

Where is the Guidance and Is It Binding? *Loper Bright* and Other News

ROBB CHASE

MINDY HERZFELD

JUD JUDKINS

ROB KOVACEV

**40th Annual TEI-SJSU High Tech Tax
Institute**

November 4, 2024

1

Agenda

Overview of Administrative Law and the APA

Tax Rules and Regulations

Challenges to Agency (IRS) Rulemaking

The Downfall of the *Chevron* Doctrine

Deference to Agency Rulemaking following *Loper Bright*

Looking Ahead

2

General Background on Administrative Law

General Concept – Administrative law focuses on the process by which federal agencies develop, issue, amend, and repeal regulations, which is commonly called rulemaking.

Administrative Procedure Act (APA) (1946):

- Provides the statutory basis for Federal Administrative Law.
- Categorizes agency actions as rulemaking or adjudication.
- Creates framework that agency rulemaking can be proposed and evaluated.

Internal Revenue Code: Gives additional rules for IRS and Treasury Department.

U.S. Code: Other Federal laws impose additional requirements for agencies.

Requirements for Agency Rulemaking

Notice – 5 USC § 553(b)

- Agency must publish a Notice of Proposed Rulemaking in the Federal Register, which shall include:
 - Time, place, and nature of the public rulemaking proceeding;
 - Legal authority for the proposed rule;
 - Either terms or substance of the rule or description of the issue.

Comment – 5 USC § 553(c)

- Agency must give interested persons the opportunity to participate by submitting written data, views, or arguments (may include oral presentation); and
- Agency must consider any relevant matter presented and incorporate in any final rules a “concise general statement of the basis and purposes.”

Publication – 5 USC § 553(d)

- Final rule must be published at least 30 days before a rule’s effective date, except for:
 - Substantive rule that grants or recognizes an exemption or relieves restriction;
 - Interpretive rules and statements of policy; or
 - Good cause found and published with the rule.

Requirements for Agency Rulemaking (cont'd)

The Attorney's General Manual on the APA provides definitions of substantive and interpretive rules:

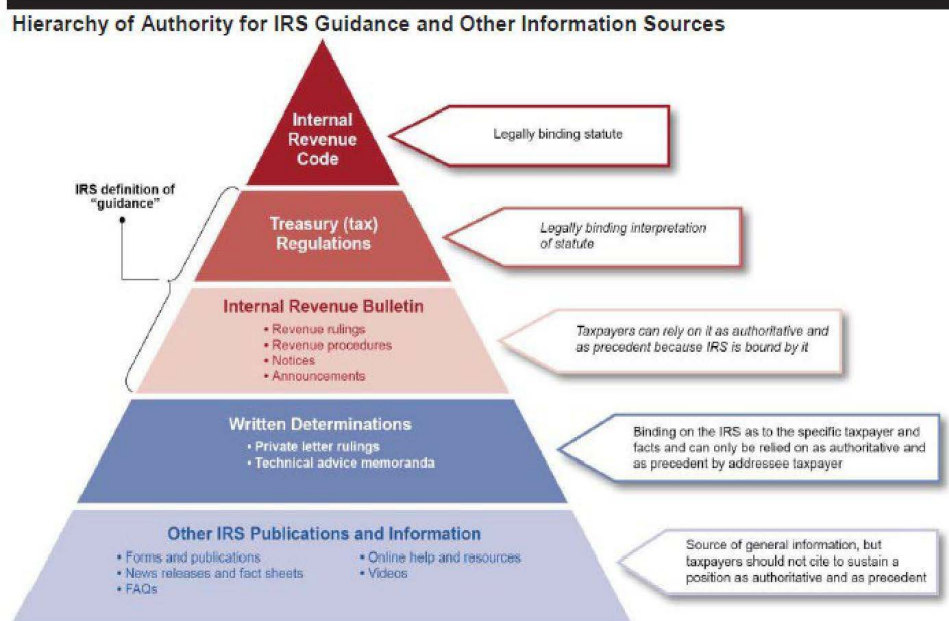
- **Substantive:** Rules issued by an agency pursuant to statutory authority and which implement a statute.
- **Interpretive:** Rules or statement issued by agency to advise the public of the agency's construction of the statutes and rules it administers.

Before *Mayo* (Sup. Ct. 2011), courts distinguished between "legislative" and "interpretive" based on whether a specific grant of rulemaking authority:

After *Mayo*, cases have treated § 7805(a) regulations as "legislative" regulations for APA purposes if they are intended to have the force and effect of law. *See Chamber of Commerce* (WD Tex 2017).

5

Tiers of IRS Guidance



Source: GAO analysis of IRS documents. | GAO-16-720

6

Treasury Regulations

Regulations come in proposed, temporary, and final form.

Proposed – not binding, but sometimes can be relied on by taxpayers.

Temporary:

- Must be accompanied by proposed regulations which will go through notice-and-comment process.
- Generally considered binding (although questions arise over satisfaction of APA's good-cause requirement).
- Temporary regulations issued after November 20, 1988, must be finalized within three years.
- If temporary regulations expire, the proposed regulation nevertheless remains in proposed form unless it is withdrawn.

Final – binding if validly promulgated (i.e., pass *Loper Bright* and APA requirements).

Treasury Regulations (cont.)

Section 7805(b) restricts use of retroactive regulations.

- **Limitations:** if authority exists to make the regulation retroactive, the effective date of final, temporary or proposed regulation may not be before earliest of (i) final rule published in the Federal Register, (ii) proposed or temporary rule published in the Federal Register, or (iii) notice substantially describing expected contents of regulation issued.
- **Authorization to Issue Retroactive Regulations:**
 - Regulations to “prevent abuse.”
 - Correction of procedural defects in prior regulations.
 - Congress explicitly authorizes Treasury to issue retroactive regulations.
 - Taxpayer is given election to apply regulation retroactively.

Treasury Regulations (cont.)

Congress has delegated authority to IRS to issue regulations in two ways:

- Section 7805(a) general grant of authority.
- Specific authority granted in the relevant statute.

Both before and after *Mayo*, courts have invalidated § 7805(a) regulations that cannot point to a gap in the relevant Code section that needs to be filled, or that add a requirement or restriction not supported by statutory text.

Internal Revenue Bulletin (I.R.B.) Guidance

I.R.B. Guidance

- I.R.B. is the “authoritative instrument of the Commissioner . . . for announcing official rulings and procedures of the Internal Revenue Service . . .”

What level of deference should apply?

- If the IRS issues a public notice and takes comments?
- If it does not issue a public notice and take comments?

The Department of Justice has stated that it will not argue for *Chevron* deference for I.R.B. guidance. Following *Loper Bright*, this policy is likely moot.

Treasury Policy Statement

Department of the Treasury issued a Policy Statement on the Tax Regulation Process (March 5, 2019):

- Commitment to notice and comment rulemaking, even for interpretive rules.
- Limited use of temporary regulations, with “good cause” statement.
- Limits on sub-regulatory guidance:
 - IRS will not seek judicial deference under *Auer* or *Chevron* in Tax Court litigation.
 - Limit effectiveness of notices setting forth anticipated proposed regulations after 18 months (taxpayers may rely but IRS will not assert adverse position based on notice).

Current Administration has thus far not rescinded or modified this Policy Statement.

Challenging Agency Rules

Judicial Review:

- 5 USC § 702: persons **harmed by** agency actions generally have a right to judicial review.

Scope of Review:

- Court may hold unlawful and set aside an agency rule found to be:
 - “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law,” 5 USC § 706(2)(A);
 - in excess of statutory authority, 5 USC § 706(2)(C); or
 - “without observance of procedure required by law.” 5 USC § 706(2)(D).

State Farm Judicial Review Standard (Sup. Ct. 1983) under APA for “legislative” regulations:

- whether the agency engaged in reasoned decisionmaking:
 - Relevant factors must be considered.
 - Agency must provide a reasoned explanation for the regulation.
 - For factual issues, agency must explain the facts found and their relation to choices is critical.
 - Arbitrary or capricious review.

Where: U.S. Tax Court (26 U.S.C. § 6214); Court of Federal Claims (28 U.S.C. § 1491); or District Court (28 U.S.C. § 1346).

Challenging Agency Rules (cont.)

In theory, there are three potential times to challenge an agency action.

- Pre-enforcement;
- During enforcement; or
- After enforcement (deficiency or refund litigation).

Taxpayers face the greatest obstacles in pre-enforcement and during enforcement challenges.

- Obstacles to a taxpayer's challenging IRS rulemaking include standing, the Anti-injunction Act, the Declaratory Judgment Act, and relevant statutes of limitation.

Tools for Attacking Treasury Regulations

Procedurally Defective (APA):

- **Argument:** Treasury failed to carry out the notice-and-comment process.
- **Example:** *Encino Motorcars* (Sup. Ct. 2016).

Arbitrary or Capricious (APA):

- **Argument:** Treasury did not engage in reasoned decisionmaking.
- **Examples:** *State Farm* (Sup. Ct. 1983)

Substantively Invalid (*Loper Bright*)

- **Argument:** Agency action / rule is not the best interpretation of the empowering statute.
- **Example:** *Varian v. Commissioner*, 163 TC No. 4 (Aug 26, 2024).

Chevron Doctrine

Chevron was based on a presumption that, when Congress left an ambiguity in a statute administered by an agency, it generally intended to let the agency resolve the ambiguity.

Typically expressed as a two-step test:

- **Step 1:** Is the statute ambiguous on the precise question at issue? If the statute is unambiguous, follow the statute, not the agency's interpretation of it.
- **Step 2:** If the statute is ambiguous, is the agency's interpretation of the statute reasonable? If so, then defer to the regulation – even if it differs from the court's view of the best interpretation.

Skidmore - Alternative Deference

The commonly cited standard is from *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944):

The weight given to an administrative judgment in a particular case depends upon, among other things, **the thoroughness evident in its consideration, the validity of its reasoning, and its consistency with earlier and later pronouncements.**

Other factors may include, *e.g.*, whether the interpretation was issued contemporaneously with the statute, how formal the guidance is, and the agency's relative expertness on the subject.

Skidmore deference was the standard courts generally applied to regulations and subregulatory guidance before *Chevron*; after *Chevron*, *Skidmore* still applied as to subregulatory guidance.

Auer Deference as to Interpreting Regulations

The Supreme Court recently reaffirmed so-called *Auer* deference, where courts defer to an agency's interpretation of its own ambiguous regulations (not statutes). *Auer v. Robbins*, 519 U.S. 452 (1997),

Whether *Auer* deference will survive is unclear:

- *Auer* is based on the presumption that an agency's power to interpret its own regulations is a component of its delegated authorities.
- But there is still tension with the APA, which requires courts to "decide all relevant questions of law" and "determine the meaning" of relevant agency action.

Regardless, *Auer* deference was narrowed significantly in *Kisor v. Wilkie*, 588 U.S. 558 (2019):

- A regulation must be **genuinely ambiguous** after exhausting all tools of interpretation.
- The agency's interpretation must be **reasonable**, within the zone of ambiguity identified.
- The **character and context** of the agency's interpretation must entitle it to deference: It must be authoritative, implicate the agency's expertise, and represent fair and considered judgment.

Loper Bright and Relentless

Loper Bright and *Relentless* are essentially the same, except that Justice Jackson was recused from *Loper Bright* but not *Relentless*:

- Under the Magnuson-Stevens Act, the National Marine Fisheries Service may require vessels to carry federal monitors to enforce agency regulations to prevent overfishing.
- The D.C. Circuit and the First Circuit upheld a National Marine Fisheries Service regulation requiring fishing boats to pay the costs of those monitors.

The Court granted review, limiting the question presented to:

- Whether the Court should overrule *Chevron*, or at least clarify that statutory silence concerning controversial powers expressly but narrowly granted elsewhere in the statute does not constitute an ambiguity requiring deference to the agency.

Loper Bright / Relentless: The Opinion

It has always been the **judiciary's** duty to say what the law is.

The Administrative Procedure Act requires the same:

- “The **reviewing court** shall decide **all** relevant questions of law.”
- “The **reviewing court**” shall set aside agency action found “**not in accordance with law.**”

Chevron was based on “a fiction”

- Courts, not agencies, are experts in statutory interpretation.
- Courts must independently construe statutes (even technical ones) when no agency is involved.
- “The better presumption” is that “Congress expects **courts** to do their ordinary job of interpreting statutes.”

“*Chevron* is overruled. Courts must exercise independent judgment” on matters of statutory interpretation.

Impact of *Loper Bright / Relentless* on Judicial, Legislative, and Rulemaking Processes

Impact on Judicial Process –

- Application of the traditional tools of statutory construction to determine the best interpretation of the statute with no deference to the agency.
- Consideration of *Skidmore* factors: A reviewing court may accord “respect” to the views of the agency based on several factors that evidence the persuasive force of the regulation.
- Court’s view of the meaning of a statute is informed not only by the agency’s perspective but also by the parties before the court as well as amici.

Impact on Legislative Process:

- Potential Changes to Tax Statutes and Implications of Grants of Rulemaking Authority
 - General v. Express Delegations, Major Questions Doctrine, and Non-delegation Doctrine

Impact on Rulemaking Process:

- Puts a premium on comment letters and active participation in the rulemaking process;
- Taxpayers should leverage their tax expertise and industry-specific knowledge;
- Provides Treasury and the IRS with a helpful and necessary perspective that they must consider;
- Develops a robust and contemporaneous administrative record to assist a reviewing court.

Loper Bright / Relentless: Express Delegations

“In a case involving an agency ... the statute's meaning may well be that the agency is authorized to exercise a degree of discretion,” as when “statutes ‘expressly delegate[]’ to an agency the authority to give meaning to a particular statutory term. ... Others empower an agency to prescribe rules to ‘fill up the details’ of a statutory scheme, ... or to regulate subject to the limits imposed by a term or phrase that ‘leaves agencies with flexibility,’ ... such as ‘appropriate’ or ‘reasonable.’”

“When the best reading of a statute is that it delegates discretionary authority to an agency, the role of the reviewing court under the APA is, as always, to independently interpret the statute and effectuate the will of Congress subject to constitutional limits. The court fulfills that role by recognizing constitutional delegations, ‘fix[ing] the boundaries of [the] delegated authority,’ ... and ensuring the agency has engaged in “‘reasoned decisionmaking’” within those boundaries.... By doing so, a court upholds the traditional conception of the judicial function that the APA adopts.”

Loper Bright / Relentless may force Congress to delegate expressly (when it wants to), bringing nondelegation concerns to the forefront:

- Congress cannot delegate its legislative authority, but historically this has just meant that Congress needs to provide an “intelligible principle.”
- The Supreme Court has not invalidated a delegation since the 1930s, but a more robust nondelegation principle is gaining traction among some Justices and lower courts.

Will *Auer* Survive after *Loper Bright*?

Whether *Auer* deference will survive is unclear:

- *Chevron* was based on a (fictional) presumption of what Congress intended regarding the interpretation of statutes.
- *Auer* is based on a different presumption — that an agency’s power to interpret its own regulations is a component of its delegated authorities.
- But there is still tension with the APA, which requires courts to “decide all relevant questions of law” and “determine the meaning” of relevant agency action.

Regardless, *Auer* deference was narrowed significantly in *Kisor*, so *Auer*’s survival may not matter in the end.

Recent application of *Loper Bright*

Varian v. Commissioner, 163 TC No. 4 (Aug 26, 2024):

- The Commissioner claimed that the Court should defer to a Treas. Reg. because even if the Court disagreed with the gov't's interpretation, the statute was ambiguous and that under *Chevron* the court had to accept the regulation because the Treasury interpretation was permissible.
- Applying *Loper Bright*, the Court emphasized that statutes have a "single, best meaning" that courts must determine.
- Acknowledging that the Executive Branch's judgment is a "body of experience" on which judges may properly resort for guidance (citing *Skidmore*), the Court nonetheless determined the statute was unambiguous.
- Thus, despite Congress delegating rulemaking authority to Treasury under the reviewed provision, the Court held that it was an "impermissibl[e]...change [to] an unambiguous provision of the statute" and so "the regulation falls outside the boundaries of any authority that Congress may have delegated under [the Code.]"
- Taxpayer favorable decision; unclear whether Commissioner will appeal.

Corner Post – Holding and Rationale

Issue: When does a plaintiff's APA claim first accrue under 28 U.S.C. § 2401(a)?

Facts:

- § 2401(a) requires that a civil action against the United States be commenced within six years "after the right of action first accrues."
- Corner Post owned a North Dakota truck stop that accepted debit card purchases and paid interchange fees to banks that processed debit card transactions.
- In 2011, the Federal Reserve Board issued a regulation regarding these fee.
- In 2021, three years after it opened business in 2018, Corner Post challenged the Federal Reserve Board's regulation on procedural and substantive grounds.
- The lower courts dismissed the case as time-barred.

Supreme Court (6-3 Decision):

- Held that the limitations period under 28 U.S.C. § 2401(a) did not start running until 2018, when Corner Post was injured by the regulation.
- A right of action accrues only when the plaintiff has the "complete and present" right to "file suit and obtain relief."

Corner Post – Practical Considerations

Under *Corner Post*, an APA claim does not accrue for the purposes of 28 U.S.C. § 2401(a)'s six-year statute of limitations until the plaintiff is injured by final agency action.

- The Court reasoned that because an APA plaintiff may not file suit and obtain relief until they suffer an injury from final agency action under 5 U.S.C. §§ 702 and 704, the statute of limitations does not begin to run until they are injured.

Combined with *Loper Bright*, *Corner Post*'s expanded time frame to bring suit against administrative agencies will likely lead to more litigation challenges to federal regulations.

Potential increase in regulation challenges:

- New opportunities to challenge older regulations.
- Opportunities for revisiting agency positions previously upheld on deference grounds.

Impact on the courts:

- Preliminary injunctions, supplemental briefing, and stare decisis

Looking Ahead

Several recent and pending cases highlight the current state of affairs.

See, e.g.:

- *Liberty Global, Inc. v. U.S.*, No. 1:20-cv-03501-RBJ (D. Colo., Apr. 4, 2022), on appeal to 10th Circuit;
- *Kyocera AVX Components Corp. v. U.S.*, No. (D.S.C., complaint filed July 28, 2022);
- *3M Co. v. Commissioner*, T.C. No. 5816-13, on appeal to 8th Circuit;
- *Mann Construction, Inc. v. US*, 24 F.4th 1138 (6th Cir. 2022);
- *CIC Services, LLC v. IRS*, No. 317-cv-110 (E.D. Tenn. 2022);
- *GBX Associates, LLC v. US*, No. 1:22-cv-401 (N.D. Ohio).

These challenges can be broken down as:

- Cases involving IRS/courts purportedly not following regulations;
- Cases involving challenges to the substantive and/or procedural invalidity of regulations;
- Challenges to the procedural validity of subregulatory guidance.

Regs Ripe for Scrutiny

Section 482?

Consolidated Return Regs?

Sec. 367 regs/ Anti-inversion regs

DCL Regs

Taxpayer Favorable v. Antiabuse rules

IRA Implementation Regs

FTC regs

TCJA implementation regs/guidance (e.g., GLAM 2024-002; CCM 202436010)

27

Questions?

Robb Chase, Partner

Eversheds

robbchase@eversheds-sutherland.com

Mindy Herzfeld, Professor

University of Florida Law School

herzfeld@law.ufl.edu

Joseph Judkins, Partner

Baker McKenzie

joseph.judkins@bakermckenzie.com

Robert Kovacev, Member

Miller & Chevalier Chartered

rkovacev@milchev.com

28