

Sundstrand Corporation and Subsidiaries, Petitioner v. Commissioner of Internal Revenue, Respondent, 89 T. C. 810 (1987)

Evidence of post-taxable-year financial data may be excluded under Rule 403 if its probative value is substantially outweighed by the potential for undue delay and waste of trial time.

Summary

In *Sundstrand Corp. v. Commissioner*, the U. S. Tax Court ruled on a motion in limine to exclude post-taxable-year financial data in a complex section 482 case involving intercompany pricing. The court held that such data, although potentially relevant, was excludable under Federal Rule of Evidence 403 because its probative value was low and outweighed by the risk of undue delay and waste of time. The case underscores the court's discretion to manage evidence in lengthy litigations and the importance of focusing on facts directly relevant to the years in issue.

Facts

Sundstrand Corporation, a U. S. company, and its wholly-owned Singapore subsidiary, Sundstrand Pacific (SunPac), were involved in a tax dispute over the arm's length nature of intercompany pricing for the taxable years 1977 and 1978. The Commissioner of Internal Revenue had made adjustments under section 482, reallocating income from SunPac to Sundstrand, claiming the pricing was not at arm's length. During the stipulation process, the Commissioner sought to include financial data from 1979 and 1980 to illustrate the pricing mechanism, which Sundstrand contested as irrelevant and a potential waste of time.

Procedural History

Sundstrand filed a petition with the U. S. Tax Court on September 12, 1983, challenging the Commissioner's adjustments. The case was at issue by October 24, 1983. After four years of discovery, the case was proceeding through stipulations and was scheduled for trial on November 30, 1987. Sundstrand filed a motion in limine on August 11, 1987, to exclude post-taxable-year financial data, which was argued and heard on August 14, 1987, with the Commissioner's objection filed on August 31, 1987.

Issue(s)

1. Whether evidence of post-taxable-year financial data is relevant and admissible under Federal Rules of Evidence 401 and 402?
2. If relevant, whether such evidence should be excluded under Federal Rule of Evidence 403 due to the potential for undue delay and waste of time?

Holding

1. No, because while the data may have some relevance, it does not bear a direct relationship to the specific issues of pricing and profits for the years in question.
2. Yes, because the probative value of the post-taxable-year financial data is substantially outweighed by considerations of undue delay and waste of time, particularly given the complexity and length of the trial.

Court's Reasoning

The court applied Federal Rule of Evidence 403, which allows for the exclusion of relevant evidence if its probative value is substantially outweighed by the danger of undue delay or waste of time. The court noted the complexity and length of the section 482 case, with extensive stipulations already in place. It found that post-taxable-year data focusing on aggregate sales and profits did not directly relate to the specific pricing and profits for the years 1977 and 1978. The court emphasized the need to limit consideration to facts ascertainable at the close of the taxable years at issue, citing *Southern Pacific Transportation Co. v. Commissioner*. The court balanced the potential probative value against the significant time that would be consumed in presenting and rebutting this data, concluding that the evidence should be excluded under Rule 403 to promote judicial efficiency.

Practical Implications

This decision highlights the importance of judicial efficiency in complex tax litigation, particularly in cases involving section 482 adjustments. Practitioners should be mindful that courts may exclude evidence from later years if it does not directly relate to the issues in the taxable years at hand, especially if its inclusion would unduly prolong the trial. The ruling reinforces the court's discretion to manage evidence to prevent unnecessary delays and encourages litigants to focus on directly relevant evidence. In similar cases, attorneys should carefully assess the relevance and necessity of presenting post-taxable-year data, considering the potential for exclusion under Rule 403. The decision may also influence how parties approach evidence stipulations and trial preparation in lengthy and complex cases.