



Dealing with the Demise of the Bob Richards Rule

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In an opinion with far-reaching implications for the business community and tax professionals, the U.S. Supreme Court recently struck down the nearly five-decades-old “Bob Richards rule” as an invalid exercise of federal common law.

At issue in the case – *Simon E. Rodriguez, as Chapter 7 Trustee for the Bankruptcy Estate of United Western Bancorp, Inc. v. Federal Deposit Insurance Corporation, as Receiver for United Western Bank* – was the “Bob Richards rule,” under which a tax refund paid to an affiliated group of corporations is presumed to belong to the subsidiary whose losses gave rise to the refund unless the parties clearly agree otherwise.

Rodriguez was represented by [Mark E. Haynes](#) of Ireland Stapleton Pryor & Pascoe in the U.S. District Court for the District of Colorado, the U.S. Bankruptcy Court for the District of Colorado, the U.S. Court of Appeals for the Tenth Circuit, and the U.S. Supreme Court. Rodriguez was also represented by Neal Kumar Katyal, Mitchell P. Reich, and Colleen E. Roh Sinzdak of Hogan Lovells in the U.S. Supreme Court.

Three circuit courts had adopted the rule while four other circuits had rejected it, and instead relied on state law to determine ownership of a tax refund.

The Internal Revenue Code allows companies in an “affiliated group” to file consolidated tax returns. With the abolition of the “Bob Richards rule” it will become more important for members of these groups to enter into written tax allocation agreements on the advice of professionals to see that their interests are implemented as to payment of tax and allocation of refunds.

Procedural History

The Rodriguez case involved United Western Bank. After the financial institution suffered huge losses, its parent, United Western Bancorp, Inc., declared bankruptcy. When the Internal Revenue Service (IRS) issued the group a \$4 million tax refund, both the bank’s receiver, the Federal Deposit Insurance Corporation (FDIC), and the parent corporation’s bankruptcy trustee, Simon Rodriguez, sought to claim the funds.

The U.S. Bankruptcy Court for the District of Colorado in 2016 granted summary judgment to the trustee, relying on Colorado common law. However, the U.S. District Court for the District of Colorado in 2017 reversed the decision the following year. Unlike the Bankruptcy Court, the District Court determined that its analysis was governed by the Bob Richards rule.

On appeal, the [Tenth Circuit affirmed the District Court’s ruling](#) in 2019 by applying the Bob Richards rule and deciding in favor of the FDIC. The trustee filed a petition for certiorari to the Supreme

Court, which struck down the rule on Feb. 25, 2020, and remanded the case back to the Tenth Circuit to make a determination without relying on the Bob Richards rule.

The [historic opinion](#) resolves a split in the circuit courts and has ramifications that extend beyond bankruptcy cases or the banking industry. Thousands of companies could be affected by this decision. It “is particularly significant for the entire area of how tax refunds are handled when you have an affiliated group of corporations filing a consolidated tax return,” said business litigation attorney Mark Haynes, a director at Ireland Stapleton who worked on the case on behalf of the Chapter 7 trustee.

A Unanimous Repudiation of the Rule

In the 9 – 0 Supreme Court ruling written by Associate Justice Neil Gorsuch, he pointed out that the IRS has allowed an affiliated group of corporations to file a consolidated federal return as long as they comply with a long list of regulations. While those regulations describe how the IRS will pay the group’s agent a single refund, they don’t explain how the refund should be distributed among the corporate members.

Consequently, many corporations have developed tax allocation agreements that specify what share of a group’s tax liability each member will pay, along with the share of any tax refund each member will receive, Justice Gorsuch wrote. In the absence of such an agreement or a dispute over its terms, courts would rely on state laws used for interpreting contracts, creating equitable trusts, or avoiding unjust enrichment, among other issues.

However, some federal courts created their own federal common law rule – the Bob Richards rule – that arose from a case decided in 1973 by the Ninth Circuit case: *In re Bob Richards Chrysler-Plymouth Corp.* The Bob Richards rule provided that, in the absence of a tax allocation agreement, a tax refund belongs to the group member responsible for the losses that led to it. But

over the years, it grew into a general rule always to be followed unless the tax allocation agreement unambiguously specified a different result.

Citing its 1938 *Erie R. Co. v. Tompkins* decision, the high court reiterated its view that there is “no federal general common law,” except in a few limited areas since rulemaking is the domain of the legislative branch. Stringent conditions must be met before federal judges can engage in such rulemaking, the high court said. One of those conditions is a “uniquely federal interest,” which the Supreme Court did not find in *Rodriguez*.

For business litigators, this opinion has made it clear that courts will be fairly restrictive in permitting the creation and enforcement of federal common law rules and will be more deferential to state laws. “In totally unrelated fields of federal common law, this decision is going to be very, very relevant,” Haynes said.

Just as significant is the certainty that this opinion affords businesses and creditors. They no longer must determine whether the Bob Richards rule applies. Instead, they have to turn to the terms of their tax allocation agreement, without worrying about this judge-created rule.

Tax Allocation Agreements Take on Greater Importance

While the opinion provides more certainty in one sense, it also increases the importance of having a well-constructed tax allocation agreement in place. Federal law no longer is going to provide a default interpretation for these pacts.

When drawing up these contracts between holding companies and their subsidiaries, attorneys and accountants should pay even closer attention to each party’s intent when it comes to tax payments and refunds because these agreements will govern in those situations.

Nobody expects to go into bankruptcy. Nevertheless, businesses should create tax allocation agreements that specify how tax refunds would be handled in such a situation.

For more information on how this court opinion may impact your business directly, contact Director Mark E. Haynes at 303.628.3609 or mhaynes@irelandstapleton.com.

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