

IRS Faces Rulemaking Pressure Following Chevron's Demise

By **Kat Lucero**

Law360 (July 1, 2024, 8:31 PM EDT) -- The Internal Revenue Service will likely face more pressure to develop tax regulations that are more firmly grounded in the law and tailored to ensure certainty for individuals, businesses and other organizations after the U.S. Supreme Court's landmark decision to overturn the decades-old Chevron doctrine.

In a case known as the Loper Bright v. Raimondo, the high court's majority on Friday struck down the 40-year-old Chevron doctrine that directed courts to defer to federal agencies' interpretations of ambiguous law.

At first blush, the move could be seen as easing the IRS' regulatory workload by pushing some of the work of interpreting legislation onto the courts. But the reality is that it will force the U.S. Department of the Treasury and the IRS to work harder to write regulations that would limit the agency's litigation risks and to demonstrate they have thoroughly vetted comments from experts and explained why the rules were designed that way, practitioners told Law360.

The Loper Bright decision should spur the IRS to develop more thorough rules based on active public engagement with practitioners and other stakeholders to give them a more robust legal foundation should they be challenged in the courts, Edward L. Froelich, counsel at McDermott Will & Emery LLP, said.

"At the end of every regulatory project, that's where they want to be," Froelich said.

Many tax practitioners had been eagerly awaiting the decision in the Loper Bright case because the IRS has long relied on the Chevron doctrine — which the high court established in a 1984 opinion in *Chevron v. Natural Resources Defense Council* — to defend tax regulations in litigation.

Many conservative justices in the current majority on the high court in the past few years had been open about their desire to end Chevron to rein in courts' deference to federal agencies — which are part of the executive branch — to interpret laws that aren't crystal clear.

The Supreme Court decided to weigh in on the fate of Chevron last year after fishing industry plaintiffs in the Loper Bright case and a similar one called *Relentless v. Department of Commerce* asked the justices to overturn Chevron to undermine a 2018 National Marine Fisheries Service rule that required fishers to pay part of the cost of having federal compliance monitors aboard their ships.

In siding with the fishing groups, a majority of justices held Friday that Chevron improperly prioritized the executive branch's legal interpretations over the judicial branch.

Chevron deference was "misguided because agencies have no special competence in resolving statutory ambiguities. Courts do," the Supreme Court's majority opinion said.

In response to the opinion, U.S. Tax Court Judge Elizabeth Ann Copeland, speaking Friday at New York University School of Professional Studies' tax controversy forum in New York, said Treasury and the IRS do have special competence in tax law. The Tax Court, she said, will continue to give considerable credence to the agencies' rules.

Meanwhile, practitioners said the decision will likely embolden more people to file lawsuits against tax regulations they dislike because the IRS no longer has Chevron to lean on.

For years, the "IRS has issued regulations expanding its power and restricting tax benefits that Congress intended taxpayers to receive" and relied on Chevron "to sustain those regulations," said Rob Kovacev, a member at Miller & Chevalier Chtd.

"Now the IRS will have to defend its regulations on the merits based on what the tax code actually says," Kovacev said.

However, while the Loper Bright decision provides ammunition for taxpayers to dispute regulatory interpretations they disagree with, Tom Cullinan, who was counselor to former IRS Commissioner Chuck Rettig and is now with Chamberlain Hrdlicka White Williams & Aughtry, said that outcome may come at the cost of reduced tax certainty.

As the highest level of IRS guidance, regulations have historically provided the most certainty when the law is ambiguous, Cullinan said. In the wake of Loper Bright, when Treasury and the IRS do decide to issue a regulation, it will be unclear to what extent taxpayers will be able to rely on it given that the courts will get the final say, he said.

"Most taxpayers put a high value on certainty in their tax affairs," Cullinan said.

One option for the IRS to try to quickly provide some certainty and clarity on tax laws is to issue so-called subregulatory guidance such as notices, announcements, revenue rulings and revenue procedures. However, such regulatory guidance does not have the force of law, Michelle Abrams Levin, shareholder at Dentons Sirote, said.

Subregulatory guidance can also be "susceptible to a challenge because there won't be as much of a record to support it unless the IRS makes the record internally," Levin said.

Another option for taxpayers seeking certainty about tax laws and regulations is to challenge them in court and let the judges decide, she said. But there's no guarantee they will get the answer they want, Levin said.

Seeking certainty through the courts is "not really a great result for taxpayers," she said.

Moving forward, practitioners said, when promulgating rules, the IRS may have to build upon its recent process of actively soliciting public feedback and providing an elaborate explanation in the preamble to

regulations explaining why the agency wrote the rules the way it did. Treasury and the IRS have been doing so in implementing many clean energy tax provisions that Congress created in the 2022 Inflation Reduction Act. Some practitioners said the agencies are also pursuing a similar undertaking in implementing a set of rules targeting partnership basis-shifting.

The IRS has pursued this process in response to recent losses in several lawsuits that challenged tax guidance, such as the listing notices on syndicated conservation easements, for failure to follow the public comment requirements under the Administrative Procedure Act.

Treasury and the IRS will likely approach rulemaking "in a way that they are able to demonstrate how they consider the issue" and "the validity of their reasoning," said Jennifer Breen, a partner at Morgan Lewis & Bockius LLP.

The Loper Bright decision "will only cause that to continue and perhaps increase," Breen said.

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