



The Andrews Kurth
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January 21-24, 2015

2015
Competition
Problem

ROYAL HARKONNEN OIL COMPANY, Petitioner

v.

UNITED STATES, Respondent

**IN THE
SUPREME COURT
OF THE UNITED STATES**

No. C15-1701-1

OCTOBER TERM 2014

***ROYAL HARKONNEN OIL COMPANY*, Petitioner**

v.

***UNITED STATES*, Respondent**

ORDER GRANTING WRIT OF CERTIORARI

PER CURIAM:

The petition for a writ of certiorari to the United States Court of Appeals for the Fourteenth Circuit is hereby granted.

IT IS ORDERED that the above-captioned matter be set down for argument in the 2015 term of this Court, said argument to be limited to the following issues:

- I. Is Harkonnen Oil's payment of taxes to the Republic of Arrakis a creditable foreign tax credit under 26 U.S.C. § 901 or 26 U.S.C. § 903?
- II. Did the IRS properly deny Harkonnen Oil's claimed foreign tax credit for all tax payments to Inter-Sietch Fremen Independence League?

**Discussion of the above issues should not include any analysis of the Foreign Corrupt Practices Act.

**UNITED STATES COURT OF APPEALS
FOR THE FOURTEENTH CIRCUIT**

**ROYAL HARKONNEN OIL
COMPANY**

Petitioner

v.

UNITED STATES

Respondent

Case No. 15-1701

Decided October 1, 2014

Before Judges Wright, Herbert, and Layton.

Wright, Circuit Judge, for the Court.

Petitioner, Royal Harkonnen Oil Company, files this appeal from the denial of a tax refund entered by the United States District Court for the Central District of New Texas in favor of respondent, the United States. For the reasons stated below, we affirm.

I. BACKGROUND FACTS

A. Royal Harkonnen Oil Company and the Republic of Arrakis

1. On March 6, 2007, Royal Harkonnen Oil Company (“Harkonnen Oil”)¹ engaged in a seismic and feasibility study of the Caladan Oil Field² in order to determine its capacity and the profitability of extracting its oil and natural gas deposits. Harkonnen Oil completed its seismic and feasibility study on October 19, 2007. Ultimately, Harkonnen Oil

¹ Harkonnen Oil is a Delaware corporation with its principal place of business in New Texas.

² The Caladan Oil Field rests entirely within the northern and eastern boundaries of the Republic of Arrakis.

concluded that the Caladan Oil Field covers approximately 231,000 square miles (containing 150 billion BOE)³ and that oil and gas reserves could be profitably extracted by utilizing new technologies and recovery techniques.

2. In a separate internal document labeled “CEO Summary: Caladan Oil Field,” Harkonnen Oil expressed concern with potential negotiations between Harkonnen Oil and the president of the Republic of Arrakis (“Arrakis”), Jules Corrino (“President Corrino”).⁴ Specifically, Harkonnen oil feared that President Corrino would demand a high royalty payment for any production within the Caladan Oil Field because (1) President Corrino’s family owns all mineral rights in Arrakis, (2) President Corrino rose to his position of authority through a defacto election/inheritance, and (3) in Arrakis, the acting President holds his position for life and therefore has questionable concern for the needs of the people. Given that a Harkonnen Oil’s seismic and feasibility study showed that a high royalty would render mineral extraction in the Caladan Oil Field unprofitable, the company considered, as an alternative, development of a smaller reservoir located entirely within Arrakis’ neighboring countries, Al Dhanab and Anbus.

3. On February 5, 2008, Harkonnen Oil began negotiations with Arrakis for the exclusive rights to develop the Caladan Oil Field. Harkonnen Oil’s CEO Vladimir Harkonnen met with President Corrino and other delegates from Arrakis in order to sign and approve an

³ BOE stands for “barrel of oil equivalent” – a measure used to aggregate oil and gas resources or production. One BOE equals approximately 6,000 cubic feet of natural gas, and the unit is used by oil and gas companies in their financial statements as a way of combining oil and natural gas reserves and production into a single measure.

⁴ President Corrino is also the Emperor of the United Thrones of the Sietch Empire and the Eternal Arrakis Empire. This hereditary and ceremonial title was created in 1864, when the Eternal Arrakis Empire (a then French Protectorate) conquered the Sietch Empire during what is locally known as the “Bloody Ten Year War.” The combined entity became the Republic of Arrakis in 1952 through a proclamation by President Corino’s grandfather and sitting Emperor. Prior to the Bloody Ten Year War, the Seitch Empire and the Eternal Arrakis Empire tolerated 1,564 years of unstable peace based on mutually beneficial economic trade mixed with frequent military conflicts caused by significant religious differences.

oil and gas lease covering the entire Caladan Oil Field. As predicted by Harkonnen Oil, the negotiations largely focused on various royalty payments demanded by President Corrino. Negotiations took place of several months.

4. While the negotiations were taking place, the Arrakis media started covering stories about the tax implications related foreign companies doing business in Arrakis. Arrakis tax law is largely based on historical religious norms that have been codified over a period of hundreds of years. Because the Arrakis Tax Code arose during a hereditary monarchy, a person or other entity was only subject to the tax code if their bloodlines were historically subjects under either the Arrakis or Sietch Thrones. Any person or entity not subject to the tax code would not be provided any protections under the law.⁵ In modern practice, such precedent resulted in an Arrakis Tax Code that applied to Arrakis citizens but rejected taxation of income earned by foreign individuals or entities residing or doing business in Arrakis.⁶ The tax rate of Arrakis citizens is based on whether individuals historically would have been subjects of the Sietch throne or the Arrakis throne. Those who would have been subjects of the Arrakis throne received a five percent lower tax rate than those citizens with historical ties to the Sietch thrones. Over time, several robust tax deductions⁷ appeared throughout the Arrakis Tax Code allowing Arrakis citizens to mitigate their tax burdens. Like the remainder of the Arrakis Tax Code, these deductions did not apply to any costs, fees, or royalties demanded of foreign individuals or entities.

⁵ On December 28, 2006, Arrakis passed the Foreign Protection Act, which provided limited police protection and due process rights to foreign individuals or entities residing or operating in Arrakis.

⁶ The highest court in the Republic of Arrakis, The Holy Royal Court, recently ruled on this issue in *Lord Remington v. Republic of Arrakis* and stated that foreign citizens and entities were not entitled to protection beyond the Foreign Protection Act, and therefore, could not be taxed.

⁷ The United States Internal Revenue Service stipulates that these deductions match available deductions under the United States Tax Code.

5. Within the previous five years President Corrino, attempted to modernize the tax code in order to comport with new international treaties and obligations. On March 10, 2008, President Corrino drafted and signed into law a new tax labeled “Republic of Arrakis Foreign Value Tax”.⁸ The Republic of Arrakis Foreign Value Tax applied to all foreign entities that operate machinery on sovereign territory of Arrakis. The tax is determined by calculating the gross receipts generated by a corporation’s operations occurring in Arrakis during the current calendar year then multiplying that amount by a tax percentage. The Republic of Arrakis Foreign Value Tax deferred designation of the exact tax percentage rate to an unspecified later date.

6. The Republic of Arrakis Foreign Value Tax tasked the Central Bank of Arrakas with calculating all applicable taxes. To ensure proper enforcement, The Republic of Arrakis Foreign Value Tax further required the deposit of all monies earned in Arrakis into the Central Bank of Arrakis prior to disbursement to the foreign entity. Once applicable funds were deposited with The Arrakis Central Bank, it would distribute all taxed funds directly to the Arrakis Treasury and issue remaining funds to the foreign entity. This disbursement process is to be completed within ninety days of each deposit.

7. On April 12, 2008, Arrakis mobilized its military into Arrakis’ northern region – commonly known as the Sietch Dunes – in order to silence the uprising. The goals of the rebellion were published in a local Arrakisian newspaper. Through the media, the dissidents declared independence of the Sietch Dunes area from Arrakis and a restoration of an

⁸ The President under the constitution of the Republic of Arrakis is allowed the right to enact one new tax every year.

independent Sietch Throne. The Sietch Dunes region declared independent by dissidents included a 62,000 square mile portion of the Caladan Oil Field.

8. During the Arrakis military mobilization, the U.S. State Department declared that it would monitor the situation in the Sietch Dunes and would pay particular attention to any atrocities committed. Such a position is important because Arrakis never ratified the Geneva Convention and its military has historically refused to provide quarter to prisoners during military campaigns. Instead, the Arrakis military historically executed all enemy combatants upon capture.

9. Initial fighting between Arrakis and the Sietch Dunes dissidents occurred along the fringes of the Sietch Dunes, where the Arrakis Military scored four quick victories. These victories led to an Arrakis blockade of all supply routes to the Sietch Dunes. During these initial confrontations, Arrakis casualties numbered 134 individuals compared to 15,000 Sietch Dune casualties.

10. Concerned about the possibility that the U.S. State Department would condemn the actions as a potential human rights violation, Mr. Harkonnen sent an email to President Corrino requesting clarification of the situation on April 15, 2008. In response, President Corrino stated that the international media exaggerated the conflict. President Corrino clarified that the conflict only involved a small group of dissidents upset about Arrakis' 1864 "annexation" of the Sietch Empire. President Corrino further stated that military action would finish within a month and there was no need to worry about any negative action by the U.S. State Department.

11. On April 26, 2008, Mr. Harkonnen flew into the Sietch Dunes area for a previously planned vacation.⁹ Mr. Harkonnen was interested in exploring the ancient Sietch Ruins¹⁰ located throughout the contested Sietch Dunes area. The expedition to the ruins was led by local guide Paul Atreides. Following Mr. Harkonnen's vacation, he arranged a face-to-face meeting with President Corrino on April 29, 2008, for a planned meeting about the proposed Caladan Oil Field lease with Harkonnen Oil.

12. On May 11, 2008, Arrakis withdrew its military from the Sietch Dunes. Simultaneously, the U.S. State Department reiterated its human rights concerns about the Arrakisian military activities. On May 12, 2008, the United Nations launched an investigation of the Arrakisian military actions in the Sietch Dunes, including the use of aggressive interrogation techniques. The United Nations never finalized a report.

13. On June 30, 2008, President Corrino applied a forty-five percent tax rate to the Republic of Arrakis Foreign Value Tax, and renamed the tax the "Republic of Arrakis Foreign Tax." The same day, Arrakis and Harkonnen Oil signed a lease ("Arrakis Lease") to develop the entire 231,000 square miles of the Caladan Oil Field. The Arrakis Lease contains provisions for a one-time bonus payment of fifty-five million dollars and a royalty of fifteen percent. Additionally, Harkonnen Oil agreed to pay the March 10, 2008 tax. Harkonnen Oil paid no other tax to Arrakis from 2008 to the present.

14. On January 15, 2009, Harkonnen Oil produced the first barrels of crude oil under the Lease. By October 30, 2009, daily production equaled 858,000 barrels of oil per day.

⁹ The vacation was booked in late 2007.

¹⁰ The Ruins of the Seitch Dunes have long been a fascination and wonder of the world. There has been a movie series about an archeologist who escaped the legendary traps of the ruins. Historically, most of the ruins were explored and plundered between 1910-1930.

On November 2, 2009, Harkonnen Oil began production on the portion of the Caladan Oil Field located under the Sietch Dunes.

B. Harkonnen Oil Company and the Sietch State

15. On March 20, 2010, a holy day for the native populace of the Sietch Dunes, a group calling themselves the Independent People of Sietch (“IPS”) declared their independence from Arrakis and declared the IPS to be the controlling political regime of an independent Sietch Dunes.¹¹ On March 21, 2010, against international outcry, Arrakis again mobilized its military to the Sietch Dunes in order to suppress the uprising. The United Nations condemned the actions of Arrakis. The U.S. State Department declared Arrakis a “Dangerous State” and withdrew its embassy from Arrakeen, the capital and largest city of Arrakis.

16. During the weeks of fighting that followed, reports indicated that forces for the IPS sustained roughly thirty-five thousand casualties and Arrakis sustained roughly four thousand casualties. On April 9, 2010, Mr. Harkonnen, along with the United States Ambassador to Arrakis, met in Arrakeen with President Corrino and Paul Atreides (the newly appointed leader of the IPS), at a conference known as the Arrakeen Peace Summit. A ceasefire was declared and President Corrino personally guaranteed the safety of all parties involved in negotiations. The Arrakeen Peace Summit continued for three days and on April 12, 2010, the parties announced a truce.

17. The truce, known as the “Sietch Dunes Peace Treaty,” stated that the Sietch Dunes region would become Sietch State and be designated an Important Province of Arrakis. The newly created Sietch State would alone appoint the Arrakis Vice-President who would

¹¹ This uprising is separate and distinct from the uprising referenced on Page 5, Paragraph 7. Both uprisings occurred in the same region.

serve in the cabinet of the President. Additionally, Sietch State agreed to send monetary tribute to the Republic of Arrakis and agreed to never seek independence again. Lastly, the IPS would become a recognized political party of Sietch State.

18. Following the signing of the Sietch Dunes Peace Treaty, President Corrino drafted an amendment to the Arrakis Constitution creating the post of Vice-President. The amendment further stated that the position could only be held by a member of the Sietch bloodline as determined by the Minister of Medicine of Arrakis. The amendment went into effect on April 13, 2010. The amendment also included a listing of powers and requirements for the Vice-President as follows:

1. Responsibility for maintaining the Sietch Dunes Peace Treaty.
2. The power to create and enforce laws in the Sietch State only as to (1) policing the State and (2) collecting the State tribute for Arrakis.
3. The power to appoint a limited council of ten individuals (“Sietch Council”) necessary to regulate the Sietch State, including conducting all judicial functions. Appointments last one year.
4. Decree and levy a single tax and have the power to amend the tax with the approval of the sitting President of Arrakis.
5. While serving, the Vice-President must live in Arrakeen.
6. All State policies must be accepted by the sitting Arrakis President before enactment.

The amendment also limited the Vice President’s term of office to one year, with elections to take place on April 15 from among eligible citizens.

19. On April 15, 2010, Paul Atreides was declared Vice-President of the Sietch State following a procedurally questionable and hurried vote. The overwhelming majority of the votes counted came from the IPS political party. Further, only those able to prove a connection to Sietch bloodlines were eligible to vote. All votes from other individuals residing

in the Sietch State were voided. The reports from voters within the Sietch State drew attention from United States, Russian, and French officials who investigated the allegations of voter fraud.

20. On April 16, 2010, as his first official act, Vice-President Atreides decreed a single tax under the fourth provision of his Vice-President Powers. According to the decree, ten percent of all income generated in the Sietch State (regardless of citizenship) less any applicable deductions¹² must be turned over to the Chief Accountant of the Sietch State. All taxes collected by Sietch were to be paid as tribute to Arrakis. At all relevant times, Harkonnen Oil paid funds owed under the April 16, 2010 decree to the Sietch State. Importantly, the April 16, 2010 decree did not impact any payments owed by Harkonnen Oil to Arrakis under the Republic of Arrakis Foreign Tax.

21. On April 19, 2010, Harkonnen Oil sent an oil and gas lease to Vice-President Atreides, as head of the Sietch State (“Sietch Lease”). On April 21, 2010, the parties executed the Sietch Lease. As part of the Sietch Lease, Harkonnen Oil paid the Sietch State a one-time bonus payment of five million dollars and an annual royalty of five percent.

22. On June 30, 2010, the United States, Russian, and French Officials declared the Sietch State Vice-Presidential election results questionable, with large reports of irregularities, but recommend no sanctions. On July 6, 2010, the U.S. State Department undesignated Arrakis as a “Dangerous State” and declared the Sietch State, “A Quasi-Autonomous Region.” The U.S. State Department agreed to establish diplomatic ties with the Sietch State. A temporary one room consulate was established within the U.S. embassy located in Arrakeen

¹² The Sietch state adopted all deductions available under the Arrakis Tax Code, but applied the deductions to all income generating entities (regardless of citizenship) residing or doing business in the Seitch State.

until a permeant location could be finalized. The U.S. Treasury Department declared that it would accept transactions from the Sietch State.

23. On July 9, 2010, the President of the General Assembly of the United Nations stated that he was prepared to push for select leadership from the Republic of Arrakis to be indicted by to the International Criminal Court for suspected war crimes orchestrated by Arrakis during the 2010 uprising. President Corrino declared the United Nations a sham organization and denied that it had any authority over the intra-border policies in Arrakis. The next day Arrakis made a multi-million dollar donation to the United Nations Refugee Agency. To date, no charges have been brought against President Corrino or any other member of the Arrakisian government or military.

C. Harkonnen Oil and the Inter-Sietch Fremen Independence League

24. On December 31, 2010, a group called the Inter-Sietch Fremen Independence League (“IFIL”) launched a rebellion in the Sietch State. They demanded Paul Atreides’s resignation as Vice-President and declared their leader, Jessica Mohiam, as the rightful heir of the historic Sietch Throne and, therefore, the only legitimate Vice-President.

25. IFIL has been classified by the U.S. State Department as an independent splinter group of the Bene Gesserit, a terrorist organization that operates in the countries surrounding Arrakis. The Bene Gesserit has been properly labeled as a terrorist organization by the U. S. State Department and the U.S. Treasury. Jessica Mohiam’s mother was a founder of the Bene Gesserit and as a result, she has been associated with the organization from birth. However, upon reaching eighteen years old on March 20, 2005, Ms. Mohiam began actively rebelling against her mother and the Bene Gesserit. Ms. Mohiam declared the Bene Gesserit an archaic organization with fundamentalist beliefs that have no place in a modern world.

Since March 20, 2005, Ms. Mohiam has lived outside the Bene Gesserit stronghold located within the country of Salusa Secundus.

26. Salusa Secundus is one of the northern neighbors of Arrakis. In December of 2007, Jessica Mohiam found support in Al Dhanab and Anbus, two countries that share a border with both Arrakis and Salusa Secundus. She received financial backing from the monarchies in both countries and has claimed that in return for the funding, she would promote economic development in any country where Sietchians historically reside (including Al Dhanab and Anbus) and would oppose the Bene Gesserit. From 2008 to the present, IFIL has operated throughout the region, moving from place to place.

27. The IFIL governing structure rests solely with a single Leader Elect. That leader is chosen through seven electoral votes distributed as follows:

- Three electoral votes are granted to the Al Dhanab royal family
- Three electoral votes are granted to the Anbus royal family
- One electoral vote is submitted by a majority election among all individuals pledging membership with IFIL

A person must receive five electorate votes to gain the title of Leader Elect. Elections are held annually at a general IFIL directorate meeting. Since the inception of IFIL in 2008, Jessica Mohiam has received all seven electorate votes in each election.

28. On January 2, 2011, IFIL was recognized as a legitimate foreign government by Al Dhanab and Anbus. Both countries declared IFIL as an independent state of the Sietch Dunes region. Al Dhanab and Anbus jointly petitioned the United States and United Nations for recognition of IFIL. Subsequently, the United States and United Nations agreed to look at

the matter for a determination. France and Russia immediately recognized the legitimacy of IFIL as a state within the Sietch Dunes region.

29. By March 2011, IFIL forcefully acquired control of a region of the Seitch State known as the “Badlands.” Following the concentration of IFIL in the Badlands, Arrakis and the Sietch State did not engage the organization in any military or police actions, other than to issue denials of their legitimacy. The Bene Gesserit immediately issued a statement published in newspapers around the globe that, “Jessica Mohiam is not a legitimate heir to the Ancient Sietch Throne, she is a heretic who is only concerned with profit, and is a puppet of the Al Dhanab and Anbus monarchies whom she pays for legitimacy.” The Bene Gesserit routinely disseminates information labeling Ms. Mohiam a “Profiteer” and “Capitalist Swine.”

30. On March 20, 2011, IFIL expanded beyond the “Badlands” and forcefully took control of a small drilling station identified as Unit #12 operated by Harkonnen Oil. Simultaneously, Ms. Mohiam released a recorded statement claiming that “Harkonnen Oil is slant drilling the Badlands and until they rectify their insolence and pay tribute, IFIL will control oil production from Unit #12. Unit #12 is located near a collection of ruins dating back to the Sietch Empire and labeled on maps as “Onn,” historically the seat of the Sietch Empire throne.

31. On March 22, 2011, Mr. Harkonnen flew to Unit #12 and met with Ms. Mohiam. They signed a handwritten oil and gas lease stating that Harkonnen Oil would pay a bonus of five hundred and fifty thousand dollars and a five percent royalty to IFIL (“IFIL Lease”). Ms. Mohiam then further declared that Unit #12 would have its income taxed at two percent. This tax is calculated by taking the receipts generated by Unit #12 and allowing for all deductions authorized by the Sietch State and then multiplying that by two percent. Mr.

Harkonnen protested the tax demand and left the negotiation. That afternoon, Mr. Harkonnen telephoned President Corrino and asked how he should handle IFIL's tax request. President Corrino stated that all legal tax disputes in Arrakis are handled by the Holy Royal Court of Arrakis.

32. On March 23, 2011, Harkonnen Oil petitioned the Holy Royal Court of Arrakis for a determination of the status of IFIL and its ability to levy a tax. On March 24, 2011, the Holy Royal Court declared, "Arrakis recognizes IFIL as a part of Sietch." Additionally, on this same day, Arrakis, Al Dhanab, and Anbus jointly executed a Free Trade Agreement and Mutual Defense Pact to increase regional economic trade.

33. On March 25, 2011, Harkonnen Oil paid IFIL the negotiated bonus and royalty amount. By separate check, Harkonnen Oil then paid IFIL the two percent tax indicating on the memo line, "Income Tax to IFIL" All of the checks and funds were deposited in a Swiss bank account, set up for IFIL by the heir to the throne of Anbus, Prince Dalamak. Ms. Mohiam paid twenty percent of the funds IFIL received from Harkonnen Oil to the monarchies of Al Dhanab and Anbus.

34. On April 15, 2011, the Sietch State held its second election and Paul Atreides and Jessica Mohiam finished in a "virtual tie." The election was supervised by the United States. On April 16, 2011, President Corrino declared Paul Atreides the winner as part of "the rights of the sitting President of the Republic of Arrakis." The United States declared the election over, but did not certify the results. The President of the United States issued Executive Order 14012 declaring "IFIL a sovereign friend of the United States, whom we would like to establish trade relations with." Executive Order 14012 also stated that "the United States would always continue to help individuals around the world obtain freedom."

D. First Annual Caladan Oil Field Conference

35. On May 16, 2011, Mr. Harkonnen, President Corrino, Vice-President Paul Atreides, and the Leader Elect of IFIL (and Vice-President-in-Protest) Jessica Mohiam met in the First Annual Caladan Oil Field Conference. The conference included private meetings, presentations of new technologies, reports on production, forecasting reports, and a lavish banquet. Following the three day conference, Vice-President Paul Atreides declared that the new tax rate to be paid by foreign companies operating on portions of the Caladan Field within the Sietch State would remain at ten percent of all monies generated within the State less applicable deductions. President Corrino lowered the Republic of Arrakis Foreign Tax to thirty-three percent. Leader Elect of IFIL (and Vice-President-in-Protest) Mohiam declared that IFIL's tax of Unit #12 would remain the same. Ms. Mohiam also stated that all payments required for "slant" drilling operations had been satisfied by Harkonnen Oil. Additionally, the Arrakis and the Sietch State agreed to consider establishing a permanent principal location for IFIL within the Sietch Dunes region, as no location had yet been agreed upon. Ms. Mohiam has repeatedly declared Onn to be her headquarters. Arrakis and the Sietch State remained silent about the status of Onn as the headquarters/principal location of IFIL

36. Following the conference, President Corrino issued Proclamation 102 stating that foreign corporations would be allowed to take all tax deductions available to Arrakis citizens. However, all deductions claimed by a foreign corporation would be capped at ninety-five percent of the dollar value of an Arrakisian citizen.¹³ Under the religious laws and practices of Arrakis, a foreign entity cannot have the same benefits as a true believer. The

¹³ For example. If a foreign entity and an Arrakisian citizen each calculated \$100 in deductions under the Arrakis Tax Code, the foreign entity could rightfully claim a \$95.00 deduction while the Arrakis citizen could rightfully claim the entire \$100.00 deduction.

religious head of Arrakis (and President Corrino's brother), High Priest Victor Corrino, blessed the new tax law as holy. Proclamation 102 did not affect the calculation of tax deductions by the Sietch State because applicable Sietch religion does not promote economic sanctions against "non-believers".¹⁴

37. Harkonnen Oil production of the Caladan Oil Field continued unhindered for the remainder of the year as Harkonnen Oil timely paid (1) the thirty-three percent tax less applicable deductions from total income generated by the Caladan Oil Field to Arrakis, (2) the ten percent tax less applicable deductions to the Sietch State for the income generated by the portion of the Cladan Oil Field resting beneath the Sietch Dunes, and (3) the two percent tax to IFIL for income generated by Unit #12.

E. Underlying Tax Suit

38. On March 15, 2012, Harkonnen Oil filed its Form 1120 United States Tax Return for the year 2011. Harkonnen Oil then timely filed Form 1118 claiming foreign tax credits for its tax payment to the Republic of Arrakis, the Sietch State, and IFIL. Prior to tax year 2011, Harkonnen Oil took its expenses from its Arrakis operations as a deduction and not as a credit.

39. The Internal Revenue Service (IRS) flagged Harkonnen Oil's 2012 tax returns¹⁵ for irregularities and proceeded to perform an audit. Upon concluding the audit, the IRS determined that the claimed foreign tax credits sought for the tax payment to Arrakis did not qualify as a credible foreign tax credit under the United States Tax Code. Instead, the IRS determined that Harkonnen Oil's tax payment to Arrakis constituted an unqualified foreign tax

¹⁴ Scholars believe this point caused the split between the faith of Arrakis and the faith of Seitch around the year, 439 A.D.

¹⁵ Harkonnen Oil is a calendar year company.

credit because the foreign tax failed to sufficiently reach net income. The IRS deemed the Harkonnen Oil's payments to the Sietch State qualified as a valid foreign tax credit. Further, the IRS determined that Harkonnen Oil's tax payments to IFIL constituted an unqualified foreign tax because IFIL was not a proper taxing authority. The IRS also declared that Harkonnen Oil's payments to IFIL violated the Sietch Dunes Peace Treaty's limitation of a single tax within the Sietch State. Finally, the IRS declared that Harkonnen Oil failed to exhaust all of its remedies to challenge a foreign tax under Sietch's domestic law.

40. After failed negotiations with the IRS, Harkonnen Oil paid the full tax (including applicable penalties and interest) and demanded a refund. Harkonnen Oil then filed suit in the Central District Court of New Tejas. After a lengthy and well publicized trial, the District Court Judge ruled in favor of the United States.

II. DISCUSSION

41. In an international tax case such as this one, we do well to start with the basics. The most basic step is to find the appropriate statute and determine its applicability. The first issue before us is whether or not payments to Arrakis are eligible foreign tax credits. Based on research and the briefs submitted, this is a question of interpretation under 26 U.S.C. §§ 901 and 903. We find the Arrakis tax is not a credible foreign tax credit because the "Republic of Arrakis Foreign Tax" is a tax that is not similar or akin to a United States Income Tax. First, the tax was named a value tax, with only the name of the tax being changed at later date (as opposed to substance of the levy). Further, payments do not qualify as an income tax if the payment does not credibly reach net income. See *Inland Steel Co. v. United States*, 677 F.2d 72, 80 (Ct. Cl. 1982). Finally, we find that Arrakis' cap on foreign corporation tax deductions fails to satisfy the definition of "significant cost recoveries" under 26 CFR 1.901-2.

42. We also find that 26 U.S.C § 903 does not afford relief to Harkonnen Oil because Arrakis' tax is not "in-lieu of" an otherwise applicable income tax. Similarly, The Central Bank of Arrakis' practice of holding funds prior to remittance does qualify as a "withholding tax" sufficient to generate a 26 U.S.C. § 903 foreign. We see no reason to move past the form of the Arrakis tax to find that 26 U.S.C. § 903 does not apply.

43. The second issue before us is whether the IRS properly denied Harkonnen Oil's claimed foreign tax credit for all tax payments to IFIL. We determine that the IRS acted properly on two independent grounds. First, the IRS properly denied the foreign tax credit on payments to IFIL because IFIL is not a valid taxable entity. While on its face, it appears that IFIL is a valid foreign entity based on Executive Order 14012 and a ruling by the Holy Royal Court, neither of these facts establish IFIL to be a sovereign political entity within the Sietch State. Further, we find the tax in violation of the Arrakis Constitution because the Arrakis Constitution only permits the Sietch State to have territorial taxing authority over a single tax within the Sietch State. Under such a constitutional provision, the tax by IFIL is an impermissible second tax. Lastly, we agree that Harkonnen Oil could have petitioned the Sietch Council for a determination on the status of IFIL and, therefore, did not exhaust all of its available remedies to reduce the IFIL tax burden. Here IFIL was not a proper taxing authority, the tax they applied was unconstitutional under Sietch Dunes Peace Treaty, and Harkonnen Oil failed to exhaust all of its remedies under a foreign jurisdiction's law. As such the payments to IFIL do not constitute a credible foreign tax credit.

III. CONCLUSION

44. In conclusion, we hold that Harkonnen Oil's payment of taxes to the Republic of Arrakis is not a creditable foreign tax credit under 26 U.S.C. § 901 or 26 U.S.C. § 903. We also hold that the IRS properly denied Harkonnen Oil's claimed foreign tax credit for all tax payments to IFIL.

AFFIRMED.

Layton, Circuit Judge, dissenting:

For the reasons discussed below, I respectfully dissent.

I. DISCUSSION

45. I believe the majority errs in the deciding of this matter. The underlying policy concern of foreign tax credits is to determine under what circumstances a literal application of the credit rules should give way to overriding policy concerns. In this case, we need to move past the literal application of the rules and focus our decision on the practical policy concerns. The fundamental goal of the foreign tax credit is to prevent the vexatious issues of double taxation and secondarily encourage foreign trade. *See, e.g., Texasgulf, Inc. v. CIR*, 172 F.3d 209 (2nd Cir. 1999). This is a noble goal that allows for United States corporations to be sterling guests to our neighbors across the globe. United States corporations operating all around the world are using up valuable resources in host nations and those nations deserve to be compensated through legal taxation without interference from the United States Tax Code.

46. Using the above policy concerns as a platform, I would uphold Harkonnen Oil's claimed foreign tax credit of all payments to Arrakis. Here, Arrakis allows Harkonnen Oil to recover costs and expenses sufficiently identical to those costs and expenses referenced in the U.S. Tax Code. As such, the Arrakis tax properly reaches net income. While the trend

under the law is to ignore the application of the foreign rules and analyze them under U.S. Tax Code standards, I would point out that the Arrakis' deductions are limited for religious reasons. Therefore, forcing a country to violate its religious tenets in order to satisfy our fear of under taxation is unconscionable. The earliest cases on the subject acknowledge that some deference should be given to the foreign perspective. *See Seatrain Lines, Inc. v. Comm'r*, 46 B.T.A. 1076, 1080 (1942). *See also, Exxon Corp. v. Comm'r*, 113 T.C. 338, 357 (1999). Otherwise we effectively make the Internal Revenue Service the final arbiter of global trade and tax law. This would promote an executive enforcement agency into the role of legislative policy making.

47. As it stands, the United States practically demands that foreign countries rewrite their tax codes in order to satisfy its fears of underpayment to the United States. The brazen truth is that most countries develop their tax codes in order to generate U.S. foreign tax credits for U.S. Companies because they need U.S. Companies to help fund or jump start economic growth. Without the foreign tax credits, U.S. Companies would be subject to double taxation and would not engage in global trade, or at the very least, engage in significantly less global trade. That is why when faced with two interpretations of a tax, courts generally apply the interpretation leading to a proper foreign tax credit.

48. Using the same policy concerns, if the levy fails as a credible foreign tax credit sufficient to satisfy 26 U.S.C. § 901, I would find that it instead satisfies 26 U.S.C. § 903. That section was created as a safety net to catch levies that are intend to be income taxes under 26 U.S.C. § 901, but fail to completely satisfy all of its requirements. *See Bank of Am. Nat'l Trust & Sav. Ass'n v. Comm'r*, 61 T.C. 752, 761 (1974).

49. Like my analysis of the Arrakis tax, I would also hold that the IRS improperly denied Harroken Oil's claimed foreign tax credit of money paid to IFIL. First, Harroken Oil properly exhausted all remedies to challenge a foreign jurisdiction's tax levy by consulting with the Holy Royal Court. That Court determined that IFIL was a part of Sietch and therefore was a valid taxing entity. Not all of historical Sietch is a part of the Sietch State.¹⁶ Arrakis, through its officials, could determine the proper legal status of IFIL. Requiring a taxpayer to seek relief from every possible competent court is not practical, cost efficient, or warranted.

II. CONCLUSION

50. In conclusion, I would reverse the lower court and grant the foreign tax credits to the Royal Harkonnen Oil Company.

¹⁶ The city of Kaza is located outside of the Sietch State, but 90% of Kaza residents hail from Sietch bloodlines.