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FINDERS-KEEPERS: WHO OWNS THE TAX REFUND OF AN INSOLVENT COMPANY

ABA TAX SECTION – TAX COLLECTION, BANKRUPTCY AND WORKOUTS COMMITTEE
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INTRODUCTION

In recent years, the ownership of a tax refund has become a major source of litigation. Potential claimants include creditors, affiliates and shareholders.

Many of the recent cases involve the FDIC. In a recurring situation, a banking subsidiary fails and is taken over by regulators. The bank holding company then files for bankruptcy. The bank holding company on behalf of a consolidated group carries back a net operating loss (NOL) and claims a refund from the IRS. The FDIC claims entitlement to the refund claim since the bank's operating loss created the NOL and resulted in the claim for refund. The result is ligation between the FDIC (as receiver for the bank) and the bankruptcy trustee for the bank holding company.

Even though many cases involved the exact fact pattern described above, the results have not been consistent or predictable. The Tenth Circuit resolved a recent case in favor of the FDIC (on behalf of the banking subsidiary). Rodriguez v. FDIC (United W. Bancorp.), 893 F.3d 716 (10th Cir. 2018) (hereinafter United Western Bancorp).

This paper discusses United Western Bancorp in depth since it represents the most current thinking by the courts as to how these cases should be analyzed. This paper attempts to make some sense of the rules and cases, which can be inconsistent or vary based on fine distinctions.

The specific issues dealt with in this paper (i.e., the carryback of tax attributes for a refund) may not come up as often in the future. The so-called Tax Cuts and Jobs Act eliminated the ability to carry back NOLs that were created in 2018 and later tax years. PL 115-97, § 13302(b)(1). However, other tax attributes (e.g., capital losses and tax credits) can still be carried back.

TAX-SHARING AGREEMENTS

Most tax refund dispute cases involve multiple corporations that file a single federal return pursuant to the consolidated return regulations.

Groups of controlled domestic corporations are permitted to file separate United States federal income tax returns with the IRS. However, few such groups file in that manner. Instead, affiliated groups of corporations typically "exercise the privilege" to file a consolidated return with the IRS. IRC § 1501; Treas. Reg. § 1.1502-75(a)(1).

An affiliated group is generally a group of U.S. corporations that has a common parent corporation and one or more subsidiaries that are 80 percent owned (by vote and value) by the common parent corporation or another member of the group. IRC § 1504(a)(1), (2). An affiliated group that files a consolidated return is called a "consolidated group." Treas. Reg. § 1.1502-1(h).

Where a consolidated return is filed, the tax (and any tax refund) is computed on a consolidated basis. The common parent of the consolidated group is generally considered the sole agent for all of the members of the consolidated group with respect to most dealings with the IRS regarding the consolidated return. Treas. Reg. § 1.1502-77(a)(1). As a result, only the common parent can generally file a refund claim with the IRS with respect to a consolidated return and the IRS will generally issue the refund only to the common parent. Treas. Reg. § 1.1502-77(a)(2)(v).

If we stopped there, it would appear that the common parent would be entitled to any tax refund (even if the refund were attributable to a subsidiary). To prevent unfairness between members of a consolidated group, it is typical for members of a consolidated group (or similar state group) to enter into a tax-sharing agreement (TSA).

TSAs typically provide for, among other things, (i) the sharing of any consolidated tax liability among members, (ii) compensation for one member's use of another member's tax attributes and (iii) the sharing among members of any consolidated refunds. See Jasper L. Cummings, Jr., "Tax Sharing Agreements and Related Contracts." Tax Notes, Sept. 22, 2014, p. 411.

The parties may enter into a TSA because a bank lender (or other creditor) requires it. Alternatively, there can be a need for such an agreement where there are minority investors. The reason for a TSA in such cases is to impose fairness among the members of the group. For example, a lender to one subsidiary would not want the subsidiary to pay an unfair portion of the group's taxes and would not want the parent to benefit from the subsidiary's losses.

TSAs may be entered into for a variety of other reasons as well. A group may have a TSA just to assist the accountants and bookkeepers in determining the net profit per company. In addition, the TSA may be there just to ensure that the parent can collect money from the subsidiaries to pay the consolidated tax liability (without having to resort to having the subsidiary declare a dividend). Where there are no outside parties involved in negotiating the TSA, the agreement could be just a statement of policy instead of a formal legal agreement.

As discussed in more detail below, bank holding companies are required to have a TSA with their banking subsidiaries.

Many of the below cases involve a TSA (and how to interpret it). Others involve what to do when there is no TSA.

NON-BANKING CASES

The earliest cases dealing with entitlement to a tax refund involved consolidated groups that were not in the banking industry. The more recent cases have involved banks and bank holding companies.

In re Bob Richards Chrysler-Plymouth Corp., 473 F.2d 262 (9th Cir. 1973), was one of the earliest cases dealing with the owner of a tax refund and is still an important case today. In Bob Richards, the Ninth Circuit determined the ownership of a consolidated tax refund in the absence of a TSA. The court held that where there is an explicit agreement as to the owner of a consolidated refund (or where an agreement can fairly be implied), then state corporate law governs the ownership of any tax refund. 473 F.2d at 264.

However, in the absence of an express or implied agreement, the Ninth Circuit held that the entitlement to the refund should be determined under federal common law. It held that "a tax refund resulting solely from offsetting the losses of one member of a consolidated group against the income of that same member in a prior or subsequent year should inure to the benefit of that member." Id., 473 F.2d at 265. In such case, the common parent corporation holds the tax refund in trust for the subsidiary. The court held that a subsidiary was entitled to the refund since the subsidiary's NOL was carried back against the subsidiary's prior year income.

The analysis of Bob Richards was applied in several cases in situations where there was no express agreement as to the owner of an NOL or tax refund. See Capital Bankshares v. FDIC, 957 F.2d 203, 207-08 (5th Cir. 1992) (tax refund); Jump v. Manchester Life & Casualty Management Corp., 438 F. Supp. 185, 189 (ED Mo. 1977) (subsidiary entitled to share of tax refund to the extent of prior taxes paid), aff'd, 579 F.2d 449 (8th Cir. 1978).

It should be noted that not all courts have agreed with the Ninth Circuit's ruling that federal common law applies in the absence of a TSA. In FDIC v. AmFin Fin. Corp., 757 F.3d 530 (6th Cir. 2014), cert. denied, 135 S. Ct. 1402 (U.S. 2015), the Sixth Circuit did not apply Bob Richards on the ground that federal law does not govern the allocation of a consolidated tax refund. The court determined that the owner of the refund is based solely upon applicable state corporate law. AmFin, 757 F.3d at 535. It should be noted that only two of the three judges supported this aspect of the decision. See id., 757 F.3d at 538-40 (Gilman concurring).

Thus, while Bob Richards provides that state corporate law generally governs when there is a TSA, the Sixth Circuit applies state corporate law even in the absence of a TSA. There are only a few cases that determine the enforceability and interpretation of a TSA under state corporate law. Those cases tend to involve states with a thriving corporate litigation practice (such as Delaware, California and New York). In other states, it is difficult to predict the outcome, based upon the dearth of authorities.

The Ninth Circuit in Western Pacific Railroad Corp. v. Western Pacific Railroad Co,, 197 F.2d 994 (9th Cir. 1951), rev'd on other grounds, 345 U.S. 247 (1953), had previously dealt with a tax benefit issue (before deciding Bob Richards). In that case, the parent corporation took a worthless stock loss with respect to the subsidiary stock. As a result, the group did not have to pay any tax on the subsidiary's profits. Even though there was no TSA the parent corporation claimed that the subsidiary should pay it for use of its losses in the amount of the subsidiary's tax savings. In an unusual set of facts, the court decided that the subsidiary controlled the parent and had a fiduciary duty to treat the parent with fairness. However, the court concluded that it was not unfair for the parent to not be reimbursed for use of its losses, since (i) it conformed to past practice and (ii) the parent was in the same economic situation as if it filed as separate return. A similar result was achieved in Meyerson v. El Paso Natural Gas Co., 246 A.2d 789 (Del. Ch. 1967) (parent did not need to reimburse subsidiary for use of losses) and Smith v. Tele-Communication, Inc., 184 Cal. Rptr. 571 (Ct. App. 1985) (parent was prevented from receiving reimbursement for use of its losses).

The analysis in Jump v. Manchester Life & Casualty Management Corp., 579 F.2d 449 (8th Cir. 1978) is unusual and bears discussion. A parent corporation and a subsidiary filed a consolidated return. The subsidiary was in the insurance business but ultimately failed and was taken over by a conservator. When the subsidiary had been profitable, it had paid to its parent its share of the consolidated tax liability. It appears that this payment was pursuant to a tax-sharing policy (and not a TSA). In the subsidiary's last years of operations, it incurred losses. These losses were used by the parent corporation as a carryback for a refund. The parent remitted some of the refund to the subsidiary and kept the rest.

It appears that the Eighth Circuit in Jump treated the above arrangement as an implied TSA and analyzed the facts under state corporate law. To do this it had to determine whether Missouri (the place of incorporation of the parent corporation) or Ohio (the place of incorporation of the subsidiary) law applied. The court decided to apply Missouri law since both corporations were headquartered there. The court then analyzed whether the parent breached its fiduciary duty to the subsidiary under Missouri law. The court noted that the subsidiary had previously agreed to join in a consolidated return and was prevented by tax regulations from withdrawing the consent in later tax years. As a result, the court concluded that the NOL of the subsidiary was not an asset of the subsidiary that was protected by a fiduciary duty. Instead, it permitted the subsidiary to receive a portion of the refund that was limited to the actual taxes paid by the subsidiary to the parent corporation.

The Jump requirement that the amount owed the subsidiary is limited to the taxes previously paid was also applied by the bankruptcy court in In re Coral Petroleum Inc., 60 BR 377 (Bankr. SD Tex. 1986). As in Jump, the subsidiary was required to determine its share of the consolidated tax liability. However, the amount owed was only recorded as a payable by the subsidiary to the parent. Similarly, the subsidiary's share of the later year refund was recorded as a receivable by the subsidiary from the parent. The subsidiary never made any payments on the payable, and the court did not believe there was an intent to make those payments. (Although the court did not use this terminology, it appears that the payable and receivables were not respected as debt obligations). Since the subsidiary had not previously paid its share of the taxes, the court held that it was fair for the parent to retain the entire refund from the IRS. 60 BR at 384-91.

The bankruptcy court in In re All Products Co., 32 BR. 811 (Bankr. E.D. Mich. 1983) treated the parties' conduct as an implied TSA. In the case, the parent corporation was profitable and used the subsidiary's losses to reduce the consolidated tax liability. In the seven years for which the parties filed consolidated returns, the subsidiary never received compensation for the losses. The court treated this as the equivalent of a binding TSA and did not require the parent to compensate the subsidiary for use of the losses.

Frequently, the parent corporation drafts the TSA and does so in a manner that benefits itself. Since the subsidiaries do not generally have an ability to refuse to sign an agreement with the parent corporation, there is a potential for abuse on the part of the parent corporation. As a result, some courts have imposed a fiduciary duty on the parent corporation to treat the subsidiary with fairness in drafting a TSA.

In Case v. New York Central Railroad Co., 204 N.E.2d 643 (NY 1965), a parent corporation had operating losses and a subsidiary had a profit. The TSA required the subsidiary to pay hypothetical tax amounts to the parent (compensating the parent for partial use of the losses). Minority shareholders of the subsidiary were of the view that the subsidiary was not being treated fairly and decided to file suit. The court held that under New York law the parent had not breached its fiduciary duty to the subsidiary. It was acknowledged that the parent was required to follow a course of fair dealing with the subsidiary. It was noted that the subsidiary was not harmed by the agreement since the actual tax would have been greater if it filed a standalone return.

The cases dealing with sharing of NOLs under state corporate law provisions generally look to issues regarding whether one party has a fiduciary duty to another and whether the parties are treating each other with fairness. If one or more of the members of the group file for bankruptcy, additional restrictions apply. The Supreme Court has held that an NOL carryback is property of the debtor's estate and cannot be interfered with by third parties (without the permission of the bankruptcy estate). Segal v. Rochelle, 382 U.S. 375 (1966).

The Second Circuit expanded the Supreme Court's protection of NOL carrybacks to NOL carryforwards. In In re Prudential Lines, 928 F.2d 565, 570-71 (2d Cir. 1991), the subsidiary had NOL carryforwards and had filed for bankruptcy. The parent corporation was entitled to a worthless stock deduction with respect to its investment in the subsidiary. Pursuant to Section 382(g)(4)(D) of the Internal Revenue Code of 1986, as amended (the Code), if the parent took a worthless stock deduction, the utility of the subsidiary's NOLs would be eliminated. Consequently, the court allowed an injunction to be placed that prevented the parent corporation from taking a worthless stock deduction.

BANKING SUBSIDIARIES

The more recent cases have all dealt with the ownership of a tax refund where the subsidiary is a bank and the parent corporation is a bank holding company. There are several statutory and regulatory provisions that apply only to banks. They are discussed here before we discuss the significant tax refund cases.

Section 6402(k) of the Code grants authority to the Treasury Department to issue regulations concerning the ownership of tax refunds from a consolidated group. This authority applies to a member of the group that is insolvent and is subject to a statutory or court appointed fiduciary. In such case, the regulations can provide that a refund attributable to losses of credits of the subsidiary can be paid to the fiduciary.

Regulations implementing Section 6402(k) were issued in the 1990s. The regulations permit the Federal Deposit Insurance Corporation (the FDIC) to notify the IRS and the common parent corporation of the consolidated group that it is a fiduciary for an insolvent financial institution. In such case, the FDIC can file a refund claim on behalf of the subsidiary or submit a refund claim that was prepared by the common parent. In such instance, the IRS can pay some or all of the refund to the FDIC. Treas. Reg. § 301.6402-7.

It is not clear that Section 301.6402-7 is being applied frequently by the FDIC. (The cases discussed below would appear to have been unnecessary if the provision had been applied.)

In addition, bank holding companies are required by their regulators to have a TSA in place with their banking subsidiaries. 2014 Policy Statement Addendum, 79 Fed. Reg. 35,230, n. 7. Payments under a TSA are required to be forwarded promptly and the timing is specified. Id., 79 Fed. Reg. 35,230.

Before 2014, there was uncertainty as to whether a TSA was required when a bank holding company elected to be treated as an S corporation (i.e., a corporation that is treated as a pass-through entity that is not generally subject to U.S. federal income tax). It is now clear that the TSA requirement does not apply if the bank holding company is not subject to corporate income tax (at the federal or state level). Id., 79 Fed. Reg. 35,229.

When TSAs are required, the TSAs must include the below paragraph (or substantially similar language):

> *The [holding company] is an agent for the [IDI and its subsidiaries] (the "Institution") with respect to all matters related to consolidated tax returns and refund claims, and nothing in this agreement shall be construed to alter or modify this agency relationship. If the [holding company] receives a tax refund from a taxing authority, these funds are obtained as agent for the Institution. Any tax refund attributable to income earned, taxes paid, and losses incurred by the Institution is the property of and owned by the Institution, and shall be held in trust by the [holding company] for the benefit of the Institution. The [holding company] shall forward promptly the amounts held in trust to the Institution. Nothing in this agreement is intended to be or should be construed to provide the [holding company] with an ownership interest in a tax refund that is attributable to income earned, taxes paid, and losses incurred by the Institution. The [holding company] hereby agrees that this tax sharing agreement does not give it an ownership interest in a tax refund generated by the tax attributes of the Institution.*

Id., 79 Fed. Reg. 35,230.

The recent court cases involving the issue of ownership of a consolidated tax refund all had a similar fact pattern. A bank holding company (Holdco) and a banking corporation (the Bank) filed a consolidated return for U.S. federal income tax purposes. Holdco and the Bank entered into a TSA. The Bank underperformed and eventually went into receivership, the FDIC was appointed as the receiver, and Holdco filed for bankruptcy. (Banking institutions are not permitted to file for bankruptcy.) The consolidated group carried back one or more

NOLs to a prior profitable consolidated return year for a refund. Holdco received the refund from the IRS. Holdco and the FDIC (on behalf of the Bank) then disputed which entity was entitled to retain the refund.

The TSA between Holdco and the Bank in many of the cases stated that the Bank was entitled to the refund. In some cases, the Bank prevailed based on the language in the TSA. In other cases, Holdco prevailed because the Bank was merely an unsecured creditor under the TSA and under bankruptcy law was entitled to collect on its claim only after creditors with a greater priority were paid in full.

In Zucker v. FDIC (In re BankUnited Fin. Corp.), 727 F.3d 1100 (11th Cir., 2013), cert denied, 571 US 1244 (2014), the Eleventh Circuit held for the FDIC (on behalf of the Bank). The Bank was entitled to the refund under the terms of the TSA. However, the TSA was ambiguous as to whether the Bank was entitled to receive the refund from Holdco under a debtor-creditor or principal-agent relationship. The Eleventh Circuit found an agency relationship (i.e., Holdco held the funds in escrow for the benefit of the Bank and the other members of the consolidated group) on the basis that the parties intended that Holdco promptly forward any tax refund to the Bank. Id., 727 F.3d at 1107.

The Eleventh Circuit came to a similar conclusion in FDIC v. Zucker (In re NetBank), 729 F.3d 1344 (11th Cir. 2013), cert. denied, 135 S. Ct. 476 (2014). It should be noted that in NetBank the TSA stated that the agreement was intended to allocate taxes under the predecessor of the 2014 Policy Statement. The Eleventh Circuit took into account the Policy Statement as extrinsic evidence that Holdco held the tax refund as agent for the Bank.

In FDIC v. Siegel, (In re IndyMac Bancorp), 554 Fed. Appx. 668 (9th Cir. Apr. 21, 2014) (mem.), the Ninth Circuit held that Holdco was entitled to retain the tax refund. The TSA provided that Holdco had the “sole discretion” to determine the “means and manner” of paying refunds and appointed Holdco as agent and attorney-in-fact for the Bank. The court did not believe that this established a principal-agent relationship under state law since the Bank did not exercise control over Holdco’s activities. Id., 554 Fed. Appx. at 670.

The Sixth Circuit in FDIC v. Amfin Financial Corp., 757 F.3d 530 (6th Cir. 2014), cert. denied, 135 S. Ct. 1402 (2015), remanded the case back to the district court for further findings on the proper interpretation of the TSA in question. The Sixth Circuit held that there was nothing in the applicable TSA that evidenced an unambiguous intent to allocate the refund to the Bank and to create a debtor-creditor relationship. Id., 757 F.3d at 534. The court held that the mere use of the terms “reimbursement” and “payment” in the TSA were not sufficient to create a debtor-creditor relationship. Id., 757 F.3d at 535. The FDIC on behalf of the Bank argued that, under Ohio law, the Bank was entitled to the refund since either a resulting trust was created or Holdco was acting as an agent for the Bank in requesting the consolidated refund. Id., 757 F.3d at 536. A resulting trust is created where the parties did not intend the holder of legal title, based on facts and circumstances, to enjoy the beneficial interest in the property. The Sixth Circuit remanded the case to the district court to determine the owner of the refund under Ohio law (taking into account extrinsic evidence with respect to the possibility that a resulting trust or agency relationship was created). Id., 757 F.3d at 538.

The Amfin Fin. case is notable in that the court rejected the proposed use of federal common law. The court stated that state law determines whether property is part of a bankruptcy case. The court refused to employ a Bob Richards analysis since, in its view, federal common law did not govern the allocation of a federal tax refund. Id., 757 F.3d at 536. There is uncertainty as to why federal common law was discussed at all. Bob Richards stands for the proposition that state corporate law applies when there is a TSA in place and federal common law applies only in the absence of a TSA. The Amfin Fin. case involved an interpretation of a TSA (so federal common law would not appear to have been relevant).

The Sixth Circuit in Amfin Fin. claimed that the Eleventh Circuit in both Bank United and Net Bank took the position that there was no federal common law that applied to determine ownership of a tax refund. Id., 757 F.3d at 536. There does not appear to be language in Bank United to support the contention by the Eleventh Circuit. The court in Net Bank only stated that the result under the "Bob Richards rule" would not have been different. 729 F.3d at 1347 n. 3. The Tenth Circuit in United Western Bancorp applied the Bob Richards rule and noted that the Sixth Circuit has a different view. 893 F.3d at 724 n. 4.

The findings of the four circuit court decisions discussed above are based on all of the specific facts and circumstances relating to the relationship between a banking subsidiary and a bank holding company. Since the situations in each of the cases is very different, it is very difficult to read them with a view to predicting how other courts will find. Presumably, some insights will be forthcoming as future cases are resolved.

UNITED WESTERN BANCORP

The Tenth Circuit decided Rodriguez v. FDIC (In re United W. Bancorp), 893 F.3d 716 (10th Cir. 2018) on June 19, 2018. The circuit had not previously decided a tax refund entitlement case. The FDIC, as receiver for the bank, was held to be entitled to the refund.

United Western Bancorp, Inc. (UWBI) was a bank holding company that held all of the stock of United Western Bank (the Bank), which was engaged in a banking business.

UWBI and the Bank filed a consolidated federal tax return. In 2008, UWBI and the Bank entered into a tax allocation agreement (the Agreement). The Agreement set up a method for (i) allocating the consolidated tax liability among the parties and (ii) compensating one party for use of its losses by another member.

In 2008, the group return showed consolidated taxable income of approximately $34.3 million. In 2010, the group return showed a consolidated NOL of approximately $35.4 million. Both the 2008 taxable income and the 2010 NOL were wholly attributable to activity of the Bank.

In 2011, the group requested a refund from the IRS of approximately $4.8 million, which was a partial recovery of the taxes paid by the Bank with respect to the 2008 taxable year. The IRS audited the group and issued a refund of approximately $4.1 million in 2015.

The Bank entered financial trouble as a result of the Great Recession. On January 21, 2011, the Bank was closed by the regulators, and the FDIC was appointed as the receiver for the bank.

The Bank receivership resulted in UWBI becoming insolvent since the Bank was UWBI's principal source of income. On March 2, 2012, UWBI filed a bankruptcy petition. A bankruptcy trustee was appointed in 2013.

In 2014, the trustee for UWBI filed a complaint with the bankruptcy court for possession of the IRS tax refund. In 2016, the bankruptcy court found for the trustee, allowing it to retain the refund. The following year, the district court reversed the bankruptcy court and found that the FDIC was entitled to the refund. The Tenth Circuit ultimately upheld the decision of the district court.

The Tenth Circuit began its analysis with a discussion of the federal common law. The circuit had previously adopted the principals of Bob Richards in that a tax refund belongs to the company responsible for the losses. Barnes v. Harris, 783 F.3d 1185, 1195 (10th Cir. 2015). As a result, the court concluded that the Bank was generally entitled to the refund since the Bank's 2010 loss was being offset by the Bank's 2008 income. UWBI only had title to the refund and was required to return it to the rightful owner.

The court noted that Bob Richards and Barnes both involved situations in which the parties had not entered into a TSA or other agreement. The court then analyzed the Agreement to determine if it affected the result.

The Agreement provided that the Bank was required to pay to UWBI each year an amount equal to the tax it would have incurred if it filed a separate return. If the Bank incurred an NOL, then the Bank was entitled to a refund from UWBI equal to the amount that it would have received if it had not joined the group. The amount of the refund was generally limited to any refund received from the IRS. However, UWBI had the discretion to pay a greater amount.

The Agreement supported the Bank's entitlement to the refund. If the Bank had filed a separate return, it would have received a refund from the IRS in an amount equal to the actual consolidated refund since the Bank's NOL was offsetting the Bank's taxable income from an earlier taxable year.

The court next considered whether the Bank was entitled to the refund under the Agreement under an agency or creditor relationship with UWBI. If neither entity was in bankruptcy or receivership, this would have been irrelevant. However, the relationship did become relevant as a result of the various proceedings. If the Bank was a mere creditor of UWBI, its claim would be just one of many against UWBI.

However, if UWBI was only holding the refund as an agent of the Bank, then the Bank would be entitled to the refund without regard to the rights of other parties.

The court noted that the Agreement was ambiguous with regard to the relationship issue. Certain provisions suggested an agency relationship. The court noted that the Agreement stated that (i) each party was to be treated as a separate taxpayer, and UWBI was only an intermediary between the party and the IRS, and (ii) UWBI was appointed by each party to act as its agent for purposes of filing a consolidated return (and actions connected therewith). On the other hand, UWBI appeared to generally be entitled to retain tax refunds and take them into account in settling obligations under the Agreement. In addition, the tax refunds did not need to be put in a trust or an escrow account on behalf of the real owner.

The court resolved the ambiguity regarding the relationship issue by looking to the terms of the Agreement itself regarding ambiguities. The Agreement stated that ambiguities were to be resolved in a manner that effectuated the intent of the Agreement (to provide for an equitable allocation of the group tax liability). Resolving the ambiguity in favor of an agency relationship allowed the Bank to receive the refund. The court effectively held that such an interpretation effectuated the intent of the Agreement since fairness would dictate the Bank was entitled to the refund under a Bob Richards analysis.

CONCLUSION

The totality of the cases described above are not always consistent with each other (either in terms of results or analysis). After 40 years and dozens of cases, it would seem that the law should be more developed than it is.

The cases are consistent in allowing a member of a consolidated group to receive a share of a consolidated tax refund where a subsidiary's losses are offsetting the same subsidiary's profits. However, the amount of the refund will generally be limited to the taxes previously paid by the subsidiary. It is very possible that this result will apply even if a TSA provides for a different result based on concepts of fairness and fiduciary duties.

The cases dealing with determining whether a subsidiary's losses offset the same subsidiary's profits all dealt with a simple situation of a consolidated group with limited members and only a single company with losses (in certain years) and profits (in other years). There is uncertainty as to how the courts would analyze a more complicated situation (e.g., hundreds of members and members with both income and losses in each year). It is possible that a court might apply reasonable TSA provisions as to how to perform the allocation or apply Section 1.1502-21(b) of the Treasury regulations, which provides for rules for allocations of consolidated NOLs for stock basis and other tax purposes.

Where the parties have adopted a formal TSA, it appears that the provisions will generally be respected except if the provisions are unfair or unreasonable. It is possible that a TSA will be more likely to be respected if third parties were involved in the negotiations (e.g., minority shareholders). A consistent course of conduct by the parties could be treated as a deemed TSA. Similarly, a written policy for allocating consolidated taxes and refunds that is consistently applied may very well be treated as a TSA. Whether a TSA exists or should be respected is likely to be analyzed under state corporate law.

In the absence of a formal or informal TSA, federal common law will generally apply. However, in the Sixth Circuit, state corporate law will apply. The problem is that federal common law has not been very well developed. Under federal common law, it appears clear that a subsidiary should receive its share of a consolidated refund if the subsidiary's income was offset by the same subsidiary's losses. However, there are no cases dealing with other fact patterns under federal common law. In such case, a court may have to fall back on state corporate law to resolve an issue (either directly or indirectly by analogy).

It also appears that NOLs of a subsidiary are entitled to some degree of protection (under corporate or bankruptcy law, if relevant). The degree of protection may depend upon such factors as (i) the ability of the subsidiary to benefit from the NOLs in the future and (ii) the hypothetical ability of the subsidiary to benefit from the NOLs if it had filed a separate tax return.

The courts have mentioned as a factor the fact that once a subsidiary consents to file a consolidated return it is bound to continue to do so. The inability of the subsidiary to revoke the consent may result in a loss of economic rights to contest what the parent does with a refund. However, the full extent of this loss of rights is not totally clear.

United Western Bancorp is an important case as it analyzed an ambiguous TSA. This should provide important assistance to those tax practitioners that are drafting TSAs in the future.

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