I. Introduction

Welcome to the latest edition of the Knight Watch! This month’s column is in two parts due to late breaking tax news. The first part, The Book Minimum Tax: The Latest (and Greatest?) in Tax Policy, covers the largest tax increase in the Inflation Reduction Act, which was signed into law on August 16, 2022. Part I is authored by Joshua David Odintz. The second part, Tax Court Proposes Rule Changes to Align with Federal Rules, describes proposed rules issued in March, 2022, that could be finalized by the end of 2022. We will discuss the Inflation Reduction Act and final Tax Court rules in future columns. Part II is authored by Lee S. Meyercord and Jackson Oliver.

II. Part I: The Book Minimum Tax: The Latest (and Greatest?) in Tax Policy

A. Introduction

"Keeping accounts is of no use when a man is spending his own money. You won’t eat less beef today because you have written down what it cost yesterday.” [1]

In September 2021, the House Committee on Ways and Means passed the Build Back Better Act, a sweeping bill that included more than $2 trillion in tax revenue raisers to fund various policies. Proposed offsets included modifying global intangible low taxed income (GILTI) to a per-jurisdiction calculation and significant changes to the base erosion and anti-abuse tax (BEAT). The House also proposed increasing the corporate income tax rate from 21 percent to 26.5 percent. Over the course of the fall, the corporate income tax rate increase was stripped out of the bill in exchange for the corporate alternative minimum tax (AMT), also known as the book minimum tax (BMT).

The Build Back Better Act (BBBA) fell apart in December 2021, and the phoenix bill (the bill known as the Inflation Reduction Act (IRA)) [2] arose from its ashes. Surprisingly, the Biden Administration’s priority, the changes to GILTI, are not part of the IRA. The only tax provisions that survived from the BBBA are the BMT and the 1 percent excise tax on stock repurchases. This column discusses the architecture of the BMT with some interesting observations and how the new tax should interact with the Organisation for Economic Co-operation and Development’s (OECD’s) Pillar Two. [3]

Unfortunately, the BMT does not have a robust legislative history since it was not marked up in either tax writing committee. The House Ways & Means work product and various House committee reports do not describe the BMT. Consequently, Treasury will need to divine Congressional intent as it provides answers to questions raised in this column.
B. Who Is Subject to the BMT?

The BMT applies to an applicable corporation. An applicable corporation is a corporation with average annual adjusted financial income of greater than $1 billion over a three-taxable-year period. For a foreign-parented corporation, the U.S. average annual adjusted financial income must also exceed $100 million over a three-taxable-year period. An applicable corporation does not include an S corporation, a real estate investment trust, or a regulated investment company. [4]

For the $100 million test, a U.S. subsidiary of a foreign-parented group computes its U.S. book income without its share of foreign branch income, controlled foreign corporation (CFC) income, adjusted financial statement income (AFSI) from a partnership interest, and without adjustments related to defined benefit pensions. [5] Also, if a foreign corporation has a U.S. trade or business, then that trade or business is treated as a separate domestic corporation for purposes of the applicable taxpayer test. [6]

Treasury has broad authority to prescribe guidance that addresses when it can include entities as part of a foreign-parented group, and when it can treat a foreign corporation as the common parent of a foreign-parented group. [7]

The BMT uses the single employer rule in Code Sec. 52 to determine whether a corporation is an applicable corporation. The application of Code Sec. 52 was modified on the Senate floor to address concerns by private equity firms that portfolio companies could be treated as related for the one-employer rule, subjecting portfolio companies to the BMT. [8] Under the rule contained in the law, all AFSI of persons treated as a single employer are treated as AFSI of the corporation or partnership. Solely for purposes of testing for an applicable taxpayer, AFSI is modified to not include partnership distributive shares, and the adjustments for covered benefit plans are not applied. [9]

Code Sec. 52(a) provides that a group of controlled corporations is treated as a single employer. Code Sec. 52 defines a controlled group of corporations by references to Code Sec. 1563, with applying a greater than 50 percent threshold to be treated as related members. It is worth noting the complex constructive ownership and stock rules in Code Sec. 1563 that could affect whether corporations are treated as part of a group of controlled corporations. Similar rules apply to determine whether a group of commonly controlled partnerships are a single employer.

While an applicable taxpayer is determined under Code Sec. 52 principles as a group, each taxpayer that files a U.S. Federal income tax return will need to compute its BMT. For example, FC is a Danish corporation that owns US1, US2, and US3. US1 and US2 are two separate U.S. consolidated groups, and US3 is a U.S. corporation that is not part of either consolidated group. Assume FC satisfies the $1 billion test and US1, US2, and US3 in the aggregate satisfy the $100 million test. US1, US2, and US3 are applicable taxpayers, and each taxpayer will need to calculate whether it owes BMT.

B. The Applicable Financial Statement

The starting point for determining applicable corporation status and the potential amount of BMT is an applicable financial statement (AFS), as defined under Code Sec. 451(b)(3) or as specified by the Secretary in regulations or other guidance.

Congress amended Code Sec. 451(b) in 2017 to address the timing of inclusion of income to ensure that income is included for income tax purposes not later than for financial accounting purposes. [10] Code Sec. 451(b)(3) has an ordering rule to define an AFS:
If a taxpayer does not have certified financial statements filed with the U.S. SEC for a 10-K, then, and only then, may a taxpayer use the next type of document in order as an AFS. For example, a foreign corporation would treat its filing with an agency similar to the U.S. SEC if it does not have financial statements in the first three categories.

**Code Sec. 451(b)(3)** works well to determine when a taxpayer should have included an item as income for tax purposes, but Treasury will need to provide further guidance on how to divide the AFS where more than one taxpayer is subject to the BMT. For example, a U.S.-headquartered business could have several consolidated groups and will need to allocate the AFS to each taxpayer. Similarly, a foreign-based group will need to make adjustments to its AFS to compute domestic income subject to the $100 million test, and it will need to exclude foreign items not subject to U.S. tax (e.g., income and losses from foreign corporations not owned by a U.S. corporation).

**C. Adjustment to the AFS**

The BMT requires an applicable taxpayer to make several adjustments to the AFS to compute its AFSI. This section discusses some of the significant adjustments.

1. **Different Taxable Years**

An AFS may cover a different other than a taxable year. Adjustments must be made to AFSI to take into account such timing differences. [11]

2. **Related Entities**

An affiliated group of corporations that file a consolidated return for the taxable year include as AFSI the items on the group’s AFS that are properly allocable to the group. [12]

An applicable corporation that is not a member of a consolidated group includes dividends received from another corporation as part of its AFSI. Also, an applicable corporation includes other items of income or losses from transactions between it and another related corporation, other than subpart F and GILTI inclusions. The Secretary can also exclude other amounts. [13]

Assume US1 owns 100 percent of US2, and the two corporations do not file a consolidated return. US1 is required to include as part of its AFSI any dividends it receives from US2. Also, if US1 makes a loan to US2 and US2 pays interest, then US1 is required to include the interest income from US2 as part of US1’s AFSI, and US2 is required to take a loss for the interest payment on its AFSI.

3. **Partnerships**

A taxpayer includes its distributive share of AFS of the partnership. This adjustment requires a partnership to compute its AFSI based on an AFS, “adjusted under rules similar to the rules of this section.”[14] Essentially,
Congress punted to Treasury, who will need to use its authority to explain how partnerships compute partnership AFSI from an AFS. The statute does not define the term “distributive share.”

The burden on some partnerships may be significant. If a partnership has a corporate partner that is an applicable corporation, the partnership will need to provide the partner with information regarding its distributive share of partnership items. Perhaps Treasury can use its broad authority to create safe harbors to reduce the burden on small partnerships.

4. Foreign Income

The foreign income rules can be beneficial for some taxpayers, while others may have a nasty surprise. A U.S. Shareholder includes its proportionate share of income and losses all of its CFCs. AFSI takes the aggregate approach and allows foreign income to be offset by foreign losses. However, an overall CFC loss cannot reduce the U.S. Shareholder’s AFSI. An overall CFC loss can be carried forward to a future year to offset CFC income, which is more generous than the annual use or lose treatment under GILTI. As part of the computation of CFC income, the U.S. Shareholder loses its qualified business asset investment (QBAI), such that previously exempt foreign income may be subject to U.S. tax.

For example, USCorp is an applicable taxpayer that owns several CFCs that manufacture low-margin widgets. In the aggregate, the CFCs do not generate GILTI because their returns are below 10 percent of QBAI; the income is completely exempt from U.S. federal income tax. However, the exempt income will be added to USCorp’s AFSI and could be subject to the BMT.

An open question is how to treat the payment of a dividend from one CFC to another. The answer should be that dividends between CFCs that are exempt for Federal income tax purposes should be ignored for BMT purposes. The BMT treats all CFCs as one and provides for a blending of all items of income and deductions. Treasury will need to address this issue in future guidance.

Like GILTI, foreign-derived intangible income (FDII) is included in AFSI without the FDII deduction.

An applicable corporation includes dividends and other income paid to it by a foreign corporation that is not a CFC. And an applicable corporation includes all items of income from a foreign branch or disregarded entity.

5. Taxes

An AFS includes taxes paid or accrued for financial reporting purposes. The BMT requires an applicable taxpayer to disregard any Federal income taxes, as well as income, war profits, or excess profits taxes imposed by a foreign country or in possession of the United States, which are taken into account on the AFS. U.S. state and local taxes are not disregarded, and continue to reduce AFSI.

6. Direct Payment of Credits

The IRA significantly modified and expanded the green energy tax provisions in the Code. A taxpayer that cannot offset its income tax with a general business credit can elect to receive a direct payment of the credit. To avoid taxing the direct payment, AFSI is reduced to disregard any amount that is treated as a direct payment.

7. Covered Benefit Plans

The BMT recognizes that an AFS may include income and associated expenses from certain retirement plans. The IRA permits adjustments to AFSI for a covered benefit plan, which is defined as (1) a defined benefit plan (other than a multiemployer plan) if the trust is employees’ described in Code Sec. 401(a) and is tax exempt under Code Sec. 501(a), (2) any qualified foreign plan, or (3) any other defined benefit plan that provides post-employment benefits other than pension benefits.
AFSI is (1) adjusted to disregard any amount of income, cost, or expense otherwise included on the AFS in connection with a covered benefit plan, and (2) modified to include any income or deductions from a covered benefit plan included by the applicable taxpayer for Federal income tax purposes. [19]

8. Depreciation

An earlier version of the BMT would have effectively taxed timing differences due to accelerated depreciation and current expensing. In response to comments from manufacturers and other affected businesses, the Senate modified the bill to address timing differences from accelerated depreciation under Code Sec. 168. AFSI is reduced by the amount of accelerated depreciation under Code Sec. 168. [20]

Other types of accelerated cost recovery, such as intangible drilling and development costs [21] and qualified tertiary injectant expenses, [22] are not explicitly carved out as adjustments. Sens. John Barrasso (R-WY) and James Lankford (R-OK) offered an amendment during the debate of the Senate reconciliation bill to add an adjustment for these items, which did not pass. Treasury has broad authority to issue guidance and could provide relief for these items.

9. Treasury Authority

Treasury has very broad authority to issue guidance to create categories of adjustments to AFSI to “carry out the purposes of this section ....” [23] The statute specifies a few areas for Treasury to address, including to prevent the omission or duplication of any item, to carry out the purposes of subchapter C pertaining to liquidations and corporate organizations and reorganizations, and to carry out the purposes of subchapter K pertaining to partnership contributions and distributions.

Congress provided some guidance on adjustments, but it has not addressed all fact patterns and all book and cash tax differences. Treasury will need to address the treatment of corporate organizations and reorganizations. How will an AFS be split when a parent spins off a subsidiary? How will purchase price accounting be addressed in the case of an acquisition? As described above, Treasury will need to create a separate set of guidance to address the treatment of partnerships.

D. Foreign Tax Credits and General Business Credits

Two sets of rules apply to BMT foreign tax credits (BMT FTCs). First, FTCs arising from taxes paid by CFCs are limited to 15 percent of the U.S. Shareholder’s share of book revenue from the CFCs. BMT FTCs from CFCs are computed on an aggregate basis, and a credit is allowed for those foreign taxes that are taken into account on the AFS of each CFC for which the U.S. corporation is a U.S. Shareholder, and the foreign tax must be paid or accrued for Federal income tax purposes. [24]

The BMT FTC provision does not cross-reference Code Sec. 904, so it appears BMT FTCs from CFCs are not subject to the limitations. Also, FTCs in the GILTI basket are not subject to the 20 percent GILTI FTC haircut. Taxpayers can fully blend all taxes, utilizing high foreign taxes to offset low taxed income.

Second, FTCs paid directly by a U.S. entity or a disregarded entity owned by a U.S. entity are not subject to the 15 percent limitation. A taxpayer that is AMT FTC-limited could consider checking the box to treat a CFC as a disregarded entity. [25]

BMT FTCs can be carried forward up to five years, which once again is more generous than GILTI.

Treasury has authority to issue regulations or guidance “as is necessary to carry out the purposes of this subsection.” [26] A question some have raised is whether Treasury has authority to create a per-country limitation on FTCs. Since CFC income is combined, it is clear the drafters intended a one-CFC approach for income and AMT FTCs.
An applicable taxpayer can offset its BMT with general business credits and is limited to 75 percent of income. [27]

E. Net Operating Losses

Like the TCJA, the BMT is not for losers. [28] An applicable taxpayer can use financial statement net operating loss (NOL) carry-forwards to offset up to 80 percent of book income. Congress limited such carry-forwards to losses arising from taxable years ending after December 31, 2019.

Congress did not explain why it selected the date for the limitation. Perhaps the limitation is related to the amount of revenue needed to pay for green energy and spending in the IRA.

The effective date could impact startup businesses that went public over the last decade, as well as businesses that went through a slump prior to 2020. While the BMT mostly raises taxes from temporary timing differences, the loss of pre-2020 BMT NOLs is a permanent tax increase. Congress should revisit this issue and allow pre-2020 BMT NOLs.

F. Pillar Two Interaction

There is a wonderful debate on Twitter regarding how the OECD should treat this new tax for purposes of the Tax Challenges Arising from the Digitalisation of the Economy—Global Anti-Base Erosion Model Rules (Pillar Two). Is the BMT a qualified domestic minimum top-up tax (QDMTT)? Or is it a CFC tax regime/income inclusion rule (IIR)?

The Model Rules require a QDMTT to (1) determine the excess profits of constituent entities located in a jurisdiction in a manner equivalent to the Global Anti-Base Erosion (GloBE) Rules, (2) operate to increase domestic tax liability on Excess Profits to the minimum rate for the jurisdiction and constituent entities for a fiscal year, and (3) be implemented and administered in a way that is consistent with outcomes provided for under the GloBE Rules and Commentary. [29]

The BMT can tax income earned outside the United States and operates as a global top-up tax for U.S.-headquartered groups. Because the BMT taxes foreign profits, it fails the first two prongs of the definition of a QDMTT. But it is certainly a DMTT!

An IIR applies the GloBE top-up tax on a jurisdictional basis. [30] The Model Rules define a CFC tax regime as “a set of tax rules (other than an IIR) under which a direct or indirect shareholder of a foreign entity … is subject to current taxation on its share of part of all of the income earned by the CFC, irrespective of whether that income is distributed currently to the shareholder.” [31]

The BMT is clearly not an IIR, as it allows an applicable taxpayer to blend jurisdictions and cross-credit FTCs, but it does operate like a CFC tax regime by topping up the income earned by the CFC at the shareholder level.

The BMT is a hybrid of a domestic minimum top-up tax and a CFC tax regime. Depending on the facts, the BMT could be a top-up of domestic income, CFC income or a blend of the two. Treasury is currently considering proposals on how to allocate GILTI and related taxes on a per-jurisdiction basis. [32] Treasury will also need to consider how to allocate the BMT between the U.S. group and the foreign group, and then again among the CFCs. The OECD and Inclusive Framework countries can decide whether to accept a proposed methodology.

G. Conclusion

“If the whole conclave of Hell can so compromise exadverse and diametrical contradictions as compolitse such a multimonstrous maufrey of heteroclites and quicquidlibets quietly, I trust I may say with all humble reverence they can do more than the Senate of Heaven.” [33]
Treasury and the Internal Revenue Service (IRS) have their work cut out for them for the next fiscal year and beyond. The biggest issues are the treatment of corporate reorganizations, the definition of distributive share of a partnership and the related rules that affect partnership AFS and AFSI, and convincing other countries to agree with an allocation method to treat the BMT as a DMTT and CFC tax regime.

And what role will the Financial Accounting Standards Board play in the BMT?

III. Part II: Tax Court Proposes Rule Changes to Align with Federal Rules

On March 23, 2022, the United States Tax Court (Tax Court) proposed amendments to its existing rules of practice and procedure and offered three new rules. The new rules concern intervention in a Tax Court proceeding, identification and certification of the administrative record, and amicus curiae briefs. The changes also include amendments drafted in response to suggestions and comments the Tax Court received from the Court’s judges and staff, the IRS Office of Chief Counsel of the IRS, and the Tax Court bar over the last few years. They seek to fill gaps in the Court’s existing procedures and reflect the Court’s ongoing effort to modernize the rules and conform them to the extent possible to the Federal Rules of Civil Procedure (FRCP). This column summarizes the three new proposed rules, the most substantive amendments to current rules, and the conflicts that led to the proposed changes.

A. Background

The Tax Court began as an executive agency created to provide a forum where taxpayers could obtain a determination of their correct tax liability before having to pay the deficiency asserted by the IRS. In 1969, the forum was accorded the status of an Article I Court. Upon this change, the Tax Court made efforts to conform its rules to those in other federal courts. However, unlike district courts, which must follow the FRCP, the Tax Court operates under its own separate set of procedural rules—the Tax Court Rules of Practice and Procedure (Tax Court Rules). In the absence of an applicable Tax Court Rule, Tax Court Rule 1(b) allows the Tax Court to "prescribe the procedure, giving particular weight to the FRCP to the extent that they are suitably adaptable to govern the matter at hand." Therefore, the Tax Court has considerable freedom to create its own rules and procedures and amend the rules at its discretion.

B. New Proposed Rules

1. Intervention

The Tax Court does not currently have a general intervention rule for third parties. Therefore, a person or entity generally may not intervene in a Tax Court proceeding as a party petitioner unless a statutory notice of deficiency has been issued to such person or entity with exceptions for unique and limited circumstances. In the absence of a general intervention rule, courts have looked to FRCP 24 in deciding whether intervention should be permitted.

Under FRCP 24(a), an applicant has a right to intervene in an action in two circumstances. First, under FRCP 24(a)(1), an applicant has a right to intervene in an action when a U.S. statute gives the applicant an unconditional right to intervene. Second, under FRCP 24(a)(2), an applicant has the right to intervene in an action when the applicant can show an interest in the outcome of the action. Alternatively, a nonparty may seek permissive intervention under FRCP 24(b) if the would-be intervener’s claims or defenses share a question of law or fact with the principal action. FRCP 24(b)(2) specifically provides for permissive intervention by a federal or state governmental officer or agency “if a party’s claim or defense is based on (A) a statute or executive order administered by the officer or agency; or (B) any regulation, order, requirement, or agreement issued or made under the statute or executive order.”
Multiple courts have interpreted FRCP 24 in the context of IRS challenges to the residency of purported residents of the U.S. Virgin Islands (USVI). In these cases, the taxpayers, claiming to be USVI residents, filed their tax returns in the USVI. The IRS issued notices of deficiency claiming the taxpayers were not residents of the USVI during the years in question and therefore should have filed returns with the IRS and paid taxes on their U.S. source income. The IRS further claimed that the three-year statute of limitations period for assessment under Code Sec. 6501 had not begun because the taxpayers never filed returns with the IRS. The taxpayers then petitioned the Tax Court and argued that the notices were time-barred (or alternatively, incorrect).

The government of the USVI sought to intervene in these cases, both as a matter of right under FRCP 24(a) and permissively under FRCP 24(b)(2), arguing that the IRS’ position threatened the USVI’s taxing and fiscal sovereignty. The Eleventh Circuit, Third Circuit, and Eighth Circuit all allowed the USVI to intervene in the Tax Court proceeding. Further, the Eleventh Circuit allowed intervention as a matter of right under FRCP 24(a)(2), which had never been granted to a third-party non-taxpayer in the Tax Court before. However, the Fourth Circuit created a circuit split when it affirmed the Tax Court in denying USVI’s intervention.

The Chief Counsel, citing the decision by the Eleventh Circuit, recommended that the Tax Court “adopt a rule that authorizes the Court to exercise discretion in granting or denying permissive intervention in its cases, but does not provide for intervention as of right, which is inappropriate in Tax Court litigation affecting only the parties before the Court.” The American Bar Association Section of Taxation (ABA Tax Section) expressed its disagreement with Chief Counsel’s proposed rule that intervention as a matter of right is “inappropriate” in the Tax Court in all cases and noted that both the Code and the court have identified certain circumstances—such as innocent spouse cases—in which intervention as a matter of right is entirely appropriate and, in fact, available.

In light of these cases and commentary, the Tax Court proposed the adoption of a general intervention rule, in place of its current practice of looking to FRCP 24. Under Proposed Tax Court Rule 63(a), intervention is allowed as a matter of right when a person is given an unconditional right to intervene under federal law. As an example, the Tax Court points to innocent spouse relief under Code Sec. 6015, where intervention as a matter of right has previously been recognized. This proposed rule is nearly identical to the rule in FRCP 24(a)(1). However, the Tax Court declined to extend an intervention of right to applicants presenting an interest in the outcome of the action as provided in FRCP 24(a)(2). The Tax Court highlighted that, unlike in other federal courts, the Commissioner is uniformly the respondent in Tax Court proceedings, while the petitioner usually is challenging a notice of a deficiency or notice of determination. Therefore, the Tax Court normally lacks jurisdiction to adjudicate the rights of nonparties, such as the beneficiary of an estate, even though intervention may be advisable and permitted under the FRCP.

Additionally, permissive intervention will be allowed when a person has a conditional right to intervene under federal law, or if the person has a stake in the outcome of the litigation that cannot be adequately protected by the parties. These proposals are consistent with the Tax Court precedent permitting intervention when doing so contributed to the disposition of an issue. For example, in Estate of Proctor, the Tax Court allowed three interveners with adverse interests in an estate tax case to intervene because their interests were not adequately protected by the existing parties and permitting the interventions would lead to a more complete presentation of the legal issues. Accordingly, permissive intervention will generally only be permitted when (1) “the ends of justice so require,” (2) the moving party has a stake in the outcome of the Tax Court litigation “which cannot be adequately protected by the parties currently before the court,” and (3) “permitting the intervention will lead to a more complete presentation of the legal issues to be decided.”

Furthermore, Proposed Tax Court Rule 63(b)(2) provides that the Tax Court may permit a Federal or State governmental officer or agency to intervene if a party’s claim or defense is based on (A) a statute or executive order administered by the officer or agency, or (B) any regulation, order, requirement, or agreement issued or
made under the statute or executive order. This proposed rule is discretionary and substantially similar to FRCP 24(b)(2).

2. Administrative Record

In deficiency cases, the Tax Court does not rely on the administrative record and instead conducts an independent review, receives evidence, and makes an independent determination of the facts and the tax liability. However, there are certain types of cases where judicial review is limited to the administrative record, such as whistleblower actions, collection review actions, and spousal relief disputes. While the Tax Court had previously adopted rules of procedure and a uniform process governing the submission of the administrative record in declaratory judgment cases, no Tax Court guidance had been offered for other situations.

To address this gap, Proposed Tax Court Rule 92 provides rules on identifying and certifying an administrative record in actions where judicial review is normally limited to the administrative record and other relevant evidence. The proposed rule generally requires the parties (or the IRS, if the parties cannot stipulate to the record) to file the entire administrative record with the Tax Court no later than 30 days after the notice of setting the case for trial is served. If a party seeks to supplement the administrative record, a party must move to supplement the administrative record no later than 60 days after the notice setting the case for trial is served, unless the court orders otherwise.

Historically, in district court cases decided on the administrative record, the parties are required to file the administrative record after the completion of discovery and the parties are ready to submit the case for decision. Proposed Tax Court Rules 92(a) and 92(b), on the other hand, do not tie the deadline for filing the administrative record to any discovery deadlines, which may present timing issues for supplementing the administrative record.

The proposed definition of the “administrative record” comprises:

[Any] request for determination or other administrative action (request), all documents submitted to the Internal Revenue Service by the taxpayer (including the taxpayer’s representative) in respect of the request, all protests and related papers submitted to the Internal Revenue Service, all written correspondence between the Internal Revenue Service and the taxpayer in respect of the taxpayer’s request for relief in such protests, all materials prepared by Internal Revenue Service personnel in connection with the administrative proceeding, all pertinent returns filed with the Internal Revenue Service, the notice of determination, recorded interviews, and any other information or communications submitted to or considered by the Internal Revenue Service in making the determination or taking the administrative action.

The proposed definition closely matches the definition used by district courts in reviewing the record of other administrative agencies. However, the proposed definition may not encompass certain oral statements and information stored on the IRS’ system electronically that are not otherwise reduced to writing.

The proposed administrative record definition may also conflict with the definition of the administrative record in the context of the Administrative Procedure Act (APA) because the administrative record may be supplemented. In a letter providing comments on Proposed Tax Court Rule 92, the Office of Chief Counsel noted that the administrative record for purposes of review of a regulation or other guidance under the APA is generally limited to the materials considered by the IRS in promulgating the rule. The administrative record for purposes of Proposed Tax Court Rule 92(c), by contrast, allows a party to move to “supplement” the administrative record if a party contends the record is “incomplete.” As a result, the administrative record for purposes of Proposed Tax Court Rule 92(c) may be different from that under the APA.
3. Amicus Curiae

The final new proposed rule involves briefs submitted by amicus curiae. Historically, the Tax Court has been relatively liberal in permitting participation by amicus curiae, although there are no prescribed standards for allowing such briefs. The Tax Court often looks to the standards set forth in Supreme Court Rule 29, FRCP 29 and local appellate court rules to determine whether such a brief will provide information to the Court beyond that provided by the parties.

Proposed Tax Court Rule 152 now provides a uniform rule for the Tax Court to accept briefs filed by amicus curiae. Proposed Tax Court Rule 152(a) provides that the Tax Court may either direct an amicus curiae to file a brief or the amicus curiae may file a motion for leave to file an amicus brief. If the amicus files a motion for leave, the amicus curiae must file the motion no later than 14 days after the first brief of the party being supported (or 14 days after the first brief is filed if no party is being supported) and attach the proposed brief. The motion must state the movant’s interest and explain why an amicus brief is desirable and the matters in the brief are relevant to the disposition of the case. The amicus brief is limited to 25 pages.

The explanation to the rule states that Proposed Tax Court Rule 152 is a corollary to Rule 29 of the FRCP and Rule 7(o) of the local rules for the U.S. District Court for the District of Columbia. Unlike Supreme Court Rule 37(a) and FRCP 29(a)(2), Proposed Tax Court Rule 152 does not contain provisions allowing for an amicus filing upon the parties’ consent. However, this may reflect the recent trend, as the Supreme Court has proposed amending its Rule 37 to remove any requirement to obtain consent or file a motion for leave before submitting an amicus brief.

C. Amendments to Current Rules

In addition to the new rules discussed above, the Tax Court also proposed amendments to the existing rules. The following addresses the most substantive amendments to rules regarding Tax Court filings, subpoenas, and discovery.

1. Tax Court Filings

Certain taxpayers are required to submit ownership information with their Tax Court petition to allow the Tax Court judges to determine whether automatic disqualification would be appropriate under the financial interest standard. Specifically, any nongovernmental corporation must submit with its petition a separate disclosure statement identifying or stating the absence of any parent corporation and publicly held entity owning a 10 percent interest in the petitioner. Further, any partnership, partnership representative, tax matters partner, or limited liability company must file a disclosure statement either identifying any publicly held entity owning an interest in the petitioner or state that no such entity exists. A form of the disclosure statement is provided in Appendix I of the Tax Court Rules.

The broad scope of parties required to file a disclosure statement has generated confusion among taxpayers. Accordingly, the proposed amendment to Tax Court Rule 20 limits the requirement to file a disclosure statement to nongovernmental corporate parties. This amendment conforms to FRCP 7.1 and eliminates the disclosure requirement for passthrough entities. Noting the limited scope of disclosures covered by the proposed amendment, the Tax Court cited the Advisory Committee Notes to FRCP 7.1 for the proposition that the rules “are calculated to reach a majority of circumstances that are likely to call for [a judge’s] disqualification on the basis of financial information that a judge may not know or recollect.”

The proposed amendments also eliminate the certificate of service requirement for most filings. Under the existing rules, all Tax Court papers other than the petition must be served by the party filing the paper and be accompanied by a certificate of service. Due to the widespread use of electronic communication, FRCP 5(b) was revised in 2018 to make service of pleadings through the court’s electronic system the default method for
serving papers upon the Court and opposing parties. [79] The Tax Court is now proposing to conform its rules to FRCP 5(b). [79] Specifically, the proposed amendment to Tax Court Rule 21(b) provides that a taxpayer can file any document with the Tax Court’s electronic filing and case management system (DAWSON) or by sending it through other electronic means that the person consented to in writing. A certificate of service for documents filed using the electronic system is now unnecessary, although service of process outside the Tax Court’s system must still be accompanied by a certificate of service.

In conjunction with these proposed amendments, Tax Court Rule 21(c) now requires a party to a Tax Court proceeding, including counsel and authorized representatives, to update the Tax Court if there is a change to the email address kept on file with the Tax Court. Corresponding changes were made to Form 10 (Notice of Change of Address) to include a line for the party’s email address. In addition, the proposed amendments include stylistic changes to Tax Court Rule 23, Form and Style of Papers. Proposed Tax Court Rule 23 omits all prefixes (e.g., Mr., Ms.) from pleadings and permits the use of a typed written name on a pleading that is filed electronically with the court to constitute that person’s signature.

2. **Subpoenas**

A subpoena may be issued in a Tax Court proceeding for testimony and production of all necessary returns, books, papers, documents, correspondence, and other evidence at any designated place of hearing. [80] The Tax Court has nationwide subpoena power and can compel documents or testimony from a person located anywhere in the United States. In district court, by contrast, a subpoena may only be issued to a witness to attend a hearing, deposition, or trial or produce documents within 100 miles of where the person resides, is employed, or regularly transacts business in person. [81]

The requesting party in a district court case may serve separate document subpoenas and testimonial subpoenas directed to the same person, [82] while the Tax Court currently provides a single form on its website to be used by parties issuing subpoenas for testimony and/or production of documents. [83] Moreover, there is no corresponding Tax Court Rule for the FRCP 45 requirement that notice be provided to all parties when any subpoena is issued to a third party for documents. [84] Because Tax Court Rules 147(a) and (b) do not mention notice and provide that the subpoena will not be filed with the court, subpoenas are not subject to the general Tax Court rules on notice found in Tax Court Rule 21(a). [85] The absence of an explicit notice requirement creates the possibility of surprise whereby one party can issue “secret subpoenas” to gather information from third parties without the opposing party’s knowledge or access to the same materials. [86]

For example, in *Ryder v. Commissioner*, [87] the IRS served 77 subpoenas on third parties without notifying the taxpayer of who had been served. In an order issued 17 days before trial, Tax Court Judge Holmes highlighted that the intended goal of Tax Court Rule 147 was to create a rule substantially similar to FRCP 45. [88] However, FRCP 45 did not provide an advance notice requirement for subpoenas at the time Tax Court Rule 147 was promulgated. [89] According to Judge Holmes, the Tax Court’s deviation from FRCP 45 was unintentional and ordered both parties to comply with the notice requirements in FRCP 45(a)(4). Therefore, the IRS was required to serve all of its previously issued nonparty subpoenas, with all responses and documents that were produced in response to those subpoenas to the taxpayer.

The decision in *Ryder* further aligned Tax Court Rule 147 with the FRCP and enhances each party’s ability to review third-party documents sufficiently in advance of trial and to stipulate to those that are not in dispute. [89] Nevertheless, while the Tax Court indicated that a notice requirement should be added to the Tax Court subpoena rules, litigants have experienced mixed results when petitioning the Tax Court to compel the other party to produce copies of all nonparty subpoenas and documents produced by any such nonparties. [91]

In light of the conflicting guidance in this area, the Tax Court proposed multiple amendments to Tax Court Rule 147. First, the rules were amended to require that any subpoena requesting the production of information must
also require attendance at a deposition, hearing, or trial. Although this proposed rule deviates from FRCP 45, which permits the issuance of separate subpoenas for testimony or documents, the proposed rule ensures the other party has the opportunity to question the witness and promotes the development of the case by the parties.

Furthermore, the party issuing a subpoena must provide notice and serve a copy of the subpoena on all other parties. This amendment eliminates the notice issues under the current rules and mirrors the notice requirement in FRCP 45(a)(4) where notice and copy of the subpoenas must be served on each party prior to service of the subpoena. This proposal provides parties with an opportunity to quash or limit abusive subpoenas. However, the ABA Tax Section expressed concern that the advance notice requirement may result in identifying witnesses, which is subject to work-product privilege, and provides the opposing party with information about the requesting party’s trial strategy. The ABA Tax Section proposed an alternative approach that permits a party to move for an order compelling production or inspection.

The proposed amendment also adds new provisions to Tax Court Rule 147 that describe the procedures for protecting the party subject to a subpoena, as well as the rules governing a party’s duties in responding to a subpoena. Under the current rules, a witness subject to a document subpoena may object by timely motion to the subpoena and request either that it be quashed or modified if it is unreasonable or oppressive or that it be conditioned on the advancement of reasonable costs of production by the subpoenaing party. Proposed Tax Court Rule 147(d)(2)(B) amends the deadline for objecting to a subpoena within (i) 15 days after the subpoena is served, or (ii) the time specified for compliance, if earlier. The amendments to Tax Court Rule 147 also provide that the Tax Court must quash or modify a subpoena that fails to allow a reasonable time to comply. However, the explanation to the proposed amendment does not offer any specific guidance on a minimum time that will be considered “reasonable.”

3. Discovery

The scope of discovery under the Tax Court Rules is generally narrower than in either the district courts or the Court of Federal Claims. Underlying the Tax Court’s overall discovery process is the principle that discovery is not to be utilized unless the parties are unable to obtain the information on an informal basis. Tax Court Rule 70 outlines the expectation that all parties attempt to obtain discovery through informal means. A party may seek discovery from the other party of information concerning any matter not privileged that is relevant to the subject matter involved in the case. The Tax Court’s standard for permissible discovery can be contrasted with the standard in FRCP 26, which applies a proportionality standard tailored to the needs of the case.

The proposed Tax Court amendments adopt the proportionality standard utilized in FRCP 26(b)(1). The proportionality standard in FRCP 26(b)(1) was slightly revised in 2015 to ensure that the factors were an explicit component of the scope of discovery, requiring parties and courts to consider them when pursuing discovery and resolving discovery disputes. The Tax Court’s purpose for adopting the proportionality rule is unclear based on the explanation and lack of published guidance. Unlike district court orders on discovery issues, which are easily accessible, the Tax Court’s rulings on discovery are typically contained in unpublished orders. Accordingly, parties should continue to monitor the application of the proportionality standard in tax disputes.

Additional proposed changes to Tax Court Rule 70 would specifically protect privileged information and trial-preparation materials. If a party withholds information otherwise discoverable by claiming that the information is privileged or subject to protection as trial-preparation material, the party would have to expressly make the claim and describe the nature of the materials not produced or disclosed in a manner that would enable other parties to assess the claim without revealing the privileged or protected information. Thus, the party must provide privilege log similar to that provided in district court.
The proposed rule also adds provisions addressing inadvertent disclosure of privileged documents that mirror FRCP 26(b)(5)(B). If information produced during discovery is subject to a privilege or protected information claim, the party claiming the privilege would be required to notify each party that received the privileged documents. The notice should be as specific as possible in identifying the information and must state the basis for the claim. After receiving notice, each party that received such information is required to return, sequester, or destroy the information and any copies in its possession.

D. Conclusion

The Tax Court’s proposed new rules and amendments modernize the rules, bring them more in line with the FRCP and fill gaps in the court’s existing procedures. Generally, these proposed new rules and amendments will provide litigants with more certainty and are a favorable development. However, litigants will need to monitor their application to understand their true impact and any unintended consequences.

Footnotes


Joshua D. Odintz is a fan of good quotes.


2 The official name of the IRA is An Act to provide for reconciliation pursuant to title II of S. Con. Res. 14.

3 For an excellent article on designing a minimum tax, see Christopher H. Hanna, Michelle Hanlon, Norman Richter & Michael Schler, *The Rise of the Minimum Tax*, TAXES, March 2022, at 55.

4 “We’re talking C corps here, right?” David Foster Wallace, *The Pale King*, at 142.

5 Code Sec. 59(k)(2).

6 Code Sec. 59(k)(2)(C).

7 Code Sec. 59(k)(2)(D).

8 For a view that private equity still has a BMT problem, see Lee A. Sheppard, *Private Equity’s Book Tax Problem*, 2022 TNTF 156-1.

9 Code Sec. 59(k)(1)(D).

10 P.L. 115-97, §13221(a).

11 Code Sec. 56A(c)(1).

12 Code Sec. 56A(c)(2)(B).
A taxpayer will need to consider how a check the box election will affect the branch, GILTI and passive baskets. For a discussion regarding baskets and limitations, see Robert E. Culbertson and Michael J. Caballero, *Rewriting the Foreign Tax Credit Limitation (Again)*, *TAXES*, March 2022, at 139.

For a discussion regarding the harsh treatment of loss companies in the Tax Cuts and Jobs Act, see Stewart Lipeles, Joshua Odintz, Katie Rimpfel, and Matthew Mauney, *The TCJA is Not for Losers*, 48, 9 TMIJ 423 (September 13, 2019).

Pillar Two Model Rules, at 64.

Pillar Two, Model Rules, Article 5.

Pillar Two Model Rules, at 54.


Hereinafter abbreviated “PROP. TAX CT. R.” in citations.


Hereinafter "FED. R. CIV. P." in citations.


*Proposed Rules of the Tax Court*, 26 TAX LAWYER 377 (1973). In a panel discussion of the proposed Rules of the Tax Court, Judge Arnold Rahim, Chairman of the Tax Court’s Rules Committee, stated: “With the enactment of the Tax Reform Act of 1969 and the consequent new status for the Tax Court under that Act, most of us felt that the time had come for a comprehensive revision of the rules. With particular attention to the Federal Rules of Civil Procedure.” *Id.* at 378.

“[T]he proceedings of the Tax Court and its divisions shall be conducted in accordance with such rules of practice and procedure … as the Tax Court may prescribe.” *Code Sec. 7453* (1954). Unless otherwise indicated, references to a “section” are to a section of the Internal Revenue Code of 1986, as amended (the “Code” or “I.R.C.”).

Hereinafter abbreviated “TAX CT. R.” in citations.
42 Tax Ct. R. 1(b).

43 Code Sec. 7453.

44 See, e.g., Tax Ct. R. 216(a) (permitting intervention by PBGC or Secretary of Labor in certain retirement plan actions); Tax Ct. R. 225 (permitting intervention in actions with respect to Code Sec. 6110 written determinations); Tax Ct. R. 245(a) (permitting intervention in certain partnership actions); Tax Ct. R. 325(b) (permitting intervention by the non-electing spouse in action for relief from joint and several liability).

45 W.C. Sampson, CA-6, 83-2 ustc ¶9432, 710 F2d 262, 264 (1983) (holding that the Tax Court has the authority to permit persons or entities who have not been issued a deficiency notice to intervene in a deficiency case pursuant to Fed. R. Civ. P. 24(b); Amazon.com, Inc. & Subsidiaries, 112 TCM 30, Dec. 60,647(M), TC Memo. 2016-131 (permitting a newspaper to intervene as a non-party movant for purposes of seeking to unseal portions of the record).

46 See G.C. Huff, CA-11, 2014-1 ustc ¶50,186, 743 F3d 790, 801 (2014) (holding that the Virgin Islands Government is permitted to intervene in a Tax Court case under FRCP 24(a)(2)), rev’g and remanding 138 TC 258, Dec. 58,982 (2012); E.J. McHenry, CA-4, 2012-1 ustc ¶50,305, 677 F3d 214 (2012) (affirming Tax Court’s order denying intervention of the Virgin Islands Government because Tax Court Rule 1(b) gives the Tax Court broad discretion to decide whether and to what extent to follow FRCP 24 and because FRCP 24 itself confers broad discretion on a trial court); A.I. Appleton, CA-3, 2011-1 ustc ¶50,429, 430 FApp’x 135, 136, 139 (2011) (permitting the Virgin Islands Government to intervene pursuant to FRCP 24(b)(2)), rev’g and remanding 135 TC 461, Dec. 58,376 (2010); J.S. Coffey, CA-8, 2011-2 ustc ¶50,742, 663 F3d 947-51 (2011) (holding that the Virgin Islands Government could intervene pursuant to FRCP 24(b)(2)).

47 Under Code Sec. 932, bona fide residents of the USVI do not have to file returns with the IRS or pay income taxes to the United States as long as they file returns with the IRS and properly report their worldwide income.


49 G.C. Huff, CA-11, 2014-1 ustc ¶50,186, 743 F3d at 801.

50 E.J. McHenry, CA-4, 2012-1 ustc ¶50,305, 677 F3d at 216.


53 See Code Sec. 6015(e)(4) (“The Tax Court shall establish rules which provide the individual filing a joint return but not making [an innocent spouse claim] … with adequate notice and an opportunity to become a party to a proceeding …” This instruction from Congress is reflected in Rule 325, which requires the IRS to serve notice of the petition on the non-requesting spouse and provides that the "notice shall advise the other individual of the right to intervene" in the case (emphasis added).

54 Prop. Tax Ct. R. 63(a)(1).


56 Prop. Tax Ct. R. 63(b).


58 Code Sec. 6213 (2000).

59 K.W. Kasper, 150 TC ___, No. 2, Dec. 61,103 (2018) (determining that in whistleblower cases Tax Court’s scope of review is generally restricted to the administrative record and the standard of review is abuse of discretion).
60 J.M. Robinette, 123 TC 85, Dec. 55,698 (2004), rev'd, CA-8, 2006-1 USTC ¶50,213, 439 F3d 455 (2006) (held that judicial review of collection-due-process determinations should be limited to the administrative record—at least for issues other than the underlying tax liability).

61 K.M. Wilson, CA-9, 2013-1 USTC ¶50,147, 705 F3d 980, 982 (2013), acq. AOD 2012-07, 2013-25 IRB (Tax Court standard of review is based on both the administrative record established at the time of the determination and any additional newly discovered or previously unavailable evidence); Code Sec. 6015(e)(7).

62 PROP. TAX CT. R. 93(a).

63 PROP. TAX CT. R. 93(b).

64 Citizens to Preserve Overton Park, Inc. v. Volpe, SCI, 401 US 402, 419-20, 91 SCI 814 (1971) (reviewing court considers the decisions in light of “the full administrative record that was before [the agency decision maker] at the time he made his decision”).

65 Letter from Julie A. Divola, Chair, Section of Taxation, American Bar Association, to Hon. Maurice Foley, Chief Judge, U.S. Tax Court (May 25, 2022) www.americanbar.org/content/dam/aba/administrative/taxation/policy/2022/052522comments.pdf.


69 This is consistent with prior decisions permitting additional documents beyond the administrative record in two situations: (1) when a party files a “motion to complete the record,” in which a party seeks to add documents to the record that were actually considered by the agency in making the challenged decision but allegedly omitted from the administrative record; or (2) when a party files a motion for leave to supplement the administrative record if the documents at issue were allegedly not considered by the agency in reaching its decision. Poplar Point RBBR, LLC, 145 FedCl 489, 494 (2019); Van Bemmelen, 155 TC 64, 73 (2020); Animal Legal Def. Fund v. Vilsack, 110 FSupp3d 157, 160 (DDC 2015) see generally Peter Constable Alter, A Record of What? The Proper Scope of an Administrative Record for Informal Agency Action, 10 UC IRVINE L. REV. 1045, 1057 (2020).

70 A computerized search indicates that the Tax Court has granted such leave in approximately 50 reported cases since 1942. See, e.g., Klukwan, 68 TCM 446, Dec. 50,053(M), TC Memo. 1994-402 (1994).


72 PROP. TAX CT. R. 152(b).


74 Tax Ct. R. 20.

75 Id.

76 Tax Ct. Form 6 ( Ownership Disclosure Statement).


78 Fed. R. Civ. P. 5(b), Committee Note—2018 Amendment.

79 PROP. TAX CT. R. 21.

80 Code Sec. 7456(a)(1); Tax Ct. R. 147.
81 Fed. R. Civ. P. 45(c)(1), (2).
84 Fed. R. Civ. P. 45(a)(4); Tax Ct. R. 147(c) (no notice is required when a party serves a subpoena to a third party for documents).
85 Tax Ct. R. 25 (providing that parties serve on other parties or other persons involved in the matter all filed paper, including “pleadings, motions, orders, decisions, notices, demands, briefs, appearances, or other similar documents or papers relating to a case ….”).
87 122 TCM 25, Dec. 61,900(M), TC Memo. 2021-88.
88 Order, dated July 8, 2016, TC No. 14619-10.
89 Fed. R. Civ. P. 45 (1970). The notice requirement was added in 1991 to give parties the same opportunity to challenge nonparty subpoenas for documents that they had to challenge subpoenas for depositions (since FRCP 30 and 31 already provided notice protection in these circumstances). See Fed. R. Civ. P. 45, Advisor Committee’s Notes (1991).
90 The ABA Tax Section previously proposed that Tax Court Rule 47 should be amended to align with the notice requirements in FRCP 45. See Letter from George C. Howell III, Chair, Section of Taxation, American Bar Association, to Hon. Michael B. Thornton, Chief Judge, U.S. Tax Court (November 10, 2015) www.ustaxcourt.gov/resources/rules/suggestions/ABA_Tax_Section_11-10-15.pdf.
91 See Order Granting Petitioner’s Motion to Compel, dated July 15, 2015, in A.M. Kissling, 120 TCM 314, Dec. 61,775(M), TC Memo. 2020-153, TC No. 19857-10 (“We do have to disagree with the Commissioner, however, that this absence of a rule creates an implication that secret subpoenas are favored … The Court will therefore adopt the notification requirement of Federal Rule 45 as a modification to the pretrial order that governs this case.”). But see Order Denying Petitioner’s Motion to Compel, dated December 2, 2016, in E.J. Tangel, 121 TCM 1001, Dec. 61,802(M), TC Memo. 2021-1, TC No. 27268-13 (“A party that issues a subpoena under Rule 147(a) and/or (b) is not required to give prior notice to the other party.”).
94 Letter from Julie A. Divola, Chair, Section of Taxation, American Bar Association, to Hon. Maurice Foley, Chief Judge, U.S. Tax Court (May 25, 2022) www.americanbar.org/content/dam/aba/administrative/taxation/policy/2022/052522comments.pdf.
95 Id.
96 T.J. Durkin, 87 TC 1329, Dec. 43,548, 1401–03 (1986), aff’d, CA-7, 89-1 USTC ¶9277, 872 F2d 1271; Tax Ct. R. 147(b).
97 Tax Ct. R. 147(b).
99 Branerton Corp., 61 TC 691, Dec. 32,479 (1974) (“The discovery procedures should be used only after the parties have made reasonable informal efforts to obtain needed information voluntarily.”); Tax Ct. R. 70-74, 80.
100 Tax Ct. R. 70(a)(1).
101 Tax Ct. R. 70(b) and 101.
Memorandum from Hon. David G. Campbell to Hon. Jeffrey Sutton at 7 (June 14, 2014). The majority of the factors were added to FRCP 26(b)(1) in 1983. In 1993, the proportionality language was revised and moved to FRCP 26(b)(2)(C) in conjunction with dividing section (b)(1).

PRO. TAX CT. R. 70(d).

PRO. TAX CT. R. 70(d)(1); FED. R. CIV. P. 26(b)(5)(A).

PRO. TAX CT. R. 70(d); FED. R. CIV. P. 26(b)(5)(B) (providing a procedure under which a party may claim that information requested in the course of discovery is privileged).

PRO. TAX CT. R. 70(d)(2); FED. R. CIV. P. 26(b)(5)(B).

PRO. TAX CT. R. 70(d)(2); FED. R. CIV. P. 26(b)(5)(B).

PRO. TAX CT. R. 70(d)(2); FED. R. CIV. P. 26(b)(5)(B).