Submitted J. Cohen
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UNITED STATES TAX COURT

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ESTATE OF NOORDIN M. CHARANIA, DECEASED, FARHANA CHARANIA, MEHRAN CHARANIA, and ROSHANKHANU DHANANI, ADMINISTRATORS

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET NO. 16367-07

Judge Mary Ann Cohen

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Cohen
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# PETITIONERS' REPLY BRIEF

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## INTRODUCTION

The parties' opening briefs have simplified the case by their agreement on many issues. Thus, the parties agree that:

(a) Belgian law determines whether or not the 250,000 Citigroup shares were held as community property;

(b) under Belgian conflict of laws principles, the ownership of matrimonial property is governed by the law of the common nationality of the spouses, in this case the law of the United Kingdom;

(c) the key question for decision is whether an English court in this case would follow the doctrine of immutability, under which the question whether property is held as community property turns on the law of the parties' domicile at the time of marriage, or the doctrine of mutability, under which the question turns on the law of the parties' domicile at the time of the decedent's death;

(d) if the immutability doctrine applies, ownership of the Citigroup shares continued to be governed by English substantive marital property law even after the move of Decedent and his spouse to Belgium, and Petitioners must lose this case because Decedent and his spouse did not formally change their marital regime under the procedures prescribed by the Belgian Code Civil;

(e) if, on the other hand, the doctrine of mutability applies, Petitioners win, because the exile of Decedent and his spouse from Uganda and their arrival in Belgium with the intent to remain there permanently brought them as a matter of law under Belgium's community property regime, with no need to follow the Code Civil formalities.

Petitioners showed in their Opening Brief that, in cases of forced exile like this one, the doctrine of immutability is uniformly recognized by leading authorities as unfair and inapplicable. Moreover, the only expert offered by the parties who actually opines on what an English court would do in this case is Barrister Cook, who states that the court would apply the doctrine of mutability and hold that Belgian substantive marital property law applies - meaning that the shares were indeed community property.

Respondent acknowledges in its Request For Findings of Fact that *its own authority*, DICEY, MORRIS & COLLINS ON THE CONFLICT OF LAWS (14TH ED.) 2006, "noted the inequity of the application of the doctrine of immutability to refugees." Resp. Br. p. 19. But Respondent never addresses that issue in its Argument, and none of its authorities ventures an opinion on what any court would do in this case.

Accordingly, we believe that Petitioners are entitled to prevail because an English court in this case of forced exile

would apply the doctrine of mutability and hold that Belgian rather than English substantive marital property law governs, with the result that the shares were held as community property.

## ARGUMENT

### I.
### THE SHARES WERE HELD AS COMMUNITY PROPERTY

#### A. The Parties Agree On The Relevant Facts

The parties' Stipulation and their respective briefs show that they concur on these few essential facts:

1. Decedent and his spouse were born in Uganda and were citizens of the United Kingdom when they married in 1967. ¶¶ 10-11, 13-14.[1]

2. When Uganda expelled all people of Asian and Indian descent from Uganda in 1972, Decedent and his family moved to Belgium, taking only a few items of personal property and owning no other assets. ¶¶ 20-21.

3. They did not intend to return to Uganda but instead intended to stay in Belgium. ¶¶ 22, 24.

4. The Citigroup shares at issue were acquired in 1997, twenty-five years after Decedent and Mrs. Dhanani had left Uganda for good. Exh. 11-J.

[1] The "¶" references are to the numbered paragraphs in the parties' Stipulation filed on Oct. 20, 2008. "Exh." references are to the Stipulation exhibits.

### B. The Parties Agree On All Relevant Legal Issues Except Whether An English Court Would Apply The Immutability Doctrine

Respondent agrees with Petitioners that Belgian substantive marital property law applies community property principles. Resp. Br. p. 27, 30-31. Respondent also agrees that Belgian conflicts law would refer the question of ownership to the law of the United Kingdom, the country of common nationality of Decedent and his wife. *Id.* pp. 17, 31.[2] Respondent further agrees that English substantive marital property law does not follow community property principles. *Id.* pp. 30, 35. Thus Petitioners are entitled to prevail if Belgium substantive marital property law applies, but not if English substantive laws applies.

Respondent does *not* agree that English conflicts law, applying the doctrine of mutability, would refer the issue of ownership in this case back to Belgian substantive marital property law, under which the Citigroup shares would be deemed

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[2] *See also* letter by Professor van Houtte, Exh. 24-J (a Belgian court would apply British law, including British choice of law principles); opinion of Nicole Atwill, Exh. 25-J (ownership of the Citigroup shares would be governed by British law); opinion of Nicole Atwill, Exh. 36-J (a Belgian court would look first to British choice of law rules to determine which jurisdiction's law should apply); letter of Nele Daam, Exh. 23-J (English law applies); opinion of Clare Feikert, Exh. 37-J (same).

community property. But Respondent's view on that score is incorrect, as we now show.

**C. An English Court Would Apply The Doctrine Of Mutability**

Respondent never addresses the question whether an English court would apply the doctrine of immutability or mutability. Its flawed position is that, because Decedent and his spouse, Mrs. Dhanani, were domiciled in Uganda when they were married, thereby coming under a regime of separate property ownership, they are stuck with that regime forever because they did not change it by following certain formal procedures under Belgian law. *See* Resp. Br. p. 41: "In fact it was the couple's failure to take the required action under the Belgian Code Civil which causes the shares to remain the separate property of decedent."[3]

An English court in this case would hold otherwise. Under the immutability doctrine, a change in residence by itself does not change the governing marital property regime; rather, the married couple must execute formal documents to effect a change. Resp. Br. pp. 36-37, 40. Under the mutability doctrine, however, no action by the couple is necessary: the change in domicile alone causes the applicable marital property law to

[3] *See also id.* at 31: "In fact, in Respondent's view, it was the failure of the spouses to take action to change their original matrimonial regime which causes the shares to be separate property."

"mutate" to the law of the new domicile. DICEY AND MORRIS ON THE CONFLICT OF LAWS (11TH ED.) 1987, Rule 156, Comment, Exh. 28-J, pp. 1068-69.

The opinion of Library of Congress specialist Clare Feikert strongly supports this view. Exh. 37-J. Feikert states that, if Decedent and Mrs. Dhanani

> intended to make Belgium their permanent and exclusive residence [as the parties have stipulated, *see* ¶¶ 22-24[4]], * * * the court would then have to determine whether the doctrine of mutability or immutability applies to the parties' matrimonial property under the English conflict of laws.

*Id.* pp. 6-7. If the spouses' failure to change their matrimonial property regime under the formalities of Belgian law was fatal to Petitioners' case, as Respondent claims, Feikert would never have gotten to the question whether the doctrine of immutability or mutability applies under English law.

The authorities cited by the parties that address the issue of mutability and cases of forced exile unanimously support the Petitioners. Thus, the British treatise DICEY AND MORRIS, cited by Respondent (at 36) states that

> the doctrine of immutability does not work well if the spouses are forced to change their domicile by political or economic pressure. It does not seem reasonable that political refugees should continue to be governed for the rest of their lives by the law of their

[4] *See also* Resp. Br. pp. 6, 7.

> matrimonial domicile - the one country in the world which they will probably never revisit.

Exh. 28-J, p. 1070. The article by William H. Newton III, cited by Respondent (at 36 and 37), also states that England "in appropriate circumstances may well look to the law of the new domicile." Exh. 27-J, p. 3 (citing DICEY). And the article by Robert Lawrence, cited by Respondent (at 37), while stating that courts "generally" follow the rule that assets do not lose their separate character "merely because the spouses have changed domicile," adds that courts will deviate from that rule "when the facts require such deviation to avoid an unfair or absurd result." Exh. 29-J, p. 7.[5]

Indeed, Barrister Cook opines that a British court would reach the same conclusion even in a case *not* involving forced exile. He states that in any case involving a long term change of domicile "there is an absurdity, particularly given increased longevity and mobility, to the property rights between a married couple being determined by a legal system in respect of which they have no remaining connection of any kind." Exh. 38-J at 6.

Respondent relies heavily on *De Nicols v. Curlier* [1900] A.C. 21 (Exh. 30), which Petitioners addressed in their Opening

[5] In the same article, Lawrence also states that a common law jurisdiction (such as England) "may adopt the modern 'contact' theory in deciding which law to apply, in which case the jurisdiction with the greatest interest in the matter will control." Exh. 29-J, p. 1.

Brief at p. 14 n.7. The case says nothing at all about circumstances of forced exile. Moreover, even Respondent's authorities acknowledge that the case does not reflect settled law. Feikert, Exh. 37-J p. 6; DICEY, MORRIS & COLLINS, Exh. 41-J, p. 1299 (both noting that the principles in *De Nicols* have not been settled and that some scholars contend that if a case is not strictly within the limits of *De Nicols* the doctrine of mutability should apply). And Barrister Cook distinguishes the case on additional grounds as well. Pet. Opening Br. at p. 14 n.7. Accordingly, *De Nicols* has no relevance to this Court's determination of this case.

Petitioners also relied in their Opening Brief on the decision in *In re Annesley* [1926] Ch. 692 (which applied French substantive law to the will of a British national), and the modern trend towards an interest analysis in choice of law matters (which would favor application of the substantive law of Belgium, the country with the strongest interest in the property ownership of Belgian domiciliaries). *See* Br. pp. 14-16, to which we respectfully refer the Court.

In sum, Respondent's view - that Decedent and Mrs. Dhanani's failure to execute formal documents bringing them under Belgium's marital property regime dooms Petitioners' case - would be relevant only if an English court were to hold in the first instance that the doctrine of

immutability applies in this case, for only then would the spouses sole recourse be to the Belgian Code Civil procedures. Here, however, an English court would rule that the doctrine of *mutability* applies, meaning that the spouses' forced exile and intent to remain permanently in Belgium was sufficient to bring them under Belgium's community property regime. Hence half of the 250,000 Citigroup shares held in Decedent's name at the time of his death belonged to his wife. Respondent's notice of deficiency should be set aside.

## II.
## NO PENALTY SHOULD BE IMPOSED

There are three reasons why no penalty should be imposed in this case. First, Respondent's abatement of the penalty assessed against the tax reported on the estate tax return similarly requires abatement of the penalty assessed against the additional tax shown on the Statutory Notice of Deficiency. Second, Petitioners had reasonable cause for any untimeliness. And third, if Petitioners are correct that there is no deficiency in estate tax, then no additional penalty may be assessed because the penalty assessed by the Notice of Deficiency relates only to the alleged deficiency. Elimination of the deficiency in tax also eliminates the penalty.

An understanding of the first and last arguments requires a clear explanation of the timing of the assessments and abatements at issue.

On November 12, 2002, Petitioners made a payment of $1,150,732.33, consisting of $1,148,216.50 of estate tax and $2,515.83 of interest. Petitioners filed an estate tax return reporting $1,148,216.50 in estate tax on April 29, 2004. Exh. 1-J. On June 21, 2004, Respondent assessed a late filing penalty of $289,085.37 and a late payment penalty of $7,115.33, both with respect to the estate tax reported on the return as filed. Resp. Br. p. 12; Exh. 5-J (Respondent's "Certificate of Assessments, Payments, and other Specified Matters").[6]

On February 22, 2007, Respondent served its Statutory Notice of Deficiency asserting that the Citigroup shares were not community property and claiming a deficiency in estate tax of $2,070,000.01. Exh. 4-J. The notice showed a total penalty for late filing of the return of $800,844.30, which Respondent reduced by the $289,085.37 it had already assessed on June 21, 2004 with respect to the tax reported on the return. *Id.* pp. 5 and 7. The notice thus assessed a penalty of $511,758.94,

[6] Under Code § 6651(a)(1), a late filing fee may be assessed in the amount of 5% of the tax for every month the return is late, for a maximum of five months, or 25%. The assessed penalty of $289,085.37 is in fact 25% of the amount stated on Respondent's "Certificate of Assessments, Payments, and other Specified Matters" as the tax shown on the return as filed ($1,156,341.49).

attributable to the incremental tax shown on the deficiency nctice. *Id.* p. 3.

On May 10, 2007, Respondent sent Petitioners a "Notice of Federal Tax Lien Filing" stating that Petitioners owed $320,412.67 with respect to the late filing and late payment penalties originally assessed on June 21, 2004. Exh. 19-P (Bate-stamp CHA 0036-37). On June 1, 2007, Respondent sent Petitioners a letter stating that, with additional interest, they now owed a total of $391,399.88. Exh. 19-P (Bate-stamp CHA 0038-40).

On July 6, 2007, Petitioners wrote to Respondent seeking a waiver of the late filing and late payment penalties on the ground that any untimeliness was due to reasonable cause. Exh. 20-P.

Respondent granted Petitioners' request and, on February 25, 2008, sent them a letter stating that the total amount they owed was $12,006.33. (Letter attached hereto at Tab A.) It is not clear why that amount remained owing but, in any event, Respondent admits that it abated the $289,085.37 penalty. Resp. Br. p. 12.[7] Exh. 5-J shows that it was abated *as of* June 21, 2004, the date it was originally assessed.[8]

[7] The only legal basis for the abatement of the penalty is a finding that the late filing was due to reasonable cause and was not due to willful neglect. Therefore the administrative

**A. Respondent's Abatement of $289,085 of The $800,844 Penalty Should Require Abatement of the Remaining $511,759**

Respondent has offered no reason for its different treatment of the late filing penalty as it relates to the tax reported on the return, on the one hand, and to the incremental tax asserted on the deficiency notice, on the other hand. It simply says that the $511,758.94 penalty asserted in the February 2, 2007 Notice of Deficiency remains in dispute "notwithstanding" the abatement of the $289,085.37 penalty assessed on June 21, 2004. Resp. Br. p. 12. *Id.*

There can be no logical or legal reason for treating the two assessments differently. Both penalties are asserted for the same late filing and in fact are really *two parts of the same penalty*. As shown above, the Notice of Deficiency showed a late filing penalty of $800,844.30, which was reduced by the already pending assessment of $289,085.37, leaving $511,758.93. Exh. 4-J, pp. 3, 5, and 7. Respondent's failure to offer any reason at all for the disparate treatment is essentially a concession that no good reason exists. Federal agencies must be

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abatement of the penalty carries with it a reasonable inference of a finding by Respondent that this standard was met.

[8] Respondent suggests that the abatement of the $289,085.37 came *before* the Notice of Deficiency assessment of the $511,758.94 (*id.*), but that is not accurate. Rather, as we have just shown, the abatement took place in February 2008, a year after the February 22, 2007 Notice of Deficiency was sent.

consistent in the application of the statutes they administer. *See, e.g., General Chemical Corporation v. U.S.*, 817 F.2d 844, 855 (D.C. Cir., 1987) (vacating the Interstate Commerce Commission's review of rail transportation rates because the Commission's "confusing and inconsistent analysis," ignoring the agency's own guidelines, "was so incomplete and conclusory as to fall below the standard of reasoned decisionmaking" and was therefore arbitrary and capricious). *See also Estate of Jung v. Comm'r*, 101 T.C. 412, 452 (1993) (holding that in failing to waive penalty for valuation understatement Commissioner abused her discretion by making a determination "arbitrarily, capriciously or without sound basis in fact"); *Estate of Berg v. Comm'r*, 976 F.2d 1163 (8th Cir. 1992) (holding that Commissioner abused his discretion in failing to abate penalty when taxpayer's valuation had a reasonable basis and was made in good faith). It follows that, because Respondent abated part of the penalty on "reasonable cause" grounds, the same "reasonable cause" warrants abatement of the rest of the penalty as well.

In any case, as Respondent recognized when it abated the $289,085.37, Petitioners did in fact have reasonable cause for the late filing.

**B. Petitioners Had Reasonable Cause**

Petitioners' failure to file a timely return was not due to willful neglect, and Respondent does not contend otherwise.

Rather, Respondent asserts that Petitioners had no "reasonable cause" for the untimeliness, citing *United States v. Boyle,* 469 U.S. 241, 245 (1985). That case, however, is different from this one in several critical respects.

First, the payment of the tax in *Boyle* was not made until the return was filed. As the Supreme Court noted, "Congress' purpose in the prescribed civil penalty was to ensure timely filing of tax returns to the end that tax liability will be ascertained and paid promptly." *Id.* p. 245. Here, the full amount reported on the estate tax return ($1,148,216.50 of tax and $2,515.83 of interest) was paid on November 12, 2002, only twelve days after the return was due and long before the tardy return was filed on April 29, 2004.[9]

Second, *Boyle* did not involve foreign nationals with minimal contacts with the United States. It is by no means intuitively obvious that the estate of a foreign national who so far as it appears never set foot in the United States or did any business in the United States would owe U.S. estate taxes simply by virtue of holding stock in a U.S. company. When Petitioners

[9] The tax payment was originally due on October 31, 2002. Petitioners filed for an extension to file the return until April 30, 2003, which Respondent granted, and for an extension to pay the tax until October 31, 2003, which Respondent never granted or denied. *See* Exh. 16-J (granting the extension for filing the return but leaving vacant the boxes ("Approved" and "Not Approved") for the extension to pay. The November 12, 2002 payment was well within the extension sought by Petitioners.

learned that U.S. estate tax might be payable with respect to the Citigroup shares, they engaged a U.S. law firm, which on their behalf requested the extensions and paid the tax.[10] Moreover, as foreign nationals with no knowledge of U.S. laws, Petitioners had every reason to believe that the critical issue was the payment of the tax, not the filing of the return, and that the payment of the tax, having been made within the time allowed for filing the return, satisfied their principal obligation to the U.S. Indeed, having paid the tax, Petitioners had no reason to delay the filing of the return. Rather, the delay in filing the actual return was occasioned by their counsel's actions, including consideration of the legal complexities regarding the ownership of the shares by Decedent's spouse as well as the practical steps required to form a qualified domestic trust.[11]

Internal Revenue Manual ¶ 20.1.1.3.1.2 (2-22-2008) provides that a taxpayer "may establish reasonable cause by providing

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[10] Petitioners have since terminated that firm and retained the undersigned counsel.

[11] For a parallel example, imagine a U.S. widow who learns that her husband's estate is subject to tax in Belgium and hires a U.S. lawyer and a Belgian lawyer to steer her through the complexities of Belgian law and pays the (sizable) amount her lawyers tell her is due. She might be forgiven - *i.e.*, have reasonable cause - for not knowing that her Belgian counsel had delayed the filing of the actual return. *See Brown v. United States*, 630 F. Supp. 57, 59 (M.D. Tenn. 1985) ("[A] taxpayer who is unable to exercise the required standard should not be penalized for a late filing.").

facts and circumstances showing that they exercised ordinary business care and prudence (taking that degree of care that a reasonably prudent person would exercise)." Here the "reasonably prudent person" should be defined as a reasonably prudent foreign national with no familiarity with U.S. tax laws who, despite a lack of contact with the U.S., sought to comply with U.S. estate tax law, hired counsel in both Belgium and the U.S., and paid what she believed (and continues to believe) to be the full amount of tax owing. That describes the Petitioners, who exercised ordinary business care and prudence in seeking to comply with U.S. tax laws.

That description also distinguishes this case not only from *Boyle* but also from the other decisions relied on by Respondent. In *Estate of Campbell v. Comm'r*, T.C. Memo 1991-615, cited by Respondent (at 48), "[t]he executrix was aware of her duty to file within the due date, and yet consciously failed to file a timely return and pay the estate tax." (P. 38.) *Estate of Ridenour v. Comm'r*, 468 F. Supp. 2d 941 (S.D. Ohio 2006), cited by Respondent (at 47, 48), like *Boyle*, involved a "failure to file [the] estate tax return and to pay the estate tax owing in timely fashion." *Id.* p. 943. And *Sandoval v. Comm'r*, T.C. Memo. 2000-189, cited by Respondent (at 48), involved experienced U.S. businessmen who had filed U.S. tax returns for their business for years.

In sum, we urge the Court to rule that Petitioners' failure to file a timely return was due to reasonable cause[12] based upon the unique facts of this case, involving U.S. estate tax on a foreign estate solely by virtue of the presence of U.S. corporate stock in the estate, essentially timely payment of $1,150,732.33 of estate tax and interest, honest efforts by Petitioners to put themselves in compliance with U.S. laws, and the prior recognition by Respondent of the unique circumstances of Petitioner's situation as evidenced by its abatement of the late filing penalty with respect to the tax reported on the return.[13]

### C. If Petitioners Paid The Correct Tax, No Additional Penalty May Be Assessed

If Petitioners are correct that the Citigroup shares were held as community property, then the payment they made on November 12, 2002 was the right amount and there is no deficiency in estate tax. The penalty on the Notice of Deficiency relates to the incremental tax assessed on the

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[13] Respondent abated the earlier penalty assessment on the basis of a letter from Petitioners' counsel (*see* Exh. 20-P), demonstrating that Respondent does not always require a sworn statement from the taxpayer before it will abate a penalty. Out of an abundance of caution, however, we have provided Respondent a sworn statement under penalty of perjury by Petitioner Farhana Charania that all of the statements in counsel's earlier letter are true. See Tab B, *infra*.

Notice. Therefore, if there is no deficiency, the penalty may not be assessed.

As we have seen, Respondent originally assessed a late-filing penalty of approximately 25% of the tax paid on November 12, 2002 - $289,085.37 - but later abated that penalty, as Respondent concedes. Resp. Br. p. 12. The $511,758.94 late filing penalty remains in dispute only if Petitioners lose on the merits, since the $511,758.94 is the penalty amount assessed in connection with additional tax Respondent asserts is owed. Exh. 4-J, pp. 3, 5, 7. If Petitioners prevail on the merits, however, the late filing fee Respondent asserted based on Petitioner's November 12, 2002 payment has already been abated and cannot be revived.

**CONCLUSION**

The Court should enter an Order that-

1. the ownership of the Citigroup shares is governed by Belgian marital property law, meaning that the shares were community property owned one-half by Decedent and one-half by his spouse;

2. no deficiency in estate tax or penalties are due from the Estate;

3. Petitioners are entitled to all correlative adjustments allowable by operation of law, including any applicable refunds for taxes overpaid;

4. in any event, any failure to timely file a timely estate tax return was due to reasonable cause; and

5. Petitioners are entitled to such other and further relief as may be appropriate.

Respectfully submitted,

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