Manroe v. Commissioner, T. C. Memo. 2020-16, U. S. Tax Court (2020)

In Manroe v. Commissioner, the U. S. Tax Court ruled it lacked jurisdiction over penalties stemming from partnership-level adjustments under TEFRA, despite having authority over the related income tax deficiencies. The decision clarifies the court's limited scope in TEFRA cases, impacting how penalties related to partnership items are contested, as taxpayers must now rely on post-payment refund actions to challenge such penalties.

Parties

Lori J. Manroe and Robert D. Manroe were the petitioners, represented by Ernest Scribner Ryder. The respondent was the Commissioner of Internal Revenue, represented by Thomas Lee Fenner and Mark J. Miller.

Facts

The Manroes participated in a Son-of-BOSS tax shelter transaction through BLAK Investments (BLAK), a partnership subject to TEFRA. They reported losses from offsetting short positions in U. S. Treasury notes and Swiss francs. After the IRS determined BLAK was a sham lacking economic substance, the Manroes received deficiency notices for tax years 2001 and 2002, including penalties for gross valuation misstatement. They challenged the premature assessments and sought to restrain collection.

Procedural History

The IRS issued a final partnership administrative adjustment (FPAA) to BLAK, which was upheld in a subsequent Tax Court decision. Following this, the Manroes received notices of deficiency for their individual tax liabilities. They filed timely petitions in the Tax Court and moved to restrain collection of the premature assessments. The court had to determine its jurisdiction over the penalties.

Issue(s)

Whether the U. S. Tax Court has jurisdiction to redetermine penalties assessed under section 6662 in a partner-level proceeding following a TEFRA partnership-level adjustment?

Rule(s) of Law

The Tax Court's jurisdiction is limited to what Congress authorizes. Under TEFRA, the court has jurisdiction over partnership items but not over penalties that relate to adjustments to partnership items unless an exception applies. Section 6230(a)(1) states that normal deficiency procedures do not apply to computational adjustments, with exceptions listed in section 6230(a)(2) and (a)(3).

Holding

The U. S. Tax Court held that it lacked jurisdiction over the penalties assessed under section 6662 in the partner-level proceeding, as the penalties related to an adjustment to a partnership item and did not fall within the exceptions provided by section 6230(a)(2) or (a)(3).

Reasoning

The court reasoned that the penalties were computational adjustments stemming from the partnership-level determination that BLAK was a sham. The court relied on the Supreme Court's decision in Woods v. Commissioner, which established that penalties relating to adjustments to partnership items could be determined at the partnership level, even if they also involved affected items requiring partner-level determinations. The court rejected the Manroes' argument that penalties related to affected items (their outside bases) were distinct from penalties related to partnership items, as this was contrary to Woods. The court also noted that the exception in section 6230(a)(2)(A)(i) for affected items requiring partner-level determinations explicitly excluded penalties related to adjustments to partnership items. The court's decision was consistent with its prior ruling in Gunther v. Commissioner and the Eleventh Circuit's decision in Highpoint Tower Tech. Inc. v. Commissioner.

Disposition

The court granted the Manroes' motion to restrain collection and refund amounts related to the income tax deficiencies but denied their motion and granted the Commissioner's motion to dismiss with respect to the penalties.

Significance/Impact

Manroe v. Commissioner clarifies the jurisdictional limits of the U. S. Tax Court in TEFRA proceedings, specifically regarding penalties related to partnership items. The decision reinforces that such penalties must be challenged in post-payment refund actions, not in pre-payment deficiency proceedings. This ruling impacts taxpayers involved in TEFRA partnerships by limiting their ability to contest penalties before payment, potentially affecting their tax planning and litigation strategies. The case aligns with recent judicial interpretations of TEFRA's jurisdictional framework and may influence future cases involving similar issues.

