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ABA Section of Taxation Report of the Task Force on Judicial Deference

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I. BACKGROUND

Recognizing the need for clearer standards regarding the degree of deference that the federal courts should confer on guidance issued by the Department of Treasury and the Internal Revenue Service, the Tax Section, under the direction of former ABA Section of Taxation Chair Pamela F. Olson, created a Task Force on Judicial Deference in 2000. It was charged with the mission of not only examining the state of the law pertaining to judicial deference across the broad range of administrative pronouncements issued by the Treasury and the IRS, but also sharing its conclusions and possible solutions with the Section of Taxation and the profession at large. Based on the agency-by-agency approach required by the Supreme Court in *United States v. Mead Corporation*, 533 U.S. 218 (2001), the Task Force analyzed the differences in the degree of authority and degree of deliberation underlying the various forms of such guidance and the impact of those differences on whether, and to what degree, judicial deference is appropriate.

In January 2004, the Task Force presented a draft Report to the Tax Section Council. Comments were received from the following Section Committees during the drafting process: Administrative Practice, Affiliated and Related Corporations, Closely Held Businesses, Corporate Tax, Court Procedure and Practice, Employee Benefits, Exempt Organizations, Foreign Activities of U.S. Taxpayers, Individual Income Tax, and Standards of Tax Practice.

II. RECOMMENDATIONS

The Task Force recognizes that in light of *Mead*, which emphasized "the great variety of ways in which the laws invest the Government's administrative arms with discretion, and with procedures for exercising it, in giving meaning to Acts of Congress," *id.* at 235-36, there is a need for an agency-by-agency consideration of the extent to which courts should give deference to administrative pronouncements under the mandate of *Chevron v. Natural Resources Defense Council*, 467 U.S. 837 (1984), which instructs a reviewing court to accept certain administrative interpretations rather than to impose its own interpretations when Congress has not spoken to the precise question at issue.

The Task Force also recognizes that post-*Mead*, there is a great deal of confusion regarding the application of *Chevron* and a particular need to develop a clear set of deference concepts for interpretations of the tax law because of, *inter*

alia: (1) the power and pervasiveness of the IRS, (2) the large number and variety of administrative pronouncements issued by the IRS, and (3) the Supreme Court's continuing reliance in its tax cases on the traditional test of *National Muffler Association v. United States*, 440 U.S. 472 (1978), rather than on *Chevron*.

The recommendations of the Task Force can be summarized as follows:

1. Federal courts should give *Chevron* deference to regulations promulgated by the Treasury and the IRS, with (i) legislative tax regulations receiving controlling deference under *Chevron* so long as they are not arbitrary, capricious, or manifestly contrary to the statute, and (ii) interpretive tax regulations receiving the same controlling deference if they are reasonable under the test of *National Muffler*, which examines such factors as the extent to which the regulation harmonizes with the plain language, origin, and purpose of the statute; the manner in which the regulation evolved; the length of time the regulation has been in effect; the reliance placed on it; the consistency of interpretation; and the degree of scrutiny Congress has devoted to the regulation;

2. Federal courts should give temporary regulations the same deference as described above, provided that the promulgation of such regulations meets the good cause standards as specified in the Administrative Procedure Act for promulgating regulations without notice and comment;

3. Federal courts should give revenue rulings, certain revenue procedures, and notices, deference under the doctrine of *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), which directs courts to take into account the agency's experience and its power to persuade, but to retain the ability to choose a better rule even if the agency interpretation is reasonable; and

4. Federal courts should take into account unofficial agency interpretations, such as private letter rulings, technical advice memoranda, and litigating positions, only to the extent to which their logic and reasoning appeal to the reviewing court.

III. REPORT

PART I: DISCUSSION OF RECOMMENDATIONS

A. *Introduction: Judicial Deference to Agency Pronouncements*

In our modern administrative state, the degree of deference that federal courts owe to administrative pronouncements is a vexing issue, one frequently scrutinized by the Supreme Court.[1] Regular attention from the Supreme Court, how-

[1]For a discussion of general policy issues regarding deference to administrative agencies, see John F. Manning, *Constitutional Structure and Judicial Deference to Agency Interpretation of Agency Rules*, 96 COLUM. L. REV. 612 (1996); Cass R. Sunstein, *Law and Administration after Chevron*, 90 COLUM. L. REV. 2071 (1990).

ever, has failed to produce clarity for administrative law, in general, or for tax law, in particular. The recent case of *United States v. Mead Corporation*, 533 U.S. 218 (2001), in which the Supreme Court addressed in detail the issue of deference to administrative agencies, introduced further confusion. *Mead* seems to have curtailed the reach of *Chevron v. Natural Resources Defense Council*, 467 U.S. 837 (1984),[2] under which administrative interpretations are entitled to a high degree of deference when Congress has not addressed the precise question at issue, and to give renewed prominence to the test of *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), under which the degree of deference a court gives to an administrative interpretation can vary depending upon a variety of factors.[3] *Skidmore*, unlike *Chevron*, allows the reviewing court to choose a better rule even if the agency interpretation is reasonable.

Before *Mead*, it seemed that a court reviewing an administrative pronouncement had to choose between affording an agency *Chevron* deference or giving the agency's interpretation no deference at all. After *Mead*, the options have expanded: *Chevron* deference, *Skidmore* deference, or no deference. *Mead*, however, offers no clear guidance as to how or when a court must choose between the *Chevron* and *Skidmore* standards. In *Mead*, the Supreme Court held that a tariff classification ruling issued by the United States Customs Service was not entitled to judicial deference under *Chevron*, but was "eligible to claim respect according to its persuasiveness," under *Skidmore*. *Mead*, 533 U.S. at 221. The Court held that "administrative implementation of a particular statutory provision qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law and that

[2]Under *Chevron*, the issue of deference arises only if Congress has not addressed the issue:

> First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, . . . the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous . . . the question for the court is whether the agency's answer is based on a permissible construction of the statute.

467 U.S. at 843-44 (citations omitted). Under step one of the *Chevron* two-step approach, courts can and do invalidate administrative pronouncements they find inconsistent with the statute, without reaching the issue of deference. For a recent step-one tax case, which invalidated a regulation dealing with disclosure of exempt organization determinations, see *Tax Analysts v. Internal Revenue Service*, 350 F.3d 100, 102-105 (D.C. Cir. 2003). This Report is limited to the issues involved when a court reaches step two of *Chevron*. The Report does not, moreover, discuss the issues that arise when a court interprets a statute prior to any agency interpretation. For a discussion of this latter set of issues, see Gregg Polsky, *Can Treasury Overrule the Supreme Court?*, 84 B. U. L. REV. (forthcoming 2004).

[3]*Skidmore* speaks of "the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade. . . ." *Skidmore*, 323 U.S. at 140. *Mead* lists "the merit of [the] writer's thoroughness, logic, and expertness, its fit with prior interpretations, and any other sources of weight" as factors under *Skidmore*. *Mead*, 533 U.S. at 235.

the agency interpretation claiming deference was promulgated in the exercise of that authority." *Id.* at 226-27. The opinion continues, "Delegation of such authority may be shown in a variety of ways, as by an agency's power to engage in adjudication or notice-and-comment rulemaking, or by some other indication of a comparable congressional intent." *Id.* It does not define what "some other indication" might be.[4]

Mead suggests that the result should turn on the intention of Congress on an agency-by-agency basis. The opinion recognizes that there are limits on the judiciary's ability to lay down rules of general application regarding deference to administrative agencies. As Justice Souter wrote, an "inescapable feature of the body of congressional legislation authorizing administrative action" is "the great variety of ways in which the laws invest the Government's administrative arms with discretion, and with procedures for exercising it, in giving meaning to Acts of Congress." *Mead*, 533 U.S. at 235-36. Similarly, a leading administrative law scholar recently wrote that "to really begin to understand agency interpretive practice" requires "case studies of individual agencies or programs by scholars who understand the substantive fields."[5] This Report presents such an analysis for the IRS/Treasury.

Ironically, it is uncertain whether *Mead* and *Chevron* will be the primary authorities governing the tax law. In tax cases, the Supreme Court has relied instead on a separate line of Supreme Court tax jurisprudence asking whether a tax regulation is reasonable.[6] The fullest statement of this reasonableness test came in *National Muffler Association v. United States*, 440 U.S. 472 (1978). Upholding a denial of tax exemption for a trade association pursuant to standards described in a regulation under section 501(c)(6), *National Muffler* tested the reasonableness of the regulation according to such factors as the extent to which the regulation harmonizes with the plain language, origin, and purpose of the statute; the manner in which the regulation evolved; the length of time the regulation had been in effect; the reliance placed on it; the consistency of interpretation; and the degree of scrutiny Congress had devoted to it. 440 U.S. at 477. *National Muffler* concluded that although the regulation at issue in the case was "not the only possible" reading of the statutory language, it merited "serious

[4]*Mead* also introduces uncertainty regarding the continued viability of *Bowles* v. *Seminole Rock & Sand Co.*, 325 U.S. 410 (1945), and its progeny, under which a court must defer to an administration agency's interpretation of its own regulation. *Seminole Rock*, 325 U.S. at 413-14. *Mead* fails to discuss the relationship of this line of cases to the rules it announces. For further discussion of *Seminole Rock*, *see infra* Part II, Section B.

[5]Jerry L. Mashaw, *Agency and Statutory Interpretation*, ISSUES IN LEGAL SCHOLARSHIP, Symposium on Dynamic Statutory Interpretation (2002), *available at* http://www.bepress.com/ils/iss3/art9/, p. 26 (last visited Feb. 24, 2004). *See also* Peter L. Strauss, *Teaching Administrative Law: The Wonder of the Unknown*, 33 J. LEGAL ED. 1, 8 (1983) (discussing view of some administrative law scholars and practitioners that administrative law must be considered and studied agency by agency).

[6]In one case, United States v. Boyle, 469 U.S. 241 (1985), the Court did cite *Chevron* in deferring to an IRS regulation. *Boyle*, 469 U.S. at 246 n.4. As discussed *infra* note 112, the case does not represent a switch from *National Muffler* to *Chevron*.

deference" under the factors listed, *id.* at 484, and that "[t]he choice among reasonable interpretations is for the Commissioner, not the courts," *id.* at 488.

Lower courts confronting the validity of interpretations of the tax law issued by the Internal Revenue Service, the Justice Department, or the Treasury (hereinafter collectively the "IRS") have been and continue to be confused.[7] Despite a lack of consistency in the case law, a set of principles emerges from the cases that can and should guide courts in deciding the level of deference owed to IRS interpretations of the tax law. As discussed further in the following sections of this Report, these principles are based on (1) the nature and role of the agency that administers this area of law, (2) the extent to which an agency interpretation has the force of law, and (3) the degree of deliberation and care that an agency puts into making an interpretation. Applying these principles, the recommendations undertake to balance the needs of the agency, the demands of tax policy, the rights of taxpayers, and the role of the courts.

B. *The Nature and Role of the IRS*

The tax law permeates every aspect of life, both business and personal. The IRS touches the lives of almost every American. For calendar year 2002, for example, Americans filed 118,538,000 individual tax returns.[8] In many ways, the pervasiveness of the IRS seems to argue for a high level deference to its interpretations. Certainty regarding tax rules is particularly important when so many citizens must comply and file returns that are consistent with them. To aid taxpayers, the IRS issues a staggering array of guidance documents, and does so in large numbers.[9]

A general policy of deference, moreover, would increase the likelihood of national uniformity regarding the meaning of the tax laws by decreasing the likelihood that courts would adopt differing views with respect to the meaning of particular provisions of the Code. A policy favoring deference also could encourage the IRS to issue as much guidance as possible.

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[7]*See infra* Part II, Section E of this Report.

[8]IR-News Rel. 2003-59, 2003 TAX NOTES TODAY 86-97 (May 5, 2003).

[9]In 2000, Tax Analysts published a draft inventory of IRS Guidance documents that included 39 distinct categories. *Inventory of IRS Guidance Documents—A Draft,* 88 TAX NOTES (TA) 305 (July 17, 2000). The annual quantities in recent years of the types of documents that are discussed later in this Report are as follows. For each type of document, a cite to the final document published in each year is also provided:

In 2001: 66 revenue rulings, *see* 2001-53 I.R.B. 637; 61 revenue procedures, *see* 2001-53 I.R.B. 653; 84 notices, *see* 2001-53 I.R.B. 642; and 124 announcements, *see* 2001-52 I.R.B. 630.

In 2002: 91 revenue rulings, *see* 2002-52 I.R.B. 991; 75 revenue procedures, *see* 2002-52 I.R.B. 997; 115 notices, *see* 2002-52 IRB 999; and 80 announcements, *see* 2002-51 IRB 980.

In 2003: 128 revenue rulings, *see* 2003-52 I.R.B. 1247; 86 revenue procedures, *see* 2003-50 I.R.B. 1211; 89 announcements, *see* 2003-52 I.R.B. 1256; 81 notices, *see* 2003-51 I.R.B. 1223.

In both 2001 and 2002, the IRS released to the public some 2,000 private letter rulings and in 2003, more than 1800 private letter rulings (based on a search of "administrative rulings; private letter rulings" in the Tax Notes Today file of LEXIS from Jan. 1, 2001 to Dec. 31, 2001; from Jan. 1, 2002 to Dec. 31, 2002; and from Jan. 1, 2003 to Dec. 31, 2003, respectively). As is discussed *infra*, private letter rulings are addressed to individual taxpayers. Before being released to the public, the rulings are redacted to eliminate names and other identifying information.

Many of the factors which the Supreme Court has identified as favoring deference to administrative agencies, in general, apply as well to the IRS. *Skidmore* speaks of agencies possessing "specialized experience and broader investigations and information than is likely to come to a judge in a particular case."[10] 323 U.S. at 139. In *Barnhart v. Walton*, 535 U.S. 212, 222 (2002), a post-*Mead* deference case, the Court lists a half a dozen factors, including "the related expertise of the agency" and "the complexity of . . . administration" as important factors calling for *Chevron* deference. These factors all favor deference toward IRS interpretations.

But another set of factors argues in favor of a cautious approach to a grant of broad deference. First, the IRS has some inherent advantages over taxpayers. For example, in judicial proceedings, the assessment or determination of the IRS is presumed to be correct.[11] Prior to 1998, the taxpayer had the burden to supply prima facie evidence contrary to the IRS's position in order to go forward with a case, as well as the ultimate burden of persuasion on the merits of the issue.[12] Only recently has Congress shifted some of the burden of proof onto the IRS. In 1998, Congress adopted section 7491 in response to the concern that "individual and small business taxpayers frequently are at a disadvantage when forced to litigate with the Internal Revenue Service."[13] It remains to be seen, however, whether this shift of the ultimate burden of factual proof to the IRS will have much of an effect. For example, the new rule does not apply to most significant corporate, partnership and trust deficiencies, in view of the $7 million net worth

[10]It has been suggested that Tax Court judges, many with IRS experience or otherwise experienced in tax practice, are less likely to defer to IRS interpretations than are generalist judges in the federal courts. Linda Galler, *Judicial Deference to Revenue Rulings: Reconciling Divergent Standards*, 56 OHIO ST. L.J. 1037, 1075-76 (1995).

[11]Welch v. Helvering, 290 U.S. 111, 115 (1933) ("[The Commissioner's] ruling has the support of a presumption of correctness, and the petitioner has the burden of proving it to be wrong").

[12]*See* Danville Plywood Corp. v. United States, 16 Cl. Ct. 584, 593-94 (1989). The 1998 Joint Committee Bluebook quotes the following explanation from *Danville* with approval: "This presumption in favor of the Commissioner is a procedural device that requires the plaintiff to go forward with prima facie evidence to support a finding contrary to the Commissioner's determination. Once this procedural burden is satisfied, the taxpayer must still carry the ultimate burden of proof or persuasion on the merits. Thus, the plaintiff not only has the burden of proof of establishing that the Commissioner's determination was incorrect, but also of establishing the merit of its claims by a preponderance of the evidence." J. COMM. ON TAX'N, 105TH CONG., GENERAL EXPLANATION OF TAX LEGIS. ENACTED IN 1998, 56 (1998).

[13]S. REP. NO. 105-174, at 44-46 (1998). This new section shifts the burden of proof on the factual issue to the IRS, as long as the taxpayer satisfies certain criteria. If the taxpayer introduces any "credible evidence" with respect to a factual issue in question, complies with substantiation requirements, maintains adequate records, cooperates with reasonable IRS requests for information, and is either a business with a net worth of $7 million or less or an individual, the burden of proof on that factual issue will then shift to the IRS. Credible evidence is described as "the quality of evidence which, after critical analysis, the court would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted (without regard to the judicial presumption of IRS correctness)." *Id.* at 45. "[I]mplausible factual assertions, frivolous claims or tax protestor-type arguments" are not credible evidence. *Id.*

limit. Moreover, early cases under section 7491 suggest that the results under the new statute do not change.[14]

Another advantage for the IRS is case law requiring that taxpayers fall squarely within a provision that grants a deduction or credit. As the Supreme Court observed in *INDOPCO v. Commissioner*, 503 U.S. 79 (1992), "In exploring the relationship between deductions and capital expenditures, this Court has noted the 'familiar rule' that an income tax deduction is a matter of legislative grace and that the burden of clearly showing the right to the claimed deduction is on the taxpayer." 503 U.S. at 84. *See also* Bingler v. Johnson, 394 U.S. 721 (1969) (recognizing the "principle that exemptions from taxation are to be construed narrowly"). Indeed, it would be inconsistent with *Mead's* call for an agency-by-agency analysis to ignore the advantage of the IRS in this regard.

Second, a general policy of broad deference seems unjustified in view of the very large, almost punitive, amounts of penalties, as well as interest charges that go well beyond time value of money considerations, that often accumulate in large tax cases and which can far exceed the original deficiency. The IRS's ability to impose confiscatory penalties and rates of interest not consistent with time value concepts warrants caution in applying deference to agency pronouncements.[15] The problem may become more severe since there are bills pending before Congress that threaten to impose no-fault penalties of 40%.[16] The Task Force believes that few, if any, other agencies can and do assert penalties of such magnitude and frequency as the IRS.[17]

Third, and most important, the primary purpose of the IRS is to raise money for the government.[18] "[T]he major responsibility of the Internal Revenue Ser-

[14]*See, e.g.*, Okerlund v. Commissioner, 53 Fed. Cl. 341, 355-56 (2002); Hunt & Sons, Inc. v. Commissioner, 83 T.C.M. (CCH) 1345, 1347-48, 2002 T.C.M. (RIA) ¶ 2002-65, at 366; Estate of True v. Commissioner, 82 T.C.M. (CCH) 27, 2001 T.C.M. (RIA) ¶ 2001-167. In a recent case, however, the Court of Appeals for the Eighth Circuit interpreted section 7491 as having a more far-reaching effect, requiring the Tax Court to analyze critically the taxpayer's evidence and explain its findings on the credibility of that evidence. Griffin v. Commissioner, 315 F.3d 1017, 1021 (8th Cir. 2003); *see also* Stephen G. Salley & Anthony J. Scaletta, *The Incredible Taxpayer: The U.S. Tax Court and I.R.C. § 7491*, 77 FLA. BAR J. 80, 82 (2003).

[15]As a general matter, interest assessed on underpayments is meant to compensate the government for the use of its tax dollars and, thus, is considered in the nature of compensation rather than penalty. This is not the case, however, with respect to so-called "hot interest," which is punitive in nature and, thus, functions as both an interest charge and a penalty. In the case of C corporations, the underpayment rate is increased by two percentage points with respect to any tax in excess of $100,000. I.R.C. § 6621(c). Moreover, the enhanced rate applies not only to the underlying tax, but also to any interest, penalties, additional amounts, and additions to tax imposed with respect to the underlying tax. Reg. § 301.6621-3(b)(2)(i). *See* Burgess J. W. Raby & William L. Raby, *Corporate Deficiency Rate Now Four Times the Refund Rate*, 2003 TAX NOTES TODAY 190-37 (Oct. 6, 2003).

[16]*See, e.g.*, S. 476, 108th Cong., § 704 (2003) (adding section 6662B "Penalty for Understatements Attributable to Transactions Lacking Economic Substance, etc.").

[17]It is noteworthy in this regard that judicial deference is not applied in the criminal area and presumably is not applied with respect to the imposition of financial penalties for criminal tax fraud. *See* Dan M. Kahan, *Is* Chevron *Relevant to Federal Criminal Law?*, 110 HARV. L. REV. 469 (1996).

[18]The IRS, perhaps uniquely among federal agencies, justifies its staff and budget requests by how much money it collects. *See Hearings Before the Subcomm. on Treasury, Postal Service, & General Gov't, of the Sen. Comm. on Appropriations*, 104th Cong., 688, 701 (1995); *see also* Gary L. Rodgers, *The Commissioner "Does Not Acquiesce,"* 59 NEB. L. REV. 1001, 1024 n.162 (1980).

vice is to protect the public fisc." United States v. Hughes Properties, Inc., 476 U.S. 593, 603 (1986). This unique purpose, in litigation outside the Tax Court, gives rise to unique laws as to administrative procedure. The Supreme Court in *Bull v. United States*, 295 U.S. 247, 259-60 (1935), recognized the unique nature of our tax assessment and collection system:

> [T]axes are the life-blood of government, and their prompt and certain availability an imperious need. . . . Thus the usual procedure for the recovery of debts is reversed in the field of taxation. Payment precedes defense. . . . The assessment supersedes the pleading, proof and judgment necessary in an action at law, and has the force of such a judgment. . . . The taxpayer often is afforded his hearing after judgment and after payment, and his only redress for unjust administrative action is the right to claim restitution.

This function of the IRS may encourage the agency to issue rulings or to promulgate regulations that test the outer limits of reasonableness. Courts have scolded the IRS for twisting laws to further revenue collections rather than Congressional purpose. *See e.g.*, Estate of Clayton v. Commissioner, 976 F.2d 1486, 1499 (5th Cir. 1992) ("Such an arbitrary and unsupported misconstruction of the statute . . . can only be explained as overzealousness in revenue collection"). As one commentator has observed: "As the nation's revenue collector . . . the IRS should be expected to construe statutes in a light most favorable to the collection of tax dollars. Deference in these circumstances deprives taxpayers of an opportunity to convince a neutral arbiter that the government's position is wrong."[19]

The IRS's stated mission has changed somewhat over the years. Until recently, the IRS Mission Statement emphasized its collection function:

> The purpose of the Internal Revenue Service is to collect the proper amount of tax revenue at the least cost; serve the public by continually improving the quality of our products and services; and perform in a manner warranting the highest degree of public confidence in our integrity and fairness.[20]

In connection with the IRS Restructuring and Reform Act of 1998, however, Congress became concerned with IRS's "lack of appropriate attention to taxpayer needs" and mandated that "a key part of the IRS mission must be taxpayer service."[21] As a result, in 1999, the IRS announced a revised mission statement: "Provide America's taxpayers top quality services by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all."[22]

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[19]Galler, *supra* note 10, at 1070-71.

[20]According to IR-News Rel. 1998-59 (Sept. 24, 1998), in which the IRS unveiled a new mission statement, the previous version dated from the 1980's.

[21]S. REP. No. 105-174, at 8 (1998).

[22]Internal Revenue Service, *The Agency and Its Mission*, *available at* http://www.irs.gov/irs/article/0,,id=98141,00.html (last visited Feb. 24, 2004).

The current IRS Commissioner, Mark W. Everson, is trying to balance collection and service. In announcing his confirmation by the Senate on May 1, 2003, the IRS proclaimed that Mr. Everson's "priorities include strengthening enforcement of the tax laws and improving services for taxpayers."[23] The Commissioner's chief of staff recently reiterated the need to balance collection and service when he described a "widespread consensus" within the IRS that the agency should focus on compliance, as well as customer service. These statements reflect that, realistically, the need to collect revenue neither can nor should be dismissed by the IRS.

In sum, some factors, such as the broad reach of the tax laws, the need for national uniformity, the complexity of the tax law, and the expertise of the IRS, quite clearly call for deference to the IRS, but others, such as the presumption of correctness for IRS determinations, the narrow reading of statutory deductions or credits, the size of possible penalties, and the revenue-raising function of the IRS, caution against it. This mixed set of factors supports a set of guidelines under which the degree of judicial deference should vary with different forms of agency guidance.

C. *Force of Law*

Under *Mead*, deciding whether an agency pronouncement merits *Chevron* deference requires an analysis both of Congressional intent to delegate authority to make rules carrying the force of law and of the agency's intent to adopt rules in the exercise of that authority. *Mead*, 533 U.S. at 226-27. The Supreme Court, however, provided no bright line test for determining whether Congress has made the requisite delegation of authority. Justice Scalia suggested in his *Mead* dissent that the Court's omission in this regard would lead to "protracted confusion." 533 U.S. at 245 (Scalia, J., dissenting). Such confusion certainly is the case for tax law.

In general. Professor Thomas Merrill and Kathryn Watts recently suggested that, at one time, Congress operated under a convention which provided a bright line test for force of law: rules or regulations have the force of law if the relevant statute specifically says so, or if Congress provided for penalties or other sanctions when rules or regulations are not followed.[24] According to Merrill and

[23] Joe Thorndike, *IRS Official Says Agency Will Emphasize Enforcement*, 99 TAX NOTES (TA) 1598 (June 16, 2003); Heidi Glenn, *Everson's IRS to Balance Service and Enforcement*, 101 TAX NOTES (TA) 465 (Oct. 27, 2003). Echoing the Commissioner's sentiments, Acting Deputy Commissioner of the IRS Large and Midsize Business Division Frank Y. Ng recently remarked, "There is a need for us to rebalance enforcement." Ng explained that both enforcement and service are a priority in addressing the IRS's overall agenda. Kenneth A. Gary & Sirena J. Scales, *Enforcement, Guidance Remain Priorities, IRS Officials Say*, 101 TAX NOTES (TA) 1378 (Dec. 22, 2003); *see also* Kenneth A. Gary, *IRS Officials Echo Everson: Quicken Audit Cycle, Push Enforcement*, 101 TAX NOTES (TA) 699 (Nov. 10, 2003). As a result of a reorganization in the Commissioner's office, there is now a new position, "Deputy Commissioner for Services and Enforcement." *See, e.g.*, T.D. 9095, 68 Fed. Reg. 65,634 (2003).

[24] Thomas W. Merrill & Kathryn Tongue Watts, *Agency Rules with the Force of Law: The Original Convention*, 116 HARV. L. REV. 467 (2002).

Watts, the convention took into account both explicit statements in the legislation and whether the statutory scheme provided for penalties or sanctions for noncompliance.

Early tax laws seem to have followed this convention. The early revenue laws expressly provided for rules with force of law.[25] The Act of July 14, 1870 gave the Secretary of the Treasury the power "to make all needful rules or regulations . . . which shall have the force of law."[26] Subsequently, in the Revenue Acts of 1917, 1918 and 1921, Congress attached penalties for failure "to make any returns required by regulations." In contrast, no sanctions were provided for failure to comply with rules promulgated under the predecessor to section 7805(a), which was first adopted in 1921.

But the convention that Merrill and Watts describe no longer is followed by the courts and, were it to be resurrected, would not work well in the case of the modern tax law. The Code was eventually amended to impose penalties for "negligence or disregard of rules and regulations;" these penalties are now provided for in section 6662. According to the regulations, rules for this purpose include revenue rulings and notices. Reg. § 1.6662-3(b)(2). Several exceptions apply to the negligence and disregard penalties, however, most notably where a taxpayer's position "has a realistic possibility of being sustained on its merits."[27] Reg. § 1.6662-3(c)(3). This limited form of penalty—penalizing a taxpayer who disregards rules and regulations only if there is not a realistic probability of the taxpayer's position prevailing—may fall short of a sanction rising to the force of law. The convention described by Merrill and Watts, then, would not settle the issue of whether Congress intended such IRS interpretations as revenue rulings, revenue procedures, and notices to have "force of law," as that phrase was applied in *Mead*.[28]

As described below, the situation becomes yet more complicated when *Mead's* additional requirement that an agency interpretation claiming deference must be promulgated in the exercise of its delegated authority to make rules having the force of law is applied to the varied forms of guidance issued by the IRS.

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[25]Much of the history that follows was developed in Merrill & Watts, *supra* note 24.

[26]Ch. 255, § 34, 16 Stat. 256, 271.

[27]"A position is considered to have a realistic possibility of being sustained on its merits if a reasonable and well-informed analysis by a person knowledgeable in the tax law would lead such a person to conclude that the position has approximately a one in three, or greater, likelihood of being sustained on its merits." Reg. § 1.6694-2(b)(1). Thus, no penalty would be applied to a taxpayer who disregards a revenue ruling or notice and expects to lose a challenge to her position, so long as her tax adviser reasonably believes in good faith that the likelihood of prevailing is at least one in three.

[28]Indeed, Merrill and Watts acknowledge that the convention they find in the historic record has disappeared, both in administrative law generally and in tax law. For most agencies, a general grant of rulemaking power has come to be seen as a grant of authority to promulgate rules with the force of law; such has not been the common understanding with respect to section 7805(a). Merrill and Watts suggest that this is based on the influence of writings by tax giants Erwin Griswold and Stanley Surrey rather than adherence to the "force of law" convention, which turned on the presence of absence of sanctions for violation. *See* Merrill & Watts, *supra* note 24, at 570-78.

Regulations. The Administrative Procedure Act (APA) defines a "rule" as "the whole or part of an agency statement of general or particular applicability and future effect designed to implement, interpret, or prescribe law or policy or describing the organization, procedure, or practice requirements of an agency." 5 U.S.C. § 551(4). The APA requires agencies to follow notice-and-comment procedures when they promulgate rules that bind the public. 5 U.S.C. § 553(b). In administrative law generally, such binding rules are known generally as legislative rules or regulations. The APA explicitly exempts from the notice-and-comment requirements "interpretative rules, general statements of policy, or rules of agency organization, procedure, or practice." *Id.*[29] In the case of regulations, tax law has used a different basis to distinguish between legislative and interpretive rules. In tax, legislative regulations are those promulgated pursuant to a specific grant of authority under some provision of the Internal Revenue Code.[30] Interpretive regulations are those promulgated under the general authority of section 7805(a), which directs the Secretary of the Treasury "to prescribe all needful rules and regulations for the enforcement of this title."[31] In promulgating interpretive regulations, the IRS invariably specifies that "section 553(b) of the Administrative Procedure Act (5 U.S.C. § 553) does not apply to these regulations."[32] At the same time, however, it is the customary practice of the IRS to follow notice-and-comment procedures for interpretive regulations.[33] Temporary regulations, whether legislative or interpretive, are issued without notice and comment.

Thus, the IRS does not claim to be exercising its authority to act with the force of law when it promulgates interpretive regulations. It does, nonetheless, use notice and comment. Moreover, failure to follow interpretive tax regulations

[29]Rules that otherwise would be subject to notice-and-comment rules also are exempt when the agency, for good cause, finds that the notice-and-comment procedure is "impracticable, unnecessary, or contrary to the public interest." 5 U.S.C. § 553(b). Issuance of temporary regulations generally is thought to come within this exception. *But see* Michael Asimow, *Public Participation in the Adoption of Temporary Regulations*, 44 TAX LAW. 343 (1991), and the discussion of temporary regulations, *infra.*

[30]*See* Ellen P. Aprill, *Muffled Chevron: Judicial Review of Tax Regulations*, 3 FLA. TAX REV. 51, 55-57 (1996).

[31]The Supreme Court has recognized the distinction between these two kinds of tax regulations. *See, e.g.*, United States v. Vogel Fertilizer Co., 455 U.S. 16, 24 (1982); *see also infra* Part II, Section D. The IRS has never asserted that section 7805(a) grants authority to issue legislative regulations, although similar language in other (non-tax) statutes has been deemed to do so.

[32]*See*, e.g, T.D. 9043, 68 Fed. Reg. 11,313 (2003). Section 30(15) of the Internal Revenue Manual, which comprises the Regulations Drafting Handbook, is consistent on this point: "5 U.S.C. 553(b) requires that a notice of proposed rulemaking be published in the Federal Register and that interested persons be given the opportunity to comment on the proposed regulations before final regulations are adopted. . . . However, these requirements do not apply if the rules are interpretative."

[33]For recent examples, *see* Supplemental Proposed Regulations on Equity Split Dollar Life Insurance, 68 Fed. Reg. 24,898 (2003); Proposed Regulations on Changes in Accounting Method, 68 Fed. Reg. 25,310 (2003); Proposed Regulations on Private Activity Bond Definition, 68 Fed. Reg. 25,845 (2003). To its credit, the IRS has often expanded the notice and comment period by announcing that it intended to issue proposed regulations, and inviting comments even before the proposed regulations are published. *See, e.g.*, Advance Notice of Proposed Rulemaking on Credit for Increasing Research Authority, 69 Fed. Reg. 43 (2004).

can give rise to penalties. Furthermore, Regulation section 601.601(a)(1) states: "Internal Revenue rules take various forms. The most important rules are issued as regulations and Treasury decisions prescribed by the Commissioner and approved by the Secretary or his delegate." This characterization does not distinguish between legislative and interpretive regulations.

Revenue Rulings and Revenue Procedures. Revenue rulings and revenue procedures, in contrast, clearly fit within the definition of interpretive rules in the APA.[34] The IRS traditionally has not taken the position that revenue rulings or revenue procedures have the force of law.[35] Originally, the IRS explicitly disavowed the binding nature of its rulings, suggesting that rulings published in the Internal Revenue Bulletin merely indicated a "trend," that revenue rulings "do not commit" the agency, and that rulings be viewed as "aids in studying" the law.[36] Nor does the IRS currently claim that its revenue rulings and revenue procedures have the force of law. The weekly Internal Revenue Bulletin states explicitly that revenue rulings and revenue procedures "do not have the force and effect of Treasury Department Regulations, but they may be used as precedents." Each Bulletin then cautions:

> In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

Under the current revenue rulings program, which began in 1953,[37] the IRS describes a revenue ruling as "an official interpretation by the Service that has been published in the Internal Revenue Bulletin." Reg. § 601.601(d)(2)(i)(a); Rev. Proc. 2003-1, 2003-1 I.R.B. 1. Revenue rulings are issued only by the IRS National Office. The IRS originally intended the 1953 program to serve three purposes. First, revenue rulings would be a vehicle through which the National Office could inform field personnel of precedents or guiding positions. Second, the Internal Revenue Bulletin, in which revenue rulings are published, would

[34]*See* Robert A. Anthony, *Which Agency Interpretations Should Bind Citizens and the Courts*, 7 YALE J. ON REG. 1, 44 n.204 (1990). Because revenue rulings are "classic examples" of interpretive rules, they are exempt from notice-and-comment issuance procedures. *See* Johnson City Medical Center v. United States, 999 F.2d 973, 980 (6th Cir. 1993) (Batchelder, J., dissenting); Northern Illinois Gas. Co. v. United States, 743 F.2d 539, 541 n.3 (7th Cir. 1984); Wing v. Commissioner, 81 T.C. 17, 27 (1983).

[35]In recent cases, the IRS argued, unsuccessfully, that revenue rulings and revenue procedures are likely entitled to deference under the *Chevron* doctrine. See *Aeroquip-Vickers, Inc. v. Commissioner*, 347 F.3d 173 (6th Cir. 2003), for revenue rulings and *Fed. National Mortgage Ass'n v. United States*, 56 Fed. Cl. 228, 234-35 (2003), for revenue procedures.

[36]*See* Internal Revenue Bulletin for January-June, 1924 (C.R. III-1), issued shortly after the agency was given authority to issue all needful rules and regulations.

[37]*See* Rev. Rul. 2, 1953-1 C.B. 484.

provide a permanent, indexed reference to IRS positions. Third, revenue rulings would enable the public to review intragency communications that the IRS uses as precedents or guides.[38] In 1989, the Service revised its description of the purposes of the revenue rulings program, as simply promoting uniform application of the tax laws and assisting taxpayers in attaining maximum voluntary compliance.[39]

A revenue procedure, according to the official IRS definition, is "a statement of procedure that affects the rights or duties of taxpayers or other members of the public under the Code and related statutes or information that, although not necessarily affecting the rights and duties of the public, should be a matter of public knowledge." Reg. § 601.601(d)(2)(i)(b); Rev. Proc. 2003-1, 2003-1 I.R.B. 1, 2. The revenue procedure program was established in 1955.[40] At that time, the IRS explicitly distinguished revenue procedures from revenue rulings, the latter pertaining to "substantive tax law," as opposed to "internal practices or procedures."[41]

In recent years, however, the IRS seems to have expanded the function of revenue procedures. For example, Regulation section 1.6011-4(b)(8)(i) provides that a transaction will not be considered a transaction within the categories that must be reported to the IRS if the Commissioner makes a determination by published guidance that the transaction is not subject to the reporting requirements. The IRS has chosen to use revenue procedures to issue such published guidance. *See* Rev. Proc. 2003-24, 2003-1 C.B. 599; Rev. Proc. 2003-25, 2003-1 C.B. 601.

Notices. Unlike revenue rulings and revenue procedures, both the history and purpose of notices are obscure. No Treasury regulation prescribes or describes notices. The Internal Revenue Bulletin, in which most notices are published, is silent on their substantive impact, stating only that "[r]ulings and procedures . . . may be used as precedents."[42] Equally silent is Revenue Procedure 2003-1, which provides only that "[t]he Service provides guidance in the form of letter rulings, closing agreements, determination letters, information letters, revenue rulings and oral advice." 2003-1 I.R.B. 1, 2.

Other official sources provide a little more insight. The Chief Counsel Publication Handbook describes the various purposes of a notice, including substantive guidance:

[38]Rev. Rul. 2, 1953-1 C.B. 484; *see also* Sandor v. Commissioner, 62 T.C. 469, 481 (1974) (noting that the purpose of publication of revenue rulings is to promote uniform application of tax laws by Service employees), *aff'd*, 536 F.2d 874 (9th Cir. 1976).

[39]Rev. Proc. 1989-14, 1989-1 C.B. 814, 814-15.

[40]Rev. Proc. 1955-1, 1955-2 C.B. 897.

[41]*Id.*

[42]*See, e.g.*, 2003-26 I.R.B. 2.

> A notice is a public pronouncement that may contain guidance that involves substantive interpretations of the Code or other provisions of the law. Notices may also be used for materials that would be appropriate for an announcement but for the need to preserve the guidance in the Cumulative Bulletin. For example, notices can be used to relate what regulations will say in situations where the regulations may not be published in the immediate future.

I.R.M. 30.15.10.

The IRS web site suggests that a notice can, in some cases, contain "guidance that involves substantive interpretation."[43] A recent Chief Counsel Notice concludes that a notice provides "final guidance," which precludes Chief Counsel attorneys from arguing a case contrary to a notice.[44] In addition, taxpayers may rely on notices for penalty avoidance purposes under Regulation section 1.6661-3(b)(2) (the "administrative pronouncement" rule). *See* Phillips Petroleum Co. v. Commissioner, 101 T.C. 78 (1993).

Commentators say very little about notices. Michael Saltzman's IRS procedure treatise discusses a litany of guidance types, from revenue rulings to information letters, but never mentions notices.[45] Another treatise contains only a brief description of notices:

> In recent years, in lieu of releasing time-consuming revenue rulings and revenue procedures, the Service has been relying heavily on notices, announcements, and information releases. The Service issues a notice when it wishes to provide guidance before a ruling or regulation is available.[46]

Case law regarding notices is also sparse. At least one case places notices below revenue rulings in the deference hierarchy, Costantino v. TRW, Inc., 13 F.3d 969, 980-81 (6th Cir. 1994), while another court places notices at the same level as revenue rulings. Phillips Petroleum Co. v. Commissioner, 101 T.C. 78, 99 (1993).

The most significant notices issued by the IRS in recent years relate to potentially abusive tax shelter transactions, which the IRS designates as "listed" for disclosure purposes. Typically, the opening paragraph of these notices suggests that they are primarily designed to alert promoters and potential investors to potential liabilities. For example, Notice 2001-16, 2001-1 C.B. 730, begins as follows:

> The Internal Revenue Service and the Treasury Department have become aware of certain types of transactions, described below, that are being marketed to

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[43]Internal Revenue Service, *Understanding IRS Guidance—A Brief Primer*, *available at* http://www.irs.gov/irs/article/0,,id=101102,00.html (last visited Feb. 24, 2004).

[44]Chief Counsel Notice CC-2003-014 (May 8, 2003), *available at* http://www.irs.gov/pub/irs-ccdm/cc-2003-014.pdf (last visited Feb. 24, 2004).

[45]*See* MICHAEL I. SALTZMAN, IRS PRACTICE AND PROCEDURE CH. 3 (Rev. 2d ed. 2003).

[46]IRA L. SHAFIROFF, INTERNAL REVENUE SERVICE PRACTICE & PROCEDURE DESKBOOK § 1:4.3(D) (3d ed. 2003).

> taxpayers for the avoidance of federal income taxes. The Service and Treasury are issuing this notice to alert taxpayers and their representatives of certain responsibilities that may arise from participation in these transactions.[47]

While these notices regarding listed transactions suggest possible legal theories in support of the IRS's position, they normally provide only a brief, general factual description, with the legal theories effectively constituting an advance notice of a litigating position. Such notices also describe potential penalties.

Other typical notices anticipate proposed regulations, *see, e.g.*, Notice 2002-18, 2002-1 C.B. 644 (duplicated loss consolidated return regulations), or provide substantive legal guidance on which taxpayers are explicitly told they may rely, *see, e.g.*, Notice 1996-8, 1996-1 C.B. 359 (cash balance plans). Some notices specifically state that they may be relied on as if they were revenue rulings. *See, e.g.*, Notice 1989-99, 1989-2 C.B. 422 (valuation freezes).

Other Guidance. The IRS issues a variety of other documents and forms of guidance involving particular transactions or disputes. Private letter rulings, for example, involve prospective transactions and are directed only at the individual taxpayers who requested them. Reg. § 601.201(b). Copies of private letter rulings, redacted to remove information that identifies the taxpayer, are made available to the public.[48] The IRS also issues technical advice memoranda, usually to resolve disputes between taxpayers and revenue agents. Reg. § 602.205(b)(5). Just recently, the IRS began issuing technical expedited advice memoranda to resolve such disputes more quickly. Rev Proc. 2002-30, 2002-1 C.B. 118. In addition, the IRS Chief Counsel's office releases a variety of inter-agency legal memoranda, *e.g.*, Field Service Advice, Chief Counsel Advice, etc., setting forth that office's analysis of substantive law. Section 6110(k) provides that such "written determinations may not be used or cited as precedent."

Conclusion. In light of the plethora of guidance issued by the IRS and the uncertainties regarding their legal status, in either absolute or in relative terms, applying the twin requirements of *Mead*—force of law and agency intention—yields mixed or inconclusive results. The varying degrees to which different IRS interpretations are imbued with the force of law and are intended to be so exercised suggest varying degrees of deference depending on the form of an IRS interpretation.

D. *Degree of Deliberation*

Also crucial is the degree of deliberation the IRS gives various kinds of interpretations. This consideration has had prominence as far back as *Skidmore*, with its language regarding "the thoroughness evident in its consideration" and

[47] *See also* Notice 2002-65, 2002-2 C.B. 690.

[48] Availability for public inspection and redaction are both statutorily required. I.R.C. § 6110(a), (c).

"the validity of its reasoning." *Skidmore*, 323 U.S. at 139. The degree of deliberation also affects the reasoning and reasonableness of an interpretation, thus tying it to *Chevron* itself. This principle is related as well to *Mead's* stated criteria of "thoroughness, logic and expertise," *Mead*, 533 U.S. at 235; to *Barnhart's* "careful consideration the Agency has given the question," *Barnhart*, 535 U.S. at 522; and to *National Muffler's* "manner in which [the regulation] evolved," *National Muffler*, 440 U.S. at 477.

By degree of deliberation, this Report does not mean a mechanical, quantitative test such as the number of hours spent in reviewing the agency pronouncement, but a qualitative test, one that takes into account the number of levels of review, in particular how high the level of review reaches,[49] and considers the degree of public input via the notice-and-comment process.

Final Regulations. Regulations receive the greatest degree of deliberation and consideration from the IRS. As Regulation section 601.601(a)(1) explains, "The most important rules are issued as regulations and Treasury decisions prescribed by the Commissioner and approved by the Secretary or his delegate. . . . After approval by the Commissioner, regulations and Treasury decisions are forwarded to the Secretary or his delegate for further consideration and final approval." This regulation goes on to specify further procedures, including public hearings and comments on proposed rules, "[w]here required by 5 U.S.C. 553," which, as noted earlier, is the provision of the APA requiring notice and comment for legislative regulations. Moreover, section 7805(f) requires the IRS to solicit comments from the Small Business Administration regarding the impact of any proposed or temporary regulation on small business.

In practice, the IRS gives the same careful consideration, including publication of proposed regulations with opportunity for notice and comment and a preamble highlighting particular comments and issues, to both legislative and interpretive regulations. The Internal Revenue Manual includes a 40,000 word chapter entitled, "Regulation Drafting Handbook," I.R.M. 30.15.20 (1995), which describes regulations as "the most authoritative component of the process that transforms tax statutes into an equitable, efficient process for collecting revenue." The procedures detailed in the Handbook include the following: a drafter from the Office of Chief Counsel, a reviewer from the Office of Chief Counsel,

[49]This principle has much in common with the suggestion made in David J. Barron & Elena Kagan, *Chevron's Nondelegation Doctrine*, 2001 SUP. CT. REV. 201 (2001), that, since the justification for *Chevron* deference is that agency interpretations are products of the executive branch, which is politically accountable through the relationship of an agency to the President, *Chevron* deference should be limited to those agency pronouncements for which officials at the highest level in the agency take personal responsibility. Along such lines, this Report reserves *Chevron* deference for those agency interpretations that are issued by the agency official with responsibility for policy, which in the case of tax law is the Assistant Secretary of the Treasury for Tax Policy, who is appointed by the President and confirmed by the Senate. The Assistant Secretary can delegate the authority to sign regulations only to the Deputy Assistant Secretary. For current delegation orders, see www.treas.gov/regs/td00-08.htm (last visited Feb. 24, 2004).

and an attorney from the Treasury Department Office of Tax Policy, working together to identify issues, often in the form of a memo; exchanging drafts of the regulations informally among this group; circulating drafts to others; guidance briefings, as needed and often in the form of a policy memo, with the Chief Counsel, the Commissioner, and individuals in the Treasury Department; preparing a signature package; soliciting public written comments; drafting an issues memo after the comment period has ended; and preparing the final regulations. All final regulations are issued as Treasury decisions, which are approved and signed by the Assistant Treasury Secretary (or Deputy Assistant Secretary) for Tax Policy, as well as the Commissioner (or Deputy Commissioner).[50]

Importantly, both interpretive and legislative regulations are promulgated through notice and comment, as noted earlier. Public participation through the APA notice-and-comment process is important for essentially two reasons. First, the combined expertise and knowledge of agency administrators and interested persons is thought to result in better rules. The process helps to ensure that important issues are not ignored and that they receive careful consideration. Second, the notice-and-comment procedure serves as a quasi-democratic process.

The adage "two heads are better than one" comes to mind when administrative rules result from the combined knowledge and expertise of agency administrators and the interested public. Members of particular groups or industries possess a wealth of information from which agencies may benefit in the drafting of rules. The Treasury Department's consistent and careful regard for public comments on proposed regulations reflects its recognition of the value of those comments. Public input, moreover, can serve to offset institutional biases in favor of or against particular groups, and enables affected persons to defend themselves against rules that may be detrimental to their interests. As the Supreme Court wrote in *Smiley v. Citibank*, 517 U.S. 735, 741 (1996), the notice-and-comment process is "designed to assure due deliberation."

Because agencies are not directly accountable to voters, the notice-and-comment process also alleviates the inherent lack of democratic debate both by allowing affected persons to have a voice in the process and by requiring the agency to read and respond to comments. Notice-and-comment procedures enable those with opposing viewpoints to attempt to influence agency action in an open fashion and minimize opportunities for administrative decision-making behind closed doors. An important feature of the process is that the APA requires notice of the "basis and purpose" of its publication. 5 U.S.C. § 553(c). The current practice of issuing detailed preambles, discussing the rules adopted

[50]For recent examples, *see* T.D. 9059, 68 Fed. Reg. 34,293 (2003) (allocation of basis among partnership assets); T.D. 9058, 68 Fed. Reg. 24,349 (2003) (interest rate for insurance company tax reserves); T.D. 9057, 68 Fed. Reg. 24,351 (2003) (waiver of certain section 1502 elections).

and alternatives rejected, demonstrates both careful consideration and responsiveness to taxpayer concerns.[51]

Courts have indicated that the notice-and-comment procedure enhances the quality of judicial review by providing affected parties an opportunity to develop an evidentiary record to support their objections to rules. *See, e.g.*, Small Refiner Lead Phase-Down Task Force v. EPA, 705 F.2d 506, 547 (D.C. Cir. 1983); Marathon Oil Co. v. EPA, 564 F.2d 1253, 1271 n.54 (9th Cir. 1977); *cf.* Schwalbach v. Commissioner, 111 T.C. 215, 228 (1998) ("purpose of notice and comment is not adequately served, on the other hand, where interested persons could not reasonably anticipate the final rules from the proposed rules"). Thus, although notice-and-comment is not a panacea,[52] notice-and-comment ensures a high level of deliberation and the quasi-democratic process that justifies *Chevron* deference.

Temporary and Proposed Regulations. Treasury regulations typically are not effective, *i.e.*, have no force of law, until they are made final by publication in the Federal Register. *See, e.g.*, Garvey, Inc. v. United States, 1 Cl. Ct. 108 (1983), *aff'd*, 726 F.2d 1569 (Fed. Cir. 1984) (proposed regulation represents only a "preliminary proposal," not binding "on respondent or on the Court"). Many times, however, Treasury simultaneously issues proposed regulations as temporary regulations. Unlike proposed regulations, temporary regulations are effective when they initially appear in the Federal Register, thus providing immediate and binding guidance to taxpayers. Significantly, temporary regulations are issued without the benefit of notice and comment.

In 1988, Congress enacted section 7805(e), which provides that temporary tax regulations issued after November 20, 1988, "shall expire" unless replaced by a final regulation within three years of the date on which the proposed regulations were issued. What legislative history there is suggests that Congress was concerned by the length of time that regulations were left in temporary form and that it wished to codify the practice of seeking post-effective comment on temporary regulations.[53]

Revenue Rulings, Revenue Procedures, and Notices. As discussed earlier, revenue rulings are official publications of the IRS, but are not as authoritative as regulations. Regulation section 601.601(d)(2)(v)(d) states, "Revenue Rulings

[51]*See, e.g.*, T.D. 8294, 55 Fed. Reg. 9426 (1990) & T.D. 8364, 57 Fed. Reg. 53,550 (1992) (consolidated return loss disallowance regulations); T.D. 8978, 67 Fed. Reg. 12,471 (2002) (intermediate sanctions for exempt organizations). At least one case has invalidated a tax regulation for failure to meet the notice requirement. *See* American Standard, Inc. v. United States, 602 F.2d 256, 267 (Ct. Cl. 1979).

[52]*See, e.g.*, Barron & Kagan, *supra* note 49; Mark Seidenfeld, *Demystifying Deossification: Rethinking Recent Proposals to Modify Judicial Review of Notice and Comment Rulemaking*, 75 TEX. L. REV. 483 (1997); Thomas O. McGarity, *The Courts and the Ossification of Rulemaking: A Response to Professor Seidenfeld*, 75 TEX. L. REV. 525 (1997); Thomas O. McGarity, *Some Thoughts on "Deossifying" the Rulemaking Process*, 41 DUKE L.J. 1385 (1992).

[53]*See* Asimow, *supra* note 29, at 362-63.

published in the Bulletin do not have the force and effect of Treasury Department Regulations (including Treasury decisions)." Neither do they receive the same kind of careful consideration and review as regulations. After written approval of a proposed ruling by the Chief Counsel, it is reviewed in the Office of the Commissioner and in Treasury's Office of Tax Policy. Revenue rulings are published in the Internal Revenue Bulletin without prior notice to the public, and the Service does not ordinarily solicit public comments before issuing them. Revenue rulings are not formally signed by the Commissioner or the Assistant Secretary for Tax Policy. Revenue rulings currently simply list the staff lawyer in the Office of Chief Counsel who is the principal author, and give that person's phone number for further information; no reference is made to section 7805.[54]

Revenue procedures, although intended to consist merely of procedural matters, *see, e.g.*, Rev. Proc. 1989-14, 1989-1 C.B. 814, sometimes reflect the IRS's position on matters of substance or statutory construction. *See, e.g.*, Rev. Proc. 1999-43, 1999-2 C.B. 579 (at issue in *Federal National Mortgage Association v. United States*, 56 Fed. Cl. 228, 234-35 (2003)) (hereinafter "*Fannie Mae*"). The same, as discussed earlier, is true of notices. As with revenue rulings, revenue procedures and notices are issued without prior notice to the public. In general, revenue procedures are developed with the same kind of deliberative process as revenue rulings, and it is likely that notices are issued through a similar process.

Other Guidance. Private letter rulings (PLRs) are issued by the IRS's National Office at the request of specific taxpayers prior to the filing of a return.[55] While the IRS generally welcomes inquiries of this sort, it may exercise its discretion not to rule in any particular situation. Procedures for obtaining PLRs are issued annually by the IRS's Office of Chief Counsel. *See, e.g.*, Rev. Proc. 2003-1, 2003-1 I.R.B. 1. Neither the Chief Counsel nor the IRS Commissioner is required to approve or sign a PLR; PLRs are issued by an Associate Chief Counsel. The Task Force understands that PLRs typically are not reviewed outside of the branch that issues them.

Technical advice memoranda (TAMs) are similar to private letter rulings in that they are issued by the National Office only in response to specific requests.[56] Unlike PLRs, however, TAMs generally are requested by IRS employees (in District Offices or Appeals Offices), but a request may sometimes be initiated by a taxpayer. TAMs address technical or procedural questions that develop during examination of a return (*i.e.*, an audit), the appeals process, or any other review in a field office. Like PLRs, TAMs are issued by an Associate Chief Counsel; neither the Chief Counsel nor the Commissioner is required to approve or sign a TAM. The Task Force understands that TAMs typically are

[54] *See, e.g.*, Rev. Rul. 2003-4, 2003-2 I.R.B. 253; Rev. Rul. 2003-13, 2003-4 I.R.B. 305.

[55] For a general discussion of the application, issuance, and review procedures for PLRs, *see* SALTZMAN, *supra* note 45, at ¶ 3.03[3].

[56] For a general discussion of the application, issuance, and review procedures for TAMs, see SALTZMAN, *supra* note 45, at ¶ 3.04[2].

not reviewed outside of the branch that issues them.

It is the policy of the IRS to announce whether or not it will follow the adverse holdings of selected cases. Those determinations, called Actions on Decision (AODs), are prepared periodically. Although the texts of AODs themselves are not formally published by the IRS, they are available in commercial databases. The conclusion of an AOD is published in the Internal Revenue Bulletin and termed an acquiescence or nonacquiesence. *See, e.g.*, Actions Relating to Decisions of the Tax Court, 2003-49 I.R.B. 1172 (Dec. 8, 2003). In the view of the IRS, the purpose of issuing AODs is to provide guidance to IRS personnel who may be working on issues similar to those in the cases. *Id.* As to the weight or status of an AOD, each AOD contains the following language:

> Unlike a Treasury Regulation or a Revenue Ruling, an Action on Decision is not an affirmative statement of Service position. It is not intended to serve as public guidance and may not be cited as precedent.

Id. See also Taxation With Representation Fund v. IRS, 646 F.2d 666 (D.C. Cir. 1981) ("The purpose of the distribution [of AODs] is to provide a research tool and guidance to Office of Chief Counsel brief writers in the field and in the National Office. The distribution also provides guidance to IRS field personnel as to the legal positions of the Office of Chief Counsel on a given issue in the time between an adverse decision in a court case and the ultimate resolution of the issue after appeal or action on the application for certiorari.").

The IRS issues other materials, *e.g.*, Publications, Forms, and Instructions, to assist taxpayers in complying with their obligations under the tax laws. The Task Force does not understand the IRS to intend any of these materials to have the force of law.

Conclusion. The IRS has established a hierarchy of procedures for various kinds of pronouncements that correlate with the level of authority assigned the pronouncements. Thus, regulations receive the most scrutiny within the IRS and, while legislative regulations and interpretive regulations share both internal development and issuance procedures, the IRS takes the position that interpretive regulations do not necessitate notice and comment. Revenue rulings, next in line, are issued through a routinized and comprehensive program within the agency, but public notice and comment is not part of the process. Other forms of informal guidance are subject to increasingly less formal review and issuance procedures.

E. *Explanation of Recommendations*

After considering the case law and special concerns applicable to the tax law, this Report makes the following recommendations to aid courts in cases involving judicial deference to IRS interpretations:

> **1. Federal courts should give *Chevron* deference to regulations promulgated by the IRS, with (i) legislative tax regulations receiving controlling deference under *Chevron* so long as they are not arbi-**

trary, capricious, or manifestly contrary to the statute; (ii) interpretive tax regulations receiving the same controlling deference if they are reasonable under the test of *National Muffler*, which examines such factors as the extent to which the regulation harmonizes with the plain language, origin, and purpose of the statute; the manner in which the regulation evolved; the length of time the regulation has been in effect; the reliance placed on it; the consistency of interpretation; and the degree of scrutiny Congress has devoted to the regulation; and (iii) temporary regulations receiving the same deference as above, provided that the promulgation of such regulations meets the good cause standards as specified in the APA for promulgating regulations without notice and comment.

This recommendation melds traditional case law involving tax interpretations with general administrative law jurisprudence. Regulations are the most authoritative of IRS pronouncements. *Mead* specifically lists notice and comment as an indication that Congress has delegated authority to make rules with the force of law, and, with the exception of temporary regulations, tax regulations are promulgated with notice and comment. As discussed above, notice and comment helps ensure careful deliberation by the agency.

Final Regulations. Regulations issued pursuant to a specific grant of authority and with notice and comment meet all of the tests of both *Chevron* and *Mead*. These legislative regulations are appropriately subject to the "arbitrary and capricious" test of *Chevron*'s step two, for legislative regulations that are promulgated pursuant to "an express delegation of authority . . . to elucidate a specific provision of the statute." *See also* APA § 706 (establishing arbitrary and capricious standard for legislative rules).

The Task Force recommends that interpretive regulations also be afforded *Chevron* deference, but articulates the test for reasonableness under *National Muffler*. The difference in the recommendation for the tests applicable to legislative and interpretive regulations acknowledges the traditional difference in the level of deference between legislative and interpretive regulations used in tax cases. That is, for both legislative and interpretive tax regulations, a regulation must be reasonable, but what is reasonable for a legislative regulation is broader and thus easier to satisfy than what is reasonable for an interpretive regulation. Once the reasonableness test is met, the regulation is given controlling power.

Some might argue that this distinction is both too complex and unjustified. In the case of other administrative agencies, regulations promulgated under the authority of a statutory provision similar to section 7805(a) are considered "legislative rules" under the Administrative Procedure Act.[57] We conclude that all

[57] *See* note 108 *infra*.

IRS regulations, whether promulgated under the grant of authority in a particular Code section or under the general authority of section 7805(a), are "legislative rules" within the meaning of the APA. The traditional and well-entrenched use of the term "interpretive" for regulations promulgated under the authority of section 7805(a) breeds inevitable confusion.[58]

Congress itself has had to deal with this confusion. The Regulatory Flexibility Analysis Act, 5 U.S.C. § 603, requires all administrative agencies to prepare an elaborate analysis of the impact of a proposed rule on small business entities. In general, this requirement applies "[w]henever an agency is required by section 553 of this title, or any other law to publish a general notice of proposed rulemaking for any proposed rule . . ." § 603(a). Because the relationship between the APA and tax regulations promulgated under section 7805(a) is so uncertain, Congress enacted a special rule regarding when the IRS must undertake this regulatory analysis: whenever an agency "publishes a notice of proposed rulemaking for an interpretative rule involving the internal revenue laws of the United States." § 603(a). At least in this regard, Congress has decided that a tax interpretive regulation shall be treated in the same way as a legislative rule under the APA.

Virtually all regulations are legislative in that their authority derives from the Congress. *Chevron*, in fact, makes that point: "sometimes the *legislative* delegation to an agency on a particular question is implicit rather than explicit." 467 U.S. at 844 (emphasis supplied.) The Task Force believes that under *Chevron* and *Mead* there are two types of "legislative" delegations: specific authority and implicit (or general) authority. Specific authority regulations emanate from specific delegations in particular Code sections; implicit (or general authority) regulations are issued under the authority of section 7805(a) to fill in gaps left by the Congress. The level of deference, however, differs: specific authority regulations are applied "unless arbitrary, capricious or manifestly contrary to the statute," while general authority regulations are applied if "reasonable." This dichotomy is spelled out in *Chevron*[59] and is restated in *Mead*, which also makes it clear that a "legislative delegation" pursuant to "generally conferred authority" (presumably such as is conferred under section 7805(a)) begets deference if "the agency's interpretation is reasonable." *Mead*, 533 U.S. at 229.

While a single test would simplify the task of the courts, we see no basis for overturning the longstanding dichotomy, which is supported by *Chevron* and

[58]For a discussion of the confusion this terminology produces, see *Bankers Life and Casualty Co. v. United States*, 142 F.3d 973 (7th Cir. 1998).

[59]"If Congress has *explicitly* left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such *legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute.* Sometimes the legislative delegation to an agency on a particular question is *implicit* rather than explicit. In such a case, a court may not substitute its own construction of a statutory provision *for a reasonable interpretation* made by the administrator of an agency." *Chevron*, 467 U.S. at 843-44 (emphasis supplied).

Mead[60] as well as the plain meaning of the applicable tests.[61] Logic also suggests that a specific Congressional delegation of authority should command a higher level of deference. *Chevron* cites *U.S. v. Morton*, 467 U.S. 822, 834 (1984), which makes this point: "[Regulations] are entitled to special deference since that was the precise objective of Congress when it delegated authority to issue regulations." This Report reviews post-*Chevron* tax cases through the end of 2003, and concludes that although *Chevron*'s two-step process has been affirmed for tax cases,[62] the Supreme Court nonetheless has consistently applied the *National Muffler* test to determine if a general authority regulation is reasonable.[63] The distinction is also appropriate since *Chevron* offers no apparent guidance for applying the reasonableness test, while *National Muffler* provides considerable guidance.[64]

The IRS's longstanding position that general authority regulations issued under section 7805(a) are "interpretive" rules, not requiring notice-and-comment procedures under the APA, does not change our view. The IRS's assertion cannot override the APA.[65] And whatever the source of the government's position, it seems inconsistent with *Chevron*; the government's position is also undercut by its invariable use of the notice-and-comment process for all regulations (other than temporary regulations). In any event, *Mead* and *Barnhart* keep the door open for *Chevron* deference to interpretations that are issued without notice-and-comment[66] and *Boeing Company v. United States*, 537 U.S. 437 (2003),

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[60]Even before *Chevron* and *Mead*, the Supreme Court recognized this distinction. *See, e.g.*, United States v. Vogel Fertilizer, 455 U.S. 16, 24 (1982); Rowan Cos. v. United States, 452 U.S. 247, 253 (1981).

[61]A position "manifestly contrary" to a statute is patently more difficult to prove than a position which must "harmonize" with the statute. The dictionary also draws a sharp distinction between arbitrary ("based on one's preference, notion, whim . . .") and reasonable ("amenable to reason; just . . . sound judgment; sensible"). WEBSTER'S NEW WORLD DICTIONARY COLLEGE EDITION (3d ed.). *See* Ellen P. Aprill, *The Law of the Word: Dictionary Shopping in the Supreme Court*, 30 ARIZ. ST. L. REV. 375 (1998).

[62]Atlantic Mut. Ins. Co. v. Commissioner, 523 U.S. 382, 387 (1998).

[63]*See* Part II, Section D, *infra.*

[64]"In determining whether a particular regulation carries out the congressional mandate in a proper manner, we look to see whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose. A regulation may have particular force if it is a substantially contemporaneous construction of the statute by those presumed to have been aware of congressional intent. If the regulation dates from a later period, the manner in which it evolved merits inquiry. Other relevant considerations are the length of time the regulation has been in effect, the reliance placed on it, the consistency of the Commissioner's interpretation, and the degree of scrutiny Congress has devoted to the regulation during subsequent re-enactments of the statute." *National Muffler*, 440 U.S. at 477.

[65]The Court of Federal Claims in *Fannie Mae*, 56 Fed. Cl. 228, 236 (2003), rejected *Chevron* deference for a revenue procedure subject to limited notice and comment because the question "is whether Congress intended for the IRS to do so." The court did not believe its anti-bootstrap analysis applied to regulations since the court concluded that "Treasury regulations undoubtedly enjoy *Chevron* deference." *Id.* at 235.

[66]Both *Mead* and *Barnhart* cite only a single case for this proposition – *NationsBank.* Notably, the *Fannie Mae* case suggests that *NationsBank* is "a case limited to the Comptroller of the Currency's long-standing personal authority to enforce the banking laws and promulgate directives with the force of law," and of the few cases cited directly or indirectly by *NationsBank*, the only case to

the Supreme Court's most recent review of tax regulations, instructs courts to give deference to interpretive regulations.

In short, were we writing on a clean slate, we might refer to tax regulations as either specific authority or general authority regulations, not as legislative or interpretive regulations. In conformance with the longstanding tax convention, however, this Report utilizes traditional nomenclature and deference levels. As discussed above, all regulations are scrutinized under the standards adopted in *Chevron* and restated in *Mead*. In applying the reasonableness test, *National Muffler* and its progeny should be applied as to interpretive regulations since that is the standard being applied by the Supreme Court.

Temporary Regulations. As explained above, this Report suggests that all IRS regulations are legislative rules within the meaning of the APA. As such, these regulations are invalid unless they are promulgated either with notice and comment or come within the APA's limited exceptions to notice and comment. A recent case, UnionBanCal v. Commissioner, 305 F.3d 976 (9th Cir. 2002), upheld a temporary regulation based on specific Code authority and noted that Congress "empowered" regulations without notice and comment. According to the court, the source of the power was the APA and the court quoted 5 U.S.C. § 553, the portion of the statute which spells out the exceptions and the disclosure procedures:

> Except when notice or hearing is required by statute, this subsection does not apply . . . when the agency for good cause finds (and incorporates the finding and a brief statement of reasons therefore in the rules issued) that notice and public procedure thereon are impracticable, unnecessary, or contrary to the public interest.

Id. at 985, n. 50.

As Professor Michael Asimow argued more than a decade ago, the IRS in promulgating temporary regulations needs to comply with the APA by publishing a detailed explanation of why notice and comment would be impracticable or contrary to the public interest, and thus why the good cause exception to notice-and-comment applies. As Professor Asimow explains:

> To establish that notice and comment procedure would be "impracticable" or "contrary to the public interest," the agency must show exigent circumstances. For example, an imminent implementation deadline imposed by a statute or judicial decision or an emergency such as a serious public health problem might qualify as good cause. Similarly, situations in which a statutory purpose would be thwarted by the absence of immediately-enforceable regulations might qualify. However, the good cause test is not met simply because an agency

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discuss notice and comment suggests it could be important: "The difficulty here is that the Comptroller adopted no expressly articulated position at the administrative level as to the meaning and impact of the provisions of sections 16 and 21 as they affect bank investment funds. The Comptroller promulgated Regulation 9 without opinion or accompanying statement." Invest. Co. Instit. v. Camp, 401 U.S. 617, 626 (1971).

> wishes to adopt immediately-effective rules to provide guidance or simplify enforcement. Moreover, claims that an emergency exists are undercut if the agency has waited a substantial period of time before adopting regulations.[67]

As Professor Asimow explains, the standards for the good cause exception would justify promulgation of temporary regulations intended to prevent transactions that have come to the attention of the IRS and which the IRS concludes constitute abuse of the Internal Revenue Code.[68] If, however, the IRS fails to comply with these APA requirements, a court could and should declare the regulation invalid on procedural grounds.[69]

If, however, this Report's position that all IRS regulations are legislative rules within the meaning of the APA is rejected, courts may have a difficult time enforcing the "good cause" requirement of the APA.[70] Nonetheless, this Report recommends that even if it should be determined that the notice and comment requirements of the APA do not apply generally to temporary tax regulations, the policies underlying the APA requirement together with the policies that underlie *Chevron* deference make it appropriate for a court to give *Chevron* deference to temporary regulations only if the IRS in promulgating them can justify the absence of notice and comment under criteria like that required under the APA. If the IRS does not provide such a justification, we would recommend that *Skidmore* deference be applied since the deliberative process rises at least to the level of a revenue ruling.

Litigating Regulations. Regulations issued in response to pending litigation should be entitled to *Chevron* deference. Generally, the period a regulation is outstanding is not relevant, even where a regulation is issued in connection with pending litigation. This is one issue as to which the case law is clear. *See* Smiley v. Citibank, 517 U.S. 735 (1996); Indianapolis Life Ins. Co. v. U.S., 115 F.3d

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[67] Asimow, *supra* note 29, at 348-49 (footnotes omitted).

[68] A recent example is T.D. 9062, 68 Fed. Reg. 37,414 (2003), a temporary regulation dealing with the assumption of partner liabilities in a "Son of BOSS" transaction. It is rare for temporary regulations, which average 39 per year for the last eight years, to rely on good cause.

[69] The opinion of the Court of Appeals for the Sixth Circuit in *Hospital Corp. of America v. Commissioner*, 348 F.3d 136, 145 n.3 (6th Cir. 2003), can be read as inviting such a challenge: "Hospital Corporation does not challenge the temporary regulations [involving section 448(d)(5)] as violations of the notice and comment requirements for rulemaking, see 5 U.S.C. § 533. Accordingly, we do not reach the issue of whether the Administrative Procedure Act requires notice and comment procedures before Treasury may promulgate temporary interpretive regulations that make substantive choices among permissible statutory interpretations."

[70] The IRS could make the following arguments to retain *Chevron* deference: (1) While temporary regulations do not receive notice and comment, *Mead* and *Barnhart* make clear that notice and comment is not always required for *Chevron* deference. (2) By issuing an interpretation as a regulation, the IRS is categorizing the interpretation as one that is made under its delegated powers to issue rules with the force of law, which is what *Mead* requires. (3) Temporary regulations receive the same high level of review as final regulations. (4) Section 7805(e) can be read as a signal that Congress intended temporary regulations promulgated after 1988 to have the force of law for three years.

430 (7th Cir. 1998); and *Barnhart*.[71] Although *National Muffler* does emphasize the timing and manner in which a regulation evolved, the Task Force does not believe that timing should prevent the IRS from changing its view if appropriate notice-and-comment issuance procedures are followed.

Proposed Regulations. This Report recommends that no deference be accorded to proposed regulations. Although proposed regulations are considered in depth by the IRS and are treated as "substantial authority" on which taxpayers may rely to avoid the substantial understatement penalty, I.R.C. § 6662(d), Notice 1990-20, 1990-1 C.B. 328, we agree with the case law that proposed regulations should not be afforded any more weight than a position advanced by the Commissioner in a brief. *See* General Dynamics v. Commissioner, 108 T.C. 107, 120 (1997); Laglia v. Commissioner, 88 T.C. 894, 897 (1987); Estate of Brown v. Commissioner, 910 F.3d 633 (9th Cir. 1999); *but see* Commissioner v. Engle, 464 U.S. 206, 228 (1984) (Blackmun, J., dissenting) (deferring to a position in proposed regulations).

If, as this Report argues, notice and comment is important and can produce changes in the content of a regulation, then a proposed regulation that is not yet subject to notice and comment must be regarded merely as a draft. Accord Commodities Futures Trading Comm'n v. Schor, 478 U.S. 833, 845 (1986) ("It goes without saying that a proposed regulation does not represent an agency's considered interpretation of its statute and that an agency is entitled to consider alternative interpretations before settling on the view it considers most sound."). The court in *Ravenswood Group v. Fairmont Assoc.*, 736 F.Supp. 1285, 1288 (S.D.N.Y. 1990), cited *Schor* with approval in considering the weight of proposed Treasury regulations issued under section 1031. At least one court believes that this principle remains valid after *Mead*. *See* Natural Resources Defense Council v. Evans, 254 F.Supp. 434, 441 (S.D.N.Y. 2003) (citing both *Mead* and *Ravenswood*). Indeed the *Evans* court asserted that an agency cannot be held to a position set forth in proposed regulations precisely because public comment could, appropriately, inspire a change in that position. *Id*. The Task Force does not believe that *Mead* mandates any level of deference to proposed regulations, which, by their very nature, are not meant to reflect law unless and until they are adopted as final regulations.

As discussed *supra*, we do recommend deference to temporary regulations in certain situations. We find this distinction both appropriate and consistent. If the IRS promulgates a regulation as both proposed and temporary, the agency is taking the position that the interpretations embodied in the regulation are more than a draft; they are the current law. Thus, should the IRS desire *Chevron* deference, it can issue the regulation as both temporary and proposed, again, so

[71] *See* Part II, Section C, *infra*. Thus, while earlier tax cases may suggest that a litigating regulation could be invalidated as an abuse of discretion, such as *Chock Full O'Nuts Corp. v. United States*, 453 F.2d 300 (2d Cir. 1971), or *Caterpillar Tractor Co. v. United States*, 589 F.2d 1040 (Ct. Cl. 1978), these cases may have been superceded by developments in Supreme Court precedent.

long as the conditions imposed by the APA for promulgating temporary regulations are met.

2. Federal courts should give revenue rulings, certain revenue procedures, and certain notices *Skidmore* deference, which directs courts to take into account the agency's experience and its power to persuade, but to retain the ability to choose a better rule even if the agency interpretation is reasonable.

The Task Force believes that after *Mead*, some kind of deference is due revenue rulings as well as those revenue procedures and notices that announce substantive interpretations of the law. If the tariff classifications in *Mead* deserved *Skidmore* deference, so must these sorts of IRS pronouncements. Post-*Mead* case law strongly supports this recommendation.

This Report, like most of the courts that have considered the issue since *Mead*, takes the position that *Chevron* deference is not appropriate for revenue rulings.[72] First, although issued under the authority of the IRS National Office, revenue rulings do not have the same force of law as do regulations (whether the regulations are legislative or interpretive). The IRS's weekly assertion, in its Internal Revenue Bulletin, that rulings do not have the force and effect of regulations makes that point.[73] Moreover, while regulations normally refer to the Congressional delegation of rulemaking authority under section 7805 as their source of authority, revenue rulings cite no such source of rulemaking authority, but simply refer to the particular Code section being interpreted. This absence is significant in applying the requirement of *Mead* that "the agency interpretation claiming deference was promulgated in the exercise of that [Congressional] authority." As pronouncements claiming less force of law, revenue rulings should receive less deference than regulations.

Second, as discussed in Section I(E), *supra*, revenue rulings are not required to receive the same kind of careful consideration that regulations receive.[74] Neither the deliberative process nor the level of involvement by top officials is as extensive for revenue rulings as for regulations. Final regulations require the signatures of both the Commissioner and the Assistant Secretary for Tax Policy; revenue rulings on the other hand, are signed only by the Chief Counsel.[75] Finally, while not dispositive, revenue rulings are not subject to notice-and-comment.

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[72]*See* Part II, Section E(2), *infra*.

[73]*See also* Reg. § 601.601(d)(2)(v)(d) ("Revenue rulings published in the Bulletin do not have the force and effect of Treasury Department Regulations.").

[74]In fact, in 2002 the then-Chief Counsel of the IRS and the Deputy Assistant Secretary for Tax Policy announced plans to streamline the process that produces revenue rulings in order "to move the guidance more quickly and efficiently." According to news reports, one goal of such an effort is to "eliminate the effect of too many lawyers trying to perfect the product." Sheryl Stratton, *IRS Looks At Ways To Improve Guidance Process*, 2002 TAX NOTES TODAY 205-2 (Oct. 22, 2002).

[75]*See* Chief Counsel Publications Handbook, I.R.M. 30.15.10 (1995).

Although some revenue rulings (or other guidance, such as notices) may receive careful review at high levels both within the IRS and Treasury, such review is not mandated by the IRS's procedural rules.[76] In order to develop policies regarding deference that are consistent and administrable, the degree of deference needs to vary among categories, not among documents.

It is also arguable that the nature of revenue rulings, unlike the nature of regulations, does not call for *Chevron* deference to the IRS. Regulations are intended to announce rules of general application, affecting many kinds of taxpayers in many kinds of situations. The IRS takes these factors into account in drafting regulations. Courts reviewing any regulation in the context of a particular case must focus on the impact of a particular regulation on the particular cases and facts before them and not on whether the regulation makes sense for the tax system as a whole. Thus, *Chevron* deference to the IRS's judgment about regulations of general effect is appropriate. In contrast, "conclusions expressed in Revenue Rulings will be directly responsive to and limited in scope by the pivotal facts stated in the revenue ruling." Reg. § 601.601(d)(2)(v)(a). Evaluating the application of law to a specific set of facts is well within a court's competence. Indeed, it is precisely the kind of task that our courts were established to perform.[77]

The Task Force reads *Mead* as mandating that revenue rulings merit *Skidmore* deference and that the pre-*Mead* position of the Tax Court that revenue rulings merit no deference cannot stand.[78] Thus, a court is free to accept or reject a position set forth in a revenue ruling on the basis of its evaluation of such factors as "the degree of the agency's care, its consistency, formality, and relative expertness, and . . . the persuasiveness of the agency's position."[79] *Mead*, 533 U.S. at 228. In the view of the Task Force, the tariff classification rulings at issue in *Mead*, which were accorded deference under *Skidmore*, have less impact[80] and receive less deliberation[81] than revenue rulings. In support of accord-

[76]While the Task Force understands that the Assistant Secretary for Tax Policy or other high level Treasury official may closely review revenue rulings that deal with significant policy issues, other rulings may receive little or no review at such levels.

[77]"Unlike a regulation, which has general applicability, a revenue ruling applies law and policy to specific facts and particular taxpayers, much as a court decision." SALTZMAN, *supra* note 45, at ¶ 3.02[1]. *See* Mashaw, *supra* note 5, for a comparison of the relative institutional competencies of courts and agencies.

[78]*But cf.* O'Shaughnesey v. Commissioner, 332 F.3d 1125, 1130 (8th Cir. 2003) ("The Supreme Court has refrained from deciding whether revenue rulings are entitled to deference.").

[79]According to *Skidmore* itself, "The weight [accorded to an administrative] judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control." 323 U.S. at 140 (*quoted in Mead*, 533 U.S. at 228).

[80]Revenue rulings may be relied upon by all taxpayers where facts and circumstances are substantially similar to those addressed in rulings. In contrast, "Customs has regarded a classification as conclusive only as between itself and the importer to whom it was issued." *Mead*, 533 U.S. at 233.

[81]Revenue rulings are issued only by the IRS National Office. Tariff classification rulings may be issued by any one of 46 Customs offices. *Mead*, 533 U.S. at 238. In 2001, the IRS issued 66 revenue rulings and, in 2002, it issued 99. *See supra* note 9. In contrast, as noted in *Mead*, Customs issues approximately 10,000 tariff classification rulings each year. 533 U.S. at 233.

ing *Skidmore* deference to tariff classification rulings, moreover, the Court noted that the highly detailed regulatory scheme under which the rulings are issued justifies utilization of Customs' specialized expertise in addressing the subtle questions presented in the case. 533 U.S. at 235. The same can be said of the tax code and regulations. The Task Force concludes that revenue rulings should receive *Skidmore* deference under *Mead*.[82]

Revenue procedures and notices, to the extent they address substantive rather than procedural matters (and are not mere statements of litigating positions), should receive *Skidmore* deference for the same reasons. They are issued by the same IRS office that issues revenue rulings, with similar internal review procedures, and without prior notice and comment. There is little indication that either Congress or the IRS itself ever intended that revenue procedures or notices would have the same status as regulations.[83]

Interpretations of Ambiguous Regulations. The Task Force believes that revenue rulings, revenue procedures and similar formal guidance interpreting ambiguous regulations should receive no more than *Skidmore* deference. This recommendation would narrow the doctrine found in *Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410 (1945), which gives controlling deference to an agency's interpretation of an ambiguous regulation.[84] Giving interpretations of regulations the same degree of deference as other interpretations cuts back on *Seminole Rock* without completely denying deference to the IRS. Moreover, giving interpretations of regulations the same kind of deference as other interpretations announced by the IRS in the same format encourages consistency and ease of administration.

Mead indirectly suggests a diminution of *Seminole Rock*. Since *Mead* conditions *Chevron* deference both on Congress delegating authority to the agency to issue rules which have the force of law and on the agency interpretation being promulgated in the exercise of that authority, few, if any, *Seminole Rock* interpretations of ambiguous regulations would qualify for *Chevron* deference. *Mead* never mentions *Seminole Rock* and thus fails to reconcile the relationship between *Seminole Rock* and *Chevron* as reinterpreted by *Mead*. Similarly, the Supreme Court in *Cottage Savings v. Commissioner*, 499 U.S. 554 (1991), neither granted deference to the government's interpretation of Regulation section 1.1001-1, nor mentioned *Seminole Rock*.

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[82]The Task Force sees no reason to treat revenue rulings issued during the course of litigation differently. The timing of issuance and the purpose of the ruling (*e.g.*, to bolster the government's litigating position) would be factors taken into account by the court under *Skidmore* in determining the persuasiveness of the ruling.

[83]Exceptions to this general rule include Revenue Procedure 2003-24, 2003-11 I.R.B. 599, and Revenue Procedure 2003-25, 2003-11 I.R.B. 601, discussed at text accompanying *supra* note 41, which claim to be an extension of a regulation. For all the reasons explained here, the Task Force believes that even these kind of revenue procedures should be afforded only *Skidmore* deference.

[84]See Part II, Section B, *infra*, for a more detailed discussion of this doctrine.

In addition, an interpretation of a regulation, if given deference under *Seminole Rock*, achieves in effect the status of a newly issued regulation. However, the interpretation may occur many years after the enactment of the underlying statute. Any deference greater than *Skidmore* deference thus seems contrary to the intent of section 7805(b)(1), which prohibits the retroactive application of most regulations.[85]

Like the dissent in *Thomas Jefferson University v. Shalala*, 512 U.S. 504 (1996),[86] the Task Force is concerned that *Seminole Rock* permits an end run around notice and comment and fosters promulgation of ambiguous rules, an important component of *Seminole Rock*, but a difficult determination in itself.[87] One scholar has argued that under the separation of powers doctrine inherent in our constitution, we prohibit lawmakers from intruding on interpreters of the law.[88] Violation of this principle would occur if *Seminole Rock* applied to administrative agencies such as the IRS, since the IRS would first write the law under its congressionally delegated authority and then would interpret it. Even if such a practice were not a constitutional violation, prudence counsels against further exacerbating the situation by giving a high level of judicial deference to these agency interpretations.

3. Federal courts should take into account unofficial agency interpretations, such as private letter rulings, certain notices, technical advice memoranda, and litigating positions, only to the extent to which their logic and reasoning appeal to the reviewing court.

Although a difficult decision, the Task Force believes that informal interpretations (such as PLRs) and litigating positions advanced for the first time in government briefs in which the IRS is a litigant[89] are not entitled to full *Skidmore* deference, and should be taken into account by the courts only to the extent to which their logic and reasoning appeal to or persuade the court. That is, no deference should be based on the experience of the IRS or attributed to the complexity of the tax law.

[85]Regulations issued within 18 months of a statute, regulations issued to prevent abuse, and regulations issued to correct procedural defects, are exceptions to the general rule.

[86]Justice Thomas wrote in dissent: "It is perfectly understandable, of course, for an agency to issue vague regulations, because to do so maximizes agency power and allows the agency greater latitude to make law through adjudication rather than through the more cumbersome rulemaking process. Nonetheless, agency rules should be clear and definite so that affected parties will have adequate notice concerning the agency's understanding of the law." *Thomas Jefferson University*, 512 U.S. at 525 (Thomas, J., dissenting).

[87]We are particularly concerned that a court might give controlling deference to an interpretation (without notice and comment) of the most ambiguous of regulations, the ubiquitous anti-abuse or anti-avoidance regulation.

[88]*See* Manning, *supra* note 1, at 627-44.

[89]Agency positions provided in *amicus* briefs have been afforded *Chevron* deference. *See, e.g.*, Auer v. Robbins, 519 U.S. 452 (1997). *But cf.* Keys v. Barnhart, 347 F.3d 990, 993 (7th Cir. 2003). In *Keys*, Judge Posner wrote "Probably there is little left of *Auer*."

Section 6110(k)(3) specifies that "written determinations,"[90] including PLRs, may not be "used or cited as precedent."[91] This statutory limitation signals to us a congressional directive to limit severely the impact of such informal guidance. This lack of precedential force is bolstered by the disclaimer adopted by the IRS itself, which appears in every PLR: "Section 6110(k)(3) provides that it may not be used or cited as precedent."[92] *See, e.g.*, P.L.R. 2003-28-028 (July 11, 2003); P.L.R. 2003-32-8034 (July 11, 2003). If taxpayers cannot rely directly on such documents for guidance, neither should the IRS have the advantage over taxpayers that *Skidmore* deference might afford.

Mead supports relying on the directive of section 6110(k)(3). *Mead* rejects the reasoning of Justice Scalia's dissent on the grounds that his "efforts to simplify ultimately run afoul of Congress's indication that different statutes present different reasons for considering respect for the exercise of administrative authority." 533 U.S. at 301. The importance of looking at the statute to determine Congressional intent appears as well in *Mead*'s discussion of *Skidmore* deference: "The Court, on the other hand, said nothing in *Chevron* to eliminate *Skidmore*'s recognition of various justifications for deference depending on statutory circumstances and agency action." *Id.* Statutory circumstances in the form of section 6110(k)(3) call for no deference to written determinations such as private letter rulings.

Moreover, these kinds of guidance are directed to individual taxpayers in particular situations. They are neither rules of general application nor adjudications. Although issued by the IRS National Office and subject to varying degrees of review, these informal interpretations are like litigating positions in that they represent the opinion of individual lawyers considering the issue. They do not receive review and approval by policymakers.

Neither should most notices qualify for full *Skidmore* deference since they are little more than an announcement of a litigating position or an announcement of proposed regulations to be issued. As described below, litigating positions should receive no deference. Since a proposed regulation receives no deference, a state-

[90]A "written determination" is a ruling, determination letter, technical advice memorandum, or "Chief Counsel advice." I.R.C. § 6110(b)(1)(A). The definition of "Chief Counsel advice" in section 6110(i)(1)(A) is broad enough to encompass the recent spate of newly fashioned guidance issued to the field by the Chief Counsel's national office, *e.g.*, field service advice. *Accord* C.C.A. 2001-46-056 (Nov. 16, 2001) (treating field service advice as a "written determination" within the meaning of section 6110(k)(3) and as without precedential value).

[91]Precedent is defined in Black's Law Dictionary (7th ed. 1999) as providing "a basis for determining later cases." Section 6110(k)(3) also permits the Secretary to establish "by regulation" a rule which would override the restriction regarding use as precedent. No such rule has been promulgated; such inaction by the IRS would be relevant under *Mead*.

[92]Consistent with this position is Notice CC-2004-012, (Feb. 19, 2004), which sets forth a number of Q&As dealing with how the Office of Chief Counsel renders legal advice to the field. Question 27 asks whether the written advice represents the "Service position." The answer is "No," because the Chief Counsel Advice "reflects the analysis and conclusion of a particular office within Chief Counsel."

ment anticipating a proposed regulation certainly should not have a higher status. However, there are some notices (*e.g.*, Notice 1998-6, 1998-1 C.B. 337) that announce substantive rules on which taxpayers may rely, that are issued by the same high level personnel as are revenue rulings, with essentially the same deliberative process, and that are published in the Internal Revenue Bulletin. This combination parallels a revenue ruling and, therefore, this limited category of notices should obtain the same *Skidmore* deference as a revenue ruling.

Similarly, positions developed during litigation and not otherwise found in previously published guidance upon which a taxpayer could have relied should receive deference only to the extent that their logic and reasoning appeal to a reviewing court. Such is the rule expressed in *Bowen v. Georgetown University Hospital*, 488 U.S. 204 (1988), where the Court stated that "[d]eference to what appears to be nothing more than an agency's convenient litigating position would be entirely inappropriate." 488 U.S. at 213. *Mead* characterizes *Bowen* as standing for "near indifference" to an "interpretation advanced for the first time in a litigation brief." *Mead*, 533 U.S. at 228.[93]

Whether *Skidmore* deference should be given to an IRS position purporting to interpret an ambiguous regulation but taken for the first time in litigation is a particularly difficult issue. As discussed above in connection with the *Seminole Rock* doctrine, consistency is desirable for the administration of the tax laws and thus, any result that would give some litigating positions greater deference than others should be rejected. *Skidmore* itself suggests that its rule of deference applies only to interpretations "that were not of adversary origin." Since the line between an ambiguous and an unambiguous regulation is so difficult to draw, we see no reason to provide litigators for the IRS with an advantage that *Skidmore* seems to reject.

Moreover, the litigators of the Department of Justice and IRS District Counsel are not necessarily policy-driven. They receive limited guidance from the policy makers at the IRS.[94] Guidance to the general public should consider broad tax policy issues. As a matter of sound tax administration, the IRS should be encouraged to write clear regulations and to clarify them in revenue rulings or

[93]*See also* CSI Hydrostatic Testers v. Commissioner, 103 T.C. 398, *aff'd* 62 F.3d. 136 (5th Cir. 1995), discussed in Part II, Section D, *infra*, which would grant some deference only if the litigating position was based on an IRS position on which the taxpayer could rely or was a longstanding position.

[94]Indeed, a former Chief Counsel of the IRS recently felt the need to issue a memorandum specifying that Division Counsel must take positions in litigation that are consistent with current IRS positions set forth in published guidance, including revenue rulings. Chief Counsel Notice 2003-014 (May 28, 2003), *available at* http://www.irs.gov/pub/irs-ccdm/cc-2003-014.pdf (last visited Feb. 24, 2004); Chief Counsel Notice 2002-043 (Oct. 17, 2002), *available at* http://www.irs.gov/pub/irs-ccdm/pubguid.pdf (last visited Feb. 24, 2004). A precursor of this announcement can be found in Revenue Procedure 1964-22, 1964-1 C.B. 689. The binding nature of IRS regulations and other guidance with respect to the government is discussed in Benjamin J. Cohen & Catherine A. Harrington, *Is the Internal Revenue Service Bound by Its Own Regulations and Rulings?*, 51 TAX LAW. 675 (1998).

regulations as soon as an issue arises. Litigation is not the place to effectively modify a regulation. The Task Force stands by this recommendation even though post-*Mead*, the courts seemed to be split on according *Skidmore* deference to certain litigating positions. *See* Part II, Section E, *infra.*

Consistent with this recommendation, the Task Force believes that less formal materials, such as Publications, Forms, and Instructions, should receive no special deference treatment. Thus, courts should take them into account only if the logic or reasoning stated therein appeals to the court. Similarly, since AODs are not intended to serve as public guidance, and may not be cited as precedent, they also should receive no special treatment.

The Task Force does not believe that the Internal Revenue Manual or the IRS's Statement of Procedural Rules merit any deference whatsoever. These documents contain internal agency management rules and descriptions of IRS operations and do not purport to apply to taxpayers except as they might be incidentally affected by the rules or procedures reflected therein.

In sum, the Task Force believes that federal courts should take into account unofficial agency interpretations that have no precedential value under section 6110(k)(3) and litigating positions adopted in briefs only if the logic and reasoning stated therein appeal to the court, without deference for the experience of the agency.[95]

F. *Conclusion*

The Task Force believes that this set of recommendations reasonably accommodates both the traditional approach to judicial deference to tax interpretations and recent Supreme Court developments. It establishes a hierarchy based upon the authority of an administrative pronouncement and the degree of deliberation the IRS gives the pronouncement. These recommendations not only honor the case law, but also present a sufficiently clear cut, and thus workable, set of rules for courts to apply.[96]

PART II: ANALYSIS OF CASE LAW

Several sets of cases involving deference to administrative interpretations establish the backdrop for this Report. These cases fall into the following cat-

[95]The Task Force considered extending "courteous respect" for unofficial agency interpretations, including litigating positions. *Skidmore* deference is described as "respect" in both *Christensen* and *Mead*. *See* Christensen v. Harris County, 529 U.S. 576, 587 (2000); *Mead*, 533 U.S. at 235. This is not surprising, since "respect" is one definition of "deference." In Webster's *Encyclopedia Unabridged Dictionary of the English Language* (1989), the first meaning of deference is "submission or yielding to the judgment, opinion, will, etc. of another." This kind of deference takes place when *Chevron* applies. The second definition is "respectful or courteous regard." Such is the kind of deference appropriate where *Skidmore* applies. This Report avoids the slippery slope created by the term "respect." In any event, a court presumably treats all participants with respect.

[96]Of course, the uncertainties of *Mead* could be eliminated if Congress itself specified the degree of deference courts should afford to various agency pronouncements, whether specifically for tax law or more broadly. *See* Elizabeth Garrett, *Legislating* Chevron, 101 MICH. L. REV. (forthcoming 2003) (discussing ways in which Congress could legislate judicial deference, including use of authorization laws, appropriations bills, and omnibus appropriations legislation).

egories: Supreme Court cases involving deference to administrative agencies in general; Supreme Court cases involving deference to administrative interpretations of an agency's own regulations; Supreme Court cases involving deference to agency litigating positions; Supreme Court cases involving deference to IRS interpretations; and tax cases in the lower courts.

A. *Supreme Court Cases Involving Deference to Administrative Agencies in General: From* Skidmore *to* Mead

Skidmore. For many years, the Supreme Court adopted a "pragmatic and contextual" approach to the degree of deference afforded administrative agencies with deference ranging from "great" to "some" to "little," depending upon a variety of factors.[97] For example, in the classic case of *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), which involved a dispute between employees and their employer over overtime compensation, the Supreme Court considered the degree of deference due an interpretive bulletin and informal rulings of the Administrator of the Wage and Hour Division of the United States Department of Labor, which was not a litigant. Those rulings called for excluding sleeping and eating time from an employee's work week and for including all other on-call time. The Court observed that, while the Administrator's conclusions were not binding, "the Administrator's policies are made in pursuance of official duty, based upon more specialized experience and broader investigations and information than is likely to come to a judge in a particular case." 323 U.S. at 139. The Supreme Court explained:

> [T]he rulings, interpretations and opinions of the Administrator under this Act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance. The weight of such a judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control.

323 U.S. at 140.

The *Skidmore* test became an important model for judicial review of administrative interpretations. According to Professor Merrill, under *Skidmore*, "[t]he default rule was one of independent judicial judgment. Deference to the agency interpretation was appropriate only if a court could identify some factor or factors that would supply an affirmative justification for giving special weight to the agency views."[98] That is, application of *Skidmore* deference is a matter of judicial discretion; the agency has to earn the court's deference to its view by satisfying various factors.

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[97] *See generally* Thomas W. Merrill, *Judicial Deference to Executive Precedent*, 101 YALE L.J. 969, 972 (1992).

[98] *Id.*

Chevron. A decision now almost 20 years old, *Chevron v. Natural Resources Defense Council*, 467 U.S. 837 (1984), seemed to signal a move away from *Skidmore* and to a newly deferential judicial attitude toward administrative interpretation. Reviewing an EPA air quality regulation, the Supreme Court in *Chevron* decreed a two-step analysis:

> First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, . . . the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress. If, however, the court determines Congress has not directly addressed the precise question at issue, the court does not simply impose its own construction on the statute, as would be necessary in the absence of an administrative interpretation. Rather, if the statute is silent or ambiguous, the question for the court is whether the agency's answer is based on a permissible construction of the statute.

467 U.S. at 843-44 (citations omitted).

The Court went on to explain that a "court need not conclude that the agency construction was the only one it permissibly could have adopted to uphold the construction, or even the reading the court would have reached if the question initially had arisen in a judicial proceeding," *id.* at 843 n.3, before continuing:

> If Congress has explicitly left a gap for the agency to fill, there is an express delegation of authority to the agency to elucidate a specific provision of the statute by regulation. Such legislative regulations are given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute. Sometimes the legislative delegation to an agency on a particular question is implicit rather than explicit: In such a case, a court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.

467 U.S. at 843-44 (citations omitted). Many scholars and lower courts have viewed *Chevron* as revolutionary, representing a "profound departure from the general principle that courts are the primary interpreters of the law"[99] and a "counter-Marbury for the administrative state."[100] Judicial deference, rather than independent judicial judgment, thus became an important norm. *Chevron* relied in part on the democratic pedigree of executive agencies to justify this deference; agencies must answer to the president, to Congress, and thus indirectly to the voters, for their interpretations of the law.

Since *Chevron* was decided, however, the Supreme Court has displayed a great deal of inconsistency about whether *Chevron* deference under step two[101]

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[99]Kenneth A. Bamberger, *Provisional Precedent: Protecting Flexibility in Administrative Policymaking*, 77 N.Y.U. L. REV. 1272, 1273 (2002).

[100]*See* Sunstein, *supra* note 1, at 2075 (1990).

[101]This Report is focused solely on the deference issues decided under step two of *Chevron*, which applies when Congress has not spoken clearly to the issue. The Supreme Court in tax cases has been able to stop at step one, which involves the "unambiguously expressed intent of Congress." *See* Atlantic Mutual Ins. Co. v. Commissioner, 523 U.S. 382, 387 (1998), discussed *infra*. Step one has

applies to interpretations developed through informal agency decision-making procedures, such as policy statements, manuals, and opinion letters. *Compare* EEOC v. Arabian American Oil Co., 499 U.S. 244, 256-58 (1991) (some but not *Chevron* deference to EEOC guidelines) *and* Stinson v. U.S., 508 U.S. 36, 44-45 (1993) (no *Chevron* deference to Sentencing Commission guideline commentary) *with* Your Home Visiting Nurse Service v. Shalala, 525 U.S. 449, 452-53 (1999) (*Chevron* deference to Medicare manual); NationsBank v. VALIC, 513 U.S. 251, 256-57 (1995) (*Chevron* deference to Comptroller of the Currency opinion letter); Pension Benefit Guaranty Corp. v. LTV Corp., 496 U.S. 633, 647-48 (1990) (*Chevron* deference to opinion letter); *and* Young v. Community Nutrition Inst., 476 U.S. 974, 978-79 (1986) (*Chevron* deference to no-action decision).

Christensen. The Court confronted the problem of deference due informal guidance in *Christensen v. Harris*, 529 U.S. 576 (2000). There, it refused to accord *Chevron* deference to an opinion letter of the United States Department of Labor's Wage and Hour Division. The opinion explained that the agency's interpretation was "contained in an opinion letter, not one arrived at after, for example, a formal adjudication or notice-and-comment rulemaking. Interpretations such as those in opinion letters—like interpretations contained in policy statements, agency manuals, and enforcement guidelines, all of which lack the force of law—do not warrant *Chevron*-style deference." 529 U.S. at 587. The opinion continues, "Instead, interpretations contained in formats such as opinion letters are 'entitled to respect' under our decision in *Skidmore v. Swift & Co.*, 323 U.S. 134 . . . (1944), but only to the extent that those interpretations have the 'power to persuade.'" *Id.* The majority opinion does not cite or discuss the Court's contrary decisions applying *Chevron* deference to such informal pronouncements. Nowhere does it state that the earlier decisions are no longer good law. Neither does *Christensen* indicate which kinds of administrative interpretations, other than notice-and-comment rulemaking or formal adjudication, are entitled to *Chevron* deference and which are not.

Mead: *Reinterpreting* Chevron. More recently, in *United States v. Mead Corp.*, 533 U.S. 218 (2001), the Supreme Court held that a tariff classification ruling issued by the United States Customs Service was not entitled to judicial deference under *Chevron* but was "eligible to claim respect according to its persuasiveness," *id.* at 221, under *Skidmore*.

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its own set of issues, which are beyond the scope of this paper, but a robust application of step one may result in many cases never reaching the deference issues inherent in step two. *See* Elizabeth Garrett, *Step One of* Chevron v. National Resources Deference Council, (Third Revised Draft), prepared for the Scope of Judicial Revision portion of the Project on the Administrative Procedure Act, June 2001, *available at* http://www.abanet.org/adminlaw/apa/chevron_revised_3.doc (last visited Feb. 24, 2004); Irving Salem & Richard Bress, *Agency Deference Under the Judicial Microscope of the Supreme Court*, 88 TAX NOTES (TA) 1257 (2000).

In a passage of critical importance, the Court held that "administrative implementation of a particular statutory provision qualifies for *Chevron* deference when it appears that Congress delegated authority to the agency generally to make rules carrying the force of law and that the agency interpretation claiming deference was promulgated in the exercise of that authority." *Id.* at 226-27. The opinion continues, "Delegation of such authority may be shown in a variety of ways, as by an agency's power to engage in adjudication or notice-and-comment rulemaking, or by some other indication of a comparable congressional intent." *Id.* It offers no guidance, however, as what "some other indication" might be. Thus, *Mead* refuses to define a bright line rule for application of *Chevron.*

The opinion rejects the notion that Congress intended administrative action to be given either *Chevron* deference or no deference at all. Together, *Mead* and *Christensen* give renewed life to the *Skidmore* standard, under which the degree of judicial deference to an administrative interpretation varies, in the language of *Mead*, with "the merit of the writer's thoroughness, logic and expertness, its fit with prior interpretation and any other sources of weight." *Mead*, 533 U.S. at 235.

Justice Scalia alone dissented in *Mead.* He predicted that courts will be sorting out the consequences of the *Mead* doctrine for years to come, that the principal effect of the majority's decision will be "protracted confusion," and that *Skidmore* deference will prove to be "a recipe for uncertainty, unpredictability, and endless litigation." *Id.* at 239, 245, 253.

Barnhart. Not long after *Mead* was decided, the Supreme Court reemphasized in *Barnhart v. Walton*, 535 U.S. 212 (2002), that *Mead* does not require notice-and-comment rulemaking for *Chevron* deference to apply. The question in *Barnhart* was whether the Social Security Administration had properly interpreted the language of the Social Security Act to limit eligibility for disability insurance to those who had demonstrated an inability to engage in any substantial gainful activity for a continuous period of 12 months. Although the agency had, in fact, recently issued notice-and-comment regulations addressing the interpretive issue,[102] the Court went out of its way to address the role of *Chevron* deference with respect to the agency's earlier interpretation to the same effect, as stated in a ruling, a manual, and a letter:

> And the fact that the Agency previously reached its interpretation through means less formal than "notice and comment" rulemaking . . . does not automatically deprive that interpretation of the judicial deference otherwise its due. . . . Indeed, *Mead* pointed to instances in which the Court has applied *Chevron* deference to agency interpretations that did not emerge out of notice-and comment-rulemaking. . . . It indicated that whether a court should give such deference depends in significant part upon the interpretive method used and the

[102]The Court also noted that the fact that the regulations had been recently issued, perhaps in response to the litigation, did not invalidate them or permit the Court to ignore them. *Barnhart*, 535 U.S. at 221 (citing Smiley v. Citibank (South Dakota), 517 U.S. 735, 741 (1996). See Part II, Section E(3), *infra*, for further discussion of deference to litigating positions.

> nature of the question at issue. . . . And it discussed at length why *Chevron* did not require deference in the circumstances there present—a discussion that would have been superfluous had the presence or absence of notice-and-comment rulemaking been dispositive.

535 U.S. at 221-22. The opinion emphasizes that the interpretation was longstanding and that an agency's interpretation of its own regulations is granted considerable leeway. It then lists a unique and novel set of factors that call for *Chevron* deference to the interpretation at issue: "the interstitial nature of the legal question, the related expertise of the Agency, the importance of the question to administration of the statute, the complexity of that administration, and the careful consideration the Agency has given the question over a long period of time." *Id.* at 522.

Conclusion. The factors listed in *Barnhart* for *Chevron* deference bear a striking similarity to the factors listed in *Mead* for *Skidmore* deference and thus make the choice between the two a difficult and confusing one for lower courts to make. Nonetheless, *Barnhart*, *Mead*, and *Christensen* force a choice between *Chevron* and *Skidmore*, and that choice is critical. Under *Chevron*, the IRS may choose among reasonable alternatives, and the agency will prevail even though the court or the taxpayer can supply a better reading of the statute. Not so under *Skidmore*;[103] when the Court in *Christensen* adopted *Skidmore* deference, it rejected the agency's view and adopted a view that it thought reflected a better reading of the statute. Admittedly, *Skidmore*, with its talk of the agency's specialized experience and broader information, may embody a tilt in favor of the agency. Under *Skidmore*, deference to an agency interpretation is tested under such criteria as consistency, thoroughness, validity of reasoning, or other factors giving the agency decision the power to persuade. Thus, the power to persuade under *Skidmore* may embody more than merely the logical power and consistency of the reasoning. The experience and informed judgment of the administrative agency can also come into play and, as a result, a court's choice between the position of the taxpayer and the government as litigants may not be the same as the choice between the arguments of two private parties, although this difference is difficult to quantify or specify precisely. Nonetheless, the courts ultimately determine what the law is under *Skidmore*. Under the *Skidmore* doctrine, a court is free to adopt what it views as the better interpretation of the statute.

As discussed *infra*, however, the Supreme Court has not relied on step two of *Chevron* in tax cases, despite ample opportunity, and this inconsistency makes the impact of *Mead* on tax law uncertain. Moreover, even if *Mead* applies to require a choice between *Skidmore* and *Chevron*, the basis for choosing between them is also uncertain.

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[103]Justice Scalia, however, does not read *Skidmore* in this manner. He writes, for example, "whereas previously, when agency authority to resolve ambiguity did not exist the court was free to give the statute what it considered the best interpretation, henceforth the court must supposedly give the agency view some indeterminate amount of so-called *Skidmore* deference." *Mead*, 533 U.S. at 239 (Scalia, J., dissenting). Since *Mead*, however, lower courts have felt free to substitute their own views for that of the IRS under *Skidmore*. *See* Part II, Section E(3), *infra*.

B. *Supreme Court Cases Involving Deference to Administrative Interpretations of an Agency's Own Regulations:* Seminole Rock *and Its Progeny*

Another series of Supreme Court cases addresses the degree of deference that courts owe to administrative interpretations of an agency's own regulations. The leading case in this series is *Seminole Rock* in which the Supreme Court held, in a dispute regarding the meaning of the words "highest price" in pricing regulations that the Office of Price Administration had issued pursuant to the Emergency Price Control Act of 1942, that the interpretation by the agency should control. Facially, *Seminole Rock* affords the agency extremely broad authority:

> Since this involves an interpretation of an administrative regulation a court must necessarily look to the administrative construction of the regulation if the meaning of the words used is in doubt. The intention of Congress or the principles of the Constitution in some situations may be relevant in the first instance in choosing between various constructions. But the ultimate criterion is the administrative interpretation, which becomes of controlling weight unless it is plainly erroneous or inconsistent with the regulation.

325 U.S. at 413-14, (emphasis added). The Court did not explain why a court "must necessarily" look to the administrative construction and cited no authority for so high a level of deference as "controlling . . . unless plainly erroneous."[104] Nor was such a rule necessary in the case since the Court concluded that the regulation was not ambiguous and "clearly applies to the facts." The Court, however, may have perceived a need to lay down a broad rule because it was interpreting not a statute but a pricing regulation and, in such a case, the "only [interpretative] tools, therefore, are the plain words of the regulation and any relevant interpretations of the Administrators." *Id.* at 414.

In *Auer v. Robbins*, 519 U.S. 452 (1997), the Supreme Court gave *Seminole Rock* deference to a clarification of a Department of Labor regulation set forth for the first time in an *amicus* brief that was filed at the request of the Court. Over the petitioner's argument that the Department's interpretation was not entitled to deference because it came in the form of a legal brief, the Court asserted that "[t]here is simply no reason to suspect that the interpretation does not reflect the agency's fair and considered judgment on the matter in question." 519 U.S. at 462. The quotation suggests that when an agency offers an interpretation as an *amicus* rather than as a party litigant, it is likely to be acting as a disinterested expert witness and, therefore, there is little risk that the interpretation being advanced was formulated simply to win the litigation.[105]

The Court's most detailed statement about deference to an agency's interpretation of its own regulations came in *Thomas Jefferson University v. Shalala*, 512 U.S. 504 (1996), which involved a position of the Secretary of Health and

[104]In *Gardebring v. Jenkins*, 485 U.S. 415, 430 (1988), the Court made an even stronger statement: "[W]e are properly hesitant to *substitute* an alternative reading for the Secretary's *unless that alternative reading is compelled* by the regulation's plain language or by other indications of the Secretary's intent at the time of the regulation's promulgation." (emphasis added).

[105]Of course, the drafters of an *amicus* brief might well have their eyes on other current or potential cases involving the agency.

Human Services, as a litigant, regarding Medicare reimbursement for certain educational costs incurred by a teaching hospital. The Secretary interpreted its own regulations as barring reimbursement under the circumstances. With the help of *Seminole Rock* deference, the agency's interpretation prevailed, 5 to 4. The Court wrote:

> We must give substantial deference to an agency's interpretation of its own regulations. . . . Our task is not to decide which among several competing interpretations best serves the regulatory purpose. Rather, the agency's interpretations must be given "controlling weight unless it is plainly erroneous or inconsistent with the regulation. . . . In other words, we must defer to the Secretary's interpretation unless an "alternative reading is compelled by the regulation's plain language or by other indications of the Secretary's intent at the time of the regulation's promulgation. . . . This broad deference is all the more warranted when, as here, the regulation concerns "a complex and highly technical regulatory program," in which the identification and classification of relevant criteria necessarily require significant expertise and entail the exercise of judgment grounded in policy concerns.

512 U.S. at 512. In the dissent, Justice Thomas argued that the doctrine unwisely encourages vague or ambiguous regulations:

> It is perfectly understandable, of course, for an agency to issue vague regulations, because to do so maximizes agency power and allows the agency greater latitude to make law through adjudication rather than through the more cumbersome rulemaking process. Nonetheless, agency rules should be clear and definite so that affected parties will have adequate notice concerning the agency's understanding of the law.

512 U.S. at 525 (Thomas, J., dissenting).

Scholars have suggested that the rationale for deferring to an agency's interpretation of its own regulations is analogous to the rationale supporting *Chevron* deference.[106] If Congress has delegated power to an agency to fill in legislative gaps, then courts should defer to any reasonable interpretation that an agency provides with respect to its own regulations. Because agencies are part of the executive branch under an elected President, it is more appropriate that an agency, rather than a court, undertake that function. The power to authoritatively interpret its own regulations may be viewed as a component of an agency's delegated lawmaking powers.[107] Moreover, as *Chevron* explains, an agency can be seen as

[106]*See* Manning, *supra* note 1, at 627-44.

[107]*See* Martin v. Occupational Safety & Health Review Comm'n, 499 U.S. 144, 151 (1991). In *Martin*, which involved deference to the Department of Labor's interpretation of Occupational Safety and Health regulations issued by that Department, the Court stated, "Because applying an agency's regulation to complex or changing circumstances calls upon the agency's unique expertise and policymaking prerogatives, we presume that the power authoritatively to interpret its own regulations is a component of the agency's delegated lawmaking powers." *Martin* imposes a limitation not suggested in *Seminole Rock*, however. The agency obtains deference only "so long as its interpretation 'sensibly conforms to the purpose and wording of the regulations.'" 499 U.S. at 150-51 (quoting N. Ind. Pub. Serv. Co. v. Porter County Chapter of Izaak Walton League of America, 423 U.S. 12, 15 (1975)).

having more expertise, and as being more politically accountable, than the courts.

Mead, however, undermines this view of the *Seminole Rock* doctrine. Since *Mead* conditions *Chevron* deference both on Congress delegating authority to the agency to issue rules that have the force of law and on the agency interpretation being promulgated in the exercise of that authority, few, if any, interpretations of agency regulations would qualify for *Chevron* deference. *Mead* never mentions *Seminole Rock* and thus fails to reconcile the relationship between *Seminole Rock* and *Chevron* as reinterpreted by *Mead*.

C. *Supreme Court Cases Involving Deference to Agency Litigating Positions*

Litigating positions that do not involve interpretation of ambiguous regulations present another set of considerations. In *Bowen v. Georgetown University Hospital*, 488 U.S. 204 (1988), the Secretary of Health and Human Services presented a new interpretation of the Medicare Statute in his brief to the Court. The Court declined to defer to that interpretation, stating that "[d]eference to what appears to be nothing more than an agency's convenient litigating position would be entirely inappropriate." 488 U.S. at 213. Accordingly, the Court concluded that courts must not defer to "agency litigating positions that are wholly unsupported by regulations, rulings, or administrative practice." *Id.* at 212.

> To the contrary, we have declined to give deference to an agency counsel's interpretation of a statute where the agency itself has articulated no position on the question, on the ground that "Congress has delegated to the administrative official and not to appellate counsel the responsibility for elaborating and enforcing statutory commands."

Id. (citations omitted).

The *Mead* opinion characterized *Bowen* as standing for "near indifference" to an "interpretation advanced for the first time in a litigation brief." *Mead*, 533 U.S. at 228. *Mead*, however, fails to address the question of whether *Seminole Rock* or *Bowen* controls if an interpretation of an ambiguous regulation is first articulated during litigation.

A different rule applies when an agency promulgates a regulation in direct response to litigation, rather than merely stating its interpretation in a brief. In *Smiley v. Citibank*, 517 U.S. 735 (1996), the Supreme Court held that a regulation issued by the Comptroller of the Currency in direct response to litigation stood on the same footing as any other regulation. While citing no authority for this position, the Court distinguished regulations from litigating positions under the following theory:

> Of course we deny deference "to agency litigating positions that are wholly unsupported by regulations, rulings, or administrative practice," . . . . But we have before us here a full-dress regulation, issued by the Comptroller himself and adopted pursuant to the notice-and-comment procedures of the Administrative Procedure Act designed to assure due deliberation. . . . That it was litigation which disclosed the need for the regulation is irrelevant.

Id.

The Court in *Smiley* limited its support for litigating regulations by saying that some litigating regulations might be arbitrary (and hence invalid) if there were a sudden and unexpected change in position which "does not take account of legitimate reliance on prior interpretation." *Id.* at 742. In the view of the Court, however, the position taken by the Comptroller of the Currency reflected positions previously taken in interpretive letters and many *amicus* briefs. *Id.* at 742-43.[108]

Conclusion. Case law affords no deference to positions developed by litigators for the first time in briefs. Similarly, positions taken in regulations are given full *Chevron* deference, even if a regulation is promulgated in response to pending litigation.

D. *Supreme Court Cases Involving Deference to IRS Interpretations of the Tax Law*

A seemingly separate line of Supreme Court cases addresses deference to regulations and other interpretations of the Internal Revenue Code. In *Skidmore* itself, the Supreme Court looked to tax law as a model, observing that it had "long given considerable and in some cases decisive weight to Treasury Decisions and to interpretive regulations of the Treasury and of other bodies that were not of adversary origin." 323 U.S. at 140. Since *Skidmore*, courts, including the Supreme Court, have generally deferred to tax interpretations so long as they are "reasonable."

Pre*-Chevron *Cases. In *United States v. Correll*, 389 U.S. 299 (1967), for example, the Supreme Court upheld a regulation permitting deductions for meals (as traveling expenses) only if a trip requires a stop for sleep or rest.[109] The Court concluded:

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[108]Lower courts have deferred to tax regulations directed at a pending controversy. For example, the insurance industry failed in its attempt to characterize Regulation section 1.809-9 (dealing with whether a differential earnings rate could be negative) as a "fighting regulation" unworthy of deference. Their argument emphasized that the regulation at issue reflected a reversal of the IRS's informal ruling position, and that the IRS had announced, four years prior to issuing the regulation, what the regulation would provide, suggesting that the IRS had "made up its mind" well before, and with indifference to, the normal deliberative process. The District Court in *Indianapolis Life Insurance Co. v. United* States, 940 F. Supp. 1370 (S.D. Ind. 1996), thought that *Chevron* was dispositive in that the only test was whether the regulation was reasonable. The Court of Appeals affirmed, ignoring *Chevron*: "[T]hey would require courts to disregard all federal tax regulations, because the Treasury is vitally interested in every tax case, and most tax questions sooner or later come to litigation. Regulation 1.809-9(a) is no worse than most, and better than some." Indianapolis Life Ins. Co. v. United States, 115 F.3d 430, 436 (7th Cir. 1997). In *United Dominion Industries v. Commissioner*, 532 U.S. 822, 838 (2001), the Supreme Court invited the IRS to change its regulation, agreeing with the IRS that "the Internal Revenue Code vests ample authority in the Treasury to adopt consolidated return regulations to effect a binding resolution of the question presented in this case."

[109]An interpretation to the same effect was first expressed in a 1940 ruling. I.T. 3395, 1940-2 C.B. 64. By the time the case reached the Supreme Court, the interpretation had been embodied in a regulation. *See* Correll v United States, 369 F.2d 87 (6th Cir. 1966) (citing Reg. § 1.162-17(b)(3)ii), (b)(4), (c)(2)).

> Alternatives to the Commissioner's sleep or rest rule are of course available. Improvements might be imagined. But we do not sit as a committee of revision to perfect the administration of the tax laws. Congress has delegated to the Commissioner, not the courts, the task of prescribing "all needful rules and regulations for the enforcement" of the Internal Revenue Code. 26 U.S.C. § 7805(a). . . . The role of the judiciary in cases of this sort begins and ends with assuring that the Commissioner's regulations fall within his authority to implement the congressional mandate in some reasonable manner.

389 U.S. at 305. *Correll* relied in large part on *Helvering v. Winmill*, 305 U.S. 79 (1938), perhaps the most significant legislative reenactment case. The Court saw the issue in *Correll* as falling squarely within the "settled principle" of *Winmill* that "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." *Correll*, 389 U.S. at 305 (quoting *Winmill*, 305 U.S. at 83). The Court continues to defer to the IRS if it finds a tax regulation "reasonable," and implicit Congressional approval has continued to be important to a finding of reasonableness.

The Supreme Court expanded on the "reasonableness" test in *National Muffler Association v. United States*, 440 U.S. 472 (1978). Upholding a denial of tax exemption for a trade association pursuant to standards prescribed in a regulation under section 501(c)(6), the Court quoted the reasonableness language from *Correll*. In language reminiscent of *Skidmore*, the Court then continued:

> In determining whether a particular regulation carries out the congressional mandate in a proper manner, we look to see whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose. A regulation may have particular force if it is a substantially contemporaneous construction of the statute by those presumed to have been aware of congressional intent. If the regulation dates from a later period, the manner in which it evolved merits inquiry. Other relevant considerations are the length of time the regulation has been in effect, the reliance placed on it, the consistency of the Commissioner's interpretation, and the degree of scrutiny Congress had devoted to the regulation during subsequent re-enactments of the statute.

440 U.S. at 477. The Court concluded that the regulation, although not the only possible reading of the statutory language, merited "serious deference" under the factors listed. *Id.* at 484. The *National Muffler* analysis melds aspects of *Skidmore* and *Chevron*. Like *Skidmore*, it considers many factors, but like *Chevron*, it evidences a high degree of deference to administrative decisions.

Although the Supreme Court has generally adopted this "reasonableness" test for interpretations of tax law, it has also distinguished between regulations promulgated pursuant to authority granted in a specific substantive provision of the Internal Revenue Code and those promulgated under the general authority of section 7805(a), which directs the Secretary of the Treasury "to prescribe all needful rules and regulations for the enforcement of this title."[110] The Supreme

[110]As explained *supra*, in the tax area, regulations promulgated under a grant of regulatory authority in a specific substantive section of the Code are generally referred to as legislative regulations,

Court wrote in *Rowan Cos. v. United States*, 452 U.S. 247, 253 (1981), and reiterated in *United States v. Vogel Fertilizer*, 455 U.S. 16, 24 (1982), that when a regulation is issued under the general authority of section 7805(a), "we owe the interpretation less deference than a regulation issued under a specific grant of authority to define a statutory term or prescribe a method of executing a statutory provision." With both kinds of regulations, a court defers to the choice of the IRS among acceptable alternatives. With legislative regulations, acceptability is judged by an "arbitrary and capricious" standard; with interpretive regulations, the standard is "reasonableness."[111]

Post*-Chevron *Cases. Without comment, the Supreme Court has adhered to the reasonableness test of *Correll* and *National Muffler* in its tax cases dealing with interpretive regulations decided since *Chevron.*[112] For example, in *Cottage Savings*, the issue was whether a financial institution realizes tax-deductible losses when it exchanges its interest in one group of residential mortgage loans for another lender's interests in a different group of residential mortgage loans. To answer that question, the Court looked to Regulation section 1.1001-1, which construed the statutory phrase "disposition of property" in section 1001 as requiring a material difference. The opinion cites both *Correll* and *National Muffler* in explaining that a court must defer to the Commissioner's regulatory interpretations of the Code so long as they are reasonable. 499 U.S. at 561. The opinion quotes the language from *Correll* quoting the language from *Winmill* regarding deemed congressional approval and legal effect of longstanding Treasury regulations and interpretations. *Cottage Savings* concluded that the regulation was reasonable because both the statutory language and the IRS requirement of a material difference were longstanding and because the material differ-

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and those promulgated under the general authority of section 7805(a) are generally referred to as interpretive. In other areas of law, regulations promulgated pursuant to language such as that in section 7805(a) are characterized as legislative regulations because the agency's regulatory authority derives from an explicit statutory grant. See United States v. Haggar Apparel Co., 526 U.S. 380 (1999); United States v. O'Hagan, 521 U.S. 642 (1997); Sullivan v. Zebley, 493 U.S. 521 (1990); *but see* Merrill & Watts, *supra* note 24.

[111]For an analysis of the components of the arbitrary and capricious review, see Lisa Bressman, *Review of the Exercise of Discretion,* ABA Section of Administrative Law and Regulatory Practice APA Project: Judicial Review drafts, *available at* http://www.abanet.org/adminlaw/apa/restatement8-2001.doc (last visited Feb. 24, 2004). Professor Bressman notes that "many cases applying the arbitrary and capricious test do so to assess the 'reasonableness' of an agency interpretation either as a part of the *Chevron* Step Two inquiry or as a separate requirement." *Id.* at 2.

[112]In *United States v. Boyle*, 469 U.S. 241 (1985), the Supreme Court upheld a regulation interpreting the phrase "reasonable cause" in section 6651(a)(1), which excuses a late filing penalty. The Court stated that the "Service's correlation of 'reasonable cause' with 'ordinary business care and prudence' is consistent with Congress's intent, and over 40 years of case law as well." *Id.* at 247 n.4 It concluded that the IRS's interpretation "merits deference." It based the deference grant by citing *Chevron* as a mere example: "*See, e.g., Chevron. . . .*" This citation suggests that a number of other cases, such as *National Muffler*, would produce the same result. Moreover, if the Court were relying on *Chevron*, longstanding case law would not be significant. Since all of the other post-*Chevron* Supreme Court tax cases clearly do not rely on *Chevron* (see *infra* Part II, Section D for a detailed discussion of the Court's post-*Chevron* tax decisions), we believe that the timid step-two reference to *Chevron* in *Boyle* suggests that the Court was not prepared in 1985 to shift to *Chevron* in tax cases.

ence requirement was consistent with the Court's own landmark precedent on realization. The case did not so much as cite *Chevron*, which had been decided seven years earlier.

Similarly, *United States v. Cleveland Indians Baseball Company*, 532 U.S. 200 (2001), cites *Correll*, *National Muffler*, and *Cottage Savings*, but not *Chevron*, in giving "substantial deference" to the IRS's "steady interpretation" of a 61 year old regulation, which implemented a 62 year old statute. 532 U.S. at 220. Oddly, the *Cleveland Indians* opinion ignores *Seminole Rock* as well as *Chevron*.[113] The Court focused its deference analysis on the longstanding existence of the IRS interpretation at issue and bolstered its position by noting that the underlying Code section had been reenacted during the life of the administrative interpretation. "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law." *Id.* One can only speculate on whether the Court would have granted "substantial deference" if there had been no supporting legislative reenactment argument.

The Court has continued to distance itself from *Chevron* as well as *Seminole Rock* in tax cases. In *Atlantic Mutual Insurance Co. v Commissioner*, 523 U.S. 382 (1998), the Court did cite *Chevron*, but it did so only in passing, and only as to step one. *Atlantic Mutual* upheld a regulation interpreting the statutory phrase "reserve strengthening" in a provision of the Tax Reform Act of 1986. The Court first considered the taxpayer's claim that the phrase had a plain meaning under the statute. It quoted *Chevron* for the proposition that, if the statute had the plain meaning claimed, the taxpayer would win because "the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." 523 U.S. at 387. The Court, however, determined that neither prior legislation nor industry use established a plain meaning for "reserve strengthening." Having made that determination, the Court did not, as we might expect, continue to rely on *Chevron*. Instead, the Court described its task as deciding "not whether the Treasury regulation represents the best interpretation of the statute, but whether it represents a reasonable one," and supported that statement with a citation to *Cottage Savings* alone. *Id.* at 549. *Atlantic Mutual*, thus, might be read as adopting *Chevron*'s two step analysis for tax and finding that the traditional reasonableness test for tax interpretations is applicable in step two of *Chevron*.

Most recently, in *Boeing Company v. United States*, 537 U.S. 437 (2003), the Court ignored both *Chevron* and *Mead*, despite the lower court's reliance on *Chevron* in its opinion and the government's reliance on both *Chevron* and

[113]The amount of deference owed to a revenue ruling interpreting a regulation was also at issue in *Cleveland Indians*. Rather than citing *Seminole Rock* for the proposition that an agency's interpretation of its own regulation is controlling unless plainly erroneous, the Court reasoned more modestly. Citing *Thomas Jefferson*, the Court gave "substantial deference" to the revenue ruling because it was longstanding and reasonable. 532 U.S. at 220. *See also* Davis v. United States, 495 U.S. 472, 484 (1990) (concluding that revenue rulings are given "considerable weight" if they involve contemporaneous construction of a statute and have been in long use, without citing *Chevron*).

Mead in its briefs. In *Boeing*, the Court upheld Regulation section 1.861-8(e)(3), which allocates research and development expenses between domestic and foreign sources, as applied to a domestic international sales corporation (DISC) by virtue of a cross-reference in Regulation section 1.994-1(c)(6)(iii). The Treasury Department, the opinion explains, could have promulgated a regulation addressing the proper allocation of research and development costs between the parent and its DISC subsidiary under specific authority delegated to it in section 994, but instead promulgated the regulation under the general authority of section 7805(a). The Court decided that even if the regulation at issue were regarded as "interpretive because it was promulgated under section 7805(a)'s general rulemaking grant rather than pursuant to a specific grant of authority," a court "must still treat the regulation with deference." 537 U.S. at 448. The opinion relies solely on *Cottage Savings* for this proposition.

The *Boeing* opinion then examined the regulation against the language of the statute. It found the IRS's position as "surely not arbitrary" and as offering the virtue of providing consistent treatment for cost items used in computing domestic and foreign income. The opinion considered the arguments of the taxpayer based on the statutory text and concluded they were "plainly insufficient to overcome the deference to which the Secretary's interpretation is entitled." *Id.* at 451. The Court did not apply *Skidmore* deference under which the agency interpretation must earn judicial respect. Its reasoning assumes that the regulation was entitled to deference, which, in certain circumstances, could be withheld by the court.

Conclusion. Readers of the Court's post-*Chevron* tax opinions are left wondering whether the Court applies a unique analysis when deciding cases involving deference to IRS interpretations of the tax law. The cases leave the relationship between *Chevron* and *National Muffler* unresolved.

E. *Tax Cases in the Lower Courts*

The relationship between *Chevron* and *National Muffler* has long puzzled lower courts. In *Walton v. Commissioner*, 115 T.C. 589, 598 (2000), *acq.*, 2003-44 I.R.B. 964, for example, the Tax Court bemoaned that "the opinion of the Supreme Court in *Chevron* failed to cite *National Muffler* and may have established a different formulation of the standard of review." The Second Circuit has characterized the choice between *Chevron* and *National Muffler* as "unsettled." General Electric Co. v. Commissioner, 245 F.3d 149, 154 n.8 (2001). In *Microsoft Corp. v. Commissioner*, 115 T.C. 228, 251 (2000), *rev'd* 311 F.3d 1178 (9th Cir. 2002), the parties avoided the dilemma by agreeing that *National Muffler* was the appropriate standard for judging the validity of the regulation.[114]

In *Rite Aid Corp. v. United States*, 255 F.3d 1357 (Fed. Cir. 2001), an important judicial deference case that invalidated legislative regulations dealing with

[114]The Tax Court upheld the regulation, but the Ninth Circuit reversed, finding that the regulation conflicted with the clearly expressed intent of Congress and the plain meaning of the statute. *Microsoft*, 311 F.3d at 1189. The Ninth Circuit opinion cites neither *Chevron* nor *Mead*.

consolidated returns, the Court of Appeals for the Federal Circuit did not apply the *Chevron* deference formula. The opinion barely mentions *Chevron* and makes no substantive use of it. Rather it cites and relies on *Rowan Cos,. Inc. v. United States*, 452 U.S. 247, 253 (1981), for the proposition that a regulation is contrary to the statute if "it is outside the scope of authority delegated under the statute." *Rowan*, in turn, relied heavily on *National Muffler*. The government, unhappy with the approach to judicial deference taken by the Federal Circuit, petitioned for rehearing and urged the Federal Circuit to adhere to the *Chevron* formula as specified by the Court of Appeals for the Sixth Circuit in another case, *Nichols v. United States*, 260 F.3d 632 (6th Cir. 2001), also involving the consolidated return regulations. The government's petition for rehearing was denied.

In several cases, as opinions acknowledge, the result would be the same under either standard.[115] Thus, the distance between a "permissible construction" in step two of *Chevron* and a "reasonable" construction in *National Muffler* might be negligible.[116] But in some cases, including those involving changes in policy, the standard used could lead to different results, as Justice Scalia argued in his *Mead* dissent.[117] *Chevron* itself involved a change in an EPA interpretation that reflected a change in administration, and thus of environmental policy. *Chevron* taught courts to bless such changes as part of our democratic process. A changed interpretation, however, would be neither contemporaneous nor longstanding, and would not have been relied on. Thus, it might not merit deference under *National Muffler*.

While the Supreme Court has not felt it necessary to apply *Chevron* analysis or the *Mead* framework to tax cases, many lower courts have felt obliged to do so. As discussed below, the post-*Mead* cases involving administrative interpretations of the tax law—whether in the form of regulations, revenue rulings, or less formal guidance—underscore the confusion both about whether *Mead* applies to tax law and about what *Mead* means if it does.[118]

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[115]*See Walton*, 115 T.C. at 598 ("In the case before us, we conclude that it is unnecessary to parse the semantics of the two tests [*Chevron* and *National Muffler*] to discern any substantive difference between them, because the result here would be the same under either.")

[116]The Court of Appeals for the Seventh Circuit observed in *Bankers Life & Casualty Co. v. United States*, 142 F.3d 973, 981-82 (7th Cir 1998), *cert. denied*, 525 U.S. 961 (1998), "While the two approaches articulate the level of deference differently, they both come down to one operative concept—reasonableness. Thus, *Chevron* and the traditional rule constitute two different formulations of a reasonableness test." In *Snap-Drape, Inc. v. Commissioner*, 98 F.3d 194, 197 (5th Cir. 1996), *cert. denied*, 522 U.S. 821 (1997), the Court of Appeals for the Fifth Circuit cited *Chevron* as the standard for legislative regulations as well as language from *Rowan Cos. v. United States*, 452 U.S. 247, 252 (1981), articulating the *National Muffler* standard—harmonization "with the plain language of the statute, its origin, and its purpose"—for interpretive regulations. *Snap-Drape*, 98 F.3d at 197.

[117]Justice Scalia noted that when it comes to changes in agency interpretation, *Chevron* and *Skidmore* take diametrically opposing views—*Chevron* requiring deference to the new position as within the authority of the Executive Branch, while *Skidmore* does not. *See* 533 U.S. at 247 (Scalia, J., dissenting). In this regard, *National Muffler*, with its attention to whether an interpretation is "longstanding," seems to be an heir of *Skidmore*.

[118]The discussion that follows considers lower court tax cases through the end of 2003.

1. *Regulations*

Traditionally, cases involving legislative regulations and cases involving interpretive regulations both cite *National Muffler* at the same time that courts afford interpretive regulations less deference than legislative regulations.[119] Lower courts applying *Chevron* to interpretive regulations have struggled to sort out whether *Chevron* increased the level of deference traditionally given to interpretive regulations under *National Muffler*. For example, in *People's Federal Savings and Loan Association v. Commissioner*, 948 F.2d 289 (6th Cir. 1991), the Court of Appeals for the Sixth Circuit reversed the Tax Court's invalidation of an interpretive regulation and chided the Tax Court for ignoring *Chevron*. According to the Sixth Circuit, interpretive regulations reflect an implicit legislative delegation of authority to the IRS, requiring deference under *Chevron*, a level of deference which the Sixth Circuit believed to be greater than that under *National Muffler*. 948 F.2d at 300.

Mead forces lower courts to consider whether the Supreme Court has now directed them to decrease the level of deference given interpretive regulations. As discussed earlier, the IRS takes the position that regulations promulgated under section 7805(a) are not binding rules under section 553(b) of the APA, and *Mead* requires that interpretations be announced with the force of law in order to partake of *Chevron* deference. Thus, courts must ask whether *Mead* has changed the level of deference owed to such regulations from the traditional standard of *National Muffler* to a lower standard under *Skidmore*.

Some courts have read *Mead* as not calling for a change in the standard for deference to regulations. In *Tax Analysts v. IRS*, 215 F. Supp. 2d 192 (D.D.C. 2002), *rev'd* 350 F.3d 1000 (D.C. Cir. 2003),[120] the court upheld Regulation section 301.6110-1(a), which interprets the phrase "written determinations under Section 6110" of the Code. *Id.* at 195. It concluded that the interpretation in the regulation was entitled to *Chevron* deference under *Mead* because it was a reasonable interpretation adopted "in a formal rulemaking process." *Id.* at 198. The opinion made no mention of whether the regulation was legislative or interpretive. Similarly, in *Marsh & McClennan v. United States*, 302 F.3d 1369 (Fed. Cir. 2002), the Court of Appeals for the Federal Circuit upheld Regulation section 301.6611-1(h), interpreting "due date" in connection with accrual of interest on overpayments. Under *Chevron* and *Mead*, it looked to the regulation, which it found reasonable, to resolve the statutory ambiguity. *Id.* at 1375-76. While the opinion discusses at length why the interpretation was reasonable, it does not discuss at all the regulation's status as either legislative or interpretive.

The Tax Court's reconsideration of *Redlark v. Commissioner*, 106 T.C. 31 (1996), in *Robinson v. Commissioner*, 119 T.C. 44 (2002), illustrates the dilemma courts face. In *Redlark*, the Tax Court had invalidated Temporary Regulation section 1.163T-8 and -9. Those regulations, which were promulgated

[119] *See* Aprill, *supra* note 30, at 60.

[120] The District Court analyzed the case under step two of *Chevron*; the Court of Appeals, in contrast, saw it as a step one case.

pursuant to section 7805(a), denied noncorporate taxpayers a deduction for interest on federal income tax deficiencies, even if the interest related to their businesses. The Tax Court, having found itself reversed by the Courts of Appeals for the Fourth, Sixth, Seventh and Ninth Circuits on the issue, revisited the question in *Robinson*. In an exhaustive analysis, citing not only *Chevron*, but also *Vogel Fertilizer*, *Correll*, *Atlantic Mutual*, *National Muffler*, and *Cottage Savings*, a majority of the Tax Court concluded that the statute was silent or ambiguous and that the regulation, therefore, was a permissible construction of the statute.

Five judges dissented. The dissents of both Judge Swift and Judge Vasquez discuss *Mead*. Judge Vasquez, joined by four other judges, wrote at length about the impact of *Mead*. He objected to the way in which the majority applied *Chevron* under pre-*Mead* case law because, in his mind, *Mead* narrowed the reach of *Chevron*. He concluded that, under *Mead*, the regulations were not entitled to *Chevron* deference because they were not issued pursuant to a "specific congressional delegation of authority having the force and effect of law,"[121] *i.e.*, because the regulations were issued pursuant to section 7805(a). 119 T.C. at 119-20. As a result, "the fact that a court pre-*Mead* found the agency's position to be reasonable under the *Chevron* standard is insufficient." *Id.* at 118. Having asserted that the majority was wrong in giving the regulation *Chevron* deference, Judge Vasquez tested the regulation's persuasiveness under *Skidmore*, and found it lacking, primarily because of its reliance on nonauthoritative Joint Committee on Taxation materials. *Id.* at 120-21.

Temporary Regulations. *Robinson* also raises the question of what degree of deference is owed to temporary regulations, post-*Mead*. Prior to *Mead*, courts generally did not distinguish between temporary and final regulations. Thus, temporary regulations were entitled to deference if they met the same tests applicable to final regulations. *See, e.g.*, E. Norman Peterson Marital Trust v. Commissioner, 78 F.3d 1289, 1297 (9th Cir. 1997) ("The fact that the regulation at issue is a temporary regulation does not change our analysis. Until the passage of final regulations, temporary regulations are entitled to the same weight we accord to final regulations."); *cf.* Kikalos v. Commissioner, 190 F.3d 791, 796 (7th Cir. 1999) (declining to decide the degree of deference that temporary regulations command because both parties had assumed that full *Chevron* deference was warranted).

In *New York Football Giants v. Commissioner*, 117 T.C. 152 (2001), which was decided after *Mead*, the Tax Court followed the pre-*Mead* cases and held that Temporary Regulation section 301.6245-1T was valid. As a legislative regulation promulgated pursuant to a specific grant of authority in section 6245, the

[121]For discussions by commentators who agree with this analysis, *see* John F. Coverdale, Chevron's *Reduced Domain: Judicial Review of Treasury Regulations and Revenue Rulings After* Mead, 55 ADMIN. L. REV. 39 (2003) (agreeing that interpretive regulations are entitled only to *Skidmore* deference post-*Mead*); Mitchell M. Gans, *Deference and the End of Tax Practice*, 36 REAL PROP., PROB. & TRUST J. 731 (2002); Merrill & Watts, *supra* note 24. *Robinson* was decided, and the articles were published, before the Supreme Court's decision in *Boeing*, which appears to use the special criteria for deference to regulations developed in tax cases.

court reasoned that it was entitled to greater deference than an interpretive regulation and, under *Chevron*, could be overturned only if arbitrary, capricious, or manifestly contrary to the statue. The opinion cited *Mead*'s holding for guidance as to when *Chevron* applies. Thus, the opinion, after *Chevron* and *Mead*, gives *Chevron* deference to a temporary legislative regulation, because it views the regulation as promulgated in the exercise of Treasury's delegated authority.

In *UnionBanCal Corp.*, the Court of Appeals for the Ninth Circuit reached very much the same conclusion, although it did so solely on the basis of *Chevron*, and without citation to *Mead*. The court rejected the taxpayer's argument regarding Temporary Regulation section 1.267(f)-1T(c)(6), governing the recognition of losses in a controlled group. The taxpayer argued, *inter alia*, that no deference to the regulation was required because it was promulgated without notice and comment. The Preamble to the regulations,[122] without explanation, stated that notice and comment was "impractical" because of "a need for immediate guidance." The court relied on *Chevron*, the APA, and the express delegation of authority in section 267 that losses not be recognized "until such time as may be prescribed in regulations" to reject the taxpayer's challenge.

The courts' analyses in *New York Football Giants* and *UnionBanCal*, however, are inconsistent with some readings of *Mead*. In his dissenting opinion in *Robinson*, for example, Judge Vasquez argued that *Mead* changed the traditional analysis. In a footnote, he took the position that in light of *Mead*, the temporary regulation at issue was not entitled to *Chevron* deference because it "did not go through notice and comment."[123] *Robinson*, 119 T.C. at 120 n.6 (Vasquez, J., dissenting). Judge Vasquez believes that after *Mead*, "*Chevron* deference is reserved for only those agency interpretations reached through notice-and-comment or comparable formal administrative procedures." *Id.* at 117. If failure to undergo notice and comment precludes deference under *Chevron* as expounded by *Mead*, then temporary regulations do not merit *Chevron* deference.

However, courts of appeals reviewing temporary Treasury regulations after *Mead* have emphasized the statement in *Mead* that *Chevron* deference does not require notice and comment.[124] Thus, in *Hospital Corporation of America v. Commissioner*, 348 F.3d 136 (6th Cir. 2003), the Sixth Circuit quoted *Mead* before upholding Regulation section 1.448-2T, which addresses treatment of expected uncollectible receivables following a change to the accrual method of accounting:

> The temporary regulations involved in this case were arrived at centrally by the Treasury Department after careful consideration. They were issued pursuant to statutory authority to 'prescribe' needful rules and regulations. *See* I.R.C.

[122]49 Fed. Reg. 46,992 (1984).

[123]Judge Vasquez's opinion also notes that "there is no evidence that it went through formal administrative procedures, and it remains in temporary form 15 years later." 119 T.C. at 120 n.6. Under current law, temporary regulations expire after three years. I.R.C. § 7805(e)(2).

[124]The District Court for the Middle District of North Carolina reached the same conclusion for a temporary legislative regulation in *Volvo Trucks North America v. United States*, No. Civ. 1:01CV00416, 2003 WL 223421 (M.D.N.C. Jan. 30, 2003).

> § 7805(a). The regulation was 'interpretive' in the same sense that the regulation in *Chevron* was interpretive—it gave content to ambiguous statutory terms. Congress clearly intended that the Treasury Department do so, and *Chevron* deference is therefore appropriate.[125]

Similarly, in reviewing the same temporary regulation as that at issue in *Robinson*, the Fifth Circuit in *Alfaro v. Commissioner*, 349 F.3d 225 (5th Cir. 2003), rejected the argument that issuance of the regulation without notice and comment eliminates *Chevron* deference. It upheld the regulation, citing to *Robinson* itself, to the five federal courts of appeals that upheld the regulation prior to the *Mead* decision, as well as to *Chevron* and *Mead*.

Thus, while some judges and commentators have read *Mead* as reducing the deference courts give to either interpretive or temporary regulations from *Chevron* to *Skidmore*, recent decisions from the courts of appeals have found temporary regulations to be entitled to *Chevron* deference. Failure of the IRS to provide notice and comment did not change the level of deference to the regulation.

2. *Revenue Rulings and Revenue Procedures*

Mead has also complicated the calibration of judicial deference due to revenue rulings, official interpretations by the IRS that are published in the Internal Revenue Bulletin as the IRS's legal conclusions based on stated facts. The Tax Court has traditionally afforded revenue rulings no deference whatsoever, while the federal appellate courts have varied in the amount of deference afforded to revenue rulings.[126] The Court of Appeals for the Federal Circuit, in *Mead*, comparing trade and tax matters, observed that "[c]ustoms' classifications rulings are in some ways an even less formalized body of interpretations than IRS revenue rulings." *Mead v. United States*, 185 F.3d 1304, 1307 (Fed. Cir. 1999). If, according to the Supreme Court in *Mead*, tariff classifications deserve *Skidmore* deference, it is unclear whether the more formalized body of interpretations represented by revenue rulings requires the higher deference of *Chevron* or whether they merit application only of *Skidmore*, perhaps with consideration of additional, or different, factors. Courts since *Mead* have had to grapple with that question.

These cases have taken a variety of approaches to the weight due to revenue rulings. To some courts, the open-ended language in *Mead* allows for the possibility that revenue rulings should receive *Chevron* deference.[127] For example, in a footnote in *American Mutual Life Assurance Co. v. United States*, 267 F.3d 1344, 1353 n.3 (Fed. Cir. 2001), the Court of Appeals for the Federal Circuit left for another day the question of whether revenue rulings are entitled to *Chevron* deference under the standards of *Mead*.

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[125]*Hospital Corp.*, 348 F.3d at 144-45. As noted earlier, *see supra* note 69, the Sixth Circuit observed that the regulation was not challenged for failure to undertake notice and comment.

[126]*See* Galler, *supra* note 10.

[127]One court did conclude, but only briefly, that under *Mead*, revenue rulings are entitled to *Chevron* deference. In *Ammex, Inc. v. United States*, No. 00-CV-73388, 2002 WL 32065583 (E.D. Mich. July 31, 2002), the court wrote:

A recent Ninth Circuit opinion reads *Mead* as directing lower courts to increase the weight given revenue rulings, albeit not to the degree of *Chevron* deference. In *Omohundro v. United States*, 300 F.3d 1065 (9th Cir. 2001), the Court of Appeals for the Ninth Circuit unambiguously concluded that the "Supreme Court decision in *Mead* . . . requires that we accord *Skidmore* deference to revenue rulings." 300 F.3d at 1069. As a result, the court overruled a 1994 case, Miller v. United States, 38 F.3d 473 (9th Cir. 1994), in which the court held that a taxpayer must file an income tax return within two years of payment of the taxes in order to recover a refund or credit. In reaching its conclusion, the court in *Miller* relied on certain language in the statute, as well as on the need to prevent forum shopping, but did not discuss or consider Revenue Ruling 1976-511, 1976-2 C.B. 482 (1976), which permitted a three-year limit on filing for refund. In light of *Mead*, however, *Omohundro* applied the *Skidmore* test to the ruling, and found the reasoning to be valid, consistent with later IRS pronouncements, and supported by the legislative history of section 6511. As a result, the Ninth Circuit held that a claim for credit or refund is timely if filed within three years from the date the income tax return is filed, regardless of when the return is filed.

In *Aeroquip-Vickers, Inc. v. Commissioner*, 347 F.3d 173 (6th Cir. 2003), the court of appeals engaged in a lengthy discussion concluding that in light of recent Supreme Court decisions, its position that revenue rulings deserve *Chevron* deference required reconsideration. It concluded that, under *Mead*, revenue rulings merited only *Skidmore* deference. In the case before it, it decided that consideration of various *Skidmore* factors called for some deference to the applicable revenue ruling, Revenue Ruling 1982-20, 1982-1 C.B. 6, which involved recapture of investment tax credits with respect to intercompany transactions that were part of a planned transfer outside of the consolidated group. The Sixth Circuit also concluded that the Tax Court mischaracterized the degree of deference to be given to revenue rulings by failing to acknowledge explicitly that some deference is due to them. The lengthy dissent agreed with the majority

> [T]he Supreme Court in *Mead* held a ruling could receive *Chevron* deference even if it was not specifically authorized by Congress and even if it did not go through the rigors of the APA. . . . In applying the *Mead* test to revenue rulings, it is clear that Congress delegated to the IRS the authority to make determinations having the force of law, *e.g.*, rules and regulations pursuant to I.R.C. § 7805(a). A revenue ruling promulgated by the Commissioner and approved by the Secretary under the express authority of § 7805 represents a formal interpretive rule. Therefore, after *Mead*, revenue rulings should be considered as controlling precedent unless shown to be arbitrary or capricious.

The judge later reversed his position, *see* Ammex, Inc. v. United States, No. 00-CV-73388, 2002 WL 31777584 (E.D. Mich. Oct. 22, 2002), in light of *The Limited v. Commissioner*, 286 F.3d 324 (6th Cir. 2002). In *The Limited*, the Sixth Circuit described revenue rulings as "typically the IRS's response to a hypothetical situation and as such . . . authoritative and binding on the IRS" but not binding on courts because they are "interpretive rulings by an administrative agency that do not require notice and comment." *The Limited*, 286 F.3d at 337. The Sixth Circuit relied on its own pre-*Mead* precedents in reaching its conclusion. *Id.* It cited only one Supreme Court case, United States v. Cleveland Indians Baseball Co., 532 U.S. 200 (2001), noting in a parenthetical that there the Supreme Court refrained from deciding the level of deference due revenue rulings, but gave the particular revenue ruling at issue "substantial judicial deference" because it reflected the IRS's longstanding interpretation of its own regulations. *Id.* at 338.

about the importance of *Mead* and that *Skidmore* deference applied to revenue rulings, but disagreed as to what *Skidmore* deference entails. According to the dissent, *Skidmore* deference is not an automatic deference to interpretive authority because *Skidmore* deference requires "persuasive reasoning" by the administrative agency. The dissent did not find the reasoning of Revenue Ruling 1982-20 persuasive.

In several other cases, courts have commented that, in light of *Mead*, revenue rulings merit some consideration, albeit not *Chevron* deference. In *Vons Companies, Inc. v. United States*, 51 Fed. Cl. 1 (2001), the Court of Federal Claims reiterated its view, in a discovery order, that revenue rulings are not binding precedent, but do require consideration. 51 Fed. Cl. at 8. In a footnote, the order suggests that *Mead* and other recent Supreme Court cases call into question any decisions that give revenue rulings the force of precedent under *Chevron*. *Id.* at 8 n.5.

The Court of Appeals for the Eighth Circuit, in *O'Shaughnessy v. Commissioner*, 332 F.3d 1125 (8th Cir. 2003), declined to defer to Revenue Ruling 1974-491, 1974-2 C.B. 290, which ruled that molten tin used in the manufacture of glass did not qualify as depreciable property. Although the IRS argued that *Mead* called for deference to the revenue ruling, the Court of Appeals looked primarily to *Cleveland Indians* as authority. It concluded that the revenue ruling before it, unlike the revenue ruling in *Cleveland Indians*, did not represent a longstanding consistent interpretation of an unchanged statute. The 1974 ruling involving the tin predated substantial changes to the depreciation system, had not been tested in the courts, and was not subsequently reconsidered by the IRS. As a result, "the district court did not err in declining to treat revenue ruling 74-491 as controlling or persuasive authority."

Mead has also influenced the Tax Court's attitude toward revenue rulings. In *Lunsford v. Commissioner*, 117 T.C. 159 (2001), Judge Halpern's concurring opinion acknowledges that the Tax Court has taken the view that revenue rulings receive no deference because they are merely opinions of a lawyer in the agency, but it also refers to *Mead*, in a "but see" citation, "for a discussion of the deference, but less than *Chevron* deference, owed to certain agency interpretations of a statute." 117 T.C. at 174 n.6 (Halpern, J., concurring). In *Tedokon v. Commissioner*, 84 T.C.M. (CCH) 657, 2002 T.C.M. (RIA) ¶ 2002-308, the Tax Court quoted the Ninth Circuit's discussion of *Mead* and *Skidmore* in *Omohundro*, and wrote, "Rev. Rul. 76-511, 1976-2 C.B. 428, likewise commands deference and is applicable to this case, since the fact pattern is the same."[128] In *Medical Emergency Care Associates v. Commissioner*, 120 T.C. 436 (2003), the Tax Court declined to defer to a revenue ruling, but did so only after a discussion of *Mead* and *Mead's* invocation of *Skidmore* and only after concluding that "we are unable to ascertain the thoroughness of the agency's consideration or the validity of its reasoning." *Id.* at 445.

[128]Nonetheless, it may be that the statement simply reflects the application of the rule, in *Golsen v. Commissioner*, 54 T.C. 742 (1970), since the Ninth Circuit is the court to which *Tedokon* would be appealed. Two other recent Tax Court cases observe that revenue rulings, although entitled to

Thus, a consensus seems to be emerging to give some weight to revenue rulings under *Skidmore*. Giving revenue rulings *Skidmore* deference would require some courts to increase the deference afforded revenue rulings, and others to decrease it. If *Mead's* approach does apply to tax law, *Mead's* invocation of *Skidmore* for tariff rulings undermines the Tax Court's traditional refusal to grant any deference to revenue rulings. As the case review above demonstrates, several judges, although not yet the Tax Court as a whole, assume that *Mead* does apply to administrative interpretations of the tax law in the form of revenue rulings.

Unlike revenue rulings, revenue procedures are rarely involved in deference disputes. This is in all likelihood because revenue procedures were meant to reflect merely internal procedures of the IRS that are published because they might affect taxpayers' rights or duties. Most litigation involving the weight of revenue procedures has arisen in contexts in which taxpayers attempted to invalidate an IRS action on the basis that the agency had not followed a revenue procedure. There is, therefore, a substantial body of case law holding that revenue procedures do not have the force and effect of law and that the IRS itself is not bound by them. *See, e.g.*, Estate of Shapiro v. Commissioner, 111 F.3d 1010, 1017 (2d Cir. 1997) (and cases cited therein); United States v. Toyota of Visalia, 772 F. Supp. 481, 486 (E.D. Cal. 1991), *aff'd*, 988 F.2d 126 (9th Cir. 1993). Among the reasons offered in support of these conclusions are that revenue procedures are procedural rules, in contrast to revenue rulings, which involve substantive tax law, Estate of Shapiro, 111 F.3d at 1017, and that revenue procedures do not require approval from the Secretary of the Treasury, Boulez v. Commissioner, 810 F.2d 209, 215 (D.C. Cir. 1987).

In at least one case since *Mead*, the IRS argued that revenue procedures are entitled to *Chevron* deference. Citing *Mead*, however, the court in *Fannie Mae*, 56 Fed. Cl. 228, 234-35 (2003), held that revenue procedures are entitled to deference under *Skidmore*, not *Chevron*. The court called attention to the preface in each issue of the Internal Revenue Bulletin to the effect that revenue procedures "do not have the force and effect of Treasury Department Regulations," which merit deference under the *Chevron* standard.

Despite the IRS's own description of revenue procedures as matters of procedure, and the courts' adoption of that characterization, revenue procedures often affect substantive rights. It might be argued therefore, that the standard of deference owed to revenue procedures should vary, depending upon whether a particular document is truly procedural rather than substantive. In other words, if a revenue procedure goes beyond mere procedure, perhaps it should be treated the same as a revenue ruling or substantive notice. Indeed, the court in *Fannie Mae* explicitly left aside the question of whether the revenue procedure at issue in

consideration, are not precedent, and cite as authority nothing more recent than *Dixon v. United States*, 381 U.S. 68 (1965). *See* Crow v. Commissioner, 2002 T.C.M. (RIA) ¶ 2002-178; Kirshenbaum v. Commissioner, T.C. Summ. Op. 2002-152 (Nov. 25, 2002). In another recent case, Rauenhorst v. Commissioner, 119 T.C. 157 (2002), the Tax Court reiterated its view that revenue rulings are not binding on the Tax Court or on other federal courts, and that the Tax Court could "in the appropriate case" disregard a ruling as inconsistent with its interpretation of the law. 119 T.C. at 173.

that case was truly procedural rather than substantive, reasoning that "[n]o statutory interpretation function is ascribed to revenue procedures." *Id.* at 235. On that basis, the court concluded that judicial decisions regarding deference to revenue rulings were of limited utility.

Post-*Mead*, the lower courts have taken inconsistent approaches with respect to revenue rulings and revenue procedures. While that may be due, at least in part, to the varying approaches taken by the courts prior to *Mead*, the courts are no closer to developing a consistent standard even with the help of the *Mead* decision. Although the language of *Mead* leaves open the possibility of *Chevron* deference for revenue rulings and revenue procedures, the fact that they are issued without notice and comment suggests that *Chevron* deference should apply only in exceptional circumstances. *Mead's* reliance on *Skidmore* for tariff rulings, moreover, implies that *Skidmore* should apply to revenue rulings and revenue procedures that address substantive, rather than procedural, matters.

3. *Informal Guidance, Notices and Litigating Positions*

Just as some judges have speculated that *Mead* calls for *Skidmore* deference to revenue rulings, so have other judges wondered whether *Mead* requires them to give *Skidmore* deference to the IRS's informal guidance and litigating positions, including briefs. As with revenue rulings, such a level of deference represents increased deference for some courts and decreased deference for others. In addition, this category of agency pronouncements evidences particular confusion regarding the *Seminole Rock* line of cases.

Despite all of the regulations issued by the IRS, many of which inevitably contain ambiguities, the *Seminole Rock* line of cases has seldom been applied in tax disputes. One notable tax case in which a court did so is *United States v. Wisconsin Power and Light Co.*, 38 F.3d 329 (7th Cir. 1998). A general counsel memorandum and a revenue ruling supported the IRS's interpretation of its regulation. The Court of Appeals for the Seventh Circuit upheld the IRS interpretation, relying on both *Seminole Rock* and *Davis v. United States*, 495 U.S. 472 (1990). Similarly, in *Connecticut General Life Insurance Co. v. Commissioner*, 177 F.3d 136 (3d Cir.), *cert. denied*, 528 U.S. 1003 (1999), the Court of Appeals for the Third Circuit found it unimportant that the IRS's interpretation of a regulation was offered for the first time during that particular controversy. What mattered to the court was that the interpretation involved a regulation; thus, "[b]ecause the interpretation advanced by the IRS is neither inconsistent with any prior interpretation of these regulations nor incompatible with their plain text," the court deferred to the interpretation. 177 F.3d at 146.

In contrast, the court in *CSI Hydrostatic Testers v. Commissioner*, 62 F.3d 136 (5th Cir. 1995), applied *Bowen* to reject an IRS litigating position interpreting the consolidated return regulations. In order for an interpretation to merit deference, the Court of Appeals required more than an "administrative practice," although a longstanding pre-litigation administrative practice might be sufficient. 62 F.3d at 136. The Fifth Circuit's one paragraph *per curiam* opinion explicitly endorsed the opinion of the Tax Court in the case, which had noted the

general rule of *Seminole Rock* that an agency's interpretation of its own regulation is entitled to deference, but concluded that "in the absence of a contrary published, or at least longstanding, interpretation of the regulation in question, deference is not the rule." CSI Hydrostatic Testers v. Commissioner, 103 T.C. 398, 408-09 (1994). The Tax Court opinion continued, "[U]nless an agency's interpretation of a statute or a regulation is a matter of public record and is an interpretation on which the public is entitled to rely when planning their affairs, it will not be accorded any special deference." 103 T.C. at 409.

One recent case, decided after *Christensen* and before *Mead*, applied *Auer* in the context of an IRS notice that interpreted an ambiguous regulation. In *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), the Court of Appeals for the Second Circuit considered the method for calculating benefits due to participants electing to receive accrued pension benefits in lump sum pursuant to a cash balance pension plan. The statute and regulations had been written for traditional defined benefit plans, however, not cash balance plans, and the issue in the case was how those regulations should apply to cash balance plans. The court held that Notice 1996-8, 1996-1 C.B. 359, which provided guidance on exactly the issue presented, was entitled to deference under *Seminole Rock* because it interpreted the agency's own regulations. Citing *Auer* and Justice Scalia's concurring opinion in *Christensen* as well as *Seminole Rock* itself, the court stated that the notice was entitled to deference regardless of its form of publication.[129] Deference to an IRS interpretation of its own regulations, according to the court, did not require the formality of a regulation or revenue ruling.

Cases decided since *Mead* demonstrate considerable inconsistency as to which line of Supreme Court cases should govern the degree of deference due a litigating position. In *Landmark Legal Foundation v. IRS*, 267 F.3d 1132 (D.C. Cir. 2001), the Court of Appeals for the D.C. Circuit concluded that, under *Mead*, interpretations developed in litigation now call for *Skidmore* deference, rather than the *Chevron* deference that it had applied in an earlier case involving the same provision of the Code. In light of *Mead*, the court wrote, "we must decide for ourselves the best reading." The court examined the phrase "data . . . received by . . . the Secretary with respect to a return or with respect to the determination of the existence, or possible existence, of liability" in section 6013(b)(2)(A), which defines "return information" for purposes of confidentiality and disclosure. The Court decided against the taxpayer, but on the basis of its own evaluation under *Skidmore* rather than on the basis of deference to the government's interpretation. It rejected the position argued by the government in its brief that the Court should defer to the IRS under *Seminole Rock*.

In *Tax and Accounting Software v. United States*, 301 F.3d 1254 (10th Cir. 2002), the Court of Appeals for the Tenth Circuit also looked to *Skidmore* to gauge the level of deference to an IRS interpretation, although it did so on the basis of *Christensen* without citing *Mead*.[130] The Tenth Circuit declined to defer

[129]In a footnote, the court stated that even if the notice were not entitled to "*Chevron*-style deference" under *Christensen*, it would still be "entitled to respect" under *Skidmore*. *Esden*, 229 F.3d at 169 n.19.

to the government's interpretation of two of the statutory requirements for the research and development credit of section 41(d)(1): "discovering information" and "process of experimentation." Although a set of regulations regarding this code section had become final in January 2001, and a new set of proposed regulations was issued in December of 2001, there were no final regulations that had gone through notice and comment at the time the case began, and the court concluded that the government's position, therefore, was due respect only under *Skidmore*.

While the government's position regarding discovery of information had been consistent in litigation regarding section 41(d)(1), its position changed as regulations were developed. Under *Skidmore*, according to the Tenth Circuit, such inconsistency in its litigating position ruled out substantial deference. For the discovery requirement, the Tenth Circuit read the plain language of the statute as mandating that the taxpayer "show that he discovered new information and that the information be separate from the product that is actually developed," *Tax and Accounting Software*, 301 F.3d at 1262, a different standard from that argued by the government. As for the meaning of "process of experimentation," the opinion determined that because the government had either taken no position or altered its position, its interpretation was entitled to "little deference" under *Skidmore*. The Court undertook its own examination of the legislative history. It concluded the research credit did require initial uncertainty as to the feasibility of the final result and that the taxpayer, as a matter of law, could not meet that requirement.

In *U.S. Freightways Corp. v. Commissioner*, 270 F.3d. 1137 (7th Cir. 2001), the Court of Appeals for the Seventh Circuit also rejected an IRS interpretation, in this instance of the meaning of the requirement in Regulation sections 1.263(a)-2 and 1.461-1(a)(2), that benefits extending "substantially" beyond the tax year had to be capitalized. The IRS, through litigating positions in other cases, and in the way that it had applied the rules in different cases, treated the word "substantially" as covering any time period extending more than a few days or perhaps a month. The court looked to *Mead* and the factors of *Skidmore* to determine the degree of deference owed this characterization. Like Justice Scalia's dissent in *Mead*, the court feared that full *Chevron* deference to informal interpretations would encourage boot strapping: "With full Chevron deference, agencies could pass broad or vague regulations through notice-and-comment procedure, and then proceed to create rules through *ad hoc* interpretations that were subject to only limited judicial review." 270 F.3d at 1142. The Seventh Circuit found that the position of the IRS in revenue rulings and in other cases evidenced no consistent practice, and that the IRS's policy, as demonstrated in examples from the applicable regulations, favored the taxpayer. The court went through this examination of consistency, as directed by *Skidmore*, before rejecting the government's position.

[130]According to one of the lawyers in the case, the case was briefed before the decision in *Mead*. Telephone call by Irving Salem to Rebecca Fowler (Oct. 23, 2002).

In *Matz v. Household International Tax Reduction Investment Plan*, 265 F.3d 572 (7th Cir. 2001), *cert. denied*, 535 U.S. 954 (2002), where the IRS was an *amicus* rather than a litigant, the outcome also turned on the level of deference to be given the government. The Court of Appeals for the Seventh Circuit in this case reversed its earlier decision, 227 F.3d 971 (7th Cir. 2000), which the Supreme Court had vacated and remanded in light of *Mead*. The court had to decide whether both vested and non-vested participants, or only non-vested participants, should be counted in determining whether a partial termination of a retirement plan has occurred. In the first opinion, the Seventh Circuit had, pursuant to *Chevron*, deferred to the IRS's position offered in its *amicus* brief, that both categories should be counted. On remand, the Court, applying *Skidmore*, rejected the IRS interpretation, and held that only non-vested participants should be counted. It reasoned that the IRS's position in the *amicus* brief was an informal agency policy pronouncement not entitled to *Chevron* deference. 265 F.3d at 574. It wrote, "We do not believe that a position set forth in an *amicus* brief, supported by some Revenue Rulings and an agency manual are formal enough to warrant *Chevron* treatment." *Id.* at 575. Moreover, the court asserted, "Upon reading *Mead*, we find that a litigation position in an *amicus* brief, perhaps just as agency interpretations of statutes contained in formats such as opinion letters, policy statements, agency manuals, and enforcement guidelines . . . are entitled to respect only to the extent that those interpretations have the power to persuade under *Skidmore*." *Id.*

The IRS's position in its *amicus* brief did not persuade under *Skidmore*. Since the statutory language was ambiguous, the regulations not helpful, the statutory framework without assistance, and the legislative history without guidance, the court fell back to the purpose of the statute, which was to protect employees' legitimate expectations of pension benefits, and, on that ground, rejected the IRS interpretation. Thus, *Matz* rejected the IRS interpretation only after at least claiming to have afforded it *Skidmore* deference. The opinion noted that *Mead* quoted language from *Skidmore* to the effect that "an agency's interpretation may merit some deference whatever its form, given the 'specialized experience and broader investigation and information' available to the agency." 265 F.3d at 574 (quoting *Mead*, 533 U.S. at 234 (quoting *Skidmore*, 323 U.S. at 139)). For the court, the quotation from *Mead* regarding "whatever its form" appears to indicate that even litigating positions merit some deference under *Skidmore*. Neither *Mead* nor *Matz* quoted the language from *Skidmore* specifying that weight be given to interpretations of governmental agencies "that were not of adversary origin," *Skidmore*, 323 U.S. at 139, to consider whether it implied that interpretations that were of adversary origin are owed little or no deference.[131]

[131]The Seventh Circuit in the *Keys* case recently concluded that the post-*Mead* brief of the Social Security Administration did not have the force of law and was entitled to "limited deference." The court analogized the government's brief to an "opinion letter," which under *Christensen* does "not warrant *Chevron*-style deference." *Keys*, 347 F.3d 990, 993 (7th Cir. 2003) (citing *Christensen*, 529 U.S. at 587). The Seventh Circuit also questioned the continuing vitality of *Aver* post-*Mead*. *See supra* note 89.

The post-*Mead* cases involving informal IRS actions demonstrate vividly the tension between *Mead*'s invocation of *Skidmore* and the rule of *Seminole Rock* and *Auer* that courts must give controlling weight to reasonable administrative-agency interpretations of their own regulations and rules. This tension is exemplified in *American Express v. United States*, 262 F.3d 1376 (Fed. Cir. 2001), in which the Court of Appeals for the Federal Circuit held that the IRS, relying on a general counsel memorandum, properly construed the term "services" in Revenue Procedure 1971-21, 1971-2 C.B. 549, to deny American Express the ability to use the ratable inclusion method for income received annually from cardholders. The issue in the case involved the IRS's interpretation of an ambiguous term in its own revenue procedure, and, according to the court, "substantial deference is paid to an agency's interpretation reflected in informal rulings." 262 F.3d at 1383. The opinion cites *Mead* and *Christensen* only for the propositions that the revenue procedure was "plainly statutorily authorized," *id.* at 1380, and that the interpretation of the revenue procedure in the general counsel memorandum was "not reflected in a regulation adopted after notice-and-comment and would probably not be entitled to *Chevron* deference. *Id.* at 1382. It relied for its holding on the authority of *Auer* and *Cleveland Indians* rather than using the factors of *Skidmore* as directed by *Mead.*

Matz, in contrast, saw *Mead* as requiring reliance on *Skidmore* instead of *Auer* and its progeny when it came to judicial deference to informal interpretations. In its list of citations, the opinion used a "compare" cite to introduce *Auer* and *Jones v. American Postal Workers Union*, 192 F.3d 417, 427 (7th Cir. 1997), in which the court had deferred to interpretations in agency *amicus* briefs because the interpretations were not *post hoc* rationalizations and reflected the agency's fair and considered judgment. The *Matz* court found such precedents not to be binding in the post-*Mead* case before it.

As *Matz* and *American Express* demonstrate, it is difficult to reconcile *Seminole Rock/Auer* and *Skidmore/Mead. Mead* directs courts to impose the procedural deference of *Skidmore* to certain informal interpretations. *Seminole Rock* and *Auer* instruct that, at least when it comes to the agency's informal interpretations of its own ambiguous regulations, a more substantial deference is due. *Mead* neither limits nor endorses the *Seminole Rock/Auer* line of cases. No language in the majority opinion in *Mead* responds to Justice Scalia's concern about deference to informal rulings interpreting ambiguous or broadly worded regulations.[132]

[132]If both *Seminole Rock* and *Mead* are good law, revenue rulings, revenue procedures, or litigating positions that interpret regulations receive greater deference than other kinds of revenue rulings or revenue procedures, which, for example, might merely interpret statutory language alone. Yet, insofar as *Skidmore* deference under *Mead* and *Christensen* turns at least in part on the degree of consideration the agency gives to formulating it interpretations, the regulations and procedures of the IRS make no distinctions based on the content or context of revenue rulings or revenue procedures.

F. *Conclusion*

The case law, from both the Supreme Court and the lower federal courts, reflects many uncertainties and inconsistencies—whether *Chevron* or *National Muffler* supplies the standard for tax law; whether or when *Chevron* or *Skidmore* applies; the extent to which legislative and interpretive tax regulations should be judged differently; whether *Seminole Rock* has continuing viability; and how informal IRS guidance and litigating positions should be treated. While this confusion is unfortunate, it offers the challenge and opportunity to set a course that is most likely to lead to the best possible administration of the tax laws.