IRS Should Brace for More Taxpayer Lawsuits With Chevron's Death

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- **Gibson Dunn lawyers say ruling unlikely to alter IRS practice**
- **Challenges to unfavorable tax regulations expected to grow**

On a technical level, the US Supreme Court's ruling in *Loper Bright Enterprises v. Raimondo* now requires courts to find the best interpretation of a statute and—in tax cases—not side with the IRS whenever its regulatory interpretation is "reasonable."

On a practical level, *Loper Bright* is unlikely to signal a significant change in the IRS's practice of issuing regulations, which the agency would say have always been the best interpretation of the law. What may change, however, is taxpayers' appetite for challenging regulations that require an unfavorable reporting position, knowing those regulations will now be held to a "best interpretation" standard.

The death of *Chevron* deference also may require courts to conduct more detailed statutory construction inquiries. But in practice, these changes may not alter the outcome in many cases—particularly against the backdrop of recent trends in decided tax case law.

Unlike many other federal agencies, the IRS receives countless requests for regulations and other formal guidance from taxpayers, advisers, and other stakeholders each year—all seeking clarity in applying the law.

Recent regulatory activity suggests *Loper Bright* and the death of *Chevron* deference may not reduce this demand for interpretive guidance or the IRS's issuance of such guidance in response. It also suggests that courts will evaluate regulations aimed at curtailing perceived abuses of the tax code in a different light, although the outcome of that evaluation may be no different than it would have been under *Chevron*.

The IRS's regulatory response to the 2017 Tax Cuts and Jobs Act helps illustrate how *Loper Bright* may affect regulatory practice. The TCJA introduced new and amended old tax code provisions, including a wholesale revision to the tax treatment of cross-border activities. In response, the Treasury Department and IRS issued hundreds of formal guidance items, including more than 50 sets of final regulations.

While certain aspects of the TCJA regulations had anti-abuse or other taxpayer unfavorable elements, the general—if not overwhelming—response from taxpayers to these regulations was favorable. This was because they addressed myriad uncertainties and ambiguities in the TCJA, helping taxpayers plan their affairs and file their returns.

Regardless of whether the thousands of interpretations of law reflected in the TCJA were the best interpretation or one of several reasonable interpretations, most taxpayers filed their returns consistently and moved on, even when a more advantageous interpretation and reporting position might be available. This practice likely will continue regardless of whether regulations receive *Chevron* deference.

There are still exceptions to the practice of following the IRS's published position when stakes are high and a taxpayer believes the IRS has gone too far. These cases, and the validity of the regulations involved, will now be litigated under the more exacting best interpretation standard of *Loper Bright*.

But the outcome may be no different. Even with *Chevron* deference, courts have been increasingly willing to invalidate taxpayer unfavorable regulations—including regulations issued under the TCJA—often on grounds unconnected to deference.

Under the best interpretation standard of *Loper Bright*, the IRS will continue issuing guidance, including regulations, interpreting tax code provisions that are—or are perceived by the IRS to be—ambiguous. While no longer entitled to *Chevron* deference, these regulations will be given a lesser degree of respect under *Skidmore v. Swift & Co.*, particularly if they're issued close in time to a statute's enactment, consistently interpreted by the IRS over time, or the regulation "rests on factual premises within [the agency's] expertise."

In defending these regulations against challenge, the IRS undoubtedly will argue that its position meets the "best interpretation" standard of *Loper Bright* and should be accepted and applied regardless of whether it's afforded deference.

Two recent guidance projects may highlight the extent to which *Loper Bright* impacts taxpayers' approach to challenging regulations, the IRS's response, and the courts' ultimate evaluation of those regulations.

The IRS on June 17 issued notices of proposed rulemaking, of intent to publish future regulations, and a revenue ruling—all aimed at preventing taxpayers from benefiting from partnership basis adjustments in circumstances the government views as inappropriate. If the substantive regulations referenced in the notice are issued, taxpayers will have strong incentives to challenge them and strong arguments for why they're not a proper interpretation or application of the underlying statutes.

The incentives for taxpayers to challenge regulations such as these remain the same. And the validity of those regulations may continue to turn on threshold considerations of statutory authority and on compliance with the Administrative Procedure Act—not whether they adopt the best or only a reasonable interpretation of the law.

The second recent guidance project that could test *Loper Bright*'s impact in tax cases involves final regulations implementing broker reporting requirements for transactions in crypto currency and other digital assets. These regulations implement the tax information reporting requirements mandated by the Infrastructure Investment and Jobs Act and have garnered more than 44,000 comments.

These reporting regulations will impose burdens on a broad range of entities, making them ripe for challenge. While not receiving *Chevron* deference, courts will give them some degree of *Skidmore* respect because they were issued under an express statutory mandate.

If challenged, the Treasury and the IRS will argue that deference isn't determinative because the regulations fit within the scope of delegated regulatory authority, while taxpayers are likely to assert that they don't. Resolving those positions is unlikely to turn on whether an interpretation of the relevant statutory provisions is the best or merely reasonable, so *Loper Bright* may again not determine the outcome.

Loper Bright will provide taxpayers with a greater incentive to challenge adverse regulations, knowing that the best interpretation and not any reasonable interpretation of a statute will prevail. But trends in recent case law suggest that these regulatory challenges may have succeeded with or without *Chevron* deference.

The cases are *Loper Bright Enterprises v. Raimondo*, U.S., 22-451, and *Relentless v. Department of Commerce*, U.S., 22-1218, decided 6/28/24.Vit occus