State Tax Administrators in the Crosshairs

• In May, 2019 Eversheds Sutherland announced a Reform Administrative Deference (RAD) Coalition, and McDermott Will & Emery announced a Deference Coalition.

• Both aimed to reduce or eliminate court deference to DORs’ regulations, administrative rules, or other guidance interpreting the states’ taxing statutes, either through legislation in the states or court rulings that reject, limit or curtail deference.

• Presumably coalition members would be major corporate clients, and perhaps trade associations, that dislike deference and also have been attacking it at the federal level.
State Tax Administrators in the Crosshairs

- ALEC began promoting a state APA regime it wrote in 2018, which features an anti-deference provision.
- 15-20 states’ attorneys general have filed amicus briefs in multiple cases in the U.S. Supreme Court attacking deference to federal agencies.
- Although a minority of state courts never had (or claim they never had) a deference tradition, most have; but within the last several years Florida, Arizona, Mississippi, Wisconsin and Michigan have taken some action to limit deference to agency interpretations.
- What is going on?

To Make Matters Worse ....

- The appearance of deference issues in at least four Supreme Court opinions this term proves that it is a very hot topic with The Supremes, and that change is in the wind because a majority of the Justices clearly don’t like deference at the federal level.
  - *Kisor v. Wilkie*: narrowly avoided reversing *Seminole Rock/Auer* deference to agency interpretation of its own rules;
  - *U.S. v. Davis*: “vague law is no law at all”;
  - *Gundy v. U.S.*: narrowly avoided striking a regulation under non-delegation doctrine, which only been applied twice (in the 1930s).
  - *Dept. of Commerce v. New York*: The Secretary of Commerce did not adequately explain his administrative choice on the census question, so did not receive *Chevron* deference.
Is Loss of *Chevron* Deference Really a DOR Problem?

- If not, why did the MTC’s Litigation Committee invite me to Boise?
- Not a universal DOR problem; and the problem may differ from federal side.
- One count showed only 11 states applied “*Chevron* deference”
  - the variety of state constitutional, administrative procedure, and judicial review regimes makes it extremely hard to generalize about the deference issue or to transport the federal issues usefully into ALL the states.
- Working assumption: if the issue did not exist for most state DORs, the two law firms would not be selling their anti-DOR deference services.

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Back to Basics: Unconstitutional Delegation?

- States can give deference to DOR if they want to:
  - Probably not a violation of the U.S. Constitution (although someone will claim it violates Art. IV., sec. 4: “The United States shall guarantee to every State in this Union a Republican Form of Government.”)
- But most state constitutions require some sort of separate of powers among three branches of governments.
  - Which can be violated if the legislature delegates legislative powers to the DOR.
  - This was the subject of *Gundy v. United States*, 139 S. Ct. 2116 (2019) in which dissenters showed high concern with over-delegation to the Attorney General to supply the effective dates for the Sex Offenders Registration Act.
- Identifying appropriate delegation is what *Chevron* is partly about.
Back to Basics: *Chevron*

- Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 467 U.S. 837 (1984) was not a constitutional case (that might create a rule applicable to states, too); no one thought congress had delegated too much authority to the agency by using the “ambiguous” word “source” of pollution in the statute.
- Rather the case is about how federal courts will interpret federal statutes and defer to federal regulations or other federal agency guidance.
- Therefore, state courts need not pay any attention to *Chevron* .... but many have, and cite it and apply it.

Back to Basics: What Does *Chevron* Stand For?

- The *Chevron* opinion sided with an oil company that liked the regulation against an environmental group that did not like the regulation, and gave *Chevron* deference to the industry-favorable regulations written by the Reagan administration, reversing a Carter administration rule.
- The statute referred to “source” of pollution; Court gave deference to agency’s definition of “source,” which made it easier for industrial plants to comply.
- But the statute did not grant specific authority to define “source” or otherwise write “the law.” Instead, agency relied on general grant of reg. authority.
  - That was IRC §7805, which probably is copied in many states: “... the Secretary shall prescribe all needful rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alteration of law in relation to internal revenue.”
Back to Basics: What Does *Chevron* Stand For?

- *Chevron* opinion stated:
  - “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.”
  - The implicit delegation of authority was in the ambiguity of the word “source” of pollution. Is it the smokestack, the one plant, the group of plants, etc.
  - Note: (1) gap = genuine ambiguity in the statute; (2) express delegation to create law can be implied by a gap; (3) “arbitrary, capricious” is the federal APA standard for all rules; (4) if deference warranted, the rule only has to be “reasonable,” which is lower standard than more-likely-than-not.

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*Chevron* Should Not Have Been Objectionable

- Today talk radio hosts/WSJ editorials discuss *Chevron* as some huge error of the runaway Supreme Court, probably not knowing it was a Reagan environmental win.
- In fact, there was NOTHING new in *Chevron*.
  - It honored separation of powers by trying to figure out whether congress wanted the agency to define the law.
  - It effectively said that the court will not second guess the agency rule so long as (1) the court can’t figure out what the statute meant by “source,” (2) the answer the agency provided is not arbitrary or capricious, and (3) it is within the zone of meaning possible under the words of the statute.
  - By recognizing that congress can grant the authority to write the law indirectly by leaving a gap or genuine ambiguity in the statute, *Chevron* was simply accommodating to real life: congress cannot fill in every blank.
    - The SCT later fleshed out the gap-filling approach in *Mead*, 533 U.S. 218 (2001), but *Mead* did not invent it: *Chevron* had already applied it.
Ambiguity Is Ambiguous

• What is the difference between (1) a Chevron deference gap-to-be-filled genuine ambiguity, and (2) an ordinary everyday statutory ambiguity that a court can interpret as well as the agency?
• Sometimes it is hard to tell, but the existence of the Chevron doctrine makes it necessary, outside of a statute that tells the agency to create a specific set of rules.
  • Examples of such specific grants of authority are consolidated return regulations and related party (§482) regulations at the federal level.
• The hallmark of a Chevron deference gap-to-be-filled genuine ambiguity is that even by applying all her legal skills a judge cannot discover a more likely than not interpretation for the statute.
• We will call all other statutory ambiguities “normal” ambiguities, which a judge can resolve by normal interpretative methods.

Which Is Which?

• Regulations, sometimes called Rules, are non case specific guidance that may be simply the agency’s interpretation of the meaning of the statute (called an interpretive rule), or may be an exercise of delegated authority to write a rule (called a legislative rule).
  • So, at the federal level, there is always a threshold question whether it is legislative (and entitled to Chevron deference) or not.
• Guidance with less authority – at the federal level revenue rulings, Notices, various sorts of general legal advice and case specific guidance – should always be interpretive only, and never entitled to Chevron deference.
• AT the state level, legislative guidance might appear in revenue rulings, Bulletins, or under other headings.
Application of *Chevron* to Tax

- The choice between finding a genuine v. normal ambiguity is wholly up to the judge evaluating the agency guidance; there is a huge tendency for judges to deny *Chevron* deference by the simple means of interpreting the statute.
  - So the “threat” of *Chevron* deference to those who don’t like it is likely overblown.
  - And the possibility of the DOR enjoying *Chevron* deference also is likely overblown.
- As proof, the USSCT has given *Chevron* deference since 1984 to only one federal tax regulation, and the case illustrates a genuine ambiguity to which such deference is appropriate.
    - Medical students are full time students and full time employees.
    - Mayo did not want to pay FICA and claimed exemption for students applied.
    - Reg. said employee status prevails when full time, because an employee should be treated as a student only when the work is incidental to study.
    - Court applied *Chevron* because it thought the meaning of “student” was inherently ambiguous in this situation and 7805 granted authority to write substantive reg.

More on *Mayo*

- Much has been made (in the federal tax bar) of *Mayo* rejecting the *National Muffler*, 440 U.S. 472 (1979) test (tax no longer “special”)
- *National Muffler* had talked about a lot of factors that bear on meaning of federal tax statute, but *Mayo* said if statute is ambiguous for *Chevron* purposes, meaning reg. is legislative, only standard is arbitrary or capricious = APA standard.
  - Logical: if statute can be interpreted, then all those other considerations may be relevant; but if it can’t be interpreted and you just have to go with non arbitrary agency regulation, all those other considerations are irrelevant.
  - The other interpretive considerations included whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose; it is a substantially contemporaneous construction of the statute; if the regulation dates from a later period, the manner in which it evolved; 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.
  - And of course there are many other tools of statutory interpretation, including legislative history.
More often, Federal Courts Will Discover They Can Interpret the Statute

• An omission from gross income triggers a longer six-year statute of limitations on assessment.
• Does an overstatement of basis of property sold constitute an omission from gross income?
• Held: no (even though it reduces the gain).
• Court did not give *Chevron* deference to regulation saying that basis overstatement = gross income omission because it interpreted the statute by looking at the purpose of the extended S/L.
• It investigated purpose of congress to give more time for assessment when the item did not appear on the face of the return.
• The sale proceeds would appear on the face of the return and IRS did not need more time to discover the sale.

Simplified Restatement of *Chevron* Meaning

• *Chevron* WAS NOT a huge shift of power from courts to agencies, because COURTS CAN AND DO RECLAIM POWER OVER THE MEANING OF THE STATUTE BY SAYING: I CAN INTERPRET IT TO MEAN this ......
• Then the opinion can say *Chevron* deference was not required because the statute was “clear.” *A statute can be “clear” even if you have to interpret it.*
Even *Chevron* Opponents Admit That

• That is precisely what Justice Gorsuch said in March, in dissent in BNSF Rwy Co. v. Loos, 139 S. Ct. 893 (3/4/19)
  - Majority ruled “compensation” for RR Retirement Tax Act purposes included tort damages paid by employer for lost wages.
  - Majority did not refer to *Chevron* and interpreted statute using many tools, including parallel statutes and their interpretations.
  - Dissent by Gorsuch applied more literal reading: how can being paid for being hurt be pay for services?
  - Described *Chevron* as having one foot in grave: “if it retains any force....”
  - BUT: Congratulated majority on not relying on *Chevron*, but rather interpreting the statute; which PROVES that the way out of *Chevron* deference is for a court to say it knows what the statute means.

So Why are DORs Concerned with *Chevron*?

• State DORs are collateral damage in the culture wars that mostly originated at the federal level, and mostly outside of tax in the areas of environmental and workplace safety rules.
  - A DOR is an especially handy target for any attack on government agencies generally, like anti-deference.
• Why now?
The Anti-deference Movement Has Grown Due to a Confluence of Recent Events at the Federal Level

- (1) the Clinton and Obama presidencies reminded Republicans that Democratic presidencies cannot be avoided, bringing New Deal-like agencies and rules (e.g., Obamacare), which must be curtailed, even when Republicans can’t control the White House;
- (2) the Republican effort to remake the federal judiciary into a different ideological model has largely succeeded;
- (3) the Mead opinion in 2001 was credited with “expanding” the reach of Chevron to the maddeningly vague category of gap filling regulations, which appeared to dispense with an intentional congressional delegation of authority to the agency;
- (4) Justice Scalia died in 2016; he was the last Republican Justice who thought deference was sometimes good because it protected executive authority from activist judges; anti-Chevron Justice Gorsuch was appointed in 2017;
- (5) in 2016 the Senate Committee on Homeland Security and Governmental Affairs held hearings in which the New Deal and Chevron were tied together as agencies running amuck, and anti-deference bills were introduced in Congress; and
- (6) in 2016 Donald Trump adopted anti-Deep State rhetoric as part of his other culture war issues.

But Are States Talking the Same Language?

- This is a huge overlooked point. State DORs know their own state APA rules, but probably don’t know the much older 1946 federal APA rules, and may not realize that there can be a disconnect between the two as they related to the language of the Chevron analysis.
- Chevron is based on the view that “legislative rules” have the force of law because congress delegated authority to the agency to write them; but “interpretive rules” do not because they are just the agency’s view of what the statute means. A taxpayer can act on a different interpretation and try to convince a court that his interpretation is correct; and an agency can change its interpretation.
  - When the taxpayer tries to contest a legislative rule, it can win only if it shows (1) congress did not grant the authority, or (2) the agency did not use the right adoption procedure (notice and comment), or (3) the agency’s choice of rule could not chin up to the low bar of “reasonable.”
  - Without that distinction between two types of rules, based on delegation of authority to write the law or not, the Chevron deference scheme is unworkable.
But Are States Talking the Same Language?

• But state statutes may use a different distinction between guidance that is entitled to more or less deference or has more or less authority.

• For example, the ULC State Model APA (2010) creates a different distinction:
  • “Rules” are subject to various adoption procedures (notice and comment, like the APA requires only for legislative rules), can be just interpretations, and all rules have the force of law.
  • In contrast, “guidance documents” are not subject to those requirements; they are “records of general applicability developed by an agency which lacks the force of law but states the agency’s current approach to, or interpretation of, law, or describes how and when the agency will exercise discretionary functions.”

Therefore, making a legislative rule is a procedural choice for the agency under the State Model APA (2010), not a matter of finding a delegation of authority by the legislature.

• That can be good for the DOR, if the result is that its courts will give deference to interpretive rules simply because of the method of adoption.

• But it makes irrelevant all of the *Chevron* sub-rules on how to identify delegations of authority to write legislative rules; and

• It eliminates the constitutional underpinning for the DOR writing a rule that goes beyond interpretation: that the legislature authorized it.
Compare US-APA and State Model APA

• 5 USC 553: notice of proposed rule making shall be published in the Federal Register .... etc.; this subsection does not apply--(A) to interpretative rules, general statements of policy, or rules of agency organization, procedure, or practice ...

• 5 USC 706: The reviewing court shall hold unlawful and set aside agency action ... found to be-- (A) arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; (B) contrary to constitutional right, power, privilege, or immunity; (C) in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; (D) without observance of procedure required by law;...

Compare USAPA and State Model APA

• That means the federal APA in 1946 forecast *Chevron*:
  • “Legislative regulation” (where congress told agency to write the law) could be invalidated only if “arbitrary or capricious.”
  • But “interpretive regulation” was not so important, did not have to be issued with notice and comment, merely stated the agency’s interpretation of the statute, and could be overturned by any court that had a different interpretation, and ignored by any taxpayer who had a different interpretation, because “not in accordance with law...”
    • The taxpayer might be penalized if he lost, but not if he won.
Compare USAPA and State Model APA

• 2010 State Model APA sec. 102(30) definition of “rule”: “implements, interprets, or prescribes law ...”

• (14) defines “Guidance document,” which means a record of general applicability developed by an agency which lacks the force of law but states the agency’s current approach to, or interpretation of, law, or describes how and when the agency will exercise discretionary functions.

• Sec. 304 prescribes procedures for adopting proposed rule. It assumes all rules are “binding” on public and agency, i.e., “has the force of law.”

• Sec. 311 says a guidance document can be issued without the rule procedures, and “shall afford the person an adequate opportunity to contest the legality or wisdom of a position taken in the document ...

Compare USAPA and State Model APA

• Model State APA sec. 508: The court may grant relief only if it determines that a person seeking judicial review has been prejudiced by one or more of the following: (A) the agency erroneously interpreted the law [not in APA]; (B) the agency committed an error of procedure; (C) the agency action is arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; ...
Recap: The Pressure Point

- In the federal system, the *Chevron* pressure point is the legislative/interpretive dividing line.
- The difficulty of finding the legislative delegation of power in the gap or ambiguity is a large part of the cause of dissatisfaction with *Chevron* deference; which may not exist in a state APA/
- The pressure has led various actors to abandon trying to make the distinction:
  - Treasury applies notice + comment to almost all regulations, claiming “fairness,” but also does not want to have to decide if interpretive or legislative
  - Truth is, most regs probably some of both.
  - DOJ claims in litigating briefs that the choice to issue an interpretive regulation using legislative regulation procedures converts it into receiving *Chevron* deference!!
  - Judges have love/hate relationship with *Chevron*, because if they have to give deference they lose power, but it’s dawning on judges that they can find the rule is interpretive and regain power.
  - And now a new 2019 Treasury Policy on guidance claims all regs have “force and effect of law,” just because they are regulations (in contrast to subregulatory guidance).

Distinction Not Going Away at Federal Level

- Several SCT opinions this term recited the legislative/interpretive regulation dichotomy.
- *Azar v. Allina*, 139 S. Ct. 1804 (2019): A case involving Medicare agency decisions; Justice Gorsuch’s opinion (1) confirms the legislative v. interpretive dichotomy of the APA; (2) says that a regulation can have both legislative and interpretive parts; (3) admit that legislative history might inform the interpretation of a statute; (4) touts the benefits of notice and comment; and (5) skirt the issue whether the statute had a “gap” (it clearly did).
- *PDR Network LLC v. Carlton & Harris Chiropractic, Inc.*, 139 S. Ct. 2051 (2019) resulted in a remand with only a brief opinion by Justice Breyer, but a lengthy concurrence by Justices Kavanaugh, Alito, Gorsuch and Thomas. The primary issue was the effect on a lower court of a special rule limiting review of FCC orders to Courts of Appeal. Justice Breyer wrote for the Court that the answer depended in part on whether the FCC order was a legislative rule or an interpretive rule. The opinion cited *Chevron* and said it was not deciding what sort of deference was due a legislative rule, but that it mattered to know which was at issue; and the lower court had not decided that.
- The concurring Justices were afraid that could force federal district judges to be bound by FCC orders without power to review them, which is a sort of *Chevron* deference issue.
**Chevron** Radiations

- There are all sorts of subissues within the **Chevron** field, which may or may not have shown up at the state level.
  - First, the deference to agency interpretation of its own regulation issue, already mentioned: *Kisor v. Wilkie* (USSC 2019).
- Wall Street Journal says about this case (3/27/19): "Regulators have been bypassing the APA more and more ... through guidance ... and interpretive rules [that] enjoy the force of law ... but don’t have to comply with the APA.

**Kisor v. Wilkie, 139 S. Ct. 2400 (2019)**

- Holding: courts should give deference to agency’s own interpretations of their “genuinely ambiguous” regulations in appropriate cases; *Seminole Rock* and *Auer* not overruled.
- Significance: This case was a stalking horse for the eventual overruling of **Chevron**; but the failure of this attack does not necessarily mean that **Chevron** will survive the next term of the USSC. There was no dissent, although four Justices did not join any of the plurality opinion and Chief Justice Roberts joined parts, but said the holding had no bearing on **Chevron**.
- Facts: The Federal Circuit ruled that an action by the Veterans’ Administration was proper because the court gave deference to the VA’s judge’s interpretation of the VA’s own regulation.
- The regulation at issue said that a decision maker must reconsider a decision if relevant records of a certain type are presented to augment the record. The ambiguous word was “relevant,” in the context of a trial or administrative hearing type proceeding.
Kisor v. Wilkie

- The attacks on Seminole Rock/Auer deference seem to have arisen very quickly as a follow-on to the attacks on Chevron deference.
- The “doctrine” has a dubious basis, but probably makes sense.
- The 1945 Seminole opinion had some broad deference language in it, but the Court itself interpreted the rule to mean what the agency said it meant, and cited a contemporaneous public Bulletin in support.
- The 1997 Auer opinion was a unanimous opinion written by Justice Scalia, who, unlike the Justices who usually sided with him, was then a deference champion. He quoted the broad language from Seminole, but clearly found the agency interpretation quite reasonable.
- He reasoned that if the agency could have written the rule that way to begin with, surely it could interpret it that way.
- So it is not at all clear that these two cases really established a deference doctrine.

Kisor v. Wilkie

- The Chief Justice joined only parts of Justice Kagan’s opinion, so all we know “for sure” is:
  - Stare decisis worked for now;
  - Likely the price of Roberts’ vote (and possibly the other four that joined the holding) was a lengthy explanation of the limits of the deference doctrine:
    - The regulation must be “genuinely ambiguous,” which means that the court cannot interpret its meaning after using “all the standard tools of interpretation,” including “text, structure, history and purpose....”
    - After that, the court can accept the agency’s interpretation only if reasonable, meaning consistent with “text, structure, history and purpose....”
Kisor v. Wilkie

- And deference will not apply at all if:
  - The agency did not actually make a reasoned interpretation at a sufficiently high level to be authoritative;
  - The interpretation does not reflect the agency’s substantive expertise;
  - The interpretation is a post hoc invention in litigation or an “unfair surprise,” as when it conflicts with a prior interpretation.

- These principles probably should be applied to *Chevron* deference too.
  - The case is not over, because on remand the lower court must determine if the regulation is ambiguous and if so if the other guidelines above are met for deference.

- Parts of the Kagan plurality opinion that may or may not stick:
  - 1) *Auer* deference is rooted in a presumption that congress intended to invest the agency with that authority.

Kisor v. Wilkie

- 2) Following agency interpretation provides uniformity, as contrasted with multiple judges coming to divergent views.
- 3) The APA does not limit the power to interpret the regulation to the courts.
- 4) *Auer* deference does not give the agency another bite at the apple by improperly evading the notice and comment process, particularly if the regulation is interpretive, which need not be issued with notice and comment.
Kisor v. Wilkie

- Chief Justice’s concurring opinion said:
  - *Auer* deference is somewhat more substantial than *Skidmore* “power of persuasion” consideration of agency view;
  - This issue is very different from *Chevron* issues and this opinion of the Court does not touch on *Chevron* issues. [which likely means he would vote to reverse *Chevron*]
  - The lengthy Gorsuch concurrence shows that the deference issues will remain hot and if and when this case comes back up it may turn out differently.
  - He said the Kagan opinion contained so many limits on deference that it was “zombified.”
  - This is an extremely odd view for a lawyer to have of an attempt to state a rule precisely, but it shows (1) the concurrers probably forced the detail to be put into the Kagan opinion, and (2) they are planning their next moves.

*Chevron* Radiations, cont’d

- *Second:* *State Farm/Chenery* gloss on agency proof of non arbitrary rule adoption.
  - These Supreme Court opinions have been read to impose standards on agency explanation of rule adoption, and were applied against Treasury by Tax Court in *Altera*.
  - Applied by SCT in the census question case.
  - Requirements both substantive (logically relate facts found to conclusion reached) and procedural (contemporaneous explanation, not ad hoc later)
  - But the promotion of these two cites is likely due to frustration with *Chevron* deference; the SCT likely did not intend them at the time to put such pressure on reg. preambles. These opinions have been overread.
  - *Chenery* did not involve a rule.
  - *State Farm* did involve a rule and said: “The reviewing court should not attempt itself to make up for such deficiencies; we may not supply a reasoned basis for the agency’s action that the agency itself has not given. SEC v. Chenery Corp., 332 U.S. 194, 196 (1947). We will, however, "uphold a decision of less than ideal clarity if the agency's path may reasonably be discerned."


Chevron Radiations, State Farm/Chenery

- States should be concerned about Altera Corp. v. Commissioner, 145 T.C. 91 (2015), reversed, __ F. 3d __ (9th Cir. 2019).
- All 15 Tax Court judges agreed to strike down regulation under § 482, one of the broadest grants of authority to reallocate income among related taxpayers.
- The basis for the ruling was that the Tax Court thought the Treasury explanation in the regulation preamble was illogical. Treasury had said the standard was what unrelated parties did, but was unable to show that unrelated parties did what it required in the regulation.
- The 9th Circuit cut the Treasury slack, because it could see Treasury was struggling to coordinate what congress said (“commensurate with income”) with historic arm’s length analysis.

Chevron Radiations: State Farm/Chenery

- Dept. of Commerce v. New York, 139 S. Ct. 2551 (2019) Applied State Farm standard to Commerce Dept. census question: (1) did agency examine the relevant data needed to make choice? (2) did it state a satisfactory explanation of its choice, showing a rational connection of the facts and data to that choice?
- Court ruled that Secretary had stated reasonable grounds to reject Census Bureau recommendations, and lower court had substituted its opinion for the agency’s reasonable choice.
- Chenery requires the agency to disclose the basis of its action.
- Normally the court’s review of that disclosed basis is limited to what it said and its official record of its action.
Dept. of Commerce v. New York

- However, in rare cases it is appropriate to go beyond the record to inquire into the mental processes of the agency, on a strong showing of bad faith or improper behavior.
- That was justified here.
- The expanded administrative record that the lower court ordered to be filed showed that the agency’s official explanation of its rational for the census question was a pretext for its real reason.
- The Secretary was determined to insert the census question before the agency made any factual investigation whatsoever.
- This is not a case where the agency had a stated reason and an unstated reason: the sole reason was the unstated reason and the stated reason was “contrived.”

Other Chevron Radiations

- National Cable & Telecommunications Association v. Brand X Internet Services, 545 U.S. 967 (2005) confirmed that a legislative regulation could overturn a court ruling.
- But Brand X does not apply if a court (meaning mostly the Supreme Court) has interpreted the statute to mean one thing before the regulation changed that (Home Concrete).
- Judulang v. Holder, 565 U.S. 42 (2011) confirmed that Chevron deference and the APA arbitrary or capricious standard mean the same thing.
Another Odd *Chevron* Case

• King v. Burwell, 576 U.S. ___ (2015) ruled that “state exchanges” includes the federal insurance exchange for purposes of the ACA.
• The agency regulation said that but the CJ’s opinion said he would not give Chevron deference to that because the issue was above the agency’s pay grade. Congress could not have intended the agency to make such a rule contrary to the plain words of the statute, but the court would do so, because it was the manifest intent of congress.

Means What for Tax Regulations?

• None of the 2019 SCT rulings on deference involved federal taxation.
• Through the end of this Court Term:
  • *Chevron* deference is safe for the moment,
  • The distinction between interpretive and legislative regulations seem to be more solid than *Chevron* itself (which is odd),
  • *Skidmore* consideration of agency views is safe for the moment,
  • the anti-delegation doctrine has not obliterated most of the Treasury regulations, but stay tuned;
  • but in those cases where the IRS claims it is interpreting a Treasury regulation, the application of *Auer* deference will be more strictly considered; and
  • The *Chenery/State Farm* vague requirements were applied in the census case, meaning that its significance continues, even though *Altera* was reversed by the 9th Circuit.
Which Way?

- SCT may eliminate *Chevron's* deference.
  - but unclear what comes next:
    - Will all regs. be interpretive, and courts can fill gaps as well as agencies?
      - Happened in *Rite Aid Corp. v. US*, 255 F.3d 1357 (2001) (invalidated the duplicated loss component of the LDR, “interpreting” the most general of statutory guidelines, and broadest regulatory grant against IRS).
      - Meaning courts write consolidated return regs?
    - Or will there be no law until Treasury write a regulation?
    - Or will there be no law until congress clarifies the statute?

What is DOR to Do in Writing Guidance?

- Assuming state has the federal APA model, know what regulations will be legislative and choose to issue a legislative regulation with full understanding of requirements and consequences.
  - Be ready to prove delegation of authority
    - Based on statute like 7805, or specific grant
      - And if specific, what does it say: carry out “provisions” or “purposes”? 
  - Follow procedural requirements
  - Even minimal guidance in the statute can trip up the regulation
    - Example *Rite Aid*: consolidated return regulation invalid because court thought the statute said Treasury could not change normal code rules for consolidated groups (?)
    - State reasons for rule at time of adoption, but preferably in notice of proposal.
What is DOR to Do in Writing Guidance?

- If rule not legislative, embrace interpretation and be prepared to support the interpretation, when authority to write the law is lacking.
- Show your work; what relied on for the interpretation.
- Show other interpretations were considered.
- Avoid retroactive guidance unless absolutely necessary
  - Adds another argument for taxpayers
  - Although interpretation in theory is what the law always was
- If state distinguishes subregulatory guidance, limit it to interpretation

What is DOR to Do in Writing Guidance?

- Subregulatory guidance
  - Consider using Notice describing transactions that will be carefully audited.
  - Consider requiring disclosure of particular transactions.
  - Consider turning “letter rulings” into general rulings.
  - Use more revenue rulings applying law to specific facts; or issue specific guidance to auditors
  - These may be “guidance documents” under Model State APA.
- Don’t plan to make law in court
  - Can be unavoidable
  - Win will always be easier with prior guidance
  - Never know what rule you will get, even if favorable to DOR.
What is DOR to Do in Writing Guidance?

- Try to discourage infection of state administrative law by the multiple federal law limits on rule making (for which, read any recent Treasury Decision adopting a regulation).

What is DOR to Do in Litigation?

- Don’t make *Altera* mistake:
  - IRS felt it could not admit exactly what it was doing in the regulation because of conflicting obligations.
  - Created its own problem with the rule’s logic and Tax Court would not let IRS out of its own claim that arm’s length meant what people do.
- Don’t automatically assume *Chevron* regime applies to states.
- If faced with anti-*Chevron* court opinion or statutory change, try to carve down its reach
  - Does not apply to interpretations
  - May be limited to state tax court decisions, or be no more than a rule for de novo review of law and facts.
  - Consider whether expertised based, delegated authority, or no deference works best.
    - Even an anti-deference statute may not preclude expertise based considerations.
What is DOR to Do in Litigation?

• Think hard before trying to “fix” vague statute in litigation.
  • Are other avenues of laws change really closed off?
  • Is it really worth it to get retroactive effect of ruling?
  • Can catching taxpayers going forward be enough for the DOR?
  • Do scorched earth litigation tactics of DOR encourage taxpayers to do the same; or is it already too late?
• Understand the different kinds of vagueness
  • *Gregory v. Helvering*: “in pursuance of a plan of reorganization” was interpreted by the Supreme Court to mean “in pursuance of a plan of reorganizing a corporation for business purposes as normally occurring in the corporate world”
  • “loss must be sustained” (sec. 165): content could be given to “sustain”
  • “economic substance doctrine” may not really be “a thing”