

No. _____

In The
Supreme Court of the United States

LEONARD L. & BARBARA F. GRIGSBY,
Petitioners,

v.

UNITED STATES OF AMERICA,
Respondent.

*On Petition for Writ of Certiorari to the United States
Court of Appeals for the Fifth Circuit*

PETITION FOR WRIT OF CERTIORARI

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I. Question Presented

The questions underlying this petition are:

1. Whether, under a proper application of law, an administrative agency finding should be given the presumption of correctness when it is uncontested that the agency conducted no independent review prior to filing a lawsuit against a taxpayer, such that a Court applies such a presumption resulting in the Grigsbys being prohibited from presenting their evidence, which included both documents and testimony, to the triers of fact.
2. Whether the petitioners had the burden of proof on summary judgment motion despite the government being *both plaintiff and the movant*.
3. Whether the existence of a fixed fee contract to deliver a flood control structure, constituted a payment for research activities or an end product.

Cajun Industries, a highly skilled construction S corporation, of which the taxpayers are shareholders, and which handles large scale industrial projects, built four structures, two flood control systems in Louisiana, and structures for two refineries to which led to improved and increased refining capacity. The tax credits which flowed from Cajun Industries' work resulted in a tax refund for its shareholders, the Grigsbys. After the Grigsby's receipt of the tax refund, the Internal Revenue Services ("IRS"), without

conducting any audit of the tax year in question made a demand for the return of the full amount of the tax refund and referred the matter to the Justice Department. The Justice Department, without seeking any information or documents themselves from the taxpayers, filed suit just prior to the limitations period. Neither agency conducted any independent review of tax positions taken prior to filing a wholly unsupported complaint against the taxpayers. The Grigsbys subsequently requested a jury trial for the highly fact-intensive case. However, summary judgment was granted for the government just prior to jury trial on the basis that there was insufficient evidence of a process or product being developed and because the research activities for the four sample projects were found to fall under a “funding exclusion” to the tax credit. The Grigsbys were never able to put their documentary and witness testimony evidence in front of a trier of fact, nor was the evidence weighed to determine fact questions under the four-part test for the R&D tax credit.

II. Parties to the Proceeding

Petitioners, (Defendants—Appellants below) are Leonard L. Grigsby and Barbara F. Grigsby, two shareholders in Cajun Industries, L.L.C. & Subsidiaries – an S Corporation.

Respondent is the United States of America, represented by the U.S. Department of Justice.

III. Corporate Disclosure Statement

Leonard L. Grigsby and Barbara F. Grigsby, Petitioners, are individuals and shareholders in Cajun Industries, L.L.C. & Subsidiaries – an S Corporation. Additional shareholders in Cajun Industries, L.L.C. & Subsidiaries include Michael and Tami Moran, and Todd W. and Ainsley R. Grigsby.

IV. Statement of Related Proceedings

The following proceedings are directly related to this case within the meaning of Rule 14.1(b)(iii):

- *United States of America v. Leonard L. Grigsby and Barbara F. Grigsby*, No. 19-00596-BAJ-SDJ, U.S.M.D. Louisiana. Final Judgment signed October 31, 2022.
- *United States of America v. Leonard L. Grigsby and Barbara F. Grigsby*, No. 22-30764, U.S. Fifth Circuit Court of Appeals. Opinion issued November 13, 2023.

- *Michael Moran & Tami Moran et. al. v. Commissioner of Internal Revenue*, Consolidating Docket. Nos. 6740-20, 6741-20, 7567-21, 7568-21, 7571-21, 25993-21, 25994-21, pending in U.S. Tax Court.

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Petition for Writ of Certiorari

The United States' critical infrastructure is in decline. The majority opinion in the U.S. is favorable to improving U.S. infrastructure. As an example of the public clamor for better infrastructure, according to a recent NPR/Marist survey, 7 in 10 surveyed said they were optimistic the recent infrastructure bill would improve roads and bridges, and a majority was optimistic that the bill would create better-paying jobs. As noted on the White House website under "*Modernizing U.S. Infrastructure: the Bipartisan Infrastructure Law*":

Governments have long understood that investments in basic infrastructure support economic activity. Crumbling roads and delays on trains, planes, and public transportation make the transport of people and goods harder and longer. Slow broadband hurts businesses and workers alike who depend on the internet for work.

The need to improve U.S. infrastructure includes more than merely roads and bridges, but also includes flood prevention, storm damage mitigation, and increased refining capacity which all have a nationwide impact. However, the largest and most complex vital infrastructure projects are typically accompanied by substantial financial risk which outweighs the benefit for private companies. While the investment and risk are often incurred by private companies, the increase in 1) new and better

products, 2) more efficient and better internal methods, processes, and techniques; and 3) the creation of more higher paying skilled U.S. jobs, benefit the public generally.

Cajun Industries, of which the taxpayers are shareholders, built four structures, two flood control systems in Louisiana, which improved the diversion of storm flooding from vital facilities in-and-around the New Orleans area, and structures which improved oil and gas refining capacity. Pursuant to Section 41 of the U.S. Tax Code, Congress promised tax credits for such qualifying activities. The tax credits from Cajun Industries' research activity resulted in a tax refund. However, without conducting any audit or examination of the tax year in question, the IRS demanded the taxpayers pay back the tax refund received.

After the Grigsbys' receipt of a tax refund, the IRS referred the matter to the Justice Department just before the expiration of the limitations period and without performing any administrative review of the tax positions taken. The referral requested that the Department file suit seeking payment back of the tax refund. At the outset of the suit, the Justice Department was unable, or unwilling, to identify the specific basis or reasons for claiming Cajun Industries' activities did not qualify under Section 41 of the Tax Code. At the end of the discovery period, and just prior to the jury trial setting in the highly fact-intensive case, summary judgment was granted in the government's favor. The decision stated that

the taxpayers did not meet their burden of proof in showing they were developing a product or process or similar property. This was despite the government's own proposed statement of facts acknowledging that Cajun Industries built the structures and evidence by way of affidavit and deposition excerpts showing Cajun Industries participation in modification of the designs. The summary judgment order did not provide analysis of the multiple deposition excerpts, affidavits, or documentary evidence or even address the low threshold standard required to demonstrate evidence of a business component. Instead, decision was rendered without the documentary and testimonial evidence ever being presented to the trier of fact as to whether Cajun Industries met the four-part test for the R&D tax credit.

The Fifth Circuit Court of Appeals held that the burden of proof was on the taxpayer on motion for summary judgment despite the fact that the government filed suit, the government was the party moving for summary judgment in place of jury trial, and the government had the ultimate burden of proof at trial to show not only the tax refund was paid in error, but how much. The Fifth Circuit affirmed that the burden of proof by rationalizing that the demand letter sent to the taxpayers just prior to filing suit constituted a "finding" that should be presumed to be correct and thus shifts the burden of proof to the taxpayers. However, in its holding the Fifth Circuit relied upon cases where taxpayers had initiated suit challenging IRS findings and had the ultimate burden of proof and ignored the fact that there was no

examination that could provide a factual analysis leading to the cursory pre-suit demand letter.

Congress' prior attempts to incentivize companies through laws intended to create U.S. jobs in the technical fields and improve U.S. infrastructure have been thwarted by a short-sighted and cynical administration that often involves issuing findings with no evaluation of the evidence, and no analysis of documents, or witness accounts. No "presumption of correctness" should be attached to administrative "findings" when there is no analysis or review of documents.

Opinions Below

The United States Fifth Circuit Court of Appeals Opinion is reported at 86 F.4th 602 (5th Cir. 2023) and is reproduced at Appendix ("App.") 2a-35a. The District Court's Ruling and Order is reported at 635 F.Supp.3d 467 (M.D.La., Oct. 19, 2022) and is reproduced at App. 36a-82a.

Jurisdiction

The United States Fifth Circuit Court of Appeals issued its Opinion on November 13, 2023. A Petition for Panel Rehearing was denied on February 22, 2024. (App. 83a-118a). This Court has jurisdiction under 28 U.S.C. § 1254(1).

Statutory Provisions Involved

Relevant provisions of the U.S. Tax Code are reproduced at App. 119a-157a.

Statement of the Case

This is a case where a taxpayer has been denied tax credits and assessed a tax amount without ever having the documentary and testimonial evidence heard, either at the administrative level or by the trier of fact in court. For practitioners in tax litigation, some of the more often-heard phrases in court opinions are that tax deductions and credits are “matters of legislative grace”, that taxpayers have the burden of proof and are expected to “square round corners”. While the common expectation is that IRS chief counsel and the counsel for the Justice Department will be motivated to conserve judicial resources and be concerned with getting most efficiently to the right answer, most taxpayers are disappointed to find use of heavy-handed tactics, unreasonably onerous discovery requests, unnecessary contacts with third parties and clients intended to harass and embarrass taxpayers have become not only common, but accepted as the norm.

The review to determine tax owed in the court setting is *de novo*, meaning the IRS is not bound by its own analysis or the findings of its agents, conclusions of its technical experts, or even the appeals officers. There is a direct tension between the *de novo* doctrine, which is based on the assumption

that the basis for the administrative findings is not relevant if the tax is to be determined “*de novo*” in court and giving the administrative agency a presumption of correctness to its findings.¹ A *de novo* review should lead to an effort to arrive at the correct amount of tax, if any is owed. Instead, it has led to little accountability for IRS agents to review evidence and evaluate the facts correctly and in order to get to the correct amount owed. Moreover, starting the investigative process all over at the outset of litigation often leads to a great burden on the taxpayer as production and examination of the administrative agency becomes irrelevant and the government is not bound by the agency’s findings. The lengthy administrative process, which usually takes years to complete, followed by the outlook of starting all over in litigation through additional years of onerous discovery is the government’s friend. Very few taxpayers have the will or means to endure this process. The government has no budget, no great incentive to be efficient, and often little accountability to be cost-effective. Such environment is a fertile ground for abuse by IRS agents and IRS chief counsel who believe that forcing submission by whatever means necessary for victory is not only acceptable, but encouraged. The only bulwark against such abuse is fair review in the courts, where the documents and evidence may be heard by a trier-of-fact. The light at the end of the tunnel for taxpayers who have endured

¹ A fair discussion of the tension may be found in “*The De Novo Doctrine: Irrelevant to Relevancy in Civil Tax Litigation*”, Michael Kummer, Florida Tax Review, 14 FLTXR 115, 142-150.

the IRS examination process, followed by years in litigation, is having their day in court, where the judge or jury will hear all the evidence.

This is a case where that bulwark failed. If the decision in this case is left as-is, it will not be the only one. Despite the facts that 1) the IRS never requested documents, 2) never interviewed witnesses, 3) made a determination to refer the matter to the Justice Department to file suit not based on review of evidence, but because the limitations period was ending, 4) the witness testimony and documents were not used to evaluate application of the four-part test for the R&D tax credit, 5) the facts were never determined by the appropriate fact finder, and 6) summary judgment was granted asserting that the taxpayers had the burden of proof and the IRS “finding” was presumed to be correct. At no point was any of the evidence considered by a trier of fact to determine the facts necessary to apply the law correctly. For taxpayers who look to their day in court as a chance to have their evidence considered, the decision in this case that they will have the burden of proof even though they did not file suit, that the IRS will be presumed correct even when there was no administrative finding based on factual analysis and evidence, and the taxpayers’ evidence will not be presented to the trier of fact, in this case a jury, is alarming and disheartening.

A. Proceedings Below

Leonard L. Grigsby and Barbara F. Grigsby (hereinafter “Taxpayers”) are shareholders of an S Corporation (“Cajun Industries”).²

Taxpayers filed a joint tax income tax return for the 2013 tax year at issue.³

On October 3, 2016, the taxpayers filed a third amended 2013 federal tax return claiming a tax refund of \$576,756 which was a resulting flowthrough of research credits claimed on Cajun Industries’ amended federal tax return for tax year ending September 30, 2013.⁴

On March 27, 2017, the IRS sent a letter to Taxpayers initially stating that the amended return could not be processed because the IRS had no record of an amended schedule K-1 from Cajun Industries.⁵

On April 24, 2017, the Taxpayers sent the IRS an amended Schedule K-1 for the tax period ending September 30, 2013.⁶

² ROA. 18, ¶6.

³ ROA. 18, ¶8.

⁴ ROA. 19, ¶16.

⁵ ROA. 19, ¶17.

⁶ ROA. 19, ¶18.

On May 4, 2017, the IRS then sent a letter to Taxpayers denying their tax refund claim on the basis that the amended 2013 return was untimely.⁷

On May 19, 2017, within 15 days, Taxpayers provided proof that the amended 2013 return was timely filed, contrary to the IRS assertion in its denial.⁸

Subsequent to receipt of proof and confirmation of receipt of the Cajun Industries K-1, the IRS processed Taxpayers' amended 2013 return and allowed the \$576,756 refund claimed plus statutory interest.⁹

On September 15, 2017, the IRS issued to Taxpayers a refund in the amount of \$671,071.38, which reflected the amount of the refund claimed by the Taxpayers on their Third 2013 Return, plus statutory overpayment interest of \$73,663.38.¹⁰

Cajun Industries, L.L.C., was subsequently notified that Cajun Industries' tax years ending September 30, 2011, and September 30, 2014, would be examined. However, Taxpayers' 2013 tax year was referred to the Justice Department tax division who filed suit on September 11, 2019, in U.S. District Court for the Middle District of Louisiana solely addressing the 2013 tax year. No administrative

⁷ ROA. 19, ¶19.

⁸ ROA. 19, ¶20.

⁹ ROA. 20, ¶22-23.

¹⁰ ROA. 83, ¶23.

investigation was conducted, and no administrative finding was made with respect to Cajun Industries' tax year ending September 30, 2013, which involved the tax credits at issue that flowed through to the Taxpayers 2013 tax return.¹¹

The United States, as plaintiff, alleged that it had erroneously issued a tax refund in the amount of \$713,440.28 for the 2013 tax year.¹² The alleged error in tax refund arises from a dispute over the Taxpayers' entitlement to tax credits under Section 41 of the Internal Revenue Code, known as the Tax Credit for Increasing Research Activities ("the R&D Tax Credit").¹³

The factual basis asserted in the U.S.'s Original Complaint was a cursory and conclusory allegation that Cajun Industries did not comply with the statutory requirements, that its research did not constitute qualified research and that it did not have documentation of its activities and expenses.¹⁴

There is no allegation in the Original Petition that the claimed research was excluded under the "funding exclusion."¹⁵

On November 14, 2019, Taxpayers filed a motion pursuant to Federal Rule of Civil Procedure

¹¹ ROA. 120-21.

¹² ROA. 17.

¹³ ROA. 17-21.

¹⁴ ROA. 20-21, ¶24-27.

¹⁵ ROA. 17-22.

12(b)(6) for dismissal for failure to state a claim and in the alternative for a more definitive statement pursuant to 12(e).¹⁶

In support of the Taxpayers' motion, they showed that the U.S. never conducted an examination of Cajun Industries' relevant tax year and could not provide sufficient facts in support of its vague factual allegations in its Complaint and that there was no finding in exam of any failure to follow statutory or regulatory guidance, or any review of documentary support which were alleged not to exist, or to have been provided.¹⁷

Additionally, in Taxpayers' motion, they asserted that the Complaint was time barred as pleaded.¹⁸

On December 5, 2019, while Taxpayers' 12(b) Motion to Dismiss and alternative request for more detail was pending, the U.S. amended its Complaint changing the date cited for the issued refund.¹⁹

On December 9, 2019, also while Taxpayers' 12(b) Motion was pending, the U.S. served discovery asking for Taxpayers' contentions as to the tax credit and supporting documentation for all employees for all projects during the relevant time period.²⁰

¹⁶ ROA. 45.

¹⁷ ROA. 45-63; 116-152.

¹⁸ ROA. 53.

¹⁹ ROA. 80, ¶23

²⁰ ROA. 164, ¶2; 166-190.

On January 10, 2020, Taxpayers' filed a motion for stay as to the discovery requests until the issues to be discovered and a reasonable scope of discovery determined.²¹

Taxpayers issued interrogatories asking for legal contentions as to the basis for asserting the tax credit should be disallowed.²² Despite the U.S. being the party that initiated the lawsuit, the District Court issued order stating that U.S. did not have to answer Taxpayers' interrogatories providing the basis for asserting Cajun Industries did not qualify for the tax credit until end of discovery period.²³

Given the fact intensive and onerous nature of discovery in such a suit, the parties requested a bifurcation of qualification issues versus quantification of the R&D tax credits.²⁴ Per agreement, discovery would proceed on the qualification aspect on four projects first to determine if qualified research occurred and would proceed to discovery and second trial on quantification depending on rulings on qualification.²⁵

The District Court granted the motion for bifurcation.²⁶

²¹ ROA. 164-190.

²² ROA. 531.

²³ ROA. 925-926.

²⁴ ROA. 938; 949-953.

²⁵ ROA. 949-953.

²⁶ ROA. 956.

On June 23, 2022, close to end of first discovery period, the District Court called a status conference and asked the U.S. if it had agreed that the case should be a jury trial.²⁷ U.S. counsel was unsure of its position at that time, but wanted time to decide whether a jury was appropriate.²⁸

The District Court directed the parties file briefs addressing whether Defendants are entitled to a jury trial.²⁹ The District Court also indicated that it wanted both trials of the bifurcated matter to occur, the first part in November and the second part in January.³⁰ No indication was given as to whether discovery would still be allowed for the bifurcated quantification of the tax credits issue.³¹

The District Court set the anticipated ten-day jury trial to begin November 14, 2022, the week before the Thanksgiving holiday, and to continue the week after the Thanksgiving holiday.³²

On August 15, 2022, the U.S. filed a motion for summary judgment alleging that none of the four projects at issue had a business component, was technological in nature, had any activities constituting a process of experimentation, or had any

²⁷ Doc. 60, *Minute Entry*; ROA. 979-985.

²⁸ *Id.*

²⁹ *Id.*

³⁰ ROA. 2146.

³¹ *Id.*

³² *Id.*

uncertainty.³³ The U.S. further argued that whether or not the four projects at issue involved research, they were all excluded because Cajun Industries was paid to conduct research and so the research activities fell under an exclusion which provides that if the party claiming research was paid to conduct research, as opposed to merely provide an end product, the research is funded and tax credit may not be claimed.³⁴ The U.S. also argued that Cajun Industries did not retain any substantial rights to the results of any research for three of the projects, and did not bear risk contingent on the success of the research for the fourth project.³⁵

On October 19, 2022, the District Court issued an order granting summary judgment in favor of the U.S.³⁶

The U.S. District Court for the Middle District of Louisiana found the following:

- That there was no evidence of a business component;³⁷
- That contracts for three of the projects, referred to as Methanex, Chevron, and Claiborne did not

³³ ROA. 987-2134.

³⁴ *Id.*

³⁵ *Id.*

³⁶ ROA. 3465.

³⁷ *Id.*

reserve substantial rights, making the research activities excluded under Section 41(d)(4)(H);³⁸

- That the contract for the East Bank project bore no risk for Cajun Industries contingent upon its research, making the research activities excluded under Section 41(d)(4)(H).³⁹

On October 31, 2022, Final Judgment was signed.⁴⁰

On November 30, 2022, Taxpayers timely filed a Notice of Appeal.⁴¹

On November 13, 2023, the United States Fifth Circuit Court of Appeals affirmed the Summary Judgment order of the U.S. District Court for the Middle District of Louisiana.

Reasons Relied on for Allowance of Writ

Every citizen who pays income tax has an interest in being assured that their tax assessment is based on the facts and evidence. In fact, the Taxpayer bill of Rights found on the IRS website expressly includes the following rights:

The right to pay no more than the correct amount of tax. Taxpayers have the right to pay only

³⁸ *Id.*

³⁹ *Id.*

⁴⁰ ROA. 3507.

⁴¹ ROA. 3510.

the amount of tax legally due, including interest and penalties, and to have the IRS apply all tax payments properly.

The right the challenge the IRS's position and be heard. Taxpayers have the right to raise objections and provide additional documentation in response to formal IRS actions or proposed actions, to expect that the IRS will consider their timely objections and documentation promptly and fairly.

The right to appeal to an independent forum. Taxpayers are entitled to a fair and impartial administrative appeal and have the right to take their cases to court.

The right to a fair and just tax system. Taxpayers have the right to expect the tax system to consider facts and circumstances that might affect their underlying liabilities.

When the IRS conducts an examination of a taxpayer, it typically will request from the taxpayer, and sometimes third parties, financial documents, receipts, and contemporaneous documents that would substantiate a taxpayer's claims to the deductions and tax credits claimed on a tax return. The IRS often will additionally conduct interviews of witnesses with personal knowledge of the reasons and basis for claiming the tax deduction or credit. If, after examination, the IRS determines that the taxpayer is deficient in tax paid, a notice of deficiency will issue identifying the amount the IRS believes the taxpayer

owes and the reasoned basis for its determination. If the taxpayer disagrees with the IRS determination, the procedure that the taxpayer is afforded is that the IRS determination may be challenged and reviewed by a court of law which will examine the facts and evidence, often in more detail. The IRS notice of deficiency is the taxpayer's "ticket" to the U.S. Tax Court. If the taxpayer is seeking a tax refund that has been denied and not paid by the IRS, the taxpayer for jurisdictional reasons must file suit in U.S. District Court or the Federal Court of Claims which have jurisdiction over tax refund claims. If, however, the taxpayer has already been issued a tax refund by the IRS, the government may initiate suit for an alleged erroneous refund. However, at least three separate U.S. Circuit Courts opinions have found that should the government file suit for alleged erroneous refund asserting the tax refund was paid in error, the government has the ultimate burden of proof to show what the error was and how much is owed. *See Soltermann v. U.S.*, 272 F.2d 387, 387 (9th Cir. 1959); see also *U.S. v. McFerrin*, 570 F.3d 672, 675 (5th Cir. 2009); see also *United States v. Commercial Nat'l Bank of Peoria*, 874 F.2d 1165, 1169 (7th Cir. 1989) ("In an action to recover an erroneous refund ..., the government bears the burden of proof.").

It seems to us to follow inescapably that the United States, as plaintiff in this case, bears the ultimate burden of proof to show not only that some amount has been erroneously refunded but also how much that amount is, for otherwise the

court is without guidance in entering an appropriate judgment.

Soltermann v. U.S., 272 F.2d 387, 387 (9th Cir. 1959).

The decision in this case should be reason for alarm as the evidence was never reviewed by the trier of fact and not only was the burden of proof shifted to the taxpayer improperly, but the administrative agency was presumed to be correct in disallowing tax credits despite never having examined the tax year in question.

I. The IRS demand letter should not be endowed with any “presumption of correctness” when there was no examination of the tax year, documents, or witnesses and no factual findings.

In finding that there was “no evidence” of Cajun Industries developing a new or improved product or process, the U.S. District Court did not address that the legal standard is a “low threshold” test where all that need be shown is some minimal improvement to a product, process, formula, invention, technique, or similar property. The District Court further ignored that both parties agreed that Cajun Industries had built two new flood control systems, the new foundation for a massive refinery, and the expansion and improvement of another refinery, which fact, by itself meets the business component test. There was also deposition and affidavit and documentary evidence in the record that

Cajun Industries participated in the modification of the designs of each of the structures. Only a fact question need be shown to have the question decided by the jury. Despite the unambiguous evidence in the record the District Court took the matter out of the hands of the jury a couple of months before trial asserting taxpayers did not meet their burden of proof, a burden which was not theirs, but nonetheless was clearly met.

In affirming the District Court's summary judgment, the Fifth Circuit Court reasoned the shift of the burden of proof to taxpayers on a basis not briefed by the government, asserting that the demand letter sent before filing suit constituted a "finding" by an administrative agency which should be given a presumption of correctness. The Fifth Circuit relied primarily upon this Court's opinion in *U.S. v. Janis*, 428 U.S. 433, 441 (1976) and its own prior opinion in *Portillo v. Comm'r*, 932 F.2d 1128, 1133 (5th Cir. 1991) to assert that the IRS' "assessment of tax liability may be presumed correct". However, the cases cited do not lead to the conclusion that such presumption is to be applied here for the following reasons: 1) the Court's premise that a determination of deficiency issued by the commissioner operates to put the ultimate burden of proof on the taxpayer is not applicable here because the Fifth Circuit case relied upon was a deficiency case where the taxpayer initiates suit challenging an administrative finding, not an erroneous refund case filed by the government without a prior examination, a meaningful difference; and 2) the document asserted to constitute a finding was a "naked

assessment”⁴² with no evidence in the record providing its basis; and 3) the Court’s premise that there was a finding by the Commissioner that tax is owed should be presumed correct without any “muscles, tendons, or ligaments of fact”. This case is not consistent with the analysis and reasoning of the authorities the Fifth Circuit Court opinion cited and therefore is in conflict with those same authorities.

The Fifth Circuit Court opinion in this case is not consistent with this Court’s opinion in *Janis*. In *U.S. v. Janis*, this Court noted that even despite a situation when burden of proof is being placed upon the taxpayer under a presumption of correctness, that when the assessment has no foundation, it is a naked assessment that is not entitled to a presumption of correctness. 428 U.S. 433, 441 (1976). An assessment that is utterly without foundation is proof that it was arbitrary. *Id.* at 442. There was no factual finding here which was entitled to a presumption of correctness. It is telling that the U.S. did not argue that there was a “finding” by the Commissioner that should be given a presumption of correctness. Presumptions of correctness do not stand when there is no “rational foundation” and there are no “ligaments of fact”.

⁴² An assessment is “naked” and “beyond saving” when “the records supporting an assessment are excluded from evidence, ... or are nonexistent, ..., so that the basis upon which an assessment is calculated is beyond the knowledge of the court.” *United States v. Schroeder*, 900 F.2d 1144, 1149 (7th Cir. 1990).

The rule placing the burden of proof on the taxpayer is a creature of common law, not a statute. *Thompson v. U.S.*, 523 F.Supp.2d 1291, 1296 (N.D.Ala. 2007). Congress weighed in on the burden of proof issue after the *Janis* and *Portillo* decisions. Section 7491 enacted by Congress in 1998 which states that even in a tax refund case filed by the taxpayer, the taxpayer can shift the ultimate burden of proof to the government merely by meeting the burden of production. “*Before the enactment of §7491 in 1998, the burden of proof in a tax refund suit was generally on the taxpayer.*” *Thompson v. U.S.*, 523 F.Supp.2d at 1294. But in 1998 Congress explicitly undertook to provide taxpayers with statutory relief from the long-standing common law burden of proof rule. *Id.* at 1295 (citing to H.R. REP. NO. 105-599, at 238 (1998) (Conf. Rep.). Section 7491 provides that a taxpayer can shift the burden of proof to the United States, by meeting the burden of production, even in a tax refund suit which is filed by the taxpayer. *Id.* at 1295.

Portillo v. Commissioner, which is the case primarily relied upon, presented a notable difference from the facts of this case. In *Portillo*, the taxpayer was challenging a notice of deficiency in U.S. Tax Court. The case did not involve the U.S. filing suit for an alleged erroneous refund. Additionally, in *Portillo*, the IRS had conducted an audit of the year at issue, the agent had sought taxpayer documents which would substantiate the taxpayer’s claims, no documents were provided after request, and the IRS agent tried to reconstruct an amount owed with the

evidence he had. There are so such facts in the record showing investigation or administrative analysis of this kind here.

The Fifth Circuit opinion states that the Grigsbys have the burden to show by preponderance of evidence the U.S. was incorrect, but even if true, preponderance of the evidence standard is the standard at trial before a jury, not the standard for summary judgment which removes the factual issues from the jury. As noted even in *Portillo*, the government's need for tax collection does not serve to excuse the government from providing some factual foundation for its assessments.⁴³ The presumption of correctness, even when applicable, has an Achilles' heel when there are "no muscles, tendons, no ligaments of fact."⁴⁴ *Portillo* found that despite an examination of the agent, requests for documents, lack of documents supplied by the taxpayer, and a notice of deficiency based on such, -- none of which occurred in this case -- that the Notice of Deficiency in that case was a "naked" assessment without any "ligaments of fact."⁴⁵

The Fifth Circuit's opinion conflicts with its own prior decision as well as decisions from the 9th and Seventh Circuit Courts of Appeal which have held in erroneous refund suits, the government has the

⁴³ *Portillo v. Comm'r*, 932 F.2d 1128, 1133 (5th Cir. 1991) (citing to *Carson v. U.S.*, 560 F.2d 693, 696 (5th Cir. 1977)).

⁴⁴ *Id.*

⁴⁵ *Id.* at 1133.

ultimate burden of proof.⁴⁶ In *U.S. v. McFerrin*, this Court had already acknowledged that in an erroneous refund suit, the Gov't has the ultimate burden of proof.⁴⁷ This Court was not alone in finding the U.S. has the ultimate burden of proof in an erroneous refund case as it cited to both the U.S. Ninth Circuit Court of Appeals opinion in *Soltermann v. U.S.*, 272 F.2d 387, 387 (9th Cir. 1959) as well as the Seventh Circuit Court of Appeals opinion in *U.S. v. Commercial Nat'l Bank of Peoria*, 874 F.2d 1165, 1169 (7th Cir. 1989). The summary judgment standard is also clear that the moving party and party that has the ultimate burden of proof, has the burden of proof on motion.⁴⁸ This is especially true in a case where a jury has been requested.

II. It is important for all U.S. taxpayers that they know judicial review means their evidence and case will be fully and fairly heard.

The District Court's decision stating that there was no evidence of a business component did not examine what was required to show a business component. The District Court ignored the proposed statements of facts of the parties acknowledging

⁴⁶ *Soltermann v. U.S.*, 272 F.2d 387, 387 (9th Cir. 1959); see also *United States v. Commercial Nat'l Bank of Peoria*, 874 F.2d 1165, 1169 (7th Cir. 1989); see also *U.S. v. McFerrin*, 570 F.3d 672, 675 (5th Cir. 2009);

⁴⁷ *U.S. v. McFerrin*, 570 F.3d at 675 (5th Cir. 2009).

⁴⁸ *Celotex Corp. v. Catrett*, 106 S.Ct. 2548, 2553, 477 U.S. 317, 323 (1986).

Cajun Industries built four new and improved structures, or the affidavits, deposition testimony, and document provided showing Cajun Industries not only built the structures but contributed to the modification of the designs. All that is required to meet the business component test is evidence showing a minimal improvement of function in a new, or improved, product, process, formula, invention, software, or technique being developed by the taxpayer. The statement of facts of both the U.S. and Grigsbys demonstrated that four structures were built and developed by Cajun Industries, one refinery expansion, one site foundation for a new refinery being relocated from Chile, one box culvert for flood control, and one retention wall for a sewage treatment plant. A review of the U.S.'s own statement of facts and evidence shows it was uncontroverted that Cajun Industries built the structures. There were disputes as to Cajun Industries' contribution as to the design, but Cajun Industries introduced deposition testimony, affidavits, contracts and even pictures sufficient to create a fact question as to Cajun Industries' contribution to the modification of the original design as to all four structures. The argument as to whether the business component should be characterized as a product or process "or similar property" is a moot point and a distraction. The uncontroverted evidence relied upon, and interrogatory responses detail the same activities. No new evidence was introduced.

In any event, both classifications (whether it be a *process* or a *product*) would constitute a business

component. Whether a process, product, or similar property, they all constitute business components under Treasury Regulation § 1.174-2(a)(3) which defines a qualifying product as “*any* pilot model, **process**, formula, invention, technique, patent **or similar property**.” The language is extremely broad reflecting congressional intent to be inclusive. Congress did not care whether a business component is characterized as a “product” or “process” or other “similar property”. The Fifth Circuit Court of Appeals decision to interpret the treasury regulation in a way that disallows that tax credit is inconsistent with congressional intent that the business component element be interpreted broadly to be inclusive, not as a basis to exclude companies from the incentive.

The government’s own proposed statement of facts acknowledged Cajun Industries built the structures at issue, which did not previously exist. Although not necessary to meet the business component test, there was also evidence in the summary judgment record creating a fact question for the jury as to contribution to the modifications as to the designs for each. Requiring taxpayers pick which characterization of their business components best fit does not address situations where the lines are difficult to draw, or something may fit in more than one category. The business component definitions themselves acknowledge there are no bright lines, or mutual exclusivity, between potential components. For example, the definition of “product”, one type of business component in the Treasury Regulations

includes within the definition a “process”. The definition of product also includes other business components such as formulas, inventions, techniques, or similar property. Whether characterized as process, or product, or other similar property, the evidence showing Cajun Industries’ activities in the participation and development of processes in the development of four new and improved structures substantiates a new or improved component. The contracts in the record describe activities and processes Cajun Industries used to build the structures. The evidence in the record at the least, allows the evidence to be presented to the jury. Such evidence should not be discounted and ignored. The opinion is alarming for the tens of thousands of taxpayers who claim the R&D tax credit.

III. The Court opinion on the funding exclusion as to the East Bank contract conflicts with the Federal Circuit and miscites an 11th Circuit Court of Appeals opinion regarding fixed fee contracts.

To date, taxpayers have relied upon payment terms as a basis for analyzing whether a company is being paid to conduct research activities, or being merely paid to produce a deliverable. To date, the test taxpayers have relied upon per Treasury Regulations is whether the payment is for the taxpayer to conduct research activities, or whether payment is for an end-product. If payment is for an end product as opposed to research activities, the funding exclusion does not

apply. *Fairchild Industries, Incorporated v. U.S.*, 71 F.3d 868 has been the seminal case for funding analysis when the contract does not expressly state whether payment is to conduct research activities, such as a grant for cancer research, or merely for an end-product that meets the customer's specifications and functional needs. In such cases, taxpayers have relied upon the *Fairchild* analysis which examines the payment terms, (i.e. fixed fee versus cost plus contracts). The Federal Circuit found that in such cases when the payment is for an end product to certain specifications and there is a fixed-fee payment structure, it is inherently risky and does not fall under the "funding exclusion".

The Fifth Circuit Court opinion not only conflicts with the *Fairchild* Federal Circuit Court holding, and Treasury Regulation 1. but also removes the only remaining class of contract payment terms to avoid the funding exclusion. In essence, potentially eviscerating the tax credit for taxpayers that operate under contracts to provide end-products. Further, in coming to the conclusion that the East Bank contract was funded because it failed the risk prong, the Court based its conclusion on flawed premises. One of the premises is that the 11th Circuit Court of Appeals opinion in *Geosyntec Consultants, Inc. v. U.S.*, 776 F.3d 1330 (11th Cir. 2015) previously found a fixed fee contract was funded. It did not. In fact, the opinion clearly states the none of the contracts examined involved fixed fee contracts. The fixed fee contracts were not part of the appeal to the 11th Circuit. Second,

the Court's premise that all-inclusive clause limiting payment to the stated fixed fee is flawed. Such language, as explained in the underlying *Geosyntec* District Court decision, actually had led to the opposite conclusion by the District Court which neither party contested.

The Fifth Circuit Court opinion erred in asserting that *Geosyntec* found a fixed fee contract to be funded. The Court first states that the *Fairchild* and *Geosyntec* cases do not stand for the proposition that all fixed price contracts are *per se* not funded. The Court then asserts that *Geosyntec* previously found fixed fee contracts to be funded citing to the portion of the 11th Circuit Court of Appeals finding that the Cherry Island contract and the WM Contract were funded. While it is true the Cherry Island and WM Contracts were found to be funded, the Cherry Island and WM Contracts were cost-plus contracts subject to an agreed maximum amount and ***were not fixed fee contracts.***⁴⁹ As stated in the 11th Circuit opinion:

Three of the contracts were fixed-price contracts, under which Geosyntec was paid a fixed total price for its work. The other three contracts were cost-plus contracts subject to a maximum, also known as “capped contract,” under which Geosyntec was paid for

⁴⁹ *Geosyntec Consultants, Inc. v. U.S.*, 776 F.3d 1330 (11th Cir. 2015).

*its labor and expenses, plus a mark-up, subject to an agreed maximum price.*⁵⁰

As to the three fixed-price contracts, the district court agreed with Geosyntec and found that those contracts were not funded. Therefore, Geosyntec remained eligible for the research tax credit for qualifying research expenses it incurred under the fixed-price contracts.⁵¹

The only two contracts before the 11th Circuit Court of Appeals were the two cost-plus subject to a maximum payment as noted in opinion:

*Geosyntec contends that the district court erred in finding that the three capped contracts were funded . . . While three capped contracts were before the district court, Geosyntec appeals . . . only two: (1) a contract with the Delaware Solid Waste Authority (DSWA) to expand the capacity of the Cherry Island Landfill in Wilmington, Delaware (the Cherry Island Contract); and (2) a contract with Waste Management, Inc. (WM) to evaluate technology for remediating groundwater beneath a warehouse in Niagara, New York (the WM Contract).*⁵²

⁵⁰ *Id.* at 1332.

⁵¹ *Id.* at 1333.

⁵² *Id.*

The Grigsbys did not argue that the *Fairchild* and *Geosyntec* cases meant that fixed fee contracts are “*per se*” not funded. They argued that both the *Fairchild* and *Geosyntec* cases found fixed fee contracts to be “inherently risky” and not funded. The fact that the contracts were fixed fee must necessarily mean something in the funding risk analysis and cannot be ignored, or otherwise there is no point in including the payment structure in the funding analysis as prior Courts have typically done.

The fact that fixed fee payment structures in this context have been found to be inherently risk should lead to a conclusion, barring any other modifying language, that there is risk to the taxpayer regarding success of the research. As argued by the Grigsbys, the East Bank contract contained risk to Cajun Industries not only because they were fixed fee contracts, but also because the East Bank contract included clauses that allowed Cajun Industries’ work to be inspected and rejected for failure to meet requirements, and stated that Cajun Industries would be tasked with remedying such failure at its own expense. Cajun Industries bore the risk of such rejection and additional costs for failure to meet requirements. Such clauses, in addition to being a fixed fee contract made the work contingent upon its success and therefore risky under a proper funding analysis.

The Fifth Circuit Court of Appeals also wrongly concluded that because the contract contained

language essentially stating that the fixed fee price was all-inclusive, meaning it included all employee wages, expenses, and costs incurred by Cajun Industries, that Cajun Industries was being paid for its research. The language was clearly providing a clear cap to what Cajun Industries could ever be paid to provide the flood control structure. This case, if the conclusion is left unclarified or corrected, has vast potential ramifications on the funding analysis for the tens of thousands of taxpayers claiming the R&D tax credit. A contract that intends to limit or cap any further financial obligation of the payor in a fixed fee contract, such as the language in the East Bank contract actually creates more risk for the payee who is unsuccessful in research activities or that can't figure out how to deliver an end-product efficiently. Such clauses are included precisely to ensure that there will be no further charges. The Court's logical conclusion that Cajun Industries was paid for research because of language included to prevent additional charges is not consistent with the prior funding risk analysis.

Finally, the Fifth Circuit Court of Appeal opinion's premise that the taxpayers conflated the guidance that stated that payment for an end-product or result with contracts for payments and services is flawed. The Fifth Circuits holding that such argument is a conflation conflicts with the 11th Circuit Court of Appeals Geosyntec opinion it cites. As cited to in Geosyntec:

*If an expense is paid or incurred pursuant to an agreement under which payment is contingent on the success of the research, then the expense is considered paid for the product **or result rather than the performance of the research**,” and the tax credit is meant to incentivize research not production.⁵³*

Note the distinction is not just between payment for product versus services, but payment for **result rather than** for “**performance of the research**.” What Congress was distinguishing was between a grant type of arrangement where a party is being paid for performance, or to put people in seats to conduct research activities without an end specification requirement (i.e. level of effort type contracts paying for hourly work to put qualified people in seats to conduct cancer research) versus paying for the end-result regardless of whether research is performed. The Court’s conclusion is logically flawed when it acknowledges that payment was not to conduct research, and then uses that to conclude payment therefore could not be contingent upon the success of the research, leading to further conclusion that the research that was uncontroversially not even contemplated in the agreement must be funded. It is a circular argument that is directly opposite to the language of the treasury regulation and congressional distinction

⁵³ *Geosyntec Consultants, Inc. v. U.S.*, 776 F.3d at 1335 (citing to Treas. Reg. 1.41-2 and H.R. Rep. No. 100-1104, vol. 2, at 78) (*emphasis added*).

above. In short, research is funded because it was not contemplated in the agreement. Such analysis would lead to the inevitable conclusion that any contract that does not mention research is funded. Given the business component requirement of the R&D encourages and requires the business component be “held for sale or lease”, this cannot be the proper analysis or the intent of Congress.

IV. This is an ideal case for the Court to address and clarify the conflict between burden of proof and a presumption of correctness, as well as provide clarification of the proper funding exclusion analysis for the R&D tax credit.

The importance of this case is not limited to the Grigsbys or Cajun Industries. This case affects all taxpayers. This case further affects all taxpayers wishing to claim the R&D tax credit. Additionally, many IRS recent arguments have a greater impact on small to mid-sized businesses. These businesses, many of whom are eligible for the research credit, may not have the formal administrative structure to meet the stringent and onerous documentary requests that Congress and the Treasury Department tried to address and avoid. Congress recognized if the documentary requirements become too onerous that there is no incentive. The Treasury Department, in keeping with Congressional intent, eliminated a specific documentation requirement for the R&D Tax Credit in Treasury Decision 9104, stating:

In formulating the proposed regulations and in response to industry criticism and a Congressional directive, the Treasury and the IRS decided against a specific research credit documentation requirement.

The preamble also states taxpayers must be provided with reasonable flexibility in how they substantiate research credits and observes Congress made clear through legislative history that the credit should not impose unreasonable recordkeeping burdens. Congressional intent refusing to impose burdensome recordkeeping on taxpayers is confirmed by the Conference Report to the Tax Relief Extension Act of 1999 in which conferees expressed their concerns and reaffirmed that eligibility for the credit should not turn on such requirements. Not only did the taxpayers in this case produce voluminous documentation, including financial records, contemporaneous projects documents, contracts, design drawings, construction documents and pictures, affidavits, deposition testimony they attached contracts, affidavits, deposition testimony, emails and project documentation only to have a summary judgment order saying they didn't meet their burden of proof they built the four structures and the IRS conclusory demand letter should be presumed correct despite the record showing no administrative review of the tax year.

Not only does the decision in this case affect the tens of thousands of taxpayers who have relied upon

Congressional promises for the R&D tax credit, and not only does the decision potentially chill such incentives provided by Congress, but it also impacts all taxpayers, who now should have the legitimate concern that presumption of correctness for “findings” given to the IRS can be based upon no foundation of fact, no review of the actual facts, no review of the relevant documents, and no review of relevant witnesses with personal knowledge. Moreover, it is alarming when considering that 1) an administrative so-called “finding” would be given a presumption of correctness when it is uncontested that the naked decision was not based on any analysis of the facts; but also 2) given such “finding” would wrest the decision away from the appropriate decision maker so that the documents, testimony, and evidence are never fairly presented. Surveys have shown Courts have been more than willing in recent years to find reasons to avoid decision-making about what the law is by more often finding ambiguity and deferring to such administrative agencies.⁵⁴ That the agency would be invested with more power by providing a presumption of correctness for a demand letter that was based upon no factual review such that the evidence is never presented and the actual facts never fairly reviewed is great cause for concern.

⁵⁴ Kent Barnett & Christopher J. Walker, *Chevron in the Circuit Courts*, 116 Mich. L. Rev. 1, 33-34 (2017) (sampling over 1,000 cases and concluding that courts of appeals find ambiguity at Chevron step one 70% of the time).

The question of whether Courts should defer even more power to administrative agencies is already before the Court in the *Loper Bright Enterprises, et. al. v. Gina Raimondo*, Cause No. 22-451. Many of the same concerns of over-deference to administrative agencies as exemplified by the courts' too willing to give a presumption of correctness of administrative finding even when there is no evidence of any administrative review. As recognized in the Fifth Circuit Court of Appeals prior opinion *Portillo v. Comm'r*, 932 F.2d 1128, 1133 (5th Cir. 1991), "*The tax collector's presumption of correctness has a herculean muscularity of Goliath-like reach, but we strike an Achilles' heel when we find no muscles, no tendons, no ligaments of fact.*"

Extending a presumption of correctness to a "finding" that has *no muscles, no tendons, and no ligaments of fact*, invests the IRS with power beyond reasonable restraint. The presumption of correctness is at direct odds with the *de novo* doctrine which is based upon the assumption that once the in the court, the trier of fact will determine the facts and the court will apply the law accordingly without deference to the administrative finding. The facts in the instant matter are an example of the need to revisit and clarify the deference given to administrative agencies when the government agency-initiated suit, is the movant on summary judgment, and there is no evidence of any fair review of the evidence during the administrative process before suit was initiated. Petitioners request this case be taken up and

considered along with the matter, *Loper Bright Enterprises, et. al. v. Gina Raimondo*, Cause No. 22-451, currently before the Court.

Conclusion

For the foregoing reasons, this Court should grant the Petition for Writ of Certiorari.

Respectfully submitted,

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