No. 12-12169-BB

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

PECO FOODS, INC. & SUBSIDIARIES,

Petitioner-Appellant

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee

ON APPEAL FROM THE DECISION OF
THE UNITED STATES TAX COURT

BRIEF FOR THE APPELLEE

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Peco Foods, Inc. & Subsidiaries, et al. v. Commissioner
(11th Cir. No. 12-12169-BB)

CERTIFICATE OF INTERESTED PARTIES AND CORPORATE DISCLOSURE STATEMENT

Pursuant to Local Rule 28.1, it is hereby certified that the following persons and entities have an interest in the outcome of this case or have participated as attorneys or judges in the adjudication of this case:

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Ellisen, Bruce R., Reviewer, Appellate Section, Tax Division, Department of Justice

Goldman, Richard, Branch Chief, Procedure & Administration, Internal Revenue Service

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Laro, David, Judge, United States Tax Court

McClendon, W. Benjamin, Attorney, Internal Revenue Service

Peco Foods, Inc. & Subsidiaries, et al. v. Commissioner
(11th Cir. No. 12-12169-BB)

CERTIFICATE OF INTERESTED PARTIES AND CORPORATE DISCLOSURE STATEMENT (continued)

Rice, John S., Attorney for Appellant, Perkins, Williams, Rice, PLLC

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STATEMENT REGARDING ORAL ARGUMENT

Counsel for the Commissioner believes that oral argument may be useful to aid the Court's disposition of this appeal.

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STATEMENT OF JURISDICTION

Peco Foods, Inc. & Subsidiaries (taxpayer) appeals from the decision of the Tax Court (Judge Laro) upholding the Commissioner's determination of income-tax deficiencies. (Doc. 72.)[1] The court had jurisdiction under Section 6213 of the Internal Revenue Code (I.R.C.) (26 U.S.C.), because taxpayer filed a timely petition for redetermination within 90 days of the mailing of the notice of deficiency authorized by I.R.C. § 6212(a). (R. 1.) The Tax Court entered its decision in favor of the Commissioner on January 19, 2012 (R. 72), and taxpayer filed a notice of appeal on April 17, 2012 (R. 73), which was timely under I.R.C. § 7483. This Court, therefore, has appellate jurisdiction under I.R.C. § 7482(a)(1).

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[1] "R." references are to the record, as compiled by the Clerk of the Tax Court. "Ex." references are to the exhibits admitted in that court. "Tr." references are to the trial transcript. "Br." references are to appellant's brief.

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v.

COMMISSIONER OF INTERNAL REVENUE,

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ON APPEAL FROM THE DECISION OF THE UNITED STATES TAX COURT

BRIEF FOR THE APPELLEE

STATEMENT OF THE ISSUE

In 1995 and 1998, taxpayer entered into two asset-purchase agreements to buy poultry-processing facilities in Sebastopol and Canton, Mississippi. Each of the agreements contained, *inter alia*, an allocation schedule, which assigned portions of the total purchase price to various listed assets. Beginning in its federal income tax return for the tax year ending April 3, 1999, however, taxpayer adopted a position

inconsistent with the allocations in the agreements. Instead, taxpayer reallocated part of the purchase price to assets not listed in the original allocation schedules, which often had a considerably shorter depreciation recovery period. Taxpayer claimed both a sizable tax adjustment under I.R.C. § 481(a) and depreciation deductions for that and following tax years based on the effect of the reallocation on its depreciation calculations. The question presented on appeal is whether the Tax Court correctly concluded that taxpayer was bound to the allocation schedules provided in the agreements, and could not unilaterally deviate from them to obtain tax benefits.

STATEMENT OF THE CASE

A. Course of proceedings and disposition in the Tax Court

Taxpayer brought suit challenging the Commissioner's determinations as to the correct treatment of certain asset allocations arising out of purchases of assets in 1995 and 1998. (R. 1.) The case proceeded to trial (R. 58), and the Tax Court upheld the Commissioner's determinations (R. 70). The court thereafter entered a

decision consistent with its opinion (R. 71), and taxpayer appealed (R. 73).

B. Statement of facts

Taxpayer is an Alabama corporation engaged in the poultry-processing business, overseeing chickens from egg until market. (Tr. 25-26.) Taxpayer has three subsidiaries: Peco Farms, Inc.; Peco Foods of Mississippi, Inc.; and Peco Foods of Brooksville, Inc. (R. 1.) In 1995 and 1998, taxpayer entered into asset-purchase agreements to buy poultry-processing facilities in Sebastopol, Mississippi, and Canton, Mississippi, respectively. (Exs. 7-J, 8-J.) This case focuses on taxpayer's attempts to vary, for tax purposes, from the purchase-price allocations set forth in the asset-purchase agreements.

1. Asset-purchase agreements

a. Sebastopol

In 1995, taxpayer contracted with Green Acre Farms, Inc., to acquire its assets, including buildings, real property, machinery, equipment, and its poultry flock, for a total payment of $27,500,000. (R. 18, ¶ 30; Ex. 7-J.) The agreement, which was governed by

Mississippi law, contained a provision prohibiting any amendment to the agreement, except to the extent that such an amendment was in writing and signed by both parties. (Ex. 7-J at 27.)

The agreement further incorporated certain schedules and exhibits. (Ex. 7-J at 28.) One of the schedules incorporated by the parties was entitled "Allocation Schedule," which allocated the purchase price, by asset, between two of taxpayer's subsidiaries. (*Id.* at Ex. D.) This schedule allocated portions of the purchase price to 26 different assets, and the parties agreed that this allocation would be used "for all purposes (including financial accounting and tax purposes)." (Ex. 7-J at 7.) The parties allocated, *inter alia*: (i) $3,802,550 to "Processing Plant Bld"; (ii) $64,800 to "Holding Shed #1"; (iii) $75,395 to "Holding Shed #2"; (iv) $1,879,545 to "Waste Water TP"; (v) $5,964,140 to "Machinery & Equip"; and (vi) $100,620 to "Furniture & Equip." (*Id.*)[2] Taxpayer relied on an appraisal from PayneSmall Investment Property Appraisals, an appraiser that it had

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[2] "Bld" in the allocation schedule was an abbreviation for building (*e.g.*, Tr. 51-52; *see* Br. 10), while "Waste Water TP" referred to the waste water treatment plant (Ex. 12-P at 27-28; *see* Br. 10).

retained, when making the allocation schedule. (Tr. 39, 41, 112-13; Ex. 12-P.) In its initial tax returns for the years following this purchase, taxpayer depreciated the entire Sebastopol plant as a "Building," employing a 39-year class life and a straight-line depreciation method to calculate the deduction. (R. 18, ¶ 31; Tr. 131-4.)

b. Canton

In May 1998, taxpayer bought another processing facility, contracting with the Marshall Durbin Corporation to buy a plant located in Canton, Mississippi. (Ex. 8-J.) In the asset-purchase agreement, which was generally governed by Alabama law (*id.* at 29), the parties agreed to a purchase price of $10,500,000 (*id.* at 7), which they agreed to allocate "among the Acquired Assets for all purposes (including financial accounting and tax purposes) in accordance with the allocation schedule attached hereto as Exhibit E" (*id.* at 9). According to testimony at trial, taxpayer had the benefit of an appraisal, prepared by PayneSmall, detailing asset value, when the allocation schedule was made. (Tr. 68-69; Ex. 13.) The allocation schedule allocated $350,000 to Real Property: Land, $5,100,000 to Real

Property: Improvements, and $5,050,000 to "Machinery, Equipment, Furniture, and Fixtures." (*Id.* at Ex. E.) This, and the other exhibits and schedules, were "considered effective as of the date of this Agreement and are incorporated herein by reference and made a part hereof." (*Id.* at 30.) The asset purchase agreement further provided:

> This agreement, its Exhibits, and the documents executed on the Closing Date and the Option Closing Date in connection herewith, constitute the entire agreement between the parties with respect to the subject matter hereof . . . . No representation, warrant, promise, inducement or statement of intention has been made by either Party which is not embodied in this Agreement or such other documents, and neither Party shall be bound by, or be liable for, any alleged representation, warranty, promise, inducement or statement of intention not embodied herein or therein. . . .

(*Id.* at 28.)

2. Changes to allocations for tax purposes

a. Cost-segregation study

In 1999, the firm Moore Stephens Frost, which had advised taxpayer on tax matters during both purchases (Tr. 111-12), prepared a cost-segregation study "to further analyze the acquisition costs of the property that [taxpayer] acquired in both Canton and Sebastopol,

Mississippi." (Tr. 145. *See also* Ex. 14; Tr. 74-75, 77, 146). A former partner of Moore Stephens Frost explained that this cost-segregation study was not prompted by any "lack of clarity" as to the agreement. (Tr. 138.) Rather, the cost segregation study came in response to the Tax Court decision in *Hospital Corp. of Am. v. Commissioner*, 109 T.C. 21 (1997), which, according to the firm, appeared to grant "greater flexibility in separating out the cost of things that might be associated with the building and more accurately associating them with the equipment." (Tr. 138.)

The cost-segregation study that was drafted by Moore Stephens Frost "basically breaks out the different components of a building" (Tr. 75), allocating portions of the purchase price to subcomponent assets not included in the original allocation schedule to either agreement (Ex. 14). This reallocation accordingly reduced the purchase price allocated to several of the assets set forth in the original allocation schedules. (*Id.*)

b. Revised tax treatment

The cost-segregation study served as the "basis for determining the depreciation claimed in the return for the year" ending April 3, 1999. (Tr. 145-46.) Taxpayer submitted with its federal corporate tax return for this tax year an IRS Form 3115 (Application for Change in Accounting Method), which indicated that taxpayer sought to change its accounting method regarding depreciation. (Ex. 1-J.) Under this method, taxpayer reallocated a portion of the Sebastopol purchase price originally allocated to the processing-plant building to various assets not originally set forth in the agreement's allocation schedule, including "Exterior Site Prep," "Process Plumbing," "Process HVAC," and "Process electrical." (R. 18, ¶¶ 32-47.) Taxpayer similarly reallocated a portion of the Sebastopol purchase price originally allocated to "Holding Shed #1," "Holding Shed #2," and "Waste Water TP" to various assets not previously set forth. (*Id.*, ¶¶ 48-62.) In addition to not being included in the original allocation agreements, these subcomponent assets often had considerably shorter depreciation recovery periods than initially claimed. (*Id.*, ¶¶ 32-62.) Taxpayer also

reallocated a portion of the Canton purchase price originally allocated to Real Property: Improvements to various component parts not set forth in the Canton agreement's allocation schedule. (*Id.*, ¶¶ 14-29.)

These reallocations resulted in changes to the amounts of depreciation previously claimed for the Sebastopol transaction, based both on the depreciation recovery period and the depreciation method for the newly added assets. On the Form 3115, taxpayer reported an I.R.C. § 481(a) adjustment of $2,135,779, which it planned to claim "over a period of four tax years in accordance with Revenue Procedure 98-60."[3] (Ex. 1-J.) This adjustment was "intended to reflect the

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[3] Section 481(a) provides: "In computing the taxpayer's taxable income for any taxable year (referred to in this section as the "year of the change")--

> (1) if such computation is under a method of accounting different from the method under which the taxpayer's taxable income for the preceding taxable year was computed, then
>
> (2) there shall be taken into account those adjustments which are determined to be necessary solely by reason of the change in order to prevent amounts from being duplicated or omitted, except there shall not be taken into account any adjustment in respect of any taxable year to which this section does not apply unless the adjustment is attributable

(continued...)

amount of depreciation which the [taxpayer] claimed should have been deducted during taxable years 1996, 1997, and 1998 for each asset." (R. 18, ¶ 31.) This adjustment amount "reflected the difference between the depreciation that was actually claimed as per set-up on the original depreciation schedules, compared that to the cost segregated depreciation, what you're entitled to claim." (Tr. 173-74.) Taxpayer claimed an I.R.C. § 481(a) adjustment of $533,944.70 on its returns for its taxable years ending April 3, 1999, April 1, 2000, March 31, 2001 and March 30, 2002, respectively. (Exs. 1-J -- 4-J.)

Taxpayer's tax returns for these tax years also included depreciation deductions based on the reallocations of the Sebastopol and Canton purchase prices. (Exs. 1-J -- 4-J.)

3. Notice of deficiency

The Commissioner issued a notice of deficiency to taxpayer, asserting deficiencies in the amounts of $120,751 for its tax year ending March 28, 1998, $678,978 for its tax year ending April 3, 1999, and

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[3](...continued)
to a change in the method of accounting initiated by the taxpayer."

$727,323 for its tax year ending March 30, 2002. (Ex. 6-J.) The notice limited the amount of the I.R.C. § 481(a) adjustment to $302,846.12, rather than $2,135,779. (*Id.* at 4.) As the adjustment was spread between the four tax years between the tax year ending in April 1999, and the year ending in March 2002, this change resulted in an increase in taxable income of $458,233.17 for each of the four years. (*Id.*)

The notice also limited the depreciation deductions claimed for each of these four years, which resulted in an increase of taxable income in the amount of $635,517 for the tax year ending April 3, 1999, $702,942 for the tax year ending April 1, 2000, $552,564 for the tax year ending March 31, 2001, and $444,978 for the tax year ending March 30, 2002. (*Id.*)

Finally, the notice asserted that taxpayer's net operating loss deduction for its tax year ending April 1, 2000 was $6,104,339, instead of the $7,265,514 claimed on the return, based on the increase in income that resulted from the reduction of the I.R.C. § 481(a) adjustment and the depreciation deductions. (Ex. 6 at 5.) This resulted in an increase in taxable income of $162,222 for tax year ended March

28, 1998, and $998,953 for the tax year ended April 3, 1999. (*Id.*) Taxpayer's net operating loss deduction for the taxable year ending March 31, 2001, likewise was limited to $5,047,941, instead of the $6,058,728 claimed on the return, because of the increase in taxable income for the 1999-2002 taxable years. (*Id.*)

4. Tax Court proceedings

Taxpayer filed a timely petition for redetermination (R. 1), and after a two-day trial (R. 58), the parties submitted briefs detailing their respective positions. The Commissioner argued that the disallowance of the I.R.C. § 481(a) adjustment and the depreciation deductions was justified by I.R.C. § 1060 and the rule adopted in *Commissioner v. Danielson*, 378 F.2d 771 (3d Cir. 1967). (R. 66.) The Commissioner explained that I.R.C. § 1060 generally provides that, when determining the allocation of assets for any applicable asset acquisition, parties are to use the allocation rules set forth in I.R.C. § 338. (*Id.* at 23-24.) If, however, "the transferee and transferor agree in writing as to the allocation of any consideration, or as to the fair market value of any of the assets, such agreement shall be binding . . . unless the Secretary

determines that such allocation (or fair market value) is not appropriate." (*Id.* at 25), *quoting* I.R.C. § 1060(a).

The Commissioner argued that taxpayer was attempting to reallocate the purchase price in violation of the terms of its agreement and I.R.C. § 1060 – allocating part of the price to subcomponents not specifically identified by the parties, and reducing the allocations actually agreed to by the parties – in order to take advantage of shorter recovery periods for purposes of the depreciation deduction. (R. 66 at 28-29.) The Commissioner contended that the parties had made their allocation decisions in the schedules attached to each contract, and I.R.C. § 1060 held them to those bargains. (*Id.*)

In addition to I.R.C. § 1060, the Commissioner argued that the *Danielson* rule also stopped taxpayer's attempts to reallocate the purchase price. The Commissioner explained that the *Danielson* rule, as endorsed by the Eleventh Circuit, provided that:

> A party can challenge the tax consequences of his agreement as construed by the Commissioner *only by adducing proof* which in an action between the parties would be admissible to alter that construction or to show its unenforceability because of mistake, undue influence, fraud, duress, et cetera.

(R. 66 at 29), *quoting Bradley v. United States*, 730 F.2d 718, 720 (11th Cir. 1984) (emphasis in original). The Commissioner asserted that the *Danielson* rule was developed to prevent a taxpayer, as here, from attempting to vary its binding allocations for tax purposes. (*Id.* at 31.) The Commissioner contended that "even changes in the tax code do not meet the *Danielson* standard warranting unilateral reformation of an agreement." (*Id.* at 33.) The Commissioner further argued on this point that taxpayer wholly failed to establish that either agreement was ambiguous, or otherwise susceptible to challenge. (*Id.* at 33-36.)

The Commissioner finally argued that the I.R.C. § 481 adjustment and the depreciation deductions were not proper even if neither I.R.C. § 1060 nor *Danielson* applied. (R. 66 at 36-41.) The Commissioner explained that taxpayer failed to demonstrate the existence and correct value of the purported sub-components to which the purchase price had been reallocated. (*Id.* at 38.) The Commissioner argued that the asset-purchase agreements, which did not mention these sub-components, gave no insight into the matter (*id.* at 38-39), and that taxpayer offered

no substantiation (*id.* at 39-41). The Commissioner also noted that taxpayer retained the burden of proof in this case. (*Id.* at 41-42.)

In its brief, taxpayer argued that neither I.R.C. § 1060, nor the *Danielson* rule, prohibited its reallocations. (Doc. 67 at 20-31.) As to the former, taxpayer argued that I.R.C. § 1060 applied to the transactions at issue, but did not require any particular allocation of the consideration paid. (*Id.* at 21-22.) Taxpayer implicitly suggested that "Processing Plant Bld" in the Sebastopol allocation schedule, and "Improvements" in the Canton allocation schedule were ambiguous (*id.* at 24), but did not contend that any of the other assets listed in the allocation schedules in either agreement were open to multiple interpretations. "Since I.R.C. § 1060(a) does not contemplate classifying assets as either I.R.C. § 1250 property or I.R.C. § 1245 property, I.R.C. § 1060(a) could not be violated by reallocating property between them." (*Id.* at 22.)

Taxpayer also argued (R. 67 at 28-31) that the *Danielson* rule was inapplicable, relying on *United States v. Fort*, 638 F.3d 1334 (11th Cir. 2011). Taxpayer asserted that *Fort* stood for the proposition that the

Danielson rule only prohibited challenges to the form of a transaction, and not to challenges to the tax effect of a transaction. (*Id*. at 29-30.) Taxpayer contended that the reallocations were not challenges to the structure of transaction, but merely sought to obtain different tax consequences within the existing structure of the agreements. (*Id*. at 30-31.)

Taxpayer finally argued that the burden of proof should shift to the Commissioner, contending that the notice of deficiency was arbitrary, as it failed to show that the cost-segregation study, on which taxpayer based its reallocations, was in error. (Br. 31-33.)

5. Tax Court opinion

The Tax Court upheld the Commissioner's determination in full. (R. 70.) The court first explained that its decision did not rest on the burden of proof. (*Id*. at 11.) In any event, the court explained that, in the Eleventh Circuit, an arbitrary notice of deficiency only shifts the burden to the Commissioner in cases of unreported income, and that, in cases of incorrect reporting of deductions, as here, "taxpayer bears the burden of proving his or her entitlement to the deductions claimed

'At all times.'" (*Id.*, n. 5.)

The Tax Court next addressed I.R.C. § 1060 and the *Danielson* rule. (R. 70 at 11-13.) The court explained that I.R.C. § 1060 binds parties to written allocations in agreements unless the Commissioner determines that the allocation is inappropriate, and that the *Danielson* rule allows a taxpayer to challenge the tax consequences of a written agreement as construed by the Commissioner only by adducing proof that would be admissible in an action between the parties to alter the construction, or show unenforceability because of mistake, fraud, duress, or other such reasons. (*Id.* at 11-12.) The court ruled that the instant case was unlike *Fort*, because it involved a challenge to the very form of the transaction as taxpayer sought to reallocate the purchase price among assets not listed in the schedules agreed to by the parties. (*Id.* at 16-17.) The court concluded, therefore, that the allocations specified in the Sebastopol and Canton asset-purchase agreements "are binding upon [taxpayer] unless (1) [the Commissioner] determines that they are not appropriate, see sec. 1060(a), or (2) the agreement is

unenforceable under traditional contract formation defenses" pursuant to the *Danielson* rule. (*Id.* at 17.)

The Tax Court then proceeded to analyze whether each agreement was enforceable under the respective governing state laws of Mississippi and Alabama. (R. 70 at 17-30.) Turning first to the Sebastopol agreement (*id.* at 17-21), the court examined whether the agreement was unenforceable under Mississippi law because of the alleged ambiguity of the term "Processing Plant Bld" (*id.* at 17). The court found that there was no ambiguity, concluding that the inclusion of "building" indicated an intent "to allocate a portion of the purchase price to a structure and not to the assets contained therein." (*Id.* at 20.) The court found further support for its conclusion based on the parties' decision to allocate $6,064,760 of the purchase price to machinery, equipment, and furniture, while allocating only $3,802,550 to the processing-plant building. (*Id.*) The court found this to be "probative of [taxpayer's] intent that the original Sebastopol allocation schedule allocated the purchase price among the specific component assets conclusively." (*Id.*) Finally, the court noted that taxpayer asserted that

the term "Processing Plant Bld" was ambiguous "only after it perceived a benefit which could be realized by subdividing the building into component assets." (*Id.* at 21.) As no ambiguity existed, the court ruled that taxpayer was bound to the original Sebastopol allocation schedule. (*Id.*)

As to the Canton agreement, the Tax Court looked to whether the term "Real Property: Improvements" was ambiguous under Alabama law. (R. 70 at 22.) The court found that the agreement, considered as a whole, showed no ambiguity. (*Id.* at 23.) The court noted that taxpayer was aware of the subcomponent assets, but did not intend to allocate additional purchase price to them, as evidenced by the fact that it did not allocate additional purchase price to the asset described as "Machinery, Equipment, Furniture [sic] and Fixtures." (*Id.*) The court ruled that its conclusion on this score was strengthened because taxpayer had obtained an appraisal by the time of the Canton agreement, and thus could have included a more detailed allocation schedule. (*Id.* at 23-24.) The court also observed that the Canton

agreement contained a merger clause, which further weighed in favor of finding the agreement unambiguous. (*Id.* at 24.)

The Tax Court then addressed, and rejected, taxpayer's argument that neither I.R.C. § 1060 nor *Danielson* prohibited it from making an initial determination of the useful lives of the Canton assets in a manner inconsistent with the original Canton allocation schedule. (R. 70 at 25.) The court ruled that the Commissioner did not abuse its discretion in prohibiting taxpayer from varying from the allocation schedule, because, otherwise, the two parties to the transaction could be treated inconsistently. (*Id.* at 26.) The court further concluded that the Commissioner did not err in determining that "Real Property: Improvements" should be subject to a 39-year depreciation period, in any case, based on the applicable Internal Revenue Code provisions and Treasury Regulations. (*Id.* at 26-28.) The court finally rejected taxpayer's reliance on *Hospital Corp. of Am. v. Commissioner*, 109 T.C. 21 (1997), concluding that, "whether the acquired assets may be subdivided into component assets is immaterial because [taxpayer] may

not deviate from its characterization of those assets as stated in the original allocation schedules." (*Id.* at 29.)

C. Standard of review

This Court reviews the Tax Court's conclusions of law de novo, and its findings of fact for clear error. *See, e.g., Campbell v. Commissioner*, 658 F.3d 1255, 1258 (11th Cir. 2011.) In particular, this Court reviews a trial court's finding as to the parties' definition of contractual terms for clear error. *See Treibacher Industrie, A.G. v. Allegheny Technologies, Inc.*, 464 F.3d 1235, 1237 (11th Cir. 2006) (trial court "did not commit clear error in finding that the parties understood the contracts to require TDY to use all of the TaC specified in the contracts"). *But see Reynolds v. Roberts*, 202 F.3d 1303, 1313 (11th Cir. 2000) ("What a contract provision means, or whether it is ambiguous, are questions of law, which we review *de novo*."). As we shall discuss, the Tax Court did not err in its interpretation of the contractual provisions under either standard.

SUMMARY OF ARGUMENT

As a general matter, a taxpayer must accept the tax consequences that follow from the way it structures a transaction. In particular, under the rule first adopted in *Commissioner v. Danielson*, 378 F.2d 771, 775 (3d Cir. 1967), which was adopted by this Court in *Bradley v. United States*, 730 F.2d 718, 720 (11th Cir. 1984), a party can challenge the tax consequences of an agreement as construed by the Commissioner only by adducing proof that in an action between the parties would be admissible to alter that construction or to show the agreement's unenforceability because of standard contract-formation defenses, such as mutual mistake, undue influence, fraud, and duress. The *Danielson* rule acts to stop unilateral reformation of a contract after-the-fact, thus protecting the Commissioner from the possibility of a whipsaw, and maintaining for the parties the reasonably predictable tax consequences of agreements.

In addition to the *Danielson* rule, I.R.C. § 1060(a) also prohibits a taxpayer from reversing course on a written agreement as to allocation or valuation, in order to claim a tax benefit. As a general matter, I.R.C.

§ 1060(a) provides that, for an applicable asset acquisition, assets shall be allocated pursuant to the method set forth in I.R.C. § 338(b)(5), when determining the transferee's basis in such assets. If the parties enter into a written allocation, however, "such agreement shall be binding" unless the Commissioner finds it inappropriate. I.R.C. § 1060(a) (flush language).

In this case, taxpayer and its respective counter-parties entered into asset-purchase agreements for both the Sebastopol and the Canton poultry-facility acquisitions. Both purchases were applicable asset acquisitions within the meaning of I.R.C. § 1060, and each included a written allocation schedule, assigning portions of the purchase price to various assets. In later tax returns, taxpayer claimed an adjustment and sizable depreciation deductions that were premised on a fundamental reallocation of the purchase price. This reallocation involved additional assets, which were not identified in the original allocation schedules. Taxpayer assigned to these assets portions of the purchase price, which, accordingly, reduced the basis previously assigned to assets in the original allocation schedule. Taxpayer's

efforts resulted in a change to its depreciation computations, as most of the subcomponent assets to which the purchase price was reallocated had relatively short recovery periods for depreciation purposes.

The Tax Court correctly upheld the Commissioner's determination that taxpayer's attempt to reallocate failed to clear the hurdles of either I.R.C. § 1060 or the *Danielson* rule. As the Tax Court ruled, taxpayer's written agreements included clear allocation schedules, and I.R.C. § 1060 and *Danielson* prohibit its attempts to deviate from these agreements unless the agreements are unenforceable. The Tax Court correctly found that neither contract was unenforceable or ambiguous, but rather contained allocations to assets with unambiguous meanings. The Tax Court correctly concluded, therefore, that taxpayer could not vary the terms of these allocation schedules to claim a subsequent tax benefit.

Taxpayer mounts a number of arguments, but none disturb the Tax Court's ruling. First, taxpayer suggests, relying on this Court's decision in *United States v. Fort*, 638 F.3d 1334 (11th Cir. 2011), that the *Danielson* rule does not apply here because taxpayer merely

challenged the tax consequences of its transaction, rather than its form. Taxpayer's reallocation, however, is not at all similar to the challenge in *Fort*, which sought to revisit a contractual agreement establishing certain tax consequences. Rather, taxpayer seeks to undo unilaterally the very structure of the transaction, reallocating the purchase price of various assets in order to maximize its own tax benefits. The *Danielson* rule was developed for precisely this situation.

Taxpayer further asserts that the Tax Court was wrong to pay heed to the agreements' characterizations of the assets at issue, and should have engaged in a facts-and-circumstances analysis to determine how the assets should be depreciated. As the court correctly ruled, however, such a facts-and-circumstances analysis is not appropriate where the parties themselves have set forth an unambiguous allocations schedule as here. In any event, such an analysis would do little good, as taxpayer fails to show that the property should be treated any differently than the Commissioner treated it.

Finally, taxpayer contends that the Tax Court erred by failing to shift the burden of proof to the Commissioner. This is irrelevant, as the court expressly noted that the burden of proof played no role in its decision. In any event, the burden of proof would not shift in this case because, contrary to taxpayer's argument, the notice of deficiency was not arbitrary. Moreover, even if the notice was arbitrary, the burden of proof only would shift in cases of unreported income, and not in cases regarding the disallowance of deductions, according to this Circuit's precedent.

ARGUMENT

The Tax Court correctly determined that taxpayer could not change the purchase-price allocations agreed upon by the parties in order to obtain a tax benefit

A. Introduction

1. Limitations on reallocations

"[W]hile a taxpayer is free to organize his affairs as he chooses, nevertheless, once having done so, he must accept the tax consequences of his choice whether contemplated or not, . . ., and may not enjoy the benefit of some other route he might have chosen to follow but did not."

Commissioner v. Nat'l Alfalfa Dehydrating and Milling Co., 417 U.S. 134, 149 (1974) (internal citations omitted). In other words, "[w]hen a taxpayer characterizes a transaction in a certain form, the Commissioner may bind the taxpayer to that form for tax purposes." *Plante v. Commissioner*, 168 F.3d 1279, 1280 (11th Cir. 1999). "This is the rule: '[a] party can challenge the tax consequences of his agreement as construed by the Commissioner only by adducing proof which in an action between the parties would be admissible to alter that construction or to show its unenforceability because of mistake, undue influence, fraud, duress, et cetera." *Id.* at 1280-1281 (quoting *Bradley v. United States*, 730 F.2d 718, 720 (11th Cir. 1984)). *See also Commissioner v. Danielson*, 378 F.2d 771, 775 (3d Cir. 1967). In other words, "if a taxpayer has entered an asset sales contract that unambiguously allocates the purchase price among the subject assets, then the taxpayer can challenge the tax consequences properly flowing from those allocations only by showing that the term would be unenforceable between the parties." *N. Am. Rayon Corp. v. Commissioner*, 12 F.3d 583, 589 (6th Cir. 1993).

The *Danielson* rule curbs "a unilateral reformation of the contract with a resulting unjust enrichment." *Danielson*, 378 F.2d at 775. This rule arose out of the sellers' attempts to ignore, for tax purposes, an allocation of purchase price in a stock-purchase agreement. *Id.* at 773-74. The Third Circuit disallowed the sellers' attempt to revise the agreement after the fact, because, if "allowed, such an attack would encourage parties to unjustifiably risk litigation after consummation of a transaction in order to avoid the tax consequences of their agreements." *Id.* at 775. The *Danielson* court also recognized that the Commissioner would face considerable problems in the collection of taxes, including "the necessity for litigation against both buyer and seller to collect taxes properly due." *Id.* As the First Circuit has explained:

> The Commissioner properly points out that for parties to agree on paper one way, benefitting one of them vis-a-vis himself, and then to permit the other to claim that the agreement was really something different, exposes him to a whipsaw. This danger is one of the purposes of the "strong proof" rule. Nor is that rule to be avoided in some individual case by a showing, (as we understand taxpayer to contend here) that no whipsaw is involved. If certainty is a desirable goal, we would not consider this a desirable exception. Rather, it could only lead to highly complicated debate.

Harvey Radio Lab., Inc. v. Commissioner, 470 F.2d 118, 120 (1st Cir. 1972). "Not only does the *Danielson* rule provide certainty to the Commissioner, it also provides a higher level of certainty to the taxpayers by maintaining 'the reasonably predictable tax consequences' of agreements." *N. Am. Rayon*, 12 F.3d at 587 (quoting *Danielson*, 378 F.2d at 775).

In addition to the *Danielson* rule, the Internal Revenue Code also limits a taxpayer's ability to alter an allocation contained in an agreement. Section 1060(a) generally provides that, for an applicable asset acquisition, assets shall be allocated pursuant to the method set forth in I.R.C. § 338(b)(5), when determining the transferee's basis in such assets, and the gain or loss of the transferor.[4] Where there is a written allocation agreement between the parties, however, "such agreement shall be binding on both the transferee and transferor unless the Secretary determines that such allocation (or fair market

[4] "Applicable asset acquisition" means any transfer (1) of assets which constitute a trade or business, and (2) with respect to which the transferee's basis is determined wholly by reference to the consideration paid. I.R.C. § 1060(c). It is undisputed that the transactions at issue in this case constituted applicable asset acquisitions under I.R.C. § 1060(c).

value) is not appropriate." I.R.C. § 1060(a) (flush language). If the parties agree in writing as to the allocation, therefore, this written allocation takes precedence over the default method of allocation previously identified.

The legislative history confirms this meaning, explaining that the provision established that a written agreement as to allocation or valuation of assets "will be binding on both parties for tax purposes, unless the parties are able to refute the allocation or valuation under the standards set forth in the *Danielson* case." H.R. Rep. No. 101-881, at 351 (1990), *reprinted in* 1990 U.S.C.C.A.N. 2017, 2353. The Committee report further explained that the "parties are bound only with respect to the allocations or valuations actually provided in the agreement." *Id.* "Thus, the parties are bound to any written partial allocation or valuation." *Id.*

2. General depreciation framework

Section 167(a) of the Internal Revenue Code generally provides a depreciation deduction of "a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence) –

(1) of property used in the trade or business, or (2) of property held for the production of income." Section 168(a) provides that the depreciation deduction shall be determined using the applicable depreciation method, the applicable recovery period, and the applicable convention. Section 168(c)(1), for its part, sets forth different classes of property and assigns applicable recovery periods to each category.

As most relevant here, nonresidential real property has an applicable recovery period of 39 years. *See* I.R.C. § 168(c)(1). Nonresidential real property is defined as "section 1250 property" that is not residential real property or property with a class life of less than 27.5 years. I.R.C. § 168(e)(2)(B); *see* I.R.C. §§ 168(i)(12), 1250(c). The regulations under I.R.C. § 1250 (Treas. Reg. (26 C.F.R.) § 1.1250-1(e)(3)) provide that "section 1250 property" includes, *inter alia*, "a building or its structural components within the meaning of paragraph (c) of [26 C.F.R.] § 1.1245–3," which provision in turn refers to Treas. Reg. § 1.48-1(e). That provision defines building as "any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter or housing, or to

provide working, office, parking, display, or sales space," including, *inter alia*, "factory and office buildings." Treas. Reg. § 1.48-1(e)(1). "The term 'structural components' includes such parts of a building as walls, partitions, floors, and ceilings . . ., and other components relating to the operation or maintenance of a building." *Id.*

B. The Tax Court correctly determined that taxpayer could not alter the allocations as agreed upon in the written agreements in order to obtain more beneficial tax treatment

The Tax Court correctly held that I.R.C. § 1060 and the *Danielson* rule both govern taxpayer's attempt to reallocate the assets in a manner different from the agreed-upon allocation schedules. The court also correctly found that the contracts and the allocation schedules are unambiguous and enforceable, and that taxpayer thus is bound to the original allocations, as the Commissioner had determined.

1. Applicability of I.R.C. § 1060 and the *Danielson* rule

As an initial matter, the Tax Court correctly ruled that both I.R.C. § 1060(a), and the *Danielson* rule, apply to the instant case. As to the former, the court correctly rejected taxpayer's attempt "to elevate the residual method of section 338(b)(5) over the written allocations."

(R. 70 at 14.) Section 1060(a) conclusively establishes that, where the parties have agreed to the allocation of any consideration, "such agreement shall be binding," thus displacing the residual method. Here, taxpayer and its respective counter-parties included written allocation schedules as exhibits incorporated in both the Sebastopol and Canton agreements. Those schedules, therefore, not the residual method of I.R.C. § 338(b)(5), are binding.

The Tax Court likewise correctly concluded that the *Danielson* rule applies to the instant case, because taxpayer's reallocation went to the form of the transaction, not simply the tax consequences. The court's conclusion (R. 70 at 16) is well-supported by the evidence. As the court noted (*id.*), the reallocations did not merely challenge a particular tax consequence. Rather, the reallocations fundamentally changed the structure of the deals. Both of the agreements listed a number of assets and allocated the purchase price among these listed assets. Taxpayer made a unilateral revisions to these allocations, changing both the assets and the amounts allocated thereto. This is a wholly different allocation than the one crafted by the parties, striking

at the heart of the transaction. The *Danielson* rule was intended to stop precisely this type of unilateral modification of an agreed-upon allocation. *See, e.g., Plante*, 168 F.3d at 1281; *N. Am. Rayon Corp.*, 12 F.3d at 588 (*Danielson* rule "prevent[s] one party to an agreement from unilaterally reforming the agreement for tax purposes").

In its brief, as in the Tax Court, taxpayer contends that the *Danielson* rule is inapposite, based on this Court's decision in *United States v. Fort*, 638 F.3d 1334 (11th Cir. 2011), asserting that the reallocations comprised merely a change to the tax consequences of the agreements. (Br. 30-32, 36-37.) In support of this point, taxpayer also argues that the reallocations merely altered the classification of depreciable property, and that taxpayer did not "need to have obtained the consent of the Commissioner" to make this change. (Br. 36.)

Both arguments fall wide of the mark. First, as the Tax Court correctly explained (R. 70 at 15-17), this Court's decision in *Fort* supports the application of the *Danielson* rule here. *Fort* recognized that *Danielson* stands for the proposition that "parties may agree to a certain form of a transaction, and that if they do, they face a difficult

burden in convincing the court that they did not actually engage in the form that they contracted to engage in." 638 F.3d at 1337-38. This Court further explained that "agreeing to *form* (*e.g.*, agreeing to sell A for B on October 18, 1985) is different from agreeing to a certain type of tax *liability* (*e.g.*, agreeing that the result of the transaction will yield no tax liability in 1985)." *Id.* at 1338 (emphasis in original). This Court ultimately ruled that *Danielson* did not apply because the taxpayer argued "that the agreed-upon form had particular tax consequences." *Id.*

In the instant case, however, taxpayer seeks to restructure the form of the transaction, modifying both the assets involved, as well as the portion of the purchase price allocated to the various assets. As the Tax Court ruled (R. 70 at 16), this is not a case, like *Fort*, where the taxpayer was challenging tax consequences that had been agreed-upon as part of a transaction. Rather, this is an attempt to restructure the agreements themselves to produce a better tax result for taxpayer. While taxpayer's attempt to modify the form of the transactions inevitably breeds "different tax liability consequences," *Fort*, 638 F.3d

at 1338, this does not alter the fact that taxpayer here is fundamentally seeking to restructure its deal. *Fort*, therefore, provides no obstacle to the application of the *Danielson* rule.

Nor is taxpayer correct that it merely changed the classification of the assets purchased, which could not amount to a challenge to the form of the transactions. (Br. 32-36.) As an initial matter, taxpayer was not changing the classification of assets; it also added assets and reallocated the purchase price in a manner inconsistent with the agreements. Moreover, the authority taxpayer introduces to support its position is inapposite. Taxpayer relies (Br. 33) principally on *Commissioner v. Brookshire Bros. Holding, Inc.*, 320 F.3d 507 (5th Cir. 2003), and *O'Shaughnessy v. Commissioner*, 332 F.3d 1125 (8th Cir. 2003), which held that a change in depreciation classification fell under the useful-life exception of Treas. Reg. § 1.446-1(e)(2)(ii)(b), and thus did not require obtaining the consent of the Commissioner. Taxpayer also points to Treasury Regulations and a Chief Counsel notice indicating that changes in computing depreciation or amortization do

not constitute a change in method of accounting under I.R.C. § 446(e). (Br. 34-35.)

As an initial matter, there is no indication that a change of form under the *Danielson* rule is synonymous with a change in the method of accounting. Additionally, none of these authorities address the situation here, *viz.*, a reallocation that goes considerably deeper than merely a change to the classification for depreciation purposes. Finally, none of these authorities discuss, much less cast doubt on the applicability of the *Danielson* rule. Taxpayer's argument thus fails to show error in the Tax Court's application of the *Danielson* rule.

In short, the Tax Court was well-justified when it concluded (R. 70 at 17) that the allocations taxpayer made in the Sebastopol and Canton transactions were binding upon taxpayer "unless (1) [the Commissioner] determines that they are not appropriate, *see* sec. 1060(a), or (2) the agreement is unenforceable under traditional contract formation defenses, *see Commissioner v. Danielson*, 378 F.2d at 775."

2. The agreements were enforceable

The Tax Court also correctly found that neither agreement was ambiguous, and thus the allocations therein were binding on taxpayer. Turning first to the Sebastopol agreement, Mississippi law applies to the determination of ambiguity. (Ex. 7-J at 27.) Under Mississippi law, an ambiguous term is "one capable of more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement and who is cognizant of customs, practices, usages and terminology as generally understood in the particular trade or business." *Dalton v. Cellular S., Inc.*, 20 So.3d 1227, 1232 (Miss. 2009) (internal quotations omitted). "The mere fact that the parties disagree about the meaning of a provision of a contract does not make the contract ambiguous as a matter of law." *Epperson v. SOUTHBank*, --- So.3d —, 2012 WL 1870806, at *4 (Miss. May 24, 2012) (internal quotations omitted).

The Sebastopol agreement is unambiguous, as the Tax Court found. (R. 70 at 19-21.) Taxpayer and Green Acres allocated portions of the purchase price to 26 different assets, and agreed that this

allocation would be used "for all purposes (including financial accounting and tax purposes)." (Ex. 7-J at 7.) The allocation schedule assigned specific values to the processing-plant building, the holding sheds, and the waste water treatment plant, as well as to categories for machinery, furniture, and equipment. (*Id.* at Ex. D.)

Taxpayer tries to import ambiguity by challenging the meaning of one of the twenty-six assets set forth in the allocation schedule, *viz.*, the processing-plant building.[5] (Br. 28-29.) In short, taxpayer contends that, although the parties referred to the processing-plant building in the allocation schedule, the amounts allocated to this asset encompassed not just that building but also the various subcomponents that were the subject of taxpayer's subsequent reallocation. (R. 18, ¶¶ 32-47.) Taxpayer fails to show ambiguity in the agreement's terms. As the Tax Court found, the agreement displays no indication that the parties' reference to "building" was meant to allocate a portion of the

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[5] Taxpayer also reallocated portions of the purchase price from the assets Holding Shed #1, Holding Shed #2, and Waste Water TP. (R. 18, ¶¶ 48-62.) Taxpayer does not argue on appeal that any of these terms were ambiguous, and thus has waived any such argument. *See United States v. Robles*, 408 F.3d 1324, 1326 n.1 (11th Cir. 2005) ("Issues not raised in a party's initial brief will be deemed waived.").

purchase price to anything but the structure itself. (R. 70 at 19-20.) And it is unlikely, that the parties would choose to allocate in the soft-voiced manner suggested by taxpayer. It seems particularly unlikely that the parties would have allocated a portion of the purchase price for subcomponent mechanical systems by allocating additional funds to the category of processing-plant building, as taxpayer suggests, because the many subcomponent systems would fit most naturally in the asset categories dedicated to machinery, equipment, and furniture – categories to which the parties had allocated a considerable portion of the purchase price. As the Tax Court found, "[t]he decision to allocate the purchase price among machinery, equipment, and furniture . . . . shows that Peco was aware of the specific component assets but chose to not allocate additional purchase price to those assets." (R. 70 at 20.)

The most natural reading of the term "Processing Plant Bld" in the allocation schedule, as the Tax Court explained, was that it merely referred to the structure, and did not also include allocations for a number of subcomponent systems too. (R. 70 at 19.) Taxpayer's initial tax returns (R. 18, ¶ 31) support this reading, as does the testimony of

one of its tax advisors, who admitted that taxpayer's change in position was not prompted by a "lack of clarity" as to the agreement (Tr. 138). In short, "building" is not ambiguous, but rather is being used as a springboard by taxpayer to launch its unilateral modification of the allocations. The *Danielson* rule prohibits it from doing so, binding taxpayer to the agreed-upon allocation schedule.

Likewise, the Canton agreement contains no ambiguity. This agreement is governed by Alabama law (Ex. 8-J at 29), which looks to a contract as a whole and gives its terms their ordinary, plain, and natural meaning, absent any indication that the terms are used in a special or technical sense. *See, e.g., Black Warrior Minerals, Inc. v. Fay*, 82 So.3d 650, 653 (Ala. 2011); *Homes of Legend, Inc. v. McCullough*, 776 So.2d 741, 746 (Ala. 2000). An instrument is unambiguous if there is only one reasonable meaning. *See Kelmor, LLC v. Ala. Dynamics, Inc.*, 20 So.3d 783, 790 (Ala. 2009).

The Canton agreement allocated the purchase price to three categories: Real Property: Land; Real Property: Improvements; and Machinery, Equipments, Furnitures and Fixtures. (Ex. 8-J at Ex. E.)

As in the case of the Sebastopol agreement, taxpayer reallocated a portion of the amount originally allocated to "Real Property: Improvements" among a number of subcomponents, usually with much shorter depreciation recovery periods than originally claimed. (R. 18, ¶¶ 14-29.) Taxpayer now claims that the term "Real Property: Improvements" was ambiguous, and that the original allocation for this asset actually included allocations for the subcomponent systems that went unnamed until taxpayer's reallocation. The Tax Court correctly found otherwise. (R. 70 at 23-24.)

As an initial point, at the time that the allocation schedule was made, taxpayer had the benefit of an appraisal, prepared by PayneSmall, detailing asset value. (Tr. 68-69; Ex. 13.) The parties, therefore, were well-equipped to allocate the purchase price to various subcomponents if they had wished to do so. They did not. Moreover, as the court noted (R. 70 at 23), if the parties had intended to allocate the purchase price to one of the three categories to cover the subcomponent systems at issue, they likely would have allocated such amounts to the machinery and equipment category, rather than Real Property:

Improvements, given that most of the subcomponents involved machinery or equipment. There is no indication that the parties allocated portions of the purchase price to Real Property: Improvements to cover the wide array of subcomponents that taxpayer now wishes to recognize in order to gain a tax benefit.

Further strengthening the court's finding that the challenged term was unambiguous, the parties included a merger clause indicating that the agreement was complete and whole. (Ex. 8-J at 28.) Under Alabama law, a merger clause creates a presumption that "the writing represents an integrated, that is, the final and complete agreement of the parties." *Ex parte Palm Harbor Homes, Inc.*, 798 So.2d 656, 660 (Ala. 2001). Taxpayer fails to disturb the Tax Court's reasonable reading of the Canton agreement, and thus taxpayer is bound to the terms of the agreed-upon allocation schedule.

C. Taxpayer's contentions in support of its reallocation are meritless

In addition to taxpayer's argument against the applicability of the *Danielson* rule discussed *supra*, it mounts two other challenges. Taxpayer contends that the court incorrectly gave primacy to "the

words used to describe the assets here involved", instead of relying on the sections of the Internal Revenue Code relating to the proper depreciable lives of assets. (Br. 21-29.) Taxpayer also argues that the burden of proof should have shifted to the Commissioner. (Br. 37-40.) Neither argument has merit.

1. Taxpayer first argues, relying on *Hospital Corp. of Am. v. Commissioner*, 109 T.C. 21 (1997), that it could subdivide the acquired assets into subcomponents for depreciation purposes, because some of the assets are more appropriately viewed as I.R.C. § 1245 property. (Br. 21-29.) Taxpayer is attempting an end-run around its own agreement. As the Tax Court properly observed (R. 70 at 29), "whether the acquired assets may be subdivided is immaterial because [taxpayer] may not deviate from its characterization of those assets as stated in the original allocation schedules." The parties here made unambiguous, written agreements, and taxpayer is bound to the allocation schedules incorporated therein. *See Plante*, 168 F.3d at 1280.

Moreover, the definitions set forth in the Internal Revenue Code refute taxpayer's attempt to characterize the acquired assets as I.R.C. § 1245 property. Nonresidential real property is defined as "section 1250 property," *see* I.R.C. § 168(e)(2)(B), which includes, *inter alia*, "a building or its structural components . . . ." Treas. Reg. § 1.1250-1(e)(3). Treas. Reg. § 1.48-1(e), which supplies the operative definition of building for this purpose, provides that a building is "any structure or edifice enclosing a space within its walls, and usually covered by a roof, the purpose of which is, for example, to provide shelter or housing, or to provide working, office, parking, display, or sales space," including "factory and office buildings." Treas. Reg. § 1.48-1(e)(1).

As an initial matter, "Processing Plant Bld" in the Sebastopol agreement clearly comes within the definition of "section 1250 property" set forth in Treas. Reg. § 1.1250-1(e)(3), which includes "a building or its structural components."[6] Furthermore, the Tax Court

[6] It should be noted that taxpayer took the position in its tax returns for its 1996-1998 tax returns that the Sebastopol poultry-processing plant was a building to be depreciated over 39 years (R. 18,
(continued...)

correctly concluded that the Commissioner was not unreasonable in determining that "Real Property: Improvements" in the Canton agreement is nonresidential real property depreciable over 39 years. (R. 70 at 26-28.) As the Tax Court explained (R. 70 at 28), the Canton agreement defined Real Property: Improvements to include, *inter alia*, "improvements, fixtures and fittings thereon" (Ex. 8-J at 1). The Tax Court concluded that this agreement language thus showed that Real Property: Improvements comprised nonresidential real property under I.R.C. § 1250 (R. 70 at 28), and taxpayer fails altogether to show that this conclusion was erroneous.

2. Taxpayer also argues the burden of proof should have shifted to the Commissioner, contending that the notice of deficiency was arbitrary because it was unsupported by I.R.C. § 1060 or the *Danielson* rule. (Br. 33-40.) As demonstrated above, the notice had ample legal support, and thus taxpayer's argument fails. Moreover, as the Tax Court noted (R. 70 at 11), the burden of proof did not figure in its decision. "The shifting of an evidentiary burden of preponderance is of

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[6](...continued)
¶ 31), which is the Commissioner's position too.

practical consequence only in the rare event of an evidentiary tie . . . ." *Polack v. Commissioner*, 366 F.3d 608, 613 (8th Cir. 2004) (quoting *Cigaran v. Heston*, 159 F.3d 355, 357 (8th Cir. 1998)). *See Geiger v. Commissioner*, 279 Fed. Appx. 834, 835 (11th Cir. 2008)("any error committed by the tax court by failing to shift the burden [under I.R.C. § 7491] was harmless, because the burden is of practical consequence only in the rare event of an evidentiary tie"). There was no indication that such a tie existed here, or that the shifting of the burden would have any effect whatsoever.

Finally, taxpayer is incorrect that the burden of proof could shift in this case.[7] In general, the Commissioner's determinations are presumed correct, and a taxpayer has the burden of showing those determinations are incorrect. *See Welch v. Helvering*, 290 U.S. 111, 115

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[7] Taxpayer has not argued that it introduced credible evidence so as to shift the burden of proof under I.R.C. § 7491, and such an argument accordingly is waived. *See Grant v. Commissioner*, 103 F.3d 948, 952 (11th Cir. 1996) ("As a general rule, a taxpayer may not address an issue on appeal which it has not first presented to the Tax Court."); *Robles*, 408 F.3d at 1326 n.1 ("Issues not raised in a party's initial brief will be deemed waived.").

(1933). While this Court has allowed the shifting of the burden to the Commissioner if "it has been shown through evidence that the Commissioner's determination is arbitrary and erroneous," *Gatlin v. Commissioner*, 754 F.2d 921, 923 (11th Cir. 1985), it has only shifted the burden in cases involving unreported income. An arbitrary notice does not cause the burden to shift in cases involving a deduction because "the taxpayer is privy to the facts that substantiate a deduction." *Id.* Even if the notice of deficiency were arbitrary, which it is not, the burden thus would remain on taxpayer.

CONCLUSION

For the reasons stated above, the Tax Court's decision is correct and should be affirmed.

Respectfully submitted,

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Dated: August 9, 2012

CERTIFICATE OF SERVICE

It is hereby certified that, on this 9th day of August, 2012, this brief was filed with the Clerk of the United States Court of Appeals for the Eleventh Circuit by using the CM/ECF system and seven (7) paper copies were sent to the Clerk by First Class Mail. Service of this brief was made on counsel for the appellant, who are not registered for the CM/ECF system, on this 9th day of August, 2012, by sending them one paper copy by First Class Mail in an envelope properly addressed as follows:

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