No.

IN THE

Supreme Court of the United States

CECILIA M. HYLTON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTION(S) PRESENTED

1. Is petitioner denied due process of law when the court of appeals failed to timely advise her whether oral argument (which each party requested) would be held on her appeal, as required by Fed. R. App. P. 34(b), and then without affording her the opportunity to argue orally issued its *per curiam*, one-paragraph decision affirming the Tax Court?

2. May the court of appeals in an unpublished one-paragraph *per curiam* opinion reject forty years of developed jurisprudence concerning the taxation of horse-related activities under 26 U.S.C. § 183, by parroting the trial judge's clearly wrong conclusions characterizing petitioner's activity as a "hobby," a decision which affirms a disputed income tax deficiency of over $3.6 million plus interest for up to fourteen years together with an accuracy-related penalty of almost $600,000 which incurs its own interest for twelve years?

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The unpublished Findings of Fact and Opinion of the United States Tax Court in *Cecilia M. Hylton v. Commissioner of Internal Revenue*, T. C. Memo. 2016-234, Docket Nos. 8887-13 & 4955-14, decided December 22, 2016, and reported at 2016 WL 7414585 (Tax Ct. 2016), concluding that petitioner's horse activity was "not engaged in for profit" within the meaning of 26 U.S.C. § 183, for each of the taxable years 2004 through 2011, is set forth in the Appendix hereto (App. 3-35).

The unpublished order of the United States Court of Appeals for the Fourth Circuit in *Cecilia M. Hylton v. Commissioner of Internal Revenue,* Docket No. 17-1777, filed on August 3, 2018, denying petitioner's timely filed petition for panel rehearing and for rehearing *en banc*, is set forth in the Appendix hereto (App. 36).

The unpublished Letter of petitioner's attorney to the Clerk of the Fourth Circuit, dated September 6, 2018, attaching the request of petitioner for oral argument, contained at page 63 of her Main Brief; the request of respondent for oral argument, contained at page 75 of its Reply Brief; and the Rule 34 Notice to the parties from the Deputy Clerk of the Court of Appeals, dated March 29, 2018, is set forth in the Appendix hereto (App. 37-44).

JURISDICTION

The *per curiam* decision of the United States Court of Appeals for the Fourth Circuit affirming the Memorandum Findings of Fact and Opinion of the United States Tax Court was entered on May 7, 2018; and its further order denying petitioner's timely filed petition for panel rehearing and for rehearing *en banc* was decided and filed on August 3, 2018 (App. 1-2; 36).

On October 26, 2018, Chief Justice Roberts granted petitioner's application for extension of time to file a petition for a writ of certiorari, extending such time to and including December 1, 2018 (Application No. 18A446). This petition for writ of certiorari is filed within the time as extended by Chief Justice Roberts.

The jurisdiction of this Court is invoked pursuant to the provisions of 28 U.S.C. § 1254(1).

RELEVANT PROVISIONS INVOLVED

United States Constitution, Amendment V:

> No person shall...be deprived of life, liberty, or property, without due process of law....

26 U.S.C. § 162:

(a) *In general*. There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including—

(1) a reasonable allowance for salaries or other compensation for personal services actually rendered;
(2) traveling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances) while away from home in the pursuit of a trade or business; and
(3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity....

26 U.S.C. § 183:

Activities not engaged in for profit

(a) *General rule*. In the case of an activity engaged in by an individual or an S corporation, if such activity is not engaged in for profit, no deduction attributable to such activity shall be allowed under this chapter except as provided in this section.

(b) *Deductions allowable.* In the case of an activity not engaged in for profit to which subsection (a) applies, there shall be allowed—

(1) the deductions which would be allowable under this chapter for the taxable year without regard to whether or not such activity is engaged in for profit, and

(2) a deduction equal to the amount of the deductions which would be allowable under this chapter for the taxable year only if such activity were engaged in for profit, but only to the extent that the gross income derived from such activity for the taxable year exceeds the deductions allowable by reason of paragraph (1).

(c) *Activity not engaged in for profit defined.* For purposes of this section, the term "activity not engaged in for profit" means any activity other than one with respect to which deductions are allowable for the taxable year under section 162 or under paragraph (1) or (2) of section 212.

(d) *Presumption.* If the gross income derived from an activity for 3 or more of the taxable years in the period of 5 consecutive taxable years which ends with the taxable year exceeds the deductions attributable to such activity (determined without regard to whether or not such activity is engaged in for profit), then, unless the Secretary establishes to the contrary, such activity shall be presumed for purposes of this chapter for such taxable year to be an activity engaged in for profit. In the case of an activity which consists in major part of the breeding, training, showing, or racing of horses, the preceding sentence shall be applied by substituting "2" for "3" and "7" for "5".

(e) *Special rule*.
(1) In general. A determination as to whether the presumption provided by subsection (d) applies with respect to any activity shall, if the taxpayer so elects, not be made before the close of the fourth taxable year (sixth taxable year, in the case of an activity described in the last sentence of such subsection) following the taxable year in which the taxpayer first engages in the activity.
(2) Initial period. If the taxpayer makes an election under paragraph (1), the presumption provided by subsection (d) shall apply to each taxable year in the 5-taxable year (or 7-taxable year) period beginning with the taxable year in which the taxpayer first engages in the activity, if the gross income derived from the activity for 3 (or 2 if applicable) or more of the taxable years in such period exceeds the deductions attributable to the activity (determined without regard to whether or not the activity is engaged in for profit).
(3) Election. An election under paragraph (1) shall be made at such time and manner, and subject to such terms and conditions, as the Secretary may prescribe.
(4) Time for assessing deficiency attributable to activity.If a taxpayer makes an election under paragraph (1) with respect to an activity, the statutory period for the assessment of any deficiency attributable to such activity shall not expire before the expiration of 2 years after the date prescribed by law (determined without extensions) for filing the return of tax under chapter 1 for the last taxable year in the period

of 5 taxable years (or 7 taxable years) to which the election relates. Such deficiency may be assessed notwithstanding the provisions of any law or rule of law which would otherwise prevent such an assessment.

26 U.S.C. § 6651(a)(1):

Failure to file tax return or to pay tax

(a) *Addition to the tax.* In case of failure—
(1) to file any return required under authority of subchapter A of chapter 61 (other than part III thereof), ...on the date prescribed therefor (determined with regard to any extension of time for filing), unless it is shown that such failure is due to reasonable cause and not due to willful neglect, there shall be added to the amount required to be shown as tax on such return 5 percent of the amount of such tax if the failure is for not more than 1 month, with an additional 5 percent for each additional month or fraction thereof during which such failure continues, not exceeding 25 percent in the aggregate....

26 U.S.C. § 6662(a):

Imposition of accuracy-related penalty on underpayments (a) Imposition of penalty If this section applies to any portion of an underpayment of tax required to be shown on a return, there shall be added to the tax an amount equal to 20 percent of the portion of the underpayment to which this section applies.

26 CFR § 1.183-2:

Activity not engaged in for profit defined.

(a) *In general.* For purposes of section 183 and the regulations thereunder, the term activity not engaged in for profit means any activity other than one with respect to which deductions are allowable for the taxable year under section 162 or under paragraph (1) or (2) of section 212. Deductions are allowable under section 162 for expenses of carrying on activities which constitute a trade or business of the taxpayer and under section 212 for expenses incurred in connection with activities engaged in for the production or collection of income or for the management, conservation, or maintenance of property held for the production of income. Except as provided in section 183 and § 1.183-1, no deductions are allowable for expenses incurred in connection with activities which are not engaged in for profit. Thus, for example, deductions are not allowable under section 162 or 212 for activities which are carried on primarily as a sport, hobby, or for recreation. The determination whether an activity is engaged in for profit is to be made by reference to objective standards, taking into account all of the facts and circumstances of each case. Although a reasonable expectation of profit is not required, the facts and circumstances must indicate that the taxpayer entered into the activity, or continued the activity, with the objective of making a profit. In determining whether such an objective exists, it may be sufficient that there is a small chance of making a large profit. Thus it may be found that an investor in a wildcat oil well who incurs very substantial expenditures is in the venture for profit even though the expectation of a profit might be considered unreasonable. In determining whether an activity is engaged in for profit, greater weight is given to objective facts than to the taxpayer's mere statement of his intent.

(b) *Relevant factors*. In determining whether an activity is engaged in for profit, all facts and circumstances with respect to the activity are to be taken into account. No one factor is determinative in making this determination. In addition, it is not intended that only the factors described in this paragraph are to be taken into account in making the determination, or that a determination is to be made on the basis that the number of factors (whether or not listed in this paragraph) indicating a lack of profit objective exceeds the number of factors indicating a profit objective, or vice versa. Among the factors which should normally be taken into account are the following:

(1) Manner in which the taxpayer carries on the activity. The fact that the taxpayer carries on the activity in a businesslike manner and maintains complete and accurate books and records may indicate that the activity is engaged in for profit. Similarly, where an activity is carried on in a manner substantially similar to other activities of the same nature which are profitable, a profit motive may be indicated. A

change of operating methods, adoption of new techniques or abandonment of unprofitable methods in a manner consistent with an intent to improve profitability may also indicate a profit motive.

(2) The expertise of the taxpayer or his advisors. Preparation for the activity by extensive study of its accepted business, economic, and scientific practices, or consultation with those who are expert therein, may indicate that the taxpayer has a profit motive where the taxpayer carries on the activity in accordance with such practices. Where a taxpayer has such preparation or procures such expert advice, but does not carry on the activity in accordance with such practices, a lack of intent to derive profit may be indicated unless it appears that the taxpayer is attempting to develop new or superior techniques which may result in profits from the activity.

(3) The time and effort expended by the taxpayer in carrying on the activity. The fact that the taxpayer devotes much of his personal time and effort to carrying on an activity, particularly if the activity does not have substantial personal or recreational aspects, may indicate an intention to derive a profit. A taxpayer's withdrawal from another occupation to devote most of his energies to the activity may also be evidence that the activity is engaged in for profit. The fact that the taxpayer devotes a limited amount of time to an activity does not necessarily indicate a lack of profit motive where

the taxpayer employs competent and qualified persons to carry on such activity.

(4) Expectation that assets used in activity may appreciate in value. The term profit encompasses appreciation in the value of assets, such as land, used in the activity. Thus, the taxpayer may intend to derive a profit from the operation of the activity, and may also intend that, even if no profit from current operations is derived, an overall profit will result when appreciation in the value of land used in the activity is realized since income from the activity together with the appreciation of land will exceed expenses of operation. See, however, paragraph (d) of § 1.183-1 for definition of an activity in this connection.

(5) The success of the taxpayer in carrying on other similar or dissimilar activities. The fact that the taxpayer has engaged in similar activities in the past and converted them from unprofitable to profitable enterprises may indicate that he is engaged in the present activity for profit, even though the activity is presently unprofitable.

(6) The taxpayer's history of income or losses with respect to the activity. A series of losses during the initial or start-up stage of an activity may not necessarily be an indication that the activity is not engaged in for profit. However, where losses continue to be sustained beyond the period which customarily is necessary to bring the operation to profitable status such

continued losses, if not explainable, as due to customary business risks or reverses, may be indicative that the activity is not being engaged in for profit. If losses are sustained because of unforeseen or fortuitous circumstances which are beyond the control of the taxpayer, such as drought, disease, fire, theft, weather damages, other involuntary conversions, or depressed market conditions, such losses would not be an indication that the activity is not engaged in for profit. A series of years in which net income was realized would of course be strong evidence that the activity is engaged in for profit.

(7) The amount of occasional profits, if any, which are earned. The amount of profits in relation to the amount of losses incurred, and in relation to the amount of the taxpayer's investment and the value of the assets used in the activity, may provide useful criteria in determining the taxpayer's intent. An occasional small profit from an activity generating large losses, or from an activity in which the taxpayer has made a large investment, would not generally be determinative that the activity is engaged in for profit. However, substantial profit, though only occasional, would generally be indicative that an activity is engaged in for profit, where the investment or losses are comparatively small. Moreover, an opportunity to earn a substantial ultimate profit in a highly speculative venture is ordinarily sufficient to indicate that the activity is engaged in for profit even though losses or only occasional small profits are actually generated.

(8) The financial status of the taxpayer. The fact that the taxpayer does not have substantial income or capital from sources other than the activity may indicate that an activity is engaged in for profit. Substantial income from sources other than the activity (particularly if the losses from the activity generate substantial tax benefits) may indicate that the activity is not engaged in for profit especially if there are personal or recreational elements involved.

(9) Elements of personal pleasure or recreation. The presence of personal motives in carrying on of an activity may indicate that the activity is not engaged in for profit, especially where there are recreational or personal elements involved. On the other hand, a profit motivation may be indicated where an activity lacks any appeal other than profit. It is not, however, necessary that an activity be engaged in with the exclusive intention of deriving a profit or with the intention of maximizing profits. For example, the availability of other investments which would yield a higher return, or which would be more likely to be profitable, is not evidence that an activity is not engaged in for profit. An activity will not be treated as not engaged in for profit merely because the taxpayer has purposes or motivations other than solely to make a profit. Also, the fact that the taxpayer derives personal pleasure from engaging in the activity is not sufficient to cause the activity to be classified as not engaged in for profit if the activity is in fact engaged in for profit as evidenced by other factors whether or not listed in this paragraph.

....

Fed. R. App. P. 34 (a) & (b):

Oral Argument

(a) In General.

(1) Party's Statement. Any party may file, or a court may require by local rule, a statement explaining why oral argument should, or need not, be permitted.

(2) Standards. Oral argument must be allowed in every case unless a panel of three judges who have examined the briefs and record unanimously agrees that oral argument is unnecessary for any of the following reasons:

(A) the appeal is frivolous;

(B) the dispositive issue or issues have been authoritatively decided; or

(C) the facts and legal arguments are adequately presented in the briefs and record, and the decisional process would not be significantly aided by oral argument.

(b) Notice of Argument; Postponement. The clerk must advise all parties whether oral argument will be scheduled, and, if so, the date, time, and place for it, and the time allowed for each side. A motion to postpone the argument or to allow longer argument must be filed reasonably in advance of the hearing date.

Fourth Circuit Local Rule 34(a):

Oral Argument; Pre-argument Review and Summary Disposition of Appeals; Statement Regarding the Need for Oral Argument.

In the interest of docket control and to expedite the final disposition of pending cases, the chief judge may designate a panel or panels to review any pending case at any time before argument for disposition under this rule. In reviewing pending cases before argument, the panel will utilize the minimum standards set forth in FRAP 34(a)(2). If all of the judges of the panel to which a pending appeal has been referred conclude that oral argument is not to be allowed, they may make any appropriate disposition without oral argument including, but not limited to, affirmance or reversal. Because any case may be decided without oral argument, all major arguments should be fully developed in the briefs. In furtherance of the disposition of pending cases under this rule, parties may include in their briefs at the conclusion of the argument a statement setting forth the reasons why, in their opinion, oral argument should be heard.

STATEMENT

Petitioner Cecilia M. Hylton ("petitioner" or "Hylton") was raised in Virginia and until 1998, she worked full-time in her family's successful real estate business ("the Hylton Group") which developed, managed and sold both commercial and residential properties in the Commonwealth. By the time she left the business, petitioner had worked her way through the company from purchasing agent to construction supervisor and then to president of this family enterprise.

As early as 1990, in part to cope with the death of her father in 1989, petitioner began her first involvement with American quarter horses, a breed of horse which competes at shows in various disciplines including "western pleasure" and "ranch pleasure." This involvement by petitioner was a part- time endeavor and she pursued it for her personal pleasure. But by 1998, with about eight years of experience in owning quarter horses, including knowledge of the basic economics of doing so, she started a sole proprietorship called "Hylton Quarter Horses" ("HQH"), which was dedicated to the breeding, training , showing and selling of American quarter horses.

With profit as her primary goal, petitioner dramatically limited her participation in the family real estate business from full-time to about ten (10) hours each week while working about 40 hours weekly on her HQH activity. Her work for HQH involved manual labor, e.g., feeding, mucking stalls, spreading shavings etc., as well as collaborating daily with HQH's trainer. Each year, HQH quarter horses competed in about 10 horse shows nationwide, a time commitment of about 6-7 days for each show, including travel time; and petitioner worked 8-10 hours daily for HQH for each of these shows.

From the outset of HQH's startup, the business plan sought to acquire potential stallions that could become successful and earn credentials through HQH's management. After HQH's chief stallion"Flashy Zipper" died unexpectedly in 2000, HQH's third year of operation, petitioner acquired two more stallion prospects. She purchased "Slip Slydun Away" in 2000, managing and developing him into the 2008 American Quarter Horse Association's ("AQHA") World Champion Senior Reining horse. In 2005, petitioner bought "Invitation to Flash" and guided him to become the 2008 AQHA World Champion Performance Halter Stallion. Continuing her success and having preserved "Flashy Zipper's" semen through cutting edge technology at Colorado State University, HQH, using that preserved semen, was able to produce "Doya Think Im Flashy," a stallion prospect who became the 2015 Reserve World Champion in the Snaffle Bit Association Ranch Pleasure discipline and the AQHA 2015 High Point Junior Ranch Pleasure Horse.

Petitioner's HQH's horse enterprise made use of four Virginia farm properties, all owned beneficially by petitioner, to house and train HQH's horses. In 2004, HQH hired Steve Meadows ("Meadows"), AQHA's Professional Horsemen's Council Chairman and National Director, as its full-time, exclusive trainer. He used one of petitioner's four horse farm properties as his family's residence; and he continued his duties as its trainer during all of the eight years at issue here. Meadows trained and showed multiple World Champions and in 2013, he won the American Ranch Horse Association World Championship in Senior Ranch Riding. From the outset, petitioner ran HQH's enterprise expecting each of these farm properties to appreciate in value which they did. She also expected that her horses would appreciate in value which they did.

In 2006, petitioner after collaborating with Meadows began moving her breeding horses to three professional breeding farms in Whitesboro, Texas, the so-called "quarter horse capital of the world," because of its concentration of breeders, trainers and potential buyers. As Meadows later stated, petitioner "wanted her horses where they'd be seen and where the top trainers would come to buy [her] horses." In 2005, HQH owned 109 horses, 106 of which were in Virginia. By 2014, of the 47 horses owned by HQH, 36 were located in Texas with only 9 in Virginia.

Once some of her horses were removed to Texas, she traveled to Texas for only about a week annually, often with Meadows. There they evaluated foals, deciding which ones had good talent, eye appeal and conformation, culling from HQH's herd those that lacked these traits. According to Meadows, petitioner "had an incredible sense of the [breeding] crosses" and a "very good eye for the horses." Petitioner insured her higher-valued horses against the risks of mortality and injury; and she carried liability and property damage insurance on all four properties in Virginia.

In starting up HQH, petitioner relied on Kenneth Anderson ("Anderson"), CPA, of Anderson Stone & Co., Ltd. P.C., who had specialized knowledge of accounting in the horse industry. He not only advised her on the startup but also represented her as an accountant for 23 years from 1991 until his death in 2013, including all of the eight years at issue in this litigation. Petitioner's adult children, George Markley

("George") and Jamie Hylton ("Jamie") served as HQH's Business Manager and Farm Manager, respectively. Jamie kept all HQH's income records, registered its horses with the AQHA, made travel arrangements for horse shows and kept all breeding papers. George kept all invoices by expense categories recommended by Anderson; and at year end, George provided Anderson with all these invoices and income records. Anderson would then produce highly detailed annual profit & loss statements for the business, each up to 21 pages in length. Anderson also prepared petitioner's tax returns for all of the eight years at issue .

HQH held monthly business meetings attended by petitioner, George, Jamie and sometimes Meadows. They reduced expenses and increased revenue by analyzing categorized invoices to make cost-cutting decisions such as reducing hay and feed costs, reducing their participation at minor horse show competitions and by, for example, terminating a participant in HQH's breeding program because of its overcharging and its failure to properly handle HQH's horses.

The market for quarter horses proved strong from 1998 through 2005. By the end of 2005, HQH had built up its herd to 109 horses. However, beginning in 2006-2007, an oversupply of young horses in the market caused prices to decline which brought reductions in breeding stock prices. This caused a drastic shrinkage in the breeding industry----over one-half of the annual foal registrations in the industry were eventually lost. The onset of the Great Recession in 2008 exacerbated these losses and prolonged these poor conditions for the industry. In 2006, AQHA's number of foal registrations was 165,114;by 2015, it projected only 72,000 registrations.

In response to this depressed market, petitioner began to steadily reduce HQH's herd from 109 horses in 2006 down to 54 by the end of 2011.Yet during this depressed market, she made significant transactions, selling "Radical Yet Fancy" for $150,000 in 2010 and "UF Certainly a Priss" for $175,000 in 2013. She also collected $150,000 of insurance proceeds in 2013 following the death of "Impulse to Sparkle."

Like any successful ongoing business, HQH had separate office space, used a professional logo, maintained a website, had a comprehensive advertising program, and showed its horses at the AQHA World Championship and other shows, all regularly attended by major quarter horse buyers. HQH used professional business cards, business stationery and had a separate mailing address. HQH maintained two separate bank accounts and petitioner reviewed all invoices before payment. She had a business plan for HQH and modified it to increase HQH's chances for profits. One innovation included establishing in 2005 the "Hylton Maiden Class," a competition open to only horses aged three years or older that had never competed, an incentive for horse owners not to enter their horses in competitions before the age of three.

In most respects, HQH operated in the same way as other profit-motivated quarter horse businesses, frequently having *higher* quality horses than most of its competitors, an attribute which gave HQH a "realistic potential" of producing a major stallion. Petitioner's innovative "Hylton Maiden Class" was well received, generated industry goodwill, led to additional customers, and established HQH as a major quarter horse industry participant which cared about horse welfare. HQH therefore had taken the time and made the substantial investment to generate goodwill in the horse business, separating itself from most of its competitors.

In 2006, petitioner purchased for HQH two motor coaches for a total price of $1,800,000 which she and other HQH personnel used for transportation, lodging and office space on the grounds when competing at horse shows; and being on site in a well appointed motor coach provided a good atmosphere for selling expensive horses with petitioner often closing major sales in her motor coach. She never owned an airplane or even chartered one to go to a show and she never used a limousine or town car at a show. Instead she continued to use these motor coaches nine years after their purchase. Nor were any of her four Virginia farms "showplaces" or recreational facilities offering entertainment.

For all the years at issue (2004 through 2011), petitioner engaged Anderson, her accountant of long standing, to prepare and file with the respondent Internal Revenue Service ("respondent" or "Service") her income tax returns on Form 1040 for her sole proprietorship. Each year, petitioner provided him with all necessary documentation to prepare accurately the complex profit and loss statements together with her income tax returns. She believed the taxes were accurate because Anderson duly reported all HQH operating income and expenses on Form 4797 when required and on Schedule F ("Profit or Loss from Farming") of her Form 1040 for each year at issue.

Respondent reviewed HQH's books and records, confirmed their accuracy, and made no substantive adjustments to petitioner's reported income or expenses. Instead, it disallowed only petitioner's losses under the authority of 26 U.S.C. § 183 ("IRC § 183"), because it deemed her HQH enterprise, one which breeds, trains, shows and sells quarter horses for profit, as an activity "not engaged in for profit."

On January 24, 2013, respondent issued a Notice of Deficiency to petitioner for the six tax years from 2004 through 2009; and on February 7, 2014, it issued another Notice of Deficiency for the tax years 2010 and 2011. Petitioner timely filed a petition in the United States Tax Court which challenged each one of those proposed deficiencies and each accuracy-related penalty. The two cases were consolidated for hearing and in December of 2015, a three-day trial was held in the United States Tax Court in Washington, D.C. before Ruwe, J. (App. 3-4).

On December 22, 2016, the trial judge issued his Memorandum Findings of Fact and Opinion (App. 3-35). After reciting most of the facts adverted to herein, Judge Ruwe addressed the propriety of petitioner using her HQH losses as reported on Schedule F of her Form 1040 to offset her non-HQH income for the taxable years 2004-2011 (App. 13-17). As he observed, under 26 U.S.C. § 183(a), if an activity is "not engaged in for profit," no deduction attributable to that activity is allowed except to the extent allowed by § 183(b) and by 26 U.S.C. §§ 162 & 212(App. 17-18).

Moreover, there is a presumption under § 183(d) that the breeding, training, showing, or racing of horses is an activity engaged in for profit if it produces gross income in excess of the deductions for any two of seven consecutive years unless respondent establishes to the contrary (App. 18). Here, however, petitioner's ownership and operation of HQH did not produce income in excess of its deductions in any time during its operation (*Id.*). Accordingly, no presumption applies and whether a profit motive exists is determined from all the facts and circumstances of each case, applying the nine non-exhaustive factors identified in Income Tax Regs., 26 CFR § 1.183-2(b) for doing so (App. 18-20).

Employing this approach, the trial court determined that petitioner carried on her business only partly in a businesslike manner; that there was no evidence that she sought or received financial advice from experts about the business end of this activity; that while she spent much of her time operating HQH, her activities also entailed significant personal and recreational aspects; that there was no credible evidence that she expected specific appreciation of either her properties or her quarter horses; that it was impossible to parse out her contribution to the success of the Hylton Group, her successful family business of which she was president before beginning this venture; that her history of successive losses sustained by HQH over the years pointed to a lack of profit motive; that she received substantial tax benefits from these losses; and that the primary reason for her HQH activities was more consistent with a "costly hobby" than with a profit motive (App. 20-27).

Having found that petitioner's HQH activities for the subject years were "not engaged in for profit," the trial judge then determined that she had not provided evidence sufficient to find that her failure to file tax returns timely for the years 2004, 2005 and 2007 was due to reasonable cause and accordingly assessed her additions to tax under 26 U.S.C. § 6651(a)(1) (App. 27-29). Finally, because petitioner's understatement of income tax for the years 2006 through 2011 was "substantial," i.e., it exceeded the greater of 10% of the tax required to be shown on the return or $5,000, and because she had not shown reasonable cause for these understatements, the trial court imposed accuracy-related penalties under 26 U.S.C. § 6662(a) (App. 29-32).

Petitioner appealed this ruling to the court of appeals. Incident thereto, both parties requested oral argument in their respective Briefs consistent with Fed. R. App. P. 34(a) (App. 42-43). On March 29, 2018, the Clerk of the court of appeals notified the parties that the appeal had been referred to a panel of the court but contrary to his/her duty under Rule 34(b) that he/she "must advise all parties whether oral argument will be scheduled, and, if so, the date, time, and place for it, and the time allowed for each side," failed to advise the parties that oral argument would *not* be scheduled and that this appeal by petitioner would be decided on the Briefs only (App. 44).

On May 7, 2018, the court of appeals in a one-paragraph *per curiam* opinion affirmed the Tax Court "for the reasons stated by the tax court" (App. 1-2). It also wrote that "[w]e dispense with oral argument because the facts and legal contentions are adequately presented in the materials before this court and argument would not aid the decisional process" (App. 2).

On August 3, 2018, the court of appeals denied petitioner's timely filed petition for panel rehearing and for rehearing *en banc* (App. 36).

On October 26, 2018, Chief Justice Roberts granted petitioner's application for extension of time to file this petition for a writ of certiorari, extending such time to and including December 1, 2018 (Application No. 18A446).

REASONS FOR GRANTING THE PETITION

1. Petitioner Was Denied Due Process When the Court Of Appeals And Its Administrative Staff Failed To Timely Advise Her Whether Oral Argument (Which Both Parties Had Requested) Would Be Afforded, As Required By Fed. R. App. P. 34(b).

Fed. R. App. P. 34(a) & (b) provide in pertinent part:

> (a) oral argument *must be allowed* in every case unless a panel of three judges who have examined the briefs and record unanimously agrees that oral argument is unnecessary for any of The following reasons:
> (A) the appeal is frivolous;
> (B) the dispositive issue or issues have been authoritatively decided; or
> (C) the facts and legal arguments are adequately presented in the briefs and record, and the

> decisional process would not be significantly aided by oral argument.
>
> (b) Notice of Argument; Postponement. The *clerk must advise all parties whether oral argument will be scheduled*, and, if so, the date, time, and place for it, and the time allowed for each side....

(emphasis supplied).

Consistent therewith, both parties requested oral argument in their respective Briefs consistent with Fed. R. App. P. 34(a) (App. 42-43). On March 29, 2018, the Clerk of the court of appeals issued a so-called "Rule 34 Notice" which notified the parties that the appeal had been referred to a panel of the court "so that they may review the case before scheduling oral argument" and that "[i]f the panel to whom this appeal has been submitted unanimously agrees that oral argument is unnecessary, the panel will issue its decision without further notice to counsel that oral argument will not be scheduled" (App. 44).

However, contrary to her duty under Rule 34(b) that she "must advise all parties whether oral argument will be scheduled, and, if so, the date, time, and place for it, and the time allowed for each side," the Clerk failed to advise the parties that oral argument would *not* be scheduled and that this appeal by petitioner would be decided only on the Briefs absent any oral argument.

Regardless of the Panel's eventual decision not to allow oral argument for any of the three reasons recited in Rule 34 (a), this failure by the Clerk to hew to her duty under Rule 34(b) to give timely notice of the Panel's decision not to allow oral argument to the parties in time to do them some good, i.e., *before the Panel rendered its final decision*, denied petitioner the opportunity to convince the Panel by motion or otherwise that oral argument was necessary. This failure, in turn, denied petitioner fair notice and a fair hearing; it violated the plain terms of Rule 34(b); and it denied her the right of meaningful access to the courts.

Rule 34(a)(2) clearly considers oral argument to be a vital part of the appeals process, i.e., it *must* be afforded the parties unless the Panel examines the Briefs (all 147 pages plus their Addenda) together with the record and unless its denial of oral argument is unanimous. In addition, Rule 34(b) provides that the Clerk *must* give notice to the parties as to whether oral arguments will be scheduled. Even then, a denial of oral argument must fit within one of three narrow exceptions.

Instead of such timely advisement by the Clerk, the parties received only the Rule 34 Notice of March 29, 2018 (App. 44), a notice which did not alert the parties as to whether or not oral argument would be allowed. This Rule 34 Notice simply does not conform to Rule 34(b)'s requirement that the Clerk "*must* advise all parties whether oral argument will be scheduled....." (emphasis supplied). There is a reason for this Rule: if notified that this important procedural right had been denied, the parties could have taken immediate, appropriate action before a final decision by the Panel (which petitioner would certainly have done); and both parties could have repeated their request for oral argument citing a potential $5 million liability for this individual petitioner, the lack of a written opinion on any of the complex issues before the Tax Court, the imposition of draconian penalties without any coherent explanation, and the presence of *multiple* fact patterns showing that this case lies entirely outside the jurisprudence developed under the other 140+ published cases dealing with horse-related activities under IRC § 183.

Indeed, the Clerk's failure to adhere to Rule 34(b) rendered a final decision by the court of appeals without oral argument a *fait accompli*, a decision which ratifies the factual and legal errors committed by the Tax Court, not the least of which is its critical misinterpretation of the important "pleasure or recreation" factor of 26 C.F.R. § 1.183-2(b)(9). In addition, how could the Panel have depended on the Tax Court's reasoning on all issues when a major one, that of an industry-wide depression, heightened by the Great Recession, and petitioner's businesslike reaction to it (by reducing HQH's herd from 109 horses in 2006 down to 54 by the end of 2011), *was completely ignored* by the Tax Court and thus also by the Panel with its all-inclusive adoption of its decision?

Pursuing a petition for rehearing or rehearing *en banc* in the aftermath of this abrupt, one-paragraph *per curiam* decision was no substitute for a timely submission *before the court of appeals decided this appeal* that oral argument was a vital and necessary precondition to understanding how many of § 1.183-2(b)'s nine factors favor the conclusion that petitioner's HQH quarter horse enterprise is one engaged in for profit and was, in fact, a business in every sense of the word.

None of this procedure in the court of appeals squares with the wording or spirit of Rule 34. All the Federal Rules of Civil Procedure, including Fed. R. App. P. 34(b), "shall be construed and administered to secure the *just*, speedy, and inexpensive determination of every action and proceeding." Fed. R. Civ. P. 1 (emphasis supplied). The right of every litigant to adequate notice and the opportunity to respond in a meaningful way to challenges to its pleadings or proof is deeply embedded in the Federal Rules' concept of fair play and substantial justice. See *Memphis Light, Gas & Water Div. v. Craft*, 436 U.S. 1,13-14 (1978); *Arnett v. Kennedy*, 416 U.S. 134, 142-146 (1974); *Mullane v. Central Hanover Tr. Co.*, 339 U.S. 306, 314 (1950). This reflects the fundamental principle of judicial administration that every person is entitled to notice and the availability of some kind of response or even a hearing before adverse judicial action is taken against him. See generally *Volkswagenwerk Aktiengesellschaft v. Schlunk*, 486 U.S. 694,707 (1988).

These embedded notions in the Federal Rules of notice and a fair opportunity to respond and be heard before judicial action is taken are founded on the principle that a llitigant's cause of action and her right to have her claims fairly heard and decided in federal court is a valuable property right entitled to due process protection. *Board of Regents v. Roth*, 408 U.S. 564, 571-572 (1972). The court of appeals' implementation of Rule 34 to deny petitioner the opportunity for oral argument without affording her the further opportunity to contest that decision in some manner denied her the process due under the protocol envisioned by the Rules.

That this denial of oral argument resulted in a one-paragraph *per curiam* decision which simply adopts the Tax Court's reasoning is not coincidence. An abbreviated procedure for affirming decisions of the trial court with *per curiam* one-paragraph decisions absent oral argument and absent any explanation or rationale for the benefit of the parties does not comport with due process because it is incompatible with the concept of a fair hearing. The articulation of reasons for a decision by an appellate court is crucial to the parties affected because its rationality legitimizes the process, justifying the result by reference to prior authority and fostering predictability and normalcy in outcomes. Moreover, reasoned results—anchored by reference to precedent and founded in part on oral argument----bolsters the public's confidence in the judiciary and promotes a code of behavior founded on rules which allow disputes to be settled in an orderly, predictable manner. See *Boddie v. Connecticut*, 401 U.S. 371, 374-375 (1971). See also *Republican Party v. White*, 536 U.S. 765, 790 (2002) (O'Connor, J., concurring). Anything less deprives parties before the court of appeals of a meaningful hearing with a fair opportunity to present their claims. *Armstrong v. Manzo*, 380 U.S. 545, 552 (1965). *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 437 (1982).

The Clerk's failure to properly advise the parties consistent with Rule 34(b) is also an unconstitutional denial of access to the courts. As the *Boddie* Court explained, the Federal government's monopoly over the dispute resolution machinery with its judicial and court personnel means that it must exercise this power evenhandedly so that every litigant is provided due process. 401 U.S. at 374-377. Thus where the federal system provides a means of appeal, it cannot then turn this opportunity into one which is discriminatory, arbitrary and totally unrelated to any federal purpose other than the clearing of its dockets. See *Scott v. McNeal*, 154 U.S. 34, 45-46 (1894). The practice of issuing *per curiam* decisions without oral argument does just that; it penalizes litigants for the dramatic increase in appeals which have beset the court system; and this systemic official action, *Christopher v. Harbury*, 536 U.S. 403, 414-415 & n.12 (2002), has deprived appellants like petitioner of a meaningful hearing on their claims.

In the final analysis, due process requires a meaningful hearing where the participants are fully armed with the relevant facts so that the decisionmaker is fully informed. *Goldberg v. Kelly*, 397 U.S. 254, 269-270 (1970) citing *ICC v. Louisville & N. R. Co.*, 227 U.S. 88,93-94 (1913) and *Willner v. Committee on Character and Fitness*, 373 U.S. 96, 103-104 (1963). The right to a fair hearing does not depend on a demonstration of certain success, only that it take place. *Cleveland board of Education v. Loudermill*, 470 U.S. 532, 544 (1985) citing *Carey v. Piphus*, 435 U.S. 247, 266 (1978). Without oral argument in this case or the opportunity to demonstrate to the court of appeals that such was necessary to make a fair decision here, petitioner was denied a meaningful hearing consonant with due process.

This procedural impropriety compounds the unfairness of summarily affirming the decision of the Tax Court without a written opinion which ratifies its remarkable misapplication of § 1.183-2(b)'s nine factors to petitioner's detriment, a result at odds with other circuit courts of appeals which have considered these nine factors, especially the "personal pleasure" factor, as exemplified by such decisions as *Roberts v. Commissioner*, 820 F.3d 247, 253-254 (7th Cir. 2016) (Posner, J.); *Faulconer v. Comm'r*, 748 F.2d 890, 902 (4th Cir. 1984); and *Wilson v. Eisner*, 282 F. 38, 42 (2nd Cir. 1922).

2. The Court of Appeals' *Per Curiam* Opinion Affirming The Tax Court's Characterization Of Petitioner's Horse Enterprise As A "Hobby" Rejects Forty Years Of Jurisprudence Under 26 U.S.C. § 183, And Unfairly Levies A Tax Deficiency Upon Petitioner Of Over $3.6 Million Plus Penalties And Interest.

In the past forty years, there have been over 140 published decisions by the Tax Court in which the primary issue was whether the "not engaged in profit" language of IRC § 183 did or did not apply to an activity involving horses. The application of this language to every other industry pales by comparison to horse-related activity with petitioner finding no other industry with more than five such published decisions. See, e.g., E. L. Hobbs & W. T. Mawer, *Business or Hobby —Which Do You Have? A Look At IRC § 183*, 15 Southern Law J., 1, 8 (2005). Ninety percent of these cases are Tax Court "Memorandum Decisions," there being no "regular" decisions authored by the Tax Court since 1979.

There are nine non-exclusive factors identified in Income Tax Regs., 26 CFR § 1.183-2(b) for applying IRC § 183's language to any particular industry in order to determine whether or not an activity is engaged in for profit, one of which is set out in § 1.183-2(b)(6). It provides in pertinent part that

> a series of losses during the initial or start-up stage of an activity may not necessarily be an indication that the activity is not engaged in for profit....*If losses are sustained because of unforeseen or fortuitous circumstances* which are beyond the control of the taxpayer, *such as...depressed market conditions, such losses would not be an indication that the activity is not engaged in for profit....*

(emphasis supplied). There was no dispute in the Tax Court that petitioner's quarter horse enterprise underwent severe economic stress beginning in 2006 caused by an oversupply of young horses in the market which, in turn, caused breeding stock prices to decline, events which were exacerbated by the Great Recession beginning in 2008, all of which lasted well past the final tax year in issue, 2011.

Petitioner's response to this depressed market was all business. She reduced HQH's herd from 109 in 2006 so that by the end of 2011, HQH owned only 47 horses. So what did the Tax Court say about this economic setback over which petitioner had no control but to which she responded as any profit-seeking businessperson would? The Tax Court (and the court of appeals through its blanket affirmation of its reasoning) *made no reference at all to these events!* To simply ignore these important facts violates § 1.183-2(b)(6) that losses resulting from "depressed market conditions" are *not* to be considered in determining the presence or absence of a profit motive.

This mistreatment of petitioner's proof is symptomatic of the Tax Court's failure to heed § 1.183-2(b)'s directive that its inquiry into whether or not a taxpayer's activities are motivated by profit is to be made on a year-by-year basis. Thus the nine factors listed in § 1.183-2(b) are to be evaluated separately for each of the years in issue, an analysis which yields remarkable results. For example, in 2005, the second year in issue and the eighth year of petitioner's new activity, a period well within "the startup stage," she had built HQH's herd up from 10 to 109 horses. In contrast, by 2011, the last year in issue, having suffered an industry-wide depression followed by the Great Recession, she met that challenge by reducing her herd from 109 to 54 horses. Yet the Tax Court simply lumped together the eight years treating them all as sharing negative traits, ignoring petitioner's distinctly separate business responses she made to the challenges she faced in the separate years in issue.

Another egregious error of law involved § 1.183-2(b)(3)'s factor, which provides that when substantial time is devoted to the activity, it indicates a profit motive. This is especially true when the taxpayer leaves another job to spend full time in the horse activity. As the Tax Court confirmed, petitioner devoted an average of forty hours per week to HQH. She also gave up her full-time job as a top executive of her highly successful family real estate business. None of the 140+ cases that have held against the taxpayer has ever involved so many hours dedicated to the new activity *and* leaving a full-time profession to do so.

By far the most egregious error involved § 1.183-2(b)(9)'s factor addressing the taxpayer's personal pleasure and recreation. Throughout its opinion, the

Tax Court time and again characterized petitioner's activity as a "hobby" for her personal pleasure. However, under the plain terms of § 1.183-2(b)(9), "the fact that the taxpayer derives personal pleasure from engaging in the activity is not sufficient to cause the activity to be classified as not engaged in for profit if the activity is in fact engaged in for profit as evidenced by other factors...."

As Judge Posner explained in *Roberts v. Commissioner*, 820 F.3d at 253-254, "[t]his is sensible since obviously many businessmen derive pleasure, self esteem, and other nonmonetary 'goods' from their businesses, and horse racing is just the kind of business that would generate such 'goods' for participants...[and] [i]t may have been a fun business, but fun doesn't convert a business to a hobby [because] [i]f it did,, Facebook would be a hobby, Microsoft and Apple would be hobbies, Amazon would be a hobby, etc. ad infinitum...." *Id.*

Moreover, the Tax Court's repetitive reference to a "hobby" defies its dictionary definition which defines hobby as an "activity pursued outside of one's regular work, primarily for pleasure." *Webster's Third Int'l Dictionary of the English Language, Unabridged* (Springfield, MA: Merriam-Webster, 1993). There is no possibility of reconciling "hobby" with the Tax Court's (and the Panel's) usage of the term, after conceding petitioner's 40-hour weekly commitment to HQH.

Besides these fundamental errors, both courts below ignored forty years of jurisprudence developed in the 140+ cases addressing IRC § 183's language when it overlooked the fact that:

1. Of these 140+ cases, this investment by petitioner was both *the largest one made* during the tax years in issue, i.e., $11 million in reported losses over the eight years at issue, and the *largest herd of horses* ever owned by a taxpayer who was found to lack a profit motive. As the Tax Court remarked in *Smith v. Commissioner*, T.C. Memo 1979-324, when considering the taxpayer's 20 consecutive years of losses there with a very large herd of horses, "...any pleasure that may accompany managing a herd of such size and involving so considerable a financial commitment must be the satisfaction one derives from owning a business." *Id*. at *33. Such is the case here.

Similarly, in *Ferris v. Commissioner*, T.C. Memo. 1972-165, at *14, the Tax Court there observed that the taxpayer's ownership of only 27-29 horses "would supply many times over the merely personal satisfaction of owning and raising fine horses." That petitioner owned *four times that many horses* at one time clearly bespeaks a business operated for profit, not one for mere personal pleasure as a "hobby."

2. Of the 140+ cases, this case alone contains *six* highly relevant fact patterns which all support petitioner's profit motive: (a) she made the largest investment during the years in issue except for one case, *Smith*, *supra*, which was decided in favor of the taxpayer's profit motive; (b) she owned the greatest number of horses except for the taxpayer in *Smith*; (c) she devoted 40 hours each week to the new HQH activity (confirmed by the Tax Court) and then elected to leave her successful family business, changing her profession entirely and adopting a new lifetime profession involving quarter horses; (d) she

moved her numerous breeding horses, including her stallions, from Virginia to Texas where she saw them about one week each year, a good business decision and hardly the stuff of a "hobby;" (e) over a four-year period, she committed to HQH about $6 million in capital while during the same period, her total net earnings from non-HQH sources were $5 million, certainly "beyond the point where [she] could be considered as merely supporting a hobby or pastime," *Mary v. Commissioner*, T.C. Memo. 1989-118, at *21; and (f) when petitioner began HQH in 1998, she adopted more vital business practices than in any of the 140+ cases, i.e., books and records, separate bank accounts, a professional advertising program, a website, engaging a professional accountant, procuring insurance, conducting monthly staff meetings, purchasing farm properties for HQH, and over the next eight years growing her herd from 10-12 quarter horses to 109.

Given these unique positive facts demonstrating a profit motive, it is inexplicable how the Tax Court or the Panel itself could conclude that petitioner's HQH enterprise was "not engaged in for profit" within the meaning of IRC § 183. This petition therefor raises the important question of whether the coherent and predictable law developed for horse-related activities under IRC § 183 can be harmonized with this decision. Petitioner submits that to allow this decision to stand will be devastating to the uniformity of the current law about how IRC § 183 should apply to horse-related activities.

3. The Imposition of Accuracy-Related Penalties Is Unfair And Illegal Under IRC § 183's Horse-Related Cases.

Under 26 U.S.C. §§ 6662(a) & 6204(c)(1), a 20 percent accuracy-related penalty applies to each year of "underpayment" unless petitioner can establish "reasonable cause" and "good faith" when she reported HQH as a business engaged in for profit during each such year. Since neither the Tax Court nor the Panel questioned her "good faith," the *sole* remaining question is whether she had "reasonable cause" for so reporting.

To address that question, petitioner again relies upon the 140+ cases which construed the "not engaged in profit" language of IRC § 183. Unlike petitioner, neither court below in addressing this issue cited any horse-related decision under IRC § 183. The reason is obvious: *none* of these 140+ cases with even remotely similar facts has ever finally been subject to the accuracy-related penalty except when the issue is not challenged. In contrast, petitioner in her Briefs cited no less than 10 of these 140+ cases, each of which negated the proposed accuracy-related penalties even though finding or affirming in each case that the taxpayer was not engaged in his or her horse activity for profit.

Of those cases, *Osteen v. Commissioner*, 62 F.3d 356 (11th Cir. 1995), *rev'g* T.C. Memo 1993-519, is probably the most useful decision since there the court reversed the penalties on horse-related activities which were "similar to those at hand." The *Osteen* Court determined that horse owners usually *do* have reasonable cause for underpayments arising from IRC

§183. Other decisions have also concluded that even though a genuine profit motive was lacking, the levy of an accuracy-related penalty was inappropriate because the taxpayer claimed deductions “with a reasonable and good faith application of the law,” *Yates v. Commissioner*, T.C. Memo. 1996-499; because there was no negligence or disregard of applicable law, *McKeever v. Commissioner*, T.C. Memo. 2000-288; because petitioners “had substantial authority for the claimed losses relating to their horse breeding and horse racing activities,” *Machado v. Commissioner*, T.C. Memo. 1995-526 at *22-23; because the taxpayer had reasonable cause and acted in good faith, *Mathis v. Commissioner*, T.C. Memo. 2013-294 at *20; or because the taxpayer made a reasonable good-faith error in applying the law to the facts, *Rodriquez v. Commissioner*, T.C. Memo. 2013-221. See also *Carmody v. Commissioner*, T.C. Memo. 2016-225; *Romanowski v. Commissioner*, T.C. 2013-55 at *44; and *Van Wicker v. Commissioner*, T.C. 2011-196.

To justify penalties, the Tax Court made the specious argument that petitioner failed to prove that Anderson, her accountant (who had passed away by the time of trial), had agreed with her decision to begin HQH in 1998. But that consideration is irrelevant: half of the taxpayers in the decisions cited above, as well as many taxpayers generally, report their taxes without the services of a professional accountant. It is no excuse to infer a lack of reasonable cause on the part of petitioner in proceeding as she did in the tax years at issue.

CONCLUSION

For the reasons identified herein, a writ of certiorari should issue to the Fourth Circuit Court of Appeals in order to review and vacate its *per curiam* decision affirming the decision of the Tax Court; and the matter should then be remanded to the court of appeals for a reconsideration of petitioner's appeal by a new Panel, affording both parties oral argument; or this Court should provide petitioner such other relief as is fair and just in the circumstances of this case.

Respectfully submitted,

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