No. ______

IN THE
Supreme Court of the United States

SIH PARTNERS LLLP, EXPLORER CORPORATION,
TAX MATTERS PARTNER,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Third Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The Third Circuit, in conflict with the D.C., Ninth, and Federal Circuits, deferred to an IRS regulation under step two of *Chevron* even though the agency, in issuing the regulation, did not purport to exercise its expertise and provided no explanation for the rule other than that the agency sought "to conform" its regulation to the statute. The court then held, again in conflict with other circuits, that the IRS, in imposing more than $75,000,000 in tax liability on petitioner, was free to disregard its own published Revenue Ruling on the basis that a Revenue Ruling "is not a regulation and does not bind the IRS."

The questions presented are:

1. Whether the Third Circuit erred in deferring to the IRS regulation under *Chevron*.

2. Whether the Third Circuit erred in holding that the IRS is not bound by its own published Revenue Rulings.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

All parties to the proceeding below are named in the caption.

Pursuant to this Court's Rule 29.6, undersigned counsel state that petitioner SIH Partners LLLP, Explorer Partner Corp., Tax Matters Partner has the following parent companies: Columbus International Holdings, Inc.; Balboa International Holdings, Inc.; LaSalle International Holdings, Inc.; and Explorer Partner Corp. No publicly held company owns 10% or more of its stock.

STATEMENT OF RELATED PROCEEDINGS

- *SIH Partners LLLP, Explorer Partner Corporation, Tax Matters Partner v. Comm'r*, No. 18-1862 (3d Cir.) (opinion issued and judgment entered May 7, 2019; order denying rehearing issued July 3, 2019).
- *SIH Partners LLLP, Explorer Partner Corporation, Tax Matters Partner v. Comm'r*, No. 3427-15 (Tax Ct.) (judgment entered Jan. 18, 2018).

There are no additional proceedings in any court that are directly related to this case.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner SIH Partners LLLP, Explorer Corporation, Tax Matters Partner ("SIH") respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit.

OPINIONS BELOW

The opinion of the Third Circuit (Pet. App. 1a-23a) is reported at 923 F.3d 296. The order of the Third Circuit denying rehearing (Pet. App. 73a-74a) is reported at 930 F.3d 586. The opinion of the United States Tax Court (Pet. App. 24a-72a) is reported at 150 T.C. No. 3.

JURISDICTION

The Third Circuit entered judgment on May 7, 2019, and denied a timely petition for rehearing on July 3, 2019. This Court has jurisdiction under 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The text of 26 U.S.C. §§ 1(h)(11), 316(a), 951, and 956, and 26 C.F.R. §§ 1.956-1, 1.956-2, and 601.601(d)(2) is reproduced at Pet. App. 75a-163a.

STATEMENT

This case involves an IRS regulation that has never been explained and makes no economic sense. The regulation governs the tax treatment of certain loan guarantees. The regulation is fundamentally irrational because it treats every loan *guarantor* as though each were the *lender* of the entire loan—even though, as a matter of basic economics, guaranteeing a loan is completely different from making the loan. When the IRS issued the regulation, it did not draw upon its expertise to implement the relevant statute. Nor did the agency offer a word of explanation for why it thought this approach made sense. The agency simply declared, in a single conclusory sentence, that its regulation was intended "to conform" to the statutory language, even though the statutory language had, in fact, expressly delegated a policy choice to the agency.

The IRS itself has recognized the regulation's irrationality, acknowledging that it can produce "strange results" if applied in a wooden and literal manner. Thus, the agency has sought to mitigate this irrationality through a published Revenue Ruling that requires the IRS to conduct an individualized analysis of the facts and circumstances surrounding the type of loan transactions at issue to ensure they are given appropriate tax treatment. In this case, the IRS refused to engage in the facts-and-circumstances analysis mandated by its Revenue Ruling and instead applied the loan guarantee regulation in a literal and irrational manner.

The Third Circuit affirmed the IRS's resulting determination that SIH was liable for more than $75,000,000 in taxes under its regulation. The court began by deferring to the regulation under step two of

Chevron, excusing the agency's total failure to explain its regulation on the ground that the regulation merely sought to mirror the statutory language. *See* Pet. App. 16a n.5. The court then held that the Revenue Ruling "does not bind the IRS," even though adhering to the Revenue Ruling would have prevented the IRS from imposing this massive tax liability on petitioner. *Id.* at 18a. Both holdings are wrong and directly conflict with decisions of other circuits.

In deferring to the regulation under *Chevron*'s second step, the Third Circuit took an approach that conflicts with the approach followed by the D.C., Ninth, and Federal Circuits. Those courts hold that deference is *not* warranted where, as here, the regulation does not reflect application of agency expertise or is not accompanied by a reasoned explanation. *See Peter Pan Bus Lines, Inc. v. Fed. Motor Carrier Safety Admin.*, 471 F.3d 1350 (D.C. Cir. 2006); *Pub. Citizen, Inc. v. U.S. Dep't of Health & Human Servs.*, 332 F.3d 654 (D.C. Cir. 2003); *BP Energy Co. v. FERC*, 828 F.3d 959 (D.C. Cir. 2016); *Good Fortune Shipping SA v. Comm'r*, 897 F.3d 256 (D.C. Cir. 2018); *Gila River Indian Cmty. v. United States*, 729 F.3d 1139 (9th Cir. 2013); *Dominion Res., Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012). Those courts have correctly concluded that, when an agency has not drawn upon its expertise in interpreting a statute and has not explained the choices it made, the underlying rationale of *Chevron* is inapplicable, and there is no reason to defer to the agency's construction.

Similarly, in holding that the IRS is not bound by its own published Revenue Rulings, the Third Circuit created a conflict with the many other circuits that have held that such rulings bind the agency. For

example, the Fifth Circuit has held that "the Commissioner will be held to his published rulings in areas where the law is unclear, and may not depart from them in individual cases." *Estate of McLendon v. Comm'r*, 135 F.3d 1017, 1024 (5th Cir. 1998). Other circuits have reached the same common-sense result: the IRS cannot ignore the Revenue Rulings it published precisely to enable taxpayers to rely on them in arranging their financial affairs. *See* 26 C.F.R. § 601.601(d)(2)(v)(*e*).

The Third Circuit's decision is seriously flawed and will have broad ramifications. It takes *Chevron* deference to a new and untenable extreme in conflict with decisions from other circuits. And it plunges taxpayers into a state of confusion by abruptly declaring that—at least within the Third Circuit—the IRS is no longer bound by its own published Revenue Rulings. This Court should grant review to bring clarity and uniformity to these important issues.

Review in this case is especially important in light of the IRS's consistent, repeated, and longstanding refusal to "follow[ ] basic rules of administrative law." *CIC Servs., LLC v. IRS*, No. 18-5019, 2019 WL 4051864, at *5 (6th Cir. Aug. 28, 2019) (Thapar, J., dissenting from denial of rehearing en banc); *see also* Kristin E. Hickman & Gerald Kerska, *Restoring the Lost Anti-Injunction Act*, 103 Va. L. Rev. 1683, 1714-15 (2017) ("[L]egal scholars and commentators have complained for decades about Treasury's weak record of compliance with the [Administrative Procedure Act] when it promulgates regulations."). In particular, "IRS preambles to regulations ordinarily do not explain why the IRS decided to adopt the particular rules in the regulations." Patrick J. Smith, *The APA's Arbitrary and Capricious Standard and*

IRS Regulations, 136 Tax Notes 271, 274-75 (2012). For many years, the Internal Revenue Manual openly proclaimed the IRS's view that "[i]t is *not necessary* to justify the rules that are being proposed or adopted or alternatives that were considered." Internal Revenue Manual § 32.1.5.4.7.3(1) (Sept. 30, 2013) (emphasis added). (The Internal Revenue Manual has been revised to cut that sentence—"[b]ut old habits die hard." Hickman & Kerska, *supra*, at 1715 n.187.) Granting review and holding that the IRS is not entitled to deference under *Chevron* when it fails to provide a reasonable explanation for its rules would spur the IRS to correct this misguided and unlawful approach to rulemaking.

A. Legal Background

1. Before 1962, U.S. shareholders of a controlled foreign corporation ("CFC") were not taxed on the CFC's earnings until they were distributed by the CFC to the shareholders. *See* Pet. App. 4a-5a. But in 1962, Congress determined that when a CFC invests its earnings in certain property in the United States, the CFC's U.S. shareholders should be taxed immediately on those earnings. *See* Revenue Act of 1962, Pub. L. No. 87-834, 76 Stat. 1006. Otherwise, U.S. shareholders could cause their CFCs to repatriate income into the United States while avoiding immediate U.S. tax by not declaring a formal dividend. *See* H.R. Rep. No. 87-1447, at 58 (1962) (goal of Section 956 was "to prevent the repatriation of income to the United States in a manner which does not subject it to U.S. taxation").

As an example, suppose that a CFC distributed a formal dividend to its U.S. shareholders, who used the dividend to purchase investment assets in the United States. Then and now, that dividend would be taxable

to the shareholders. But until 1962, if the CFC instead purchased the same U.S. investment assets, the value of that purchase would not have been immediately taxed. To counteract this problem, Congress enacted 26 U.S.C. § 956.

Section 956 specifies certain *types* of domestic investments by a CFC that are treated as deemed repatriations to the United States, triggering accelerated tax on the CFC's U.S. shareholders, just as if the CFC had declared a formal dividend in the amount of the U.S. investment. *See* § 956(c). Under Section 956, whenever a CFC invests in "tangible property located in the United States," "stock of a domestic corporation," or "an obligation of a United States person" (i.e., a loan), its U.S. shareholders must generally include a specified amount of the CFC's previously untaxed earnings in their income. *Id.* Because the CFC is using its earnings for investments in the United States, Congress determined that those earnings should be taxed as if the CFC had formally repatriated its earnings to its U.S. shareholders via a dividend. *See* S. Rep. No. 87-1881 at 88 (1962) (describing a Section 956 investment as "substantially the equivalent of a dividend").

Section 956 also generally specifies the *amount* of the CFC's earnings that a U.S. shareholder must include in its income based on these deemed repatriations. *See* § 956(a). That amount is the CFC's "basis" in the property—that is, the amount the CFC has invested in the property (up to the amount of the CFC's previously untaxed earnings). *Id.*

But Congress did *not* specify how Section 956 would tax loan guarantees made by CFCs. Instead, Congress called upon the IRS to exercise its expert judgment, as demonstrated by Section 956's drafting

history and plain text. The House version of what became Section 956 included pledges and guarantees in the list of CFC transactions that would automatically trigger U.S. tax, the list now contained in Section 956(c). *See* Revenue Act of 1962, H.R. 10650, 87th Cong., § 13(a). But in the enacted version of the statute, Congress moved loan guarantees into a separate subsection of Section 956 and directed that a CFC "shall, *under regulations prescribed by the Secretary*, be considered as holding an obligation of a United States person if such [CFC] is a pledger or guarantor of such obligations." 26 U.S.C. § 956(d) (emphasis added). Thus, Congress expressly delegated to the IRS the authority to determine *when* loan guarantees should be treated as deemed repatriations of earnings into the United States and in what *amount* they should be taxed.

Congress had good reasons for directing the IRS to determine when loan guarantees should be treated as deemed repatriations, rather than creating a bright-line statutory rule. Unlike a loan made by a CFC, a loan *guarantee* by a CFC is not an investment in U.S. property. A lender acquires an *asset*, but a guarantor becomes subject to a contingent *liability*. Unlike a loan, a loan guarantee does not necessarily make additional funds available to a shareholder. And unlike a lender, a loan guarantor has no tax basis in the guarantee that can serve to measure the amount repatriated. Ensuring that taxation of CFC loan guarantees reflects economic reality—the polestar of the tax code—thus requires judgment and expertise.

2. The IRS did not take account of these differences between loans and loan guarantees in promulgating a regulation to implement Section

956(d). Two specific provisions (collectively, the "Guarantee Regulation") are relevant here. The first, 26 C.F.R. § 1.956-2(c)(1), provides that *any* CFC guarantee causes the CFC to hold an "obligation of a United States person." The second, 26 C.F.R. § 1.956-1(e)(2), provides that the amount subject to immediate tax is the *full* principal amount of the underlying loan, not the value of the guarantee. Thus, despite Congress's recognition that guarantees are different from loans, the Guarantee Regulation treats every CFC guarantee as though the CFC were directly lending the entire underlying loan amount to its U.S. shareholder.

The IRS offered no explanation for its economically irrational approach. It merely stated, in a single conclusory sentence, that *all* of its regulations implementing Section 956 were collectively intended to "conform the Income Tax Regulations to section 956 of the Internal Revenue Code." 29 Fed. Reg. 2,599, 2,599 (Feb. 20, 1964) (citation omitted). The IRS did not mention Congress's express delegation of authority to promulgate regulations governing guarantees, much less explain how it had filled the statutory gaps expressly left open by Congress or brought its expertise and judgment to bear in adopting the Guarantee Regulation. *See id.*

In the years since it promulgated the Guarantee Regulation, the IRS has recognized that the Regulation can produce "strange results" if applied literally. IRS Field Service Advice No. 200216022 at 12 (Jan. 8, 2002). When multiple CFCs guarantee the same loan, for example, each and every guarantee results in a deemed repatriation equal to the full amount of the underlying loan. In those cases, "the aggregate amount of United States property treated

as held by CFCs may exceed the unpaid principal amount of the obligation." 80 Fed. Reg. 53,058, 53,061-68 (Sept. 2, 2015). Similarly, the Guarantee Regulation treats all guarantees as effective repatriations of the entire guaranteed loan, even guarantees that do not actually make any additional funds available to a CFC's shareholders or only marginally improve the loan's financial terms for the debtor.

For these reasons, the IRS has historically not applied the Guarantee Regulation literally. As it explained in a published Revenue Ruling concerning CFCs, "[t]he facts and circumstances of each case must be reviewed to determine if, in substance, there has been a repatriation of the earnings of the controlled foreign corporation." Rev. Rul. 89-73, 1989-1 C.B. 258; *see also* 26 C.F.R. § 601.601(d)(2)(v)(*e*) (taxpayers are entitled to "rely upon Revenue Rulings published in the [Internal Revenue] Bulletin in determining the tax treatment of their own transactions").

B. Factual and Procedural Background

1. In 2007, Merrill Lynch issued a $1.485 billion loan to an affiliate of petitioner SIH. Pet. App. 32a-33a. Thirty-nine SIH affiliates, including two CFCs, guaranteed that loan. *Id.* at 33a. At that time, SIH and its non-CFC affiliates had nearly twice the amount of the loan—more than $2.7 billion—in liquid net assets on deposit with Merrill Lynch. CA3 JA 72-74. By contrast, the two CFCs had *combined* net assets of approximately $240 million. *Id.* In 2010 and 2011, those CFCs distributed their earnings through a formal dividend to SIH, which paid taxes at the rate for qualified dividend income under 26 U.S.C. § 1(h)(11).

On subsequent audit, the IRS determined that, because the CFCs were co-guarantors of the Merrill Lynch loan, those same earnings distributed and taxed in 2010 and 2011 should instead have been taxed in 2007 and 2008 at the ordinary income tax rate under the Guarantee Regulation. Pet. App. 27a. SIH petitioned the Tax Court for review, arguing that the CFCs' earnings were not subject to accelerated taxation in 2007 and 2008, but that, if they were, the qualified dividend income rate should apply. *Id.* at 39a, 63a, 67a. The Tax Court granted summary judgment to the IRS. *Id.* at 24a.

2. The Third Circuit affirmed. It first held that the Guarantee Regulation was entitled to deference under *Chevron* step two, explaining that "[a]bsent evidence that the agency failed to follow a clear statutory mandate," the court could not "find that the regulations were arbitrary and capricious." Pet. App. 13a. "Nothing in the record," it asserted, "shows that the agency's interpretation of the scope of the statutes was unreasonable, or that the regulations in question failed to implement an articulable statutory mandate." *Id.* at 14a. After all, the court stated, "it makes logical sense to hold that loan guarantees should be treated the same as a direct loan, a position supported by a straight-forward reading of the Act." *Id.* at 13a. The Third Circuit did not cite any authority for its assertion that it makes "logical sense" to treat a loan guarantee as if it were the underlying loan (something that the IRS generally does *not* do elsewhere in interpreting the tax code). *Id.*

The Third Circuit excused the IRS's failure to provide any explanation for the Guarantee Regulation because the regulation "track[s] the text of § 956(d) nearly verbatim." Pet. App. 16a n.5. "The almost

word-for-word match," it stated, "keeps the IRS's terse explanation in line with the general principle that the more a regulation departs from a statute, the more an agency must explain itself." *Id*. And "[b]ecause the challenged regulations barely rocked the statutory boat, and because of the lack of public commentary and the straight-forward nature of the regulations," it concluded, "little explanation was needed." *Id.*

The Third Circuit rejected SIH's argument that Revenue Ruling 89-73 required the IRS to examine the facts and circumstances surrounding the transaction. Pet. App. 18a. The court excused the IRS from "employ[ing] its own facts-and-circumstances guidance" based on an argument that the IRS itself never advanced. *Id.* "A revenue ruling," the court held, "is simply the opinion of the Service's legal counsel which has not received the approval of the Secretary nor of Congress. A ruling is not a regulation and does not bind the IRS." *Id.* Because the court held the Revenue Ruling nonbinding, it did not reach the question whether the Ruling would have barred or reduced SIH's tax liability in this case.

Finally, the Third Circuit held that the reduced tax rate applicable to qualified dividends did not apply to the deemed repatriations arising from the CFC guarantees. *See* 26 U.S.C. § 1(h)(11) (establishing tax treatment of "qualified dividend income"). Longstanding IRS guidance directs that "[a] distribution by a corporation to a third party *for the benefit* of a shareholder is a constructive dividend." Rev. Rul. 73-605, 1973-2 C.B. 109 (emphasis added). And the Third Circuit acknowledged that guarantees taxed under Section 956(d) are taxed on the theory that they are "given for the benefit of shareholders." Pet. App. 21a. Nonetheless, the court concluded that

investments taxed under Section 956 cannot qualify as statutory constructive dividends because they are not always "distributed . . . *to* any shareholder." *Id.* at 20a (emphasis added).

The Third Circuit denied SIH's timely petition for rehearing. Pet. App. 74a.

REASONS FOR GRANTING THE PETITION

I. THE THIRD CIRCUIT'S APPROACH TO *CHEVRON* DEFERENCE CONFLICTS WITH THE RULE IN OTHER CIRCUITS.

The Third Circuit's decision to defer to the Guarantee Regulation under *Chevron* step two—when the IRS did not purport to interpret Section 956(d) or offer any contemporaneous explanation of the regulation—directly conflicts with decisions of the D.C., Ninth, and Federal Circuits. Those courts hold that *Chevron* step two deference is *not* appropriate where, as here, the agency does not acknowledge the open policy question and does not bring its expertise to bear through a reasoned explanation. Under these circumstances, *Chevron*'s fundamental rationale—that courts properly defer to the expert judgment of agencies interpreting the statute they administer—is not satisfied.

This Court should grant review to resolve the conflict and make clear that *Chevron* step two deference is reserved only for those cases where the agency has actually exercised its expertise and informed policy judgment in interpreting the statute.

A. The Conflicting Approaches To *Chevron* Step Two.

1. By deferring to the IRS regulation, the Third Circuit stretched *Chevron* deference past the point any other court has gone.

In Section 956(d), Congress "explicitly left a gap for the agency to fill," expressly delegating "authority to the [IRS] to elucidate a specific provision of the statute by regulation." *Chevron U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 843-44 (1984). Congress declined to decide how loan guarantees would be taxed and instead provided that a CFC "shall, *under regulations prescribed by the Secretary*, be considered as holding an obligation of a United States person if such [CFC] is a pledger or guarantor of such obligations." 26 U.S.C. § 956(d) (emphasis added). And Congress said nothing about how much of a CFC's earnings should be taxed with respect to guarantees.

Yet when it promulgated its Guarantee Regulation, the IRS failed to recognize the policy choice it was making and did not bring its expertise to bear by *interpreting* the statute. To the contrary, the IRS simply announced, in a single sentence, that *all* of its regulations implementing Section 956 were issued "to conform" the agency's regulations to the statute. 29 Fed. Reg. 2,599, 2,599 (Feb. 20, 1964).[1] And far from "elucidat[ing]" Section 956(d), *Chevron*, 467 U.S. at 844, the IRS adopted a rule that "track[s]

[1] The sentence reads: "In order to conform the Income Tax Regulations (26 CFR Part 1) to section 956 of the Internal Revenue Code of 1954, as added by section 12(a) of the Revenue Act of 1962 (76 Stat. 1006), such regulations are amended to include the following new sections . . . ." 29 Fed. Reg. at 2,599.

the text of § 956(d) nearly verbatim," Pet. App. 16a n.5, and "essentially repeats [the] statutory provision," IRS CA3 Br. 27; *see also id.* at 25 (the Guarantee Regulation "simply mirror[s] the statutory language"). *Compare* 26 U.S.C. § 956(d), *with* 26 C.F.R. § 1.956-2(c).

Where, as here, a statute *expressly* delegates rulemaking authority without specifying a rule, it is impossible for the agency to promulgate regulations that merely "conform" to the statute. By necessity, the agency must make its own policy decision to arrive at its rule. The IRS failed to recognize that the Guarantee Regulation reflects a significant policy choice and failed to provide any explanation for the choice it made.

The Third Circuit nonetheless held that *Chevron* deference was warranted. The court did not suggest that the IRS had exercised policy judgment or brought its expertise to bear in interpreting the statute. Nor did the court question the IRS's failure to explain its regulation. Instead, the court held that the "almost word-for-word match" between the regulation and the statute "keeps the IRS's terse explanation in line with the general principle that the more a regulation departs from a statute, the more an agency must explain itself." Pet. App. 16a n.5.[2]

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[2] Of course, that principle cannot excuse the IRS's complete failure of explanation. *See Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) ("[T]he agency must examine the relevant data and articulate a satisfactory explanation for its action including a rational connection between the facts found and the choice made." (internal quotation marks omitted)).

2. The Third Circuit's approach directly conflicts with the rule followed in the D.C., Ninth, and Federal Circuits. None of those courts would have deferred to the IRS regulation, as they do not give *Chevron* deference to unexplained regulations that merely purport to track the statute and do not reflect the exercise of agency expertise.

The D.C. Circuit holds that *Chevron* step two deference is appropriate *only* when the agency acknowledges the question left open for agency interpretation *and* offers a reasoned explanation for adopting its regulation.

In *Peter Pan Bus Lines, Inc. v. Federal Motor Carrier Safety Administration*, 471 F.3d 1350 (D.C. Cir. 2006), the court held that "*Chevron* step 2 deference is reserved for those instances when an agency recognizes that the Congress's intent is not plain from the statute's face." *Id.* at 1354. The court explained that "[i]n precisely those kinds of cases, it is incumbent upon the agency *not* to rest simply on its parsing of the statutory language—it must bring its experience and expertise to bear in light of competing interests at stake." *Id.* (citation and alteration omitted; emphasis added).

Similarly, in *ITT Industries, Inc. v. NLRB*, 251 F.3d 995 (D.C. Cir. 2001), the court held that *Chevron* deference is unwarranted where the agency fails "to acknowledge that the question" it is called upon to answer is "an open one, *i.e.*, that, in *Chevron* terms," the statute and precedent "are silent on the issue." *Id*. at 1004. Rather, deference is appropriate *only* where the agency "engage[s] in considered analysis and explain[s] its chosen interpretation." *Id.*

The D.C. Circuit has applied this rule in many cases. For example, in *Public Citizen, Inc. v. United*

States Department of Health & Human Services, 332 F.3d 654 (D.C. Cir. 2003), the court held that where an agency "does little more than repeat the statutory language," the court will not defer under *Chevron*, because there is "no interpretation of [the statute] to which we might defer." *Id.* at 661. When an agency provides "no reasoning that [the court] can evaluate for its reasonableness, the high level of deference contemplated in *Chevron*'s second step is simply inapplicable." *Id*.

Likewise, in *BP Energy Co. v. FERC*, 828 F.3d 959 (D.C. Cir. 2016), the court explained that it would not defer to an agency interpretation because the agency "ha[d] not adequately explained why" it made the choice it did. *Id.* at 965. The agency "d[id] not provide an indication of the reasoning behind [its] interpretation," made "no reasonable attempt to grapple with or even refer back to the statutory text," and failed to "identify factors underlying its interpretation that are rationally related to [the statute's] purpose" or "other considerations that it believe[d] counsel[ed] in favor of its interpretation." *Id.* at 965-66 (citations omitted; punctuation altered). Instead, the agency "assume[d]" its interpretation "to be the true meaning of [the statute], and d[id] not even acknowledge that the [agency wa]s engaging in interpretation." *Id.* at 966.

And in *Good Fortune Shipping SA v. Commissioner*, 897 F.3d 256 (D.C. Cir. 2018), the court refused to defer to the IRS's unexplained regulations: "When the IRS promulgated the [regulation], it offered no justification for treating bearer shares differently than nominees and trustees under [the statute]. That's enough to render the

distinction inadequate for purposes of *Chevron* Step Two." *Id.* at 264.

The Ninth Circuit likewise refuses to defer under *Chevron* to an unexplained regulation that does not reflect an agency's considered policy judgment. In *Gila River Indian Community v. United States*, 729 F.3d 1139 (9th Cir. 2013), the court held that the Secretary of Interior's interpretation of the Gila Bend Act was not entitled to deference because "[t]he Secretary's decision reflect[ed] a failure to grapple with the ambiguity" in the statute. *Id.* at 1147. "*Chevron* deference does not apply," the court explained, "where an agency mistakenly determines that its interpretation is mandated by plain meaning, or some other binding rule." *Id.* at 1149 (citing *Negusie v. Holder*, 555 U.S. 511, 518-19 (2009)). And there, the Secretary had erroneously concluded that the statutory text was clear. *See id.*

It made no difference to the Ninth Circuit that the agency also "added that it would reach the same conclusion '[e]ven if Congress's intent was less clear.'" *Gila River*, 729 F.3d at 1150 (alteration in original). That "one-sentence caveat" was "not entitled to *Chevron* deference, because the Secretary did not provide any *explanation* for this decision." *Id.* (emphasis added). "Without an explanation of the agency's reasons," the court emphasized, "it is impossible to know whether the agency employed its expertise or simply pick[ed] a permissible interpretation out of a hat." *Id.* (internal quotation marks omitted; alteration in original). An "'agency must . . . articulate a satisfactory explanation for its action.'" *Id.* (omission in original) (quoting *State Farm*, 463 U.S. at 43). And "deferring to the Secretary's unexplained caveat would permit the

agency to sidestep its duty to bring its expertise to bear on the 'difficult policy choices' it is tasked with making." *Id.* (quoting *Negusie*, 555 U.S. at 523).

The Federal Circuit follows the same approach. In *Dominion Resources, Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012), the court invalidated an IRS regulation implementing a provision of the Tax Code where the IRS failed to "provide a reasoned explanation for adopting [the] regulation." *Id.* at 1319. The court emphasized that the preamble to the IRS's proposed regulation "provided no rationale other than the general statement that the regulations are intended to implement the [statutory] method." *Id.* "Similarly, the IRS provided no rationale in the final regulations." *Id.*[3]

The Third Circuit attempted to distinguish the Federal Circuit's decision in *Dominion Resources* and the D.C. Circuit's decision in *Good Fortune Shipping* on the grounds that the regulation at issue in the former contradicted the statute, and the regulation at issue in the latter departed from the IRS's prior interpretation. *See* Pet. App. 16a n.5. But those purported distinctions make no difference. The IRS may have thought that its Guarantee Regulation "conformed" to Section 956, but it offered no explanation to show that it grappled with the text and

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[3] The Federal Circuit fully articulated this conclusion in applying *State Farm*, having separately held that the regulation was substantively unreasonable at *Chevron* step two. *See Dominion Resources*, 681 F.3d at 1317-19. But it (unsurprisingly) made the same point in applying *Chevron*, explaining that it could "discern[ ] no reasonable explanation" for the regulation. *Id.* at 1318-19; *see also Judulang v. Holder*, 565 U.S. 42, 52 n.7 (2011) (explaining that the Court's analysis under *Chevron* step two "would be the same" as under *State Farm*).

purpose of the statute, which presented a range of potential policy choices that the IRS failed to recognize. That is *precisely* the circumstance in which the D.C., Ninth, and Federal Circuits refuse to defer under *Chevron*.

B. The Third Circuit's Approach Violates Bedrock Principles Of Administrative Law.

1. The fundamental premise underlying *Chevron* deference is that "an agency to which Congress has delegated policy-making responsibilities may, within the limits of that delegation, properly rely upon the incumbent administration's views of wise policy to inform its judgments." *Chevron*, 467 U.S. at 865. "Filling gaps in the Internal Revenue Code plainly requires the Treasury Department to make interpretive choices for statutory implementation at least as complex as the ones other agencies must make in administering their statutes." *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. 44, 56 (2011).

But if the IRS does *not* exercise its expertise and informed judgment in selecting a particular policy, then courts should not defer under *Chevron*. The agency's rule cannot be a "'reasonable *interpretation*' of the enacted text" if the agency does not purport to *interpret* the text at all. *Mayo Found.*, 562 U.S. at 58 (emphasis added). "After all, [courts] defer to an agency's statutory interpretations not only because Congress has delegated law-making authority to the agency, but also because that agency has the expertise to produce a reasoned decision. If an agency fails or refuses to deploy that expertise . . . it deserves no deference." *Vill. of Barrington v. Surface Transp. Bd.*, 636 F.3d 650, 660 (D.C. Cir. 2011) (citations omitted).

The Third Circuit's holding that an unexplained regulation can satisfy *Chevron* step two also conflicts with this Court's decision in *Encino Motorcars, LLC v. Navarro*, 136 S. Ct. 2117 (2016). In that case, the Court emphasized that "[o]ne of the basic procedural requirements of administrative rulemaking is that an agency must give adequate reasons for its decisions." *Id.* at 2125. A regulation that is supported by no reasoned explanation "is itself unlawful and receives no *Chevron* deference." *Id.* at 2126. Indeed, this Court has long refused to defer to regulations when the agency provided no reasoning to explain the policy choice it has made. *See Adamo Wrecking Co. v. United States*, 434 U.S. 275, 287 n.5 (1978) ("Since this Court can only speculate as to his reasons for reaching that conclusion, the mere promulgation of a regulation, without a concomitant exegesis of the statutory authority for doing so, obviously lacks 'power to persuade' as to the existence of such authority.").

For these reasons, the Third Circuit erred in giving *Chevron* deference to an unexplained regulation that did not reflect the application of agency expertise but merely purported to parrot the statute. "When," as in this case, "Congress expressly delegates the authority to fill a gap in a statute, Congress speaks, in effect, directly, and says, succinctly, that it wants the agency to *annotate* its words." *Buongiorno v. Sullivan*, 912 F.2d 504, 509 (D.C. Cir. 1990) (Thomas, J.) (emphasis added).

At a more fundamental level, the Third Circuit seriously misread *Chevron* by holding that "[a]bsent evidence that the agency failed to follow a clear statutory mandate, [a court] cannot find that the regulations were arbitrary and capricious." Pet. App. 13a; *see also id.* at 14a n.4 (rejecting argument that

the Guarantee Regulation was unreasonable because "the plain language of the statutes in question does not impose [a] requirement on the agency"). Courts proceed to step two of the *Chevron* analysis only *after* "determin[ing] that statutory ambiguity has left the agency with a range of possibilities." *Vill. of Barrington*, 636 F.3d at 660. By declaring that it would defer to the IRS's regulations *unless* Congress's contrary mandate was "clear" and expressed in the statute, the Third Circuit rendered step two a nullity. According to the Third Circuit, the very circumstances that move the analysis to step two—statutory ambiguity—also prevent a determination that the agency acted arbitrarily.

2. Under any appropriate *Chevron* analysis, the Third Circuit should not have deferred to the Guarantee Regulation. The regulation is irrational because it treats all CFC guarantors as if they were lenders, regardless of circumstances. But guarantees almost *never* provide the full economic value of the underlying loan. *See Plantation Patterns, Inc. v. Comm'r*, 462 F.2d 712 (5th Cir. 1972) (identifying the narrow circumstances in which a guarantee can be recharacterized as a direct loan). And they obviously do not do so when the loan is collateralized far in excess of its principal amount and guaranteed by *dozens* of well-funded parties. This case illustrates the absurdity of the IRS's approach. The Guarantee Regulation treats each CFC guarantor as making a loan of $1.485 billion, even though the loan had 39 different guarantors, neither CFC had anywhere near that much to lend, and—if each of those guarantors had been a CFC with sufficient earnings—the Regulation would have resulted in an income inclusion of *$58 billion* based on a loan of less than $1.5 billion.

The IRS offered no reasoning for taking the approach it did. The agency was obligated at a minimum to explain why it chose to subject the full amount of the underlying loan to accelerated tax. *See* 26 C.F.R. § 1.956-1(e)(2). That choice cannot be explained as simply parroting or "conforming" to the statute, since guarantees do not have an "adjusted basis," and the statute does not otherwise specify the amount subject to immediate tax. 26 U.S.C. § 956(a).

The Third Circuit endorsed what it considered a "straight-forward determination that the amount to be included in the domestic shareholder's income should equal the amount of the loan the CFC guaranteed up to the amount of the CFC's earnings" on the theory that "it makes logical sense to hold that loan guarantees should be treated the same as a direct loan." Pet. App. 13a. But treating guarantees the same as loans does *not* make logical (or economic) sense, and that is precisely why Congress moved guarantees into a separate subsection of the statute and tasked the IRS with determining how they should be treated. And by deferring to the Guarantee Regulation based on a rationale that the IRS failed to offer during the rulemaking process (and that defies economic reality), the panel undermined the bedrock administrative law principle that a court cannot consider, much less proffer, post hoc explanations for agency action. *See SEC v. Chenery Corp.*, 332 U.S. 194, 196 (1947).[4]

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[4] The Third Circuit initially declared that SIH improperly relied on "hindsight" in contending that the Guarantee Regulation was substantively and procedurally invalid. Pet. App. 9a-11a. But the court later acknowledged SIH's argument "that even at the time they were promulgated the regulations were arbitrary and capricious because the IRS failed to exercise

This Court should grant review to correct the Third Circuit's fundamental errors in applying *Chevron* and to clarify the appropriate standards under *Chevron*'s second step. Doing so in this case is especially important to correct the IRS's longstanding refusal to comply with the fundamental administrative law requirements of reasoned decisionmaking, including "the IRS's general practice of not explaining the reasons for its rules." Patrick J. Smith, *The APA's Arbitrary and Capricious Standard and IRS Regulations*, 136 Tax Notes 271, 274 (2012).

To be sure, this Court may decide that *Chevron*'s regime is unsalvageable and that it is the province and duty of courts, not agencies, to say what the law is in the face of statutory ambiguities. *See*, *e.g.*, *Kisor v. Wilkie*, 139 S. Ct. 2400, 2425 (2019) (Roberts, C.J., concurring) ("Issues surrounding judicial deference to agency interpretations of their own regulations are distinct from those raised in connection with judicial deference to agency interpretations of statutes enacted by Congress. I do not regard the Court's decision today to touch upon the latter question." (citation omitted)); *id.* at 2448-49 (Kavanaugh, J., joined by Alito, J., concurring in the judgment) (agreeing with the Chief Justice); *Michigan v. EPA*, 135 S. Ct. 2699, 2713 (2015) (Thomas, J., concurring) ("These cases bring into bold relief the scope of the

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its expertise." *Id.* at 12a. "Hindsight"—in this case, decades of IRS practice refusing to apply the Guarantee Regulation as written because it leads to absurd results—merely "*confirms* the unreasonableness of its regulations." SIH CA3 Br. 32-37 (emphasis added); *see*, *e.g.*, IRS Field Service Advice No. 200216022, at 12 (Jan. 8, 2002) (recognizing that the literal application of the Guarantee Regulation "could produce strange results").

potentially unconstitutional delegations we have come to countenance in the name of *Chevron* deference."); *Gutierrez-Brizuela v. Lynch*, 834 F.3d 1142, 1149 (10th Cir. 2016) (Gorsuch, J., concurring) ("But the fact is *Chevron* and *Brand X* permit executive bureaucracies to swallow huge amounts of core judicial and legislative power and concentrate federal power in a way that seems more than a little difficult to square with the Constitution of the framers' design."). But it is only this Court that may take that step.

II. THE THIRD CIRCUIT'S HOLDING THAT PUBLISHED REVENUE RULINGS DO NOT BIND THE IRS CONFLICTS WITH DECISIONS OF OTHER CIRCUITS.

A Revenue Ruling is an "official interpretation by the Service" of the tax law. 26 C.F.R. § 601.601(d)(2)(i)(*a*). Thus, in navigating the complex tax code, taxpayers are entitled to "rely upon Revenue Rulings published in the [Internal Revenue] Bulletin in determining the tax treatment of their own transactions." § 601.601(d)(2)(v)(*e*). The IRS has explained that although published Revenue Rulings "do not have the force and effect of Treasury Department Regulations," they "are published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose." § 601.601(d)(2)(v)(*d*). This differentiates published Revenue Rulings from "unpublished ruling[s]" and other informal, taxpayer-specific guidance, which may not "be relied on, used, or cited, by any officer or employee of the [IRS] as a precedent in the disposition of other cases." § 601.601(d)(1).

Although this Court has not yet decided whether *courts* are bound by published Revenue Rulings, *see*

United States v. Cleveland Indians Baseball Co., 532 U.S. 200, 220 (2001), every court of appeals to consider the question before this case had held that the *IRS* is bound by them. The Third Circuit's contrary holding squarely conflicts with decisions of other federal courts of appeals. Certiorari is warranted to resolve this clear and indisputable conflict on an issue of immense importance to taxpayers—whether they can conduct their business and plan their affairs in reliance on the IRS adhering to its Revenue Rulings when assessing taxes.

A. The Third Circuit Stands Alone In Holding That The IRS May Disregard Its Published Revenue Rulings.

1. The leading case holding that Revenue Rulings bind the IRS is the Fifth Circuit's opinion in *Estate of McLendon v. Commissioner*, 135 F.3d 1017 (5th Cir. 1998). The court noted significant uncertainty about whether *courts* must defer to Revenue Rulings, but determined that it could avoid that question: "Most questions of deference to a revenue ruling involve an argument by the taxpayer that a particular ruling is contrary to law. Here, however, the argument to ignore or minimize the effect of [the revenue ruling] comes from the Commissioner, the very party who issued the ruling in the first place." *Id.* at 1024.

That argument was flatly inconsistent with binding Fifth Circuit precedent, under which "the Commissioner will be held to his published rulings in areas where the law is unclear, and may not depart from them in individual cases." *McLendon*, 135 F.3d at 1024. Furthermore, "the Commissioner may not retroactively abrogate a ruling in an unclear area with respect to any taxpayer who has relied on it." *Id.*; *see*

also Silco, Inc. v. United States, 779 F.2d 282, 286 (5th Cir. 1986) ("[T]axpayers may generally rely on published revenue rulings in determining the tax treatment of their own transactions.").

Applying those principles, the Fifth Circuit ruled for the taxpayer: "The Commissioner ignored the clear language of his own ruling in declaring deficiencies, and it is precisely this kind of tactic that *Silco* declares to be intolerable." *McLendon*, 135 F.3d at 1025. Because the Tax Court erred in disregarding a published Revenue Ruling upon which the taxpayer "was entitled to rely," the Fifth Circuit reversed and rendered judgment for the taxpayer. *Id.*

Many other circuits agree with the Fifth Circuit that published Revenue Rulings bind the IRS.

The Sixth Circuit, in *The Limited, Inc. v. Commissioner*, 286 F.3d 324 (6th Cir. 2002), explained that Revenue Rulings "are one of four ways that the IRS can publicly memorialize its interpretations of the Tax Code." *Id.* at 337. "The other three methods are regulations issued pursuant to a specific congressional directive; regulations issued under the IRS's general authority to interpret tax laws; and private letter rulings." *Id.* "Revenue rulings do not apply as broadly as regulations, nor as narrowly as private letter rulings." *Id.* In particular, the Sixth Circuit held, "revenue rulings are typically the IRS's response to a hypothetical situation and as such are *authoritative and binding on the IRS*." *Id.* (emphasis added).

The D.C. Circuit has similarly held that "Revenue Rulings bind both the Service and the taxpayer." *Stichting Pensioenfonds Voor de Gezondheid, Geestelijke en Maatschappelijke Belangen v. United States*, 129 F.3d 195, 198 (D.C. Cir. 1997). Revenue

Rulings, the court explained, are "the second most important agency pronouncements that interpret the Code." *Id.* "Although Revenue Rulings 'do not have the force and effect of Treasury Department Regulations,' they are 'published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose.'" *Id.* at 198-99 (quoting 26 C.F.R. § 601.601(d)(2)(v)(*d*) (1997)). To be sure, the D.C. Circuit ultimately rejected the taxpayer's argument, concluding that none of the Revenue Rulings issued under the relevant Code provision constituted "controlling authority" because none was "substantially the same" as that case. *Id.* at 199. But that inquiry would have been unnecessary had the D.C. Circuit agreed with the Third Circuit that Revenue Rulings are simply a form of "internal guidance directions" that "are not binding on [the] agency." Pet. App. 18a. Indeed, the D.C. Circuit summarily dismissed the taxpayer's attempt to rely on "General Counsel Memoranda" for precisely that reason—informal, unpublished "'GCMs,'" unlike published Revenue Rulings, "have no precedential value." *Stichting Pensioenfonds*, 129 F.3d at 200.

The Ninth Circuit has also held that Revenue Rulings bind the IRS. In *Estate of Rapp v. Commissioner*, 140 F.3d 1211 (9th Cir. 1998), the executor of an estate relied on a published Revenue Ruling, arguing that it was "binding on the IRS Commissioner." *Id.* at 1216. The Ninth Circuit agreed, explaining that "revenue rulings are not binding as to the taxpayer, but may limit the IRS' ability to assert a position that is contrary to that asserted in the ruling if the ruling is published, to the extent that the ruling addresses a similar issue." *Id.* at 1217. Far from dismissing published Revenue

Rulings, as the Third Circuit did, the Ninth Circuit carefully examined the cited Ruling and determined that it was inapposite. *See id.* at 1217-18.[5]

Unsurprisingly, in light of this previously unbroken line of authority, the Tax Court treats Revenue Rulings as "concessions by the Commissioner," who may not abandon "the principles and public guidance articulated in the Commissioner's currently outstanding revenue rulings." *Rauenhorst v. Comm'r*, 119 T.C. 157, 171 (2002); *see also id.* ("[W]e cannot agree that the Commissioner is not bound to follow his revenue rulings."); *Cascade Designs, Inc. v. Comm'r*, 79 T.C.M. (CCH) 1542 (T.C. 2000) ("Previously, in similar situations, we have treated respondent's position in a revenue ruling as a concession of the issue.") (collecting cases); *Dobson v. Comm'r*, 320 U.S. 489, 502 (1943) ("While [the Tax Court's] decisions may not be binding precedents for courts dealing with similar problems, uniform administration would be promoted by conforming to them where possible.").

And a leading treatise explains that "revenue rulings are published so that taxpayers can rely on them in determining the tax treatment of their own

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[5] The Tenth Circuit emphasized the taxpayer's right to rely on published Revenue Rulings in *Shellito v. Commissioner*, 437 F. App'x 665 (10th Cir. 2011). There, the court of appeals held the IRS to its longstanding position, reflected in published Revenue Rulings, on the deductibility of certain business expenses. "While revenue rulings are not binding on either the Tax Court or this court," the Tenth Circuit explained, courts "are entitled to give them consideration and the public generally has the right to rely on positions taken by the Commissioner in revenue rulings." *Id.* at 670 n.7 (internal quotation marks omitted).

transactions and need not request specific rulings applying the principles of a published revenue ruling to the facts of their particular cases." Boris I. Bittker et al., *Federal Income Taxation of Individuals*, ¶ 46.05[4] (3d ed. 2019) (internal quotation marks omitted). To enable taxpayers to rely on published Revenue Rulings, they "are binding on IRS officials until revoked." *Id.*

2. The Third Circuit disagreed with all of these circuits and authorities in holding that Revenue Rulings "are not binding" on the IRS. Pet. App. 18a. The court mischaracterized Revenue Rulings as "simply the opinion[s] of the Service's legal counsel," *id.*, not "official interpretation[s] by the Service" itself, 26 C.F.R. § 601.601(d)(2)(i)(*a*). The court also cited *Schweiker v. Hansen*, 450 U.S. 785 (1981), for the general proposition that "internal guidance directions are not binding on an agency and do not have the force of law." Pet. App. 18a. But that case held only that a Social Security Administration employee's errors, including his "minor breach" of the SSA's "13-volume handbook for internal use," did not "estop the Government from insisting upon compliance with valid regulations governing the distribution of welfare benefits." *Schweiker*, 450 U.S. at 788-90. This Court did not suggest that an agency could disregard guidance that the agency publishes precisely so that the public can "rely upon" the agency's decision. 26 C.F.R. § 601.601(d)(2)(v)(*e*).

To the contrary, this Court has repeatedly upheld "the principle that agencies should provide regulated parties fair warning of the conduct [a regulation] prohibits or requires." *Christopher v. SmithKline Beecham Corp.*, 567 U.S. 142, 156 (2012) (internal quotation marks omitted); *see also Kisor*, 139 S. Ct. at

2417-18 ("[A] court may not defer to a new interpretation . . . that creates 'unfair surprise' to regulated parties."); *NLRB v. Bell Aerospace Co.*, 416 U.S. 267, 295 (1974) (suggesting that an agency should not change an interpretation in an adjudicative proceeding where doing so would impose "new liability . . . on individuals for past actions which were taken in good-faith reliance on [agency] pronouncements").

B. The Question Is Important And Recurring.

The consequences of the Third Circuit's holding are alarming. Revenue Rulings provide essential guidance for taxpayers. If courts do not enforce the Commissioner's "duty of consistency between his rulings and litigation position[s]," *Derby v. Comm'r*, 95 T.C.M. (CCH) 1177 (T.C. 2008), and instead allow the Commissioner to retroactively depart from published rulings, taxpayers cannot conduct their business and plan their affairs with confidence that the Commissioner will treat like cases alike.

As a result of the Third Circuit's holding, taxpayers in Delaware, New Jersey, and Pennsylvania cannot "rely upon Revenue Rulings . . . in determining the tax treatment of their own transactions"—unlike taxpayers in every other state. 26 C.F.R. § 601.601(d)(2)(v)(*e*); *see also Burnet v. Harmel*, 287 U.S. 103, 110 (1932) (federal tax laws are "to be interpreted so as to give a uniform application to a nation-wide scheme of taxation"). And in cases appealable to the Third Circuit, the Tax Court may no longer treat the IRS's "position in a revenue ruling as a concession of the issue," *Cascade Designs, Inc.*, 79 T.C.M. (CCH) 1542, although it will continue to do so in cases appealable to other circuits. *See Golsen v.*

Comm'r, 54 T.C. 742, 757 (1970) (holding that the Tax Court must "follow a Court of Appeals decision which is squarely [o]n point where appeal from [its] decision lies to that Court of Appeals and to that court alone").

This case illustrates the significance of Revenue Rulings. *First*, had the IRS adhered to Revenue Ruling 89-73 as petitioner had insisted it must, the $75,000,000 tax liability could not have been imposed. The facts and circumstances of this case show that there was no repatriation in substance. *See* Rev. Rul. 89-73, 1989-1 C.B. 258 ("The facts and circumstances of *each* case must be reviewed to determine if, in substance, there has been a repatriation of the earnings of the controlled foreign corporation.") (emphasis added). SIH and its non-CFC affiliates had assets on deposit with Merrill Lynch that were almost double the entire amount of the loan. *See* CA3 JA 66-67. The CFC guarantees did not enable SIH's affiliate to borrow a greater amount than it otherwise could have borrowed. *See id.* Rather, they provided Merrill Lynch with (unnecessary) assurance that SIH and its U.S. affiliates could not avoid their obligations by transferring assets to the CFCs. Had the IRS applied its facts-and-circumstances test, it would have concluded that there was a minimal repatriation in substance, if any, through the CFC guarantees.[6]

[6] The IRS did not suggest below that it is not bound by published Revenue Rulings. Nor did the IRS contend that the CFC guarantees in this case amounted to a repatriation in substance in the amounts taxed. Instead, the IRS argued that Revenue Ruling 89-73 does not demand a facts-and-circumstances test and applies only when the IRS attempts "to recharacterize the form of a transaction based on its true substance." IRS Br. 40. Those arguments are incorrect. *See* SIH CA3 Reply 17-19. But the Third Circuit did not reach them,

Second, the Third Circuit's confused discussion of whether the qualified dividend rate applies to Section 956(d) inclusions is flatly inconsistent with the IRS's definition of constructive dividends in its own Revenue Rulings, as well as with the Code itself and relevant precedent. The court reasoned that CFC guarantees taxed under Section 956(d) cannot qualify as statutory constructive dividends because they are not always "distributed . . . *to* any shareholder." Pet. App. 20a (emphasis added). But the IRS has explained that "[a] distribution by a corporation to a third party *for the benefit* of a shareholder is a constructive dividend." Rev. Rul. 73-605, 1973-2 C.B. 109 (emphasis added). If CFC guarantees are properly taxed at all, it is only because they confer a benefit on U.S. taxpayers, and thus, per the IRS's own Revenue Ruling, they should be treated as constructive dividends taxable at the qualified dividend rate. *See* 26 U.S.C. § 1(h)(11); S. Rep. No. 87-1881 at 88 (1962) (explaining that, under Section 956, "earnings brought back to the United States are taxed to the shareholders on the grounds that this is substantially the equivalent of a dividend being paid to them"). This conclusion is reinforced by the statutory definition of "dividend," 26 U.S.C. § 316(a), and by caselaw holding that the constructive-dividend doctrine governs situations where a corporation confers valuable benefits *on* a shareholder without distributing property directly *to* the shareholder. *See*, *e.g.*, *Hagaman v. Comm'r*, 958 F.2d 684, 690-91 (6th Cir. 1992).

Because the Third Circuit's dismissive treatment of Revenue Rulings creates a conflict with other

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having dismissed the Revenue Ruling as mere internal guidance that does not bind the IRS.

circuits, upends well-settled Tax Court practice, finds no support in this Court's precedent, and would allow the Commissioner to depart from the IRS's own published rulings without explanation, this Court should grant certiorari.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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