No. 21-1397

In the

Supreme Court of the United States

IN RE GRAND JURY

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR *AMICUS CURIAE* THE BUCKEYE INSTITUTE IN SUPPORT OF PETITIONER

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QUESTION PRESENTED

Whether a communication involving both legal and non-legal advice is protected by attorney-client privilege where obtaining or providing legal advice was one of the significant purposes behind the communication.

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INTEREST OF *AMICUS CURIAE*[1]

Amicus Curiae The Buckeye Institute was founded in 1989 as an independent research and educational institution—a "think tank"—whose mission is to advance free-market public policy in the states. The staff at The Buckeye Institute accomplishes the organization's mission by performing timely and reliable research on key issues, compiling and synthesizing data, formulating free-market policy solutions, and marketing those policy solutions for implementation in Ohio and replication throughout the country. The Buckeye Institute is a nonpartisan, non-profit, tax-exempt organization as defined by I.R.C. section 501(c)(3). The Buckeye Institute's Legal Center engages in litigation, and files and joins amicus briefs that are consistent with its mission and goals.

The Buckeye Institute recognizes the significant legal complexity of engaging in productive activity and commerce in the United States, and supports principles that ensure that all who do so can comfortably, securely, and efficiently receive all necessary legal advice. This case raises important questions about the scope of the attorney-client privilege, an essential privilege in the modern world, in connection with the

[1] Pursuant to Supreme Court Rule 37.3(a), both Petitioner and Respondent have each consented to The Buckeye Institute filing this *amicus curiae* brief in support of Petitioner. Pursuant to Supreme Court Rule 37.6, *amicus curiae* states that no counsel for any party authored this brief in whole or in part, nor did any person or entity, other than *amicus*, its members, or its counsel make a monetary contribution to the preparation or submission of this brief.

provision of tax advice, an area of law of notorious uncertainty and difficulty. The Buckeye Institute supports the application of the attorney-client privilege in every area where legal advice is relevant, including with respect to tax law and tax returns.

SUMMARY OF ARGUMENT

The tax law of the United States is voluminous and complicated. The Internal Revenue Code itself is 6,871 pages long, the sum total of the Code and the Treasury regulations interpreting it is approximately 75,000 pages long, and on top of all of that there is a collection of IRS guidance, revenue rulings, revenue procedures, case law from courts, and similar publications that also form the body of the tax law.

Any person trying to engage in productive activity in the United States is faced with this complicated morass of authorities. Even minor reporting foot-faults can trigger massive penalties: late filing of an FBAR report of foreign bank and financial accounts, for instance, could result in the forfeiture of 50% of the entire balance of the account even if there was no failure to report and pay on the underlying income related to the account. Given the complexity of the tax law and the significance of even minor errors, the tax context is an area where open and honest communication between attorneys and clients is essential.

On the other hand, it is well recognized that there is no general accountant-client privilege. So, a natural question this presents is: what is the proper treatment of a communication that is arguably both a legal communication and made for purposes of tax return preparation? In the context of tax law, most legal advice—

perhaps almost all—is given to assist the taxpayer in determining what to put on one or more tax returns. As such, any approach to resolving the question of attorney-client privilege in this context must take into account that most tax advice is *both* legal *and* tax-return preparation advice, and it is usually impossible to break this down any further as a practical matter.

Given the impracticability of determining the "most" primary reason behind most types of advice that are both legal advice and tax-return preparation advice, the lower court's proposed test is simply unworkable, and an approach such as that taken by the D.C. Circuit in *Kellogg* is more appropriate. The only reason to reject the *Kellogg* approach would be if the tax context were not worthy of protection in the same way as other areas of law where there may be a dual purpose with respect to communication. But there is no reasonable justification for such an approach.

This Court should also reject the approach seemingly followed by the Seventh Circuit in *United States v. Frederick*. The *Frederick* approach would chill confidence in the attorney-client privilege. A key motive behind the Seventh Circuit's adoption of the rule in *Frederick* seemed to be a fear of inadvertently creating an accountant-client privilege through the simple expedient of hiring a lawyer to be a tax return preparer. In any dual-purpose scenario, however, it is possible that a communication would be covered by attorney-client privilege but would not have been covered if neither party were an attorney. The tax-return preparation context is no different and does not justify a different rule.

ARGUMENT

I. U.S. TAX LAW HAS BECOME MORE COMPLEX THAN EVER, NECESSITATING RELIABLE AND CONFIDENTIAL LEGAL ADVICE.

The tax law of the United States is voluminous, necessitating ordinary taxpayers to consult with tax attorneys in order to comply with filing and payment obligations. The starting point for a taxpayer seeking to comply with the tax law is the congressionally-enacted statutory framework located in Title 26 of the United States Code. According to Government figures, the Internal Revenue Code itself is 6,979 pages long.[2] When the Treasury regulations promulgated by the U.S. Department of the Treasury as the Government's official interpretation of the Internal Revenue Code are considered, the estimated figure jumps to a staggering 75,000 pages.[3] A taxpayer cannot stop there, however, as the previously-mentioned 75,000 pages does not paint the full picture, which requires a review of IRS guidance, revenue rulings, revenue procedures, notices, announcements, and case law.

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[2] Office of Law Revision Counsel, United States Code, Release Point 117-214, Title 26—Internal Revenue Code (Oct. 19, 2022), *available at* https://uscode.house.gov/download/releasepoints/us/pl/117/214/pdf_usc26@117-214.zip.

[3] "The U.S. tax code has grown so huge that nobody really knows how long it is. During the 2016 presidential campaign, candidates routinely cited a figure of seventy-three thousand pages—a number that seems to include about thirty-five hundred pages of the law itself, plus another seventy thousand pages of regulations." T.R. Reid, *A Fine Mess: A Global Quest for a Simpler, Fairer and More Efficient Tax System* 214 (2017).

The tax law is also inherently complicated, which results from multiple factors.[4] In the first instance, there is an attempt to achieve equity and fairness in the assignment of the tax burden among different types of taxpayers across an almost limitless field of increasingly complex transactions. The tax law has also become Congress's preferred tool to encourage certain activities deemed to be socially or economically beneficial. This is not to mention the political process itself, which spawns complexity as an unintentional byproduct of political compromises and logrolling. Further adding to the complexity is the fact that the tax law is not a static document, but rather consists of a patchwork of legislation, administrative rules and guidance that change on an annual basis, and judicial decisions.[5]

Any person or business trying to set up shop and engage in productive activity in the United States immediately faces this complicated morass of statutory

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[4] "Today, no matter what their income, Americans confront extraordinary complexity in filing their taxes. In 1940 the instructions to Form 1040 were about four pages long. Today the instruction booklet spans more than one hundred pages, and the form itself has more than ten schedules and twenty worksheets. The tax code contains more than seven hundred provisions affecting individuals and more than fifteen hundred provisions affecting businesses." Michael J. Graetz, *100 Million Unnecessary Returns: A Simple, Fair, and Competitive Tax Plan for the United States*, 14 (2008).

[5] On occasion, Congress has attempted to address the complexity of the Tax Law, including enacting subsection IX of subpart (ii) of § 7803(c)(2)(B) as part of the IRS Restructuring and Reform Act of 1998, known as the "anti-complexity clause." Ironically, this clause was "included in a massively complex piece of legislation that added some thirty thousand words and scores of complicated new deductions, exemptions, and credits to the bloated multivolume corpus of the nation's tax law." Reid, *supra* n.3, at 5.

language, regulations, rulings, and more. Although it is obvious that the tax law can impose substantial costs on any for-profit enterprise (and even non-profit enterprise), there are, on top of that, basic foot-faults that can impose unexpected costs on taxpayers. For instance, the recipient of a gift of substantial size from a foreign person can trigger a reporting obligation, even though, generally, the recipient of a gift does not have to pay income tax on the gift.[6] The failure to report the gift can impose a penalty of up to 5% *of the entire amount of the gift for each month of late filing* (up to a maximum of 25%)![7] That is an extraordinarily large penalty for a transaction that does not even generally create an underlying substantive tax liability. The recipient of the gift hopefully has a good legal advisor who will inform him or her of this trap for the unwary.

Another example (present in the current case) is the requirement that a U.S. person who has a financial interest in or signatory authority over a foreign bank or financial account file an FBAR (on the mandated FinCEN Report 114) if the aggregate value of the foreign financial account exceeds $10,000 at any time during such year.[8] The non-filing (or incomplete or incorrect filing) of an FBAR can result in the implementation of civil monetary penalties of $100,000 or *50% of the balance* in the account at the time of the

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[6] 26 U.S.C. § 102; Notice 97-34, 1997-1 C.B. 422.

[7] 26 U.S.C. § 6039F(c).

[8] 31 U.S.C. § 5314.

violation, whichever is *greater*.[9] Again, a minor filing error could result in enormous penalties, unrelated to any underlying substantive tax imposed. The individual subject to the FBAR filing requirement better have a legal advisor who can flag this obligation.

The importance of trustworthy legal advice in the tax context is not just a feature of the complexity of the tax law. The tax law is frequently unclear, uncertain, and prone to multiple reasonable interpretations. Judicial doctrines that focus on "economic substance" require one to weigh the significant economic consequences of a transaction versus the related tax benefits,[10] and the "substance over form" doctrine requires one to look at what a transaction "really" is to determine whether the tax benefits are consistent with the chosen form.[11] All of these questions require taxpayers to obtain reasoned legal judgments; taxpayers cannot merely rely on calculators and accountants to supply the answers.

Luckily for those who need legal advice to navigate the many rules applicable to those who live and are engaged in productive activities in the United States, the courts have long recognized the attorney-client privilege as one of the strongest privileges under law. This Court has explained that the "attorney-client privilege is the oldest of the privileges for confidential communications known to the common law"

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[9] 31 U.S.C. § 5321(a)(5)(C).

[10] *See, e.g., Gregory v. Helvering*, 293 U.S. 465 (1935).

[11] *See, e.g.*, *Frank Lyon Co. v. United States*, 435 U.S. 561, 573 (1978) (courts must look "to the objective realities of a transaction rather than to the particular form the parties employed").

and is designed to "encourage full and frank communication between attorneys and their clients and thereby promote broader public interests in the observance of law and administration of justice."[12]

There are few areas where open and honest communication between attorneys and clients is needed more than in the tax context. Taxpayers must disclose a substantial volume of private information to a tax attorney to enable the practitioner to render complete and accurate advice and to respond and negotiate fair resolutions to tax controversies. Without confidence that these disclosures will be confidential, taxpayers might be unwilling to have a full and frank discussion with their legal advisors, potentially resulting in costly errors, causing taxpayers not to properly report information on their tax return (which could disadvantage the IRS in many circumstances), and otherwise disrupting the tax reporting and collection process. As such, any rule that this Court sets out should be appropriately protective of legal communications between taxpayers and their legal advisors, or else taxpayers and businesses will be crippled in their ability to obtain effective tax advice and to comply with the tax laws.

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[12] *Upjohn v. United States*, 449 U.S. 383, 389 (1981).

II. LEGAL ADVICE AND TAX-RETURN PREPARATION ADVICE ARE FREQUENTLY INTERTWINED, WITH NO PRACTICAL WAY TO DISENTANGLE THEM.

While the attorney-client privilege is well-settled, it is also well established that there is no general accountant-client privilege.[13] Generally, courts have held that information provided to an accountant to be placed on a person's tax return is not protected against discovery by the tax authorities.[14] Amongst the rationales for the lack of such a privilege are that (1) it is important to the tax-enforcement regime that the IRS can investigate the background to a taxpayer's tax return (given the self-reporting nature of a taxpayer's tax liabilities), and (2) a tax return, which by its nature is submitted to a third party, namely the IRS or another taxing authority, is generally not expected to be confidential, and "the transmittal operates as a waiver of the privilege."[15]

A natural question is presented: what should be the rule if a communication, document, or other material is arguably *both* (1) a legal communication between a taxpayer and a legal advisor, and (2) information that may be used on, or to prepare, a tax return? Lower courts have used a few different tests with respect to such "dual-purpose" communications. One has seemingly held that dual-purpose attorney-

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[13] *United States v. Arthur Young & Co.*, 465 U.S. 805, 816–17 (1984).

[14] *United States v. Frederick*, 182 F.3d 496, 500–01 (7th Cir. 1999).

[15] *Id.* at 501.

client communications are not privileged if *any* purpose for the communication was non-legal.[16] Another has held that dual-purpose communications are privileged where *one* of the significant purposes is to obtain or provide legal advice.[17] The lower court here applied something it referred to as the "primary purpose test," under which a dual-purpose communication only is privileged where the legal purpose is *at least* as significant as any non-legal purpose.[18]

The common element among the above-mentioned tests is that they seek to identify the underlying purposes of attorney-client communications. The problem in the tax context, however, as with any test that disfavors the application of the attorney-client privilege, is that tax advice is very frequently *both* legal in nature *an*d geared toward the provision of information on a tax return. Frankly, the legal advice is more than just "geared" toward the provision of information—it is sought for and provided because what is reported on the return and the consequent potential tax liability is fundamentally the only thing the taxpayer cares about. The following examples are illustrative of the difficulty in bifurcating the legal and non-legal purposes with respect to tax communications.

Consider a small corporation attempting to calculate how much of its income can be offset by prior

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[16] *Id.* at 500–01.

[17] *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754, 760 (D.C. Cir. 2014).

[18] *In re Grand Jury*, 23 F.4th 1088 (9th Cir. 2022).

years' net operating losses (NOLs).[19] It dutifully examines the Internal Revenue Code and notices § 382. Section 382 directly affects the amount of NOLs that a corporation can claim on its U.S. federal income tax return, by limiting the amount of income that can be offset by such NOLs. This limitation, however, is triggered only when a "loss corporation" undergoes a statutorily defined "ownership change" during a three-year "testing period" that ends on the day of any ownership shift involving a five-percent shareholder. Once a taxpayer navigates the complicated analysis of determining whether § 382 applies, the taxpayer must then ascertain the annual § 382 limit on the "new loss corporation" from using "pre-change" losses against "post-change" income. Adjustments are needed to account for certain built-in gains and losses at the time of the statutorily defined ownership change (based on a combination of statutory language, regulations, an IRS notice, and some proposed regulations).

Faced with this giant collection of complicated provisions, the small corporation rushes to consult expert tax counsel (as it should). All of these complicated questions will be analyzed by tax counsel, with multiple exchanges of spreadsheets, analyses, historical data, and the like. But, at the end of the day, the main thing the corporation wants, and will get from its tax advisor, is *the amount of NOLs that can offset its income*—a number that will appear on its tax return.

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[19] Generally, if a corporation has net losses in a given year (in other words, losses exceeding its income), the corporation can carry the losses forward to offset net income earned in future years—this excess loss is referred to as a net operating loss, or NOL. 26 U.S.C. § 172. The usability of these NOLs is subject to a collection of complicated limitations, including the limitation discussed below.

The *only* reason the corporation is seeking tax advice from its tax lawyer is to get this number. Accordingly, are the communications with the tax lawyer "primarily" for the purpose of obtaining legal advice (given that interpretations of reams of legal authorities are needed)? Or "primarily" for preparing the corporation's tax return, because that's the ultimate calculation and determination that the corporation wants (and gets) from the tax advisor? The answer is inherently unclear.

Or, consider a small corporation, wholly owned by a single entrepreneur, that is undergoing a cash crunch. The entrepreneur lends the corporation some cash to help it out, with somewhat flexible terms—but with a clear requirement to pay interest, which the corporation dutifully pays as specified under the loan agreement. The corporation's chief financial officer wonders, when preparing the corporation's tax return, whether the corporation can deduct the interest. The officer, after investigation, learns that the deductibility of interest depends on whether the purported loan from the corporation's owner is "debt" or "equity" for tax purposes.

Debt-equity disputes constitute a major area of litigation in the federal court system, especially in the U.S. Tax Court. The legal analysis to determine the proper classification of an instrument as debt or equity is based on all of the relevant facts and circumstances. Courts have identified as many as sixteen specific factors to be considered when making a debt-

versus-equity determination, while the IRS has identified eight.[20] Further, the applicability and weight of each factor depends on the facts and circumstances of each case and requires more than merely tallying them up.[21] No one factor is determinative.[22] All of these very fact-specific inquiries are heavily dependent on weighing the factors, determining which authorities one considers most applicable to the facts, identifying criteria that seem less relevant, and even more considerations—all lacking clear right-or-wrong answers, with no determinations made by rote calculation, but rather requiring the exercise of often very subtle legal judgments.

The chief financial officer consults with a tax lawyer. The tax lawyer diligently analyzes the significant authorities and the facts, and provides a recommendation as to the tax classification of the purported loan. But again, the chief financial officer is not doing this out of mere curiosity as to the corporation's capitalization. Rather, the officer wants to know *what number to put down as interest deductions on the corporation's tax return*. Is the exchange of information and documentation between the tax attorney and the

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[20] *See United States v. Uneco, Inc.*, 532 F.2d 1204, 1208 (8th Cir. 1976) (identifying 10 factors); *Estate of Mixon v. United States*, 464 F.2d 394, 402 (5th Cir. 1972) (identifying 13 factors); *Fin Hay Realty Co. v. United States*, 398 F.2d. 694, 697 (3d Cir. 1968) (identifying 16 factors); *Dixie Dairies Corp. v. Commissioner*, 74 T.C. 476, 493 (1980) (identifying 13 factors); *see also* Notice 94-47, 1994-1 C.B. 357.

[21] *Bauer v. Commissioner*, 748 F.2d 1365, 1368 (9th Cir. 1984).

[22] *Tyler v. Tomlinson*, 414 F.2d 844, 848 (5th Cir. 1969).

corporation "primarily" for legal-advice purposes? Or "primarily" for tax-return purposes?

Even something as simple as whether a receipt of cash constitutes *income* in the first place is a question that can implicate important questions of tax law and engender significant uncertainty. Let's say a shareholder receives cash from a corporation. Income? Maybe. Was it a distribution? Then it may be income if there were enough "earnings and profits" in the corporation—an often tricky and uncertain tax calculation requiring a multitude of adjustments.[23] If the corporation did not have enough "earnings and profits," then perhaps the cash received by the shareholder is not income, and the distribution just reduces the shareholder's tax basis in the stock.[24] But did the shareholder redeem shares as part of the receipt of cash? Then perhaps the cash is a "redemption" for tax purposes, which causes the cash to be treated as (potentially) a capital gain or loss.[25] This inquiry turns on very nebulous questions such as whether the redemption is "essentially equivalent to a dividend."[26] Did the shareholder, rather than engaging in a redemption, instead sell the stock to a related corporation? Now one must analyze the notoriously difficult-to-understand § 304 of the Code.

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[23] *See* 26 U.S.C. §§ 301(a), (c)(1); 316(a).

[24] *See* 26 U.S.C. § 301(c)(2).

[25] *See* 26 U.S.C. § 302.

[26] *See* 26 U.S.C. § 302(b)(1).

There are many more examples that follow the above framework, and indeed, perhaps most tax advice is of a similar type. A taxpayer needs to know how to fill out its tax return, runs into a complicated or ambiguous legal question regarding the appropriate interpretation of the tax laws (the answer to which is essential for determining what the taxpayer will report on its tax return), asks a tax lawyer for the best interpretation or a range of acceptable interpretations, and follows the advice when completing the tax return. What's the primary purpose of the communications? Tax return preparation or legal advice? To put it simply, that is an unanswerable question: the advice is for *both*, and can't be subdivided as a practical matter any further.[27]

III. THERE IS NO JUSTIFICATION FOR TREATING TAX LEGAL ADVICE DIFFERENTLY FROM OTHER KINDS OF LEGAL ADVICE.

Given the impracticability of determining the sole "primary" reason behind most types of advice with aspects of both legal advice and tax-return preparation advice, the lower court's proposed test is

[27] "[T]rying to find *the* one primary purpose for a communication motivated by two sometimes overlapping purposes (one legal and one business, for example) can be an inherently impossible task. It is often not useful or even feasible to try to determine whether the purpose was A or B when the purpose was A and B. It is thus not correct for a court to presume that a communication can have only one primary purpose . . . . Rather, it is clearer, more precise, and more predictable to articulate the test as follows: Was obtaining or providing legal advice *a* primary purpose of the communication, meaning one of the significant purposes of the communication?" *In re Kellogg*, 756 F.3d at 759–60.

simply unworkable. The obvious alternative, then, is for the Court to adopt a practical and commonsense approach similar (or identical) to the test set forth by the D.C. Circuit in *In re Kellogg Brown & Root, Inc.*, 756 F.3d 754 (D.C. Cir. 2014). Under the D.C. Circuit's version of the primary purpose test, sometimes referred to as the "significant purpose" test, the court will determine whether a significant purpose of the communication was to obtain or provide legal advice. If a significant legal purpose is present, the entire communication is privileged. The significant-purpose test is not relative, meaning that the importance of other non-privileged purposes behind the communication will not destroy privilege so long as the privileged purpose itself is significant.

The only reason to reject the *Kellogg* approach would be to consider the tax context to be "special," not worthy of protection in the same way as other areas of law where there may be a dual purpose with respect to communication—the lower court in this case, indeed, hinted at that.[28] But there is no reasonable justification for such an approach. The Brief for Petitioner extensively and appropriately discusses this point and explains the utter lack of support for a special rule in the tax context.

One court of appeals adopted a rule that could be considered the opposite of the rule in *Kellogg*: in *United States v. Frederick*, the Seventh Circuit con-

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[28] *See* Pet. App. 11a (distinguishing *Kellogg* as applying to the context of "corporate internal investigations" rather than in the "tax context").

cluded that dual-purpose legal and tax-return preparation advice is inherently not privileged.[29] There is no reason for this Court to adopt the approach in *Frederick*.

First, the *Frederick* approach would chill confidence in the attorney-client privilege. At best it would produce rigidly stilted discussions between attorneys and clients in an attempt to avoid discussing non-legal (and thus non-privileged) issues that could taint the entire communication. Consider the examples discussed in this brief in Point II, *supra*: the extensive and complicated legal analyses needed to address debt-equity issues, § 382, or ostensibly simple distributions or redemptions on corporate shares, or numerous other cases, would potentially be entirely exempt from the privilege under this approach (and at the very least it would be quite unclear whether any particular communication would be privileged).

Second, a key motive behind the Seventh Circuit's adoption of the rule in *Frederick* seemed to be a fear of inadvertently creating an accountant-client privilege through the simple expedient of hiring an accountant or tax-return preparer who also happened to be a lawyer.[30] If the *Frederick* approach were to be applied very narrowly—perhaps exempting from any privilege (as being inherently non-legal) only "drafts of the returns (including schedules)" and "worksheets

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[29] 182 F.3d 496 (7th Cir. 1999).

[30] *Id.* at 500.

containing the financial data and computations required to fill in the returns," this perhaps would be a reasonable rule.[31]

Applying this rationale any further—for example, applying this rule to any communication with respect to the legal analysis underlying any calculation reported on a tax return or on work papers—makes little sense. In any dual-purpose scenario (even outside tax-return preparation), it is possible that a communication would be covered by attorney-client privilege but would not have been covered if neither party were an attorney. Just consider the internal investigations addressed in *Kellogg* and *Upjohn*— it was certainly possible (if foolish) for the corporations involved to conduct internal investigations without involving lawyers. A lawyer-less internal investigation would (obviously) not generate communications covered by attorney-client privilege. Would one say that the *Kellogg* and *Upjohn* rules accidentally create an "internal investigator-employee" privilege that shouldn't be circumvented by the mere use of lawyers in the internal investigation? That would be absurd.

Such an argument is just as absurd when applied to tax advice from tax attorneys. Yes, seeking advice from tax lawyers may result in some communications being privileged that would not be if the communications were made solely by an accountant.[32]

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[31] *Id.*

[32] Ever since the enactment of 26 U.S.C. § 7525, communications with an accountant in many circumstances might be privileged pursuant to the Internal Revenue Code to a similar extent as with an attorney. But the distinction will still be important. 26

That is also true in the internal-investigator context as well (and in any dual-purpose situations). Thus, the expansion of the privilege that was seemingly the main concern of the Seventh Circuit in *Frederick* is something that shouldn't be a concern at all, and in any event, that concern can be addressed through excluding from privilege the schedules showing the tax-return numbers.

CONCLUSION

For the foregoing reasons as well as the reasons set forth in the Brief for Petitioner, the judgment of the court of appeals should be reversed.

U.S.C. § 7525 contains, for instance, exceptions to the application of its privilege that would not apply to attorney-client communications. *See* 26 U.S.C. § 7525(a)(2) (privilege only assertable in noncriminal Internal Revenue Service or federal court proceedings); (b) (privilege not applicable with respect to participation in a "tax shelter").

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