No. 09-837

In the Supreme Court of the United States

Mayo Foundation for Medical Education and Research; Mayo Clinic; and Regents of the University of Minnesota,

Petitioners,

v.

United States,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF OF *AMICUS CURIAE* PROFESSOR KRISTIN E. HICKMAN IN SUPPORT OF RESPONDENT

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INTEREST OF *AMICUS CURIAE*[1]

Amicus is an Associate Professor of Law at the University of Minnesota Law School who teaches and writes in the areas of tax and administrative law. *Amicus* has a longstanding academic interest in the standards of review that courts employ in evaluating the substantive validity of Treasury regulations. *Amicus* has written extensively about judicial review of agency legal interpretations both generally and in the context of tax cases. *See, e.g.*, Kristin E. Hickman & Matthew D. Krueger, *In Search of the Modern* Skidmore *Standard*, 107 Colum. L. Rev. 1235 (2007); Kristin E. Hickman, *The Need for* Mead*, Rejecting Tax Exceptionalism in Judicial Deference*, 90 Minn. L. Rev. 1537 (2006); Thomas W. Merrill & Kristin E. Hickman, Chevron*'s Domain*, 89 Geo. L.J. 833 (2001). This Court has previously cited *Amicus*'s work regarding the scope of *Chevron* review. *See United States v. Mead Corp.*, 533 U.S. 218, 230 n.11 (2001). *Amicus* also co-authors an administrative law textbook. *See* Kristin E. Hickman & Richard J. Pierce, Jr., *Federal Administrative Law* (2010).

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[1] Consistent with Supreme Court Rule 37.3(a), *Amicus* files this brief with the written consent of both parties. Consistent with Supreme Court Rule 37.6, *Amicus* hereby certifies that this brief was not authored in whole or in part by counsel for any party and that *Amicus* received no monetary contribution toward the preparation or submission of this brief other than the general financial support of the academic institution with which she is affiliated. The views expressed in this brief are those of *Amicus* and do not necessarily reflect those of her employer.

Consistent with her scholarly interests, *Amicus* submits this brief solely to address issues regarding the standard of review for general authority Treasury regulations raised by the Petitioners and their *amici*. *Amicus* hopes this brief will assist the Court in resolving that important question. *Amicus* disclaims any view regarding either the clarity of Internal Revenue Code § 3121(b)(10) or the reasonableness of Treas. Reg. § 31.3121(b)(10)-2(c) as an interpretation of that statute.

SUMMARY OF THE ARGUMENT

Briefs in this case filed by the Petitioners and *Amicus Curiae* Professor Carlton M. Smith raise two important questions regarding the standard of review by which the Court should assess the substantive validity of Treas. Reg. § 31.3121(b)(10)-2(c). The first question is whether *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1986), or *National Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979), provides the appropriate evaluative standard for Treasury regulations promulgated pursuant to general authority delegated by § 7805(a) of the Internal Revenue Code, 26 U.S.C. § 7805(a). Assuming that the *Chevron* standard applies, the second question is whether *National Muffler* offers a tax-specific gloss on *Chevron* analysis, requiring a court to invalidate a general authority Treasury regulation that interprets an ambiguous statute as unreasonable if it lacks consistency, contemporaneity, or longevity, or if it was promulgated in reaction to an adverse judicial decision.

Consistent with the Court's decision in *United States v. Mead Corp.*, 533 U.S. 218 (2001), the Court should apply the *Chevron* standard of review in evaluating general authority Treasury regulations. *Mead* premises eligibility for *Chevron* deference on whether the agency interpretation carries the force and effect of law. General authority Treasury regulations like Treas. Reg. § 31.3121(b)(10)-2(c) clearly carry the force and effect of law.

The Court's post-*Chevron* jurisprudence has never squarely addressed whether the Court's pre-*Chevron* opinion in *National Muffler* requires a different standard of review for general authority Treasury regulations. Before this case, litigants have failed to raise the question clearly and unequivocally for the Court's consideration. The Court's post-*Chevron* statements regarding deference to general authority Treasury regulations have been mixed and inconclusive. Although the lower courts have exhibited some confusion regarding the question, since the Court's decision in *Mead*, the trend in the circuit courts of appeals has favored *Chevron* review. When viewed within the broader context of the Court's jurisprudence regarding judicial review of agency legal interpretations, it is clear that the *National Muffler* standard is best viewed as synonymous with that of *Skidmore v. Swift & Co.*, 323 U.S. 134 (1940). Just as the Court replaced *Skidmore* with *Chevron* as the standard of review for general authority regulations in other statutes, so the Court should conclude with respect to *National Muffler* and general authority Treasury regulations.

The Court should also resist the invitation to incorporate *National Muffler* factors such as contemporaneity, longevity, consistency, and responsiveness to adverse judicial decisions in assessing the reasonableness or permissibility of a general authority Treasury regulation at *Chevron* step two. The Court's *Chevron* jurisprudence clearly rejects basing a determination that an agency interpretation is unreasonable or impermissible on such factors. Beyond the existence of the Court's decision in *National Muffler*, no reason has been offered, and none exists, for the Court to treat properly promulgated Treasury regulations differently.

ARGUMENT

I. THE COURT SHOULD APPLY THE *CHEVRON* STANDARD OF REVIEW IN EVALUATING TREAS. REG.§ 31.3121(b)(10)-2.

A. The Court Reviews Agency Regulations That Carry The Force Of Law Using The *Chevron* Standard.

For several years now, the Court has recognized two competing standards of review for evaluating the substantive validity of agency legal interpretations. *See United States v. Mead Corp.*, 533 U.S. 218, 226–27 (2001); *Christensen v. Harris County*, 529 U.S. 576, 586–87, (2000). The first, articulated by the Court in *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), contains a two-part analysis. First, the Court assesses the clarity of the relevant statute. *Id.* at

842. If the statute's meaning is clear, that is the end of the inquiry, for both agencies and the courts must abide by clearly expressed congressional intent. *Id.* at 842–43. If the statute is ambiguous, however, then the second prong of the *Chevron* standard calls upon reviewing courts to defer to any interpretation thereof that is reasonable or permissible and not arbitrary or capricious.[2] *Id.* at 843.

The second standard that the Court uses in considering challenges to agency legal interpretations is that articulated in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944). *Skidmore* and its progeny call upon

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[2] *Amicus Curiae* Professor Carlton M. Smith suggests that the Court in *Chevron* and *Mead* articulated an arbitrary and capricious standard for "express" delegations of interpretive authority and a separate reasonableness standard for "implicit" ones. Am. Br. at 12–14 & 14 n.3. He then equates explicit delegations with specific grants and implicit delegations with general grants of rulemaking authority. *See id.* at 14 n.3. Although this argument reflects a creative parsing of the *Chevron* opinion, the Court has not followed this distinction in its post-*Chevron* jurisprudence. The Court has often used the "arbitrary and capricious" phraseology in analyzing general authority regulations under *Chevron* step two. *See, e.g.*, *Ragsdale v. Wolverine World Wide, Inc.*, 535 U.S. 81, 86 (2002); *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 742 (1996); *Sullivan v. Zebley*, 493 U.S. 521, 528 (1990). The Court has similarly deferred to specific authority regulations as "reasonable" or "permissible" interpretations. *E.g.*, *Household Credit Servs. v. Pfennig*, 541 U.S. 232, 242–43 (2004); *Verizon Communications, Inc. v. FCC*, 535 U.S. 467, 501–02, 523 (2002); *National Cable & Telecomm. Ass'n, Inc. v. Gulf Power Co.*, 534 U.S. 327, 333 (2002). In other words, the Court uses these phraseologies interchangeably, with "reasonable" and "permissible" serving as rhetorical equivalents and as the opposite of "arbitrary and capricious."

reviewing courts to consider various factors in determining the degree of deference that is appropriate for a given agency legal interpretation: "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." *Id.* at 140.

In *United States v. Mead Corp.*, 533 U.S. 218 (2001) this Court adopted a two-part test for evaluating whether a particular agency legal interpretation is eligible for *Chevron* rather than *Skidmore* deference. *Id.* at 226–27. First, the Court asks whether Congress has given the agency in question the authority to bind regulated parties with "the force of law." *Id.* If Congress has made such a delegation, then the Court inquires whether the agency has "exercise[d] . . . that authority." *Id.* Where the answers to both of *Mead*'s questions are affirmative, then *Chevron*'s two-part standard of review applies. *See id.* at 237–38. If the answer to either of *Mead*'s two questions is negative, however, then *Skidmore* offers the appropriate evaluative standard. *Id.* at 237–38.

B. General Authority Treasury Regulations Like Treas. Reg. § 31.3121(b)(10)-2 Carry The Force Of Law.

The Internal Revenue Code (I.R.C.) explicitly grants the Secretary of the Treasury (Treasury) broad authority to interpret its various provisions through rulemaking. Some of these delegations are

conveyed through specific authorizations or mandates to promulgate regulations to fill congressionally-identified statutory gaps. *See, e.g.*, 26 U.S.C. §§ 67(c)(1); 163(e)(3)(B)(ii); 263A(e)(5); 1502. Additionally, numerous specific substantive provisions of the I.R.C. contain more general language giving Treasury the authority to adopt rules as "necessary to carry out the purposes of this paragraph" or "this subsection" or "this section"—sometimes with specific examples, *see, e.g.*, 26 U.S.C. §§ 108(c)(5); 167(e)(6); 170(f)(12)(F)—and other times without. *See, e.g.*, 26 U.S.C. §§ 21(f); 162(m)(5)(H); 1244(e); *see also* N.Y. State Bar Ass'n Tax Section, *Report on Legislative Grants of Regulatory Authority* 2–6 (Nov. 3, 2006) (elaborating types of specific authority grants in the I.R.C.). Finally, I.R.C. § 7805(a) grants Treasury the general rulemaking authority to develop "all needful rules and regulations for the enforcement of" the entirety of Title 26 of the U.S. Code. 26 U.S.C. § 7805(a). Treasury routinely invokes this general authority grant in promulgating all Treasury regulations, even where specific authority may also support its actions. *See* Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance With Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727, 1751, 1754–57 (2007) (documenting empirical analysis showing citation to I.R.C. § 7805(a) in 100% of 232 Treasury regulation projects studied and lack of citation to specific authority even where available).

Established administrative law doctrine holds that properly issued legislative rules carry the force

of law while interpretative rules do not. *See, e.g.*, *Chrysler Corp. v. Brown*, 441 U.S. 281, 302–03 (1979); 1 Richard J. Pierce, Jr., *Administrative Law Treatise* § 6.4 (5th ed. 2010). Mimicking (imprecisely) the language of administrative law and the Administrative Procedure Act (APA), *see* 5 U.S.C. § 553, the tax community commonly refers to specific authority Treasury regulations as "legislative" and to general authority Treasury regulations as "interpretative," sometimes shortened as "interpretive." *See, e.g.*, Irving Salem et al., *ABA Section of Taxation Report of the Task Force on Judicial Deference*, 57 Tax Law. 717, 728 (2004). Both drawing from and contributing to this practice, Treasury claims that the vast majority of its regulations interpreting the I.R.C. are promulgated under the general authority of I.R.C. § 7805(a) and, thus, are interpretative rules exempt from notice-and-comment rulemaking under APA § 553. *See* Internal Revenue Serv., *Internal Revenue Manual* § 32.1.5.4.7.5.1 (stating that "most IRS/Treasury regulations are interpretative, and therefore not subject to these provisions of the APA"); Hickman, *Coloring Outside the Lines*, *supra*, at 1750 (documenting claims of APA inapplicability in more than 80% of 232 Treasury regulation projects). Treasury also claims authority under I.R.C. § 7805(e) to issue legally binding temporary regulations with only post-promulgation notice and comment. *See, e.g.*, *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, No. 25868-06, 134 T.C. No. 11, 2010 WL 1838297 at *21 (May 6, 2010) (Halpern & Holmes, J.J., concurring). Whether Treasury regulations issued under I.R.C. § 7805(a) are interpretative rules for

purposes of APA rulemaking requirements is a hotly litigated issue at present.[3] Regardless, the Court should not misconstrue either the tax community's use of the interpretative term to describe general authority Treasury regulations or the controversy over Treasury's interpretation of APA rulemaking requirements as indicators that these regulations lack the force of law, for several reasons.

First, while the Court has never identified precisely the characteristics that indicate whether an agency legal interpretation carries the force of law, congressional imposition of penalties for noncompliance would seem conclusive proof of legal force. *See, e.g.*, Thomas W. Merrill, *The* Mead *Doctrine: Rules and Standards, Meta-Rules and Meta-Standards*, 54 Admin. L. Rev. 807, 827–30 (2002). Congress has imposed penalties upon taxpayers and tax return preparers who fail to

[3] In May of this year, two judges from the United States Tax Court rejected the government's position on this question. *See Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, No. 25868-06, 134 T.C. No. 11, 2010 WL 1838297 *17–22 (May 6, 2010) (Halpern & Holmes, J.J., concurring). The issue is pending before several of the circuit courts of appeals. *See, e.g.,* Reply Brief for the Appellant, *Salman Ranch, Ltd. v. Comm'r*, No. 09-9015 (10th Cir. June 1, 2010); Brief for the Appellant, *Grapevine Imports, Ltd. v. United States*, No. 2008-5090 (Fed. Cir. May 25, 2010); Reply Brief for the Appellant, *Comm'r v. M.I.T.A. Partners*, No. 09-60827 (5th Cir. May 6, 2010); Brief for the Appellee, *Home Concrete & Supply, LLC v. United States*, No. 09-2353 (4th Cir. Apr. 30, 2010); Brief for Bausch & Lomb Inc. as Amici Curiae Supporting Appellees, *Salman Ranch, Ltd. v. Comm'r*, No. 09-9015 (10th Cir. Apr. 27, 2010); Brief for Bausch & Lomb Inc. as Amici Curiae Supporting Appellees, *Comm'r v. M.I.T.A. Partners*, No. 09-60827 (5th Cir. Apr. 14, 2010).

comply with general as well as specific authority Treasury regulations. *See, e.g.*, 26 U.S.C. § 6662(a)-(b)(1) (imposing penalties for failure to comply with "rules or regulations"); 26 U.S.C. § 6694(b) (same); *see also* Treas. Reg. § 1.6662-3(b)(2) (defining "rules and regulations" as including "temporary or final Treasury regulations issued under the [Internal Revenue] Code"); Treas. Reg. § 1.6694-3(e) (same).

Second, Treasury, the Internal Revenue Service, tax professionals, taxpayers, and the courts all operate with the understanding that both specific and general authority Treasury regulations are legally binding on the government and taxpayers alike. *See, e.g.*, *Swallows Holding, Ltd. v. Comm'r*, 515 F.3d 162, 168–69 (3d Cir. 2008) (holding that reasonable final Treasury regulations promulgated under I.R.C. § 7805(a) carry the force of law); *Estate of Gerson v. Comm'r*, 507 F.3d 435, 438 (6th Cir. 2007) (noting that both temporary and final general authority Treasury regulations are legally binding); *Bankers Life & Cas. Co. v. United States*, 142 F.3d 973, 979 (7th Cir. 1998) (recognizing that all Treasury regulations have the force of law); Sheldon I. Banoff, *Dealing with the "Authorities": Determining Valid Legal Authority in Advising Clients, Rendering Opinions, Preparing Tax Returns, and Avoiding Penalties*, 66 Taxes 1072, 1086, 1092 (1988) (noting legal effect of final and temporary Treasury regulations); Donald L. Korb, *The Four R's Revisited: Regulations, Rulings, Reliance, and Retroactivity in the 21st Century: A View From Within*, 46 Duq. L. Rev. 323, 327–330 (2008) (recognizing binding effect of all Treasury regulations).

Third, while the Court has declined to declare notice-and-comment rulemaking as an absolute prerequisite for *Chevron* review, the Court has recognized "a very good indicator of delegation meriting *Chevron* treatment in express congressional authorizations to engage in the process of rulemaking . . . that produces regulations . . . for which deference is claimed." *United States v. Mead Corp.*, 533 U.S. 218, 229 (2001). Even beyond its delegations of authority to Treasury to promulgate rules backed by sanctions for noncompliance, Congress expressly signaled its intent that Treasury should utilize notice-and-comment rulemaking in promulgating its regulations. Specifically, in response to Treasury's habit of promulgating temporary regulations without notice and comment, Congress enacted I.R.C. § 7805(e) requiring Treasury to accompany temporary regulations with a notice of proposed rulemaking and giving Treasury three years to complete the notice-and-comment process. *See* 26 U.S.C. § 7805(e); *see also* Michael Asimow, *Public Participation in the Adoption of Temporary Tax Regulations*, 44 Tax Law., 343, 363–64 (1991) (documenting history of I.R.C. § 7805(e)); Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Treasury Regulations*, 3 Hous. Bus. & Tax L.J. 248, 254 (2003) (describing reasons for adopting I.R.C. § 7805(e)). Additionally, Treasury claims to and does utilize either pre- or post-promulgation notice and comment in adopting most Treasury regulations, irrespective of the authority supporting their issuance. *See, e.g.*, Internal Revenue Serv., *Internal Revenue Manual* §§ 32.1.2.3.3; 32.1.5.4.7.5.1 (declaring Treasury policy of pursuing public notice and comment for all

regulations); Hickman, *Coloring Outside the Lines*, *supra*, at 1749 (documenting that 95% of 232 Treasury regulation projects employed either pre- or post-promulgation notice-and-comment rulemaking). Indeed, Treas. Reg. § 31.3121(b)(10)-2 is a product of notice-and-comment rulemaking. *See* Final Regulation, Student FICA Exception (T.D. 9167), 69 Fed. Reg. 76404 (Dec. 21, 2004), 2005-1 C.B. 261; Notice of Proposed Rulemaking and Notice of Public Hearing, Student FICA Exception, 69 Fed. Reg. 8604 (Feb. 25, 2004).

Finally, the tax community's habit of labeling only those regulations issued under I.R.C. § 7805(a) as issued under general authority neglects the variety of rulemaking authorizations contained within other provisions of the Internal Revenue Code. Historically, delegations of rulemaking power characterized as specific authority in both the I.R.C. and in other statutes tended to instruct government officials to promulgate rules or regulations to fill a congressionally-identified gap in the statute. Hence, the often-cited, paradigmatic example of tax legislative rules are those promulgated pursuant to I.R.C. § 1502, which contains just this sort of specific authority grant. *Compare* Communications Act of 1934, Pub. L. No. 73-416, § 220, 48 Stat. 1064, 1078–80 (codified at 47 U.S.C. § 220) (giving the FCC the authority to adopt uniform accounting rules). Even those members of the tax community who disclaim the applicability of *Chevron* for Treasury regulations issued under I.R.C. § 7805(a) acknowledge the eligibility for *Chevron* deference of specific authority Treasury regulations. *See, e.g.*, Irving Salem et al.,

ABA Section of Taxation Report of the Task Force on Judicial Deference, 57 Tax Law. 717, 738 (2004). As noted above, however, many grants of rulemaking authority contained within substantive provisions of the Internal Revenue Code are linguistically indistinguishable from I.R.C. § 7805(a). A grant of authority, contained in a substantive provision of the I.R.C., to prescribe regulations "as necessary to carry out the purposes of this" section, subsection, or paragraph ultimately extends Treasury no greater rulemaking power than it possesses as a result of I.R.C. § 7805(a). Characterizing the former as legislative (and thus carrying the force of law) and only the latter as interpretative (and thus not) places too much importance on an arbitrary distinction.

In short, the Court should not consider either the tax community's use of the interpretative label or Treasury's interpretation of APA rulemaking requirements as dispositive of whether general authority Treasury regulations carry the force and effect of law. Whatever that standard may mean at the margins for purposes of *Chevron* eligibility, general authority Treasury regulations clearly carry the force and effect of law. In light of the Court's reasoning in *United States v. Mead Corp.*, 533 U.S. 218 (2001), the Court should evaluate the substantive validity of Treas. Reg. § 31.3121(b)(10)-2 using the *Chevron* standard of review.

II. THE COURT SHOULD NOT DISREGARD THE *CHEVRON* STANDARD IN FAVOR OF *NATIONAL MUFFLER* REVIEW IN EVALUATING THE VALIDITY OF GENERAL AUTHORITY TREASURY REGULATIONS.

Several years before deciding *Chevron*, in *National Muffler Dealers Ass'n, Inc. v. United States*, 440 U.S. 472 (1979), this Court assessed the substantive validity of a Treasury regulation issued pursuant to general authority under I.R.C. § 7805(a). In so doing, the Court articulated a series of factors as relevant for purposes of evaluating the regulation:

> 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.

Id. at 477.

A few years later, but again before deciding *Chevron*, this Court again evaluated general authority Treasury regulations in two cases—*Rowan Companies, Inc. v. United States*, 452 U.S. 247 (1981), and *United States v. Vogel Fertilizer Co.*, 455 U.S. 16 (1982). In both *Rowan Companies* and *Vogel Fertilizer*, the Court distinguished general authority Treasury regulations from those issued pursuant to specific authority, and counseled less deferential review using the *National Muffler* standard for the former. *See Rowan Cos.*, 452 U.S. at 253; *Vogel Fertilizer*, 455 U.S. at 24–25.

Amicus Curiae Professor Carlton M. Smith contends that this Court should continue to apply the *National Muffler* standard rather than *Chevron* in evaluating the substantive validity of general authority Treasury regulations. Am. Br. at 3, 40. In fact, this case represents the first time the Court has been asked clearly and unequivocally whether or not *Chevron* replaced *National Muffler* as the standard of review for these interpretations of law. Further, a thorough review of the tax and nontax jurisprudence strongly supports the conclusion that applying *Chevron* rather than *National Muffler* in reviewing general authority Treasury regulations is more consistent with existing jurisprudence.

A. The Court Has Not Explicitly Addressed Whether Or Not *Chevron* Replaced *National Muffler* As The Evaluative Standard For General Authority Treasury Regulations.

Far from consistently counseling *National Muffler* as the appropriate evaluative standard for general authority Treasury regulations, this Court's post-*Chevron* jurisprudence has been inconclusive on the question. In *Cottage Savings Ass'n v. Commissioner*, 499 U.S. 554 (1991), the Court clearly cited and applied *National Muffler*'s multiple factors in evaluating a general authority Treasury regulation. *Id.* at 560–61. Subsequently, in *Boeing Co. v. United States*, 537 U.S. 437 (2003), the Court cited *Cottage Savings* as supporting deference toward a regulation it identified as promulgated under I.R.C. § 7805(a). *Id.* at 448. But in *United States v. Boyle*, 469 U.S. 241 (1985), the Court rejected a taxpayer's challenge to the validity of a general authority Treasury regulation, stating expressly that the regulation was entitled to deference under *Chevron*. *Id.* at 246 n.4. And in *Atlantic Mutual Insurance Co. v. Commissioner*, 523 U.S. 382 (1998), the Court cited and clearly applied the *Chevron*'s two steps in deferring to a Treasury regulation that both parties described on brief as "interpretive." *See id.* at 387–91; *see also* Brief for the Petitioner at 4, *Atlantic Mut. Ins. Co. v. Comm'r*, 523 U.S. 382 (1998) (No. 97-147); Brief for the Respondent at 4, 20, 21, 35, *Atlantic Mut. Ins. Co. v. Comm'r*, 523 U.S. 382 (1998) (No. 97-147).

In *United States v. Burke*, 504 U.S. 229 (1992), after the Court's majority resolved the case without citing or employing either *Chevron* or *National Muffler*, Justice Scalia writing in concurrence cited and applied *Chevron* in concluding that the IRS's interpretation of the statute was unreasonable. *Id.* at 242. Nevertheless, in *Commissioner v. Estate of Hubert*, 520 U.S. 93 (1997), Justice Scalia cited *National Muffler* as supporting judicial deference to a general authority Treasury regulation as a "reasonable interpretation of" the statute. *Id.* at 127–28, 138. In *Newark Morning Ledger Co. v. United States*, 507 U.S. 546 (1993), Justice Souter writing in dissent cited both *Chevron* and *National Muffler* among cases supporting judicial deference to a Treasury regulation. *Id.* at 575–76.

Finally, in a few tax cases, the Court has cited *National Muffler* in dicta more generally as supporting judicial deference to Treasury regulations. In *Skinner v. Mid-America Pipeline Co.*, 490 U.S. 212 (1989), a case concerning whether tax legislation violated the nondelegation doctrine, the Court cited *National Muffler* as generally supporting judicial deference to the IRS Commissioner's "reasonable interpretations" of the Internal Revenue Code. *Id.* at 222. In *United States v. Cleveland Indians Baseball Co.*, 532 U.S. 200 (2001), the Court cited *National Muffler* among other cases as counseling deference to reasonable Treasury regulations, *see id.* at 218–19, after which the Court concluded that the regulation did not address the precise question at issue and instead deferred to an interpretation advanced through several revenue rulings as the agency's

"longstanding interpretation of its own regulations." *See id.* at 219 (citing *Thomas Jefferson Univ. v. Shalala*, 512 U.S. 504, 512 (1994)). *See also United Dominion Indus., Inc. v. United States*, 532 U.S. 822, 840–41 (2001) (Stevens, J., dissenting) (citing *National Muffler* in favor of resolving statutory ambiguity through executive action but acknowledging that no Treasury regulation addressed the issue at hand).

In summary, the Court's precedents appear evenly divided in actually applying *Chevron* versus *National Muffler* to evaluate general authority Treasury regulations. Although citations to *National Muffler* slightly outnumber those to *Chevron* in concurring and dissenting opinions and in dicta in tax cases, these various references are sufficiently mixed to disprove any claim to a definitive conclusion. The reason for the muddle is clear: notwithstanding a disagreement among the circuit courts of appeals, discussed below, that emerged during the 1990s over the standard of review for general authority Treasury regulations, briefing before this Court in tax cases over the past 25 years has failed to present that question squarely. In all of the above cited cases, the parties and *amici* either failed clearly to identify a standard of review or cited one or both of *Chevron* and *National Muffler*, often among other cases, as supporting judicial deference without articulating that the two cases might offer different review standards. Correspondingly, many of the Court's citations to *National Muffler* accompany boilerplate references to deference and reasonableness that the *Chevron* opinion would likewise support. The most

reasonable inference to draw from this history is that the Court has not explicitly addressed whether *Chevron* supplanted *National Muffler* as the standard of review for general authority Treasury regulations.

B. The Trend In The Circuit Courts Of Appeals Favors The *Chevron* Standard For Evaluating General Authority Treasury Regulations.

Prior to the Court's decision in *United States v. Mead Corp.*, 533 U.S. 218 (2001), the lower courts exhibited tremendous confusion over the relationship between *Chevron* and *National Muffler*. *See Boeing Co. v. United States*, 258 F.3d 958, 963 (9th Cir. 2001) (acknowledging a split and reserving the question); *Gen. Elec. Co. v. Comm'r*, 245 F.3d 149, 154 n.8 (2d Cir. 2001) (same). At least one circuit—the Sixth—expressly adopted *Chevron* rather than *National Muffler* as the standard of review for general authority Treasury regulations. *See Peoples Fed. Sav. & Loan Ass'n of Sidney v. Comm'r*, 948 F.2d 289, 299, 304 (6th Cir. 1991). Other circuits concluded that *National Muffler* provided the appropriate standard of review and required a lesser degree of deference than *Chevron*. *See, e.g.*, *St. Jude Med., Inc. v. Comm'r*, 34 F.3d 1394, 1400, 1402 (8th Cir. 1994) (abrogated on other grounds by *Boeing Co. v. United States*, 537 U.S. 437 (2003)); *Snowa v. Comm'r*, 123 F.3d 190, 197 (4th Cir. 1997); *Snap-Drape Inc. v. Comm'r*, 98 F.3d 194, 197 (5th Cir. 1996); *see also Schuler Indus., Inc. v. United States*, 109 F.3d 753, 754–55 (Fed. Cir. 1997) (suggesting similar position in case evaluating specific authority Treasury

regulation). Still other circuits found *Chevron* and *National Muffler* to be indistinguishable as a practical matter. *See, e.g.*, *Bankers Life & Cas. Co. v. United States*, 142 F.3d 973, 978–83 (7th Cir. 1998).

Since this Court's decision in *Mead*, however, the trend among the circuit courts of appeals has been markedly in favor of *Chevron*. In *Swallows Holding, Ltd. v. Commissioner*, 515 F.3d 162 (3d Cir. 2008), the Third Circuit explicitly addressed the question of whether *National Muffler* retained independent vitality as a standard of review for general authority Treasury regulations after *Chevron*, concluding that it did not and that *Chevron* provides the appropriate standard of review. *See id.* at 167–68. Having previously reserved the question, the Second Circuit seems also to have concluded that *Chevron* rather than *National Muffler* provides the standard of review for evaluating general authority Treasury regulations. *See McNamee v. Dep't of Treasury*, 488 F.3d 100, 105 (2d Cir. 2007). The Sixth Circuit, which already employed *Chevron* to assess general authority Treasury regulations, reaffirmed its conclusion that *Chevron* is the proper standard. *See Estate of Gerson v. Comm'r*, 507 F.3d 435, 437–38 (6th Cir. 2007); *Littriello v. United States*, 484 F.3d 372, 376–78 (6th Cir. 2007); *Hosp. Corp. of Am. & Subs. v. Comm'r*, 348 F.3d 136, 140–41 (6th Cir. 2003). Meanwhile, the Fifth Circuit, which previously utilized the *National Muffler* standard, has acknowledged a need to revisit the question in light of *Mead*. *See Kornman & Assoc., Inc. v. United States*, 527 F.3d 443, 455 n.10 (5th Cir. 2008). Indeed, the Eighth Circuit in this case clearly applied

Chevron, though, like Petitioners, Pet. Br. at 36, that court invoked *National Muffler* in evaluating the reasonableness of Treas. Reg. § 31.3121(b)(10)-2 at *Chevron* step two. *See Mayo Found. for Med. Educ. & Research v. United States*, 568 F.3d 675, 680–81 (8th Cir. 2009).

This trend does not mean that *Mead* has eliminated all confusion over the role of *National Muffler* in evaluating general authority Treasury regulations. For example, the United States Tax Court continues to prefer the *National Muffler* standard for general authority Treasury regulations, only applying *Chevron* in such cases when the circuit court to which a case may be appealed does. *Compare, e.g.*, *Swallows Holding, Ltd. v. Comm'r*, 126 T.C. 96, 130–31 (2006), *vacated* 515 F.3d 162 (3d Cir. 2008), *with New Millennium Trading, L.L.C. v. Comm'r*, 131 T.C. 275, 286–87 (2008). Without acknowledging that *Chevron* might provide an alternative, the Tenth Circuit has continued to apply the *National Muffler* standard, extending at least the impression of a circuit split over the issue. *See Scanlon White, Inc. v. Comm'r*, 472 F.3d 1173, 1175 (10th Cir. 2006). Other circuits that applied *National Muffler* in cases prior to this Court's decision in *Mead*, like the Fourth Circuit and the Federal Circuit, have not revisited the question since. Lower courts would certainly benefit from clarifying instruction from this Court. Nevertheless, in light of *Mead*'s holding basing *Chevron* eligibility on whether an interpretation carries the force of law, and given the obvious legal force of general authority Treasury regulations, it is unsurprising that the lower courts

are according *Chevron* analysis a greater role in these cases.

C. The Court Should Recognize *National Muffler* As Indistinguishable From *Skidmore* Review, And Thus As Replaced By *Chevron* As The Standard Of Review For General Authority Treasury Regulations.

The Court did not pull the *National Muffler* standard from thin air. For decades before deciding *Chevron*, this Court again and again counseled a less deferential, multi-factor standard like that articulated in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), for evaluating agency interpretations of law issued pursuant to tax and nontax general authority grants. Rather than reflecting a unique, tax-specific standard of review, *National Muffler* and its pre-*Chevron* progeny fall squarely within this broader jurisprudence. With *Chevron*, the Court signaled a shift in favor of a more deferential posture in reviewing general authority regulations that carry the force and effect of law. So, too, the Court should conclude with respect to general authority Treasury regulations.

Many regulatory statutes dating from the Progressive and New Deal eras, including but not limited to the early federal income tax laws, included both specific and general authority rulemaking grants. *See, e.g.*, Communications Act of 1934, Pub. L. No. 73-416, §§ 4(i) & 220, 48 Stat. 1064, 1068, 1078 (granting both general and specific authority, respectively, to the Federal Communications

Commission); Revenue Act of 1921 §§ 204(b)–(c), 217(e), & 1303, 42 Stat. 227, 231, 244–45 & 309 (giving Treasury and the IRS both specific and general authority. The Court and legal scholars alike considered both tax and nontax regulations promulgated pursuant to specific authority grants as carrying the force and effect of law, and thus legislative in character. *See, e.g.*, *Columbia Broad. Sys. v. United States*, 316 U.S. 407, 416–22 (1942); *Md. Cas. Co. v. United States*, 251 U.S. 342, 349 (1920); Kenneth Culp Davis, *Administrative Rules—Interpretative, Legislative, and Retroactive*, 57 Yale L.J. 919, 928–29 (1948); Robert C. Brown, *Regulations, Reenactment, and the Revenue Acts*, 54 Harv. L. Rev. 377, 384–85 (1941). By contrast, both tax and nontax general authority regulations were considered nonbinding, and thus interpretative. *See, e.g.*, Davis, *Administrative Rules*, *supra*, at 928-30; Stanley S. Surrey, *The Scope and Effect of Treasury Regulations Under the Income, Estate, and Gift Taxes*, 88 U. Pa. L. Rev. 556, 557–58 (1940).

In light of this dichotomy, the Court counseled strong, "controlling" judicial deference to specific authority regulations—legislative rules—interpreting both tax and nontax statutes. *Am. Tel. & Tel. Co. v. United States*, 299 U.S. 232, 236–37 (1936) (applying this standard to a nontax specific authority regulation); *see also, e.g.*, *Atchison, Topeka & Santa Fe Ry. v. Scarlett*, 300 U.S. 471, 474 (1937) (same) *Comm'r v. S. Tex. Lumber Co.*, 333 U.S. 496, 503 (1948) (applying same standard to a specific authority tax regulation); Erwin N. Griswold, *A Summary of the Regulations Problem*, 54 Harv. L. Rev. 398, 401

(1941) (discussing judicial review of specific authority Treasury regulations). In both tax and nontax cases involving general authority regulations—interpretative rules—the Court was less deferential but discussed factors such as contemporaneity, longevity, and consistency, and congressional reenactment that, where present, justified giving agency interpretations respect. *See, e.g.*, *Burnet v. Chi. Portrait Co.*, 285 U.S. 1, 16 (1932) (opining that "great weight is attached to the construction consistently given to a statute by the executive department charged with its administration" even though "[t]he court is not bound by an administrative construction"); *Mason v. Routzahn*, 275 U.S. 175, 178 (1927) (deferring to contemporaneous and long-standing Treasury practice expressed in regulations); *Helvering v. R.J. Reynolds Tobacco Co.*, 306 U.S. 110, 114–15 (1939) (noting consistency and congressional reenactment in deferring to general authority Treasury regulation); *see also* Griswold, *supra*, at 404–11 (discussing the role of contemporaneity and "long-continuedness" in extending judicial deference to general authority Treasury regulations). The Court's decision in *Skidmore*, counseling deference based on a variety of persuasive factors including consistency, fits squarely within this jurisprudence. *See Skidmore*, 323 U.S. at 140.

In his renowned treatise, Kenneth Culp Davis documented this historical dichotomy between specific and general authority regulations and the degrees of deference extended by the courts. *See* 2 Kenneth Culp Davis, *Administrative Law Treatise* §§ 7.8–7.14 (2d ed. 1979). In *Batterton v. Francis*, 432

U.S. 416 (1977), the Court summarized its past deference jurisprudence similarly, extending strong deference to legislative regulations and lesser deference based on such factors as timing, consistency, and expertise for interpretative regulations under *Skidmore* and other cases. *See id.* at 425–26 & 425 n.9. In calling for a less deferential *National Muffler* review for general authority Treasury regulations, the Court in *Rowan Companies, Inc. v. United States*, 452 U.S. 247 (1981), explicitly linked the *National Muffler* standard to its analysis regarding specific versus general authority regulations in *Batterton v. Francis* as well as to earlier tax cases. *Rowan Cos.*, 452 U.S. at 252–53.

Indeed, the resemblance between the *Skidmore* and *National Muffler* standards is striking. With both standards, the Court relies upon the presence or absence of several contextual factors to ascertain the degree of deference a reviewing court should extend to an agency legal interpretation. In *Skidmore v. Swift & Co.*, the Court identified "the thoroughness evident in [an interpretation's] consideration, the validity of its reasoning, [and] its consistency with earlier and later pronouncements" as persuasive factors. *Id.* at 140. In *United States v. Mead Corp.*, 533 U.S. 218 (2001), drawing from both pre- and post-*Chevron* precedents, the Court described *Skidmore* analysis with two slightly different lists of factors: first, "[t]he degree of the agency's care, its consistency, formality, and relative expertness, and... the persuasiveness of the agency's position," *id.* at 228; and then, "thoroughness, logic, and expertness, [and] its fit with prior interpretations." *Id.* at 235.

Historically, congressional reenactment was a consideration in *Skidmore* analysis, but the persuasiveness of this factor has declined in modern jurisprudence. *See* 2 Davis, *Administrative Law Treatise*, *supra*, at § 7:14. Like *Mead*, *National Muffler* offers a marginally different list of relevant considerations from *Skidmore*, but the listed factors are consistent with those that emerge from the broader *Skidmore* jurisprudence: "contemporaneous construction," "the manner in which [the regulation] evolves," "length of time," "reliance," "consistency," and "the degree of [congressional] scrutiny." *National Muffler*, 440 U.S. 472, 477 (1979). *National Muffler* speaks of regulations "harmoniz[ing] with the plain language of the statute, its origin, and its purpose." *Id.* But it is difficult to imagine the Court applying *Skidmore* analysis to defer to a regulation that did not. In short, when viewed in the context of a broader jurisprudence, it is difficult to distinguish *National Muffler* from *Skidmore* analysis.

The 1960s and 1970s saw a virtual explosion of agency rulemaking, with agencies seeking to achieve more policy objectives through general authority regulations. *See* 1 Richard J. Pierce, Jr., *Administrative Law Treatise* § 1.6 (5th ed. 2010). The lower courts addressed this expansion of rulemaking activity by characterizing many general authority regulations as legislative rather than interpretative based on what the regulations did rather than the source of their authority. *See, e.g.*, *Nat'l Nutritional Foods Ass'n v. Weinberger*, 512 F.2d 688, 697 (2d Cir. 1975) (concluding that FDA regulations issued pursuant to general authority were legislative rules

because they were legally binding); *see also* 2 Davis, *Administrative Law Treatise*, *supra*, at §§ 7.13, 7.15 (documenting lower court blurring of the distinction between legislative and interpretative rules); Michael Asimow, *Nonlegislative Rulemaking and Regulatory Reform*, 1985 Duke L.J. 381, 393–401 (noting declining relevance of the specific versus general authority distinction).

Consistent with this trend, this Court's decision in *Chevron U.S.A. Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), recognized that exercises of implicit (*i.e.*, general authority) as well as explicit (*i.e.*, specific authority) delegations merit strong deference. *Id.* at 843–44. Whatever the scope of the legislative and interpretative labels in the post-*Chevron* era, as the Court made clear in *United States v. Mead Corp.*, 533 U.S. 218 (2001), the touchstone for *Chevron* eligibility is whether an agency action carries the force of law, not whether the authority exercised is specific or general. *Id.* at 226–27. The regulation at issue in *Chevron* was a general authority regulation promulgated under a grant that strongly resembles I.R.C. § 7805(a). *Chevron*, 467 U.S. at 840–841 (citing Final Rule, Requirements for Preparation, Adoption and Submittal of Implementation Plans and Approval and Promulgation of Implementation Plans, 46 Fed. Reg. 50766 (Oct. 14, 1981)); *see also* 42 U.S.C. § 7601(a) (granting EPA general authority to promulgate regulations under the Clean Air Act). Hence, this Court has repeatedly extended *Chevron* deference to general authority regulations under a variety of statutes. *See, e.g.*, *National Cable & Telecomm. Ass'n*

v. Brand X Internet Servs., 545 U.S. 969, 980–81 (2005); *Household Credit Servs., Inc. v. Pfennig*, 541 U.S. 232, 238–39 (2004); *Sullivan v. Everhart*, 494 U.S. 83, 87, 88–89 (1990); *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 842–43, 844 (1986); *cf. Gonzales v. Or.*, 546 U.S. 243, 258–59 (2006) (recognizing the Court's application of *Chevron* standard in evaluating exercises of general authority). Whatever the confusion generated in the lower courts by a lack of clarity in the Court's post-*Chevron* tax jurisprudence, no reason has been offered, and none exists, for treating general authority Treasury regulations differently.

In sum, *National Muffler* is merely one of many in the line of pre-Chevron cases that counsels *Skidmore* review for general authority regulations. Every persuasive factor cited by the Court in *National Muffler* can be found in other pre-*Chevron* cases involving general authority regulations under one or another regulatory statute. Thus, to the extent that *Chevron* supplanted *Skidmore* as the evaluative standard for general authority regulations under other statutes, this Court should find that *Chevron* did the same for regulations promulgated under I.R.C. § 7805(a).

III. THE COURT SHOULD NOT SPECIALLY INCORPORATE *NATIONAL MUFFLER* FACTORS INTO *CHEVRON* STEP TWO ANALYSIS IN TAX CASES.

In their opening brief, Petitioners cite *Chevron* as the applicable standard of review, Pet. Br. at 19,

and then construct arguments against Treas. Reg. § 31.3121(b)(10)-2 consistent with *Chevron*'s two-step approach. Nevertheless, in their analysis under *Chevron*'s second step, Petitioners rely upon *National Muffler* for the proposition that Treas. Reg. § 31.3121(b)(10)-2 is unreasonable, among other reasons, for its lack of contemporaneity, longevity, or consistency, and for the fact that Treasury promulgated the regulation in response to adverse interpretations of I.R.C. § 3121 by the courts of appeals. Br. at 36. While such factors may weigh against respecting an agency's interpretation under the review standard articulated in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), for agency actions lacking the force of law, the Court should not employ these factors in the context of *Chevron* analysis as a basis for finding a properly promulgated Treasury regulation unreasonable or impermissible.

The Court has occasionally identified the presence of such factors as additional reasons for deferring to an agency interpretation that it has found otherwise to be eligible for *Chevron* deference. *See, e.g.*, *Barnhart v. Walton*, 535 U.S. 212, 219–220 (2002) (finding an agency interpretation "permissible" under *Chevron* analysis, and offering the interpretation's longevity as an additional reason for extending deference). The Court has declined, however, to find the absence of these factors as a basis for refusing to defer under *Chevron*. *See, e.g.*, *Smiley v. Citibank (South Dakota), N.A.*, 517 U.S. 735, 740 (1996) (rejecting "antiquity or contemporaneity," as well as a regulation's responsiveness to litigation, as reasons to reject an

interpretation under *Chevron*). And rightly so.

In *Chevron*, the Court recognized that, where Congress has delegated primary interpretive authority to an agency rather than the courts, Congress intended agencies to be able to change their minds—whether due to changed circumstances, based on trial and error, or in response to political elections. *Chevron*, 467 U.S. at 865–66. In *National Cable & Telecomm. Ass'n v. Brand X Internet Servs.*, 545 U.S. 969 (2005), the Court reemphasized this premise by concluding that, in the face of statutory ambiguity, an agency action carrying the force and effect of law will be entitled to *Chevron* deference even if it directly contradicts an earlier judicial interpretation. *Id.* at 982.

Rejecting regulations duly promulgated through notice-and-comment rulemaking for their recency or their inconsistency with past interpretations would repudiate the central premise of *Chevron*. Rejecting regulations duly promulgated through notice-and-comment rulemaking for their contradiction with past judicial opinions, where the statute is ambiguous, would repudiate *Brand X* as well. No reason has been offered, and none exists, for the Court to treat tax cases differently from those involving other statutes with respect to these factors.

CONCLUSION

Whether or not the Court ultimately affirms or reverses the Eighth Circuit, the Court should clarify (1) that *Chevron* rather than *National Muffler* provides the appropriate standard for reviewing the substantive validity of general authority Treasury regulations like Treas. Reg. § 31.3121(b)(10)-2 and (2) that *National Muffler* factors should play no greater role in *Chevron* step two analysis in tax cases than in nontax cases.

Respectfully submitted,

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October 4, 2010