

SUPREME COURT OF THE UNITED STATES

Boeing Co. v. United States

537 U.S. 437 (2003) · No. Nos. 01-1209 and 01-1382 · Decided March 4, 2003

SUMMARY

The Supreme Court considered whether Treasury Regulation 26 C.F.R. § 1.861-8(e)(3) validly governed the allocation of research and development expenses in calculating combined taxable income under the DISC and FSC export-tax regimes. The Court held that the regulation was a reasonable interpretation of the Internal Revenue Code and related DISC regulations and affirmed the Ninth Circuit. Boeing therefore was not entitled to a refund of additional taxes assessed after the IRS reallocated its research expenses.

CASE DETAILS

COURT	Supreme Court of the United States
WRITING FOR THE COURT	Justice Stevens; Chief Justice Rehnquist; Justice O'Connor; Justice Kennedy; Justice Souter; Justice Ginsburg; Justice Breyer; Justice Thomas; Justice Scalia
JURISDICTION	Federal
DECIDED	March 4, 2003
DOCKET	Nos. 01-1209 and 01-1382
DISPOSITION	affirmed
PROCEDURAL POSTURE	Boeing sought a tax refund after the IRS reallocated research-and-development expenses and assessed additional tax. The District Court granted summary judgment for Boeing, the Ninth Circuit reversed, and the Supreme Court granted certiorari to resolve a circuit conflict.
STANDARD OF REVIEW	The validity and application of the Treasury regulation were reviewed de novo, with deference given to the Secretary of the Treasury's reasonable interpretation of the Internal Revenue Code.
PRECEDENTIAL VALUE	binding Supreme Court precedent
PARTIES	The Boeing Company and subsidiaries, United States in No. 01-1382 v. United States in No. 01-1209, Boeing Sales Corporation and related entities in No. 01-1382

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QUESTIONS PRESENTED

1. Whether Treasury Regulation § 1.861-8(e)(3) (1979), which allocates R&D expenses across products within relevant two-digit SIC categories, was validly applied in computing combined taxable income for DISC and FSC transactions.
2. Whether the DISC statute and related regulations gave Boeing an unqualified right to allocate product-specific R&D expenses only to the products to which Boeing factually related them.
3. Whether the statutory text of 26 U.S.C. §§ 861 and 994, the DISC regulations, and legislative history defeated the Secretary of the Treasury's interpretation and application of the R&D allocation regulation.

HOLDINGS

1. Treasury Regulation § 1.861-8(e)(3) (1979) may validly be applied to allocate Boeing's deductible R&D expenses among products within the relevant two-digit SIC category and to apportion those expenses between Boeing and its export subsidiaries when computing combined taxable income.
2. The taxpayer's choice of transaction grouping under 26 C.F.R. § 1.994-1(c)(7) is controlling as to the grouping of sales and the choice of transfer-pricing method, but it does not give the taxpayer exclusive authority to determine how R&D costs are allocated among the grouped items or apportioned between the DISC and its parent.
3. The terms 'attributable' and 'combined taxable income' in 26 U.S.C. § 994, together with 26 U.S.C. § 861(b), do not prohibit reasonable categorical allocation of R&D expenses under § 1.861-8(e)(3).

KEY QUOTATIONS

"In sum, Boeing's arguments based on statutory text are plainly insufficient to overcome the deference to which the Secretary's interpretation is entitled." (451)

"Treasury Regulation § 1.861-8(e)(3) fills this gap by providing that R&D expenditures that are related to all income reasonably connected with the taxpayer's relevant two-digit SIC category or categories are "allocable to all items of gross income as a class . . . related to such product category (or categories)."" (455)

"The fact that Congress did not legislatively override 26 CFR § 1.861-8(e)(3) (1979) in enacting the FSC provisions in 1984 serves as persuasive evidence that Congress regarded that regulation as a correct implementation of its intent." (457)

FACTUAL BACKGROUND

Boeing operated domestic international sales corporation and foreign sales corporation subsidiaries and generated substantial export sales of commercial aircraft. For the tax years at issue, Boeing deducted approximately \$3.6 billion in Company Sponsored R&D expenses by assigning them to particular aircraft programs, including programs that generated no sales in the year the expenses were incurred. The IRS reallocated those expenses across products within the relevant two-digit SIC category under Treasury Regulation § 1.861-8(e)(3) (1979), reducing the untaxed profits of Boeing's export subsidiaries and increasing Boeing's taxable income.

PROCEDURAL HISTORY

The IRS reallocated Boeing's Company Sponsored R&D expenses for tax years 1979 through 1987, increasing the taxable profits attributed to Boeing rather than its export subsidiaries. Boeing paid approximately \$419 million in additional tax and filed a refund action. The District Court held the Treasury regulation invalid as applied to DISC and FSC transactions and entered summary judgment for Boeing. The Ninth Circuit reversed, and the Supreme Court affirmed.

DISPOSITION

affirmed

CASES CITED

- St. Jude Medical, Inc. v. Commissioner, 34 F.3d 1394 (8th Cir. 1994)
- Cottage Savings Assn. v. Commissioner, 499 U.S. 554, 560-561 (1991)
- Lorillard v. Pons, 434 U.S. 575, 580-581 (1978)
- United Dominion Industries, Inc. v. United States, 532 U.S. 822, 839 (2001) (Thomas, J., concurring)
- Leavell v. Blades, 237 Mo. 695, 700-701, 141 S.W. 893, 894 (1911)
- Morales v. Trans World Airlines, Inc., 504 U.S. 374, 384 (1992)
- Crawford Fitting Co. v. J. T. Gibbons, Inc., 482 U.S. 437, 445 (1987)