No. 19-1009

IN THE

Supreme Court of the United States

ALTERA CORPORATION ET AL.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF *AMICI CURIAE* NATIONAL ASSOCIATION OF MANUFACTURERS, SEMICONDUCTOR INDUSTRY ASSOCIATION, SOFTWARE FINANCE AND TAX EXECUTIVES COUNCIL, UNITED STATES COUNCIL FOR INTERNATIONAL BUSINESS, NATIONAL FOREIGN TRADE COUNCIL, SOFTWARE AND INFORMATION INDUSTRY ASSOCIATION, FINANCIAL EXECUTIVES INTERNATIONAL, SILICON VALLEY LEADERSHIP GROUP, SILICON VALLEY TAX DIRECTORS GROUP, COMPUTING TECHNOLOGY INDUSTRY ASSOCIATION, THE TAX COUNCIL, TECHNOLOGY NETWORK, INC, AND INFORMATION TECHNOLOGY INDUSTRY COUNCIL IN SUPPORT OF PETITIONERS

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March 6, 2020

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INTEREST OF *AMICI CURIAE*[1]

Amici are trade associations and industry membership organizations representing a broad spectrum of industry interests that are affected by the decision of the Ninth Circuit below.

1. The National Association of Manufacturers is the largest manufacturing association in the United States, representing small and large manufacturers in every industrial sector and in all 50 states. Manufacturing employs over 12 million men and women, contributes roughly $2.1 trillion to the U.S. economy annually, has the largest economic impact of any major sector, and accounts for two-thirds of the private-sector research and development.

2. The Semiconductor Industry Association is the voice of the U.S. semiconductor industry, one of America's top export industries and a key driver of America's economic strength, national security, and global competitiveness. Semiconductors are the microchips that control all modern electronics and the semiconductor industry directly employs nearly a quarter of a million people in the United States.

3. The Software Finance and Tax Executives Council (SoFTEC) is the voice of the software industry on matters of state, federal, and

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[1] Both parties have consented to the filing of this brief by amici curiae. No party or counsel for a party authored this brief in whole or in part or made a monetary contribution intended to fund the preparation or submission of this brief. No person other than amici curiae, their members, or their counsel made a monetary contribution intended to fund the preparation or submission of this brief.

international tax policy. SoFTEC submitted comments in connection with the notice of proposed rulemaking at issue here. SoFTEC also appeared and presented evidence at the agency's hearing on the proposed regulations.

4. The United States Council for International Business (USCIB) advances the global interests of American business. It does so through advocacy that calls for an open system of world trade, finance and investment, where business can flourish and contribute to economic growth, human welfare and sustainable development. USCIB's advocacy spans a broad range of policy issues, leveraging the expertise of our business members.

5. The National Foreign Trade Council (NFTC), founded in 1914, is the oldest business association dedicated to international tax, trade, and human resource matters. The NFTC represents more than 250 U.S. company members and encourages policies to eliminate major tax inequities in the treatment of U.S. companies abroad.

6. The Software & Information Industry Association (SIIA) is the principal trade association for the software and digital information industries. The 700-plus software companies, data and analytics firms, information service companies, and digital publishers that constitute its membership serve nearly every segment of society, including business, education, government, healthcare, and consumers. Many of SIIA's members have operations and affiliates abroad and are subject to taxation in multiple countries.

7. Financial Executives International represents the interests of more than 10,000 chief financial

officers and other senior financial executives from over 8,000 major companies in the U.S. and Canada.

8. Silicon Valley Leadership Group was founded in 1978 by David Packard, co-founder of Hewlett-Packard Company, and represents more than 350 of Silicon Valley's most respected employers. Leadership Group member companies, which range from start-ups to some of the largest global technology companies, provide nearly one in every three private sector jobs in Silicon Valley and account for over $3 trillion in annual economic activity.

9. The Silicon Valley Tax Directors Group, composed of 97 company members, promotes sound, long-term tax policies that support the global competitiveness of the U.S. high-technology industry.

10. The Computing Technology Industry Association is a non-profit trade association that addresses the needs of the information technology industry. It has more than 2,000 members, 3,000 academic and training partners and tens of thousands of registered users spanning the entire information communications and technology industry.

11. The Tax Council is a non-partisan organization promoting sound tax and fiscal policies since 1966 and is comprised of Fortune 500 companies.

12. Technology Network, Inc. (TechNet) is a national network of CEOs and senior executives of technology companies, with more than two million employees, in the fields of information technology, e-commerce, biotechnology, clean energy and venture finance. TechNet is organized to promote the growth of the technology industry and to advance America's global leadership in innovation.

13. The Information Technology Industry Council represents the interests of the information and communications technology industry, including member companies that are among the global leaders in innovation from all areas of information and communications technology, including hardware, services, and software.

Amici's members are the engines of growth for the U.S. economy. They dedicate billions of dollars to research and development to bring new products and services to the world market. Many of *Amici*'s members engage in intercompany transfer pricing and are subject to the U.S. Department of Treasury regulations at issue here. *Amici*'s members are also subject, through their foreign subsidiaries, to the transfer-pricing tax regimes of numerous foreign nations. Many *Amici* members are located within the jurisdiction of the Ninth Circuit. *Amici* accordingly submit this brief in support of the petition for certiorari.

INTRODUCTION

This is a case of exceptional importance, both practical and legal. Cost-sharing agreements of the type at issue in this case are common. They are used widely by *amici*'s members and other entities to enable related entities to jointly develop intellectual property without having to determine complex ownership questions (with substantial tax implications) if the intangible property later proves to be valuable. Recognizing their validity, Treasury long ago established a regulatory regime that both facilitates the use of cost-sharing agreements and establishes their prerequisites. Central to that regime is the longstanding principle that parties to

such agreements must share costs when and to the same extent that unrelated parties dealing at arm's length would do so.

Given industry's reliance on this regime, the Ninth Circuit's decision allowing Treasury to dispense with the arm's-length standard's bedrock comparability analysis for stock-based compensation costs has enormous financial implications for many companies. As petitioner notes, over 80 companies have disclosed in filings with the Securities and Exchange Commission (SEC) that the decision below may have potential impacts that, on an aggregate basis, total billions of dollars. Petn. 25-26. Sixty-seven of these companies are in the Ninth Circuit. *Id.* 31.

Nor do the ramifications of the decision below end there. *Amici*'s members engage annually in *trillions* of dollars of cross-border intercompany transactions in reliance on treaties that, at the urging of the United States, recognize the arm's-length standard. By allowing the Internal Revenue Service to jettison the comparability analysis that, prior to the decision below, has been central to the arm's-length standard, the Ninth Circuit has upset the objective of the treaties: to have a single uniform standard for cross-border transfer pricing. The decision below thus raises unsettling questions about the tax treatment of countless international transactions.

Beyond these vitally important practical considerations, the decision below casts a spotlight on the pressing need for meaningful judicial review of agency action in the tax field. Members of this Court have noted the enormous power that deference under *Chevron, U.S.A., Inc.* v. *Natural Resources Defense*

Council, Inc., 467 U.S. 837 (1984), confers on agencies and the unelected officials who populate them.[2] But the dangers of agency overreach are particularly pronounced in the tax field.

When Treasury announces a rule that, as here, is inconsistent with decades of judicial and regulatory precedent and bereft of empirical support, affected taxpayers cannot simply bring a pre-enforcement challenge. Treasury has long argued, and courts have generally agreed, that the Anti-Injunction Act bars such suits. *See*, *e.g.*, *Florida Bankers Ass'n* v. *Dep't of Treasury*, 799 F.3d 1065 (D.C. Cir. 2015); but cf. *Chamber of Commerce* v. *IRS*, 2017 WL 4682050 (W.D. Tex. Oct. 6, 2017), *appeal dismissed as moot*, 2018 WL 3946143 (5th Cir. July 26, 2018). Under Treasury's view, therefore, taxpayers must wait to raise such challenges in litigation after the IRS issues a notice of deficiency or pay taxes they do not believe they owe and then sue for a refund.

This limitation on judicial review has adverse consequences for taxpayers. It forecloses an early, industry-wide challenge to the validity of the regulation. Thus, where there are strong reasons to

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[2] *See*, *e.g.*, *City of Arlington* v. *FCC*, 569 U.S. 290, 314-15 (2013) (Roberts, C.J., joined by Kennedy and Alito, JJ., dissenting) (noting "the danger posed by the growing power of the administrative state" and that "*Chevron* is a powerful weapon in an agency's arsenal"); *Gutierrez-Brizuela* v. *Lynch*. 834 F.3d 1142, 1149 (10th Cir. 2016) (Gorsuch, J., concurring) (*Chevron* allows agencies to "concentrate federal power in a way that seems more than a little difficult to square with the Constitution"); B. Kavanaugh, *Two Challenges for the Judge as Umpire: Statutory Ambiguity and Constitutional Exceptions*, 92 Notre Dame Law Review 1907, 1911 (2017) (noting that *Chevron* deference "encourages agency aggressiveness on a large scale").

believe that a regulation rests on an invalid rationale (as was true here), taxpayers face years of uncertainty concerning the propriety of the taxes they must pay. At the same time, the delay in judicial review "encourages" a "casual disregard for … general administrative law norms" by Treasury and the IRS. K. Hickman and G. Kerska, *Restoring the Lost Anti-Injunction Act*, 103 Va. L. Rev. 1683, 1687 (2017) ("Hickman and Kerska"). Indeed, "scholars and commentators have complained for decades about Treasury's weak record of compliance with the [Administrative Procedure Act (APA)]." *Id.* at 1714. If and when taxpayers finally get their day in court, moreover, they face an agency that is not simply defending a policy choice announced in a recently promulgated rule of general application. The IRS is an interested party, with strong financial incentives to advance new or different interpretations of rules issued years earlier.

That is precisely what happened here. After all 15 judges of the Tax Court unanimously rejected the IRS's claim that requiring related parties to share the costs of stock-based compensation was consistent with the arm's-length standard, the IRS adopted a new theory on appeal. It managed to persuade two judges that Treasury's 2003 regulations actually "make clear that, in the context of a [cost-sharing agreement], the arm's-length standard does *not* require an analysis of what unrelated entities do under comparable circumstances." Appellant's Br. 57 (internal quotation marks and brackets removed). The IRS claimed—and the majority below agreed—that passing references to snippets of legislative history were sufficient to provide notice of this startling departure from decades of practice based on a straightforward reading of the regulations

themselves. But none of the many sophisticated commenters, including tax specialists, addressed this theory in the rulemaking, because Treasury had never suggested it.

Review is thus warranted in this case for reasons similar to those that led the Court to grant review in *Christopher* v. *SmithKline Beecham Corp.*, 567 U.S. 142 (2012), and *Kisor* v. *Wilkie*, 139 S. Ct. 2400 (2019). First, as in *Christopher*, the IRS seeks to impose massive liability on significant segments of industry based on an interpretation that is nothing more than a *post hoc* rationalization or convenient litigating position.

Second, as in *Kisor*, the Court should grant review to enforce critical limits on agency deference, particularly given the heightened dangers of overreach in the tax setting. Here, interested parties were never given notice or an opportunity to address the rationale on which the rule was sustained. *See Motor Vehicle Mfrs. Assoc.* v. *State Farm Mutual Auto. Ins. Co.*, 463 U.S. 29 (1983). Treasury itself did not acknowledge and explain why it was ignoring longstanding arm's-length comparability analysis in the case of stock-based compensation costs. *Encino Motorcars, LLC*, v. *Navarro*, 136 S. Ct. 2117 (2016). And the IRS did not defend the rule based on the rationale Treasury had advanced in support of the rule. *SEC* v. *Chenery Corp.*, 318 U.S. 80, 92-93 (1943).

The Ninth Circuit not only failed to enforce these requirements, it gave *Chevron* deference to a post-hoc rationale that the IRS advanced to salvage the rule after the Tax Court thoroughly exposed the deficiencies of Treasury's actual justification. The consequences of these errors are simply too great to await further "percolation" of the issues and

development of a division among the circuits. Massive amounts of money are at stake and for several dozen companies, the decision below is the final word on the validity of Treasury's deeply flawed rule, and the propriety of the bait-and-switch tactics the IRS used to defend it.

This Court should grant the petition.

REASONS FOR GRANTING THE PETITION

I. THE DECISION BELOW IMPERMISSIBLY UPSETS SIGNIFICANT RELIANCE INTERESTS.

A. Taxpayers Had Reasonable Reliance Interests On Treasury's Rationale For Its Stock-Based Compensation Rule.

Treasury's 2003 rulemaking took place in the context of a well-established legal framework. Since 1935, Treasury regulations have provided that Treasury's authority (under what is now 26 U.S.C. § 482) to allocate income and deductions between related entities in order "clearly to reflect the income" of each is to be guided by the "arm's-length" standard. *See* Art. 45-1, Regulation 86 (1935). This principle applies both to the sharing of income between related entities, and the sharing of costs. Accordingly, a Treasury regulation provides that, "in every case," the IRS will look to what unrelated parties transacting at arm's length would have done. *See* 26 C.F.R. § 1.482-1(b)(1).

In 1986, Congress adopted the so-called "commensurate with income" standard. 26 U.S.C. § 482. This standard, however, applies only with respect to the narrow category of income from "transfer[s] (or license[s]) of intangible property."

And even where it applies, Treasury has historically taken the position that "intangible income must be allocated on the basis of comparable transactions if comparables exist." *A Study of Intercompany Pricing Under Section 482 of the Code* (1988) ("White Paper"), I.R.S. Notice 88-123, 1988-2 C.B. 458, 474. Thus, Treasury had interpreted the "commensurate with income" standard to be consistent with the rest of the longstanding framework. Pet. App. 52a-54a (dissent).

Given the importance of the 2003 rule and the arm's-length standard, it is unsurprising that Treasury's notice of proposed rulemaking concerning the sharing of stock-based compensation costs generated comments from numerous corporations, interest groups, and tax specialists, some of whose representatives also spoke at a public hearing. Pet. App. 98a-99a. Several *amici* and their members presented substantial comments and evidence. *Id*. at 98a-101a.

The rulemaking did not announce or imply that Treasury was thinking of declaring real-world comparable transactions irrelevant to the arm's-length analysis for cost-sharing. That would have been a dramatic departure from decades of practice involving the arm's-length standard, and would undoubtedly have elicited vociferous opposition. Instead, commenters understood that real-world evidence of how unrelated companies behave remained the touchstone under the arm's-length standard. And they showed that unrelated corporations in similar arrangements do *not* share responsibility for stock-based compensation. *Id*. at 99a-101a. Under the arm's-length standard, then, related companies should not be required to do so, either.

Among other things, commenters told Treasury that:

- They "knew of no transactions between unrelated parties . . . that required one party to pay or reimburse the other party for amounts attributable to stock-based compensation."
- No such agreements were evident from a survey of companies that were members of the American Electronics Association.
- No such agreements could be found in the EDGAR database maintained by the SEC.
- Model accounting procedures from the Council of Petroleum Accountant Societies (COPAS) recommended that stock options *not* be included in cost-sharing.
- "Federal acquisition regulations prohibit reimbursement of amounts attributable to stock-based compensation."

And the commenters presented several examples of real-world, arm's-length agreements in which stock-based compensation was *not* reimbursed. *Id.*

In response, Treasury said, in cursory fashion, that the cited transactions did "not share enough characteristics . . . to establish that parties at arm's length would not take stock options into account in the context of an arrangement similar to a [cost-sharing agreement]." Pet. App. 231a. That comment reflected Treasury's view that real-world comparable transactions remained the best evidence of arm's-length behavior, but (according to Treasury) no such evidence was available. "While the results actually realized in similar transactions under similar circumstances ordinarily provide significant evidence

in determining whether a controlled transaction meets the arm's length standard, in the case of [cost-sharing agreements] such data may not be available." *Id*. *If only valid comparisons existed*, Treasury was saying, *it would gladly use them.*

Given this comparables-focused response, no one could have understood that Treasury actually believed that real-world comparables were legally irrelevant. In fact, Treasury asserted that unrelated parties in cost-sharing agreements *would* share stock-based compensation costs. Treasury wrote that such parties "*would ensure* . . . that the arrangement reflect all relevant costs, including all costs of compensating employees"; they "*would not distinguish* between stock-based compensation and other forms of compensation"; "the party committing employees to the arrangement generally *would not do so* on terms that ignore the stock-based compensation." Pet. App. 232a-233a (emphases added).

Thus, taxpayers expected that, when the regulation was eventually subject to judicial review, its validity would be assessed based on the empirically-based arm's length standard. This judgment was later vindicated by the Tax Court. Not a single judge of the *en banc* Tax Court found that the arm's-length standard, and its focus on comparable transactions, had been abrogated or modified by statute, or that the stock-based compensation rule was consistent with that standard.

B. The IRS Offered A New And Unexpected Rationale For The Rule In Litigation.

It was a complete surprise to the taxpayer community when, 13 years after Treasury published

its final rule in 2003, the IRS announced its radically new understanding of the nature of the arm's-length standard. The IRS claimed in its Ninth Circuit brief that the regulations actually "make clear that, in the context of a [cost-sharing agreement], the arm's-length standard does *not* require an analysis of what unrelated entities do under comparable circumstances." Appellant's Br. 57 (internal quotation marks and brackets removed); *see also id.* at 46-47. To justify its final rule, Treasury had engaged in tortured efforts to explain away the data and evidence commenters had provided. Yet the IRS asserted on appeal that promulgation of the new rule "did not require an examination of data, fact-finding, or consideration of evidence before the agency." *Id.* at 57-58 (internal quotation marks and brackets removed). And while Treasury had claimed in the final rule that the commenters' comparisons were not truly comparable, the IRS dismissed Treasury's discussion of this evidence as "extraneous": "[S]ince Treasury reasonably determined that it was statutorily authorized to dispense with comparability analysis in this narrow context, there was no need for it to establish that the uncontrolled transactions cited by commentators were insufficiently comparable." Appellant's Br. 64. The IRS acknowledged on appeal that its current position "change[s] the legal landscape" (Br. 30, 46), but Treasury never gave proper notice of such a change in the rulemaking.

The Ninth Circuit majority concluded that Treasury provided the public with adequate notice of its (supposed) intention to abandon the bedrock principle of arm's-length comparability by quoting from the legislative history of the 1986 amendment that added the "commensurate with income" language. Pet. App. 35a-36a, 39a-40a. But these

vague references cannot possibly be taken as an adequate statement that Treasury planned to abandon its longstanding endorsement of real-world comparisons. Pet. App. 64a (dissent). After all, Treasury had stated in its 1988 White Paper (which also relied on congressional intent) that even the "commensurate with income" standard should take real-world comparisons into account where they exist. *See* Pet. App. 14a-15a; *id.* at 53a-54a (dissent). Indeed, Treasury's own endorsement of the comparability standard—in its dismissal of commenters' cited transactions on the ground that they supposedly were insufficiently comparable—itself belies the notion that Treasury was abandoning the standard with respect to stock-based compensation.

In short, the preamble to the final rule does not support the IRS's novel account of what the bases for Treasury's actions were in 2003. As Judge Smith observed, by accepting the IRS's revisionist history, "the [panel] majority renders extensive comments irrelevant, and is strangely untroubled by the idea that no member of the tax community noticed this alternative reasoning or submitted a relevant comment." Pet. App. 159a (dissent from denial of rehearing *en banc*).

C. Review Is Required To Protect The Significant Reliance Interests Of Taxpayers.

This Court has recognized that deference to agency interpretations of their own regulations is unwarranted where the agency seeks to impose "potentially massive liability" and it "appears that the interpretation is nothing more than a convenient litigating position, … or a *post hoc* rationalizatio[n]

advanced by an agency seeking to defend past agency action against attack." *Christopher*, 567 U.S. at 155 (quoting *Bowen v. Georgetown Univ. Hospital*, 488 U.S. 204, 213 (1988), and *Auer* v. *Robbins*, 519 U.S. 452, 462 (1997)). That is true with respect to the IRS's newly-minted and litigation-driven interpretation of the "commensurate with income" language in section 482. The potential liabilities here are truly massive, both for individual companies and on an industry-wide basis. And the IRS's argument below is such a transparent *post hoc* rationalization that the IRS was forced to dismiss Treasury's actual analysis as "extraneous," precisely because the new rationale is so far afield from the standard that all commenters and Treasury itself viewed as controlling when the rule was adopted.

The resulting harms to the reliance interests of taxpayers are significant in two distinct respects. First, taxpayers have always understood that the arm's-length standard requires a comparability analysis—*i.e.*, an examination of how third parties dealing at arm's length behave in comparable circumstances—except in the limited circumstance of a license or transfer of intangible property when comparable transactions do not exist. White Paper, I.R.S. Notice 88-123, 1988-2 C.B. 458, 474. The arm's-length standard governs countless trans-border transactions subject to treaties that incorporate that standard. By accepting an unprecedented and apparently uncabined deviation from that standard here, the decision below introduces uncertainty in an area where the need for certainty is particularly vital. *See United States* v. *Byrum*, 408 U.S. 125, 135 (1972) (noting the dangers of "depart[ing] from an interpretation of tax law which has been generally

accepted when the departure could have potentially far-reaching consequences"). *See infra* § II.

Second, taxpayers were entitled to expect that the validity of the stock-based compensation rule would ultimately be judged on the basis of the rationale Treasury advanced for that rule in 2003. Eighty years of law and practice establish that the arm's-length standard imposes a fact-intensive test. The arms-length standard, as well as the focus on comparable transactions of unrelated parties, is embedded in the law that Treasury developed in the United States and encouraged abroad. It is profoundly unfair for the IRS to require taxpayers to live with a rule for over a decade and then, when its validity is finally tested in court, to propound a new rationale for it—particularly where that rationale deviates from decades of practice. "[T]he foundational principle of administrative law [is] that a court may uphold agency action only on the grounds that the agency invoked when it took the action." *Michigan v. EPA*, 135 S. Ct. 2699, 2710 (2015); *State Farm*, 463 U.S. at 50. This principle must apply with particular force where the agency insists that regulated parties cannot bring pre-enforcement challenges to the agency's action.

For these reasons, it is simply no answer to argue (as the government likely will) that the Court should await a circuit split before acting. Companies engaged in foreign transactions need to know *now* whether they can continue to rely on the arm's-length comparability standard for existing and upcoming cross-border arrangements. And at least 67 companies whose income is materially affected by the decision below have little chance of escaping the impact of the decision. *See Golsen v. Commissioner*,

54 TC 742 (1962) (Tax Court follows the law of the circuit in which cases arise). Moreover, under the government's approach to the Anti-Injunction Act, the IRS controls whether, when, and where to bring future deficiency cases based on the stock-based compensation rule. Taxpayers thus have little ability to precipitate a division among the circuits, particularly given the amounts of money at stake and the pressures to settle rather than risk interest and penalties.

II. THE DECISION BELOW WILL UNDERCUT AMERICA'S COMPETITIVE ADVANTAGE IN THE TECHNOLOGY SECTOR.

The Ninth Circuit's opinion threatens significant exposure and uncertainty for *amici*'s members. Pet. 29-31; *see also* Pet. App. 331-338a (listing U.S. tax treaties that incorporate the arm's-length standard). The decision upsets decades of precedent concerning the meaning of the arm's-length standard and the settled expectations of U.S. multinational companies. *Amici*'s members engage annually in trillions of dollars of cross-border intercompany transactions. They rely heavily upon U.S. and international recognition of the arm's-length standard for their cross-border transactions, including transactions that involve the joint development of intangible assets. Given the significant interests of U.S. multinational companies—many of which are based in the Ninth Circuit—this Court's review is warranted now.

As the petition explains, the arm's-length standard is not a unique feature of U.S. tax law. To the contrary, the United States has long championed the standard and made it "the international norm." 1988 White Paper, 1988-2 C.B. 458 at *31. As a result, the

arm's length standard is reflected in the network of international treaties that were negotiated in part by the United States. The key objective was to ensure all nations are using a consistent approach in determining how profits and deductions are allocated among related parties. As Treasury explained, "virtually every major industrial nation takes the arm's length standard as its frame of reference in transfer pricing cases." *Id.* at 43,539. The arm's-length standard's reference to how unrelated parties actually interact is central to international norms regarding transfer pricing. *See, e.g.*, IRS, Report on Application and Administration of Section 482, at ii-iii, 2.2-2.4 (1999), www.irs.gov/pub/irs-pdf/p3218.pdf.

Under U.S. bilateral tax treaties, the arm's length-standard looks to what unrelated parties do or would do in comparable circumstances. For example, the income tax treaty with the United Kingdom provides that if the conditions made between the two enterprises in their financial relations "differ from those that would be made between independent enterprises," then profits could be reallocated. 2001 U.S.-United Kingdom Income Tax Treaty, art. 9 (July 24, 2001); 7 Tax Treaties (CCH) ¶ 10901.09.1 at 201.019. If the United States were to depart unilaterally from the arm's-length standard, it may be allocating costs to a country that did not recognize the costs as ones that arm's-length parties would share, risking double taxation by both countries of the same income. *Amici*'s members have a significant interest in the uniform application of the arm's length standard to avoid double taxation in a global operating environment.

III. REVIEW IS WARRANTED TO AFFIRM AND REINFORCE CRITICAL LIMITS ON JUDICIAL DEFERENCE IN THE AREA OF FEDERAL TAXATION.

This Court recently upheld the principle of deferring to agency interpretations of their own regulations but, in doing so, affirmed and "reinforce[d] its limits." *Kisor*, 139 S. Ct. at 2408. Given the financial implications of the decision below and the unique dangers of overreach in the area of federal taxation, the Court should grant review here for similar reasons.

As scholars have noted, the difficulty taxpayers face in bringing pre-enforcement challenges "encourages" a "casual disregard for … general administrative law norms" by Treasury and the IRS. Hickman and Kerska, 103 Va. L. Rev. at 1687. As an interested party seeking money, moreover, the IRS has strong incentives to gloss over defects in Treasury's reasoning and instead to frame its litigation positions as essential to preventing corporate tax evasion. Take this very case, for example. Treasury regulations *facilitate* the use of cost-sharing agreements between related parties, and unrebutted empirical evidence shows that unrelated parties do *not* share stock-based compensation when they enter into such agreements. Yet, the IRS convinced the majority below that requiring related parties to share such costs is somehow necessary to combat "tax abuse by multinational corporations with foreign subsidiaries." Pet. App. 7a. *See also id.* at 7a-8a (referring to incentives for "tax avoidance" and "transaction-shuffling" by related parties); *id.* at 10a "the problem of abusive transfer pricing practices created a new adherence to a stricter arm's length standard"). In

conjunction with *Chevron* deference, therefore, the IRS's ability to delay and frame that review in terms that are unfavorable to taxpayers creates a unique environment for agency overreach—and a correlative need for this Court to reinforce limits on *Chevron* deference in the tax area.

Accordingly, the Court should grant review to emphasize the principles of administrative law that appropriately cabin *Chevron* deference in the tax field. Just as *Auer* deference is "rooted in a presumption about congressional intent," *Kisor*, 139 S. Ct. 2412, so, too, is *Chevron* deference. *See United States* v. *Mead Corp.*, 533 U.S. 218, 229 (2001). It is reasonable to assume that Congress intended courts to defer to interpretations of the Tax Code that actually reflect *Treasury's* "authoritative, expertise-based, fair[, or] considered judgment," *Kisor*, 139 S. Ct. at 2414 (brackets in original, internal quotation marks omitted; citing *Mead*, 533 U.S. at 229-31 as "adopting a similar approach to *Chevron* deference"). But that assumption does not apply where, as here, a court is asked to defer to a statutory interpretation that Treasury did not announce when it promulgated its final rule, and that instead appeared in appellate briefs filed by the IRS.

Indeed, in promulgating that rule, Treasury simply purported to apply the traditional arm's-length comparability analysis. Its conclusion that its rule was consistent with the evidence in the record was a classic failure of reasoned decision-making, as the Tax Court held. It was particularly improper, therefore, for the Ninth Circuit to rely on *Chevron* principles to excuse this failure. That error would have been avoided had the Ninth Circuit applied the bedrock rule that courts can sustain an agency's

action based only on the rationale that the agency itself gave for that action, not theories propounded by agency counsel in litigation. *Chenery*, 318 U.S. at 87; *Michigan v. EPA*, 135 S. Ct. at 2710.

CONCLUSION

For the foregoing reasons and those stated in the petition, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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March 6, 2020