

The Moore Tax Case

The recent Supreme Court decision in the *Moore v. United States* case has stirred significant discussion within the realms of tax law and policy. The case challenged the constitutionality of the Mandatory Repatriation Tax (“MRT”), a provision of the 2017 Tax Cuts and Jobs Act (“TCJA”). On June 20, 2024, the Supreme Court issued its opinion that the MRT does not violate the Direct Tax Clause of the Constitution. This update discusses the basics of the background, arguments, and potential implications of this ruling.

Background of the Case

Charles and Kathleen Moore, the plaintiffs, owned shares in an Indian agricultural equipment company. Despite not receiving any dividends or income from their investment, they were required to pay approximately \$15,000 under the MRT, which taxes U.S. shareholders on the undistributed earnings of foreign corporations. More specifically, the MRT required, under Section 965 of the Internal Revenue Code, that U.S. shareholders owning 10% by vote or value of certain “controlled foreign corporations” (“CFC’s”) pay a one-time transition tax on a deemed

repatriation of certain realized but undistributed income of the CFC that would not otherwise have been subject to current taxation under the prior existing rules for CFC's. The Moores argued that this tax was unconstitutional, claiming it violated the Sixteenth Amendment, which they contended only allows Congress to tax realized income, and asserting that no income had been realized.

The MRT was designed to target certain U.S. shareholders currently deferring taxes on the undistributed earnings of CFC's not currently taxed under the Subpart F rules. By taxing these undistributed earnings, Congress aimed, arguably, to prevent tax avoidance and ensure that U.S. shareholders pay taxes on their global income. Alternatively, the rule simply incentivized/forced U.S. shareholders of CFC's to accelerate repatriation of certain non-Subpart F earnings, creating a one-time boost of current year tax revenues (but reducing future tax revenues).

The Supreme Court's Decision

In a 7-2 decision, the Supreme Court upheld the constitutionality of the MRT. Justice Brett Kavanaugh, writing for the majority, asserted that the MRT does not exceed Congress's authority under the Constitution. The Court emphasized that Congress has long treated certain entities, like partnerships and S corporations, as pass-throughs for tax purposes, attributing their undistributed income to shareholders or partners, who are then taxed on that income. The Court also noted that the principle has repeatedly been invoked by courts in upholding the general Subpart F taxation rules applicable to CFC's.

Justice Kavanaugh noted that the decision was narrow and did not address broader issues related to potential wealth taxes. The Court's ruling was specific to the taxation of undistributed income realized by pass-through entities and did not extend to hypothetical scenarios involving both entity and shareholder taxation.

Implications of the Ruling

The Supreme Court's decision has significant implications for U.S. tax policy:

Validation of the MRT: The ruling confirms that Congress has the authority to tax the undistributed earnings of foreign corporations owned by U.S. shareholders. This reinforces the government's ability to tax offshore earnings through anti-deferral and deemed repatriation rules.

Impact on Wealth Taxes: Although the Court did not directly address the constitutionality of wealth taxes, the decision may influence future legal challenges. The Court's emphasis on realized income suggests that taxes on unrealized gains might face constitutional scrutiny. This is particularly relevant as lawmakers propose new taxes targeting the wealth of high-net-worth individuals.

Clarification of the Sixteenth Amendment: The ruling provides at least some additional clarity on the interpretation of the Sixteenth Amendment concerning what constitutes taxable

income. By upholding the MRT, the Court has indicated that income does not necessarily have to be realized in the traditional sense to be subject to federal taxation.

Precedent for Future Cases: The decision sets a precedent for future cases involving the taxation of foreign earnings and the broader application of the Sixteenth Amendment. It underscores the Court's willingness to uphold complex tax provisions designed to target tax deferral.

Conclusion

The *Moore v. United States* case represents a pivotal moment in U.S. tax law, reaffirming Congress's power to tax U.S. shareholders on undistributed earnings of foreign entities and setting the stage for future debates on wealth taxation. The Supreme Court's narrow yet impactful ruling highlights the ongoing evolution of tax policy in international contexts. As lawmakers and policymakers navigate these issues, the principles touched upon in this case will undoubtedly play a critical role in shaping the future of U.S. taxation.

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