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IN THE SUPREME COURT OF THE UNITED STATES

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CHARLES G. MOORE, ET UX.,)

Petitioners,)

v.) No. 22-800

UNITED STATES,)

Respondent.)

- - - - -

Washington, D.C.

Tuesday, December 5, 2023

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 10:09 a.m.

APPEARANCES:

ANDREW M. GROSSMAN, ESQUIRE, Washington, D.C.; on behalf of the Petitioners.

GEN. ELIZABETH B. PRELOGAR, Solicitor General, Department of Justice, Washington, D.C.; on behalf of the Respondent.

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P R O C E E D I N G S

(10:09 a.m.)

CHIEF JUSTICE ROBERTS: We will --
we'll hear argument this morning in Case 22-800,
Moore versus United States.

Counsel.

ORAL ARGUMENT OF ANDREW M. GROSSMAN

ON BEHALF OF THE PETITIONERS

MR. GROSSMAN: Mr. Chief Justice, and
may it please the Court:

The word "income" is not an inkblot.
"Income" was understood at the time of the
Sixteenth Amendment's adoption to refer to gains
coming into the taxpayer, like wages, rents, and
dividends. Appreciation in the value of a home,
a stock investment, or other property is not and
never has been taxed as income. The reason is
that a gain is not income unless and until it
has been realized by the taxpayer.

The Court squarely held as much in
Eisner versus Macomber just a few years
following adoption of the amendment, and the
Court's decisions have held that line for a
century.

That precedent makes easy work of this

1 case. It is undisputed that the Petitioners
2 realized nothing from their stock investment.
3 They were taxed not because they had any income
4 but because, in 2017, they happened to own
5 shares in a corporation carrying retained
6 earnings on its books.

7 This is a tax on the ownership of
8 property. It therefore must be apportioned.

9 Dispensing with the need for
10 realization sweeps away what the Framers
11 regarded as the essential check on Congress's
12 power to tax property. The government cannot
13 identify a single thing that Congress couldn't
14 tax as income under its position that
15 realization is unnecessary. Without
16 realization, there is no limiting principle.

17 Accepting the government's position on
18 income would make a hash of the current law.
19 The Tax Code's gateway definition of "gross
20 income" exerts the full measure of Congress's
21 taxing power under the Sixteenth Amendment by
22 reaching all income from whatever source
23 derived.

24 If the government's position in this
25 case is right, then current law already requires

1 taxpayers to report and pay tax on appreciation
2 in the value of all their assets, on corporate
3 earnings for any stocks that they own, and on
4 any paper gains from their contracts and loans.

5 That's not how the income tax has ever
6 worked going back to 1913. Again, the reason
7 the law doesn't work that way is the obvious
8 one. Unrealized gains are not income. The only
9 way to make sense of the income tax as it's
10 existed for a century is to stick with the
11 original meaning of the Sixteenth Amendment.

12 The Court should reaffirm that there
13 is no income without realization.

14 I welcome the Court's questions.

15 JUSTICE THOMAS: When you say
16 "realization," what -- do you have a definition
17 for that or an explanation as to exactly what it
18 is, and -- and how is it different from, say,
19 attribution?

20 MR. GROSSMAN: Thank you, Justice
21 Thomas. Realization in the main is going to be
22 receipt, but in other instances, it would be
23 other types of enjoyment of an economic gain
24 such that the taxpayer can put that gain to his
25 or her own uses and benefits. That might be

1 forgiveness of a loan or it might be assignment
2 of income to a third party.

3 CHIEF JUSTICE ROBERTS: Well, there
4 certainly is realization here by the
5 corporation, if not the taxpayers, right? It
6 isn't a case like appreciation of property where
7 nothing has happened. You know, you buy a
8 property, you're holding it for 20 years, you
9 haven't sold it, nothing has happened. Here,
10 something has happened, and income has gone to
11 the corporation, isn't that right?

12 MR. GROSSMAN: Yes. The corporation
13 has income, and we -- we don't dispute that the
14 corporation realized income over the decade-plus
15 years that are being taxed by the MRT. But I --
16 I think it really is like the instance of simply
17 appreciation of property from the point of view
18 of the shareholders.

19 The shareholders' interest in the
20 corporation is solely a capital interest, a
21 property interest, and so the value of their
22 capital has increased. It has appreciated.
23 But, as shareholders, no, they have not realized
24 any income.

25 JUSTICE SOTOMAYOR: So tell me, what's

1 -- why do we permit taxing of individual
2 partners when either state law or their
3 partnership agreement doesn't realize the income
4 to them? In many states, a partner doesn't have
5 personal ownership, doesn't get the value of the
6 partnership, yet we've permitted that tax.

7 MR. GROSSMAN: Thank you, Justice
8 Sotomayor. A partnership is a fundamentally
9 different form of organization than a
10 corporation. The law has always recognized that
11 a corporation is a person separate from the
12 shareholders in that corporation. And there
13 simply isn't that separate personhood that
14 applies to partnerships. The partnerships are
15 simply a group of people who come together to
16 undertake a business activity, and when they do
17 so, the income that comes in to them is their
18 income directly. That's --

19 JUSTICE SOTOMAYOR: So what do you do
20 with Subpart F or Subpart S or all of the other
21 ways in which we have attributed corporate
22 income to individuals?

23 MR. GROSSMAN: The --

24 JUSTICE SOTOMAYOR: You don't
25 challenge -- you don't challenge the

1 constitutional of Subpart F.

2 MR. GROSSMAN: That isn't at issue in
3 this case.

4 JUSTICE SOTOMAYOR: But, in your
5 brief, you don't appear to be challenging it.

6 MR. GROSSMAN: We think that Subpart F
7 follows the commonly accepted method that
8 Congress has used to address situations when a
9 taxpayer has interposed a corporate structure
10 between themselves and income that is
11 otherwise theirs to the --

12 JUSTICE SOTOMAYOR: Well, but that's
13 the whole purpose of a corporate structure.
14 People do that all the time, particularly for
15 that purpose. You don't incorporate unless you
16 want the corporate shield. You don't
17 incorporate unless you want the benefits of the
18 corporate protection.

19 So, under your theory, Subpart F,
20 Subpart S -- these are longstanding taxing
21 mechanisms by the government -- your theory
22 would undermine those as well, wouldn't it?

23 MR. GROSSMAN: I don't think that's
24 right. Subpart F, again, works on simply
25 categories of income on a current basis where

1 those categories of income are properly viewed
2 as being -- and Congress determined are properly
3 viewed as being earned by the shareholders due
4 to the nature of the categories of income that
5 are addressed under the statute.

6 JUSTICE SOTOMAYOR: Well, it seems --
7 I'm sorry. Go ahead.

8 JUSTICE BARRETT: So you concede that
9 Subpart F is constitutional? I just want to be
10 sure that I understand your answer.

11 MR. GROSSMAN: We think that the
12 defect with the MRT doesn't really apply to
13 Subpart F. You know, Sub -- the Court has never
14 considered the constitutionality of Subpart F,
15 but, as we take it, we don't think that there's
16 a constitutional issue there.

17 JUSTICE BARRETT: So what is the
18 distinction? Is it just that other parts of
19 Subpart F, to the extent that they tax income,
20 do it on an annual basis and the MRT was a one
21 shot that went backwards?

22 MR. GROSSMAN: I think that's part of
23 it. But, again, I think what -- what it really
24 is is that the MR -- is that the MR -- is -- I'm
25 sorry -- is that Subpart F addresses this

1 fundamental income-shifting concept, whereas the
2 MRT doesn't, and that's so in two respects.

3 First of all, Subpart F operates on a
4 current basis while the corporation is subject
5 to the control of the controlling shareholders,
6 whereas the MRT takes no account of whether --

7 JUSTICE SOTOMAYOR: I -- I'm sorry.
8 There's no question that you meet the definition
9 of Subpart F. You need in Subpart F at least 10
10 percent of the company's share, and the company
11 has to be owned more than 50 percent by U.S.
12 owners. So it's identical in terms of the
13 percentage of ownership or the percentage of
14 shares.

15 MR. GROSSMAN: That's right, but
16 Subpart F, unlike the MRT, aligns the control
17 and the ability to redirect income with the year
18 that it is applicable to. The MRT takes account
19 --

20 JUSTICE SOTOMAYOR: It sounds to me
21 that what you're attacking is only a due process
22 issue of how long the tax is for, not the
23 ability to tax.

24 MR. GROSSMAN: I don't think that's
25 right for the reason that -- I think whether you

1 owned a particular piece of property on a given
2 date, which is the question that the MRT asks,
3 is sort of the sine qua non of a tax on
4 property, whereas Subpart F looks at income as
5 it comes in while the controlling shareholder
6 has the ability to redirect that stream of
7 income.

8 JUSTICE BARRETT: But isn't that then
9 just a question of whether it's fair to
10 attribute -- fair from a due process point of
11 view, as Justice Sotomayor was saying, whether
12 it's fair to attribute the income generated by
13 KisanKraft to the Moores, which is a distinct
14 question of whether there was income within the
15 meaning of the Sixteenth Amendment, right?

16 MR. GROSSMAN: Well, I think it
17 ultimately comes down to a Sixteenth Amendment
18 question for the same reason that the Court
19 thought so in Macomber, which is that a
20 shareholder's interest in a corporation,
21 including in its income, is a capital interest
22 and therefore a property interest.

23 And so, if there is some reason to
24 look beyond that and attribute income to the
25 shareholder, that would necessarily raise a

1 question of income and why it is that the
2 shareholder isn't being taxed on what would
3 otherwise be a property interest.

4 So I think the Court has always
5 addressed this sort of question as a question of
6 income, and that includes, for example, all of
7 the assignment-of-income cases that the Court
8 has decided over the years.

9 JUSTICE SOTOMAYOR: Can I go back to
10 square -- to first principles?

11 The concept of realization was very
12 well established at the time that the Sixteenth
13 Amendment was adopted, but the amendment does
14 not reference realization. All that the
15 drafters had to do was add the word "realize"
16 after "income" to lay and collect taxes on
17 income realized, but they never used the word
18 "realize."

19 And then I look at the history both
20 before and after the ratification, as far back
21 as 1864, not so far back, Congress taxed -- from
22 the ratification -- Congress taxed "gains and
23 profits of all companies, whether incorporated
24 or partnerships, in" -- "in estimating the
25 annual gains, profits, or income of any person

1 entitled to the same, whether divided or
2 undivided."

3 In 1913, just eight months after the
4 ratification of the Sixteenth Amendment,
5 Congress included undistributed corporate
6 earnings to certain shareholders.

7 Your brief tries to distinguish all
8 these things, but I come back to the main point.
9 Both sides can point to congressional actions
10 that taxed some realized income, some
11 didn't unrealize -- didn't tax unrealized
12 income, but we have examples of Congress taxing
13 realized -- unrealized income.

14 Why don't I take it that the plain
15 text of the amendment doesn't make reference to
16 realization?

17 MR. GROSSMAN: I think there are two
18 central features of the text of the amendment
19 that reflect that it does apply only to realized
20 gains.

21 The first is simply the use of the
22 word "income." I would particularly commend to
23 the Court's attention the amicus brief followed
24 -- filed by the Professors of Law and
25 Linguistics, which analyzes the use of the word

1 "income" in period text, but --

2 JUSTICE SOTOMAYOR: As I go back, all
3 of this goes back and forth, because the
4 government has other definitions. We're --
5 we're -- we're back in square one if what we're
6 doing is weighing historical definitions.

7 MR. GROSSMAN: The weighing in this
8 case, Your Honor, is quite lopsided. The
9 government relies principally on two definitions
10 that were -- that were put forward by economists
11 in the years following the amendment's adoption,
12 neither of which reflects the common
13 understanding at the time.

14 One of the economists recognized that
15 he was simply espousing his own economic views
16 divorced from any question of law or common
17 understanding, and the second economist
18 recognized that the common understanding of
19 "income" is what we say that it was, a realized
20 gain.

21 So far as the common understanding of
22 the term was concerned, the -- the only
23 indication that the Court has before it, aside
24 from dictionaries, which, again, lopsidedly
25 favor our position, is -- is the corpus

1 linguistics analysis of the Professors of Law
2 and Linguistics, which looks at how the word was
3 used in everyday language at that time, and it
4 concludes that unanimously, where it's possible
5 to distinguish, "income" meant realized gains.

6 There's also in the amendment the
7 language "from whatever source derived." As we
8 pointed out, "derived" was generally meant to
9 refer to concepts like receipts. And, indeed,
10 again, the amicus brief of the Professors of Law
11 and Linguistics recognize that when income was
12 described as being derived, it was always used
13 in that fashion.

14 JUSTICE KAGAN: I thought that --

15 JUSTICE KAVANAUGH: I guess I'm not
16 sure -- go ahead.

17 JUSTICE KAGAN: Go ahead.

18 JUSTICE KAVANAUGH: Go ahead.

19 JUSTICE KAGAN: I thought that that
20 was just a response to Pollock, which had
21 distinguished between income on personal
22 property and other forms of income, and all that
23 the Sixteenth Amendment authors were -- were
24 doing is to say that distinction that Pollock
25 drew, we don't approve of that distinction.

1 MR. GROSSMAN: Right. I think that
2 what the Sixteenth Amendment did was remove the
3 necessity to consider whether income came from
4 one source, particularly property, versus other
5 types of sources. But, in so doing, it
6 necessarily required as a precedent that the
7 amounts -- that what was being taxed, in fact,
8 be income and not something else.

9 JUSTICE JACKSON: But why should we
10 take the common meaning of "income" rather than
11 the legal meaning given the context that Justice
12 Kagan points out?

13 I mean, if the Sixteenth Amendment was
14 specifically responding to this Court's legal
15 precedent related to the meaning of "income," I
16 guess I'm curious as to why you think that the
17 common meaning of "income" is what we should be
18 focused on when we try to understand what the
19 Sixteenth Amendment meant when it used that
20 term.

21 MR. GROSSMAN: Well, that's certainly
22 the approach the Court typically takes in
23 addressing questions of original meaning, but
24 that aside, that's what the Court's -- Court's
25 cases have said for Merchants Bank and Macomber

1 again and again, that -- that the Sixteenth
2 Amendment is to be construed according to its
3 ordinary meaning.

4 And I would note that if the Court
5 were to depart from that and say, for example,
6 that personal property was not subject to
7 apportionment, which I take it to be the thrust
8 of the -- the questions in this direction, taxes
9 on personal property, that is, that would more
10 -- that would upend pretty much the entire line
11 of the Court's Sixteenth Amendment jurisprudence
12 over the past century --

13 JUSTICE SOTOMAYOR: But why?

14 JUSTICE KAVANAUGH: Are we --

15 JUSTICE SOTOMAYOR: I'm sorry. Go
16 ahead.

17 JUSTICE KAVANAUGH: No, go ahead.

18 JUSTICE SOTOMAYOR: All right. But
19 why? If what we do is to think about a
20 particular tax, which seems to be what we've
21 been doing for over a hundred years, to see
22 whether that tax is -- is income as understood
23 by attribution or as an excise tax or by other
24 principles, we wouldn't have to give -- we would
25 consider each tax on its own form.

1 You're asking us to just announce what
2 realization is out of context. And for the last
3 hundred years, we've been studiously avoiding
4 doing that because we recognize that it's
5 dangerous to do that. To -- to state a -- a
6 word like "realization," we then have to come up
7 with a working definition that applies to every
8 piece of property and every way in which people
9 gain wealth. It doesn't seem logical to me.

10 MR. GROSSMAN: Respect --

11 JUSTICE SOTOMAYOR: Why don't you just
12 concentrate on why Congress can't say that in
13 certain situations it's going to ignore the
14 corporate form and attribute to the individual
15 shareholders certain income? That's what it's
16 been doing all along. And, here, it doesn't
17 need realization because Congress has attributed
18 this to the individual owners of the
19 corporation.

20 MR. GROSSMAN: Respectfully, the Court
21 has already said in multiple occasions that
22 realization is, in fact, required for there to
23 be income under the Sixteenth Amendment. It's
24 not only Macomber. It's also McLaughlin versus
25 Alliance Insurance. It's the Safety Card

1 Heating.

2 JUSTICE SOTOMAYOR: Yes, on certain
3 types of property but not all.

4 MR. GROSSMAN: It's Ivan Allen.

5 JUSTICE SOTOMAYOR: Where we also said
6 that taxes can -- that partnerships can be taxed
7 individually even when the partners are not
8 receiving the property.

9 We have Subchapter F and S. We have
10 had all sorts of different forms of wealth that
11 we have attributed to individuals rather than to
12 the corporate -- to -- to the legal forms of
13 ownership.

14 MR. GROSSMAN: And all of those taxes
15 rely on the principle that the Court expressed
16 in cases like Horst and Banks, which is -- which
17 is that income should be taxed to he who earns
18 it and enjoys its benefits.

19 JUSTICE KAGAN: And putting aside,
20 Mr. Grossman, whether there's any realization
21 requirement at all, I mean, there is quite the
22 history in this country of Congress taxing
23 American shareholders on their gains from
24 foreign corporations, and you can see why,
25 right?

1 Congress -- the U.S. Government can't
2 tax those foreign corporations directly, and
3 they wanted to make sure that Americans didn't
4 kind of stash their money in the foreign
5 corporations, watch their money grow, and never
6 pay taxes on them.

7 So, you know, there's a long
8 century-old history of these kinds of taxes on
9 gains from your holdings in a foreign
10 corporation. Why is this any different and why
11 shouldn't we understand that to be quite well
12 settled, that Congress can implement those taxes
13 and enforce those taxes for those purposes?

14 MR. GROSSMAN: The taxes in that area
15 have typic -- have followed the pattern that I
16 described of simply a taxpayer interposing a
17 corporation between themselves and income that
18 would otherwise be theirs, and those provisions
19 from the beginning --

20 JUSTICE KAGAN: Well, that's this --

21 MR. GROSSMAN: Those provisions --

22 JUSTICE KAGAN: -- isn't it?

23 MR. GROSSMAN: It isn't. Those
24 provisions from the beginning have typically --

25 JUSTICE KAGAN: These are the same

1 shareholders as in Subpart F.

2 MR. GROSSMAN: The difference is that
3 those provisions have typically addressed things
4 like passive income and related party
5 transactions that are properly attributable to,
6 say, a parent corporation.

7 In other words, a parent corporation
8 could own an income-generating asset itself, or
9 it could simply shift that into a corporation,
10 into a foreign corporation, and thereby avoid
11 the income.

12 And what the law has recognized is
13 that just as in cases like Horst and Banks,
14 that's effectively an assignment of income and
15 that -- and that it can be attributed to the --
16 to the person who -- the parent corporation for
17 that reason because the parent corporation is
18 the one that controls the flow of the income as
19 it's coming in.

20 The MRT, by contrast, operates as a
21 tax on property. It doesn't take account of any
22 power that the shareholder had over the income
23 as it was coming in the door to the corporation.
24 It only takes account of the ownership in 2022.

25 JUSTICE KAVANAUGH: That seems to be

1 an argument about timing. In other words, we
2 have realization in this case. The entity
3 realized income. The question then is
4 attribution, and we've long held that Congress
5 may attribute the income of the company to the
6 shareholders or the partnership to the partners,
7 and the only real wrinkle, I think, here is that
8 it goes back and captures prior years' income.

9 MR. GROSSMAN: I think there are two
10 -- two wrinkles. One is that, with respect to
11 those prior years, the statute doesn't require
12 that the shareholders being taxed had any
13 ability to control the disposition of the income
14 in those years. That's a fundamental
15 distinction.

16 The second is that Subpart F --

17 JUSTICE KAVANAUGH: That's not true
18 for the facts of this case, though, correct?

19 MR. GROSSMAN: It is not true for the
20 facts of this case, but -- but --

21 JUSTICE KAVANAUGH: But you're saying
22 generally. Yeah.

23 MR. GROSSMAN: Well, I think -- I
24 think it just demonstrates that this is a tax on
25 property. In other words, do you own something

1 on a particular date, as opposed to what do you
2 do with the past? Did you have that power in
3 the past?

4 But, second, the provisions --

5 JUSTICE KAVANAUGH: If it had been
6 taxed year by year, would that have been
7 permissible?

8 MR. GROSSMAN: No, and that's the
9 second wrinkle, so to speak.

10 In this -- the -- the MRT is sort --
11 is the inverse of what -- of its press -- of its
12 predecessors in the statutes. All the
13 predecessors, like the foreign personal holding
14 company provisions, as well as Subpart F, focus
15 on categories of income. They're susceptible to
16 being reassigned into the corporate form.

17 Congress has never reached so far as
18 to tax shareholders of foreign corporations on
19 the active business income of those
20 corporations, but --

21 JUSTICE KAVANAUGH: Well, why is --
22 why is that different analytically? I mean,
23 this was all part of a big change from a
24 worldwide tax system to a territorial tax
25 system, and this is one piece of that, but I

1 guess I'm not sure why the -- which kind of
2 income is at issue matters for the ultimate
3 analysis of whether the attribution is
4 permissible.

5 MR. GROSSMAN: Because all of these
6 attribution schemes going back to the very
7 beginning have focused on effectively the
8 fraudulent or improper availment of the
9 corporate form to avoid income, and they've
10 always done that historically by focusing on
11 particular categories of income that are
12 susceptible to that type of abuse.

13 Congress took that to the max as it
14 amended Subpart F over the years to capture more
15 and more types of that sort of income avoidance.

16 What's interesting is that Subpart F
17 says you've captured the field, now let's get
18 everything else, and the "everything else" is
19 the active business income that's attributable
20 solely to the foreign corporation's own
21 legitimate business activities overseas. And so
22 a -- the shareholder in a foreign corporation
23 stands in no different position with respect to
24 that income than a shareholder in, say,
25 Microsoft or any other corporation.

1 This isn't the type of income that
2 that shareholder would, in the ordinary course
3 of affairs or as a matter of reality, be able to
4 shift around into a corporate form and thereby
5 avoid receiving it themselves.

6 I also want to address just the
7 difficulties that the government's
8 interpretation would raise with respect to the
9 current Tax Code.

10 As I noted, the Tax Code already --
11 already reaches the full extent of Congress's
12 authority under the Sixteenth Amendment. And if
13 the government is right, therefore, that certain
14 novel categories of income -- certain novel
15 categories of what had heretofore been regarded
16 as unrealized income or unrealized depreciation
17 were -- were subject to taxation under the
18 Sixteenth Amendment, then those would already be
19 subject to taxation under existing law.

20 JUSTICE JACKSON: Can I ask you a
21 question about your argument before you go on
22 with the government's?

23 So, if we agree with you that the
24 Sixteenth Amendment's use of income requires
25 realization and that the MRT does not meet the

1 realization requirement -- those are two, I
2 think, different steps of your analysis -- it
3 seems to me that all we've done is demonstrate
4 that the Sixteenth Amendment doesn't justify the
5 MRT.

6 Don't you still have to demonstrate
7 that the MRT is a direct tax in order to
8 establish that the Constitution has been
9 violated?

10 MR. GROSSMAN: Well, if the MRT is not
11 a tax on income, then I think it stands to
12 reason that it would be a tax on the ownership
13 of shares, because, otherwise, the --

14 JUSTICE JACKSON: Well, the government
15 makes another argument in their -- in their
16 brief. For example, they offer that it could be
17 an excise tax. So I guess my point is just any
18 indirect tax I would think just has to be
19 uniform under the Constitution. So it seems as
20 though it's your burden, regardless of this
21 issue about realization, to -- to establish that
22 this tax is a direct tax in order to sustain
23 your constitutional argument.

24 Am I wrong about that?

25 MR. GROSSMAN: We alleged below that

1 it was a direct tax. The government filed a
2 motion to dismiss. It argued that it was, in
3 fact, a tax on income. It did not dispute --

4 JUSTICE JACKSON: So I appreciate that
5 people haven't argued this. Would we then send
6 it back to the Ninth Circuit to determine this
7 issue of whether or not it's a direct tax?

8 MR. GROSSMAN: I think --

9 JUSTICE JACKSON: Or is it your
10 argument that we can -- we can sustain its
11 constitutionality just because we haven't had
12 briefing on this particular aspect of it?

13 MR. GROSSMAN: Well, I -- I think what
14 the Court could do is answer the question
15 presented. As to whether or not there would be
16 anything left for remand, I think it's at the
17 Court's discretion as to whether it wishes to
18 reach the government's excise tax argument.

19 So far as that argument is concerned,
20 again, the bare text of the statute operates
21 based solely on ownership of a particular piece
22 of property on a particular date and takes no
23 account of any type of business operations of
24 the people whom it's taxing.

25 That is the sort of tax that Flint,

1 which I think is the high watermark of the
2 Court's excise tax jurisprudence, indicates is,
3 in fact, a tax on property and cannot be
4 sustained as an excise tax. So I think the
5 Court could very easily make short work of that
6 argument.

7 Go -- go -- going to the government's
8 position in regard to --

9 JUSTICE ALITO: Is that argument
10 within the question presented?

11 MR. GROSSMAN: No, Your Honor.

12 JUSTICE ALITO: Was it preserved?

13 MR. GROSSMAN: No, Your Honor. It was
14 raised for the first time before this Court.

15 So far as the government's position is
16 concerned, I mean, just think about, for
17 example, if someone has a contract to sell
18 widgets to a third party in a future year. If
19 the price of widgets goes down so that they're
20 less expensive to manufacture or acquire, then
21 necessarily that person has received an economic
22 gain. Under the government's position, that
23 would be taxable. Thank you.

24 CHIEF JUSTICE ROBERTS: Thank you,
25 counsel.

1 Justice Thomas, anything further?

2 JUSTICE THOMAS: Would your case be
3 any different or your argument be any stronger
4 if you -- we were talking about real estate
5 rather than owning stocks in a corporation or an
6 interest in a corporation?

7 MR. GROSSMAN: No, Your Honor. Pretty
8 much all of the Court's Sixteenth Amendment
9 cases over the course of the last century have
10 concerned personal property in the form of
11 investments. I think it's well established at
12 this time that taxes on personal property --

13 JUSTICE THOMAS: Well, actually, what
14 I'm more interested in is not necessarily a
15 distinction between real and personal property
16 but rather being invest -- having an investment
17 in a corporate form or partnership where you can
18 actually -- there is an argument that -- that
19 the income had been realized by the corporation
20 or income had been realized, as you've heard
21 this morning, by the partnership and whether or
22 not that should then be attributed to the --
23 those who invest in those organizations -- in
24 those companies, whereas, in real estate, unless
25 there is a transaction, a sale or a lease or

1 something, there's no taxable transaction.

2 So would there be a difference between
3 a stake in a corporation or partnership, as
4 opposed to real estate or personal -- other
5 personal property?

6 MR. GROSSMAN: I don't think so. I
7 mean, the Court has applied the same principles
8 across the sweep of its Sixteenth Amendment
9 cases. Pretty much all of the early ones
10 applying the principle that we put forward did
11 involve corporate investments and different
12 types of corporate reorganizations that the
13 government argued resulted in income to the
14 shareholders.

15 But the Court applied the same
16 principles in cases like Horst, for example --
17 I'm sorry -- Bruun, for example, that involved
18 real property and recognized that in that
19 instance there equally had to be realization.
20 Likewise, in Blatt, the Court reached the
21 opposite result in Bruun with -- again, with
22 respect to an improvement made to real property.

23 So we don't think the constitutional
24 principles are any different. I think the only
25 difference perhaps with respect to corporate

1 shares is that the government might have an
2 argument that there is some type of constructive
3 realization under -- under the statute that
4 imposes the tax.

5 JUSTICE THOMAS: But isn't that a --
6 as a -- just based on the questions this
7 morning, that seemed to be a vulnerability that
8 you would not have with real property, for
9 instance.

10 MR. GROSSMAN: I don't think it's a
11 vulnerability given that the line -- given the
12 general principle that's required and given the
13 nature of this tax. I think it would be a more
14 difficult case if this tax were structured in an
15 entirely different fashion that didn't operate
16 in the way that it does, but that's obviously a
17 hypothetical that's not before the Court.

18 CHIEF JUSTICE ROBERTS: Justice Alito?

19 JUSTICE SOTOMAYOR: One last question.
20 Does your theory put at risk limited liability
21 companies, closely held corporations, limited
22 partnership corporations? I mean, there's all
23 sorts of corporate forms that are there. You --
24 your definition, I think, would affect the
25 government's ability to tax those individual

1 partners, no? Those individual shareholders.

2 MR. GROSSMAN: No, Your Honor.

3 JUSTICE SOTOMAYOR: Why not?

4 MR. GROSSMAN: We don't think that
5 those provisions present any constitutional
6 difficulty whatsoever. Again, a corporation is
7 different. The Court's cases have recognized
8 that.

9 JUSTICE SOTOMAYOR: What -- I don't
10 know why. Meaning, whether it's limited
11 liability or -- or closely held, it's still a
12 corporation.

13 MR. GROSSMAN: Well, first of all, I
14 mean, you've got -- distinguishing a corporation
15 from partnership, I mean, again, you have the
16 doctrine of corporate personhood that the Court
17 has long understood does make a difference in
18 these circumstances.

19 But so far as other types of
20 corporations like S corporations are concerned,
21 there is an election that is made by all of the
22 shareholders to those corporations to allow
23 pass-through taxation.

24 If somebody wants to come to the
25 government and say, I am earning income and

1 that's how I've organized my business and am
2 operating it, I think the government can accept
3 that as a concession.

4 JUSTICE SOTOMAYOR: We're going back
5 to whether attribution is legal. Thank you.

6 MR. GROSSMAN: I don't think it's a
7 question of attribution, Your Honor. I think
8 it's a question of a concession by the
9 shareholders.

10 JUSTICE SOTOMAYOR: Well, no, that's
11 exactly the point, which is why should they get
12 to choose and not the government where to
13 attribute the income.

14 MR. GROSSMAN: Well --

15 JUSTICE SOTOMAYOR: Thank you,
16 counsel.

17 CHIEF JUSTICE ROBERTS: Justice Kagan?

18 JUSTICE KAGAN: So, at the risk of a
19 little bit repeating some of the discussion,
20 it -- it seems to me that there are four
21 principal -- there may be others, but there are
22 four principal kinds of taxation that Congress
23 has repeatedly countenanced and that this Court
24 certainly has done nothing to get in the way of
25 that you have to distinguish here, and I just

1 want to make sure I understand your distinctions
2 and whether there's a single distinction that
3 sort of covers all of these or whether each one
4 has a different explanation.

5 So here are my four. It's Subpart F,
6 it's S Corporations, it's partnerships, and it's
7 taxing on an accrual basis. So give me why it
8 is that you think we can decide for you without
9 putting any of those kinds of very established
10 taxation schemes at risk.

11 MR. GROSSMAN: At a 10,000-foot level,
12 Your Honor, they all hew to the realization line
13 as it's been developed in the Court's cases and
14 by historical precedent.

15 JUSTICE KAGAN: See, I would have
16 thought that none of them hewed to the
17 realization line.

18 MR. GROSSMAN: I -- I think that the
19 --

20 JUSTICE KAGAN: I mean, that's why
21 this is my question, I guess.

22 (Laughter.)

23 MR. GROSSMAN: Again, Subpart F uses
24 that familiar -- that familiar mechanism of
25 simply attributing income to the person who

1 earned it even if they've directed it somewhere
2 else, and it's long -- and taxes of that nature
3 have long been justified on that basis.

4 S corporations, again, are by election
5 of the shareholders. If they concede that this
6 is, in fact, their income and that's how they're
7 operating their business, I don't think that the
8 government would have any basis not to take them
9 at their word should the government choose to do
10 so.

11 So far as partnerships are concerned,
12 again, there's no separate person that sits
13 above the shareholders of -- of a -- or, I'm
14 sorry, the partners of a partnership. And those
15 have always been treated differently going back
16 to -- I mean, gosh, going back to the Dartmouth
17 College case, where it wasn't even new at that
18 point.

19 But, with respect to income, going
20 back to Gibbons versus Mahon, which recognized
21 it as a well-established principle at that point
22 that corporations are different in that respect
23 from partnerships, indeed, that was the basis on
24 which Macomber rejected the same -- the same
25 argument.

1 And then, finally, with respect to
2 accrual, the Court already addressed that issue
3 in the Safety Car Heating & Lighting case, where
4 it held that standard Sixteenth Amendment
5 realization principles -- and -- and it cited,
6 among others, Macomber -- apply to the accrual
7 method of accounting.

8 So, you know, whatever question there
9 might be about that methodology and -- and its
10 constitutional status, I think, at this point,
11 that's been long established and is water under
12 the bridge.

13 JUSTICE KAGAN: Mm-hmm. And can I go
14 back to Justice Thomas's question, which is your
15 own definition of "realization"? And I'm just
16 going to give you Macomber's, and tell me if you
17 agree with it or disagree with it or think it
18 needs to be modified.

19 Macomber said, "That which precedes
20 from the property is severed from the capital,
21 is received or drawn by the recipient, that is,
22 the taxpayer, for his separate use."

23 Is that your definition too?

24 MR. GROSSMAN: I think subsequent case
25 law has recognized that the separation concept

1 maybe doesn't necessarily apply in every
2 circumstance, although it does apply in the
3 circumstance of distinguishing shareholders
4 versus corporations.

5 JUSTICE KAGAN: Yeah. So, for
6 example, in Bruun, we basically ignored the
7 separation requirement, correct?

8 MR. GROSSMAN: The Court said that it
9 was applicable in the corporate context but not
10 necessarily in other contexts, in that example,
11 for example, an improvement that was made to
12 land that was not severable from the land.

13 JUSTICE KAGAN: And that -- that
14 definition really wouldn't be very good to -- to
15 explain Subpart F, is that correct too?

16 MR. GROSSMAN: Well, I think what the
17 Court has recognized in subsequent cases is that
18 it's really the concept of realization as
19 opposed to, say, actual receipt that is
20 important.

21 I mean, look, it's going to --

22 JUSTICE KAGAN: So what you're saying
23 is basically we've left Macomber behind?

24 MR. GROSSMAN: No. I think the
25 Court's cases through Glenshaw Glass, you know,

1 up through as recently as, say, Indianapolis
2 Power & Light or Banks recognize that there is
3 something more that is needed -- that is needed
4 than a mere economic gain.

5 JUSTICE KAGAN: No, no, no. I wasn't
6 suggesting that we've left entirely behind any
7 concept of realization. I mean, that's a
8 different question, but that we've left the
9 Macomber definition of "realization" behind.

10 MR. GROSSMAN: I don't think -- I -- I
11 think that Macomber's holding in that respect
12 remains good law. I don't think that it's been
13 left behind.

14 Macomber goes on to recognize, for
15 example, regarding corporations that there may
16 be appropriate circumstances for the law to look
17 behind the corporate form to ascertain the true
18 right and actions of the shareholder with
19 respect to income.

20 And so I think take -- Macomber taken
21 as a whole does recognize this principle and it
22 used the best language that occurred to the
23 judges in the context of the case to express
24 that, look, in most cases, it's going to be
25 receipts, but in other cases, something else may

1 well qualify.

2 JUSTICE KAGAN: Thank you.

3 CHIEF JUSTICE ROBERTS: Justice
4 Gorsuch?

5 JUSTICE GORSUCH: I think the argument
6 we -- we've kind of heard from the other side
7 involves, okay, if there is a realization
8 requirement, it's met here because the
9 corporation realized the income, and then it
10 just becomes a question of attribution of that
11 realized income, and Congress has a free hand
12 there, and the Sixteenth Amendment says nothing.

13 Your response.

14 MR. GROSSMAN: My response is that
15 income is -- I mean, the Court has always looked
16 at questions of income from the point of view of
17 the shareholder. If you point to a Sixteenth
18 Amendment case or a case involving gross income
19 under -- under the Tax Code, the Court has
20 always looked at the individual circumstances of
21 the shareholder to ascertain whether or not
22 that -- that shareholder has actually realized a
23 gain.

24 And so, for example, Indianapolis
25 Power & Light, a 1990 case, the Court looked

1 specifically at the facts regarding certain
2 types of customer security deposits. It didn't
3 look at it as some sort of abstract inquiry
4 where things might be assigned and so forth. It
5 sought to address the question as to whether or
6 not that's shareholder income.

7 Macomber did exactly the same thing
8 with respect to shareholders of corporations. I
9 think the Court would certainly have to reverse
10 Macomber, which the government has not asked it
11 to do, to get beyond the idea that, you know, to
12 some free-floating notion of income is
13 sufficient for the government to point at
14 something and tax it to a particular individual
15 as their income.

16 JUSTICE GORSUCH: It -- it -- you're
17 saying, if I -- if I can put a fine point on it
18 if I understand it, the question is whether it's
19 income to the taxpayer who's being taxed?

20 MR. GROSSMAN: Yes, Your Honor.

21 JUSTICE GORSUCH: Okay. And then I'd
22 like for you to go back to a discussion you had
23 with Justice Jackson, and I understand your
24 point that the excise argument has been
25 forfeited or perhaps even waived in this case.

1 I just want your thoughts on it
2 generally as an original matter. You know, we
3 have the Hylton case from quite a long time ago,
4 carriages were thought perhaps not to be a
5 direct tax.

6 Could the government as an original
7 matter call this an excise tax?

8 MR. GROSSMAN: I think the answer
9 resoundingly would be no. The whole point of
10 the direct tax clauses was to make it difficult
11 for Congress to levy these types of taxes while
12 still leaving that authority available at -- you
13 know, in times of emergency.

14 And so far as taxes on personal
15 property and things like investments were
16 concerned, that was addressed extensively during
17 the ratification debates of the -- for the
18 Constitution, and it was really -- it was really
19 one of the primary arguments of the
20 anti-federalists against ratification of the
21 Constitution, was that permitting the
22 government -- permitting Congress to levy direct
23 taxes would simply be a step too far and would
24 -- and would allow Congress to destroy --
25 destroy the states and reach all the property

1 that was known to all families across the
2 country.

3 So, I mean, that was one of the
4 foremost concerns, and the way -- the way that
5 the Framers addressed that was to render these
6 types of taxes specifically subject to
7 apportionment. I mean, this was addressed and
8 discussed at the Connecticut, the Pennsylvania,
9 and the Virginia ratifying convention by James
10 Madison, by Chief -- Chief Justice Marshall.

11 It was a central concern at the time.
12 And as a matter of original meaning, this sort
13 of investment, this sort of property, is
14 something that necessarily was subject -- taxes
15 on it was subject to apportionment.

16 JUSTICE GORSUCH: Sorry. One last
17 question returning to my first one. Apologies
18 to shift you about.

19 If the Court were to hold that the
20 only realization requirement is some realization
21 somewhere along the chain by a corporation
22 antecedent to the taxpayer, what would be the
23 consequences of a holding like that?

24 MR. GROSSMAN: The consequences would
25 be to open the door to taxation of practically

1 everything. I mean, all property that a person
2 owns is the fruit of income at some point in
3 time, whether it might be income, you know, that
4 they received long in the past.

5 I mean, ultimately, all property that
6 we have is made up of flows of income that have
7 then been invested. And so, if all that was
8 necessary was some level of income, then
9 Congress could simply point at anything and say,
10 well, at some point, this was income to some
11 person at some level and, therefore, can be
12 subject to taxation without apportionment.

13 JUSTICE GORSUCH: I suppose we could
14 and maybe would have to draw lines as to how far
15 back in -- in time one can go in assessing that
16 chain of realization.

17 MR. GROSSMAN: That's right. And I
18 don't really understand how the Court would do
19 that based on the constitutional text. The
20 government's definition of "income" is simply
21 the increase in a person's wealth between two
22 points in time.

23 Well, if the time is set at a person's
24 birth or many decades in the past, that could
25 reach some or potentially all of their property,

1 and I don't really understand what the limiting
2 principle would be.

3 JUSTICE GORSUCH: Thank you.

4 CHIEF JUSTICE ROBERTS: Justice
5 Kavanaugh?

6 JUSTICE KAVANAUGH: In your brief, to
7 distinguish Subpart F and S corps and
8 partnerships, you used the phrase "constructive
9 realization," and I would ask if you could
10 define what you mean by "constructive
11 realization."

12 MR. GROSSMAN: Sure. We use
13 "constructive realization" as a blanket term to
14 encompass such concepts as constructive
15 realization and assignment of income, and it
16 just generally -- it refers to the general
17 principle espoused in cases like Banks and like
18 Horst that income should be taxed to the person
19 who earns it and enjoys its benefits.

20 And Congress, when it has enacted
21 cases relying on that sort of doctrine, you
22 know, has approached it in that nature, in other
23 words, assessing whether the income at issue is
24 something that in the ordinary course of affairs
25 could be attributed to the person, to -- to the

1 particular taxpayer at issue regarding, say,
2 categories of income or abuse of the corporate
3 form and so forth.

4 JUSTICE KAVANAUGH: Okay. Thank you.

5 CHIEF JUSTICE ROBERTS: Justice
6 Barrett?

7 JUSTICE BARRETT: Except there are
8 situations, you know, there are cases in which
9 state law said that partners couldn't have
10 control over the property or pull it out
11 unilaterally and which we've said it's okay for
12 that income to be attributed to the partner.

13 I understand that partnerships are a
14 different kind of form because, as an ownership
15 matter, the partners would own it equally, but I
16 guess I don't think our cases have established
17 control as the linchpin. Can you kind of point
18 me in the right direction if you disagree?

19 MR. GROSSMAN: With respect to
20 partnerships, if you accept the view that simply
21 a partnership's income is directly the income of
22 its partners, then restrictions on the use to
23 which partnerships may put their income, such as
24 distribution -- distributing it in certain
25 circumstances, is no different from a state law

1 preventing an individual from using their own
2 income in some particular fashion, spending it
3 on a particular item that they might wish to
4 purchase.

5 JUSTICE BARRETT: But I guess I just
6 mean that control -- you know, when we're
7 thinking about how to define "income," I'm just
8 questioning whether control can really be the --
9 the word to use, as opposed to just some sort of
10 distinction between capital and income, you
11 know, the, you know, seed and its fruit, right?
12 I mean, it seems to me that control might go a
13 little bit too far.

14 MR. GROSSMAN: I don't -- well, I --
15 control has always been an essential element of
16 income attribution statutes because the general
17 idea has to be that the taxpayer at issue has
18 the ability to redirect that stream of income
19 somewhere else and thereby avoid it and avoid
20 taxes on it.

21 JUSTICE BARRETT: Why isn't that a due
22 process issue? I guess this goes back to
23 Justice Gorsuch's point about what would the
24 consequences be and we would have to draw lines.
25 You said that means that something that was

1 earned income anywhere along the line ultimately
2 lands in, you know, my bank account and then it
3 can be considered income to me.

4 But is that a Sixteenth Amendment
5 problem, or is that a due process problem where
6 we have to draw lines about when it's fair to
7 attribute one person's income to someone else?

8 MR. GROSSMAN: I think it can raise
9 issues under both, but the Court has
10 traditionally considered it to be a Sixteenth
11 Amendment issue not only in Macomber but in
12 trust cases like Corliss, where, again, the
13 Court considered it a question of did the
14 taxpayer have control over the -- over the --
15 its stream of income that he had in that case
16 redirected into a trust for the benefit of his
17 close family members.

18 I mean, that's the way the Court has
19 always analyzed it, from the point of view of
20 the taxpayer and whether that taxpayer has
21 actually received income or not.

22 JUSTICE BARRETT: And last questions
23 about Subpart F. I just want to be sure that I
24 understand your position.

25 You say that income is about whether

1 the person has the ability to direct the income
2 stream. Am I accurately repeating what you said
3 when it's about attribution?

4 MR. GROSSMAN: I think that is a
5 necessary part of it, yes.

6 JUSTICE BARRETT: It's a necessary
7 part of it. And you've also said that Subpart F
8 corporations in general, of which, you know,
9 KisanKraft meets the definition, Subpart F
10 corporations and Subpart F do not pose the same
11 Sixteenth Amendment problem that you see here,
12 right?

13 MR. GROSSMAN: We -- we think that --
14 oh, do you mean with respect to the application
15 of Subpart F aside from the MRT?

16 JUSTICE BARRETT: Yes.

17 MR. GROSSMAN: Yes.

18 JUSTICE BARRETT: Okay. And is that
19 because -- kind of going back to your point
20 about control, is the distinction then between
21 MRT and the rest of Subpart F this idea that in
22 the other context, the shareholders have some
23 more ability to direct the stream?

24 MR. GROSSMAN: Well, I think it's two
25 things. It's not that they have more ability;

1 it's that they have any ability, because, again,
2 under the terms of the statute, the MRT doesn't
3 take account as to whether or not a shareholder
4 exercised control while that stream of income
5 was coming in the door. It only focuses on
6 ownership in 2017.

7 But also, that degree of control has
8 also been -- has also been combined historically
9 with the question of whether or not the types of
10 income being taxed are those that are
11 susceptible to that sort of abuse such that
12 attribution is appropriate.

13 JUSTICE BARRETT: You mean so there's
14 some sort of like fraud overlay to this, like is
15 this really functioning as a tax shelter, as
16 Justice Kagan was pointing out?

17 MR. GROSSMAN: That's how Congress
18 addressed it in the very first --

19 JUSTICE BARRETT: And that's a
20 constitutional requirement?

21 MR. GROSSMAN: I think Congress --
22 Congress certainly viewed it that way in the
23 very first income tax statute. That provision
24 regarding fraudulent avilment of corporations
25 to avoid income was specifically limited

1 specifically by many of the chief proponents of
2 the Sixteenth Amendment to avoid the precise
3 question that we're addressing -- the precise
4 defect that we're addressing today.

5 Their view was that you could not
6 ordinarily attribute corporate income to
7 shareholders but could do so only in the
8 instance where there was some sort of fraudulent
9 abuse of a corporation to avoid income. And
10 that's --

11 CHIEF JUSTICE ROBERTS: Justice
12 Jackson?

13 JUSTICE JACKSON: Yes. I'm interested
14 in your conversation with Justice Gorsuch about
15 the sort of original meaning of the direct tax
16 clause, and I'm trying to understand whether
17 it's your position that as -- as an original
18 matter, the direct tax clause was interpreted to
19 include income and all sorts of things, or was
20 it narrow.

21 I had thought originally, as we said
22 in the Hylton case, that it was pretty narrowly
23 focused on capitations and taxes on land. Am I
24 wrong about that?

25 MR. GROSSMAN: The Hylton case had

1 three seriatim opinions. Two of them viewed it
2 as a consumption tax regarding conveyance of
3 persons. The third of them, by Justice Iredell,
4 adopted the view that, well, if it's difficult
5 to apportion something, then it should not be
6 subject to apportionment.

7 JUSTICE JACKSON: What about Justice
8 Patterson's explanation that this was a pretty
9 narrow clause and that it was designed to
10 protect southern states and slavery from federal
11 interference, that that was really what was
12 going on here, and, therefore, when you're
13 looking at direct taxes, you're talking about --
14 or direct, yeah, taxes, as opposed to indirect,
15 you're talking about certain kinds of things and
16 that it's not necessarily others, income and
17 that sort of thing?

18 MR. GROSSMAN: Well, I think, as a
19 matter of original meaning, that's incorrect.
20 But I would note in the context of that opinion
21 it was dicta. It certainly didn't stand for the
22 position of the Court.

23 JUSTICE JACKSON: Did the Court, until
24 Macomber, hold that income was direct?

25 MR. GROSSMAN: Not with respect so

1 much to income, Your Honor --

2 JUSTICE JACKSON: Or, I'm sorry,
3 Pollock is what I'm saying, Pollock.

4 MR. GROSSMAN: Well, prior -- I mean,
5 I think the case that addressed this issue prior
6 to Pollock was Springer --

7 JUSTICE JACKSON: Mm-hmm.

8 MR. GROSSMAN: -- which did adopt the
9 narrower interpretation of the direct tax
10 clauses.

11 JUSTICE JACKSON: So, up until
12 Pollock, which was addressed by the Sixteenth
13 Amendment, we had a very narrow conception of
14 direct tax?

15 MR. GROSSMAN: For a 20-year period,
16 there was. Subsequent to that, as I -- as I
17 said, pretty much all of the Court's Sixteenth
18 Amendment cases over the past century have
19 concerned taxes on personal property in the form
20 of investments. So I think the Court would
21 really have to upend its jurisprudence if it
22 were to decide at this late date that the direct
23 tax clauses ought to be given some other
24 interpretation.

25 JUSTICE JACKSON: All right. Let me

1 ask you about realization, going back to Justice
2 Thomas's very first question, and what the
3 definition is.

4 I guess I'm trying to understand
5 whether you think Congress has the authority to
6 define what constitutes realization or not. Is
7 that something you are giving to the Court
8 through constitutional interpretation, or who --
9 who gets to decide what the realization line is?

10 MR. GROSSMAN: Well, I think, as an
11 initial matter, yes, I mean, Congress does get
12 deference on that. But it actually has to try
13 to do that, which is not what it did in this
14 case. I mean, again, the tax here on its face
15 turns on ownership of property on a particular
16 date, and it doesn't take into account it would
17 --

18 JUSTICE JACKSON: No, I guess I don't
19 understand your answer. If Congress -- could we
20 find that there is realization in this case,
21 that there is realization? Like, who -- who
22 makes the definition of "realization"? Could
23 the Court determine that there's realization
24 here under a definition that we are
25 appreciating?

1 MR. GROSSMAN: I mean, the government
2 has never argued that there's realization in
3 this case. The government has simply presented
4 its alternate -- the other argument that
5 realization is not required. So I think it
6 would be unusual for the Court to reach out and
7 decide a question of that import without the
8 government actually having addressed it.

9 JUSTICE JACKSON: But would -- are you
10 asking us to -- maybe I'm -- let me put it this
11 way. Are you asking us to adopt a particular
12 definition of "realization" under which your
13 client wins in this case? If we disagree with
14 you about what "realization" means, do you lose?

15 MR. GROSSMAN: We're simply asking the
16 Court to adopt -- to reaffirm the definition
17 that it's applied since nearly the dawn of the
18 Sixteenth Amendment. So I -- I don't think
19 we're asking --

20 JUSTICE JACKSON: Even though the
21 Sixteenth Amendment doesn't have realization in
22 it, you're saying that the implied realization
23 requirement has a definition that you're asking
24 the Court to adopt?

25 MR. GROSSMAN: We're simply asking the

1 Court to say that realization is necessary as
2 that concept has been espoused in the Court's
3 decisions over the course of a century.

4 JUSTICE JACKSON: Thank you.

5 CHIEF JUSTICE ROBERTS: Thank you,
6 counsel.

7 General Prelogar.

8 ORAL ARGUMENT OF GEN. ELIZABETH B. PRELOGAR
9 ON BEHALF OF THE RESPONDENT

10 GENERAL PRELOGAR: Mr. Chief Justice,
11 and may it please the Court:

12 The MRT is firmly grounded in the
13 Sixteenth Amendment's text and history. The
14 amendment allows Congress to impose taxes on
15 incomes. That phrase had a well-established
16 meaning drawn from numerous preratification
17 income taxes that Congress enacted before this
18 Court's decision in Pollock.

19 Several of those taxes were like the
20 MRT in that they taxed shareholders on
21 undistributed corporate earnings, including the
22 income taxes in 1864, 1865, 1867, and 1870. And
23 this Court upheld Congress's power to impose
24 those taxes in Hubbard.

25 The Sixteenth Amendment's drafters,

1 therefore, would have understood taxes on
2 incomes to include taxes like the MRT.

3 That's confirmed by the very first
4 income tax Congress enacted under the Sixteenth
5 Amendment. That 1913 law taxed certain
6 shareholders on their pro rata shares of
7 undistributed corporate earnings. And the trend
8 of pass-through taxation has continued
9 throughout the next century from taxes on
10 partners to S Corporation shareholders, to
11 foreign corporation shareholders under
12 Subpart F.

13 Against all that history, Petitioners
14 stake their case on Macomber. But the Court has
15 limited Macomber to taxes on particular stock
16 dividends that are not at issue here. If the
17 Court now extended Macomber's discussion to
18 invalidate all taxes on undistributed business
19 earnings, it would cause a sea change in the
20 operation of the Tax Code and cost several
21 trillions of dollars in lost tax revenue.

22 Petitioners say that every other
23 provision of the Tax Code could be saved under a
24 theory of constructive realization, but they
25 don't provide a comprehensive definition of that

1 term or explain why it would rescue every
2 provision except the MRT.

3 My friend today said it's a blanket
4 term that's defined by the circumstances where
5 you can say that constructive realization
6 occurred. But that's simply circular.

7 And by conceding constructive
8 realization, they've acknowledged Congress's
9 power to draw reasonable lines about what counts
10 as income and who can be taxed on it, which is
11 exactly what Congress did in the MRT.

12 Finally, the Court doesn't actually
13 need to resolve any fundamental questions in
14 this case about whether the Sixteenth Amendment
15 requires realization. The MRT taxes income that
16 was actually realized by the foreign
17 corporations, and Congress permissibly
18 attributed the tax on that realized income to
19 U.S. shareholders just as it has done in any
20 number of pass-through taxes throughout our
21 nation's history. The Court could say only that
22 and affirm.

23 I welcome the Court's questions.

24 JUSTICE THOMAS: When you say
25 "realized," "it has been realized," what do you

1 mean by that?

2 GENERAL PRELOGAR: I think that this
3 is a paradigmatic case of realization, Justice
4 Thomas, insofar as the thing that's being taxed,
5 the underlying tax base for the MRT, are the
6 earnings that actually were -- came into the
7 corporation, the foreign corporation's coffers.

8 So the tax base here was the
9 substantial ordinary business income that the
10 foreign corporation generated through its
11 operations in the foreign country and that has
12 to date been subject to tax deferral.

13 That income has never been taxed at
14 the corporate or entity level. Instead, what
15 Congress did in the MRT is enact a pass-through
16 tax that attributed the liability on that actual
17 income that was realized to the U.S.
18 shareholders.

19 JUSTICE THOMAS: Outside of the
20 context of the MRT, do you think that the --
21 just the -- the increase in value of real
22 property could be a taxable event?

23 GENERAL PRELOGAR: So I think that
24 that raises a more difficult question. This
25 presses on the idea of whether you can

1 characterize gains in the form of appreciation
2 as income that's taxable.

3 I -- I think that there's a strong
4 argument that that falls within a definition of
5 "income" that looks to whether there have been
6 economic gains over time, and it's important to
7 note that Congress has at various time imposed
8 taxes on that kind of appreciation.

9 Some of the Civil War era income tax
10 laws that I pointed to at the beginning of my
11 introduction had appreciation-based taxation for
12 certain property like livestock, and still today
13 there are really important provisions of the Tax
14 Code that effect -- effectively tax individuals
15 on appreciation. For example, the
16 mark-to-market taxes that my friend has conceded
17 are constitutional treat a taxpayer as though
18 there was a realizable event at the end of the
19 tax year for certain futures contracts, for
20 certain life insurance holdings, securities
21 dealers holding, that mark the amount of the
22 value to the market price even in the absence of
23 any kind of sale.

24 So I think that there is strong
25 support for the idea that you can tax at least

1 certain forms of --

2 CHIEF JUSTICE ROBERTS: Well --

3 GENERAL PRELOGAR: -- appreciation.

4 JUSTICE KAVANAUGH: In your --

5 CHIEF JUSTICE ROBERTS: Well, if
6 you're --

7 JUSTICE BARRETT: But --

8 CHIEF JUSTICE ROBERTS: -- there's
9 strong support -- I mean, you've -- you've
10 buried Macomber, I mean, and that takes away a
11 lot of the strong support for a pretty basic
12 proposition that the -- the government can't tax
13 as income to the property owner the appreciation
14 in value of the property.

15 So, I mean, what is left to defend
16 that proposition without Macomber?

17 GENERAL PRELOGAR: Well, Mr. Chief
18 Justice, I -- I disagree with the suggestion
19 that Macomber involved a tax on appreciation.
20 The Court there instead concluded --

21 CHIEF JUSTICE ROBERTS: Well, but I
22 mean I know your -- your argument that it's
23 limited to stock dividends, but it also has been
24 recognized as the -- at least in the beginning,
25 before it certainly narrowed over time, as

1 standing for the proposition that the government
2 cannot tax the appreciation in -- in property.

3 And you've taken that off the board in
4 your presentation today. So I, one, wonder if
5 you can give us a little more view or assurance
6 in what's left to defend that proposition once
7 you've stabbed Macomber.

8 (Laughter.)

9 GENERAL PRELOGAR: Well, Mr. Chief
10 Justice, I want to say that we're invoking this
11 Court's own precedent about Macomber's scope and
12 reach. It's the Court itself that said that
13 Macomber is limited to the particular type of
14 stock dividend at issue there. And -- and that
15 type of stock dividend didn't actually represent
16 any kind of economic gain to the taxpayer.

17 In other words, in Macomber, the
18 taxpayer received additional shares in the
19 company, but it was a stock split and her shares
20 were diluted in a commensurate amount so that
21 the Court said, from the taxpayer's perspective,
22 there was no difference in her ownership stake
23 in the company both before and after the
24 stock --

25 JUSTICE KAGAN: Well, I appreciate --

1 CHIEF JUSTICE ROBERTS: If you wanted
2 to -- if you wanted to defend the proposition
3 that the government cannot tax the appreciation
4 in property without -- without any other event
5 of realization, what would you cite given the
6 fact that Macomber is not on the table?

7 GENERAL PRELOGAR: Well, the thing
8 that I would cite if the Court were looking for
9 a limiting principle that takes appreciation off
10 the table at least in certain circumstances
11 would be history.

12 I -- I do think that there is a
13 different historical foundation for that type of
14 tax compared to what we have here, which is a
15 pass-through tax on actually realized corporate
16 income. So I think that the Court could reserve
17 judgment on whether there might be principled
18 lines based on the history of that type of tax
19 scheme to suggest that it wouldn't be what the
20 Framers of the Sixteenth Amendment had in mind.

21 But, again, I -- I do want to
22 emphasize the fundamental distinction between a
23 tax base that focuses on actually realized
24 income and then attributes it to a different
25 taxpayer, which is a prevalent feature of the

1 Tax Code and which involves many of the
2 provisions my friend today --

3 JUSTICE KAVANAUGH: And -- and your --

4 GENERAL PRELOGAR: -- has conceded are
5 --

6 JUSTICE ALITO: One of your strongest
7 --

8 GENERAL PRELOGAR: -- possibly
9 optional.

10 JUSTICE ALITO: -- one -- one of your
11 -- the arguments that you press most strongly
12 and, certainly, it has resonated a lot in the
13 coverage of this case is that the adoption of
14 the Petitioners' arguments would have
15 far-reaching consequences, isn't that correct?

16 GENERAL PRELOGAR: That's correct.

17 JUSTICE ALITO: So do you think it is
18 fair then to explore what the consequences of
19 your argument would be?

20 GENERAL PRELOGAR: I am happy to talk
21 about the consequences of our argument, although
22 I -- I want to say at the outset I think that
23 the Court could resolve this case quite
24 narrowly.

25 JUSTICE ALITO: Now the -- the Ninth

1 Circuit held that "The Supreme Court has made
2 clear that realization of income is not a
3 constitutional requirement but is instead
4 founded on administrative convenience."

5 Is that correct?

6 GENERAL PRELOGAR: The Ninth Circuit
7 was referring to this Court's decision in
8 Cottage Savings, where the Court did say that
9 realization requirements are founded on
10 administrative convenience.

11 JUSTICE ALITO: Well, not -- not the
12 question whether that's a correct interpretation
13 of our prior precedents. Is it your position,
14 as I understand you to argue in your brief, that
15 realization is not required? The Sixteenth
16 Amendment simply permits the taxation of income
17 whether realized or not?

18 GENERAL PRELOGAR: We certainly think
19 that there is no bright-line realization rule or
20 requirement under the Sixteenth Amendment and
21 that Congress is permitted to tax certain forms
22 of unrealized gains.

23 I don't want to suggest that the Court
24 here needs to set out to define "income" for all
25 purposes or to announce any bright-line rules

1 about realization. I think it's sufficient here
2 for the Court to say that you have before you a
3 particular type of tax on undistributed
4 corporate earnings that were actually realized
5 and to look at the history and tradition that
6 demonstrates that that fits well within
7 Congress's --

8 JUSTICE GORSUCH: General -- General
9 --

10 GENERAL PRELOGAR: -- income tax
11 authority.

12 JUSTICE ALITO: Well, what I'm trying
13 to do is to understand the breadth of your
14 argument, just as we need to understand the
15 consequences of -- of Petitioners' argument.

16 So I take it what you've said is that
17 realization is not a requirement. You say that
18 explicitly in your -- in your brief, unless you
19 want to walk back from that.

20 GENERAL PRELOGAR: We think they're
21 wrong to say it always is a requirement.

22 JUSTICE KAVANAUGH: We don't have to
23 agree with you on that for you to prevail I
24 think you've said in your opening as well
25 because, even assuming or leaving open whether

1 realization is a constitutional requirement,
2 there was realized income here to the entity,
3 and then it's attributed to the shareholders in
4 a manner consistent with how Congress has done
5 that and this Court has allowed.

6 GENERAL PRELOGAR: That's correct,
7 Justice Kavanaugh. We think that here the
8 constitutional question is actually quite easy
9 and it doesn't require the Court to consider
10 some of the foundational questions about the
11 meaning of the Sixteenth Amendment in other
12 consequence -- other contexts because, here, we
13 have paradigmatic realized income at the entity
14 level, and this functions just like the
15 pass-through taxes on partnerships, the taxes on
16 other types of corporate shareholders,
17 S Corporation shareholders, and, particularly in
18 the context of foreign corporations, the tax
19 under Subpart F of which the MRT is just a part.

20 JUSTICE GORSUCH: General --

21 JUSTICE ALITO: So your answer is that
22 there need not be realization by the taxpayer;
23 it's sufficient if there's realization by some
24 other entity, correct?

25 GENERAL PRELOGAR: Under the Sixteenth

1 Amendment, that's correct, although there is a
2 due process question in that context about the
3 limits on Congress's ability to attribute income
4 that was realized by one taxpayer to another
5 taxpayer.

6 JUSTICE ALITO: All right. That --
7 the due process question and that's a question
8 of substantive due process.

9 GENERAL PRELOGAR: That's how this
10 Court has analyzed it in cases like Burnet
11 versus Wells, where it was looking at the limits
12 on Congress's ability to make that kind of
13 attribution decision.

14 JUSTICE ALITO: And anything under
15 substantive due process involving an economic
16 regulation like this, the only thing that would
17 need to be shown is that it was rational for
18 Congress to do what it did?

19 GENERAL PRELOGAR: Yes. The Court has
20 looked at whether Congress has made an arbitrary
21 choice, whether it's acted unreasonably. But I
22 think that the Court's precedents reveal that
23 the Court really has looked at whether the
24 taxpayer who owes the tax liability has a
25 relationship to the underlying --

1 JUSTICE ALITO: Well, if this -- if
2 it's a rational basis review, then that's not
3 much, right? So we could say the 30-year
4 requirement here is a substantive due process
5 issue, so we don't have to grapple with it here.

6 But, to be honest, we would be saying,
7 you know, unless you can show it was irrational,
8 that would be sufficient.

9 GENERAL PRELOGAR: Well, I want to be
10 precise about the doctrine here. You mentioned
11 the 30-year lookback period. I think that that
12 actually has to do with retroactivity principles
13 under the Due Process Clause, and I think that
14 that's some -- somewhat different than the
15 attribution question that we had been discussing
16 about whether Congress can fairly attribute tax
17 liability to one person for income that was
18 earned at the entity level.

19 I recognize that maybe there are some
20 complicated questions out there that could exist
21 in this space, but the important point is that
22 here we have an enormous amount of history and
23 tradition on our side to support the idea that
24 this particular attribution decision falls well
25 within constitutional bounds.

1 JUSTICE ALITO: Well, I -- I -- I
2 understand you want to talk about this case,
3 and, ultimately, we have to talk about this
4 case, but I just want to understand how far your
5 argument goes, how far does it logically go.

6 So, under your argument, does the
7 Sixteenth Amendment allow the taxation -- it
8 allows the taxation of income, and you define
9 income as an increase in -- an economic gain
10 between two points in time.

11 So let's say that somebody graduates
12 from school and starts up a little business in
13 his garage, and 20 years later, 30 years later,
14 the person is a billionaire. Can Congress --
15 under your argument, can Congress tax all of
16 that on the ground that it's income?

17 GENERAL PRELOGAR: So, if that has
18 already been taxed, as I imagine it would
19 through annual income taxes, then it sounds to
20 me like the hypothetical is actually functioning
21 as a property tax --

22 JUSTICE ALITO: All right. Let me --

23 GENERAL PRELOGAR: -- insofar as
24 looking --

25 JUSTICE ALITO: -- let me change --

1 let me change this.

2 GENERAL PRELOGAR: -- at the total
3 value of the assets.

4 JUSTICE ALITO: The appreciation in
5 stock value over 20 or 30 years, could Congress
6 say we want to reach back and tax all of that?

7 GENERAL PRELOGAR: So I think that's a
8 hard --

9 JUSTICE ALITO: That's economic gain
10 between two periods of time.

11 GENERAL PRELOGAR: Yes. I --

12 JUSTICE ALITO: Between two points in
13 time.

14 GENERAL PRELOGAR: I think that's a
15 harder question, and here's why. I do think
16 that that would fit within an ordinary
17 conception of income as covering economic gain
18 between two points of time and focusing on the
19 increment of gain, but we don't have the same
20 tradition to support Congress levying income
21 taxes in that manner.

22 JUSTICE GORSUCH: Well --

23 GENERAL PRELOGAR: Now the Court
24 might conclude if it was --

25 JUSTICE GORSUCH: -- General --

1 General, I'm sorry to interrupt, but on this
2 point, in -- in your brief at least, and I
3 understand your argument is a little bit
4 different here today, but in your brief at
5 least, you confronted the -- the question
6 whether Congress could tax millions of Americans
7 who hold small amounts of stock in their
8 retirement investment accounts, and you say yes,
9 and you point to the 19 -- 1864 Civil War laws.
10 And then you say, but that would be
11 administratively unworkable.

12 So, as I understood at least in your
13 brief, the answer to Justice Alito's question, I
14 think, is, yes, that could happen.

15 GENERAL PRELOGAR: So I think this is
16 a really important point, Justice Gorsuch, and
17 let me clarify that that statement in the brief
18 was referring to the idea of pass-through
19 taxation on all large -- or -- or -- or all
20 corporate shareholders.

21 That would function like the MRT. The
22 basis for the tax would be the corporation's
23 earnings. And then the shareholders would be
24 responsible for a pro rata share of the
25 corporation's earnings. That's a different type

1 --

2 JUSTICE GORSUCH: I'm not sure --

3 GENERAL PRELOGAR: -- of

4 pass-through tax --

5 JUSTICE GORSUCH: -- that -- that --

6 GENERAL PRELOGAR: -- than I

7 understood --

8 JUSTICE GORSUCH: -- I'm not sure

9 that's clear. I -- it -- it seemed to me at

10 least that the argument was, that you were

11 dealing with, was the change in value over time

12 and stock prices increase. Could you tax that

13 unrealized -- otherwise what we'd consider

14 unrealized gain, treat that as a realized gain?

15 And -- and the answer is yes because they did

16 that in 1864 and because, if there's any

17 limitation, it has to do with administrative

18 workability.

19 GENERAL PRELOGAR: In 1864, they were

20 doing a pass-through tax on the corporate

21 earnings, and so the calculation of the tax was

22 not based on the appreciation in the shares but

23 rather was based on what the corporation had

24 actually earned as its income. I --

25 JUSTICE GORSUCH: Okay.

1 GENERAL PRELOGAR: And I don't want to
2 suggest that a tax on appreciation in stock
3 would necessarily be invalid. As I had
4 mentioned to Justice Thomas, there are
5 provisions on the books today that my friends
6 concede are constitutional.

7 But let me say that to the extent that
8 this question and Justice Alito's question is
9 pressing on the idea that maybe this kind of
10 appreciation should just be beyond the reach of
11 Congress's taxing power --

12 JUSTICE GORSUCH: No. I'm just asking
13 what the limits of your argument are, and -- and
14 it -- it seems to me there are none.

15 GENERAL PRELOGAR: Well, I certainly
16 think that Congress has broad taxing power. And
17 what I was about to say is that here the
18 relevant question is not whether Congress has
19 the power to tax in the first place. The Court
20 has said Congress has plenary power. It can tax
21 people just for existing. The question is --

22 JUSTICE GORSUCH: And if I could --

23 GENERAL PRELOGAR: -- whether that's a
24 direct tax that has to be apportioned --

25 JUSTICE GORSUCH: Sure.

1 JUSTICE PRELOGAR: -- or whether it's
2 subject to the rule of uniformity as an indirect
3 tax.

4 JUSTICE GORSUCH: And if I might
5 address what I now perceive to be kind of a
6 backup argument, so the first argument, the
7 brief argument, is no realization requirement.
8 Today, I'm hearing, well, even if there is
9 realization, there was somewhere-in-the-chain
10 realization, and then Congress can attribute it
11 freely as it wishes.

12 And I understand that argument, but
13 I'm not sure how we fit it with our precedent.
14 If we ditch Macomber, I understand your
15 argument. But let's assume Macomber isn't
16 completely misguided, okay? I think those were
17 your words, "misguided." I -- I look at
18 Phellis, I look at Bruun, I look at Horst, and
19 it seems to me at least as I read them that
20 they're all trying to work within Macomber's
21 framework and talking about is it fair to say
22 that there was realization to the taxpayer, not
23 realization somewhere back in the chain of
24 history and income realized by the corporation
25 or a parent or a subsidiary or whomever.

1 And just as a matter of precedent now
2 I'm talking, what -- what's mistaken about that?

3 GENERAL PRELOGAR: So, in those
4 subsequent cases, I wouldn't say that the Court
5 was mistaken there. It did happen to find a
6 realization on the facts of those particular
7 cases to the --

8 JUSTICE GORSUCH: For the taxpayer,
9 right?

10 GENERAL PRELOGAR: For the taxpayer.
11 Of course, they involved different types of tax.
12 None of those cases involved a pass-through tax.
13 And so I think, looking at what is maybe the
14 closest precedent to the situation that we have
15 here, I'd point to the Court's decision in
16 Heiner versus Mellon, which considered the
17 propriety of the tax on partners even in a
18 circumstance where they couldn't actually access
19 the partnership income --

20 JUSTICE GORSUCH: Sure.

21 GENERAL PRELOGAR: -- because state
22 law prohibited a distribution to them. And the
23 Court said --

24 JUSTICE GORSUCH: But you haven't
25 made a --

1 GENERAL PRELOGAR: -- that was
2 perfectly fine.

3 JUSTICE GORSUCH: -- you haven't made
4 an argument that there was realization to this
5 taxpayer, though, have you?

6 GENERAL PRELOGAR: But the whole
7 premise of pass-through taxation --

8 JUSTICE GORSUCH: I mean, just -- just
9 answer that --

10 GENERAL PRELOGAR: Yeah.

11 JUSTICE GORSUCH: -- before you launch
12 off. You haven't made that argument, right?

13 GENERAL PRELOGAR: We don't think that
14 the tax's constitutionality depends on whether
15 these taxpayers get a distribution because this
16 is a pass-through tax just like the other
17 contexts I've been mentioning. And I think that
18 there are kind of two ways --

19 JUSTICE GORSUCH: I'll take --

20 GENERAL PRELOGAR: -- to think about
21 it.

22 JUSTICE GORSUCH: -- I'll take that as
23 a yes.

24 (Laughter.)

25 GENERAL PRELOGAR: Well, I was about

1 to say there are two ways to think about it.
2 One is to say that there was a realized income
3 at the entity level, and Congress can
4 permissibly attribute that to the taxpayer.

5 Another way to look at it would be to
6 say that the taxpayer has a close enough
7 relationship to that underlying income for
8 Congress to permissibly treat it as income to
9 the taxpayer itself.

10 JUSTICE GORSUCH: But we don't have
11 that argument before us. What do we do about
12 that? That argument hasn't been made.

13 GENERAL PRELOGAR: Well, we certainly
14 intended to make that argument, and I understand
15 our briefing to focus on both aspects of this
16 issue. We, of course, joined issue with
17 Petitioners on whether the Sixteenth Amendment
18 requires realization because that is a --

19 JUSTICE GORSUCH: To the taxpayer or
20 to anybody, and you say no, it doesn't require
21 realization, and now today you're saying maybe
22 it requires realization but not to the taxpayer.

23 The one argument that I'm missing is
24 that there was realization here to the taxpayer.
25 That's just not even in the briefs. It's not in

1 the argument today. What do I do about that?

2 GENERAL PRELOGAR: Well, I think we
3 did say that --

4 JUSTICE GORSUCH: If you think there
5 is realization to this taxpayer, why didn't --
6 why didn't -- why didn't you make that argument?

7 GENERAL PRELOGAR: We are not
8 suggesting that there's anything like strict
9 realization in the sense of the taxpayer having
10 received something in hand. But I don't even
11 understand Petitioners now to be saying that's
12 what's required because --

13 JUSTICE GORSUCH: Well, of course --

14 GENERAL PRELOGAR: -- they concede
15 that any number of other --

16 JUSTICE GORSUCH: -- not. And -- and
17 our -- our cases in -- in -- in Bruun and Horst
18 say that there can be something like a
19 constructive realization in a partnership
20 situation or a fraud situation or an
21 S Corporation situation. We've been clear about
22 that, that there's some enjoyment that the
23 taxpayer has over that money, some control. He
24 may assign it elsewhere. He may choose to keep
25 it in the S Corp, whatever, but he controls it.

1 And so there's some realization under
2 Macomber's framework that's enough. But that
3 argument that this taxpayer had that kind of
4 enjoyment isn't in the briefs before us.

5 GENERAL PRELOGAR: Just --

6 JUSTICE GORSUCH: And I'm just
7 wondering what do I do about that.

8 GENERAL PRELOGAR: Well, I think we
9 did make that argument because we made the point
10 that to the extent the Court goes down the road
11 of recognizing some theory of constructive
12 realization, then the MRT would fit within that
13 same framework because Petitioners haven't
14 identified any actual distinction between how
15 those other tax contexts operate and how the MRT
16 operates.

17 JUSTICE GORSUCH: Let's -- let's just
18 say I don't see that argument. Then what do you
19 want me to do? Am I supposed to vacate and
20 remand if -- for -- for consideration of that
21 question? Is it waived? You know, what -- what
22 would you have me do?

23 GENERAL PRELOGAR: I -- I certainly
24 think that in our brief we argued that here the
25 taxpayers can properly be held accountable for

1 the -- the corporation's income and that the
2 Court can say that in --

3 JUSTICE GORSUCH: I got that -- I got
4 that argument, General.

5 GENERAL PRELOGAR: Yes.

6 JUSTICE GORSUCH: I got the argument
7 that either there's no realization or, as a
8 backup, there's realization and fair
9 attribution. But, if I'm working within this
10 Court's precedents, if I don't consider them
11 wholly misguided, okay, if I'm not willing to
12 overturn a hundred years' worth of precedent,
13 which you're asking us to do, and -- and the
14 question is, is it fair to say this -- this
15 taxpayer constructively or actually realized
16 this income, should I vacate and remand?

17 GENERAL PRELOGAR: No, you should
18 affirm because, here, we made the argument that
19 there is the same level of control and exactly
20 the same relationship as in Subpart F.

21 So we did make this argument, Justice
22 Gorsuch. We made the point that, if the Court
23 is focused on things like control or influence,
24 that there is no relevant distinction with
25 Subpart F because this is taxing in precisely

1 the same way as Subpart F operates.

2 JUSTICE BARRETT: And, General, what
3 do you think is the significance of Petitioners'
4 concession that Subpart F is constitutional to
5 your point?

6 GENERAL PRELOGAR: I think that that
7 is an incredibly significant concession here
8 because it demonstrates that even if the Court
9 were to apply a lens of control or influence, I
10 think the right word to use would be
11 relationship to the income, Petitioners have
12 acknowledged that 10 percent U.S. shareholders
13 have the requisite level of relationship in
14 order to properly have income attributed to
15 them.

16 Now my friend suggested that there's
17 some fundamental difference with Subpart F
18 because it taxes different types of income. I
19 think he said it's income where you can
20 interpose the corporate form.

21 I -- I -- I don't understand that
22 distinction because, of course, the Sixteenth
23 Amendment says that Congress can tax all income
24 from whatever source derived. So the Sixteenth
25 Amendment's text by its own terms makes clear

1 that the different forms of income being taxed
2 don't make a relevant constitutional difference.

3 And even if you look at it as a
4 factual matter, my friend's argument doesn't
5 withstand scrutiny because he suggested that,
6 for example, all of this income could have been
7 earned by the taxpayer himself. But that
8 doesn't explain many important features of
9 Subpart F, like ensuring risks outside the --
10 the country of incorporation for the CFC or
11 doing business in countries that are subject to
12 U.S. sanctions.

13 Those are parts of Subpart F income,
14 and I don't think that there is a relevant
15 distinction with respect to whether it could be
16 properly attributed to the taxpayer.

17 JUSTICE KAGAN: Justice Gorsuch said
18 you were asking us to overrule a hundred years
19 of our precedent. Sounds bad. Are you?

20 (Laughter.)

21 GENERAL PRELOGAR: I am not asking the
22 Court to overrule any precedent in this case.
23 I'm asking the Court to follow its precedent
24 that postdates Macomber and makes clear that the
25 discussion in that case was limited to the

1 particular type of stock dividend at issue
2 there.

3 I recognize that there is language in
4 Macomber that seemed to have broader sweep, but
5 this Court itself has already recognized that
6 that is not the right way to read the language
7 in --

8 JUSTICE KAVANAUGH: Which precedent --

9 JUSTICE GORSUCH: General -- General,
10 if I might, though, I mean, in -- in Macomber,
11 it said realization. You say that's misguided.
12 In Phellis, we said that we were following --
13 applying the tests laid down in Macomber. In
14 Bruun, we said that -- that -- that it was -- it
15 was following Macomber's understanding of
16 income. And in Horst, it said that we direct --
17 it said much the same thing. I'm not going to
18 bother with the quote. But, in each of those
19 cases at least, it purported to be faithfully
20 following Macomber.

21 GENERAL PRELOGAR: Justice Gorsuch --

22 JUSTICE GORSUCH: Now --

23 GENERAL PRELOGAR: -- I just --

24 JUSTICE GORSUCH: -- you just disagree
25 with that, I guess.

1 GENERAL PRELOGAR: I disagree with
2 that reading of those cases because I think, if
3 you look at each of the cases you mentioned, the
4 Court did find realization on the particular
5 facts there but using different standards than
6 Macomber itself had articulated.

7 Take, for example, Bruun. That was a
8 case where I think you said the Court was --
9 said it was faithfully applying its
10 interpretation of income, but -- but the Court
11 in Bruun specifically disavowed the aspect of
12 Macomber that said you have to be able to
13 separate the economic gain from the underlying
14 property.

15 JUSTICE GORSUCH: Certainly, it talked
16 about control, but -- but it -- it -- it -- it
17 spoke of applying Macomber. Now maybe you think
18 it was deluding itself, but that's how the Court
19 perceived what it was doing.

20 Shouldn't that count for something?

21 GENERAL PRELOGAR: But look at the
22 Court's statements in Griffiths. There, the
23 Court said that Macomber's theoretical bases had
24 been undermined, that it had "in effect been
25 limited to the particular type of stock dividend

1 at issue" there and that it didn't have
2 controlling weight even with respect to other
3 types of stock dividends --

4 JUSTICE KAGAN: So what --

5 GENERAL PRELOGAR: -- let alone other
6 types of economic gains.

7 JUSTICE KAGAN: -- so what do you
8 understand to be the current state of our
9 precedent? I mean --

10 JUSTICE GORSUCH: Yeah.

11 JUSTICE KAGAN: -- at a certain point,
12 you said, well, Macomber was confronting
13 something that that stock dividend had no
14 economic consequence whatsoever. And that was
15 true, and that could have been. I mean,
16 Macomber could have been decided in a paragraph
17 saying that, but that's not what the Court did.

18 Then, as you say, there are many cases
19 following Macomber which basically leave
20 Macomber's own theory of realization in the
21 dust, but what do you -- what do you take to be
22 the current state of our precedent that we need
23 to pay attention to?

24 GENERAL PRELOGAR: I think that if
25 this Court had before it another stock dividend

1 case that involved an economically substanceless
2 split, then Macomber would control. That's what
3 Griffiths said. Macomber's limited to that
4 particular type of stock dividend.

5 But the Court itself in any number of
6 follow-on cases has said that Macomber doesn't
7 have controlling weight outside that context.
8 The Court said in Glenshaw Glass the statements
9 in Macomber were not intended to provide a
10 touchstone for resolving all future gross income
11 questions that could arise.

12 So I think, to the extent that that
13 leaves Macomber as a bit of an island unto
14 itself, that is just the natural effect of this
15 Court's subsequent precedent, and we're asking
16 the Court to follow that precedent here.

17 JUSTICE KAVANAUGH: And the precedent
18 most on point for you I think you said is
19 Heiner, right, the partnership case?

20 GENERAL PRELOGAR: That's right. I
21 think it involved the most analogous tax to the
22 MRT.

23 JUSTICE KAVANAUGH: And why --
24 explain -- explain why that dictates the result
25 here or strongly supports the result here from

1 your perspective since that's the one you're
2 relying on most.

3 GENERAL PRELOGAR: It strongly
4 supports the result in this case because, in
5 Heiner, the Court confronted a situation where
6 partners claimed they could not lawfully be
7 taxed on partnership income on a pass-through
8 basis because state law operated to preclude any
9 distributions of that partnership income to
10 them. So, by definition, under state law, the
11 partners were not going to personally realize
12 that income. State law prohibited the
13 distribution.

14 And the Court rejected the claim from
15 the partners and said that it didn't make a
16 difference with respect to the permissibility of
17 that pass-through tax from the partnership
18 entity level to the partners themselves.

19 Now Petitioners have suggested that
20 partnerships can just be distinguished down the
21 line because they say that partnerships have a
22 different legal status than corporations.

23 But it's not like partnerships have an
24 innate legal status. Instead, they're creatures
25 of state law, and there are any number of states

1 out there that define a partnership as distinct
2 from the underlying partners themselves.

3 We also have good case law that
4 governs Subpart F in the lower courts. This has
5 been applied in numerous additional contexts
6 involving pass-through taxation and corporations
7 in particular, and it's not just the modern
8 laws, Justice Kavanaugh, it is all of the
9 history here.

10 For virtually the entirety of this
11 nation's experience with an income tax, there
12 have been laws on the book other than the brief
13 period when Pollock governed where Congress has
14 taxed corporate income at the shareholder level.
15 That is a classic pass-through tax and it's how
16 the MRT operates.

17 JUSTICE KAVANAUGH: I -- I agree with
18 that history and your description of it. I was
19 just isolating the -- the case that's really
20 kind of closest, I think, is Heiner, and I just
21 wanted you to spell that out.

22 JUSTICE BARRETT: Apart from -- I --

23 JUSTICE KAVANAUGH: What about the
24 fact -- I'm sorry.

25 JUSTICE BARRETT: Sorry, go ahead.

1 JUSTICE KAVANAUGH: Go ahead.

2 JUSTICE BARRETT: I was just going to
3 ask you, if Heiner is closest on this
4 pass-through point, what's your best federal
5 case upholding a federal tax on appreciation, or
6 do you have one?

7 GENERAL PRELOGAR: So I don't have a
8 case from this Court that upholds a tax on
9 appreciation. I think there are some -- some
10 lower court cases that have considered things
11 like accrual accounting or other situations.
12 There are fewer taxes that reach appreciation.
13 I think the pass-through mechanism is the more
14 common one when we're thinking about gains that
15 aren't realized to the taxpayer himself. But
16 there are, I think, a variety of -- of taxes out
17 there and have been through history.

18 JUSTICE BARRETT: Like the
19 mark-to-market one you were referring to before?

20 GENERAL PRELOGAR: Exactly. And it's
21 really important to recognize the importance of
22 being able to tax in that context.

23 The situation that Congress confronted
24 that prompted it to enact these mark-to-market
25 taxes is the fact that taxpayers can often

1 manipulate realization events.

2 So, for example, they can enter into
3 offsetting futures contracts that don't really
4 have any economic substance to them but allow
5 the taxpayer to hold on to the one that has a
6 gain, to defer taxation, maybe get favorable
7 capital gains rates, and to sell the one that's
8 a loss and thereby immediately have a taxable
9 event. And Congress recognized that that was
10 a -- a loophole in the Tax Code that could
11 enable this kind of -- of abuse.

12 JUSTICE BARRETT: So there are taxes
13 like the mark-to-market one that tax based on
14 appreciation, but it's fair to say that we would
15 be doing something new if we accepted your
16 argument that income is any kind of economic
17 gain, appreciation included?

18 GENERAL PRELOGAR: I appreciate the
19 opportunity to clarify because we are not
20 actually asking the Court to define "income"
21 that way.

22 I think, if there is a lesson to be
23 drawn from Macomber, it's that there's a real
24 danger in trying to -- to, as an abstract
25 matter, define "income" for all purposes or to,

1 you know, as -- as Glenshaw Glass said, to
2 provide a touchstone for all future cases, in
3 part because our experience with the Tax Code is
4 that taxpayers often latch on to those
5 statements and use it as a basis to try to avoid
6 taxation going forward.

7 So I don't think that the Court needs
8 to approach this issue by adopting some global
9 or universal definition of "income." The
10 Internal Revenue Code itself doesn't define
11 "income." Instead, it says that income is all
12 income from whatever sources realized and then
13 gives some illustrative examples.

14 I don't think my friends are offering
15 the Court a definition of "income" because they
16 say income is realized gains or maybe some
17 category of unrealized gains that you can say
18 are constructively realized. I don't think it's
19 necessary for the Court to actually try to
20 comprehensively define it here.

21 CHIEF JUSTICE ROBERTS: Thank you,
22 counsel. I understood your answer to Justice
23 Barrett to be the same as the answer that you
24 gave me with respect to a unrealized increase in
25 value from one time to another time in real

1 property, that you didn't have any authority to
2 support that.

3 GENERAL PRELOGAR: That's right. I'm
4 not pointing to a case from this Court that I
5 think would find that that's taxable. There's
6 also nothing from this Court, other than reading
7 Macomber for all it's worth, that I think would
8 necessarily rule that out.

9 CHIEF JUSTICE ROBERTS: And when you
10 just said that's the lesson of Macomber, you
11 mean that's the lesson of Macomber's demise?

12 GENERAL PRELOGAR: Yes, exactly, that,
13 ultimately, I think the Court recognized that
14 those statements which were rendered as an
15 abstract matter and opined on taxes that weren't
16 directly presented there had untenable
17 consequences and were also profoundly
18 ahistorical.

19 So I think there's a lot of wisdom in
20 following the approach the Court articulated in
21 Griffiths, where the Court said we don't rule on
22 the constitutionality of a tax until we find
23 that Congress has actually laid that tax. I
24 think the Court should take each tax as it comes
25 for purposes of resolving these questions.

1 CHIEF JUSTICE ROBERTS: Thank you.

2 Justice Thomas?

3 Justice Alito?

4 JUSTICE ALITO: General, I still want
5 to understand the limits of your argument. I am
6 quite concerned by the potential implications of
7 Petitioners' argument, and you stress that in
8 your brief. You say that if we rule in
9 Petitioners' favor, then large, important pieces
10 of the Tax Code will also logically fall. And I
11 think that's a fair argument. But I think it's
12 also a fair argument to do the same thing with
13 your position, and I want to understand the
14 limits of your position.

15 Now, coming in, I understood your
16 position to be that realization is not required
17 and that the Sixteenth Amendment -- realization
18 to the taxpayer is not required, and, therefore,
19 the Sixteenth Amendment allows the taxation of
20 income. And you seem to define "income" in your
21 brief as economic gain between two points in
22 time, and you say it is that -- those
23 well-established principles that distinguish
24 income taxes from property taxes.

25 So, if that is correct, then what

1 about the appreciation of holdings in securities
2 by millions and millions of Americans, holdings
3 in mutual funds over a period of time without
4 selling the -- the shares in those mutual funds?
5 Can those be taxed under the Sixteenth
6 Amendment?

7 GENERAL PRELOGAR: I think, if
8 Congress actually enacted a tax like that, and
9 it never has, that we would likely defend it as
10 an income tax. But you don't have to agree that
11 that tax would be valid in order to uphold the
12 MRT. So, if you think that --

13 JUSTICE ALITO: Well, I understand
14 that. And in order to rule for Petitioners, we
15 don't have to say anything about Subpart F or
16 S Corporations or partnerships or the accrual
17 method of taxation. But your answer is that
18 would probably -- you'll at least go that far --
19 that would probably be permissible under your
20 interpretation of the Sixteenth Amendment?

21 GENERAL PRELOGAR: I think it probably
22 would, but I think the Court could draw lines
23 based on history, and if there truly were a
24 widespread tax on all amount of appreciation for
25 every taxpayer, that wouldn't look like anything

1 Congress has done before. The Court has
2 sometimes used history like that to draw
3 principled lines.

4 Here, we have exactly the opposite
5 situation where Congress has enacted a tax that
6 looks exactly like any number of pass-through
7 taxes through history. So, here, I think
8 history functions as a rule of inclusion with
9 respect to the propriety of this tax.

10 JUSTICE ALITO: Now, as to the -- the
11 Chief Justice's question, how about the
12 appreciation in value of real property?

13 GENERAL PRELOGAR: I think it would be
14 subject to the same analysis that would fit
15 within a conception of income as economic gain
16 between two points in time. But Congress hasn't
17 traditionally taxed that, and so perhaps the
18 Court, if it were confronted with that
19 situation, would conclude that there is a
20 historical line or limiting principle here.

21 JUSTICE ALITO: So, unless history
22 rules that out, I'm not quite sure how
23 Congress's failure to enact a tax in the past
24 brings that outside the Sixteenth Amendment if
25 the tax would otherwise fall within the

1 Sixteenth Amendment, but you say that that
2 potentially is also taxable as income under your
3 theory?

4 GENERAL PRELOGAR: Yes. And I think
5 it's clearly taxable under the Constitution.
6 Again, this is not a question about Congress's
7 power. It's about the mode of taxation and
8 whether to apportion that tax or not.

9 JUSTICE ALITO: Now, if some sort of
10 constructive realization or some test for
11 attribution is required, what is your test? How
12 far may Congress go in attributing income to
13 someone who has not realized that income in the
14 standard understanding of that term?

15 GENERAL PRELOGAR: I would apply the
16 test the Court used in Burnet versus Wells,
17 which presents the most closely analogous
18 situation. A taxpayer argued that because he
19 had been the grantor of a trust, he couldn't be
20 held liable for the gains in the trust, it
21 couldn't properly be attributed to him because
22 he had no continuing control and wouldn't
23 personally enjoy those gains, which instead went
24 to the beneficiaries.

25 This Court rejected that claim, and

1 what it said is that Congress had not acted
2 arbitrarily. In making that attribution
3 decision, it looked at the taxpayer's
4 relationship to the underlying income and
5 concluded that there was good reason to tax the
6 grantor in that circumstance, including to avoid
7 shifting income to lower-income taxpayers.

8 But, if the Court were applying that
9 kind of attribution analysis here, I think the
10 MRT, like many pass-through taxes, is equally
11 constitutional. Here, the income has never been
12 taxed at the entity level, and there are real
13 complications with trying to tax foreign
14 corporations directly. So, in many respects,
15 these large U.S. shareholders who, by
16 definition, together collectively have a
17 majority stake in a closely held corporation are
18 in many senses the most suitable person or
19 entity to tax.

20 JUSTICE ALITO: Well, have we ever
21 said -- and maybe we should in this case say --
22 that the Sixteenth Amendment applies differently
23 to income or property that is obtained abroad
24 than it does to income or property possessed
25 within the United States?

1 GENERAL PRELOGAR: The Court hasn't
2 previously said that, but my friend himself
3 suggests that in thinking about these issues,
4 the Court should focus on the potential for tax
5 avoidance or tax abuse.

6 And I think that that concession just
7 underscores the point that when you are using a
8 foreign corporation, it provides a ready vehicle
9 to shelter funds offshore, keep them out of the
10 reach of U.S. taxing authorities, and, thus,
11 complicate efforts to access those funds even
12 when they have a really significant connection,
13 as they do here, because these companies are
14 majority owned by U.S. taxpayers.

15 And it's important to recognize too
16 that this case is not the paradigmatic case of
17 how the MRT applies. The overwhelming majority
18 of taxpayers subject to this are domestic
19 corporations, often parent companies of wholly
20 owned foreign subsidiaries who have arranged
21 their affairs to be able to keep this money
22 offshore, to a period of long tax deferral. But
23 I think that it would be anomalous to suggest
24 that the money is forever out of the reach of
25 U.S. taxing authority.

1 JUSTICE ALITO: Now the Petitioners
2 were in on the ground floor with this
3 corporation, but what if they had simply bought
4 into the company the day before the MRT made
5 taxes due? Wouldn't that look an awful lot like
6 a tax on capital rather than a tax on income in
7 any sense of the word?

8 GENERAL PRELOGAR: So I have three
9 reactions to that. I think that the underlying
10 nature of what's being taxed, which are the
11 realized earnings of the corporation, wouldn't
12 change. I do think that raises a harder
13 attribution question because that taxpayer would
14 have less of a direct relationship to the thing
15 that's being taxed, and so maybe someone in that
16 situation would have a better as-applied due
17 process claim. As you mentioned, the Moores
18 themselves aren't in that position.

19 The second thing I would say is that
20 if the Court is interested in exploring this
21 as-applied due process issue, it's important to
22 note that the MRT is not unique in this regard.
23 There are other taxes in other contexts where
24 the Court has recognized that someone can be
25 taxed on gain in property that happened before

1 the ownership stake was obtained. That was the
2 holding in Taft versus Bowers, where the Court
3 considered this issue with respect to the gift
4 tax. It's also how Subpart F itself can
5 operate. You can buy shares in the controlled
6 foreign corporation and be taxed under Subpart F
7 with respect to earnings that happened before
8 you bought your stake.

9 The third point I would make is that
10 as a factual matter, this situation is unlikely
11 to arise, and that's because Congress has
12 enacted other provisions of the code that
13 largely tie the gains to the person who owned
14 the shares at the relevant time. This is 26
15 U.S.C. Section 1248, and it taxes gains at the
16 time of sale. So, in your hypothetical, in --
17 in 2017, when the person is buying the -- the
18 share in the company, it taxes gains to the
19 seller as though they were paid out of the
20 retained corporate earnings.

21 And then there's a parallel provision
22 for the buyer under the MRT, 26 U.S.C.
23 965(d)(2)(B), that ensures that the buyer
24 doesn't have to include that in his income
25 through a cross-reference to Section 959.

1 JUSTICE ALITO: All right. One --

2 GENERAL PRELOGAR: So, in those ways,
3 I think that Congress was trying to attribute
4 the income to the person --

5 JUSTICE ALITO: Uh-huh. Okay.

6 GENERAL PRELOGAR: -- who owned the
7 shares at the relevant time.

8 JUSTICE ALITO: Thank you. One -- one
9 last subject. I'm sorry to go on so long on
10 this. Your brief makes an awful lot out of
11 Collector versus Hubbard, decided in 1871. To
12 what degree does your argument depend on that?

13 GENERAL PRELOGAR: Our argument
14 doesn't depend on Hubbard. You know,
15 ultimately, we think that what carries the day
16 here is the overwhelming history that
17 demonstrates that Congress has long taxed income
18 at the corporate level to shareholders.

19 Hubbard upheld that exercise of
20 authority, and so I think, if you're looking at
21 the text of the Sixteenth Amendment and what
22 those who drafted it would have in mind, they
23 would have been well aware of this pass-through
24 taxation and of the Hubbard precedent itself --

25 JUSTICE ALITO: Do you think that --

1 GENERAL PRELOGAR: -- but --

2 JUSTICE ALITO: -- do you think
3 that -- I'm sorry to interrupt. Do you think
4 that Hubbard decided that the tax that was at
5 issue in Hubbard satisfied Article I, Section 2,
6 and Article I, Section 9, which draws a
7 distinction between direct and indirect taxes?
8 Do you think that the Court decided that
9 question in Hubbard?

10 GENERAL PRELOGAR: So Hubbard's
11 discussion of this issue is brief. I don't
12 think that it parsed the constitutional text
13 that way, although it did say that this was
14 within Congress's power to enact. So I
15 understand that to be a constitutional holding,
16 but I acknowledge that it didn't get into the
17 specific provisions of the Constitution or their
18 interpretation.

19 JUSTICE ALITO: Do you think it was
20 overruled in Pollock?

21 GENERAL PRELOGAR: So I think that --
22 I don't think it would be right to say that
23 Pollock was the last word on it, of course,
24 because, even if it was overruled in Pollock,
25 the Sixteenth Amendment came along and it

1 self-reversed Pollock.

2 JUSTICE ALITO: Well, do you think
3 that the Pollock court understood itself to be
4 overruling Hubbard?

5 GENERAL PRELOGAR: I think it's
6 possible that, yes, the Pollock court understood
7 itself to be overruling Hubbard. It was
8 obviously adopting an understanding of what
9 constitutes a direct tax. That was a sharp
10 departure from what had come before.

11 I guess what I would say, Justice
12 Alito, is that it seems to me implausible that
13 the drafters of the Sixteenth Amendment, in
14 seeking to overturn Pollock and fully revive
15 Congress's pre-existing income tax authority,
16 would have meant to do so with respect to all
17 the ways Congress had exercised that authority
18 except for the type of pass-through tax that
19 Hubbard specifically approved.

20 JUSTICE ALITO: Well, I mean, if -- if
21 the Court in Hubbard thought that it was
22 overruling Pollock -- Hubbard -- I'm sorry, if
23 the Court in Pollock thought it was overruling
24 Hubbard, what do you make of the fact that it
25 doesn't even mention Hubbard, and, as far as I

1 can tell, Hubbard was never cited by the
2 attorneys in that case?

3 And, you know, I looked back at
4 Professor Fiss's volume in the Oliver Wendell
5 Holmes Devise of the Supreme Court on what he
6 has to say about Pollock, and he says, "Pollock
7 was a special ceremonial occasion for the Court.
8 The greatest lawyers of the day appeared for
9 both sides."

10 So the greatest lawyers for the day
11 didn't understand that there was Hubbard that
12 had supported -- you know, the -- the -- the --
13 the attorney arguing for the government just
14 didn't realize that they had Hubbard on the book
15 that supported their position?

16 GENERAL PRELOGAR: Well, maybe they --

17 JUSTICE ALITO: And the Court entirely
18 missed it?

19 GENERAL PRELOGAR: Maybe they missed
20 an opportunity to make a good argument in that
21 case. But I think, ultimately --

22 (Laughter.)

23 GENERAL PRELOGAR: -- the important
24 point is -- is that relying on Pollock and
25 trying to parse Pollock versus Hubbard ignores

1 the effect of the Sixteenth Amendment.

2 You know, this was -- this was an
3 amendment to the Constitution that was
4 specifically designed to restore a pre-existing
5 power, and the right way to look at how that --
6 what that power means is to look at how it had
7 actually been exercised before.

8 JUSTICE ALITO: All right. Thank you.

9 CHIEF JUSTICE ROBERTS: Justice
10 Sotomayor?

11 JUSTICE SOTOMAYOR: I don't fault the
12 parties for shooting for the stars and -- and --
13 but I guess the tenor of the questions is that
14 nobody's happy with anybody's definition of
15 anything, okay?

16 (Laughter.)

17 JUSTICE SOTOMAYOR: You started by
18 suggesting a narrow ruling. I think there are
19 two ways to narrowly rule. Tell me if one is
20 better than the other if at all, okay, but,
21 first, we can say there is a realization
22 requirement, and, here, it was realized because
23 the corporation realized it. You have to deal
24 with Justice Gorsuch's concern that you waived
25 that argument. I may disagree with him, but

1 that we can work out among ourselves.

2 But the bottom line, we could rule
3 that way, or we could do it the way Justice
4 Kavanaugh started his question, which is we
5 assume that there's a realization requirement
6 and -- and it was met here.

7 So which of the two ways should we do
8 it and -- and how not -- and why not?

9 GENERAL PRELOGAR: It would be
10 critically important for the Court to do it
11 through Justice Kavanaugh's approach. That is,
12 I don't think the Court needs to resolve
13 anything about whether the Sixteenth Amendment
14 requires realization. Here, we happen to have
15 it, and this kind of tax corresponds to
16 pass-through taxes we've had through history,
17 and that suffices to resolve this case. We have
18 serious concerns with the Court --

19 JUSTICE SOTOMAYOR: Does that -- the
20 history is that Congress can attribute that
21 realization?

22 GENERAL PRELOGAR: Correct, that
23 Congress can attribute that realization by the
24 corporation to the shareholders and there are
25 taxes that look like that at virtually all

1 points in our nation's history.

2 The reason why I would strongly
3 caution the Court away from adopting a
4 realization requirement is not only that we
5 think that it is inaccurate, profoundly
6 ahistorical, inconsistent with the text of the
7 Sixteenth Amendment, but it would also wreak
8 havoc on the proper operation of the Tax Code.

9 I think that there are pass-through
10 taxes that would withstand scrutiny if the Court
11 affirms the attribution holding, but, as I had
12 mentioned to Justice Barrett, there are a number
13 of critically important provisions of the code
14 that don't actually have that kind of
15 pass-through mechanism and don't turn on
16 realization at all.

17 That includes the mark-to-market
18 taxes, original issued discount on bonds that
19 drives prices in bond markets and avoids what
20 could otherwise be sheltering of income that
21 should be taxable. It includes the expatriation
22 tax when people renounce their United States
23 citizenship.

24 So I think that there are various ways
25 in which adopting any form of a realization

1 requirement would have profound practical
2 consequences, and it's unnecessary for the Court
3 to go down that road in light of the serious
4 legal arguments against that reading.

5 JUSTICE SOTOMAYOR: Thank you.

6 CHIEF JUSTICE ROBERTS: Justice Kagan?

7 JUSTICE KAGAN: And, General Prelogar,
8 just to take you back to the implications of
9 Mr. Grossman's argument, you know, he's made a
10 number of statements in his brief and today as
11 well about how he would distinguish this tax
12 from many others, from Subpart F, from
13 S Corporations, from partnerships, from accrual,
14 from you name it. There -- there might be more.

15 What do you worry about and why?

16 GENERAL PRELOGAR: I worry that none
17 of those proposals actually hold up and provide
18 a basis to distinguish the MRT. So, at first,
19 he suggests it has to do with control. But, as
20 I had explained to Justice Barrett before, the
21 level of control here is exactly the same as
22 under Subpart F.

23 These are 10 percent shareholders,
24 U.S. shareholders of closely held foreign
25 corporations, and so control cannot be the

1 relevant difference. It's also not the
2 difference with respect to partnerships and
3 S Corporation shareholders who might have even a
4 lower than 10 percent stake and nevertheless can
5 have income attributed to them.

6 Then he says maybe the answer is
7 consent, and he points to S Corporations and
8 says that turns on a theory of consent. But I
9 don't think that that works either because, to
10 the extent that there's any kind of realization
11 requirement out there in the Sixteenth
12 Amendment, consent couldn't cure that difficulty
13 or give taxpayers a basis to allow Congress to
14 tax things that are outside its authority, and
15 it doesn't even work as a descriptive matter
16 because the S Corporation shareholders might buy
17 their interest in the company and never
18 personally consent to pass-through taxation, or
19 they might change their minds and remove their
20 consent and say I don't want to be taxed on it
21 anymore, but if they have a minority stake in
22 the company, they're stuck with it and continue
23 to have pass-through taxation. So I don't think
24 consent works.

25 Then he says maybe it has something to

1 do with the type of income under Subpart F.
2 But, as I've explained before, we don't think
3 that the type of income matters under the
4 Sixteenth Amendment. And, here, this is
5 paradigmatic income. This is ordinary business
6 income, substantial earnings realized by the
7 company. And I think it would be a really
8 anomalous result to say this type of income
9 uniquely is exempt from pass-through taxation.

10 He also suggests that maybe it turns
11 on the potential for abuse and maybe that
12 explains some of these other taxes. But there
13 again, I think that the -- the MRT itself
14 responds to the concern that these domestic
15 corporations in the main, also some individual
16 shareholders, have been able to keep the money
17 offshore in the closely held foreign
18 corporations and thereby defer taxation on them.

19 So, with respect to every possible
20 point of difference, we just don't think it
21 holds up as a descriptive matter, and so there's
22 a real concern we have that if the Court goes
23 down one of these roads and nevertheless
24 invalidates the MRT, it's not a principled
25 distinction.

1 JUSTICE KAGAN: And then, with respect
2 to the furthest -- the implications of the
3 furthest reaches of your argument that Justice
4 Alito was asking about, and you said with
5 respect to a number of taxes, which we'll
6 probably never see in our lifetimes, but you
7 said, if we did see them, you would probably
8 defend them.

9 I mean, when you say that, that's your
10 job, right?

11 (Laughter.)

12 GENERAL PRELOGAR: Yes, we generally
13 defend the constitutionality of statutes.

14 JUSTICE KAGAN: Yeah. So -- so how
15 should we think about that set of possibilities?

16 GENERAL PRELOGAR: So I think the
17 important starting point is to recognize that
18 those are hypotheticals, as you mentioned, that
19 are unlikely to ever come to pass.

20 There's a really good reason that
21 Congress frequently chooses to tax based on
22 realization, and it's the administrative
23 practicalities of the situation. Otherwise,
24 it's complicated to track fluctuations in value
25 over time or to engage in a valuation analysis

1 for assets that might be hard to value.

2 So, in the main, Congress frequently
3 does choose to rely on realization, and I think
4 some of the hypotheticals about taxing all
5 people who have shares or taxing all home
6 appreciation are unlikely ever to come to pass.

7 But I also think that it's important
8 for the Court to not rely on concerns about
9 those types of far-fetched hypotheticals to
10 announce bright-line rules about what the
11 Sixteenth Amendment requires that could actually
12 take down critically important provisions of the
13 Tax Code and that respond to real-life concerns
14 and very legitimate exercises of the taxing
15 power.

16 In particular, many of the times when
17 Congress has chosen to tax in the absence of
18 realization, it's because taxpayers can abuse
19 the rules. They can manipulate realization
20 events, or they can make use of certain
21 structures or financial instruments to shield
22 assets from taxation. And any coherent or
23 proper administration of the Tax Code has to be
24 able to respond to that kind of taxpayer abuse.

25 JUSTICE KAGAN: Thank you.

1 CHIEF JUSTICE ROBERTS: Justice
2 Gorsuch?

3 JUSTICE GORSUCH: Would you agree,
4 General, that when the Court opens a door,
5 Congress tends to walk through it?

6 (Laughter.)

7 GENERAL PRELOGAR: I don't want to
8 overgeneralize on the back-and-forth between the
9 Court and Congress, but -- but, Justice Gorsuch,
10 if I am anticipating correctly where you're
11 going --

12 JUSTICE GORSUCH: I'm just -- maybe
13 you are, maybe you aren't. Probably are. You
14 usually are.

15 (Laughter.)

16 JUSTICE GORSUCH: But, if -- if the
17 only bar to Congress from enacting a tax on
18 millions of Americans' retirement accounts and
19 mutual funds is administratability, they're
20 pretty clever over there, aren't they?

21 GENERAL PRELOGAR: Well, Justice
22 Gorsuch, I think that this goes to the point --

23 JUSTICE GORSUCH: They know how to get
24 around administration concerns pretty well,
25 don't they?

1 GENERAL PRELOGAR: I think that there
2 would be good reasons for them to avoid the
3 administrative complexities that would open up
4 --

5 JUSTICE GORSUCH: Oh, sure, as a
6 policy matter, but -- but, you know, isn't it --
7 isn't it the case that that would open a big
8 door?

9 GENERAL PRELOGAR: They -- that door
10 is already open. Congress can enact that tax.
11 They just --

12 JUSTICE GORSUCH: Right. No, I
13 understand your position.

14 GENERAL PRELOGAR: -- might have to
15 apportion it.

16 JUSTICE GORSUCH: It's been open
17 forever in your view.

18 GENERAL PRELOGAR: Yes.

19 JUSTICE GORSUCH: Yeah. Right.

20 GENERAL PRELOGAR: That the
21 Constitution gives Congress the power --

22 JUSTICE GORSUCH: Okay.

23 GENERAL PRELOGAR: -- to tax that.

24 JUSTICE GORSUCH: And then, in terms
25 of your argument here as well about there's no

1 difference between income and that -- and that
2 kind of -- that unrealized capital gain, you're
3 familiar with, you know, the 1918 tax cases
4 obviously. The government's brief in that case,
5 one of my industrious law clerks pulled it, and
6 there, the government does draw that distinction
7 and says that that kind of capital gain is not
8 income because the individual received, the
9 taxpayer received, nothing, and that's not
10 income. It's a mere gain of or loss of capital
11 value. Are you familiar with that?

12 GENERAL PRELOGAR: I'm not sure
13 exactly which brief you're talking about. Do
14 you happen to know the date?

15 JUSTICE GORSUCH: Yeah. It's the 19
16 -- the Solicitor General's brief in the 1918
17 income tax cases, and it's pages 32 and 53.

18 GENERAL PRELOGAR: So I would have to
19 look at the particular issue that was being
20 considered there. There are a number of
21 statutory realization requirements that could
22 explain those statements. There have also been
23 a lot of evolution in the -- the thinking about
24 these issues following Macomber.

25 I recognize that the -- the government

1 has sometimes taken a broader view of Macomber
2 itself, for example, but that was in an era when
3 the Court itself had been unclear about the
4 reach of Macomber before the Court has sharply
5 limited it.

6 JUSTICE GORSUCH: Okay. And then I do
7 think there is room for some narrow ground, as
8 -- as Justice Sotomayor suggested. You -- if
9 one thinks that the question is attribution you
10 call it -- I think your friend on the other side
11 would call it is it realized by the taxpayer.
12 You say is it fairly attributed to the taxpayer.
13 Potato/potato, I -- I sometimes wonder.

14 GENERAL PRELOGAR: I'm from Idaho, so
15 I -- I love that.

16 JUSTICE GORSUCH: You totally get
17 that.

18 (Laughter.)

19 JUSTICE GORSUCH: You totally get what
20 I'm saying. If we're talking about the same
21 thing, you make a pretty persuasive argument
22 that under the MRT, the Moores do have
23 constructive control, that it is fairly
24 attributable to them because they're a 10
25 percent stakeholder and some other facts.

1 Again, I may be missing it. I don't
2 see that argument in the brief. Assume --
3 assume that argument hasn't yet been made, okay?
4 What do I do?

5 GENERAL PRELOGAR: I agree, Justice
6 Gorsuch, that we haven't made the argument
7 expressly in terms of control because we don't
8 think that's the right standard. But we very
9 clearly did make the argument that the MRT is
10 constitutional for the very same reasons --

11 JUSTICE GORSUCH: Sure.

12 GENERAL PRELOGAR: -- Petitioners say
13 that the Subpart F regime is constitutional.

14 JUSTICE GORSUCH: I -- I -- I
15 understand that, but -- but --

16 GENERAL PRELOGAR: Yeah.

17 JUSTICE GORSUCH: -- but just answer
18 my question. You know, if we -- if we think
19 that there's some constructive realization or
20 attribution requirement required, but that
21 hasn't been adjudicated yet, it hasn't been
22 argued yet, what should I do?

23 GENERAL PRELOGAR: If you think it
24 hasn't been argued yet, I, of course, disagree
25 on the facts --

1 JUSTICE GORSUCH: No, I -- I
2 understand.

3 GENERAL PRELOGAR: -- but the Court
4 can affirm on an alternative ground, even one
5 that the party didn't raise. The Court said
6 that in Dahda versus United States, for example.
7 So I think it would be open for the Court to
8 affirm on that ground because we do think it's a
9 very strong argument, and I would encourage the
10 Court to do so.

11 JUSTICE GORSUCH: Okay. And then you
12 -- you've argued that attribution is a feature
13 of due process rather than income under the
14 Sixteenth Amendment. But all of our cases,
15 whether we're talking about partnerships or you
16 want to talk about S corps or -- or Schedule F,
17 have treated it as whether it's a form of income
18 to the taxpayer under the Sixteenth Amendment.
19 That's how we've grounded our analysis so far.
20 It would seem quite a change to move it over to
21 due process. Can you -- can you react to that?

22 GENERAL PRELOGAR: Sure. So I think,
23 actually, the Court's central case on
24 attribution was a due process case. This is
25 Burnet versus Wells. It involved the grantor of

1 a trust. And the Court there put it explicitly
2 in due process terms.

3 JUSTICE GORSUCH: Well, you mentioned
4 partnership earlier, and -- and I went back and
5 looked at that, and due process, those words
6 don't -- you said that's --

7 GENERAL PRELOGAR: Yes.

8 JUSTICE GORSUCH: -- the best case for
9 you. Those words just don't appear anywhere
10 in -- in Justice Brandeis's opinion. It's all
11 about whether it's -- you can call it fairly
12 attributable or realized by the partner.

13 GENERAL PRELOGAR: And I think that
14 it's perfectly fine for the Court to look at
15 this through the lens of the Sixteenth Amendment
16 because you get to the same ultimate result,
17 which is that, ultimately, the question then
18 would be can Congress fairly attribute this
19 income to you, the taxpayer. And, here, we have
20 overwhelming history and tradition going all the
21 way back to the 1860s and 1870s demonstrating
22 that, yes, Congress can.

23 JUSTICE GORSUCH: And are some of
24 those factors that you look at whether they
25 control the -- the entity, whether there's some

1 evidence of fraud in its use of the entity?

2 What else would you add to that list?

3 GENERAL PRELOGAR: I would look at the
4 taxpayer's overall relationship to the income
5 and the -- and the entity. You know, I -- I
6 hesitate to try to put the gloss of control on
7 it for a couple of different reasons. One is
8 that I think that would incentivize taxpayers to
9 try --

10 JUSTICE GORSUCH: Sure.

11 GENERAL PRELOGAR: -- to argue in an
12 individual case they don't have control.

13 JUSTICE GORSUCH: I'm not suggesting
14 that's necessary.

15 GENERAL PRELOGAR: Right. That could
16 be --

17 JUSTICE GORSUCH: I'm suggesting it
18 might be sufficient.

19 GENERAL PRELOGAR: Yes. I would
20 absolutely agree that might be the sufficient --
21 that might be sufficient to establish that
22 Congress made a fair attribution decision in
23 that case. I would just caution the Court away
24 from constitutionalizing that or saying it's
25 necessary in every case.

1 JUSTICE GORSUCH: Roger that. What --
2 what other factors would you have us look at?

3 GENERAL PRELOGAR: The other kinds of
4 factors the Court has looked at or the statement
5 it made in Burnet versus Wells was whether
6 Congress has made an attribution decision that's
7 unrelated to any privilege or benefit. I think
8 using that standard, it works for us here as
9 well because there are obvious benefits
10 associated with doing business through a
11 controlled foreign corporation which is closely
12 held and could keep the money offshore for all
13 of those years subject to tax deferral.

14 So I think the --

15 JUSTICE GORSUCH: Let me pause you
16 there.

17 GENERAL PRELOGAR: Yes.

18 JUSTICE GORSUCH: So the -- the
19 foreign aspect of it and -- and the difficulty
20 of otherwise obtaining some kind of tax on it
21 should factor in our analysis you think?

22 GENERAL PRELOGAR: Again, I think
23 those are --

24 JUSTICE GORSUCH: Could.

25 GENERAL PRELOGAR: -- conditions that

1 could be sufficient. I wouldn't want the Court
2 to say they are absolutely --

3 JUSTICE GORSUCH: Necessary.

4 GENERAL PRELOGAR: -- necessary in
5 every case.

6 JUSTICE GORSUCH: I got it.

7 GENERAL PRELOGAR: And, of course, we
8 have things like partnerships where there's not
9 necessarily --

10 JUSTICE GORSUCH: Sure.

11 GENERAL PRELOGAR: -- any abuse. It's
12 a convenient way to structure taxation with
13 respect to certain types of entities.

14 JUSTICE GORSUCH: It was very helpful
15 to me. Any other factors you'd have me
16 consider?

17 GENERAL PRELOGAR: I think you have
18 covered the waterfront of the things that have
19 already emerged in the case law. I guess, if I
20 step back to a 30,000-foot level, the one thing
21 I would say is that I would urge the Court not
22 to try to set down an explicit set of principles
23 to govern all cases for the very reasons I was
24 describing earlier, that we have seen taxpayers
25 latch onto that --

1 JUSTICE GORSUCH: Roger --

2 GENERAL PRELOGAR: -- and then seek to
3 avoid taxation.

4 JUSTICE GORSUCH: -- Roger that too,
5 okay?

6 (Laughter.)

7 JUSTICE GORSUCH: And that would take
8 care, though -- if -- if we wrote that that way,
9 it would take care of all of your concerns about
10 S corporation -- Schedule F or, you know, the --
11 the mark-to-market, and -- and potentially the
12 MRT?

13 GENERAL PRELOGAR: Yes. I --
14 certainly, I think the MRT, in addition to all
15 of those other taxes, satisfy the -- the types
16 of criteria that the Court has looked at that
17 are relevant to this attribution question.

18 JUSTICE GORSUCH: Whether we call it
19 attribution or constructive realization?

20 GENERAL PRELOGAR: Yes.

21 JUSTICE GORSUCH: Potato/potato.

22 GENERAL PRELOGAR: Well, on that one,
23 I would -- I would shy away from constructive
24 realization just because I think it introduces
25 an additional layer of ambiguity in the code. I

1 mean, by definition, it means not actual
2 realization, and so I think that --

3 JUSTICE GORSUCH: Well, no, I --

4 GENERAL PRELOGAR: -- it's a term that
5 doesn't appear in the code itself that
6 Petitioners --

7 JUSTICE GORSUCH: -- the way -- the
8 way I read our precedent maybe -- and I'll just
9 -- I'll stop, but the way I read our precedent
10 at least is it's -- it's fairly saying that this
11 individual realized, gained control of, or could
12 be reasonably adjudged to have done that by
13 Congress, this person has control over these
14 assets.

15 And you've given me a very helpful
16 list of factors from this Court's history and --
17 and practice, consistent with our precedent,
18 rather than calling it all misguided, that might
19 work. Fair enough?

20 GENERAL PRELOGAR: I don't think that
21 it's right to say that this list of factors
22 gives the taxpayer sufficient control over the
23 assets just, again, because the concept of
24 control can be inherently confusing here if it
25 suggests a majority stake. You know, the

1 S corporation shareholders --

2 JUSTICE GORSUCH: Right.

3 GENERAL PRELOGAR: -- they might have
4 a 1 percent stake in the company --

5 JUSTICE GORSUCH: I -- I -- I --

6 GENERAL PRELOGAR: -- and not have any
7 control.

8 JUSTICE GORSUCH: Okay.

9 GENERAL PRELOGAR: So I think that's
10 -- that's where I have a little bit of
11 disagreement on how to describe what we're
12 discussing.

13 JUSTICE GORSUCH: Okay. That's very
14 helpful to me. Thank you, General.

15 CHIEF JUSTICE ROBERTS: Justice
16 Kavanaugh?

17 JUSTICE KAVANAUGH: You don't want us
18 to use the phrase "constructive realization"?

19 GENERAL PRELOGAR: Yes. I think that
20 that phrase is inherently amorphous. It doesn't
21 appear in the code.

22 JUSTICE KAVANAUGH: Right.

23 GENERAL PRELOGAR: It appears to be a
24 phrase that Petitioners have --

25 JUSTICE KAVANAUGH: Right.

1 GENERAL PRELOGAR: -- invented for
2 purposes of trying to save these other taxes.

3 JUSTICE KAVANAUGH: On the --

4 GENERAL PRELOGAR: And I think it
5 would open up immediate disputes about what
6 exactly it encompasses.

7 JUSTICE KAVANAUGH: Right. And on the
8 proverbial open door for Congress, members of
9 Congress want to get reelected.

10 (Laughter.)

11 JUSTICE KAVANAUGH: So some of the
12 hypos are -- are --

13 GENERAL PRELOGAR: Yes, I think that
14 there are huge --

15 JUSTICE KAVANAUGH: -- that's why
16 they're farfetched, although who knows how
17 things would change.

18 On some of Justice Alito's
19 hypotheticals, though, if -- if things came to
20 pass, I think you acknowledged, I just want to
21 confirm, that unlike this case, where you say
22 that historical practice supports this,
23 Congress's historical practice, the Court's
24 cases, if there were something novel, that lack
25 of historical support would at least be a strike

1 against it, not dispositive necessarily.

2 Is that an accurate summary of what
3 you said about that?

4 GENERAL PRELOGAR: Yes. I think that
5 the -- the point I was trying to make is that,
6 first, yes, there are huge practical and policy
7 reasons why these taxes wouldn't be enacted,
8 and, second, if it came to pass, then the Court
9 could assess that tax on its own terms and it
10 might look to history and think, huh, this is
11 something new.

12 I do want to be clear that we don't
13 think that the novelty alone would be
14 dispositive, as you mentioned. Certainly,
15 Congress has some power to enact taxes that it
16 hasn't enacted before, but it would certainly
17 provide a reason to scrutinize that tax a little
18 more carefully.

19 Here, the Court doesn't have to go
20 down that road because the history is all on our
21 side.

22 JUSTICE KAVANAUGH: One hypo of my own
23 just to make sure it's covered. I think it's an
24 easy one, but I want to make sure. If there
25 were a federal tax on the value of someone's

1 property, you agree that's a direct tax -- or --
2 or on the value of someone's holdings, you agree
3 that's a direct tax that would have to be
4 apportioned, correct or not?

5 GENERAL PRELOGAR: Exactly. That's a
6 quintessential tax on property because it's
7 looking at the total value of the asset and it's
8 doing it at a particular point of time. And
9 maybe you could even levy it again and again on
10 the same value, like any homeowner experiences
11 with a property tax bill for the home. That's
12 totally different from an income tax, where
13 you're taxing the increment of gain over time
14 and generally only doing it one time with any
15 future tax looking to a new increment of gain
16 over a new period of time.

17 JUSTICE KAVANAUGH: Okay. Last
18 question. Your position on the MRT, and you
19 cite Heiner and Subpart F and -- and S Corps and
20 say this is all similar in kind.

21 The one wrinkle -- and I just want to
22 make sure we're on the same page -- is that this
23 goes back a lot of years and rolls in income
24 from many past years.

25 What should we say about that?

1 GENERAL PRELOGAR: So I have --

2 JUSTICE KAVANAUGH: And let me just
3 add, and he says, ultimately, if you can just
4 roll in, I think, income at any point in time,
5 then that really becomes not much of a limit at
6 all.

7 GENERAL PRELOGAR: So let me react to
8 that in a couple of different ways. I think
9 that the length of the lookback period here
10 can't change the underlying character or
11 classification of what's being taxed as income.
12 This was actual earnings brought in by the
13 company, kept in their coffers.

14 If it was income in year one, then I
15 don't think there's any expiration date on
16 classifying it as income in a future year, and I
17 think it would be anomalous for Congress to lose
18 its ability to tax that as income just because
19 it's granted a period of tax deferral.

20 So, instead, I think that the lookback
21 period, instead of relating to the Sixteenth
22 Amendment or any fundamental questions about
23 what income constitutes, is instead a
24 retroactivity concern. It, I think, arises
25 under the Due Process Clause and would turn on

1 whether Congress had a legitimate purpose for
2 having this kind of lookback period and used
3 rational means.

4 Here, we think that that is clearly
5 satisfied. Petitioners raised a retroactivity
6 due process argument below. The court rejected
7 it in the Ninth Circuit. They haven't renewed
8 it here. And I think it's because it clearly
9 fails under precedent, like United States versus
10 Carlton, but, ultimately, I would urge the Court
11 to -- to recognize that that is not about the
12 proper characterization of the underlying tax
13 base.

14 JUSTICE KAVANAUGH: Thank you.

15 CHIEF JUSTICE ROBERTS: Justice
16 Barrett?

17 JUSTICE BARRETT: I want to follow up
18 on some of -- on your factors to Justice
19 Gorsuch.

20 So you talked about how it could be
21 fair, you know, Justice Kavanaugh just said
22 S Corps, partnerships, you know, an MRT, to --
23 and the MRT tax, to say that this is
24 attributable to the shareholders or to the
25 partners or, you know, to the seller of the

1 trust.

2 How do we know that? Is it because
3 this is closely held? Because I assume what
4 your friend on the other side is going to say
5 is, well, they -- they had 10 percent, you know,
6 they -- they -- they weren't majority holders,
7 and so they couldn't force a distribution. So
8 how -- how would you articulate that when it can
9 fairly be attributed if we're not talking due
10 process, if we're talking about it from a
11 Sixteenth Amendment point?

12 GENERAL PRELOGAR: Yes. So I think,
13 at the outset, the Court could rely on the
14 lessons to be drawn from history and tradition
15 here. This functions like the early income
16 taxes that I pointed to from the 1860s and 1870
17 that taxed shareholders on corporate income.

18 At that point in our nation's history,
19 corporations were generally closely held. There
20 were fewer Americans who owned stock, and so I
21 think that they -- they functioned quite
22 analogously to the MRT insofar as they reached a
23 distinctive category of shareholders generally
24 in those closely held corporations.

25 You know, at the end of the day, I

1 guess what I would say is that certainly, we
2 think it's a factor in our favor that this
3 reaches relatively large U.S. shareholders.
4 It's true it's 10 percent, so they don't have to
5 have a majority stake, but the premise of
6 Congress is that these kinds of large
7 shareholders can usually work together with
8 other shareholders in this closely held
9 corporation. There aren't going to be that many
10 of them to direct the company's policy or to
11 force a distribution as the case may be. And
12 that kind of threshold, 10 percent, appears
13 throughout the law, not just in the Tax Code,
14 but in the securities context, for example,
15 there are additional obligations imposed on 10
16 percent shareholders of companies.

17 So wherever the line might be drawn in
18 thinking about it from this relationship to the
19 funds and level of influence of the
20 corporation's policy, I think 10 percent falls
21 well within the line of what should be
22 recognized as permissible.

23 JUSTICE BARRETT: Okay. Thanks.

24 CHIEF JUSTICE ROBERTS: Justice
25 Jackson?

1 JUSTICE JACKSON: So are there
2 drawbacks to setting this up in the way that
3 Justice Gorsuch has articulated? I mean, I
4 guess I'm a little concerned because I heard you
5 respond to Justice Sotomayor by saying that one
6 of your primary concerns is that we not suggest
7 that realization is required.

8 And would -- would -- would taking the
9 approach that Justice Gorsuch has articulated
10 require us to do that, or could we assume -- or
11 how -- how do we get around the other caution
12 that you put forward?

13 GENERAL PRELOGAR: So, if I understood
14 Justice Gorsuch's approach -- and I hope I'm not
15 getting it wrong -- the idea behind this
16 approach would be to recognize that here we
17 actually have realized income, so the Court
18 doesn't need to resolve the status of that under
19 the Sixteenth Amendment and, instead, the
20 pressure point is whether Congress could enact a
21 pass-through tax on the 10 percent U.S.
22 shareholders --

23 JUSTICE JACKSON: But is that fairly
24 --

25 GENERAL PRELOGAR: -- that are subject

1 to this income.

2 JUSTICE JACKSON: -- is that fairly
3 encompassed by this question presented? I mean,
4 this sort of goes to your discussions with
5 Justice Alito, I think. I -- I thought the
6 question presented was about the extent to which
7 the Sixteenth Amendment requires realization.

8 So, if we're going now beyond that,
9 are we out of -- out of the territory that is
10 fairly encompassed here?

11 GENERAL PRELOGAR: I don't think so
12 because I think the answer to the question
13 presented would be we don't have to decide in
14 all contexts here there was a realization. And
15 so, as we said in our brief in opposition to
16 this case, we don't actually think that the case
17 presents the question presented because here
18 there was actual realization by the corporation.
19 And the real dispute between the parties is
20 whether Congress made a fair attribution
21 decision.

22 JUSTICE JACKSON: Let me ask you just
23 another question about the government's brief.
24 Why did the government make an argument about
25 excise taxes at the end?

1 GENERAL PRELOGAR: So we think that
2 the MRT is clearly constitutional on an excise
3 tax theory as well. There's been some -- some
4 suggestion at argument this morning that maybe
5 we didn't present that argument below, and that
6 is incorrect.

7 In the Ninth Circuit, we said that
8 even if the MRT isn't properly characterized as
9 an income tax, it's not a direct tax. And we
10 said that therefore, Congress had Article I
11 authority to enact it and pointed to the
12 Spreckels Sugar case, which is an excise tax
13 case.

14 So I think we did preserve the
15 argument. The Ninth Circuit didn't have
16 occasion to reach it because it ruled in our
17 favor on the primary income tax argument. But,
18 if this Court had any doubt about whether this
19 is a proper income tax, we think the Court could
20 affirm on the excise tax argument in particular.

21 And as I had mentioned in an earlier
22 response, one of the important things for the
23 Court to keep in mind is that 99 percent of the
24 tax owed under the MRT is owed by domestic
25 corporation shareholders, large U.S. companies,

1 for example, that have these foreign
2 subsidiaries where they've been holding money
3 overseas for a number of years. And this would
4 be a tax on the privilege of doing business with
5 those corporate relationships and in that
6 corporate form. So, at the very least, we'd
7 urge the Court not to invalidate the MRT and all
8 of its circumstances without proper
9 consideration of that argument.

10 JUSTICE JACKSON: And that's because
11 the constitutional question is whether or not it
12 is a direct tax, because that would be the
13 circumstance under which apportionment is
14 required?

15 GENERAL PRELOGAR: Yes, exactly. And
16 I think this relates to your earlier questions,
17 Justice Jackson, about the meaning of Hylton and
18 about whether this can in any sense properly be
19 considered a direct tax.

20 You know, ultimately, I think one of
21 the ways to understand the categories in the
22 Constitution is in relation to one another. And
23 at the very least, this is not a tax on land.
24 This is not a tax on personal property. It's
25 not a head tax. Therefore, it's not a direct

1 tax. And we think it's either an excise or an
2 income tax.

3 JUSTICE JACKSON: One final question
4 about Macomber. Why -- why shouldn't we take
5 this opportunity to just put an end to it? I
6 mean, if we were to apply the stare decisis
7 factors that the Court goes through when it
8 decides whether or not to formally overrule a
9 precedent, doesn't Macomber fail anyway?

10 GENERAL PRELOGAR: I agree that
11 Macomber would fail those factors in an
12 appropriate case. The reason we haven't asked
13 the Court to overrule Macomber here is because
14 we just think it's inapplicable by the terms of
15 subsequent precedent that have already said
16 Macomber only has controlling weight with
17 respect to that very specific type of stock
18 dividend.

19 And so I think the Court has already
20 done the work here of effectively leaving
21 Macomber limited --

22 JUSTICE JACKSON: But, if we disagree
23 with you and we applied the stare decisis
24 factors, you would say the government would
25 still win on its view that Macomber is not good

1 law or controlling in this case?

2 GENERAL PRELOGAR: If -- if this Court
3 thought it were necessary to walk through the
4 stare decisis factors, then, yes, I think that
5 in each instance, Macomber was egregiously
6 wrong. It didn't grapple with the text of the
7 Sixteenth Amendment in a legitimate way or look
8 at all of the history that I think is relevant
9 to that question. It has been subsequently
10 eroded by any number of additional precedents.

11 And in the end, with reliance
12 interests, here, Congress has relied on those
13 subsequent precedents by enacting any number of
14 taxes that wouldn't satisfy Macomber's
15 realization framework. And Petitioners
16 themselves acknowledge that Macomber's
17 realization framework couldn't actually carry
18 the day because the taxes that they have said
19 are constitutional wouldn't survive under
20 Macomber.

21 JUSTICE JACKSON: Thank you.

22 CHIEF JUSTICE ROBERTS: Thank you,
23 counsel.

24 Rebuttal, Mr. Grossman?

25

1 REBUTTAL ARGUMENT OF ANDREW M. GROSSMAN

2 ON BEHALF OF THE PETITIONERS

3 MR. GROSSMAN: Thank you.

4 The government's recalibrated
5 position, as explained by my friend, is not
6 narrow and the Court should not mistake it as
7 such. The government's view that a
8 corporation's earnings can simply be attributed
9 to a -- to any corporate shareholder is
10 staggeringly broad.

11 Corporations like Microsoft and Exxon
12 Mobil have hundreds of billions of dollars of
13 retained earnings on their books that they've
14 invested in corporate assets, research and
15 development, and -- and other -- and other
16 activities. And in some cases, those retained
17 earnings exceed the current value of shares.

18 Under the government's view and I
19 think as demonstrated by the MRT, apparently,
20 Congress could simply tax backwards, reaching
21 back as far as -- as -- as it would care to do
22 so, to attribute those retained earnings going
23 back many years to current shareholders, again,
24 in some instances in excess of the value of the
25 -- of their current holdings.

1 But I think the Court should also keep
2 in mind that there is an impact to that
3 position, that purportedly narrower position,
4 under the existing code, which is that there is
5 no carveout for -- against taxing shareholders
6 in the current code on corporate earnings.

7 If those are Sixteenth Amendment
8 earnings, then -- I'm sorry, Sixteenth Amendment
9 income to shareholders, then they are already
10 subject to the income tax through the gateway
11 definition of gross in -- income that reaches
12 everything that is income under the Sixteenth
13 Amendment. So there's no carveout. Those would
14 already be subject to it.

15 I think this just demonstrates the way
16 that the government's position would make a hash
17 of existing law and cause enormous confusion
18 with respect to how our tax system functions.

19 By consequence -- by -- by contrast, I
20 -- I don't think that there are any serious
21 consequences of the realization principle that
22 we've put forward in this case because it is the
23 thread that runs through the Court's
24 jurisprudence going back over a century and is
25 the glue that holds together the Tax Code as it

1 exists today.

2 Every tax that my friend has mentioned
3 falls into one of two categories. Some of
4 those, particularly regarding the -- the abuse
5 of the corporate firm -- form, turn on theories
6 of constructive realization or you might say
7 assignment of income. I don't think there's
8 much of a distinction.

9 The remainder of them are
10 straightforward excise taxes that are supported
11 by the history -- the long history -- long --
12 long history of congressional practice. These
13 include, for example, the original issue
14 discount. It's simply an excise tax on the
15 transaction regarding the transfer of a bond.
16 Congress has been levying taxes like that for
17 over 130 years at this point.

18 Others, like the mark-to-market taxes,
19 are excise taxes, like in -- like in Spreckels,
20 on conducting business in a specified fashion.
21 Again, those sorts of taxes predate the
22 Sixteenth Amendment, and nobody has ever called
23 into question their constitutionality as such.

24 There's also case law. If it was
25 simply enough for the -- for the -- if it was

1 simply enough to attribute income to anybody
2 with a close relationship to it, all of the
3 Court's corporate reorganization cases and cases
4 involving shareholder rights and really pretty
5 much all the Sixteenth Amendment cases involving
6 trusts and everything else would have been about
7 a sentence long because it wouldn't really take
8 much more than that for the Court simply to say,
9 well, there's a close enough relationship and so
10 who cares whether or not the person realized
11 income or not. Of course, that's not the
12 inquiry the Court has undertaken.

13 And so far as Macomber's rule is
14 concerned -- and the Court has applied the
15 dividing line recognized by Macomber as recently
16 as 1975 in Ivan Allen and it's carried forward
17 the same principle in cases like Indianapolis
18 Power & Light in 1990, as well as restating it
19 in Cottage Savings in 1991.

20 I don't think real -- real -- this
21 concept of realization is anything unfamiliar to
22 our law, and, indeed, it's the only way to
23 understand the current Tax Code.

24 Every -- Congress has -- the -- the --
25 the anti-income, income avoidance provisions of

1 the Tax Code are long, lengthy, reticulated. I
2 don't envy anybody who's had to spend their time
3 reading Subpart F and practices in that field.
4 But the reason those are so complicated and
5 reticulated is because Congress has tried to
6 stay within the realization line.

7 It's done everything it can to fit
8 that framework, where it would have been the
9 easiest thing in the world, if -- if Congress
10 thought it had the power to do it, simply to
11 say, well, if you own shares in a foreign
12 corporation, whatever the ownership threshold,
13 simply pay taxes on those earnings.

14 That's not the way the tax -- that
15 these sorts of taxing provisions have ever
16 worked. Instead, they get at the idea who is
17 really earning the income and -- and -- and
18 receiving the benefit by it, and that person
19 should be the one to pay taxes on it. We think
20 they all fit that mold.

21 I'd like to briefly address the 1864
22 tax. The Court in Hubbard recognized that it
23 was a tax on property. Subsequently, in
24 Brushaber, the Court recognized that at the
25 time, that wasn't really considered or thought

1 about as being much of a defect with respect to
2 the direct tax clauses under sort of the
3 reasoning of Springer. And, of course, Macomber
4 rejected the exact same argument.

5 We would ask the Court to reverse.
6 Thank you.

7 CHIEF JUSTICE ROBERTS: Thank you,
8 counsel, General.

9 The case is submitted.

10 (Whereupon, at 12:14 p.m., the case
11 was submitted.)

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