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Mayo Foundation v. U.S.: Supreme Court Applies Chevron Analysis to Tax Cases

Understanding the Implications of Giving Deference to IRS Regulations

WEDNESDAY, MARCH 23, 2011

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Today's faculty features:

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Mayo Foundation v. U.S.: Supreme Court Applies Chevron Analysis to Tax Cases

Strafford Publications, Inc. Seminar

March 23, 2011

Presented By
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Overview

- A Short Review of Administrative Law Principles
- The Question Presented and Case Background
- The Prior Circuit Decisions
- *Mayo*

Administrative Law

- Separation of Powers
  - Not explicit in the Constitution
  - Refers to structural checks and balances between the three branches
- Nondelegation Doctrine
  - "Intelligible Principle"
  - Modern, complex society invites extensive executive action
- Judicial Review of Agency Rule-Making
  - *Chevron USA, Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984)
  - *National Muffler Dealers Assn., Inc. v. United States,* 440 U.S. 472 (1979)
  - *Skidmore v. Swift & Co.,* 323 U.S. 134 (1944)
  - Administrative Procedures Act (APA), Pub.L. No. 79-404, 60 Stat. 237
- Congress or the Executive?

Question Presented

- Petition for Certiorari filed January 14, 2010
- Certiorari granted June 2, 2010 with this question:

> Whether the Treasury Department can categorically exclude all medical residents and other fulltime employees from the definition of "student" in 26 U.S.C. § 3121(b)(10), which exempts from Social Security taxes "service performed in the employ of a school, college, or university" by a "student who is enrolled and regularly attending classes at such school, college, or university.“

- Note that § 3121(b) provides a definition of “employment” and (b)(1)-(21) provide for exceptions to this term, and thus to the imposition of FICA taxes.

Overview of Facts

- Medical residents in the Mayo Clinic participated in a three to five year structured training and educational program through the University of Minnesota.
- Under the program, the university exercised educational control of the activities of the residents at the clinic by determining educational goals, tracking completion of assignments, evaluating performance and appointing hospital staff members to be members of the University with consequent faculty authority over the residents.

Overview of Facts

- Residents carried out typical student activities by reading from assigned textbooks and journal articles, attending regular lectures and conferences, and taking written exams which were evaluated by the attending faculty physicians.
- Most of the residents' time was spent in the actual practice of medicine from 50 to 80 hours a week, In 2005, Mayo paid its residents annual “stipends” ranging between $41,000 and $56,000 and provided them with health insurance, malpractice insurance, and paid vacation time.

Minnesota v. Apfel, 151 F.3d 742 (8th Cir. 1998)

- The issue arose after the State of Minnesota brought suit against the Social Security Administration disputing an assessment of contributions relating to the stipend payments to its medical resident students.
- On appeal, the Eighth Circuit held in favor of the State on two alternate grounds, the second of which was based on an exception for service performed by a student in Title 42 which has the same language as IRC § 3121(b)(10): service performed in the employ of a school, college, or university "if such service is performed by a student who is enrolled and regularly attending classes at such school, college, or university." 42 U.S.C. § 418(a)(10).
- Teaching hospitals and universities (including the Mayo Foundation) around the country took note and began filing refund claims with the IRS.

Prior Circuit Decisions and IRS Response

- Four Circuits, the Second, the Sixth, the Seventh and Eleventh, held that the student exception to the definition of employment is unambiguous and does not categorically exclude medical residents.

  "We agree with the Sixth, Seventh, and Eleventh Circuits that the statute is unambiguous and that whether medical residents are "students" and the Hospitals "schools" is a question of fact, not a question of law. The statute expressly defines which individuals fall within the scope of the student exception: students who are "enrolled and regularly attending classes." 26 U.S.C. § 3121(b)(10). It also establishes the types of employment that qualify for the student exception: "service performed in the employ of ... a school, college, or university." *Id. United States v. Memorial Sloane-Kettering Cancer Center*, 563 F.3d 19 (2d Cir. 2009).

- IRS responded by promulgating new regulations after notice and comment that specifically excluded fulltime medical residents from the student exception. Prior regulations focused on the relationship of the services performed to the course of study and did not impose an hours limit.

Eighth Circuit Decision (568 F.3d 675)

- Notwithstanding the conclusion of these other circuits, the Eighth Circuit concluded that the statute was ambiguous.
  - Focuses on the application of the exception to medical residents and decides that the statute is ambiguous *in this context*.
    - If that is the test for ambiguity then all statutes are ambiguous at some level, but there is a difference between generality and ambiguity.
    - The court also makes the curious remark that it does not disagree with the other circuits because they were about "the statute *as construed in the prior regulations.*" How are regulations relevant where a statute is unambiguous?
  - Appeals to the amended regulations which, as noted, specifically exclude the fulltime medical resident from the student exception, But the statutory language has not changed so how is this relevant?
- In the course of its decision, the Eighth Circuit reviewed the history of the social security statutes and legislative history surrounding enactment of student exception and concluded that the exception was directed to part-time school workers.

Circuit Conflict?

- Mayo argued that there was a circuit conflict in its petition for certiorari. Four other circuit courts held that the student exception was unambiguous and did not exclude medical residents per se whereas the finding of the Eighth Circuit even after the promulgation of the IRS's "litigating" regulation seemingly depended upon a finding under *Chevron* that the statute was ambiguous.
- The Solicitor General argued there was no conflict because the other circuit decisions did not consider the amended regulations but did "rely on the fact" of the prior regulations in their decisions. Opp. Br. at 12.
- However, given the language in the decision, the Supreme Court likely granted certiorari to clarify the standard of deference to be given to agency rule-making.

Mayo Foundation For Medical Ed. & Research, et al. v. United States, 131 S. Ct. 704 (2011)

- Unanimous with one recusal – Justice Kagan
- Order of analysis
  - Is the statute ambiguous?
  - *Chevron* applies unless there is a different standard for tax regulations
  - There should be no difference in standard of review of Treasury regulations versus other rulemakings of other federal agencies.
  - Under *Chevron*, therefore, ascertain next whether the agency in fact acted pursuant to the authority which was granted to it by Congress.
    - Section 7805(a), which is a general grant of rule-making authority, supplied the necessary congressional authorization and
    - The Treasury's promulgation after notice and comment was a "significant sign" of appropriate exercise of that authority.
  - Review regulation and determine whether it is a reasonable interpretation of the statute

National Muffler No More

- "Aside from our past citation of *National Muffler*, Mayo has not advanced any justification for applying a less deferential standard of review to Treasury Department regulations than we apply to the rules of any other agency. In the absence of such justification, we are not inclined to carve out an approach to administrative review good for tax law only. To the contrary, we have expressly "[r]ecogniz[ed] the importance of maintaining a uniform approach to judicial review of administrative action." *Dickinson* v. *Zurko*, 527 U. S. 150, 154 (1999). See, *e.g., Skinner* v. *Mid-America Pipeline Co.*, 490 U. S. 212, 222–223 (1989) (declining to apply "a different and stricter nondelegation doctrine in cases where Congress delegates discretionary authority to the Executive under its taxing power")."

Observations On *Mayo*

- What was the standard the Supreme Court used to determine ambiguity?
  - Dictionary definition not sufficient "as applied to working professionals"
  - Full-time professor example
  - No apparent reference to legislative history, but underlying perception of what Congress could not have intended
  - Reference to two other Code provisions addressing medical residents

Observations on *Mayo*

- There was no significant consideration given to the fact that Congress makes explicit drafting decisions to give the Treasury Department regulatory authority within the Code provision itself.
  - Specific grant of rule-making authority formed the basis for the now apparently defunct distinction between legislative and interpretive regulations. Why does Congress draft specific grants of authority if there is already a sufficient legislative delegation of rule-making authority within IRC § 7805(a)?
- Instead the Supreme Court embraces the notion that uniformity in review of agency action is itself a fundamental judicial virtue.
- Deferral to Congress versus deferral to Executive?

The Future With *Mayo*

- Can IRS extend *Chevron* deference to other guidance by including notice and comment procedures?
- Does *Mayo* weaken IRS arguments that other types of guidance, such as revenue rulings or temporary regulations, should have *Chevron* treatment because these do not have notice and comment?
  - *Cf. Nationsbank of North Carolina, N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251 (1995) (Comptroller grant of application entitled to deference)
  - Are nonprecedential letter rulings eligible for *Chevron* treatment?
- Victory is not always permanent – IRS can promulgate litigation regulation to override prior court decision.

Chevron and Tax Cases After *Mayo*

by

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March 23, 2011

Mayo Found. for Med. Educ. & Research v. United States 131 S.Ct. 704 (2011)

Key Points and Highlights

- Explicitly rejects *National Muffler* in favor of *Mead and Chevron* as governing judicial evaluation of general authority Treasury regulations. Slip @ 11-12.
  - Administrative law has changed substantially since the late 1970s and early 1980s, when the Court decided *National Muffler* and cases most actively advocating its application to general authority Treasury regulations, like *Rowan Cos. v. United States* and *United States v. Vogel Fertilizer Co.* Slip @11.
  - In the post-*Chevron*, post-*Mead* era, whether a congressional delegation of rulemaking power is specific or general no longer matters for purposes of judicial deference doctrine. Slip @ 11.
  - "We believe *Chevron* and *Mead*, rather than *National Muffler* and *Rowan*, provide the appropriate framework for evaluating" the general authority Treasury regulation at issue in this case, and given the Court's analysis, other general authority Treasury regulations as well. Slip @ 11.

Mayo Found. for Med. Educ. & Research v. United States
131 S.Ct. 704 (2011)

Key Points and Highlights

- Expressly concludes that Treas. Reg. § 31.3121(b)(10)-2(d)(3)(i) is entitled to *Chevron* review under the standard for *Chevron*-eligibility articulated in *Mead*. Slip @ 12.
  - Treasury's power to "prescribe all needful rules and regulations" under I.R.C. § 7805(a) is "a very good indicator of delegation meriting Chevron treatment." Slip @11-12 (citing *United States v. Mead Corp.*).
  - That Treasury promulgated the regulation at issue using notice and comment rulemaking is "a 'significant' sign that a rule merits *Chevron* deference." Slip @ 12 (citing *United States v. Mead Corp.*).
  - Also, *Chevron* is appropriate "[w]here an agency rule sets forth individual rights and duties, where the agency focuses fully and directly upon the issue, where the agency focuses fully and directly upon the issue, where the agency uses full notice-and-comment procedures to promulgate a rule, [and] where the resulting rule falls within the statutory grant of authority." Slip @ 12 (citing *Long Island Care at Home, Ltd. v. Coke*).

Mayo Found. for Med. Educ. & Research v. United States
131 S.Ct. 704 (2011)

Key Points and Highlights

– Generally rejects tax exceptionalism from broader administrative law doctrine governing judicial review of agency action.

> "Mayo has not advanced any justification for applying a less deferential standard of review to Treasury Department regulations than we apply to the rules of any other agency. In the absence of such justification, we are not inclined to carve out an approach to administrative review good for tax law only. To the contrary, we have expressly '[r]ecogniz[ed] the importance of maintaining a uniform approach to judicial review of administrative action.' *Dickinson v. Zurko*, 527 U.S. 150, 154 (1999). See, *e.g.*, *Skinner v. Mid-America Pipeline Co.*, 490 U.S. 212, 222-223 (1989) (declining to apply 'a different and stricter nondelegation doctrine in cases where Congress delegates discretionary authority to the Executive under its taxing power')."

Mayo Found. for Med. Educ. & Research v. United States
131 S.Ct. 704 (2011)

Implications

- Tax practitioners will need to become much more familiar with the nuances of *Mead*, *Chevron*, and *Skidmore*.
- Tax practitioners will want to become much more familiar with related standards of judicial review of agency action and with Administrative Procedure Act procedural requirements as well.
  - E.g., *Mayo* does not address the question of judicial deference for temporary regulations.
- IRB guidance documents (revenue rulings, revenue procedures, and notices) are the next big battleground for judicial review of tax cases.

Chevron, *Skidmore*, and *Mead*

- *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984)
  - Step one: "whether Congress has directly spoken to the precise question at issue"; if not,
  - Step two: "whether the agency's answer is based on a permissible construction of the statute"
- *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944)
  - multi-factor analysis considering, *inter alia*, "the thoroughness evident in [the agency's] consideration [of the interpretive question], the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it the power to persuade, if lacking power to control"
  - Note: analysis equivalent to *Chevron* step one is implicit in this standard as well
- *United States v. Mead Corp.*, 533 U.S. 218, 226-27 (2001)
  - whether "Congress delegated authority to the agency generally to make rules carrying the force of law, and . . . the agency interpretation claiming deference was promulgated in the exercise of that authority"

Judicial Deference Framework

Step Zero: *United States v. Mead Corp.*

1) Did Congress give the agency in question the authority to bind regulated parties with the force of law?
2) Did the agency exercise that authority in adopting the interpretation at issue?

If yes to both ↓

If no to either ↓

***Chevron* step one:**
Is congressional intent clear?
De novo review using traditional statutory interpretation methods.

***Skidmore* "respect"** based on multi-factor analysis – in theory, the court remains the primary interpreter

If no ↓

If yes →

***Chevron* step two:**
Is the agency's interpretation reasonable/permissible?
Highly deferential.

End of the inquiry, as unambiguous statutes leave no room for interpretation by courts or agencies.

Chevron Step One Issues

- Framing the step one test: *See Chevron*, 467 U.S. 837 at 842-43.
  - "[W]hether Congress has directly spoken to the precise question at issue."
  - Whether "the intent of Congress is clear."
  - Whether "the statute is silent or ambiguous with respect to the specific issue."
  - How clear must the statute or congressional intent be?
- Scope of the step one inquiry:
  - Which tools are included in "traditional tools of statutory construction?" *See Chevron*, 467 U.S. 837, 843 n.9.
  - Should the court consider legislative history at step one or step two?
  - What role should substantive canons play in *Chevron* analysis?
- Phrasing the interpretive question:
  - *E.g., FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120 (2000): "whether cigarettes are drug delivery devices" versus "whether the statute gives the FDA jurisdiction over tobacco"

Chevron Step Two & Other Administrative Law Doctrines

- In describing *Chevron* step two analysis, the Supreme Court uses "reasonable" and "permissible" interchangeably and as the opposite of "unreasonable," "impermissible," or "arbitrary and capricious."
- Plausible arguments under *Chevro*n step two:
  - Substantive invalidity: The agency's interpretation of the statute is substantively invalid; even if the statute is susceptible of more than one reasonable interpretation, the interpretation advanced by the agency is not one of the permissible alternatives. *See, e.g.*, *AT&T Corp. v. Iowa Utilities Bd.*, 525 U.S. 366 (1999).
  - Process invalidity: The agency's interpretation of the statute is arbitrary and capricious according to the principles of "hard look review" under APA § 706(2)(A). *See, e.g.*, *Covad Commc'ns v. FCC*, 450 F.3d 528, 537 (D.C. Cir. 2006) (incorporating hard look review into *Chevron* step two analysis); *Manella v. Comm'r*, 631 F.3d 115, 127-28 (3d Cir. 2011) (Ambro, J. dissenting) (same).
  - Procedural invalidity: The agency's interpretation of the statute is not entitled to deference for its failure to satisfy the procedural requirements of APA § 553. *See, e.g.*, *Burks v. United States*, 2011 WL 438640 at n.9 (5th Cir. Feb. 9, 2011) (suggesting the Court would not defer to a procedurally invalid temporary regulation).

Chevron Step Two & Other Administrative Law Doctrines
Hard Look Review

- APA §706(2)(A): The reviewing court shall … hold unlawful and set aside agency action, findings, and conclusions found to be … arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."
- The agency must contemporaneously explain the reasoning behind its action.
  - Is there a "rational connection between the facts found and the choice made?"
  - Did the agency
    - rely "on factors which Congress has not intended it to consider?"
    - fail "to consider an important aspect of the problem?"
    - offer "an explanation for its decision that runs counter to the evidence before the agency?"
  - Is the agency's action "so implausible that it could not be ascribed to a difference in view or the product of agency expertise?"
  - "Post hoc rationalizations for agency action" in litigation are unacceptable.

Motor Vehicle Mfrs. Ass'n of the U.S. v. State Farm Mutual Auto. Ins. Co., 463 U.S. 29 (1983); *see also FCC v. Fox Telev. Stations, Inc.,* 129 S.Ct. 1800 (2009).

Chevron Step Two & Other Administrative Law Doctrines
APA Procedural Requirements

- Basic procedural requirements of APA § 553 for legislative rules that carry "the force of law"
  - Notice of proposed rulemaking: If an agency decides to shift course too sharply from its original notice, the agency must begin again with a revised notice.
  - Opportunity for written comments
  - Concise statement of basis and purpose: must address all significant comments.
  - Publication in the Federal Register thirty days before effective date.
- *Exceptions:*
  - *Interpretative rules, procedural rules, and policy statements are exempt.*
  - *Good cause: where notice and comment are impracticable, unnecessary, or contrary to the public interest; the agency must assert this exception contemporaneously with specificity and particularity.*
- Circuit split: Can an agency "cure" procedurally invalid regulations or rulings with post-promulgation notice and comment?
  - *Compare Burks v. United States*, 2011 WL 438640 at n.9 (5th Cir. Feb. 9, 2011), *with Grapevine Imports, Ltd. v. United States*, 2011 WL 832915 at *10 (Fed. Cir. Mar. 11, 2011).

Next Battleground: IRB Guidance

- Internal Revenue Bulletin: Revenue rulings, revenue procedures, and notices "do not have the force and effect of Treasury regulations," though taxpayers "generally may rely" upon them.

but

- I.R.C. § 6662 & Treas. Reg. § 1.6662-3: "rules and regulations" for the purpose of assessing underpayment penalties include revenue rulings and notices. T.D. 8381 says some revenue procedures also may be treated as rules and regulations for this purpose, depending upon the facts and circumstances.

but

- Taxpayers who take return positions contrary to revenue rulings and notices will not be assessed penalties "if the contrary position has a realistic possibility of being sustained on the merits."

but

- DOJ Tax, IRS ask courts for *Chevron* deference (eligibility for which is premised on the interpretation carrying the "force of law") and maintain that, except for their lack of notice-and-comment rulemaking, revenue rulings are indistinguishable from Treasury regulations for this purpose.

also

- Does it matter that notices can lead to retroactively effective Treasury regulations under I.R.C. § 7805(b)?

IRB Guidance: Key Cases

- Post-*Mead*, most practitioners and scholars assume that revenue rulings, revenue procedures, and notices are interpretative rules or policy statements and that, to the extent these documents are even reviewable, *Skidmore* provides the appropriate standard of review.
  - *Nelson v. Comm'r*, 568 F.3d 662, 665 (8th Cir. 2009): acknowledged that the Supreme Court had not resolved the standard of review for revenue rulings, but applied *Skidmore* as "the framework we follow" in such cases.
  - *Kornman & Assoc., Inc. v. United States*, 527 F.3d 443, 452-57 (5th Cir. 2008): concluded after full consideration that *Skidmore* rather than *Chevron* deference applies to revenue rulings.
  - *Aeroquip-Vickers, Inc. v. Comm'r*, 347 F.3d 173, 181 (6th Cir. 2003): held that *Mead* requires *Skidmore* rather than *Chevron* deference for revenue rulings.
  - *PBS Holdings, Inc. v. Comm'r*, 129 T.C. 131, 144-45 (2007): identified *Skidmore* as the appropriate evaluative standard for revenue rulings.

IRB Guidance: Key Cases

- DOJ routinely asks the courts for *Chevron* deference, and some courts have issued opinions suggesting they may be persuadable.
  - *Tualatin Valley Builders Supply, Inc. v. United States*, 522 F.3d 937, 948 (9th Cir. 2008) (O'Scannlain, J. concurring): the panel majority declined to specify a standard of review, but Judge O'Scannlain agreed with the government that a revenue procedure was entitled to *Chevron* rather than *Skidmore* deference.
  - *See also Texaco Inc. v. United States*, 528 F.3d 703, 711 (9th Cir. 2008): recognizing the government's claim of *Chevron* deference for revenue ruling without deciding the issue, and acknowledging Judge O'Scannlain's opinion in *Tualatin Valley*.
  - *See also Bluetooth SIG Inc. v. United States*, 611 F.3d 617, 622 & n.6 (9th Cir. 2010): concluding that revenue rulings are entitled to at least *Skidmore* deference, and recognizing Judge O'Scannlain's Tualatin Valley opinion.

IRB Guidance: Key Cases

- *Cohen v. United States*, 578 F.3d 1 (D.C. Cir. 2009), *decision vacated and petition for rehearing on banc granted*, 2010 WL 864466 (D.C. Cir. Mar. 11, 2010):
  - A split panel held that a notice was a legally binding substantive (*i.e.*, legislative) rule subject to judicial review for noncompliance with APA procedural requirements, rather than a policy statement exempt from judicial review as non-final agency action.
  - *En banc* oral argument was held September 29, 2010.
  - The D.C. Circuit did not address the issue of judicial deference to IRB guidance in the panel opinion and will have no reason to do so in its *en banc* opinion. Instead, the court is focused on questions concerning the timing of judicial review for APA procedural challenges in tax cases.
  - But if the court reaches a conclusion regarding whether the notice is a legislative rule or a policy statement, that holding could have profound implications for both judicial deference and the applicability of APA notice and comment requirements to IRB guidance documents.

Resource Material

- Thomas W. Merrill & Kristin E. Hickman, Chevron*'s Domain*, 89 Geo. L.J. 833 (2001).
- Kristin E. Hickman, *The Need for* Mead*: Rejecting Tax Exceptionalism in Judicial Deference*, 90 Minn. L. Rev. 1537 (2006).
- Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727 (2007).
- Kristin E. Hickman, *In Search of the Modern* Skidmore *Standard*, 107 Colum. L. Rev. 1235 (2007).
- Kristin E. Hickman, *Of Lenity,* Chevron*, and KPMG*, 26 Va. Tax Rev. 905 (2007).
- Kristin E. Hickman, *A Problem of Remedy: Responding to Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements,* 76 Geo. Wash. L. Rev. 1154 (2008).
- Kristin E. Hickman, *IRB Guidance: The No Man's Land of Tax Code Interpretation*, 2009 Mich. St. L. Rev. 240.

Taxpayer Considerations and Strategies Following *Mayo Foundation*

Strafford Publications Webinar

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Mar. 23, 2011

Review: *Mayo Foundation* clarifies that all tax regulations get *Chevron* deference.

- Even "general authority" regulations (issued under I.R.C. § 7805) receive *Chevron* deference.
- *National Muffler* analysis is no longer applicable.
- Ends the historical distinction between "legislative" (specific authority) and "interpretative" (general authority) regulations.

What “strategies” must taxpayers consider?

- Taxpayers face new tensions in deciding whether to take return positions that may be contrary to “general authority” regulations.
- Increased deference to such regulations heightens the importance of opportunities for administrative advocacy.

Taxpayers face new tensions in deciding whether to take return positions that may be contrary to “general authority” regulations.

The Code imposes penalties on taxpayers for taking positions contrary to regulations.

- **I.R.C. § 6662(b)(1)**: imposes 20-percent penalty on underpayments attributable to negligence or disregard of rules or regulations.

- **Treas. Reg. § 1.6662-3(b)(2)**: includes "intentional" disregard (*i.e.*, if the taxpayer knows of the rule or regulation that is disregarded).

Taxpayers can avoid the penalty by disclosure.

- **Treas. Reg. § 1.6662-3(c)(1)**: no penalty for taking a position contrary to a regulation if the position:
  - (i) is disclosed,
  - (ii) represents a "good faith challenge" to the validity of the regulation, and
  - (iii) has a "reasonable basis."
- *Mayo Foundation* changes the calculus of what constitutes a "good faith challenge" and a "reasonable basis."

Form **8275-R**
(Rev. August 2008)

Department of the Treasury
Internal Revenue Service

Regulation Disclosure Statement

Use this form only to disclose items or positions that are contrary to Treasury regulations. For other disclosures, use Form 8275, Disclosure Statement. See separate instructions.

► Attach to your tax return.

OMB No. 1545-0889

Attachment Sequence No. **92A**

Name(s) shown on return

Identifying number shown on return

Part I **General Information** (see instructions)

(a) Regulation Section	(b) Item or Group of Items	(c) Detailed Description of Items	(d) Form or Schedule	(e) Line No.	(f) Amount
1					
2					
3					
4					
5					
6					

Part II **Detailed Explanation** (see instructions)

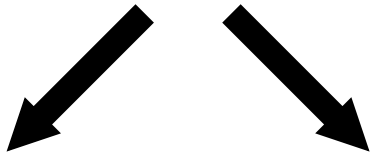
1

Will Schedule UTP render Form 8275-R obsolete for large corporate taxpayers?

- **Rev. Proc. 2011-13**: "complete and accurate disclosure" on Schedule UTP will be treated as if the corporation filed a Form 8275-R
  - **But** the Rev. Proc. also says that it does not apply with respect to penalty for disregarding regulations under section 6662(b)(1).
  - Does "complete and accurate" disclosure on Schedule UTP require the same level of detail as would be required on Form 8275-R?

Mayo changes the calculus in deciding whether to disclose a "contrary" position.

- Will greater deference to agency regulations encourage taxpayers to find ways of not taking positions contrary to regulations?



- Disclose "contrary" position?
  - Invite IRS challenge
  - Face *Chevron* deference
- Reframe position?
  - Don't disclose
  - Risk 20 % penalty

Penalties are also imposed on return preparers for taking positions contrary to rules or regulations.

- **Treas. Reg. § 1.6694-3(c)(1)**: penalty for disregarding a rule includes taking a position that is contrary to a rule or regulation that the preparer knows of, or is reckless in not knowing of.
- **Treas. Reg. § 1.6694-3(e)**: includes the Code, temporary/final regulations, and revenue rulings or notices (other than notices of proposed rulemaking).
- **Treas. Reg. § 1.6694-3(c)(2)**: Can avoid penalties if the position is disclosed and has a reasonable basis.

Penalties for disregarding rules and regulations apply to positions contrary to published guidance.

- **Treas. Reg. § 1.6662-3(b)(2)**: penalty for taking a position contrary to a revenue ruling or a notice.

- But not if the contrary position has a *realistic possibility* of being sustained on its merits.
  - **Notice 90-20**: Approximately one-in-three chance?

Tensions should not be as pronounced for positions contrary to revenue rulings.

- Purpose and procedure of revenue rulings suggest that *Chevron* deference is not appropriate.
  - Notice-and-comment process typically not followed.
  - **Rev. Proc. 2003-1**: revenue rulings are interpretations that apply law to a specific set of facts.
  - **Rev. Proc. 89-14**: the purpose of revenue rulings is to "promote uniform application of the tax laws by Service employees and to assist taxpayers in attaining maximum voluntary compliance."

But countervailing factors suggest courts may give *Chevron* deference to revenue rulings.

- ***Mayo Foundation***: Treasury's general authority under Code Sec. 7805 is a "very good indicator of delegation meriting *Chevron* treatment."
- ***General Motors Corp. v. United States***, 103 AFTR 2d 2009-1354 (D.C. MI. 2009): because revenue rulings are issued under the authority of Sec. 7805, they "should be considered as controlling precedent unless… arbitrary or capricious."
  - *But see* ***Ammex, Inc. v. United States***, 367 F3d 530 (CA-6, 2004), (giving "some level of deference" to a revenue ruling, though not endorsing *Chevron* deference).

Increased deference heightens the importance of opportunities for administrative advocacy.

Chevron "step two" requires an agency to explain its reasoning for issuing regulations.

- ***Motor Vehicle Mfrs Ass'n v. State Farm Mut. Auto. Ins. Co.***, 463 U.S. 29, 50 (1983): "[A]n agency's action must be upheld, if at all, on the basis articulated by the agency itself."
  - *See* ***Manella v. Comm'r***, No. 10-1308 (3d Cir. 2011).

- **5 U.S.C. § 553(c)**: "[T]he agency shall incorporate in the rules adopted a concise general statement of their basis and purpose."

An agency's failure to explain its reasoning may undermine a claim of deference.

- Deference given to administrative agencies "carries with it the correlative responsibility of the agency to explain the rationale and factual basis for its decision, even though we show respect for the agency's judgment in both."
  - ***Bowen v. American Hosp. Ass'n***, 476 U.S. 610 (1986) (using agency's articulated rationale in preamble as basis to invalidate agency regulation).

The required notice-and-comment process creates an opportunity to conduct "discovery".

- Notice-and-comment is an integral part of the justification for giving agencies *Chevron* deference.
- The process can be used to force the agency to articulate (and commit to) its rationale for a particular decision.

- Pushing advocacy outside the courtroom?

Circular 230 Disclaimer

- 31 CFR Part 10, § 10.35, requires us to notify you that any tax advice in this presentation was not intended or written to be used, and cannot be used, for the purpose of avoiding penalties.