, the Amended Judgment upheld penalties asserted in the FPAA, and stated that such penalties were applicable to "underpayments of tax attributable to adjustments to contribution amounts in excess of the corrected basis." The Amended Judgment addressed solely partnership matters, and confirmed that the "partners of [Arbitrage] reserve their right to pursue partner-level defenses to [the] penalties."

Based on the adjustments sustained in the Amended Judgment, the IRS issued an "Affected Item Statutory Notice of Deficiency". That Notice asserted that changes needed to be made to Highpoint's return based on the adjustments sustained in the partnership-level proceeding for Arbitrage. The Partner-Level Notice adjusted Highpoint's outside basis in Arbitrage, which attached to the Euros it received in redemption of its partnership interest, and asserted that Highpoint's adjusted basis in the Euros must be calculated "without reference to Arbitrage" and that such basis was "limited to their purchase price or [Highpoint's] purported cash contribution to [Arbitrage]." The Partner-Level Notice reduced Highpoint's basis in the Euros to $0.00 and eliminated a short-term capital loss claimed on its tax return related to the sale of the Euros as well as a deduction for professional fees. The Partner-Level Notice also asserted a deficiency related to a partnership-level loss incurred by Arbitrage during 1999.

The Partner-Level Notice asserted partner-level penalties on the deficiency created by the adjustments to Highpoint's return. The IRS alleged Highpoint had "not established substantial authority for the position taken" and had "not shown that it had a reasonable belief … that the position taken was more likely than not the correct treatment" of the transactions related to Arbitrage and the sale of the Euros. The Partner-Level Notice imposed "a 40 percent penalty … on the underpayment attributable to the gross valuation misstatement of the adjusted basis in [Highpoint's] partnership interest in [Arbitrage] and the consequent basis in the Euros sold or exchanged to which the basis in the partnership attached."[3]

In accordance with 26 U.S.C. § 6213(a), Highpoint timely filed its Petition with the Tax Court disputing the adjustments asserted in the Partner-Level Notice. In its Petition, Highpoint disputed both the deficiency and the penalty asserted in the Partner-Level Notice. Highpoint contested the adjustments made in the Partner-Level Notice and raised its defenses against the 40 percent penalty under 26 U.S.C. § 6664(c). Highpoint alleged the IRS had erred by failing to recognize its partner-level good faith reasonable cause defenses to the penalty, and the fact that it had relied on its qualified professional advisors – defenses that had been unavailable in the partnership-level proceeding for Arbitrage.

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[3] The Notice also erroneously applied the 40 percent basis penalty to the entire deficiency – including non-basis "affected items" such as the disallowance of Highpoint's fees.

Four days after filing its Petition, the IRS issued Highpoint a Notice of Tax Due on Federal Tax Return ("IRS Demand") dated February 8, 2016. The IRS Demand assessed the same tax due and the same 40 percent basis penalty pursuant to 26 U.S.C. § 6662(h) asserted in the Partner-Level Notice. The IRS Demand also sought interest for a total demand in excess of $20 million. Highpoint later received a Notice of Intent to Levy informing Highpoint of the IRS's intent to levy Highpoint's property to collect the amounts asserted in the IRS Demand, as well as an additional failure-to-pay penalty.

In response to the Notice of Intent to Levy, Highpoint filed a Motion to Restrain Collection pursuant to 26 U.S.C. § 6213 and TAX COURT RULE 55 to restrain the IRS from the improper collection of taxes, penalties, and interest for 1999, to which the IRS filed an Objection. On September 15, 2016, Highpoint filed its Response to the Objection, and the IRS filed a Motion to Dismiss and to Strike a Portion of the Proposed Deficiency and the Entire Penalty.

On July 17, 2017, Judge Goeke issued his Order granting Highpoint's Motion in part and denying in part and granting the IRS Motion with respect to the penalty. Judge Goeke's Order held that the Tax Court had jurisdiction with respect to the capital gain income and the disallowance of fees, but that it lacked jurisdiction over the penalty. Highpoint filed a Motion for Reconsideration of the July 17 Order, which Judge Goeke denied. Highpoint timely filed its Notice of Appeal to the United States Court of Appeals for the Eleventh Circuit and paid its filing fee on February 1, 2018.

The Tax Court entered its Orders under the authority of 26 U.S.C. §§ 6213(a) and 6214(a)[4]. Section 7482(a) grants the United States Court of Appeals exclusive jurisdiction to review Tax Court decisions, and 26 U.S.C. § 7482(a)(3) specifically recognizes a Tax Court order "entered under authority of Section 6213(a) and which resolves a proceeding to restrain … collection … as a decision of the Tax Court. That comports with TAX COURT RULE 190(b), which characterizes an "order granting or denying a motion to restrain … collection" as a "decision of the Court for purposes of appeal." Venue lay with the Eleventh Circuit because Highpoint maintained its principal place of business in Florida at the time of its Petition.

The parties filed their briefs, and a three judge panel heard oral arguments in Atlanta, Georgia on May 16, 2019. On July 24, 2019, the panel issued its Opinion affirming the July 17, 2017 Tax Court Order. The Court concluded that the valuation-misstatement penalty at issue was triggered by the partnership-level determination that Arbitrage lacked economic substance and related to an adjustment to a partnership item. The Court excluded the penalty from the Tax Court's partner-level deficiency jurisdiction under 26 U.S.C. § 6230(a)(2)(A)(i).

Highpoint files this Petition for Writ of Certiorari within 90 days of the Eleventh Circuit opinion.

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[4] Section 6214(a) bestows foundational jurisdiction upon the Tax Court in deficiency proceedings to determine "additions to tax", which include penalties. *See* 26 U.S.C. § 6665.

REASONS FOR GRANTING THE PETITION

This case raises serious questions about the supremacy of the Supreme Court, the fluidity of the plain meaning doctrine, and the endorsement of an algebraically absurd sequence. Three points frame those concerns: (i) 26 U.S.C. § 6664(c) bars imposition of, among others, the basis-specific 26 U.S.C. § 6662(e) penalty in the face of "reasonable cause"; (ii) the basis-specific penalty is imposed upon the tax deficiency resulting from a basis determination; and (iii) here, that basis, any resulting loss, and any resulting deficiency must still be determined based on partner-level facts in the Tax Court partner-level proceeding.

Justice Scalia confirmed in *Woods*, 571 U.S. at 42, that "Each partner's outside basis [in his partnership interest] … must be adjusted at the partner level before the penalty can be imposed." Justice Scalia, no stranger to the plain meaning doctrine, determined the proper sequence after reconciling all of the implicated statutes – including 26 U.S.C. § 6664(c).

Without citing Justice Scalia's description of that practical sequence or the 26 U.S.C. § 6664(c) reasonable cause prohibition, the Tax Court and Eleventh Circuit reversed the sequence under the banner of the "plain meaning" doctrine. That sequence reversal overrides this Court's reconciliation of the implicated statutes and endorses the algebraically absurd imposition of the basis penalty *before* determining the basis or any resulting tax deficiency: Unknown ~~Z~~ x 40% = .4 Unknown Penalty. If opposite sequences somehow flow from the same "plain meaning," the doctrine affecting every statute requires greater definition.

Justice Scalia's practical sequence fulfills the Congressional design of the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") by streamlining the partnership/partner process and eliminating the multiplicity of proceedings. That sequence also ensures that the IRS at least accurately calculate (if not accurately assert) any penalty and does not require the taxpayer to pay systemically overstated amounts. Above all else, the practical sequence provides the partner the opportunity to assert his partner-level defenses to the basis penalty in the same proceeding as the basis determination.

As the age of this 1999 case proves, the TEFRA Partnership Procedures (and its 2018 successor) already unmercifully delay by decades the final answer for those partners whose partnerships have been audited – without adding the further delays and expense by requiring a fragmented, duplicative refund trial for those who can pay the (overstated) penalty within six months of the IRS demand or the fragmented, duplicative Collection Due Process trial for those who cannot pay the inaccurate penalty. Stiff-arming trial of the "reasonable cause" bar to the prematurely imposed basis penalty *by 20 to 30 years* works a greater absurdity.

The IRS is quick to prejudice the Court with pejoratives but reversing this Court's statutory reconciliation threatens all of the businesses among the more than 3.7 million partnership returns recently reported as filed in 2016. *See* IRS Publication 5338. The threat of duplicative partner proceedings hovering over their 28.2 million partners should unnerve citizens, the Commissioner, and the Courts.

A. CONGRESS SOUGHT TO STREAMLINE – NOT MULTIPLY – PROCEEDINGS.

Congress enacted the Tax Treatment of Partnership Items Act of 1982, as Title IV of TEFRA, to ensure consistent treatment of partnership items on the individual partners' returns and promote judicial economy by eliminating duplicative proceedings. *See* H.R. Conf. Rep. 97-760 (1982) at 599. Writing for a unanimous Court, Justice Scalia began *Woods* "with a brief explanation of the statutory scheme for dealing with partnership-related tax matters." 571 U.S. at 38. As Justice Scalia explained, any adjustments to partnership items must be made first in a partnership-level proceeding addressing matters relevant to all of the partners. Only after that partnership-level proceeding can adjustments be made at the individual partner level:

> A partnership does not pay federal income taxes; instead, its taxable income and losses pass through to the partners. A partnership must report its tax items on an information return and the partners must report their distributive shares of the partnership's tax items on their own individual returns. Before 1982, the IRS had no way of correcting errors on a partnership's return in a single, unified proceeding. Instead, tax matters pertaining to all the members of a partnership were dealt with just like tax matters pertaining only to a single taxpayer: through deficiency proceedings at the individual-taxpayer level. Deficiency proceedings require the IRS to issue a separate notice of deficiency to each taxpayer, who can file a petition in the Tax Court disputing the

alleged deficiency before paying it. Having to use deficiency proceedings for partnership-related tax matters led to duplicative proceedings and the potential for inconsistent treatment of partners in the same partnership. Congress addressed those difficulties by enacting the Tax Treatment of Partnership Items Act of 1982, as Title IV of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA).

Under TEFRA, partnership-related tax matters are addressed in two stages. First, the IRS must initiate proceedings at the partnership level to adjust "partnership items," those relevant to the partnership as a whole. It must issue [a Notice of Final Partnership Administrative Adjustments] notifying the partners of any adjustments to partnership items, and the partners may seek judicial review of those adjustments. Once the adjustments to partnership items have become final, the IRS may undertake further proceedings at the partner level to make any resulting "computational adjustments" in the tax liability of the individual partners. Most computational adjustments may be directly assessed against the partners, bypassing deficiency proceedings and permitting the partners to challenge the assessments only in post-payment refund actions. Deficiency proceedings are still required, however, for certain computational adjustments that are attributable to "affected items," that is, items that are affected by (but are not themselves) partnership items.

This Court wrestled in *Woods* with whether a partnership-level proceeding should address the 26 U.S.C. § 6662(h) basis penalty[5] the IRS sought to impose on the partner's outside basis in his or her partnership interest because, as this Court wrote, outside basis undeniably constitutes a partner-level item that can only be adjusted in the partner-level proceeding. The law attributes that basis to the assets distributed to the partners upon their redemption of their partnership interest, and impacts the gain or loss the partners report on their returns upon their partner-level sale of those assets.

That reality triggers three critical points under the statutes reconciled by this Court in *Woods*. One, the determination of the existence of the partnership is absolutely a "partnership item" but, as this Court held in *Woods*, the "applicability" of a penalty relating to that partnership item must be determined in the partnership proceeding only on a "provisional" basis. Two, as this Court also held in *Woods*, the outside basis attributed to the distributed assets must be determined at the partner level *before* the basis-specific penalty can be imposed. And, three, the IRS Partnership Notice disregarded the partnership and deemed the partners to have directly acquired the distributed assets. Hence, they acquired a cost basis in those assets. That cost basis underscores the double barrel wisdom of the *Woods* sequence.

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[5] To be precise, 26 U.S.C. § 6662(b)(3) asserts a penalty on "substantial valuation misstatements," (e)(1)(A) parenthetically includes "(adjusted basis of any property)", and (h) then applies a penalty equal to 40 percent of the tax attributable to any substantial valuation misstatement over a heightened threshold.

B. "EACH PARTNER'S OUTSIDE BASIS ... MUST BE ADJUSTED AT THE PARTNER-LEVEL *BEFORE* THE PENALTY CAN BE IMPOSED."

After being barred for 16 years from presenting its partner-level reasonable cause facts, Highpoint received the Partner-Level Notice. At last, Highpoint could defend itself against the 40 percent partner-level, basis-specific penalty and do so in the same partner-level Tax Court proceeding that would determine that same partner-level Euro basis.

Or so Highpoint thought. Highpoint never imagined that the IRS could violate the 26 U.S.C. § 6664(c) prohibition against imposing a penalty in the face of reasonable cause. Highpoint knew the partner-level Tax Court proceeding was required to determine the basis in the Euros Highpoint sold but never imagined the Tax Court somehow could not consider either the basis-specific deficiency penalty or Highpoint's reasonable cause for reporting that basis on its return. Highpoint never imagined that the instrument for streamlining partnership/partner proceedings, the TEFRA Uniform Partnership Procedures, would be construed as requiring at least one, if not two, fractured, duplicative additional proceedings. And in its wildest dreams, Highpoint never conceived that the Supreme Court's recognition of the only practical sequence – determining the basis before imposing the basis penalty – would be ignored in favor of this algebraically absurd reversal:

Undetermined Def. on Undetermined Basis
X 40%
.4 Undetermined Penalty

No one can properly solve the penalty variable without first determining the partner-level deficiency (on which that 40 percent penalty is based) in the ongoing partner-level deficiency proceeding. And no one can properly solve the deficiency variable without first solving the outside basis, the cost basis in the Euros, and the resulting capital gain or loss in the ongoing partner-level deficiency proceeding.

What confuses many people is the incomplete thought that disregarding the partnership means the partner has no partnership interest and thus no outside basis. True enough, but that begs the question – what is the Euro cost basis, how many Euros did the partner sell, in what year? Those partner basis questions require the Tax Court partner proceeding.

The Partner-Level Notice simply ignores any cost basis in the Euros despite the reality that Highpoint purchased the AIG Euro options contributed to Arbitrage (along with its cash contribution) and the IRS FPAA determined that Highpoint is deemed to directly acquire the separate Euros Arbitrage distributed to it. Those Euros did not come free and their cost basis must be finally determined in the pending partner-level Tax Court proceeding.

That still undetermined cost basis in the Euros will impact the still undetermined gain or loss upon their sale; that still undetermined gain or loss will impact the still undetermined deficiency; and that unknown deficiency is required to calculate the still undetermined basis-specific penalty. The only known certainty about the penalty the IRS plucked, assessed, and demanded is just this: it is wrong.

Justice Scalia, renowned for statutory construction, reconciled all the implicated statutes which led the Court to conclude that basis must be determined before the basis penalty can be imposed. That statutory jurisdictional analysis begins with Congress recognizing in 1997 that some penalties flow from partnership level activity. Prior to that point, all penalties constituted partner-level "affected items" reserved for the partner-level affected item proceeding even where the error related to a partnership item. Consequently, Congress amended 26 U.S.C. §§ 6221, 6226(f), and 6230(a)(2) to move the "applicability" of a penalty "that relates to an adjustment to a partnership item" to the partnership level:

6221 ... the tax treatment of any partnership item (and the *applicability* of any penalty, addition to tax, or additional amount which *relates to an adjustment to a partnership item*) shall be determined at the partnership level.

6226(f) SCOPE of JUDICIAL REVIEW.— A court with which a petition is filed in accordance with this section shall have jurisdiction to determine all partnership items of the partnership for the partnership taxable year to which the notice of final partnership administrative adjustment relates, the proper allocation of such items among the partners, and the *applicability* of any penalty, addition to tax, or additional amount *which relates to an adjustment to a partnership item.*

6230(a) COORDINATION WITH DEFICIENCY PROCEEDINGS.—

(1) IN GENERAL.— Except as provided in paragraph (2) or (3), subchapter B of this chapter shall not apply to the assessment or collection of any computational adjustment,

(2) DEFICIENCY PROCEEDINGS TO APPLY IN.—

(A) Subchapter B shall apply to any deficiency attributable to—

(i) affected items which require partner level determinations (other than penalties, additions to tax, and additional amounts that *relate to adjustments to partnership items*) ... (emphasis added).

Notably, Congress limited the penalties in the partnership proceeding to those relating to "partnership items" – not to "partnership items" *and* "affected items," and not to all items. Absent reducing that limitation to surplusage, penalties relating to partner-level "affected items" remained within the jurisdiction of the "affected item" proceeding. And that proceeding invokes the Tax Court deficiency procedures where, as here, partner-level factual determinations are required to determine basis. If determining basis first requires partner-level factual determinations, then determining the basis penalty also first requires those same partner-level factual determinations.

As Justice Scalia recognized, these TEFRA penalty amendments invoke the underlying penalty statutes, including 26 U.S.C. §§ 6662(e) and (h) imposing a heightened 40 percent penalty on deficiencies attributable to basis adjustments and 26 U.S.C. § 6664(c) barring the "imposition" of penalties in the face of good faith reasonable cause. Section 6662(e) defines "substantial valuation misstatement" as "the value of any property (or the adjusted basis of any property)" and (h) imposes a 40 percent penalty where the reported amount is 400 percent of the amount determined to be correct. Critical to Justice Scalia's analysis in *Woods* (but omitted by the courts below), 26 U.S.C. § 6664(c) good faith reasonable cause bars "imposing" the penalty in mandatory terms:

> (1) IN GENERAL. – *No penalty shall be imposed* under this part with respect to any portion of an underpayment if it is shown that there was a *reasonable cause* for such portion and that the taxpayer acted in *good faith* with respect to such portion. (Emphasis added).

As the Eleventh Circuit here and the Supreme Court in *Woods* confirmed, the law barred Highpoint from offering any partner-level defenses in the partnership proceeding — much less Highpoint's partner-level reasonable cause defenses to the basis-specific penalty the IRS Partner Notice later asserted against the basis Highpoint alone reported on its return. So how can one reconcile the bar against asserting reasonable cause and the bar against imposing the penalty in the face of reasonable cause?

This Court drew the dispositive distinction in *Woods* between determining the "applicability" of the 26 U.S.C. § 6662(h) basis penalty on a "provisional" basis at the partnership level and only "imposing" the penalty on the partner *after* adjusting the outside basis in the partner-level proceeding. In that way, the interrelated statutory steps flow in a logical, straightforward sequence. Interestingly, the IRS honored that sequence and distinction in the Partner-Level Notice which serves as the jurisdictional foundation for this partner-level case, by including the 26 U.S.C. § 6662(h) basis penalty and invoking Highpoint's partner-level defenses. The IRS then reversed field and abandoned that sequence by "imposing" the basis penalty via assessment and collection demands *after* Highpoint petitioned the Partner-Level Notice to Tax Court, but *before* the Tax Court determined the basis and any resulting deficiency in the still pending partner-level action.

That IRS reversal in position contravenes the emphasis this Court placed in *Woods* upon the partner-level "imposition" of the penalty: "penalties for tax underpayment must be *imposed* at the partner level, because partnerships themselves pay no taxes. And imposing a penalty always requires some determinations that can be made only at the partner level." *Id*. at 40. (Emphasis in original). It is possible a partner may not have carried over the significant errors determined in the partnership-level proceeding to his own return, or that such errors were not enough to trigger the penalty, "or if they did, the partner may nonetheless have acted in good faith with reasonable cause, which is a bar to the imposition of many penalties, see § 6664(c)(1)." *Id.*

"Notwithstanding that every penalty must be imposed in partner-level proceedings after partner-level determinations, TEFRA provides that the *applicability* of some penalties must be determined at the partnership level." *Id.* 40-41. (Emphasis in original). For that reason, "[t]he applicability determination is … inherently provisional; it is always contingent upon determinations that the court in a partnership-level proceeding does not have jurisdiction to make." *Id.* at 41. This Court held "that TEFRA gives courts in partnership-level proceedings jurisdiction to determine the applicability of any penalty that could result from an adjustment to a partnership item, even if imposing the penalty would also require determining [partner-level items]." *Id.*

This Court reiterated the "provisional" nature of that "applicability" determination and stressed the partner's right to present his partner-level defenses:

> The partnership-level applicability determination, we stress, is provisional: the court may decide only whether adjustments properly made at the partnership level have the potential to trigger the penalty. Each partner remains free to raise, in subsequent, partner-level proceedings, any reasons why the penalty may not be imposed on him specifically. *Id.* at 41-42.

In *Woods*, the District Court did not have the authority to adjust the basis at the partnership level, but it could still determine the provisional applicability of a partnership item penalty based on the adjustments it did have the authority to make as part of the partnership-level proceeding.

This Court concluded, "Each partner's outside basis still must be adjusted at the partner level before the penalty can be imposed, but that poses no obstacle to a partnership-level court's provisional consideration of whether the economic-substance determination is legally capable of triggering the penalty." *Id*. at 42.

Consistent with the *Woods* sequence, the Tax Court undeniably possesses continuing partner-level penalty jurisdiction – especially where it relates to penalties asserted by a partner-level Notice of Deficiency against a partner-level "affected item":

* First, traditional Tax Court plenary jurisdiction still includes penalty jurisdiction. *See* 26 U.S.C. §§ 6213 (Tax Court jurisdiction over "additions to tax" asserted by Notice of Deficiency), 6665 ("[T]he penalties provided by this chapter … shall be assessed, collected, and paid in the same manner as taxes"), 7442 (incorporates Tax Court jurisdiction found elsewhere in Title 26).

* Second, the Tax Court has exercised its partner-level penalty jurisdiction at the request of the IRS. *Meruelo v. Commissioner*, 132 T.C. 355 (2009), *aff'd*, 691 F.3d 1108 (9th Cir. 2012).

* And third, even the IRS and Eleventh Circuit recognize that the Tax Court possesses partner-level penalty jurisdiction in CDP cases.

Hence, the practical sequence recognized by this Court in *Woods* comports with the Tax Court jurisdiction to determine the partner-level basis *before* "imposing" the partner-level basis-specific penalty.

C. THE DICKENSIAN ABSURDITY DOES NOT CURE THE ALGEBRAIC ABSURDITY.

As Highpoint enters its *third decade* of litigation reminiscent of Dickens' *Bleak House*, the "cure" which the IRS pressed on the Eleventh Circuit is that Highpoint should *start* one of two different new cases duplicative of the pending partner-level deficiency proceeding. The Eleventh Circuit opinion reasons that the acknowledged algebraic absurdity is somehow an acceptable "absurdity" under the plain meaning doctrine because "there are at least two other partner-level proceedings available in which the appropriate deficiency and precise amount of the penalty can be determined – CDP proceedings or refund proceedings." *Highpoint v. Commissioner*, 931 F.3d 1050, 1060, n.9 (11th Cir. 2019). Lack of money forces Highpoint onto the deferred Collection Due Process path which, while providing some ultimate access to justice, remains delayed, complex, expensive, and at war with the Congressional purpose of streamlining procedures. Highpoint must wait for the IRS to begin its collection process at some point during the 10 year limitations period following the 2016 assessment (26 U.S.C. § 6502) *before* Highpoint can assert any of its partner-level defenses – justice delayed, memories faded, resources wasted senselessly.

The partner-level 1999 reported basis, 1999 asset cost basis facts, and 1999 authorities in the now pending partner-level Tax Court deficiency trial will be the same in the basis-specific penalty trial – with those facts and authorities supplying the 1999 reasonable cause defenses. That duplication collides with the overarching Congressional TEFRA purpose.

Under the banner of plain meaning, the IRS persuaded the Tax Court and Eleventh Circuit to reverse the practical sequence this Court recognized from its reconciliation of all the implicated statutes. One cannot long wonder how plain the meaning may or may not be when respected courts read the same statutes to convey opposite sequences and when one sequence ignores the statutory "partnership item" limitation and renders an algebraic absurdity.

The seminal "plain meaning" case remains *United States v. American Trucking Ass'ns*, 310 U.S. 534, 542 (1940), where this Court outlined this analysis:

> There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes. Often these words are sufficient in and of themselves to determine the purpose of the legislation. In such cases we have followed their plain meaning. When that meaning has led to absurd or futile results, however, this Court has looked beyond the words to the purpose of the act. Frequently, however, even when the plain meaning did not produce absurd results but merely an unreasonable one 'plainly at variance with the policy of the legislation as a whole' this Court has followed that purpose, rather than the literal words. *American Trucking* at 543.

The reversed sequence violates all four elements: (i) not plain, (ii) creates algebraic absurdity, (iii) requires "futile" CDP administrative proceeding, and (iv) adds duplicative proceedings at war with overarching legislative policy.

The reversed sequence reduces the "partnership item" limitation to surplusage and creates the algebraic absurdity. The Dickensian duplicative "cure" inflicts more harm than the ailment. Forced down the CDP path by lack of money, Highpoint must ask just how plain can the "plain meaning" doctrine be, if it requires a *2006* CDP statutory amendment to retroactively cure the algebraic absurdity the reversed sequence attributes to the *1997* TEFRA amendments?

Highpoint has no control over how many more years will pass before that CDP process can be *started*. The partner must wait for the Secretary to file a lien or levy his property. The IRS has ten years from assessment to take those actions. 26 U.S.C. § 6502. The partner then must timely file a request for a CDP Administrative Hearing under 26 U.S.C. §§ 6230(b) and 6330(b). The IRS prior penalty determination renders that IRS hearing (which the partner must attend) a futile, foregone conclusion. To contest that conclusion, the taxpayer has 30 days to "petition the Tax Court for the review of such determination." 26 U.S.C. § 6330(d)(1). Only then, the CDP litigation *begins*.

Congress did not amend 26 U.S.C. § 6330(d) *until 2006*. It granted the Tax Court sole jurisdiction over CDP, in lieu of the District Court requiring full payment as a prerequisite. The Tax Court first applied the 2006 expansion of its jurisdiction to partner-level penalties *in 2017* – 20 years after the 1997 TEFRA amendments. The CDP "cure" cannot retroactively create a "plain meaning" nor condition the punitive-protection right to trial upon the cruel delay of *starting* the duplicative partner reasonable-cause proceeding 20 to 30 years after the fact.

D. TRADITIONAL TAX COURT JURISDICTION CONTINUES TO COVER A PARTNER PENALTY RELATING TO PARTNER ITEMS.

The foundational Tax Court jurisdiction survives. In 1924, Congress created the predecessor to the Tax Court, the Board of Tax Appeals, to provide the fundamental fairness of allowing citizens to contest IRS assertions they believe to be wrong on a pre-payment basis *before* the IRS imposes its claims. This prepayment forum ensures equal access to the judicial review of the proposed governmental taking of private property, and advances the constitutional protection that no person be deprived of property without the due process of law. The Supreme Court stressed the importance of this right in *Flora v. United States*, 362 U.S. 145, 159 (1960) , by quoting the House Ways and Means Committee Report:

> The committee recommends the establishment of a Board of Tax Appeals to which a taxpayer may appeal prior to the payment of an additional assessment of income, excess-profits, war-profits, or estate taxes. Although a taxpayer may, after payment of his tax, bring suit for the recovery thereof and thus secure a judicial determination on the questions involved, he cannot … secure such a determination prior to the payment of the tax. *The right of appeal after payment of the tax is an incomplete remedy, and does little to remove the hardship occasioned by an incorrect assessment*. … He is entitled to an appeal and to a determination of his liability for the tax prior to its payment. *Id*. at 158-9 (emphasis added).

Based on these principles, Congress provided an extensive set of prepayment "deficiency" procedures under Subchapter B of the Code for citizens to contest IRS claims in Tax Court. That foundational Tax Court deficiency jurisdiction continues to provide taxpayers a pre-payment forum to contest income, gift, and estate tax deficiencies and penalties asserted by the IRS in a Notice of Deficiency.

Tax Court plenary jurisdiction begins with 26 U.S.C. § 7442 which bestows jurisdiction found elsewhere in Title 26. In turn, 26 U.S.C. § 6214(a) provides the foundational jurisdiction over deficiency proceedings – including "additions to tax." Additions to tax include the 26 U.S.C. § 6662 penalty at issue here under 26 U.S.C. § 6665, which states that "any reference in [the Code] to 'tax' imposed by [the Code] shall be deemed also to refer to the … penalties provided by this chapter." Section 6212 requires that the IRS generally issue a "notice of deficiency" before pursuing claims for income, estate, gift, and certain other tax deficiencies and additions to tax which 26 U.S.C. § 6665 extends to the 26 U.S.C. § 6662 penalty. ("[T]he … penalties provided by this chapter … shall be assessed, collected, and paid in the same manner as taxes … ."). 26 U.S.C. § 6213(a) then grants the taxpayer the right to contest that notice in Tax Court by timely filing a Petition. *See Pearson v. Commissioner*, 149 T.C. 424, 428 (2017) ("The Court's jurisdiction in a deficiency case depends on the issuance of a valid notice of deficiency and a timely filed petition.").

CONCLUSION

Trite but true, justice delayed is justice denied. Only Justice Scalia's practical sequence fairly reconciles the implicated statutes, serves the Congressional anti-duplicative proceeding purpose, and cures both the algebraic absurdity and the Dickensian absurdity. The supremacy of this Court's statutory reconciliation and the "plain meaning" doctrine deserve better than the reversed sequence. For these reasons, we respectfully submit that the petition for writ of certiorari should be granted.

Respectfully submitted,

DAVID D. AUGHTRY
Counsel of Record
CHAMBERLAIN, HRDLICKA,
WHITE, WILLIAMS & AUGHTRY
191 Peachtree Street, 46th FL
Atlanta, Georgia 30303-1747
Phone: (404) 659-1410
david.aughtry@chamberlainlaw.com

Attorney for Petitioner

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