No. 12-1085

In the Supreme Court of the United States

MARK CURCIO, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

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

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether the court of appeals correctly applied a clear-error standard of review to the Tax Court's determination that contributions to a purported welfare benefit plan were not "ordinary and necessary" business expenses under 26 U.S.C. 162(a), and that petitioners' businesses therefore were not entitled to deduct the contributions for federal income tax purposes.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-22a) is reported at 689 F.3d 217. The opinion of the Tax Court (Pet. App. 23a-76a) is unreported but is available at T.C. Memo. 2010-115 and 2012 WL 2134321.

JURISDICTION

The judgment of the court of appeals was entered on August 9, 2012. A petition for rehearing was denied on December 7, 2012 (Pet. App. 91a-92a). The petition for a writ of certiorari was filed on March 5, 2013. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. Petitioners are business owners who, through their business entities (S corporations and, in one instance, a partnership), made contributions to a purported welfare benefit plan known as Benistar 419 Plan (the

Plan). Their business entities claimed tax deductions for the contributions. Pet. App. 1a-3a. The Plan was designed to be a multiple-employer welfare benefit plan under 26 U.S.C. 419A(f)(6) providing pre-retirement life insurance to covered employees. Pet. App. 2a. Companies that enroll in the Plan contribute funds to a trust account, maintained by the Plan, that is intended to fund the death benefits provided by the Plan. The Plan uses these contributions to acquire one or more life insurance policies on employees covered by the Plan, and it withdraws funds from the trust account to pay the premiums on those policies. *Id.* at 2a-3a.

Although the Plan is required to pay death benefits in the event of a covered employee's death, and although the Plan purportedly acquires life insurance policies to fund these benefits, the employees themselves determine the type of insurance used to fund their benefits. Pet. App. 3a. The employees select the insurance carrier and the benefit amount, and they decide whether the Plan will purchase term, whole, universal, or variable life insurance to fund their benefits. *Id.* at 29a. When an employer enrolls in the Plan, a prospective insured employee's insurance agent prepares and sends an insurance policy application to an insurance company for the size and type of policy desired by the employee, obtains a commitment from the insurance company, and informs the Plan of the amount of the premiums. C.A. App. 1500-1502, 1504-1508. The Plan then bills the employers, collects contributions, and pays the policy premiums. Pet. App. 27a, 33a.

Petitioners, working with their individual insurance agents, enrolled in the Plan and selected insurance policies to fund their benefits under the Plan. Pet. App. 4a-8a. Petitioners' businesses made contributions to the

Plan to pay the insurance policy premiums, and the businesses claimed deductions for the contributions as expenses of funding welfare benefits for an employee. *Ibid.* The only employees enrolled in the Plan by the businesses owned by petitioners Curcio, Jelling, and Smith were Curcio, Jelling, and Smith themselves. Petitioner Mogelefsky's business enrolled only Mogelefsky and his stepson. *Ibid.*

b. The Internal Revenue Service (IRS) issued notices of deficiency disallowing the deductions claimed by petitioners' businesses for the contributions to the Plan. The IRS determined that those contributions were not deductible because they were not ordinary and necessary expenses incurred in carrying on a trade or business under 26 U.S.C. 162(a), and, alternatively, that payments to the Plan were not deductible contributions to a multiple-employer welfare benefit plan under 26 U.S.C. 419A(f)(6). C.A. App. 1065. The IRS further determined that one of the contributions made to the Plan by petitioner Mogelefsky's business was a constructive dividend to him. Pet. App. 8a-9a.

The denial of the deductions increased petitioners' reported flow-through income from their business entities. As a result, the IRS determined income tax deficiencies against petitioners Curcio and Jelling for tax year 2001-2004, and against petitioners Smith and Mogelefsky for tax year 2003. Pet. App. 24a-25a. The IRS also assessed accuracy-related penalties under 26 U.S.C. 6662(a) against each of the petitioners. Pet. App. 24a-25a. Petitioners filed petitions in the Tax Court challenging the IRS's determinations, and the cases were consolidated. *Id.* at 23a.

2. After a trial, the Tax Court ruled in favor of the government. Pet. App. 23a-76a. The court rejected

petitioners' argument that their businesses' contributions to the Plan were deductible as "ordinary and necessary expenses" of a business under 26 U.S.C. 162(a). Pet. App. 48a. The Tax Court explained that an expense is deductible under Section 162(a) if it (1) was paid or incurred during the taxable year; (2) was for carrying on a trade or business; (3) was an expense; (4) was necessary; and (5) was an ordinary expense. *Id.* at 51a. The court stated that "[d]etermining whether an expenditure satisfies each of these requirements involves a question of fact." *Ibid.* (citing *Commissioner* v. *Heininger*, 320 U.S. 467, 475 (1943)).

The Tax Court noted that the contributions petitioners' businesses had made to the Plan "were far in excess of the annual cost of term life insurance coverage," and that the court was required to "consider why petitioners would pay such excess amounts and whether those contributions were ordinary and necessary business expenses or payments to petitioners personally." Pet. App. 53a. The court explained that the excess payments "are of particular concern here, where the participating companies made contributions exclusively on behalf of their owners that were distributable to the owners at no or low cost." *Id.* at 54a.

The Tax Court observed that, although petitioners' businesses had many employees, Curcio and Jelling's businesses had enrolled only Curcio and Jelling in the Plan, Smith's business had enrolled only Smith, and Mogelefsky's business had enrolled only Mogelefsky and his stepson. Pet. App. 38a-39a, 42a-43a, 44a-45a. The court explained that the purpose of Curcio and Jelling's enrollment was to fund a buy-sell agreement between them that stipulated that if one partner died, the other would buy the deceased partner's stake in their busi-

nesses. *Id.* at 39a. Their life insurance policies named each other as the beneficiaries and were designed to ensure that each would have sufficient liquidity to purchase the other's share. *Ibid.* The court further noted that Smith had stated in his insurance application that the purpose of the insurance was "retirement planning," *id.* at 59a, that Smith and Mogelefsky had terminated their participation three years after they enrolled, and that Smith had later made a withdrawal and had taken a loan from his policy. *Id.* at 44a, 46a-47a.

The Tax Court explained that "[p]etitioners acted as though they owned personally both their Benistar policies and the underlying policies," Pet. App. 58a, and that "Benistar Plan itself promoted the implication that it was merely a conduit to the underlying policies and not the actual insurer," *id.* at 59a. The court also explained that before 2002, "Benistar Plan would distribute the underlying insurance policies to covered employees for free," and that after 2002, "Benistar Plan would charge a withdrawal fee * * * lower than 10 percent," which was far lower than the applicable federal interest rates during the relevant period. *Id.* at 61a, 64a. The court explained that petitioners therefore "could easily retrieve the value in those policies with minimal expense." *Id.* at 64a.

The Tax Court stated that, "[a]fter considering the facts and weighing the evidence, we conclude * * * that contributions to Benistar Plan were payments on behalf of petitioners personally and were not ordinary and necessary business expenses under [S]ection 162(a)." Pet. App. 64a. The court explained that "[t]he level of control that covered employees exerted over their underlying policies, the degree to which contributions to Benistar Plan were structured around those

underlying policies, and the means through which covered employees could procure a distribution of those underlying policies all lead us to conclude that Benistar Plan is a thinly disguised vehicle for unlimited tax-deductible investments." *Id.* at 64a-65a. The court stated that its decision "turn[ed] on [its] factual findings regarding the mechanics of [the] Plan and [its] conclusion that petitioners had the right to receive the value reflected in the underlying insurance policies." *Id.* at 48a.

Because the Tax Court concluded that the businesses' contributions to the Plan were not ordinary and necessary business expenses, the court did not reach the IRS's alternative determination that, as a matter of law, the Plan did not qualify under 26 U.S.C. 419A(f)(6) as a multiple-employer welfare benefit plan. Pet. App. 49a. The Tax Court further held that accuracy-related penalties were properly determined against petitioners. *Id.* at 70a-76a.

3. The court of appeals affirmed. Pet. App. 1a-22a. The court stated that "[w]hether an expense is 'ordinary and necessary' within the meaning of [Section] 162(a) is a 'pure question[] of fact in most instances,'" and that it would accordingly review the Tax Court's determination for clear error "[u]nless 'a question of law is unmistakably involved.'" *Id.* at 13a (quoting *Heininger*, 320 U.S. at 475). The court further stated that the determination that a taxpayer is liable for an accuracy-related penalty is also a factual finding reviewed for clear error. *Id.* at 13a-14a.

The court of appeals held that the Tax Court had not clearly erred when it found that the expenditures at issue in this case were not ordinary and necessary business expenses. Pet. App. 14a. The court explained that

"[e]xpenditures may only be deducted under [26 U.S.C.] 162 if the facts and the circumstances indicate that the taxpayer made them primarily in furtherance of a bona fide profit objective independent of tax consequences." *Id.* at 10a (quoting *Green* v. *Commissioner*, 507 F.3d 857, 871 (5th Cir. 2007)). The court explained that "[t]he record supports the conclusion that the contributions [to the Plan] were not normal, usual, or 'helpful for the development of the [taxpayers'] business.'" *Id.* at 14a (quoting *Commissioner* v. *Tellier*, 383 U.S. 687, 689 (1966)). "Rather," the court concluded, "the evidence demonstrates that the contributions were made solely for the personal benefit of petitioners." *Id.* at 14a-15a.

The court of appeals further explained: "We do not hold that purchasing a life insurance policy with a cash component can never be an ordinary and necessary business expense. Such a determination is fact intensive and must be made on a case by case basis." Pet. App. 17a. The court concluded that "[i]n this case, where petitioners could withdraw from the Plan at any time and obtain personal control over cash-laden policies, and where other evidence in the record demonstrates that the taxpayers contributed to the Plan solely for their personal benefit, the tax court did not clearly err in finding that the contributions were not ordinary and necessary business expenses." *Ibid.*

ARGUMENT

Petitioners contend (Pet. 15-22) that the court of appeals should have applied *de novo* rather than clear-error review to the Tax Court's determination that contributions by their businesses to a purported welfare-benefit plan were not ordinary and necessary business expenses under 26 U.S.C 162(a). The court of appeals applied the appropriate standard of review, and its deci-

sion does not conflict with any decision of this Court or another court of appeals. Further review is not warranted.

1. a. Section 419 of Title 26 establishes rules governing the *amount* of the deduction that may be taken for employer contributions to a welfare benefit plan. See, *e.g.*, 26 U.S.C. 419(b). Section 419 itself, however, does not render such expenditures deductible in the first instance. Rather, contributions paid by a business to a welfare benefit plan are deductible from income only "if they would otherwise be deductible," 26 U.S.C. 419(a)(2); see Pet. App. 48a—*i.e.*, if they qualify for a deduction under an Internal Revenue Code provision other than Section 419. Petitioners contend that the contributions at issue here are deductible under 26 U.S.C. 162(a), which provides that "[t]here 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." See 26 C.F.R. 1.162-10 (1960) ("Amounts paid or accrued within the taxable year for * * * medical expense, recreational, welfare, or similar benefit plan, are deductible under section 162(a) if they are ordinary and necessary expenses of the trade or business").

For a payment to be deductible under 26 U.S.C. 162(a), it must "(1) be paid or incurred during the taxable year, (2) be for carrying on any trade or business, (3) be an expense, (4) be a necessary expense, and (5) be an ordinary expense." *Commissioner* v. *Lincoln Sav. & Loan Ass'n*, 403 U.S. 345, 352 (1971) (quotation marks omitted)). An "ordinary" expense is one that is "of common or frequent occurrence in the type of business involved." *Deputy* v. *du Pont*, 308 U.S. 488, 495 (1940). A "necessary" expense is one that is "appropriate and

helpful" for the taxpayer's business. *INDOPCO, Inc.* v. *Commissioner*, 503 U.S. 79, 83 (1992) (citation omitted). In *Commissioner* v. *Heininger*, 320 U.S. 467 (1943), the Court stated that "[e]xcept where a question of law is unmistakably involved," the question "[w]hether an expenditure is directly related to a business and whether it is ordinary and necessary are doubtless pure questions of fact in most instances." *Id.* at 475.

The factual nature of the Section 162(a) inquiry was well-settled even before *Heininger*. In *Welch* v. *Helvering*, 290 U.S. 111 (1933), the Court (applying a prior version of 26 U.S.C. 162(a)) explained that a taxpayer may prove that an expense is "necessary for the development of the [taxpayer's] business" by demonstrating that the expense is "appropriate and helpful," and that an assessment of whether an expense is "ordinary," is "a variable affected by time and place and circumstance." *Id.* at 113-114. The court stated that "[t]he standard set up by the statute is not a rule of law; it is rather a way of life. Life in all its fullness must supply the answer" to what is "ordinary." *Id.* at 115.

The Court further elaborated on the factual nature of the inquiry in *du Pont*, *supra*. In *du Pont*, the Court explained that "[o]rdinary has the connotation of normal, usual, or customary * * * [and] the fact that a particular expense would be an ordinary or common one in the course of one business and so deductible * * * does not necessarily make it such in connection with another business." 308 U.S. at 495. Rather, the Court stated, "[i]t is the kind of transaction out of which the obligation arose and its normalcy in the particular business which are crucial and controlling." *Id.* at 496. The Court observed that review of prior cases deciding

whether an expense is ordinary therefore "is of little aid since each turns on its special facts." *Ibid.*

Factual determinations made by a district court in civil litigation are reviewed for clear error. See Fed. R. Civ. P. 52(a)(6). Decisions of the Tax Court are reviewed using the same standard that would apply to review of any particular issue in a district court. See 26 U.S.C. 7482(a)(1). The court of appeals therefore correctly reviewed for clear error the Tax Court's factual determination that the contributions made by petitioners' businesses to the Plan were not ordinary and necessary business expenses for purposes of Section 162(a).

b. Petitioners contend (Pet. 18-19) that the question whether the contributions to the Plan were deductible as ordinary and necessary business expenses is a mixed question of law and fact that should have been reviewed *de novo* by the court of appeals. That is incorrect.

A mixed question of law and fact is one "in which the historical facts are admitted or established, the rule of law is undisputed, and the issue is whether the facts satisfy the statutory standard, or to put it another way, whether the rule of law as applied to the established facts is or is not violated." *Pullman-Standard* v. *Swint*, 456 U.S. 273, 289 n.19 (1982). But the Tax Court in this case was not simply taking undisputed facts and testing them against a settled legal standard. To determine whether the contributions to the Plan were ordinary and necessary business expenses under Section 162(a), the Tax Court analyzed historical facts and weighed the statements made in documents and testimony to draw conclusions about whether enrollment in the Plan was intended to help petitioners' businesses, or instead to benefit petitioners personally. That is precisely the type

of determination that the Court in *Heininger* described as "[a] pure question[] of fact." 320 U.S. at 475.

Furthermore, even if the question whether a particular expenditure is an ordinary and necessary business expense under Section 162(a) were a mixed question of law and fact, as petitioners contend, a clear-error standard would nevertheless be appropriate under this Court's precedents. Petitioners are correct (Pet. 17-18) that *de novo* appellate review applies to *some* mixed questions of law and fact, such as the existence of probable cause or reasonable suspicion, the voluntariness of a confession, and a state court's conclusion about whether counsel in a criminal case was constitutionally ineffective. This Court's decisions make clear, however, that the standard of review to be applied to mixed questions of law and fact will vary depending on the issue.

In *Salve Regina College* v. *Russell*, 499 U.S. 225 (1991), the Court stated that deferential review of mixed questions of law and fact is appropriate when "it appears that the district court is 'better positioned' than the appellate court to decide the issue" or when "probing appellate scrutiny will not contribute to the clarity of legal doctrine." *Id.* at 233; see *Cooter & Gell* v. *Hartmarx Corp.*, 496 U.S. 384, 402 (1990) ("[T]he district court is better situated than the court of appeals to marshal the pertinent facts and apply the fact-dependent legal standard mandated by Rule 11."). That is true here. The Tax Court, given its greater familiarity with the evidence and witnesses in a trial that it conducted, was in a better position than the court of appeals to assess the purpose served by the enrollment of petitioners' businesses in the Plan. And, given the fact-specific nature of the inquiry, which here turned in part on idiosyncratic factors such as the fact that the Plan

provided life insurance benefits only to petitioners themselves and to petitioner Mogelefsky's stepson, "probing appellate scrutiny" would not have "contribute[d] to the clarity of legal doctrine." *Salve Regina*, 499 U.S. at 233; see *du Pont*, *supra*, 308 U.S. at 496 (explaining that review of prior cases deciding whether an expense is ordinary "is of little aid since each turns on its special facts").[1]

The Court has also applied deferential review in cases "present[ing] a mixed question of law and fact [where] 'the mix weighs heavily on the "fact" side.'" *Brown* v. *Plata*, 131 S. Ct. 1910, 1932 (2011) (quoting *Lilly* v. *Virginia*, 527 U.S. 116, 148 (1999) (Rehnquist, C.J., concurring in judgment)). That is the case here, where the Tax Court's decision "turn[ed] on [its] factual findings regarding the mechanics of [the] Plan and [its] conclusion that petitioners had the right to receive the value reflected in the underlying insurance policies." Pet. App. 48a. Use of a clear-error standard of review therefore would be appropriate even if the underlying "ordinary and necessary" issue were properly characterized as a mixed question of law and fact.

2. Petitioners contend (Pet. 15-22) that the court of appeals' application of a clear-error standard of review conflicts with this Court's decision in *Frank Lyon Co.* v. *United States*, 435 U.S. 561 (1978), and is based on deci-

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[1] Petitioners observe that this is a "test case[]" that was intended to determine the outcome of other disputes where taxpayers claimed deductions for contributions made to the Benistar 419 Plan. Pet. 18 n.10 (citation omitted). But the fact that many taxpayers participated in this particular Plan and claimed tax deductions for their contributions does not undermine the conclusion that the district court is "'better positioned' than the appellate court to decide the issue." *Salve Regina*, 499 U.S. at 233.

sions of this Court that are no longer good law. Petitioners misunderstand those precedents.

a. The issue in *Frank Lyon* concerned the federal income tax consequences of a sale-and-leaseback agreement in which Frank Lyon Company took title to a building from Worthen Bank & Trust Company and simultaneously leased the building back to Worthen. 435 U.S. at 562. Frank Lyon filed a federal income tax return claiming deductions for various expenses incurred in connection with the transaction. *Id.* at 568. Although the IRS had determined that Frank Lyon was not the owner of the building for tax purposes and that the expenses therefore were not deductible, the district court concluded that the deductions were allowable because the legal intent of the parties was to create a bona fide sale-and-leaseback agreement and the rents were reasonable throughout the periods of the lease. *Id.* at 568-570. The court of appeals reversed, explaining that it had "undert[aken] its own evaluation of the facts" and had concluded that Frank Lyon was not the true owner of the building for tax purposes. *Id.* at 570.

This Court reversed, explaining that the court of appeals' analysis of the ownership issue was based on "speculation" that Worthen would exercise a purchase-option. *Frank Lyon*, 435 U.S. at 581. The Court stated that it "[could] not indulge in such speculation in view of the District Court's clear finding to the contrary." *Id.* at 581. The Court observed in that regard that although "[t]he general characterization of a transaction for tax purposes is a question of law subject to review," "[t]he particular facts from which the characterization is to be made are not so subject." *Id.* at 581 n.16. That passage indicates that the Court viewed the district court's conclusion about the nature of the transaction as a *factual*

determination, not as the resolution of a mixed question of fact and law subject to *de novo* review. The factual question resolved by the district court in *Frank Lyon* (whether the sale-and-leaseback transaction was a sham) is similar to the factual question resolved by the Tax Court in this case (whether contributions to the Plan were for business purposes or for petitioners' personal gain). The Court's decision in *Frank Lyon* is thus fully consistent with the court of appeals' application of a clear-error standard of review in this case.

The Court in *Frank Lyon* recognized that acceptance of the sale-and-leaseback arrangement as a non-sham transaction did not "automatically compel the further conclusion that [Frank Lyon] is entitled to the items claimed as deductions." 435 U.S. at 580.[2] The Court explained, however, that the conclusion as to deductibility "readily follow[ed]" from the facts. *Ibid.* The same is true in this case. The court of appeals properly reviewed for clear error the Tax Court's factual determination that the Plan contributions were not ordinary and necessary business expenses. Once that determination had been sustained, the conclusion that the contributions therefore were not deductible under Section 162(a) "readily followed."

b. Petitioners contend (Pet. 18-19, 21) that this Court's decision in *Heininger*, *supra*, has been "eroded" or "overridden" by the enactment of 26 U.S.C. 7482. Petitioners' reliance on Section 7482 is misplaced.

By enacting Section 7482, Congress overruled the Court's holding in *Dobson* v. *Commissioner*, 320 U.S.

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[2] That further conclusion is perhaps what the Court referred to as "[t]he general characterization of a transaction for tax purposes" subject to review as a question of law. *Frank Lyon*, 435 U.S. at 581 n.16.

489 (1943), that a decision of the Tax Court must be upheld unless there is a "clear-cut mistake of law." *Id.* at 501-502. That statement implied that, even where purely legal rulings were concerned, Tax Court decisions were entitled to appellate deference rather than reviewed *de novo*; and it could be read to state that the Tax Court's factual findings were not subject to appellate review at all. Both of those limitations would constitute departures from the principles that generally govern appellate review of trial court decisions. Section 7482 directs the courts of appeals to review Tax Court decisions "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." 26 U.S.C. 7482(a)(1). This Court has already recognized that *Dobson* "is, of course, no longer the law insofar as it ordains a greater weight to be attached to the findings of the Tax Court than to those of any other fact-finder in a tax litigation." *Commissioner* v. *Duberstein*, 363 U.S. 289 n.11 (1960). Accordingly, there is no need for this Court to grant certiorari to clarify that *Dobson* has been superseded by statute. See Pet. 20.

Section 7482 does not, however, "erode[]" or "override[]" *Heininger*. Pet. 18-19. In holding that a deferential standard of review should be applied to a Tax Court determination that a particular expenditure is or is not an ordinary and necessary business expense, the Court in *Heininger* did not rely on the Tax Court's special expertise on that subject, or on any other factor specific to the Tax Court. Rather, the Court stated in *Heininger* that such a determination is a finding of fact. 320 U.S. at 475. Once that characterization was established, the conclusion that the Tax Court's finding

should be reviewed deferentially represented a routine application of general principles of appellate review.

Nothing in Section 7482 undermines any aspect of the *Heininger* Court's reasoning. Section 7482 does not speak to whether an "ordinary and necessary expense[]" determination is properly viewed as a finding of fact or as a legal conclusion. The *Heininger* Court's holding that the determination is one of fact therefore remains good law. And, as explained above (see p. 10, *supra*), factual findings made by a district court in a civil case tried without a jury are reviewed for clear error. Section 7482's directive that Tax Court decisions are reviewable "in the same manner and to the same extent" thus confirms that the Tax Court determination at issue here should be reviewed under a clear-error standard.

3. Petitioners contend (Pet. 12-14) that the courts of appeals are in conflict on the standard of review that should be applied to the Tax Court's determination whether an expense was ordinary and necessary under Section 162(a). That is incorrect.

Petitioners contend (Pet. 12-13) that the Sixth Circuit reviews "ordinary and necessary" determinations by the Tax Court *de novo*. The decisions petitioners cite do not support that characterization. *The Limited, Inc.* v. *Commissioner*, 286 F.3d 324 (6th Cir. 2002) was not a Section 162(a) case. Rather, it involved "the Tax Court's legal interpretation of the phrase 'deposit with persons carrying on the banking business' as used in [26 U.S.C.] 956(b)(2)(A)." *Id.* at 331. The court stated that "[b]ecause this challenge involves an interpretation of law, we review the Tax Court's decision *de novo*." *Id.* at 331-332.

The other two Sixth Circuit cases that petitioners cite involved undisputed facts, see *Malone & Hyde, Inc.* v. *Commissioner*, 62 F.3d 835, 836 (6th Cir. 1995) ("[t]he

facts were stipulated"); *Mitchell* v. *Commissioner*, 73 F.3d 628, 631 (6th Cir. 1996) ("[t]he facts are uncontroverted")), and the court stated that the application of law to uncontroverted facts is reviewed *de novo*. *Malone & Hyde, Inc.*, 62 F.3d at 838; *Mitchell*, 73 F.3d at 631. Those cases do not show that the Sixth Circuit takes a different approach from other courts of appeals in reviewing Section 162(a) determinations made by the Tax Court. Indeed, in *Car-Ron Asphalt Paving Co.* v. *Commissioner*, 758 F.2d 1132 (1985), a case involving the question whether kickbacks in return for construction bids were ordinary and necessary business expenses under Section 162(a), the Sixth Circuit noted that the Tax Court had "found, as a matter of fact, that the kickbacks were not necessary," and it concluded that "[t]his finding [was] not clearly erroneous." *Id.* at 1134.

Petitioners contend (Pet. 13-14) that the Ninth and Tenth Circuits vary the standard of review for Section 162(a) issues depending on whether factual or legal issues predominate. In the decisions petitioners cite, the courts considered whether the specific question before them was predominantly a legal or a factual issue, and then applied the appropriate standard of review. In *Kurzet* v. *Commissioner*, 222 F.3d 830 (10th Cir. 2000), for example, the court explained that the parties' dispute concerned the Tax Court's conclusion that expenses for a private jet were not reasonable business expenses, and the court concluded that this was a factual determination that it would review for clear error. *Id.* at 834.

In contrast, those courts have concluded that other issues presented in Section 162(a) cases were legal rather than factual, and they accordingly reviewed the Tax Court's decisions *de novo*. In *Moss* v. *Commissioner*,

831 F.2d 833 (9th Cir. 1987), the court explained that certain Tax Court findings, to the effect that the taxpayers "had a plan of capital improvements for [their] Hotel" and that "the expenditures at issue were part of that plan," involved historical facts and therefore were subject to clear-error review. *Id.* at 838. The court observed, however, that those facts "[we]re not in dispute." *Ibid.* The court then addressed the taxpayers' argument that the Tax Court had "misinterpreted the rehabilitation doctrine in applying it to the facts as stipulated by the parties" to determine whether those expenses were deductible. *Ibid.* The court concluded that this was a legal determination that should be reviewed *de novo*. *Ibid.*

In *Pollei* v. *Commissioner*, 877 F.2d 838 (10th Cir. 1989), the court explained that the factual record was not controverted, and that the primary dispute between the parties—*i.e.*, whether a police officer is commuting (and thus his expenses are not deductible) or on duty (and thus his expenses are deductible) when he is driving to work—was a legal question that the court would review *de novo*. *Id.* at 839-840. And in *Colorado Springs National Bank* v. *United States*, 505 F.2d 1185 (10th Cir. 1974), the court concluded that the question whether start-up costs for *entry* into a business were deductible as ordinary and necessary business expenses under Section 162(a) was not a factual question but a legal question subject to *de novo* review. *Id.* at 1188-1189.

The Ninth and Tenth Circuit decisions that petitioners cite do not reflect confusion or internal inconsistency within those courts' jurisprudence. Rather, they simply reflect the unsurprising fact that Section 162(a) cases, like other civil actions, are *capable* of presenting both

legal and factual issues. Those decisions are consistent with the analysis of the court below, which explained that it would apply clear-error review to the Tax Court's determination "[u]nless 'a question of law is unmistakably involved.'" Pet. App. 13a (quoting *Heininger*, 320 U.S. at 475). Petitioners have identified no legal issue involved in this case that is separate from the Tax Court's factual determination that the contributions made by petitioners' businesses to the Plan were not ordinary and necessary business expenses under Section 162(a) because those expenditures were intended to benefit petitioners personally rather than to benefit the businesses.

4. Finally, this case would be a poor vehicle in which to review the question presented. Contrary to petitioners' assertion (Pet. 26-32), the outcome here would have been the same regardless of the standard of review applied. As the court of appeals observed, evidence in the record such as the deposition testimony of Plan creator Daniel Carpenter, the Plan Brochure, and "[e]vidence pertaining to the individual owners" firmly demonstrates that "the Plan was designed to benefit only owners and their families and not the businesses." Pet. App. 15a. Contributions to the plan therefore were for petitioners' "personal benefit, not the benefit of their respective business entities." *Ibid.* The conclusion that contributions to the Plan are not deductible as ordinary and necessary business expenses "readily follows" from that evidence, *Frank Lyon*, 435 U.S. at 580, and *de novo* review by the court of appeals would have yielded the same result.

Furthermore, the arguments that petitioners present in support of their position that *Heininger* is no longer good law, and that *de novo* review should be applied to

the Tax Court's Section 162(a) determinations, were not presented to or considered by the court of appeals. In their opening brief in the Second Circuit, petitioners stated that the court of appeals, "as a general rule, reviews the Tax Court's legal conclusions *de novo* and its factual findings for clear error. However, when there are mixed questions of law and fact, as there are here, the review is *de novo*." Pet. C.A. Br. 32 (citations omitted). Petitioners did not elaborate on their assertion that this case presents a mixed question of law and fact.

The government argued in response that whether an amount paid by a business entity is an ordinary and necessary business expense under 26 U.S.C. 162(a) is a question of fact reviewed for clear error. Resp. C.A. Br. 39 (citing, *inter alia*, *Heininger*, *supra*). Petitioners did not address the standard of review in their reply brief, nor did their petition for rehearing assert any challenge to the court of appeals' application of a clear-error standard. The Court should not review the question presented in a case where petitioners' arguments for a *de novo* standard of review are presented for the first time in their petition for a writ of certiorari.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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