No. 19-435

In the Supreme Court of the United States

SIH PARTNERS LLLP, EXPLORER CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

Before 1962, a U.S. shareholder of a controlled foreign corporation (CFC) could defer taxation on the CFC's earnings until the earnings were distributed to the shareholder. In 1962, Congress enacted Subpart F of the Internal Revenue Code, 26 U.S.C. 951 *et seq.*, to eliminate that deferral where the U.S. shareholder uses the CFC's earnings directly or indirectly. Under Subpart F, if a CFC loans money to a U.S. person, then the U.S. shareholder must include the amount of that obligation in taxable income (up to the earnings of the CFC). See 26 U.S.C. 956(a) (2006); 26 U.S.C. 956(c) (2006 & Supp. II 2008). In addition, if the CFC guarantees a loan to a U.S. person, the CFC "shall, under regulations prescribed by the Secretary, be considered as holding [the] obligation." 26 U.S.C. 956(d) (2006).

In 1964, the U.S. Department of the Treasury promulgated regulations that address the treatment of CFC guarantees by establishing a general rule and an exception for conduit financing arrangements. Under the general rule, CFC guarantors of a loan to U.S. persons are treated as holding the obligation, and their U.S. shareholders must include the amount of the loan in their taxable income (up to the earnings of the CFC). 26 C.F.R. 1.956-1(e)(2), 1.956-2(c)(1) (2008). The questions presented are as follows:

1. Whether the court of appeals correctly held that the Treasury regulations that address CFC guarantees are valid.

2. Whether, if the regulations are valid, the court of appeals nonetheless should have remanded the case for application of a facts-and-circumstances test.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-23a) is reported at 923 F.3d 296. The opinion of the Tax Court (Pet. App. 26a-72a) is reported at 150 T.C. No. 3.

JURISDICTION

The judgment of the court of appeals was entered on May 7, 2019. A petition for rehearing was denied on July 3, 2019 (Pet. App. 73a-74a). The petition for a writ of certiorari was filed on September 30, 2019. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. The United States taxes the income of its citizens and residents on a worldwide basis, subjecting the income from domestic and foreign activities to the same tax burden, while providing a foreign tax credit to alleviate double taxation. 26 U.S.C. 61(a); 26 U.S.C. 901-908

(2006 & Supp. II 2008).[1] When calculating its income for U.S. tax purposes, a U.S. partnership (like petitioner) must include income earned abroad. To some extent, however, U.S. taxpayers can limit taxation on their foreign income by separately incorporating their foreign operations.

Before 1962, the earnings of foreign corporations that were controlled by U.S. taxpayers (controlled foreign corporations, or CFCs) escaped U.S. taxation until those earnings were distributed to the U.S. taxpayer, even though the U.S. taxpayer would be subject to full U.S. taxation on foreign income it earned directly. See S. Rep. No. 1881, 87th Cong., 2d Sess. 78 (1962) (1962 Senate Report). "[T]axpayers attempting to avoid domestic taxes though nevertheless seeking to benefit from foreign earnings of their CFC hit upon the idea of taking loans either from the CFC or from third-party financial institutions using the CFC's assets as collateral or having the CFC guarantee the loans." Pet. App. 4a-5a. This permitted U.S. shareholders "effectively to obtain a monetary return on their foreign investment" while deferring U.S. taxation on foreign income. *Id.* at 5a.

In 1962, Congress sought to limit this practice and other adverse consequences stemming from tax deferral with respect to earnings of U.S.-controlled companies. See 1962 Senate Report 78-79; H.R. Rep. No. 1447, 87th Cong., 2d Sess. 57 (1962) (1962 House Report). Congress enacted Subpart F of the Internal Revenue Code, 26 U.S.C. 951 *et seq.*, which restricts tax deferral on

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[1] The Tax Cuts and Jobs Act, Pub. L. No. 115-97, Tit. I, 131 Stat. 2054, made certain changes to the U.S. system of taxation. Because those changes were not in effect for the years at issue in this case (2007 and 2008), they are not relevant here. Unless otherwise noted, this brief cites to the 2006 version of the United States Code.

foreign income for U.S. shareholders of a CFC. See 26 U.S.C. 951(b) (defining "United States shareholder"); 26 U.S.C. 957(a) (defining CFC).

As relevant here, under Section 951(a)(1)(B), U.S. shareholders must include in their income the earnings of their CFCs that are directly or indirectly invested in "United States property." 26 U.S.C. 956(c) (2006 & Supp. II 2008); see 26 U.S.C. 951(a)(1)(B). "In general terms," Section 956(c)(1) defines U.S. property as "all tangible and intangible property located in the United States," S. Rep. No. 938, 94th Cong., 2d Sess. 225 (1976) (1976 Senate Report); see 26 U.S.C. 956(c)(1); 26 U.S.C. 956(c)(2) (2006 & Supp. II 2008) (providing limited "[e]xceptions" from the definition of U.S. property). As relevant here, Section 956(c)(1)(C) specifically includes as U.S. property "an obligation of a United States person"—*e.g.*, a loan. 26 U.S.C. 956(c)(1)(C). Thus, if a CFC makes a loan to its U.S. affiliate, that loan is considered U.S. property held by the CFC, the amount of which is includable in the shareholder's income to the extent of the CFC's untaxed earnings. Such loans (like other income invested in U.S. property) are "deemed to be distributed to the U.S. shareholders" and thus repatriated for U.S. tax purposes. 1976 Senate Report 224. That rule is based on "the belief that the use of untaxed earnings of a [CFC] to invest in U.S. property [i]s 'substantially the equivalent of a dividend' being paid to the U.S. shareholders." *Id.* at 225. The relevant Internal Revenue Code provisions do not contemplate any case-specific inquiry into the reasons for the CFC's U.S. investments, or whether (or to what extent) the U.S. shareholder benefits from the investment. See 26 U.S.C. 951, 956 (2006 & Supp. II 2008).

The rule for CFCs' investments in U.S. loans could easily be avoided if a CFC could guarantee a third

party's loan to a U.S. person without triggering taxation under Section 951(a)(1)(B). For example, instead of borrowing $1000 directly from the CFC, a U.S. affiliate of the CFC could induce an outside lender to extend a loan in that amount by directing its CFC to guarantee the loan, thus indirectly using the CFC's untaxed earnings without having the CFC loan it the funds directly. Section 956(d) eliminates that potential for abuse. It provides that, if a CFC pledges or guarantees an obligation of a U.S. person, the CFC "shall, under regulations prescribed by the Secretary, be considered as holding [the] obligation." 26 U.S.C. 956(d). Thus, if a CFC loans money to its U.S. affiliate, or guarantees a loan by another party to its U.S. affiliate, the CFC has invested in U.S. property, and its U.S. shareholders must include in income certain amounts of the CFC's earnings.[2]

The amount to be included in the U.S. shareholder's income is the shareholder's pro rata share of "the lesser of" (i) the average amount (on a quarterly basis) of U.S. property held by the CFC during the taxable year or (ii) the CFC's applicable earnings (as defined in Section 956(b)(1)). 26 U.S.C. 956(a). The amount of U.S. property to be taken into account is the property's "adjusted basis." *Ibid.* Ordinarily, a lender takes a basis in a loan equal to the unpaid principal. Pet. App. 52a.

b. In 1963, the U.S. Department of the Treasury proposed regulations to implement newly enacted Section 956. 28 Fed. Reg. 3541 (Apr. 11, 1963); C.A. App. 417-505. With respect to the treatment of CFC guarantees, Treasury proposed a "General rule" that mirrored the

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[2] Earnings taxed to U.S. shareholders under Section 951 are not taxed a second time when later distributed by the CFC to the U.S. shareholder as dividends. 26 U.S.C. 959.

language of Section 956(d), providing that "any obligation * * * of a United States person * * * with respect to which a [CFC] is a pledgor or guarantor shall be considered for purposes of section 956(a) [and the related regulatory provision] to be United States property held by such [CFC]." C.A. App. 490 (Prop. Treas. Reg. § 1.956-2(c)(1), 28 Fed. Reg. at 3550) (emphasis omitted). Treasury also proposed an exception to that general rule for "certain conduit financing arrangements." *Id.* at 491 (Prop. Treas. Reg. § 1.956-2(c)(2), 28 Fed. Reg. at 3550) (emphasis omitted).

With regard to the amount of the CFC's U.S. investment due to loans or loan guarantees, the proposed regulations similarly mirrored the statutory language. For loans, the amount was the CFC's "adjusted basis" in the loan—that is, the unpaid principal amount of the loan. C.A. App. 479 (Prop. Treas. Reg. § 1.956-1(e)(1), 28 Fed. Reg. at 3549); see Pet. App. 52a. For guarantees, the amount was the "unpaid principal amount * * * of the obligation with respect to which the [CFC] is a pledgor or guarantor." C.A. App. 480 (Prop. Treas. Reg. § 1.956-1(e)(2), 28 Fed. Reg. at 3549).

Treasury received several comments in response to the proposed regulations, and held a public hearing in June 1963. C.A. App. 384-385. None of the comments raised concerns about the rules relating to loan guarantees. Pet. App. 42a; C.A. App. 319-383. Only one commenter made a suggestion regarding guarantees: the American Bar Association suggested that the exception for conduit financing arrangements in Proposed Treasury Regulation § 1.956-2(c)(2) should be broadened. Pet. App. 42a; C.A. App. 337-338.

In 1964, "[a]fter consideration of all such relevant matter as was presented" during the comment period,

Treasury promulgated final regulations. C.A. App. 388; see T.D. 6704, 1964-1 C.B. 284. The guarantee regulations were adopted substantially unchanged from the proposed regulations, and they are currently codified at 26 C.F.R. 1.956-1(e)(2) and 1.956-2(c)(1). The exception for conduit financing arrangements was broadened, and it is now codified at 26 C.F.R. 1.956-2(c)(4). See Pet. App. 42a-43a. The preamble to the final regulations emphasized that the regulations were designed to conform Treasury's income-tax regulations to newly enacted Section 956. C.A. App. 387; see Pet. App. 42a.

In the subsequent half-century, Congress has not questioned Treasury's construction of Section 956(d), although it has enacted multiple amendments to Section 956. See Pet. App. 59a-60a (listing statutory amendments). Treasury has amended its Subpart F regulations numerous times but has left in place its clear, categorical rules regarding guarantees. *E.g.*, 73 Fed. Reg. 38,113 (July 3, 2008); 67 Fed. Reg. 48,020 (July 23, 2002); 53 Fed. Reg. 22,163 (June 14, 1988); 45 Fed. Reg. 52,373 (Aug. 7, 1980). Until this suit, the regulations had not been challenged. Pet. App. 7a, 66a-67a.

2. During the tax years at issue (2007-2008), petitioner was a Delaware partnership owned indirectly by five individual taxpayers. Pet. App. 29a-30a. Petitioner, in turn, owned 100% of the stock of two CFCs. *Id.* at 7a. Petitioner also had a number of U.S. affiliates. *Ibid.* In 2007, one of petitioner's U.S. affiliates borrowed $1.5 billion from Merrill Lynch (the Loan). *Ibid.* The Loan was guaranteed by, among others, petitioner's two CFCs. *Ibid.*

In 2011, the CFCs distributed earnings to petitioner. Pet. App. 7a. At that time, the Commissioner of the Internal Revenue Service (IRS) determined that petitioner

had income inclusions under Sections 951(a)(1)(B) and 956(d) for 2007-2008 because its CFCs had invested in U.S. property by guaranteeing the Loan. *Ibid.* The CFCs' applicable earnings during 2007-2008 were far less than the $1.5 billion Loan. *Ibid.* Accordingly, the total amount included in petitioner's income was approximately $380 million. *Id.* at 8a; see 26 U.S.C. 956(a)(2). The Commissioner further determined that the income inclusions under Sections 951(a)(1)(B) and 956(d) did not qualify for the lower "qualified dividend" tax rate under 26 U.S.C. 1(h)(11)(B)(i), but were instead taxable as ordinary income. Pet. App. 8a.

3. The Tax Court granted summary judgment to the Commissioner and denied petitioner's motion for summary judgment. Pet. App. 26a-72a.

The Tax Court held that petitioner must include in income the CFCs' applicable earnings for 2007-2008. As noted above, under 26 C.F.R. 1.956-1(e)(2) and 1.956-2(c)(1) (2008), if a CFC guarantees an obligation of a U.S. person, it is considered to hold that obligation, and a U.S. shareholder must include in its income the CFC's previously untaxed applicable earnings to the extent that they are less than the unpaid principal. Applying that rule to the stipulated record, the court upheld the Commissioner's income inclusions because (i) petitioner's CFCs had guaranteed an obligation (the Loan) of a U.S. person, and (ii) the CFCs' applicable earnings were approximately $380 million for 2007-2008. Pet. App. 38a-39a, 67a.

The Tax Court rejected petitioner's argument that the regulations were invalid under the Administrative Procedure Act (APA), 5 U.S.C. 706(2)(A), because Treasury had failed to engage in "reasoned decisionmaking." Pet. App. 49a; see *Motor Vehicle Mfrs. Ass'n of the U.S.,*

Inc. v. *State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). The Tax Court explained that Treasury's rationale for the regulations could "'reasonably be discerned'": Treasury had sought to "adhere[] to the text of the statute" by "equat[ing] the treatment" of guarantees with the treatment of loans. Pet. App. 52a (citation omitted); see *id.* at 51a-52a.

The Tax Court further held that Treasury's regulations reflect a reasonable interpretation of the statute that is entitled to deference under *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). Pet. App. 55a-63a. The court observed that neither party had argued that "Congress ha[d] spoken directly" to the question "when and in what amount a CFC will be considered to hold United States property under section 956 as a result of its guaranty of an obligation of a United States person." *Id.* at 57a. The court accordingly proceeded to "step two of *Chevron*," where it determined that the regulations were "'based on a permissible construction of the statute.'" *Ibid.* (citation omitted).

Petitioner contended that the regulations reflect "an unreasonable policy choice" because "Congress 'was only concerned in section 956 with investments in U.S. property that repatriate earnings,'" while a CFC's guarantee of an obligation is "not 'necessarily'" such a transaction, but instead must be considered based on the particular "'facts and circumstances.'" Pet. App. 58a. In rejecting that argument, the Tax Court explained that "nothing in the statute or its legislative history suggests that Congress expected Treasury to craft ad hoc exceptions based on some sort of facts-and-circumstances test." *Id.* at 59a. The court also found it significant that the regulations had been in effect for nearly 50 years,

during which time Congress had made other revisions to Section 956 while reenacting Section 956(d) without change. *Id.* at 62a-63a (quoting *Smiley* v. *Citibank (S.D.), N.A.*, 517 U.S. 735, 740 (1996)) (brackets in original). The court viewed that history as "strongly suggest[ing] that [Congress] did not view Treasury's construction of section 956(d) as unreasonable or contrary to the law's purpose." *Id.* at 63a; see *id.* at 59a-63a.

Petitioner relied in part on affidavits from its officers that purported to demonstrate the reasons for, and value of, the guarantees. The Tax Court held that such evidence was legally irrelevant. Pet. App. 63a-67a. The court observed that if, as petitioner contended, the guarantee was unnecessary for the receipt of the Loan, then "the solution" was to have not made the guarantee, which would have permitted petitioner to "avoid[]" the "application and effects of the regulations." *Id.* at 66a. In that regard, the court noted petitioner's "acknowledg[ment that] the rules promulgated for pledges and guarantees lend themselves to easy tax planning." *Id.* at 67a.

4. The court of appeals affirmed. Pet. App. 1a-23a.

The court of appeals rejected petitioner's arguments that the guarantee regulations are arbitrary and capricious, that Treasury had failed to provide an adequate explanation for them, and that the rules reflect an unreasonable interpretation of the statute. Pet. App. 10a-19a. Each of those arguments rested on petitioner's assertion that, at the time the regulations were promulgated, the agency had "failed to exercise its expertise to recognize" two issues: (1) "the possibility that if the IRS considers individually multiple CFCs that guaranteed the entire loan, the CFC shareholder may incur in-

come larger than the loan"; and (2) the potential existence of guarantees that are not necessary to the receipt of a loan, which on petitioner's view, should not "be regarded as a repatriation." *Id.* at 10a, 12a.

The court of appeals first rejected petitioner's argument that the regulations were arbitrary and capricious. Pet. App. 13a. The court explained that Section 956(d) does not provide "substantive mandates" for either fact-specific issue raised by petitioner, and that there was "no showing that Congress even recognized these issues." *Ibid.* With respect to the possibility of multiple guarantees, the court observed (1) that "when the agency solicited public comments about the regulations" in 1963, "it did not receive any comment about the possibility of multiple-counting of loan guarantors," *id.* at 14a; (2) that petitioner had not "provide[d] evidence suggesting" that the issue was anything other than "hypothetical" at that time, *id.* at 15a; and (3) that the agency had represented at oral argument that it still was "unaware of a single instance where the inclusion of income under § 956(c)(1)(C) has resulted in the domestic shareholder receiving income greater than the loan amount," *ibid.*

The court of appeals further held that Treasury had provided an "adequate explanation" for the regulations. Pet. App. 16a n.5; see *id.* at 10a. The court explained that, although Treasury's explanation for the rule was "terse," "little explanation was needed" because the regulations were "straight-forward" and "track the text of § 956(d)," and because Treasury had received no "public commentary" regarding the proposed guarantee provisions. *Id.* at 16a n.5; see *id.* at 11a-13a. For these reasons, the court found this case distinguishable from two cases in which the D.C. and Federal Circuits had held

that the IRS had provided inadequate explanations for other rules. *Id.* at 16a n.5 (citing *Good Fortune Shipping SA* v. *Commissioner*, 897 F.3d 256, 262 (D.C. Cir. 2018), and *Dominion Res., Inc.* v. *United States*, 681 F.3d 1313, 1317-1319 (Fed. Cir. 2012)).

The court of appeals also rejected petitioner's argument that Section 956(d) required the agency to take a different regulatory approach. Examining the regulations' general rule, which treats loan guarantees in the same way as direct loans, the court determined that Treasury's interpretation was "supported by a straightforward reading of the Act." Pet. App. 13a. The court agreed with the Tax Court that the plain text of Section 956(d) permits categorical rules and does not "inquire into the relative importance that a creditor attaches to a guaranty" or the "guarantor's financial strength." *Id.* at 17a (citation omitted). The court of appeals also rejected petitioner's contention that Treasury should have limited the regulations to what petitioner termed "obligations that amount to a repatriation in substance," holding that petitioner's approach conflicted with "the plain language of the statutes in question." *Id.* at 14a n.4.

Finally, the court of appeals rejected petitioner's argument that, even if the regulations were valid, the court should remand the matter to the IRS to make a "facts-and-circumstances" determination with respect to their application to this case. Pet. App. 17a; see *id.* at 17a-19a. Petitioner relied on Revenue Ruling 89-73, 1989-1 C.B. 258, Pet. App. 17a, in which the IRS had invoked the substance-over-form doctrine to re-characterize a CFC's loan transaction. The court agreed with the Tax Court that petitioner's contentions regarding the factual circumstances of this case were "irrelevant in determining under the regulations whether the guaranty

gives rise to an investment in United States property." *Ibid.* (citation omitted). In any event, the court of appeals stated, the revenue ruling was "not binding on [the] agency" and did "not have the force of law." *Id.* at 18a.[3]

ARGUMENT

Petitioner contends (Pet. i) that (1) the court of appeals should not have deferred to the guarantee regulations under *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984), and (2) the Commissioner should have relied on a facts-and-circumstances test based on Revenue Ruling 89-73. Those arguments lack merit. The court of appeals correctly held that the half-century-old regulations promulgated under Section 956(d) are neither arbitrary, capricious, nor inconsistent with the statute, and that those rules required petitioner to include in its income the earnings of its CFCs due to their guarantees of a loan to a U.S. affiliate. The revenue ruling on which petitioner relies concerns loan transactions rather than guarantees, addresses only situations in which a transaction's substance does not match its form, and expressly states that it creates no rights for taxpayers. The court of appeals therefore appropriately declined to rely on it. The court's decision does not conflict with any decision of this Court or another court of appeals. Further review is not warranted.

1. The court of appeals correctly held that Treasury's guarantee regulations are neither arbitrary, ca-

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[3] The court of appeals also affirmed the Tax Court's determination that petitioner's income inclusions attributable to the CFCs' guarantees were properly taxed as ordinary income rather than at the lower rate applicable to "qualified dividend income" under 26 U.S.C. 1(h)(11). Pet. App. 19a-23a; see *id.* at 67a-71a.

pricious, nor inconsistent with Section 956(d). That decision does not conflict with any decision of this Court or of another court of appeals.

a. i. Section 956(d) provides in relevant part 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 * * * guarantor of such obligations." 26 U.S.C. 956(d). Consistent with Section 956's plain language, the regulation establishes a general rule and a limited exception. The general rule states that "any obligation * * * of a United States person * * * with respect to which a [CFC] is a pledgor or guarantor shall be considered for purposes of section 956(a) and paragraph (a) of this section to be United States property held by such [CFC]." 26 C.F.R. 1.956-2(c)(1) (2008). The exception—which petitioner does not suggest applies here—excludes from the general rule "certain conduit financing arrangements," "depend[ing] upon all the facts and circumstances in each case." 26 C.F.R. 1.956-2(c)(4) (2008). Treasury's inclusion of that exception in the 1964 rule reflects the agency's understanding that the phrase "under regulations prescribed by the Secretary" in 26 U.S.C. 956(d) authorized Treasury to identify situations in which a CFC's guarantee of a loan to a U.S. person will *not* give rise to taxable income.

Nothing in the statute required the agency to adopt petitioner's proposed approach, under which the tax consequences of a CFC's loan guarantee would depend on whether one or multiple guarantees is involved, or on whether a particular guarantee is necessary to procure a loan. Pet. App. 13a; see *id.* at 10a. Section 956(d) contains no qualifiers as to when a guarantor should be treated as holding an obligation. Although Section 956(d) authorizes Treasury to issue regulatory exceptions, and

Treasury has done so for certain conduit financing arrangements, the statute does not require any particular exception (or any exception at all) to Section 956(d)'s general rule.

Treasury's decision to adopt a largely categorical rule, subject only to the conduit financing exception, comports with the statutory history and purpose. Section 956 was enacted as an anti-abuse measure. See pp. 2-4, *supra*; 1962 House Report 58. It describes U.S. investments in broad, categorical terms to ensure that U.S. shareholders may not "use the earnings of controlled foreign corporations without payment of tax." 1976 Senate Report 226; see *ibid.* (If a CFC's earnings are used—whether directly or indirectly—to support a U.S. investment, they are treated as "an effective repatriation * * * which should be taxed."). By similarly defining U.S. investments broadly to include all CFC guarantees other than those fitting within the exception for conduit financing, Treasury's Section 956(d) regulations serve Congress's anti-abuse purpose by "prevent[ing]" the tax-free use of CFC earnings to guarantee loans to U.S. shareholders. 1962 House Report 58.

ii. The petition for a writ of certiorari focuses on whether the court of appeals correctly applied the principles announced in *Chevron* concerning deference to agency interpretations of ambiguous statutory language.[4] The Court has held that "[t]he principles underlying * * * *Chevron* * * * apply with full force in the tax context." *Mayo Found. for Med. Educ. & Res.* v. *United*

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[4] In a single paragraph, petitioner suggests (Pet. 23-24) that this Court may determine that "*Chevron*'s regime is unsalvageable." Petitioner does not ask this Court to overrule *Chevron*, however, nor does it suggest that *Chevron* applies in weakened form in tax cases. See *ibid.*

States, 562 U.S. 44, 55 (2011). In this case, however, the court of appeals devoted only a single paragraph of its opinion to a recitation of *Chevron* principles. See Pet. App. 13a-14a. The court correctly understood the primary issue to be whether Treasury had acted arbitrarily and capriciously in exercising its acknowledged discretionary authority to promulgate regulatory exceptions, either by failing to adopt an additional regulatory exception for situations involving multiple guarantees of the same loan, or by failing adequately to explain its decision not to adopt such an exception.

In rejecting that challenge, the court of appeals observed that, "when the agency solicited public comments about the regulations when it was considering their adoption, it did not receive any comment about the possibility of multiple-counting of loan guarantors being an issue with the regulations." Pet. App. 14a. The court stated that it "cannot and will not find half-century old regulations arbitrary and capricious, based on insights gained in the decades after their promulgation, when the challenger * * * has not made a showing that those insights were known or, perhaps, at least should have been known to the agency at the time of the regulations' promulgation." *Id.* at 11a. The court further observed that, to the extent petitioner argued that Treasury had irrationally "failed to amend or promulgate new regulations to conform to later observed economic realities," its challenge failed because petitioner "ha[d] not shown that it requested the IRS to amend its regulations." *Id.* at 11a n.3. The court's analysis and rejection of petitioner's APA challenge are consistent with established administrative-law principles and do not implicate the proper application of *Chevron*.

Even if the Third Circuit had agreed with petitioner that *Chevron* principles are inapplicable in this case, and that the court should interpret the relevant statutory language de novo, there is no reason to suppose that the court would have reached a different outcome. Petitioner contends that Treasury should have accorded different treatment to loans for which a CFC is one of multiple guarantors, and to loans in which the CFC's guarantee appears to be unnecessary to the loan's procurement, than to CFC-guaranteed loans generally. See Pet. App. 10a. That argument is premised, not on statutory language that even arguably draws such a distinction, but on petitioner's view that Treasury's contrary approach is economically irrational and inadequately explained. The court of appeals properly treated that challenge as a contention that the regulation is arbitrary and capricious; analyzed that argument at length; and persuasively explained why the challenge failed.

iii. Petitioner's contrary arguments lack merit.

Petitioner contends (Pet. 12, 19-24) that the court of appeals should not have upheld the guarantee regulation because the agency neither "purport[ed] to interpret Section 956(d)" nor "offer[ed] any contemporaneous explanation of the regulation." Pet. 12. That contention—which also underlies petitioner's claim of a circuit split, see pp. 20-23, *infra*—is mistaken.

Treasury established a general rule that tracks the language of Section 956(d), see 26 C.F.R. 1.956-2(c)(1) (2008), and an exception for conduit financing arrangements, see 26 C.F.R. 1.956-2(c)(4) (2008). Section 956(c) likewise establishes categorical rules and limited exceptions for loans to U.S. persons and other types of investments in U.S. property. Treasury's decision to craft a regulatory exception for guarantees provided in conduit

financing arrangements—an exception that is not found in or compelled by Section 956(d)—makes clear that the agency both recognized and exercised its discretionary authority under that provision.

Treasury explained at the time its regulations were promulgated that the rules were written to "conform" to the statutory text. C.A. App. 387 (29 Fed. Reg. 2599, 2599 (Feb. 20, 1964)). Although the court of appeals acknowledged that the agency's explanation was "terse," it found that explanation "adequate" and "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. Here, the regulations track the statute, and the IRS had received no comments questioning or expressing concern with the guarantee rules. See *id.* at 14a. The court of appeals' determination that the agency's explanation was adequate comports with this Court's recognition that an agency's "explanation is clear enough" if its "'path may reasonably be discerned.'" *Encino Motorcars, LLC* v. *Navarro*, 136 S. Ct. 2117, 2125 (2016) (citation omitted).

Petitioner next contends (Pet. 21) that the "regulation is irrational because it treats all CFC guarantors as if they were lenders," while (on petitioner's view) "guarantees almost *never* provide the full economic value of the underlying loan." Section 956, however, does not contemplate any inquiry into the purpose of the CFC's investment in U.S. property or its value to the U.S. shareholder. Rather, if the CFC directly or indirectly holds any U.S. property as defined in Section 956(c), then its U.S. shareholders must include the amount determined by Section 956(a). The statute therefore makes it irrelevant whether the CFC's earnings provide

any value to the U.S. shareholder or are actually repatriated. Thus, if a CFC loans money to a U.S. person, Section 956(c) applies during the life of the loan even if the U.S. person fully repays the loan, and without regard to whether the U.S. shareholder benefits from the loan.

In light of this statutory scheme, it was at least reasonable for Treasury to adopt regulations that treat guarantees as the statute treats loans—*i.e.*, without inquiring into the circumstances of a particular transaction. By adopting rules that largely mirror the categorical statutory language, Treasury both avoided the potential for abuse through loan guarantees and provided clear and predictable rules that allow for "easy tax planning." Pet. App. 67a. It certainly did not act irrationally in declining to create a special rule to address the specific issues that petitioner raises regarding unnecessary guarantees or guarantees by multiple CFCs, particularly given the failure of any commenter to raise similar issues at the time Treasury acted. See *id.* at 13a.

Petitioner further suggests (Pet. 7, 22) that, because Congress included guarantees in Section 956(d), but included loans as "property" in Section 956(c), Congress "directed" Treasury to treat guarantees differently. In particular, petitioner observes (Pet. 7) that a prior version of the bill that became Section 956(d) would have included in income earnings that U.S. shareholders' CFCs invested in all "nonqualified property," including loan guarantees. H.R. 10650, 87th Cong., 2d Sess. §§ 951, 953 (as introduced Mar. 12, 1962). But the fact that the bill was revised to identify particular categories of "United States property" in Section 956(c), 26 U.S.C. 956(c)(1), and to address guarantees in Section 956(d), does not suggest that Congress intended to preclude

Treasury from promulgating bright-line rules with respect to loan guarantees. To the contrary, Treasury itself suggested the revised language that Congress ultimately enacted, and the agency stated that the revisions pertaining to pledges, guarantees, and other investments in U.S. property were merely "technical changes." Senate Comm. on Finance, 87th Cong., 2d Sess., *Draft of Statutory Language, with Accompanying Explanation, of Amendments Proposed by the Secretary of the Treasury on May 10, 1962, to Sections 13, 15, 16, and 20 of H.R. 10650*, at 2 (Comm. Print 1962).

As the Tax Court recognized, Pet. App. 59a-60a, subsequent amendments to Section 956 further undermine petitioner's contention that the guarantee regulations violate congressional intent. Congress has repeatedly amended Section 956, but it has never disturbed Section 956(d) or the guarantee regulations. *Ibid.*; cf. *Cottage Sav. Ass'n* v. *Commissioner*, 499 U.S. 554, 561 (1991) (deferring to a Treasury regulation and observing that "'Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law'") (citations omitted); see also *Barnhart* v. *Walton*, 535 U.S. 212, 220 (2002) (according weight to agency's interpretation where "Congress has frequently amended or reenacted the relevant provisions without change").[5]

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[5] The ultimate issue in this case is whether the Commissioner correctly determined a deficiency in petitioner's tax reporting. In the court of appeals, the Commissioner argued that, even if the regulations were invalid, the statutory language of Section 956(d) is nevertheless operative and supports the income inclusions here. See Gov't C.A. Br. 49-53. Although the court did not reach this issue, it presents an additional basis for denying further review.

b. Neither this Court nor any other court of appeals has addressed Treasury's guarantee regulations under Section 956(d). Petitioner does not allege (Pet. 13-19) any division of authority regarding the validity of the regulations at issue here.

Instead, petitioner claims (Pet. 13-19) that the decision below conflicts with decisions of other courts of appeals regarding *other* regulations. Petitioner relies in part (Pet. 15-18) on decisions declining to afford deference when an agency mistakenly believed that its interpretation was required by the statute. In *Peter Pan Bus Lines, Inc.* v. *Federal Motor Carrier Safety Administration*, 471 F.3d 1350 (D.C. Cir. 2006), the agency had stated that the "plain language" of the statute "compelled" a particular result, and "d[id] not permit" the agency to hold otherwise. *Id.* at 1353-1354 (citations and emphases omitted). Similarly, in *Gila River Indian Community* v. *United States*, 729 F.3d 1139 (9th Cir. 2013), the agency "mistakenly determine[d] that its interpretation [wa]s mandated" by the "plain meaning" of the statute. *Id.* at 1149 (citing *Negusie* v. *Holder*, 555 U.S. 511, 521 (2009)) (refusing to apply *Chevron* deference where agency mistakenly deemed its interpretation "mandated" by a decision of this Court).

Here, the agency made no such statement. Although Treasury stated in 1964 that its regulations "conform[ed]" to the statute, it did not suggest that Section 956(d) precluded it from adopting a regulatory exception of the sort that petitioner now advocates. C.A. App. 387. To the contrary, Treasury's promulgation of a *different* regulatory exemption manifests the agency's evident understanding that Section 956 does not mandate a categorical rule. Treasury's failure in 1964 to discuss the particular exception that petitioner advocates simply

reflects the fact that no commenter suggested such an exception. See Pet. App. 14a. The D.C. and Ninth Circuits have declined to apply *Peter Pan Bus Lines* and *Gila River*, respectively, to cases that more closely resemble the facts at issue here. See *Perez-Guzman* v. *Lynch*, 835 F.3d 1066, 1079 n.8 (9th Cir. 2016) (distinguishing *Gila River* where nothing in the "administrative history * * * suggest[s] the agency saw [the statute] as compelling the regulation's particular approach" and the agency exercised "its expertise by crafting" a regulatory scheme that was consistent with, but not mandated by, the statute), cert. denied, 138 S. Ct. 737 (2018); *Association of Private Sector Colls. & Univs.* v. *Duncan*, 681 F.3d 427, 445 (D.C. Cir. 2012) (rejecting reliance on *Peter Pan Bus Lines* because the agency's "use of the word 'clear'" did not demonstrate "that the agency meant to suggest that its regulatory interpretation was 'compelled by Congress'") (quoting *Peter Pan Bus Lines*, 471 F.3d at 1354).

Petitioner's reliance (Pet. 15) on *ITT Industries, Inc.* v. *NLRB*, 251 F.3d 995 (D.C. Cir. 2001), is similarly misplaced. There, the court faulted the agency for having "failed even to acknowledge that the question" at issue "was an open one." *Id.* at 1004. But here, Treasury acknowledged its authority to promulgate regulatory exceptions to Section 956(d)'s coverage by proposing and adopting both a general rule and an exception for certain conduit financing arrangements. And in 2015, after the tax years at issue here, Treasury solicited public comments on the question whether to "limit the aggregate inclusions to the unpaid principal amount of the obligation" where multiple CFCs guarantee a single U.S. loan. 80 Fed. Reg. 53,058, 53,062 (Sept. 2, 2015). Treasury ultimately declined to adopt this approach.

See 81 Fed. Reg. 76,497, 76,503 (Nov. 3, 2016); cf. Pet. App. 15a (explaining that this problem appears to be "hypothetical," and does not apply in this case). But Treasury's discussion of the issue confirms the agency's understanding of its own authority under the statute.

Petitioner also cites (Pet. 16, 18-19) decisions of the D.C. and Federal Circuits that declined to apply *Chevron* deference based on the agency's inadequate explanation of its interpretation of a statutory term. But while those cases reached different *results* than the Third Circuit reached here, that disparity simply reflects the distinct facts at issue in each case. For example, in *Good Fortune Shipping SA* v. *Commissioner*, 897 F.3d 256 (2018), the D.C. Circuit determined that the agency had provided an insufficient explanation for a rule that "appear[ed] to rewrite" the statute, came "'close to violating'" its "'plain language,'" and "abandoned" the agency's prior interpretation. *Id.* at 263-264 (citation omitted). Similarly in *Dominion Resources, Inc.* v. *United States*, 681 F.3d 1313 (2012), the Federal Circuit determined that Treasury had insufficiently explained a regulation that the court believed "directly contradict[ed]" the specific rule "that Congress intended the statute to implement." *Id.* at 1317. Because none of those factors is present in this case, *Good Fortune Shipping* and *Dominion Resources* do not support petitioner's argument. See Pet. App. 16a n.5; see also *BP Energy Co.* v. *FERC*, 828 F.3d 959, 965 (D.C. Cir. 2016) (remanding to the agency for further explanation of order that made "no 'reasonable attempt to grapple' with or even refer back to the statutory text'") (quoting

Council for Urological Interests v. *Burwell*, 790 F.3d 212, 223 (D.C. Cir. 2015)).[6]

2. Petitioner also challenges (Pet. 24-33) the court of appeals' determination that the IRS was not bound by Revenue Ruling 89-73 in this case. That issue likewise does not warrant this Court's review.

a. After upholding the regulations, the court of appeals rejected petitioner's argument that the IRS nonetheless was required to apply a "facts-and-circumstances" analysis under Revenue Ruling 89-73. Pet. App. 16a-17a. Petitioner sought such an analysis because, in its view, "the CFC guarantees were not essential to its domestic parent entity's ability to obtain the loans," and thus "should not have been deemed as investments in United States properties" and "included in its income." *Id.* at 17a. In rejecting that argument, the court affirmed (and quoted extensively from) the decision of the Tax Court, which had stated that "[n]either section 956(d) nor the regulations inquire into the relative importance that a creditor attaches to a guaranty," and

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[6] *Public Citizen, Inc.* v. *U.S. Department of Health & Human Services*, 332 F.3d 654 (D.C. Cir. 2003), is even further afield. See Pet. 15-16. There, the court of appeals determined that an agency manual was not entitled to *Chevron* deference because "there [wa]s nothing to distinguish [it]" from manuals that this Court had "twice cited * * * as an archetype of the kind of document that is not entitled to such deference." *Public Citizen, Inc.*, 332 F.3d at 660 (citing *United States* v. *Mead Corp.*, 533 U.S. 218, 234 (2001), and *Christensen* v. *Harris Cnty.*, 529 U.S. 576, 587 (2000)). The court then explained in dicta that, "even if [it] were prepared to accord *Chevron* deference" to the manual at issue, the manual contained "no interpretation" of the relevant statute "to which [the court] might defer." *Id.* at 661. This case, by contrast, involves a published regulation issued pursuant to notice-and-comment procedures, and petitioner's core argument is that Treasury acted arbitrarily and capriciously in its exercise of discretionary authority.

that the regulations instead "provide categorically that any obligation of a United States person with respect to which the CFC is a guarantor shall be considered United States property held by the CFC." *Ibid.* (citation omitted). In these circumstances, the court of appeals stated, the revenue ruling was "not bind[ing on] the IRS" and did not "have the force of law." *Id.* at 18a (citations omitted).[7]

Petitioner contends that the court of appeals' determination was incorrect because a revenue ruling is an "'official interpretation by the [IRS]'" on which taxpayers are "entitled" to rely. Pet. 24 (quoting 26 C.F.R. 601.601(d)(2)(i)(a) (2008), and citing 26 C.F.R. 601.601(d)(2)(v)(e) (2008)). Those principles, however, do not support petitioner's position in this case. Petitioner relies on Revenue Ruling 89-73, in which the IRS invoked the substance-over-form doctrine to recharacterize a CFC's loan transaction. Rev. Rul. 89-73, 1989-1 C.B. at 258-259. Regardless of the "binding" nature of revenue rulings more generally, Revenue Ruling 89-73 does not apply here for at least three reasons.

First, Revenue Ruling 89-73 addressed a loan, not a guarantee. Rev. Rul. 89-73, 1989-1 C.B. at 258. By its own terms, it therefore is inapplicable to this case. See 26 C.F.R. 601.601(d)(2)(v)(e) (2008) (cautioning that, because "each Revenue Ruling represents the conclusion of the [IRS] as to the application of the law to the entire state of facts involved, taxpayers, [IRS] personnel, and others concerned are cautioned against reaching the

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[7] As petitioner notes (Pet. 31 n.6), the Commissioner did not argue below that revenue rulings generally do not bind the IRS. Instead, it argued (as it does in this Court, see pp. 24-26, *infra*), that Revenue Ruling 89-73 is inapposite in this case. See Gov't C.A. Br. 38-41.

same conclusion in other cases unless the facts and circumstances are substantially the same").

Second, Revenue Ruling 89-73 addressed a situation in which a transaction's form was inconsistent with its substance. The revenue ruling re-characterized the formal transaction (multiple back-to-back loans that were excepted from Section 956's scope) according to its economic substance (*i.e.*, as a single loan covered by Section 956). Rev. Rul. 89-73, 1989-1 C.B. at 258-259. Here, by contrast, petitioner does not dispute that the CFCs' guarantees are guarantees in both form and substance.[8] Rather, petitioner contends (Pet. 31) that those guarantees should not have the tax consequences that Congress and Treasury assigned to them—*i.e.*, income inclusion—because they did not (in petitioner's view) amount to a "repatriation in substance." But as the statute and regulation make clear, that is not the legal test. See pp. 13-19, *supra*. Instead, the only relevant inquiry is whether the CFCs were "guarantors" of the Loan; because petitioners do not dispute that they were, the statute and regulation require income inclusion. See Gov't C.A. Br. 38-41.

Third, Revenue Ruling 89-73 itself states that only the Commissioner, and not the taxpayer, may disregard a transaction's form and the tax consequences that flow therefrom. See Gov't C.A. Br. 38-41; Rev. Rul. 89-73, 1989-1 C.B. at 259 ("These holdings do not provide a taxpayer the right to compel the [IRS] to disregard the

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[8] That the private lender might have been willing to extend the Loan even without the CFCs' guarantees (Pet. 31) does not convert the guarantees into something else. A mortgage is no less a mortgage merely because the homebuyer possessed sufficient resources to pay the purchase price in cash.

form of its transactions for Federal income tax purposes."); see also *Commissioner* v. *National Alfalfa Dehydrating & Milling Co.*, 417 U.S. 134, 149 (1974) ("This Court has observed repeatedly that, while a taxpayer is free to organize his affairs as he chooses, nevertheless, once having done so, he must accept the tax consequences of his choice, whether contemplated or not."). Thus, it is not clear what it would mean for the IRS to be "bound" by Revenue Ruling 89-73 here, insofar as it would not give petitioner the right to demand application of a facts-and-circumstances test in place of the bright-line rule imposed by the regulations.

b. Petitioner urges (Pet. 25-30) this Court to grant a writ of certiorari on the theory that the courts of appeals disagree as to whether revenue rulings bind the IRS. Once again, the decisions on which petitioner relies are distinguishable, and further review is not warranted.

Petitioner's "lead[]" authority (Pet. 25) is the Fifth Circuit's decision in *Estate of McLendon* v. *Commissioner*, 135 F.3d 1017 (1998). But the court there stated that "the Commissioner will be held to his published rulings in areas *where the law is unclear*." *Id.* at 1024 (emphasis added). The guarantee regulations—which have been in place for more than 50 years—establish a clear rule treating guarantees as includable in income, subject to an exception (for conduit financing arrangements) that is inapplicable here. See Pet. App. 13a, 50a-51a. That the regulations have provided clear guidance for more than half a century is confirmed by the nearly complete absence of litigation over their meaning. *Id.* at 66a-67a. The binding effect of revenue rulings when the law is "unclear" (Pet. 25) therefore is irrelevant.

Estate of McLendon is further distinguishable because the revenue ruling at issue there was "unambiguous in its support for the [taxpayer's] position," while the Commissioner's position appeared to be "inconsistent with the ruling's clear language." 135 F.3d at 1024 n.13. Here, by contrast, petitioner seeks to avoid the tax consequences that flow from CFC guarantees by compelling the IRS to disregard both the form and substance of the relevant transaction. Revenue Ruling 89-73 does "not provide a taxpayer the right to compel the [IRS] to disregard the form of its transactions for Federal income tax purposes." Rev. Rul. 89-73, 1989-1 C.B. at 259.

Petitioner also cites (Pet. 26-28) decisions of the Sixth, Ninth, and D.C. Circuits. But in each of those cases, the court of appeals *declined* to rely on the revenue ruling at issue, on the ground that it addressed materially different facts. See *The Limited, Inc.* v. *Commissioner*, 286 F.3d 324, 338 (6th Cir. 2002) (declining to rely on a revenue ruling because such rulings "often provide the IRS's interpretation of a hypothetical set of facts," and should "not [be] extend[ed] * * * beyond the hypothetical situation presented"); *Estate of Rapp* v. *Commissioner*, 140 F.3d 1211, 1216-1218 (9th Cir. 1998) (declining to rely on revenue ruling because, while such rulings "may limit the IRS' ability to assert a position that is contrary to that asserted in the ruling," the circumstances in the relevant ruling were not "factually similar to the instant case"); *Stichting Pensioenfonds Voor de Gezondheid, Geestelijke en Maatschappelijke Belangen* v. *United States*, 129 F.3d 195, 199 (D.C. Cir. 1997) (declining to rely on a revenue ruling because the taxpayer could "prevail only by identifying a Revenue Ruling awarding an exemption in a case having facts

and circumstances 'substantially the same'" as the case before it), cert. denied, 525 U.S. 811 (1998). None of those decisions supports petitioner's position, because Revenue Ruling 89-73 applies to loans, not guarantees; addresses the specific circumstance of multiple back-to-back loans, which is not at issue here; concerns a transaction in which the form differs from the substance (whereas here, the transaction is in both form and substance a loan guarantee); and specifically precludes taxpayers from invoking the ruling as a ground for demanding that the IRS re-characterize their transactions. See pp. 24-26, *supra*.

c. Even if some tension existed among the circuits regarding the binding effect of revenue rulings, this case would be a poor vehicle to consider that question. As already discussed, even if the court of appeals had considered Revenue Ruling 89-73 "binding," that ruling would support the Commissioner and not petitioner. And while petitioner suggests (Pet. 30) that the Commissioner has attempted to "depart from published rulings," that is simply not the case. Petitioner cites no agency guidance—precedential or non-precedential—in which the Commissioner disregarded a CFC guarantee, or deemed it to be less than the outstanding loan amount, based on the guarantee's value or lack thereof.

Petitioner asserts that review is necessary because "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.'" Pet. 30 (quoting *Cascade Designs, Inc.* v. *Commissioner*, 79 T.C.M. (CCH) 1542, 1553 (2000)). But as just discussed, the revenue ruling at issue here does not address guarantees, does not consider situations in which a transaction's form matches its substance, and creates no rights in taxpayers;

it therefore was not "a concession of the issue," *ibid.* (citation omitted), in this case. At a minimum, review of the Third Circuit's decision is premature, because it is not yet clear how that court (or the Tax Court) will apply the decision to circumstances in which a prior revenue ruling actually addresses the question presented in new litigation and supports the taxpayer's position.[9]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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[9] Petitioner briefly questions (Pet. 32) the court of appeals' determination that Section 1(h)(11)'s preferential tax rate for qualified dividends does not apply to income inclusions under Sections 951 and 956. That issue is not expressly encompassed in the questions presented (Pet. i) or "fairly included therein," Sup. Ct. R. 14(1)(a). In any event, the court of appeals' determination that the general income tax rate applies is correct and consistent with the decision of the only other court of appeals to have addressed this issue. Pet. App. 21a-23a; see *Rodriguez* v. *Commissioner*, 722 F.3d 306, 309 (5th Cir. 2013) (holding that Section 951(a)(1)(B) inclusions "do not constitute qualified dividend income" because they "involve no distribution or change in ownership").