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1 P R O C E E D I N G S

2 (10:02 a.m.)

3 CHIEF JUSTICE ROBERTS: We'll hear argument
4 first this morning in Case 11-139, United States v.
5 Home Concrete & Supply.

6 Mr. Stewart.

7 ORAL ARGUMENT OF MALCOLM L. STEWART

8 ON BEHALF OF THE PETITIONER

9 MR. STEWART: Mr. Chief Justice, and may it
10 please the Court:

11 The disputed question in this case concerns
12 the meaning of the phrase "omits from gross income an
13 amount properly includible therein" in 26
14 U.S.C. 6501(e)(1)(A). More specifically, the question
15 is whether an omission from gross income occurs when a
16 taxpayer overstates his basis in sold property and
17 thereby understates the gain that results from the sale.

18 In December 2010, after notice-and-comment
19 rulemaking, the Treasury Department issued published
20 regulations that interpreted section 6501(e)(1)(A) to
21 apply in overstatement of basis cases. Those
22 regulations reflect a reasonable interpretation of
23 ambiguous statutory language, and they are accordingly
24 entitled to deference under Chevron.

25 CHIEF JUSTICE ROBERTS: Well, but only if

1 your reading of the Colony decision is correct, right?
2 If we think that Colony definitively resolved the
3 question before you, the regulation can't overturn that.

4 MR. STEWART: If the Court in Colony had
5 interpreted the statutory language to be unambiguous, or
6 if the Court in Colony had issued an authoritative
7 interpretation that Congress had then built upon, that
8 would be correct. But the Court in Colony stated that
9 the language was, in its words, "not unambiguous."

10 JUSTICE SCALIA: Yes, but once -- once we
11 resolve an ambiguity in a statute, that's the law, and
12 the agency cannot issue a -- a regulation that changes
13 the law just because, going in, the language was
14 ambiguous.

15 MR. STEWART: I think -- I don't think that
16 the Court in Colony purported to give a definitive
17 definition of the phrase "omits from gross income an
18 amount properly includible therein" wherever it appears
19 in the United States Code. And the Court in the first
20 paragraph of its opinion in Colony said the sole
21 question before us is whether the taxpayer is subject to
22 the extended assessment period under the 19 -- under the
23 Internal Revenue Code of 1939.

24 And as the D.C. Circuit, for instance,
25 pointed out in Intermountain, what we are interpreting

1 now is the 1954 code. It's true that, like the 1939
2 code, it includes the phrase "omits from gross income an
3 amount properly includible therein," but it also
4 includes adjacent provisions that bear upon the meaning
5 of that phrase. I think --

6 CHIEF JUSTICE ROBERTS: Well, if they use
7 the exact same phrase, and it's a fairly detailed --
8 it's not just a normal phrase they might use elsewhere,
9 I think it's reasonable to assume that that phrase came
10 in with the baggage it -- it carried from the Colony
11 case; right?

12 MR. STEWART: I think it's important to
13 remember that the 1954 code was enacted in 1954, and the
14 Colony decision came in 1958. And so, I would take your
15 point that if Congress had enacted the same language
16 after this Court's decision in Colony, then the adjacent
17 statutory provisions that we're relying on would be
18 pretty indirect means of an -- of expressing an intent
19 to change the law.

20 But what Congress was reacting to in 1954
21 was not this Court's Colony decision; it was reacting to
22 a circuit conflict and trying to resolve that conflict.

23 JUSTICE SCALIA: Yes, but our job is not to
24 plumb Congress's psyche and decide what they had in
25 mind. It's to interpret the statute. And if, as you

1 acknowledge, it's a pretty obscure way to change the law
2 from what we said it was, the law that's written there,
3 that's a very obscure way to change it. I'm inclined to
4 think that the law stays the way it was.

5 MR. STEWART: Well, let me point to the
6 statutory provisions that I have in mind, to explain a
7 little bit more fully why we think that the context in
8 which the new provision or the 1954 provision appears
9 bears on the -- the proper interpretation of the
10 disputed phrase.

11 It's at page 1a of the red brief, the
12 appendix to the Respondents' brief.

13 And the -- the general rule stated in
14 subsection (A) is: "If the taxpayer omits from gross
15 income an amount properly includible therein which is in
16 excess of 25 percent of the amount of gross income
17 stated in the return," the assessment period is 6 years
18 rather than 3 years.

19 And it's important to recognize that, for
20 purposes of the Internal Revenue Code generally, the
21 term "gross income" is defined to include gains derived
22 from dealings in property. And in that sense, it
23 might --

24 JUSTICE SOTOMAYOR: But that -- but that
25 argument hasn't changed between the predecessor statute

1 and this statute. You made the same argument under the
2 Colony statute. It lost. So, you can't go back to that
3 argument because it's already been rejected.

4 So, what goes from that?

5 MR. STEWART: Well, if you look at
6 subparagraph (i), Roman (i) -- or Roman (i) after the
7 general rule, it says: "In the case of a trade or
8 business, the term 'gross income' means the total of the
9 amounts received or accrued from the sale of goods or
10 services (if such amounts are required to be shown on
11 the return) prior to diminution by the cost of such" --
12 "of such sales or" --

13 JUSTICE SOTOMAYOR: My problem with your
14 argument as I read it in the brief, it's a bit
15 convoluted, as Justice Scalia observed. But if Congress
16 intended to change Colony, it wouldn't just have created
17 this subdivision (i); it would have changed the main
18 statement. So, why don't we read this as simply saying
19 we accept whatever Colony said, and the only thing we're
20 -- we're creating exceptions around are the following?
21 The exception argument.

22 MR. STEWART: As I say, I would agree that
23 if Congress had passed this statute after the Court's
24 decision in Colony, that this would have been a fairly
25 oblique way to reflect an intent to change what the

1 Court had done. But Congress was acting in 1954, before
2 the Court's decision in Colony, and it was reacting to a
3 circuit conflict.

4 And I think it's -- it's just as fair to say
5 that --

6 JUSTICE SCALIA: So, this language would
7 have one meaning if the very same language were adopted
8 after our decision in -- in Colony and a different
9 meaning if it were adopted, as it was, before our
10 decision in Colony.

11 MR. STEWART: Well, in our -- I think --

12 JUSTICE SCALIA: That's a very strange
13 approach to a -- to the meaning of a statute, it seems
14 to me.

15 MR. STEWART: It may be strange, but I think
16 in a sense it's the Respondents who are striving for
17 strangeness, in the following way --

18 JUSTICE KENNEDY: Well, but -- but you're
19 saying -- and I'm just trying to supplement
20 Justice Scalia's question so -- so you can continue to
21 answer it.

22 You're saying that the split is somehow more
23 obscure or more imprecise in its formulation than what
24 Colony did. You're saying that, oh, if Congress knew
25 about Colony, they would have done it differently, but

1 it was a split, this was close enough for government
2 work. That seems to be your argument. And I --

3 (Laughter.)

4 MR. STEWART: No, I -- I guess there are two
5 things I'm saying. The first thing I'm saying is, in
6 order to construe the statute, we need to not put
7 ourselves in -- attempt to put ourselves in the minds of
8 Congress, but at least be aware of the state of the
9 world at the time that Congress acted.

10 And in 1954, when Congress acted, there was
11 the circuit split. And if Congress had wanted to
12 endorse the Colony rule going forward and apply it to
13 trades -- to non-trade and -business taxpayers as well
14 as trades and businesses, the most natural thing would
15 have been to change the word "amount" in the main rule
16 to "item," to make clear that the main rule would apply
17 only when an item of gross receipts had been left off
18 the return altogether.

19 It also would have been natural, if Congress
20 had wanted that rule to apply going forward, to change
21 the term "gross income" in the main rule to say "gross
22 receipts" because gross income --

23 JUSTICE KENNEDY: I still don't understand
24 why the world was different after Colony addressed the
25 split than before Colony addressed the split. The issue

1 is still the same.

2 MR. STEWART: I guess the way I would
3 respond to your question, Justice Kennedy, is to say if
4 you look at the statute in its current form, both the
5 text of the main rule and the adjacent provisions that
6 contextually bear on its meaning, then I think ours is
7 by far the better interpretation. And, really,
8 what Respondents --

9 JUSTICE SCALIA: Well, by far? By a little
10 maybe, and I might agree with that, but -- but we're not
11 writing on a blank slate here.

12 MR. STEWART: And what --

13 JUSTICE SCALIA: Indeed, I think Colony may
14 well have been wrong, but there it is. It's -- it's the
15 law, and it said that that language meant a certain
16 thing. And the issue is whether this is -- this change
17 is enough to change the meaning of the statute. And --
18 and I'm dubious about that.

19 MR. STEWART: I guess my main point is we
20 think our reading of the text is better, and what
21 Respondents have going for them is the argument that,
22 whether or not this is the way you would otherwise
23 construe the statute, once Colony has said what the
24 statute meant, the Court is bound by it.

25 And our point is that methodology doesn't

1 really work with this provision, because the Court in
2 Colony --

3 JUSTICE KAGAN: Mr. Stewart, don't you have
4 two arguments? One is that the statute changed, but the
5 other is that even the statute remained the -- even if
6 the statute remained the same, Colony itself was a
7 decision that found ambiguity in the statute. So, you
8 have the power under Brand X to go back to that statute
9 and reinterpret it, if you will.

10 MR. STEWART: We do have the power under
11 Brand X, but we -- we don't think that the Court needs
12 to reach that question. And when the Court in Colony
13 said that the --

14 JUSTICE KAGAN: But if the Court thinks it
15 has to reach that question because it agrees more with
16 Justice Scalia than with you as to whether this statute
17 stays the same, then you have independent Brand X
18 arguments, don't you?

19 MR. STEWART: Yes, we do.

20 CHIEF JUSTICE ROBERTS: Well, about that
21 argument, you rely very heavily on the fact that
22 Justice Harlan used the term "ambiguous," right?

23 MR. STEWART: Yes.

24 CHIEF JUSTICE ROBERTS: But he was writing
25 very much in a pre-Chevron world. I -- he was certainly

1 not on notice that that was a term of art or would
2 become a term of art. And, of course, I didn't know
3 him, but my sense is he was very gracious and polite.
4 And you can see him saying, well, that's a good
5 argument, but.... He's not the sort of person who would
6 say this is it, this is it.

7 I don't think you necessarily can take the
8 use of the word "unambiguous" in his opinion to mean
9 what it does today.

10 JUSTICE GINSBURG: But he did say that
11 something was unambiguous, and that was the little (i)
12 that was added. And he also said he wasn't taking any
13 position on the '54 code; isn't that so?

14 MR. STEWART: That's correct.

15 JUSTICE GINSBURG: He did.

16 MR. STEWART: And the Court said that both
17 at the end of its opinion and it also said at the
18 beginning the only question before us is whether the
19 extended assessment period applies under the '39 code.

20 CHIEF JUSTICE ROBERTS: Is there -- is there
21 a case where we applied Chevron deference to a
22 pre-Chevron opinion? In other words saying, well, the
23 Court looked at that, but the Court said it was
24 ambiguous; and so, we apply Chevron.

25 MR. STEWART: I'm not aware of any case.

1 Obviously, Brand X is a recent decision of this Court.
2 And I would agree with you that it's perilous to kind of
3 put a Chevron overlay on decisions that were issued
4 before Chevron.

5 JUSTICE BREYER: Even without Chevron -- I
6 mean, even apply it, I would have thought the point of
7 Brand X is you look at the language of the statute and
8 you look at what Congress intended, and where they
9 intended the agency to have power to interpret, you
10 follow the agency. And you could do that after the
11 event if the basis for your decision is that it isn't
12 clear.

13 But that isn't Harlan's opinion at all. He
14 goes and looks at what Congress meant, and what they
15 meant is treat basis like you treat a deduction. And he
16 gathers that from the legislative history. And so, I
17 don't see the basis for saying now the agency still has
18 power.

19 Now, forget that one. I mean, that's one
20 point you might want to address, but I may be too unique
21 in that, in which case it's not worth your time.

22 MR. STEWART: Let me give two -- let me --
23 let me give two responses to that, Justice Breyer. I
24 think in effect what Justice Harlan did for the Court in
25 Colony was to construe the term, the reference to an

1 amount of gross income, as though it meant item of gross
2 receipts. That was the practical effect of the Court's
3 decision. And I think two of the -- two of the adjacent
4 provisions of the current code make clear that that's
5 not a --

6 JUSTICE BREYER: No, I didn't think that was
7 the basis. I thought the basis is that there are two
8 kinds of things: One is you just don't put in some big
9 category of stuff in your return, and the agency can
10 never figure that one out. And the other is where you
11 don't state your deductions correctly.

12 And now, the cost of goods sold and the
13 basis are difficult cases because of the way the -- the
14 code defined "gross income." It defines it in terms of
15 gain. But Harlan says they're like deductions for
16 purposes of this statute. That's how I read it.

17 But I have a different question. You can
18 pursue this one if you want. My -- what's really
19 bothering me about this case -- and I can't quite figure
20 out the answer to this -- is it seems to me when they
21 filed that tax return in April of 2000, it was a
22 terrible loophole, but these lawyers have the job of
23 creating loopholes or at least trying to take advantage
24 of them. Okay? And the IRS had told them this was
25 okay. Indeed, they had informal advice to that effect.

1 Now, there's a -- you don't put the date of
2 the year 2000 reg, and I don't know if you're both
3 talking about the same thing. I was really surprised
4 there was no date there. Then what happens is, after
5 you lose in every circuit -- not you personally -- they
6 lose in every circuit; and then in the year 2009, they
7 say, though we lost and though we told everybody this is
8 okay at the time they filed the return, now we're going
9 to pass a new reg and we're going to penalize them,
10 taking all back this money 9 years later. That seems to
11 me pretty unfair. So, I'd like to know just that
12 answer.

13 MR. STEWART: Well, at the time that the
14 2009 regulation was promulgated first in temporary form,
15 we had lost cases in two courts of appeals. One was
16 Bakersfield in the Ninth Circuit, but the court of
17 appeals in that case said that because the statutory
18 language was ambiguous, the agency might be able still
19 to promulgate a regulation that would get Chevron
20 deference.

21 JUSTICE KENNEDY: And what was -- and what
22 was the date of that, Bakersfield?

23 MR. STEWART: That was in, I believe,
24 either -- I believe 2008 was the Ninth Circuit --

25 JUSTICE KENNEDY: Oh, okay.

1 MR. STEWART: -- decision in Bakersfield.
2 It was -- at any rate, it was before the -- the issuance
3 of the regulation in temporary form. A couple of months
4 before the regulation was promulgated, we had lost
5 Salman Ranch in the Federal Circuit, but that was by a
6 two-to-one vote. At that time, we had won this issue in
7 four trial courts --

8 JUSTICE KAGAN: But, Mr. Stewart, prior to
9 this latest round of litigation, had the IRS ever said,
10 ever given any indication, that it viewed Colony as not
11 controlling any -- any -- any longer?

12 MR. STEWART: Yes, I think probably the best
13 indication of our -- the position in the intervening
14 years -- and we agree that there's a surprising dearth
15 of law -- was the Fifth Circuit litigation in Phinney,
16 P-H-I-N-N-E-Y, which was decided in 1968. Phinney
17 involved a situation in which the taxpayer accurately
18 reported the amount of gross receipts, approximately
19 \$375,000, but misstated the nature of the receipts as
20 proceeds of a stock sale rather than of an installment
21 sale. And the reason that that misstatement of the
22 nature of the receipt made a difference was that it
23 potentially affected the taxpayer's entitlement to take
24 a stepped-up basis.

25 And so, the court of appeals in Phinney said

1 that was subject to the extended assessment period, that
2 the misstatement of the nature of the --

3 JUSTICE KAGAN: And as a result of this
4 case, had the IRS suggested in any kind of guidance or
5 rulings or anything else that it viewed Colony as an
6 outdated decision? Because, you know, I'm a taxpayer,
7 and I'm reading Colony and I'm thinking the language of
8 the statute is still the same; why wouldn't Colony
9 control?

10 MR. STEWART: Well, I -- I think one reason
11 you might think that is that if you were -- you -- the
12 opinion was not oblivious to the fact that the 1954 code
13 had been enacted in the meantime, and the Court went out
14 of its way to say: We are discussing only the 1939
15 code, and we are not pronouncing on the meaning of the
16 1954 code, other than to note that our -- our conclusion
17 in this case is consistent with the unambiguous language
18 of new 6501(e)(1)(A). And as the D.C. Circuit explained
19 in Intermountain, that is best read as a reference to
20 subparagraph (i), which says that for a trade or
21 business taxpayer, "gross income" will mean gross
22 receipts without an offset for the cost of acquiring
23 goods and services. So --

24 JUSTICE SCALIA: If --

25 MR. STEWART: -- I think, as a taxpayer, you

1 would at least be on notice that there was uncertainty
2 as to the proper meaning of the -- the code. Judge
3 Boudin had written for the First Circuit in a case
4 called CC&F W. Operations in 2001 that it was at least
5 doubtful whether the main holding of Colony carried over
6 to the new -- the 1954 code. That was certainly dictum,
7 but it also flagged the fact that this was a subject of
8 uncertainty.

9 And remember, the provision at issue here
10 doesn't bear on the legality of the taxpayer's
11 substantive returns. The only question is whether the
12 IRS has 3 years or 6 years to make an extended
13 assessment. So, as of 2003, when 3 years from the date
14 of the return had run for these taxpayers, I think the
15 -- what was out there gave them notice that there was at
16 least uncertainty whether Colony applied.

17 JUSTICE BREYER: You say in your brief on
18 page 4: "In 2000, the IRS issued a notice informing
19 taxpayers that Son-of-BOSS transactions were invalid
20 under the tax law." And you cite without a date. So, I
21 was sort of curious whether that particular cite came
22 before or after they filed their return.

23 MR. STEWART: I don't know whether --

24 JUSTICE BREYER: And they say that -- and
25 I -- in July 2000, 3 months after they were filed, the

1 Commissioner reiterated his view: "It has long been
2 held that the extended statute of limitations," da, da,
3 da, "is limited to when specific receipts or accruals
4 are left out of the" -- of gross income, which is
5 basically the Colony statement.

6 MR. STEWART: Well, the --

7 JUSTICE BREYER: Are you talking about the
8 same thing?

9 MR. STEWART: No. No, those were two
10 different documents.

11 JUSTICE BREYER: Okay.

12 MR. STEWART: The two --

13 JUSTICE BREYER: So, there are two different
14 documents. So -- so, in July, they're telling the tax
15 bar this is okay. And what you say is this document
16 here, which you refer to without a date, told them it
17 wasn't okay.

18 MR. STEWART: Well, first of all --

19 JUSTICE BREYER: I'd be rather curious if
20 you could sort that out.

21 MR. STEWART: Well, the 2000 notice that the
22 Respondents have cited -- I think the -- the most
23 important point to make about it is that it was the view
24 of a single -- of the district counsel for a single
25 district within the IRS.

1 JUSTICE BREYER: I -- I know there are many
2 ways of downplaying that, but I'm just curious as to
3 what happened. What about the one you cited? When was
4 that?

5 MR. STEWART: I don't know the exact date in
6 2000, but it has long been established that transactions
7 lacking economic substance and transactions motivated
8 purely for tax avoidance purposes may be disregarded
9 from -- by the IRS. That -- that was a pre-existing
10 proposition.

11 When we issued the notice with respect to
12 Son-of-BOSS transactions in particular, that was simply
13 the IRS's way of informing taxpayers that we regard this
14 particular avoidance mechanism as encompassed by the
15 general principle that transactions lacking economic
16 substance --

17 CHIEF JUSTICE ROBERTS: Well, yes, that's
18 the general principle. But the point you made just a
19 few moments ago is -- I think is responsive to that,
20 which is: We're not talking about the merits; we're
21 talking about a statute of limitations. The whole point
22 of a statute of limitations is some things that are bad
23 are -- are -- are gone.

24 MR. STEWART: That's --

25 CHIEF JUSTICE ROBERTS: You can't go back to

1 them.

2 MR. STEWART: That's correct, and that's the
3 proposition that the Respondents are citing the
4 different 2000 document for. They are citing it as
5 though it were a definitive statement of agency position
6 as to the operation of the assessment period. It -- it
7 was not that. It was a document issued by a single
8 district counsel. And in a sense, the -- the reference
9 to Colony as continuing to -- as though it continued to
10 govern the -- the 1954 code was dictum because the
11 district counsel, even in that document, stated that it
12 would not be inappropriate to --

13 CHIEF JUSTICE ROBERTS: At what -- at what
14 level of the IRS bureaucracy can you feel comfortable
15 that the advice you're getting is correct?

16 MR. STEWART: Well, this --

17 CHIEF JUSTICE ROBERTS: A single district
18 counsel -- you go to there and say, what do you think?
19 And it tells you, and you say, well, that's fine, but I
20 know you don't count; so, I want to talk to your
21 boss and boss --

22 (Laughter.)

23 MR. STEWART: No, this is not advice to the
24 taxpayer. That document was a memorandum from the
25 district counsel to another IRS official. The other IRS

1 official was seeking guidance with regard to the
2 question of whether we needed to get within the 3-year
3 assessment period or whether it was appropriate to rely
4 on the 6-year assessment period. And although the
5 district counsel cited Colony in a way that it suggested
6 that it continued to control the operation of the 1954
7 code, the district counsel stated on the facts of this
8 case it would not be inappropriate to rely on the --

9 CHIEF JUSTICE ROBERTS: So -- so, what that
10 -- what happened here is that the taxpayer came to the
11 same conclusion as a district counsel of the IRS.

12 MR. STEWART: That's correct, but not --
13 didn't come to the same conclusion as the IRS did in
14 litigating the case in Phinney, didn't come to the same
15 conclusion as the IRS did in --

16 JUSTICE BREYER: What about the -- that's
17 the July. What about this other, undated one? Now, I
18 notice what you say about it. You said that it
19 described "arrangements that unlawfully 'purport to
20 give'" them -- if I read that piece of paper, which I
21 might -- and you probably read it because you cited
22 it -- will I come away with the impression, uh-oh, these
23 loophole arrangements, Son of BOSS, which previously
24 seemed to be okay are now not okay? Is that the
25 impression I'll have?

1 MR. STEWART: I -- first I would say --

2 JUSTICE BREYER: Is that the impression you
3 had?

4 MR. STEWART: That notice would not say --
5 tell you anything relevant to the computation of the
6 assessment period.

7 JUSTICE BREYER: Okay. All right. That's
8 what I suspect. Then look at the unfairness of this.
9 I'm not saying there aren't worse unfairnesses in the
10 world, but, nonetheless, people spent a lot of money.
11 The whole Bar has gone to an enormous effort.
12 Everything up through 2000 being -- seems to say you can
13 do this. You have a case on point in the Supreme Court.
14 And then 9 years later, after continuous litigation, the
15 IRS promulgates a regulation which tries to reach back
16 and capture people who filed their return 9 years
17 before.

18 MR. STEWART: Again, I'm not quite sure what
19 you mean by saying: would seem to say that you could do
20 this. I don't think that there were any affirmative IRS
21 statements that could lead people to believe that the
22 Son-of-BOSS mechanism was okay, but what --

23 JUSTICE GINSBURG: Can you clarify,
24 Mr. Stewart, two things that Justice Breyer brought up?
25 One, he said that the IRS had given people advice that

1 Son of BOSS was okay; it would work -- this tax shelter,
2 this tax scheme, would work.

3 And then he said -- he suggested that a
4 basis is like deductions. And you agree that
5 overstatement of deductions don't get you the longer
6 statute of limitations. So, why -- why should an
7 inflated basis get you to 6 years when inflated
8 deductions don't? That's one question.

9 And the other question is, is it so, that
10 agents told people that Son of BOSS would work? Is --

11 MR. STEWART: No. No, it's not true that
12 the IRS had advised people that Son-of-BOSS transactions
13 were okay. It wasn't until 2000 that the IRS issued a
14 specific document that said, as a matter of agency
15 policy, they're not okay. But, again, that document was
16 just a kind of case-specific application of the more
17 general -- of the more general proposition that
18 transactions lacking economic substance can be
19 disregarded.

20 With respect to why the overstatement of
21 basis is treated differently from the overstated
22 deduction, that follows inexorably from the language of
23 the code. That is, Congress defined the conduct that
24 would trigger the general rule as an omission from gross
25 income, and because of the way that gross income is

1 defined, an overstatement of basis can lead to an
2 understatement of gain, which in turn is taken into
3 account in computing gross income. A deduction may
4 ultimately affect taxable income, but it doesn't affect
5 gross income. And so, there would be no way of reading
6 the statute to encompass that.

7 Now, as to why Congress would have done
8 this, I think a clue is furnished by subparagraph Roman
9 (ii), which is at the bottom of page 1a, and it says:
10 "In determining the amount omitted from gross income,
11 there shall not be taken into account any amount which
12 is omitted from gross income stated in the return if
13 such amount is disclosed in the return, or in a
14 statement attached to the return, in a manner adequate
15 to apprise the Secretary of the nature and amount of
16 such item."

17 And so, that provides a safe harbor that
18 says even if you fall within the general rule, even if
19 you understated your gross income by more than
20 25 percent, if, at some point in the return, you gave
21 the IRS adequate information to notice that the
22 misstatement had taken place, you will be off the hook
23 for the 6-year assessment period.

24 And I think that is highly relevant in
25 responding to the policy concern that Justice Harlan

1 identified in Colony. That is, Justice Harlan said the
2 reason we think that Congress intended to restrict the
3 statute to situations where an item is left off the
4 return altogether is that those would be the most
5 difficult for the IRS to catch; the IRS would be placed
6 at a special disadvantage.

7 Here in subparagraph (ii), Congress has
8 accomplished the same intent but through a different
9 mechanism. That is, it's made the general rule sweep
10 more broadly but given taxpayers an out where the
11 disclosures are adequate.

12 If I could reserve the balance of my time.

13 JUSTICE KENNEDY: Just on that point -- and
14 we'll find out in a minute -- is the Respondent going to
15 say, well, it's always implicit that you have a basis;
16 everybody knows you have a basis?

17 MR. STEWART: I don't think that --

18 JUSTICE KENNEDY: So, that's -- so, that's
19 necessarily what you're telling the government.

20 MR. STEWART: I don't think he will say --
21 I don't want to speculate too much on what he will say,
22 but I think his position is an overstatement of basis
23 could never trigger the assessment period because the
24 item of gross receipts would have been adequately
25 disclosed.

1 CHIEF JUSTICE ROBERTS: Thank you, counsel.
2 Mr. Garre, is it implicit that you always
3 have a basis?

4 ORAL ARGUMENT OF GREGORY G. GARRE
5 ON BEHALF OF THE RESPONDENTS

6 MR. GARRE: Your Honor, our position is the
7 one that the Court reached in Colony, which is that an
8 overstatement of basis is not an omission from gross
9 income. What the Court held in Colony was that an
10 omission -- an omission from gross income is where you
11 leave out a specific taxable item or receipt.

12 We think the court of appeals got it right
13 when it concluded that the statute of limitations on the
14 statute -- on the tax assessments at issue expired in
15 2003 and rejected the IRS's extraordinary efforts to
16 avoid that result by discombobulating this Court's
17 decision in Colony and by seeking to retroactively
18 reopen and extend the statute of limitations.

19 What the Government relies on principally is
20 the addition of subparagraph (i) in the code, and that
21 was added in 1954, before the Court's decision in 1958.
22 And I'd like to make a few points about subparagraph (i)
23 because I think it's the crux of the Government's
24 position.

25 The first is just the anomaly of their

1 argument, that by adding this subparagraph -- and it's
2 on page 1a of the addendum to the red brief -- which
3 explicates the definition of "gross income" in one
4 specific context, the sale -- the cost of goods or
5 services by a trade or business, Congress meant to
6 change the general rule -- and that's what it called it,
7 the "general rule" -- in subsection (A).

8 JUSTICE KAGAN: Well, why do you think they
9 added that paragraph? Because it seems clear that there
10 was a circuit split at that time about exactly this
11 question and that this paragraph was a response to that
12 circuit split. So, what else could Congress have meant
13 by it?

14 MR. GARRE: Well, Your Honor, I think that's
15 probably right. It thought it was agreeing with the
16 taxpayer side of the circuit split. There's legislative
17 history indicating that it also thought it was
18 addressing the computational rule of how to get gross
19 income, which factors into the 25 percent trigger.

20 I think what maybe is most important is that
21 this Court in Colony looked at the 1954 amendments at
22 the suggestion of the government and concluded that its
23 decision was consistent with the 1954 amendments.
24 That's in the last line of the decision.

25 JUSTICE KENNEDY: Were most of the --

1 JUSTICE GINSBURG: But that's got to mean --
2 that's got to refer to (i). It can't refer to the --
3 Harlan said two things. He said it's ambiguous;
4 therefore, I'm going to look at the legislative history
5 to find out what the predecessor section means.

6 And then he says: I'm not going to
7 speculate on what this new thing means, but I do want to
8 point out that the result we reach in Colony is in
9 harmony with the unambiguous language of 6501, et
10 cetera. The only unambiguous language that he could be
11 referring to is in (i) because he has just -- he had
12 said the earlier language was ambiguous.

13 MR. GARRE: Well, I don't -- I don't think
14 so, Your Honor. First of all, you're right, he referred
15 to the whole 6501(e)(1)(A), which includes both
16 subsections. It's not clear that he was identifying
17 subparagraph (i). He could have well been referring to
18 subparagraph (ii), along the lines of what my friend
19 just spelled out, because much of the Colony decision
20 was based on addressing the situation where the -- where
21 the IRS is at a special disadvantage because something's
22 been left out entirely. And that really kind of gets to
23 the heart of subparagraph (ii).

24 But the anomaly of the Government's
25 construction here today is that Colony would come out

1 differently, because Colony doesn't involve a taxpayer
2 involved in the sale of goods or service; it involved a
3 taxpayer in the sale of real property. So, even though
4 this Court in Colony said --

5 JUSTICE SOTOMAYOR: -- real estate developer
6 in the business of buying and selling property. So, I'm
7 not sure that I buy your argument that it can't be goods
8 and services, because that was the services of this
9 particular company.

10 MR. GARRE: Your Honor, the sale of real
11 property, whether in parcels or otherwise, has always
12 been treated differently than the sale of -- costs of
13 goods or services, which really is a term of art. And
14 if you go back at Colony, you can see that the Court
15 referred to basis, referred to property, and that's
16 precisely the way that the parties did in their brief.
17 The Solicitor General in its own brief framed the
18 question presented as overstatement of basis in the sale
19 of property.

20 That's the situation that we have here
21 today. The subparagraph (i) they're referring to is
22 addressed to the specific situation of a trade or
23 business involved in the sale of costs of goods or
24 services --

25 JUSTICE KENNEDY: And I --

1 MR. GARRE: -- which is different.

2 JUSTICE KENNEDY: I was going to ask in
3 conjunction with Justice Kagan's discussion, were the
4 pre-Colony cases that involved splits -- did most of
5 those or any of those relate to the sales of goods and
6 services or were they all real estate sales? Do --

7 MR. GARRE: Your Honor, the Uptegrove case
8 did, the Third Circuit case. But they involved -- the
9 fact is they involved both the sale of property and the
10 sale of goods and services. And at that time, no one
11 was drawing this bright-line distinction.

12 JUSTICE KENNEDY: Well, but the Congress
13 drew it, as I think is implicit in Justice Kagan's
14 question, when it talks just about goods and services.

15 MR. GARRE: It did do that. There was one
16 reason for Congress to address that specific situation,
17 in that there was a regulation that had defined "gross
18 income" differently. It's appended at the end of our
19 brief, and it was discussed in Uptegrove. So, there was
20 a reason to single that out. But I think the more --

21 JUSTICE KENNEDY: And the other reason, it
22 was goods and services. There's always FIFO and LIFO.
23 I mean, there's -- you know, taxpayers who sell goods
24 have inventory cushions. And so, the IRS is very, very
25 well aware that that kind of judgment is involved in all

1 these statements. It's not quite the same with basis.

2 MR. GARRE: Well, Your Honor, I think it's
3 the opposite, if I understand your question, which is
4 that taxpayers typically put more information which is
5 going to put the IRS on notice when you're dealing with
6 basis and the sale of property as opposed to the costs
7 of goods and services, which involve many transactions
8 and you're dealing with them in the aggregate. When
9 you're dealing with the sale of property, as in Colony
10 and here, you're dealing with specific disclosures as to
11 the basis.

12 Here, if you look on page 151 of the JA, it
13 lays out the adjustment in the basis. And the same was
14 true in Colony. And so, to the extent that there's a
15 distinction there, I think it cuts in favor of the
16 taxpayer.

17 The problem for the Government is all of the
18 amendments in 1954 were pro-taxpayer amendments as
19 relevant here; and yet, the Government's conclusion is
20 that by adding this subsection addressing the specific
21 situation, it meant to take away the general rule in a
22 way that hurt taxpayers. It's inconsistent with what
23 this Court said in Colony because the Court --

24 JUSTICE GINSBURG: Well, why would they be
25 redundant? I mean, if the statute without little (i)

1 meant what you said it meant, then there would be no
2 occasion to put this in, because "omission from gross
3 income" would refer to items of income, period. That's
4 -- so, what work does (i) do, if it just -- if the main
5 rule, the general rule, is as you say it is?

6 MR. GARRE: Your Honor, everyone agrees it's
7 not redundant, even the Government, because what it does
8 is, at a minimum, it has a computational effect of
9 affecting the 25 percent trigger. The amount to get to
10 the trigger has to be --

11 JUSTICE KAGAN: But you agree that that's
12 not why Congress passed that provision?

13 MR. GARRE: Well, it's not clear, Justice
14 Kagan. The -- the Federal Circuit in the Salman Ranch
15 case cited legislative history that suggested it was
16 trying to achieve just that result. But I think the
17 broader point I would make is it's not at all uncommon
18 for Congress to act to provide an answer to a specific
19 situation that had come up by explicating it. And yet,
20 one doesn't conclude that, in doing that, it's intended
21 to overstate -- override the entire general rule that's
22 stated, particularly where it doesn't touch the language
23 that's the subject of the general rule. Congress didn't
24 in any way touch the phrase interpreted in Colony,
25 "omission from gross income."

1 And the anomaly gets even greater if you
2 look at Congress's actions after Colony. In 1965,
3 Congress amended the heading. Now, granted it's only a
4 heading, but it amended it, the heading to the
5 subsection, to mean "Substantial omission of items,"
6 which is perfectly consistent with Colony's
7 interpretation, directly contrary to the Government's
8 interpretation.

9 In 1982, Congress re-enacted the same
10 language, "omission from gross income," found in the
11 provision at issue in Colony in 26 U.S.C. 6229, which is
12 the provision for partnerships. And yet, it omitted the
13 subparagraph (i) that the Government relies upon as the
14 transformative provision narrowing the general rule.
15 And so, why on earth would -- would Congress omit that
16 subparagraph if it did the transformative work that the
17 Government suggests?

18 The Government doesn't have a response
19 except to say that they have to be interpreted the same
20 way, which makes no sense given the emphasis it's
21 placing on subparagraph (i). I think the answer is, is
22 subparagraph (i) just doesn't have and was never
23 intended to have the transformative effect that the
24 Government suggests.

25 Whatever -- we can talk about what the Court

1 meant in Colony, but I do think that it's critically
2 important that Colony is entitled to full stare decisis
3 effect. In fact, it's stare decisis coupled with
4 Congressional re-enactment. The Government describes
5 the world after Colony, but the fact is, if you go back
6 and look, no one thought that Colony was just a ship
7 passing the night that had only retrospective
8 significance. Everybody, including the IRS, appreciated
9 that Colony was a landmark decision.

10 JUSTICE KAGAN: Well, Mr. Garre, where do
11 you find evidence of that? Because you cite some cases
12 in your brief that end up not really supporting your
13 position. And as far as I can see, there's only one
14 case after Colony that deals with the question of
15 whether Colony continues to govern after the 1954
16 amendments. And that case, which is Phinney, seems to
17 cut in the opposite direction. So, am I missing
18 something? Are there cases that -- that favor you that
19 say that, yes, Colony continued to control?

20 MR. GARRE: I think what my response would
21 be first as to Phinney, the Fifth Circuit has clarified
22 that the Government's construction of Phinney is just
23 wrong. Phinney was consistent with the Colony rule. It
24 dealt with a particular application of it.

25 JUSTICE KAGAN: Well, whatever the Fifth

1 Circuit said about Phinney, when I read Phinney, it
2 seems to me to cut in the Government's direction if not
3 to be entirely on all fours. But I asked, are there any
4 other cases that you have that suggest that the courts
5 did think that Colony was continuing to be the governing
6 rule?

7 MR. GARRE: If I could make one point on
8 Phinney, and then I'll address the other cases. I would
9 ask you to look at the Solicitor General's opposition
10 brief in Phinney, which recognized that Colony was the
11 governing principle. One would think that the
12 Government thought that Colony was just a shot in time,
13 had no ongoing significance, they would have said that
14 in the opposition brief in Phinney. The Solicitor
15 General accepted Colony as the governing rule, as
16 everyone did.

17 As to the cases, I think it's fair to say
18 that, no, we can't point to a case in the 1950s, '60s,
19 or '70s where they specifically confronted the question
20 before the Court today. But what I -- what I -- what I
21 can say is look at the cases that we cite in our brief,
22 and all of those cases discuss this Court's opinion in
23 Colony as if it continues to have lasting effect on the
24 interpretation of the "omits from gross income." And
25 yet, in the Government's -- the IRS's own internal

1 documents -- we cite two, 1976 and 2000 -- where the IRS
2 internally is treating Colony as a landmark decision
3 which controls on a current going-forward basis.

4 JUSTICE KAGAN: Because what I was thinking,
5 Mr. Garre -- and tell me what you think the consequence
6 of this would be -- is that if I were a tax lawyer and
7 somebody came to me and said is Colony still the rule, I
8 would have said: Well, I can't tell you 100 percent. I
9 think you're good 70 to 80 percent. You know, it's the
10 same language, and there's Colony out there, and -- and
11 -- and nothing the IRS hasn't said that Colony doesn't
12 control, but I can't -- so, I'm giving a 70 percent.

13 Do you win if that's the state of the world
14 as I see it?

15 MR. GARRE: Well, I don't know how you would
16 put a percentage on -- on, in effect, whether Colony was
17 a "step one" case or not. I mean --

18 JUSTICE KAGAN: Well, in terms of what a
19 taxpayer thinks, whether Colony continues to govern.

20 MR. GARRE: I think so. I mean, I think,
21 you know, the IRS's actions here really put taxpayers in
22 an extraordinary situation. I mean, they're taking a
23 decision of this Court that says an overstatement of
24 basis -- no, that's not an omission of gross income.
25 They're relying on the 1954 amendments to get around

1 that. Look at the Colony decision. The Colony decision
2 says the 1954 amendments -- no, this decision is
3 perfectly consistent with those.

4 And here comes the Government --

5 JUSTICE GINSBURG: But it also said before
6 that, Mr. Garre, and without doing more than noting the
7 speculative debate between the parties as to whether
8 Congress manifested an intention to clarify or --
9 clarify or change the 1939 code. So, not taking a
10 position on whether the new section changes the code.
11 And the part that is in harmony -- I can't see how that
12 could be read to mean anything other than the (i), which
13 is unambiguous and certainly in harmony with the result
14 in Colony.

15 MR. GARRE: Justice Ginsburg, the government
16 in Colony argued that the 1954 amendments compelled its
17 interpretation, which was the one that the Court
18 rejected. If -- if this Court -- this Court must have
19 considered that argument in reaching the opposite
20 conclusion. I think -- I think you're right, that it's
21 fair to describe that language as dictum. But this
22 Court has many times said that even if something is
23 dictum, if it explicates the Court -- Court's holding,
24 the lower courts and this Court would give it great
25 weight in its --

1 JUSTICE GINSBURG: But as I read it, it
2 isn't saying and Colony controls; it's saying we're not
3 going to take a position on what the 1954 code does,
4 whether it clarifies or changes.

5 MR. GARRE: I think that the prefatory
6 language there -- I think -- I think you're right.
7 That's a fair characterization. But, ultimately, what
8 the Court said was its holding was in harmony with the
9 new statute. And you can't reach that conclusion if you
10 agree with the Government's interpretation.

11 JUSTICE GINSBURG: But he says "unambiguous
12 language," and he can't mean the general rule because
13 he's already said that is ambiguous. He's got to mean
14 the new provision, which is certainly unambiguous.

15 MR. GARRE: I don't think it has to be (i),
16 Your Honor. I think it could be subsection (ii). We
17 don't know which one he was referring to. And the
18 reason why it could be subsection (ii) is because a
19 great deal of the Court's analysis dealt with the -- the
20 question whether the Commissioner was at a disadvantage.

21 I would like to address the rationale in
22 Colony. My friend has referred --

23 CHIEF JUSTICE ROBERTS: Before -- if I could
24 just interrupt you, before you do so, to follow up on
25 Justice Kagan's question.

1 Under our current regime, can you ever give
2 more than a 70 percent chance? Because you have, in the
3 absence of a definitive Supreme Court ruling, the IRS
4 can reach a different result and it can do that
5 retroactively. So, I mean, you don't disagree with
6 that, right? I mean, if we determine that Colony was
7 ambiguous, the IRS can change the rule in Colony, and it
8 can apply that rule, new rule, retroactively. That's
9 what our cases say, right?

10 MR. GARRE: Well, we do disagree with it --
11 I mean, I certainly accept the Brand X part of that.
12 What we disagree with is that (a) the IRS has the
13 authority to retroactively apply an interpretation of a
14 statute, which gets to the meaning of 7805(b)(1); and
15 (b) whether or not the regulation in this case on its
16 face applies it retroactively. But I accept --

17 JUSTICE SOTOMAYOR: Well, they can't -- they
18 can't change the interpretation of the statute, but they
19 are the agency with expertise to define a term within a
20 statute. Why don't they have the expertise to define
21 either what the words "gross income" mean or don't mean?

22 MR. GARRE: Well, they don't have any leeway
23 to overturn this Court's decision if that decision
24 specifically addressed the question. And that's the
25 language of Chevron, and as it turns --

1 JUSTICE SCALIA: No, and if it is --
2 according to Brand X, if it specifically addressed the
3 question and said that there was no ambiguity. But
4 according to Brand X, if there's ambiguity, despite a
5 holding of this Court, the agency can effectively
6 overrule a holding by a regulation, right? Isn't that
7 what Brand X says?

8 MR. GARRE: Brand X says that --

9 JUSTICE SCALIA: So, the only question here
10 is, as the Chief Justice put it, whether -- whether
11 indeed Colony meant by "ambiguous" ambiguous.

12 MR. GARRE: I --

13 JUSTICE SCALIA: It depends on what the
14 meaning of "ambiguous" is, right?

15 (Laughter.)

16 MR. GARRE: I don't think so, for this
17 reason: Because Colony -- at the beginning of the
18 Court's decision, Justice Harlan in a gracious way, as
19 the Chief suggested, pointed out that there could be
20 some ambiguity in the text. But then he went on to
21 apply the traditional tools of statutory construction.

22 JUSTICE ALITO: But I can hardly even think
23 of a statutory interpretation question that we've gotten
24 that doesn't involve some degree of ambiguity, if we're
25 honest about it. We take a case where there's a

1 conflict in the courts of appeals. And so, there was at
2 least enough ambiguity in those cases for one or more
3 courts of appeals to come to an interpretation that's
4 contrary to the one that we ultimately reach. So, what
5 degree of ambiguity is Brand X referring to?

6 MR. GARRE: Well, I would -- I would think
7 that Brand X refers back to Chevron and looks to the
8 first step of Chevron. Brand -- what Brand X is looking
9 to is whether or not -- it's really a step one or step
10 two case. And on step one, Chevron looks to whether
11 Congress has addressed the specific question presented.
12 And if you look at the Court's decision in Colony, what
13 Justice Harlan said was Congress was addressing itself
14 to the specific situation where a taxpayer actually
15 omitted some income receipt or accrual in his
16 computation of gross income, and not --

17 JUSTICE KAGAN: Well, that was the specific
18 situation, but then the question was, how clearly did
19 Congress speak to that specific situation? And in order
20 to get his result, Justice Harlan says first that the
21 statute is -- that the statutory text is ambiguous, goes
22 to a bunch of legislative history, and none of that
23 legislative history actually speaks to the exact
24 question before the Court, only by implication.

25 So, if you look at the whole of -- of the

1 Colony opinion, it sure seems as though there's a lot of
2 extrapolation going on and essentially a lot of
3 ambiguity.

4 MR. GARRE: Well, I would disagree with
5 that, respectfully, Your Honor. I think the -- the
6 holding of the Court -- and, again, it's entitled to
7 stare decisis effect even if this Court might approach
8 it differently today under different modes of statutory
9 construction or otherwise. The holding of the Court was
10 that Congress addressed the specific situation of
11 whether an overstatement of basis was an omission from
12 gross income, and the Court said no.

13 JUSTICE KAGAN: Well, in the end, there has
14 to be a resolution. But the question is, what does it
15 look like before you get to that resolution? And -- and
16 Justice Harlan is doing a lot of tap dancing there, you
17 know, going to this Senate report, going to that House
18 report, going to this colloquy, before he can come up
19 with an answer.

20 MR. GARRE: He was employing the traditional
21 tools of statutory construction, not just legislative
22 history. He talked about the structure and purpose and
23 the patent tax incongruities created by the government's
24 position that an overstatement --

25 JUSTICE GINSBURG: But he did say -- he did

1 say he was looking to -- he said the text isn't clear;
2 therefore, I look to the legislative history.

3 MR. GARRE: And that's a tool of statutory
4 construction.

5 JUSTICE BREYER: I agree with you on that.
6 The -- and I agree with Justice Scalia, actually. There
7 are many different kinds of ambiguity, and the question
8 is, is this of the kind where the agency later would
9 come and use its expertise? And you're saying here it
10 was up to the Congress and looking at what they had in
11 mind.

12 All right. Maybe that's the base -- best
13 ground, but suppose it turns out a majority think you're
14 not right on that. Okay? Now, here's my question:
15 Assuming you're wrong on that, which I'm not sure you
16 are, but assuming you're wrong, now we get to this
17 regulation. Here is my problem: One -- I have no doubt
18 at some level it seems rather unfair, but that instinct
19 is not enough. The question is what -- what's the law?

20 (A) You can say the word "open" doesn't
21 include this case. But we run into the problem that an
22 agency has great authority to construe its own
23 regulation.

24 (B) You could say that, well, there's this
25 statute out there that says don't apply it, and there

1 are two routes there. One is something to do with
2 language, which I think you can think of, which seems to
3 cut very much against you if read naturally, but you can
4 strain it to read it in your favor. And the other has
5 to do with a parenthetical where, once again, although
6 they left it out of their brief and they put in
7 ellipses, I can see why they left it out because when
8 you read it it's again ambiguous. We run into the same
9 problem.

10 Then you could say: Well, they're not
11 supposed to do these things retroactively, either on
12 common law administrative law grounds or something like
13 that; they shouldn't do it; it's unfair.

14 And they'll say: But, you see, it wasn't
15 that unfair; a child of 2 would have known this was a
16 loophole. That's how they would have characterized it.
17 And the IRS never said anything, except for one district
18 director in a different district that really encouraged
19 or underwrote this kind of thing. So, it's not nearly
20 as unfair as you think. If you live by loopholes,
21 you'll die by regulation. You know, something like
22 that.

23 So, looking at those four possible grounds
24 -- and I can't think of a fifth -- you take your choice.
25 Which is the strongest, and how do you apply to the --

1 reply to the objection?

2 MR. GARRE: Well, I think you would first
3 look at the language of the regulation and see whether
4 or not --

5 JUSTICE BREYER: "Open," that's the term.

6 MR. GARRE: -- by its terms, it applies
7 retroactively. This Court has made clear, it made clear
8 in the Bowen case, that it's not retroactively unless
9 there's a clear -- not retroactive unless there's a
10 clear statement of retroactivity. And our position is,
11 whatever else is true, that what the effective date
12 provision says and the preamble says, it's just unclear
13 about whether it's retroactive or not.

14 JUSTICE SCALIA: I never thought that a
15 revision of a statute of limitation was retroactive
16 legislation, just as I've never thought that a provision
17 altering rules of evidence for a crime, even for crimes
18 that were committed before that alteration, is
19 retroactive legislation.

20 MR. GARRE: Well, I --

21 JUSTICE SCALIA: You know, the crucial date
22 is the date -- at least it's not -- well, you can extend
23 the statute of limitations.

24 MR. GARRE: I think it's retroactive in the
25 worst way, for this reason: It at a minimum

1 extinguishes an affirmative defense, the statute of
2 limitations. This Court recognized that --

3 JUSTICE SCALIA: No, I --

4 MR. GARRE: -- in the Hughes Aircraft case.

5 JUSTICE SCALIA: So, say it's unfair, but
6 I'm not sure that the rule against -- presumption
7 against retroactivity technically applies.

8 MR. GARRE: Well, again, I mean, I think if
9 you look at Landgraf and the cases talking about what is
10 retroactive, this regulation here if it is applied
11 retroactivity -- retroactively has the consequence this
12 Court points to as the worst kind of retroactivity,
13 which is extinguishing a valid defense in litigation and
14 imposing new consequences for past actions. Hughes
15 Aircraft recognizes that, as do the many courts of
16 appeals that we've cited in our brief.

17 JUSTICE SOTOMAYOR: Presumptively because
18 you're saying that this is a new interpretation. But
19 the IRS is taking the position that the meaning hasn't
20 changed --

21 MR. GARRE: Well --

22 JUSTICE SOTOMAYOR: -- that it's just
23 clarifying some ambiguity that the courts have had; not
24 that it's had.

25 MR. GARRE: And with all due respect, the

1 law in 2003 when the statute of limitations expired was
2 Colony. Even if the Court -- the agency had leeway to
3 reinterpret it, it's changing the law. And the reason
4 why it's doing that is it's doing it retrospectively.

5 If you look at cases like Brand X, the
6 theory is you have one interpretation, and then the
7 agency going forward can have another one. In Brand X,
8 the agency sought to apply its -- its new interpretation
9 prospectively. Here, it's doing retrospectively, and
10 when it does that, it changes the law. Maybe the
11 concrete example of that is --

12 JUSTICE SOTOMAYOR: There's too many
13 presumptions in your answer. The first is that Colony
14 controlled --

15 MR. GARRE: No, no --

16 JUSTICE SOTOMAYOR: -- what to me itself
17 says it's not -- it's not interpreting the new
18 statute --

19 MR. GARRE: My point on that --

20 JUSTICE SOTOMAYOR: -- whatever its footnote
21 meant.

22 MR. GARRE: No, my point on that was not
23 that Colony controlled as a step one matter; it's that
24 even if the Government is right that Colony just said
25 this is one permissible reading, it was the law as the

1 -- it was the permissible reading and the law until the
2 government changed it. And the government didn't change
3 it, try to change it, until 2009. The statute of
4 limitations in this case expired in 2003.

5 And so, if the government can adopt a new
6 interpretation going forward, the question is, can it
7 apply that interpretation retrospectively during the
8 time frame in this case? And our position on that is
9 that they certainly haven't done so unambiguously. And
10 that -- as this Court said in *St. Cyr*, ambiguity means
11 unambiguous prospectivity. And the Court also
12 rejected --

13 JUSTICE KAGAN: Do you -- do you understand
14 the preamble as part of the regulation? Because if I
15 look at the preamble, the preamble seems pretty clear to
16 me. It seems to me that your view that the government
17 did not do this clearly enough must rest on looking at
18 the regulation without the preamble.

19 MR. GARRE: No. No. I mean, the Court
20 could -- I mean, certainly, we think you'd go first to
21 the regulation. And it says "was open." The preamble
22 says, quote, this is "not retroactive." It says it does
23 not apply to open tax -- it only applies to open tax
24 years, and not to reopen closed tax years. That's on 75
25 Federal Register 78,898. The government -- the way that

1 the government gets there is to say that, well, even
2 though we've passed the regulation long after the
3 statute of limitations expired, because this case is
4 pending, we can apply the new interpretation in
5 determining whether the period closed long before we
6 passed this regulation.

7 At a minimum, that's -- that's a highly
8 strained, if not convoluted, way to get around
9 retroactivity.

10 The way that the regulation's effective date
11 and the preamble speaks about whether this is
12 retroactive or not is really kind of nonsensical. And I
13 think, at a minimum, the taxpayer ought to get the
14 benefit of that, and this Court should say that if the
15 government really wants to do -- take the extraordinary
16 step that it's taken here to retroactively reopen a
17 statute of limitations, it ought to do so in clear terms
18 and not the convoluted way it's done here.

19 We also think that the -- the IRS just
20 lacked the authority to -- to legislate, to -- to pass a
21 new interpretation on a statute retroactively. That
22 gets to the meaning of 7805 and whether -- which says
23 regulations relating to a statutory provision enacted
24 after the '96 legislation which purported to strip the
25 IRS of authority to act retroactively, whether the

1 "enacted after" clause modifies "regulation" or
2 "statute." And we think, in context, it must modify
3 "regulation" because there's two types of IRS
4 regulations: regulations relating to statutes and
5 regulations relating to IRS internal practices.

6 And what Congress said is internal
7 practices -- sure, you can operate retroactively when
8 appropriate. With respect to new interpretations of
9 statutes, not retroactive. That was landmark
10 legislation as part of the Taxpayer Bill of Rights.

11 JUSTICE KAGAN: I take your point about the
12 purpose, but you would have to ignore every rule of
13 grammar that there is in order to read it your way,
14 don't -- wouldn't you?

15 MR. GARRE: Not if you read "regulations
16 which relate to statutory provisions" as -- as one
17 thing. Regulations which relate to statutory provisions
18 as opposed to regulations which relate to IRS
19 provisions. And if you look at the legislative history,
20 it's clear Congress was thinking about that distinction.
21 If you do read that as one unit, then the "enacted on or
22 after" obviously modifies that.

23 I think you have to look at it in context
24 and in light of the purpose of it, to get to that
25 conclusion. But courts have adopted that conclusion.

1 The American Council on -- American College of Tax
2 Counsel lays out those cases.

3 We think Judge Wilkinson got it right when
4 he referred to the IRS's position in this case as "an
5 inversion of the universe" and concluded that accepting
6 IRS's position would stretch accepted administrative
7 deference principles beyond their logical and
8 constitutional limit.

9 The IRS has the tools of its -- at its
10 disposal to identify tax deficiency and to take
11 appropriate action timely. Congress acted in 2004 to
12 respond to the precise situation precipitating this case
13 with Son-of-BOSS transactions. It amended 6501 not by
14 changing the meaning of what's an omission from gross
15 income, but by adopting a new provision which requires
16 taxpayers involved in listed transactions like Son of
17 BOSS to report many additional things, and saying that
18 the statute of limitations did not apply at all if they
19 didn't make those reporting requirements.

20 So, going forward, the only impact of the
21 Court's decision in this case is going to apply to
22 everyday regular taxpayers who simply erroneously
23 misstate or overstate the basis in the sale of a home or
24 other assets. There's no reason to take the
25 extraordinary steps that the IRS takes -- asks you to

1 take in this case to reach that conclusion.

2 We would ask the Court to affirm the
3 judgment of the court of appeals, to reject the IRS's
4 aggressive position on administrative power, and put an
5 end to a case that the taxpayer should have never had to
6 file in the first place.

7 CHIEF JUSTICE ROBERTS: Thank you, counsel.

8 MR. GARRE: Thank you, Your Honor.

9 CHIEF JUSTICE ROBERTS: Mr. Stewart, you
10 have 3 minutes remaining.

11 REBUTTAL ARGUMENT OF MALCOLM L. STEWART

12 ON BEHALF OF THE PETITIONER

13 MR. STEWART: Thank you, Mr. Chief Justice.

14 I'd like to make three quick points.

15 First, Mr. Garre refers to the amended
16 heading of section -- subsection 6501(e), which now
17 states "Substantial omission of items," but I think the
18 heading simply points up the fact that some provisions
19 within subsection (e) refer to amounts and some to
20 items. Subsection (e)(2), which deals with estate and
21 gift taxes, refers to omission of items.

22 And the legislative history makes clear that
23 Congress chose that term precisely to make clear that
24 the understatement -- or the overstatement or
25 understatement of an item that was reported will not

1 give rise to the extended period.

2 The second thing is that, at bottom,
3 Respondents argue that the -- that the phrase "amount of
4 gross income" should be construed to mean item of gross
5 receipts. And they don't offer any real textual
6 argument as to why that would be a sound reading.
7 Really, they rely exclusively on Colony. But the Court
8 in Colony said, at the beginning of its opinion, that it
9 was pronouncing only on the 1939 code. It said at the
10 end of its opinion that it was not generally trying to
11 construe the 1954 code.

12 And it stated that the relevant -- the most
13 relevant language was not unambiguous. And I think the
14 recognition of ambiguity is relevant in part because it
15 sets up our Brand X argument, but it's also relevant
16 because saying that a particular snippet of language is
17 ambiguous is to recognize that its meaning may vary
18 depending on context. And the --

19 CHIEF JUSTICE ROBERTS: Mr. Stewart, I know
20 you've got a -- your third point, and I want to let you
21 get it out, but you mentioned Brand X. Have we ever
22 applied Brand X to one of our decisions? Have we ever
23 said an agency by regulation can alter and change one --
24 a Supreme Court decision?

25 MR. STEWART: No. I mean, Brand X was the

1 first case that announced the Brand X principle, and the
2 Court has not applied it since.

3 Justice Stevens --

4 CHIEF JUSTICE ROBERTS: Well, but that was
5 applying it to a court of appeals decision.

6 MR. STEWART: That was applying it to a
7 court of appeals decision.

8 CHIEF JUSTICE ROBERTS: Right. We've never
9 said an agency can change what we've said the law means.

10 MR. STEWART: No. Justice Stevens wrote a
11 separate opinion in Brand X, suggesting that it might
12 not apply to decisions of this Court, but the Court as a
13 whole did not pronounce on that.

14 And then the third point I would want to
15 make is that Mr. Garre referred to cases and one IRS
16 General Counsel opinion that were issued during the
17 period between 1958 and 2000 that applied Colony to the
18 current statute, but they did so in a very specific way.
19 That is, they relied on the aspects of Colony that
20 talked about Congress's purpose to reserve the extended
21 assessment period for cases in which the IRS was at a
22 special disadvantage due to inadequate disclosure. And
23 those cases applied that language in elucidating current
24 subparagraph (ii), which provides a safe harbor in cases
25 of adequate disclosure.

1 Respondents' position goes much further,
2 though. Respondent is attempting to rely on Colony for
3 the proposition that even if its disclosures were
4 inadequate, the extended period still can't be applied
5 to it.

6 And none of the decisions on which
7 Respondents rely establish that proposition.

8 Thank you.

9 CHIEF JUSTICE ROBERTS: Thank you, counsel,
10 counsel.

11 The case is submitted.

12 (Whereupon, at 11:02 a.m., the case in the
13 above-entitled matter was submitted.)

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