IN THE UNITED STATES TAX COURT

[redacted] Petitioner,	)	Docket No. 8866-03
vs.	)	
COMMISSIONER OF INTERNAL REVENUE SERVICE, Respondent	)	

PETITIONER'S SUPPLEMENTAL MEMORANDUM OF AUTHORITIES IN OPPOSITION TO RESPONDENT'S MOTION FOR SUMMARY JUDGMENT AND IN SUPPORT OF PETITIONER'S CROSS MOTION FOR PARTIAL SUMMARY JUDGMENT

Pursuant to Tax Court Rule 121 and the Order of the Court on October 25, 2004, Petitioner submits the following Supplemental Memorandum of Authorities in Opposition to Respondent's Motion for Summary Judgment and in Support of Petitioner's Cross Motion for Partial Summary Judgment as follows**:**

INTRODUCTION

The Court ordered further briefing following oral arguments on Summary Judgment held on October 25, 2004. Petitioner's initial brief cited certain case law that indicated Antarctica should be classified as a foreign country for the purpose of IRC § 911. This supplement is intended to provide additional support to the arguments previously stated. Additionally, Petitioner argues that the text of Treas. Reg § 1.911-2(h) by no means excludes Antarctica from the regulatory definition and, even if the Court believes that some deference is owed to the regulation, Antarctica could reasonably be found to be within its definition. This supplemental brief also contains further arguments not addressed in Petitioner's opening brief.

ISSUES

1. What is the proper scope of judicial review of a regulatory statute?

2. Is the degree of deference owed to Treas. Reg. § 1.911-2(h), if any, affected if it is classified as a legislative regulation?

3. Does Treas. Reg. § 1.911-2(h) classify Antarctica as a foreign country under a literal reading of the regulation?

4. Do other "traditional tools of statutory construction" support the finding that Antarctica is a foreign country?

ARGUMENTS

1. Even if Treas. Reg. § 1.911-2(h) is construed to exclude Antarctica from its definition of foreign country, it is owed no deference as the determination of Antarctica's status can be properly decided under Step One of *Chevron*.

2. Even if Treas. Reg. § 1.911-2(h) is classified as a legislative regulation, it is owed no deference as the case should be decided under Step One of *Chevron*.

3. The text of Treas. Reg. § 1.911-2(h) does not exclude Antarctica from its definition of a "foreign country".

4. Various "traditional tools of statutory construction" support the determination that Antarctica is a foreign country for the purposes of IRC § 911.

A. EVEN IF TREAS. REG. § 1.911-2(h) IS CONSTRUED TO EXCLUDE ANTARCTICA FROM ITS DEFINITION OF FOREIGN COUNTRY, IT IS OWED NO DEFERENCE AS THE DETERMINATION OF ANTARCTICA'S STATUS CAN BE PROPERLY DECIDED UNDER STEP ONE OF *CHEVRON*.

As discussed in Petitioner's opening brief, the U.S. Supreme Court addressed the scope of judicial review of agency pronouncements in *Chevron USA, Inc. v. National Resources Defense Council,* 467 U.S. 837 (1984). Even though the recent case of *U.S. v. Mead*, 533 U.S. 218 (2001) may have curtailed the reach of *Chevron, supra,* the basic framework for judicial review of agency pronouncements remains unaffected.

In *Chevron*, the court announced a two-step process for the interpretation of regulatory statutes and ruled that deference to any agency interpretation arises only if it is determined that Congress has not addressed the issue. In *Chevron*, the Supreme Court held:

> "First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute." *Id.* at 842-43 (footnotes omitted).

To interpret a regulatory statute, a court first determines the extent to which the statutory meaning with respect to the issue before the court is clear. See *Atlantic Mutual Insurance Co., et al. v. Internal Revenue*, 523 U.S. 382 (1998). However, this initial determination is often something more than just merely reading the text of a statute; there is far more to it than that, and an analysis under this first inquiry known as "Step One" of *Chevron* can be extensive. If a determination is made at Step One, then Congress has "spoken to the precise question" and the interpretation is then resolved. See *Step One of Chevron v. National Resources Defense Council, Third revised draft American Bar Association Project on the Administrative Procedures Act*. Step One of *Chevron*, therefore, determines the role of the judiciary in interpreting regulatory statutes. In its formulation of Step One of the *Chevron* test, the Court included a crucial footnote:

> "The judiciary is the final authority on issues of statutory construction and must reject administrative constructions which are contrary to clear congressional intent. If a court, employing "traditional tools of statutory construction" ascertains that Congress had an intention on the precise question at issue, that intention is law and must be given effect." *Chevron*, 467 U.S. at 843 n.9 (citations omitted).

Therefore, using traditional tools of statutory construction, including dictionary definitions and statutory text, a court can determine if Congress has spoken on the issue.

Only if the statutory meaning is found to be ambiguous or if the statute is silent *after a Step One analysis* does a court then decide whether the agency's interpretation of the statute is permissible. This is often referred to as "Step Two" of *Chevron* and it is only under this step that the issue of deference arises. It is clear that this case should be resolved under a Step One analysis.

Clearly, courts can and do invalidate administrative pronouncements they find inconsistent a statute, without reaching the issue of deference (i.e., without going to Step Two). A recent Step One tax case which invalidated a regulation dealing with the disclosure of exempt organization determinations is found in *Tax Analysts* v. *Internal Revenue Service*, 350 F.3d 100, 102-105 (D.C. Cir. 2003). There, the Court did not even consider if deference of any sort was owed to the regulation because it found that Congress directly spoke to the precise question:

> "Because Tax Analysts claims that the Treasury regulations violate the Internal Revenue Code, we proceed in accordance with *Chevron U.S.A. Inc v. National Resources Defense Council*, Inc. (citation omitted). We first ask, as always, 'whether Congress has directly spoken to the precise question at issue.' Id. At 842. If it has, both we and the IRS 'must give effect to the unambiguously expressed intent of Congress.' Id. at 842-43. We evaluate the statute's clarity without deference to the agency's interpretation. (citations omitted). Only if we find the statute silent or ambiguous with respect to the question at issue do we proceed to Chevron's second step, asking whether the agency's interpretation is 'based upon a permissible construction of the statute.' 350 F.3d. 100 at 102-103.

The Petitioner asserts that if IRC § 911 is read to exclude Antarctica, such construction violates the Internal Revenue Code and, therefore, similar to the situation in *Tax Analyst, supra*, this Court must use the *Chevron* approach to resolve the issue. The first inquiry in a Step One analysis is statutory language, and under Step One this Court must first examine the statutory language itself using "traditional tools of statutory construction." See *Tax Analyst*, supra and *Atlantic Mutual Insurance Co., supra*. Following the lead of the Supreme Court those tools

clearly show that Antarctica should be found to be a foreign country based upon the plain language of the statute. While it may seem counter-intuitive that the Court must refer to sources such as a dictionary or other statutory text to discern if the meaning of a term is clear or unambiguous, that is exactly what *Chevron* requires. If a court finds that there is a plain meaning by using traditional tools of statutory construction, then Congress has spoken on the precise issue.

It can be forcefully argued that this case should be determined in favor of Petitioner under a Step One analysis due to the interplay between the ruling in *Smith v. U.S.*, 507 U.S. 197 (1993) and the prescribed analytical framework under *Chevron*. By finding in *Smith* that the ordinary sense of the word "foreign country" included Antarctica, the Supreme Court used a traditional tool of statutory construction, there using a dictionary definition, and found that Congress had spoken on the issue. Here, as the Court is called upon to interpret IRC § 911, the U.S. Supreme Court has provided the precise analysis and a road map under *Chevron* which compels a finding that the term "foreign country" has a plain meaning and one that includes Antarctica within the definition.

While the Supreme Court in *Smith* used other traditional tools of statutory construction to reach its decision, its first holding was based upon the ordinary meaning of the word. The court held that:

> "The common sense meaning of the term undermines petitioner's attempt to equate it with 'sovereign state.' The first dictionary definition of 'country' is simply 'a region or a tract of land.' *Webster's New International Dictionary*, 609 Second Ed. 1935. 507 U.S. at 201. … the ordinary meaning of the language itself, we think, includes Antarctica, even though it has no recognized government." (emphasis added) 507 U.S. at 202.

As the term "foreign country" was found to have a plain meaning, this Court should review the issue under *Chevron* Step One and find that IRC § 911 includes Antarctica as a foreign country.

It is interesting to note that the Supreme Court in *Smith* overruled the D.C. Circuit case of *Beattie v. U.S.*, 756 F.2d 91. In *Beattie*, the D.C. Circuit ruled that Antarctica was not a

foreign country for the purpose of the FTCA. The approach taken by the D.C. Circuit in *Beattie* was based upon a sovereignty analysis similar to that taken in *Martin*, and as set forth in Treas. Reg. § 1.911-2(h). Thus, the Supreme Court in *Smith* also rejected an analysis of the concept of "foreign country" strictly based upon a sovereignty test.

B. EVEN IF TREAS. REG. § 1.911-2(h) IS CLASSIFIED AS A LEGISLATIVE REGULATION, IT IS OWED NO DEFERENCE AS THE CASE SHOULD BE DECIDED UNDER STEP ONE OF *CHEVRON*.

Tax cases often distinguish between legislative and interpretative regulations. Legislative regulations are those promulgated to a specific grant of authority under some provisions of the Internal Revenue Code. Interpretative regulations are those promulgated under the general authority of IRC §7805(a), which directs the Secretary of Treasury "to prescribe all needful rules and regulations for the enforcement of this title." See *U.S. v. Vogel Fertilizer Co.*, 455 U.S. 16, 24 (1982).

Notwithstanding, deference to a regulation, either interpretative or legislative, only takes place under Step Two of *Chevron*. However, with legislative regulations, in the event that Step One is not dispositive, the courts often assess the validity of the regulation under a "arbitrary and capricious standard", whereas with interpretative regulations, the standard is one of "reasonableness." See *ABA Section of Taxation Report of the Task Force on Judicial Deference*, Tax Lawyer, Vol. 57, No. 3 at 728. It may be that the only effect of classifying the regulation as legislative would be to give it *Chevron* deference if an analysis occurred at Sep Two of *Chevron*. See *Mead*, 533 U.S. at 226-227.

Courts can and do overturn legislative regulations that are found inconsistent with the statute. For example, in *Rite Aid Corp. v. U.S.*, 255 F.3d 1357 (Fed. Cir. 2001), the Court of Appeals for the Federal Circuit invalidated legislative regulations dealing with consolidated returns.

C. THE TEXT OF TREAS. REG. § 1.911-2(h) DOES NOT EXCLUDE ANTARCTICA FROM ITS DEFINITION OF A "FOREIGN COUNTRY".

In the prior memoranda, the Respondent has cited *Martin v. Comm'r*, 50 T.C. 59 (1969), a case decided under prior IRC § 911, for the proposition that Antarctica should be not considered to be a "foreign country" for the purpose of current IRC § 911. As conceded by the government, the *Martin* case cannot be applied as precedent to the case before the Court. By focusing on *Martin*, one may erroneously assume that Treas. Reg. § 1.911-2(h) mandates the conclusion that Antarctica is not a foreign country. In *Martin*, the court cited a prior regulation that used more restrictive language to support its finding that Antarctica was not a foreign country. However, a close reading of the current regulation says nothing of the sort. Treas. Reg. § 1.911-2(h) states as follows:

> "The term 'foreign country' when used in the geographical sense includes any territory under the sovereignty of a government other than that of the United States. It includes the territorial waters of the foreign countries (determined in accordance with the laws of the United States), the air space over the foreign country, and the seabed and subsoil of those submarine areas which are adjacent to the territorial waters of the foreign country and over which the foreign country has exclusive rights, in accordance with international law, with respect to the exploration and exploitation of natural resources." (emphasis added).

The language employed in the regulation merely states that a foreign country "includes any territory under a sovereignty of a government other than that of the United States . . ." This does not require the exclusion of Antarctica from the definition, and there may be other circumstances where sovereignty may not be dispositive.

At oral argument, Petitioner noted that there are a number of countries around the world where the United States may not recognize the sovereignty of a particular government. For the reasons stated in Petitioner's opening brief, a more inclusive approach to "foreign country" status could be interpreted consistent with the regulation. This Court would not be required to

overturn this regulation in order to find that Antarctica is a foreign country, but would merely interpret the regulations' meaning more broadly. However, interpreting the regulation is not necessary here, as the case should be resolved under Step One of *Chevron*. Notwithstanding, including Antarctica within the current treasury regulation definition would be consistent with the analysis of the U.S. Supreme Court in *Smith* under a *Chevron*-like analysis. As stated above, the U.S. Supreme Court rejected the approach taken by the D.C. Circuit in *Beattie* where the determination of foreign country was based solely upon sovereignty. In rendering its opinion under *Smith*, not only did it find that Antarctica was a foreign country, but it rejected the approach under a sovereignty-based determination of foreign country.

The Respondent cited a revenue ruling interpreting the previous regulation. The Tax Court has traditionally afforded revenue rulings no deference whatsoever and, therefore, this interpretation of the prior regulation carries no weight for this Court.

Therefore, the Petitioner argues the regulation itself is not dispositive and would urge that this Court interpret the regulation in a manner which would include Antarctica within the scope of IRC § 911.

D. VARIOUS "TRADITIONAL TOOLS OF STATUTORY CONSTRUCTION" SUPPORT THE DETERMINATION THAT ANTARCTICA IS A FOREIGN COUNTRY FOR THE PURPOSES OF IRC § 911.

In a Step One *Chevron* analysis, the various "traditional tools of statutory construction" can be numerous. In addition to the statutory text and dictionary definitions, the court can look at statutory structure and framework, including other laws. Under this category, courts may look at other statutes for guidance. Importantly, courts have observed "the meaning of one statute may be affected by other acts, " *See FDA v. Brown and Williamson Tobacco Corp.*, 120 Sup. Ct. 1291, 1301 (2000) and *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 809 (1989). Accordingly, under this statutory tool, it is proper for the court to look at other authorities, and the

opinion in *Smith* and the opinion in *David Smith, et al. v. Raytheon Co.*, 297 F. Supp. 2d 399 (2004) is properly considered in this light as part of the *Chevron* Step One analysis.

An examination of foreign law concepts is also helpful and a proper tool of statutory construction. If one examines the various theories under international law to determine the status of a foreign country, Antarctica meets the definition under various configurations of the tests. *See Exploring the Foreign Country Exception: Federal Tort Claims and Antarctica*, David J. Betterman. In Mr. Betterman's article, he summarizes seven different theories, including the literalist, venue and statutory theories. This analysis was separate and apart from the FTCA. At least five different theories support the contention that Antarctica is a foreign country, even without a recognized sovereignty. For example, under one test, so long as the land is not subject to U.S. sovereignty, it is classified as a foreign country.

Subsequent legislative activity is a traditional tool, but here there does not seem to be any subsequent legislative activity that would be helpful.

Additionally, courts often look at legislative purpose. Courts routinely consider statutory purpose in their search for statutory meaning. Although policy arguments relevant in choosing among competing meanings for ambiguous statutory language are also within the province of Step Two, the general purpose of Congress in enacting a certain regulatory framework may provide evidence of legislative intent with respect to particular provisions that provide evidence of a range of meanings permissible under the statute. *See AT&T Corp. v. Iowa Utilities Board*, 525 U.S. 366, 412 (1999). As argued in Petitioner's opening brief, one of the legislative purposes of the IRC § 911 exclusion appears to be to offset the disadvantages of accepting a foreign post. Double taxation does not appear to have been the only concern, otherwise a tax credit regime would have been used. See *Rhoades and Langer*, U.S. International Tax and Tax Treaty §201.

Courts also use legislative history as one of the traditional tools of statutory construction. However, some courts have declined to look at legislative history as part of a Step One analysis. The different approaches have been characterized as the "intentionalist" v. "textualist"

approach. Textualist are not particularly concerned with discovering congressional intent, at least in as much as it differs from the directives found in the statutory language itself. *See Antonin Scalia, A Matter of Interpretation, Federal Courts and the Law*, 23-47 (1997). Intentionalists have traditionally considered legislative history to illuminate statutory meaning and congressional intent. *See Steven Breyer On the Uses of Legislative History and Interpreting Statutes*, 65 S. Cal. L. Rev. 845 (1992). Most legislative history of the statute is dated and not applicable. The definitional changes in the treasury regulations for "foreign country" may provide some support for Petitioner under this category.

Canons of construction are tools of statutory construction available for courts in a Step One review. Courts have long used these rules of interpretation as a guide to statutory meaning. Canons are employed to clarify and narrow meaning, so their use implies some amount of ambiguity or unclarity in the statutory text, and is one of the incongruities in this body of law. Canons usually do not come into play if the language is self evidently clear, incapable of more than one meaning. Recourse to dictionaries and statutory structure and legislative purpose, uncontroversial aspects of Step One inquiry, occurs because the statutory text, standing alone, is not entirely clear. Thus, even though the use of canons signals some ambiguity in the statutory text, the current judicial practice of using most of the canons in Step One to discern statutory meaning is consistent with other interpretative practices. *See Garrett, Step One of Chevron v. Natural Resources Defense Council, supra*. Many of the arguments made in Petitioner's opening brief should be considered by the Court as part of the canons of construction and, therefore, reference to the brief is hereby made.

Textual canons aim to discover what statutory text typically means to an ordinary speaker of the language and to discern the "plain" or "ordinary" meaning of the statutory provisions. They reflect linguistic conventions and understandings and are uncontroversially used by courts at Step One. *See Garrett, Step One of Chevron v. Natural Resources Defense Council, supra*. As argued above, these types of textural canons lend support to the characterization of Antarctica as a

foreign country. *See Chevron*, 467 U.S. at 860. Rules that are designed to reveal ordinary usage are particularly appropriate at Step One and, based upon *Smith*, support the Petitioner's position.

Substantive canons are also available for statutory interpretation at Step One. Substantive canons are rules of interpretation that do more than mirror wide-spread linguistic conventions; instead, these canons work to vindicate certain policy values. Substantive canons do not appear to have applicability here.

CONCLUSION

For the foregoing reasons, Petitioner believes that this is a case of first impression and, as Respondent is unable to demonstrate that Congress intended IRC § 911 to exclude Antarctica from its scope, summary judgment should enter for Petitioner. The other arguments contained in the initial Memorandum Brief in Opposition to Respondent's Motion for Summary Judgment and in Support of Petitioner's Cross Motion for Partial Summary Judgment concerning *res judicata*, and IRC §863 are valid arguments and further support the Petitioner's position in his motion.

RESPECTFULLY SUBMITTED this 26th day of January, 2005.

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Larry D. Harvey

CERTIFICATE OF MAILING

The undersigned hereby certifies that on this 26th day of January, 2005, a true and correct copy of the **PETITIONER'S SUPPLEMENTAL MEMORANDUM OF AUTHORITIES IN OPPOSITION TO RESPONDENT'S MOTION FOR SUMMARY JUDGMENT AND IN SUPPORT OF PETITIONER'S CROSS MOTION FOR PARTIAL SUMMARY JUDGMENT** was deposited into the United States mail, postage prepaid, addressed to:

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