No. 22-9

In the Supreme Court of the United States

WHIRLPOOL FINANCIAL CORPORATION, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

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

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

A U.S. taxpayer that controls a foreign corporation must include in its taxable income certain earnings of the "controlled foreign corporation" (CFC), including "foreign base company sales income" (FBCSI). 26 U.S.C. 951(a)(1)(A), 954(a)(2), 957(a). Section 954(d) defines FBCSI to include two primary types of income. First, it provides that FBCSI includes income that the CFC derives from certain sales transactions between the CFC and a "related person," such as a wholly owned subsidiary of the CFC. 26 U.S.C. 954(d)(1). Second, it provides that where the CFC's "carrying on of activities * * * through a [foreign] branch * * * has substantially the same effect as if such branch * * * were a wholly owned subsidiary," then, "under regulations prescribed by the Secretary the income attributable to the carrying on of such activities * * * shall constitute [FBCSI] of the [CFC]." 26 U.S.C. 954(d)(2). The Secretary of the Treasury has promulgated regulations implementing Section 954(d)(2). In this case, the court of appeals held that the sales income earned in 2009 by Whirlpool Financial Corporation's Luxembourg CFC was unambiguously FBCSI under Section 954(d)(2)'s terms. The question presented is:

Whether the court of appeals permissibly based its conclusion that the 2009 sales income was FBCSI on the terms of Section 954(d)(2) without articulating a further rationale based on a since-superseded version of the Treasury Department's implementing regulations.

ADDITIONAL RELATED PROCEEDINGS

United States Court of Appeals (6th Cir.):

Whirlpool Fin. Corp. v. *Commissioner*, No. 20-1899 (Dec. 6, 2021)

United States Tax Court:

Whirlpool Fin. Corp. & Consol. Subsidiaries v. *Commissioner*, No. 13986-17 (June 9, 2020)

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-40a) is reported at 19 F.4th 944. The opinion of the Tax Court (Pet. App. 41a-92a) is reported at 154 T.C. 142.

JURISDICTION

The judgment of the court of appeals was entered on December 6, 2021. A petition for rehearing was denied on March 2, 2022 (Pet. App. 93a-94a). On May 13, 2022, Justice Kavanaugh extended the time within which to file a petition for a writ of certiorari to and including June 30, 2022, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. a. In 1962, Congress enacted Subpart F of the Internal Revenue Code, which requires U.S. corporations to pay taxes on certain kinds of income earned by their foreign subsidiaries. See Revenue Act of 1962, Pub. L. No. 87-834, § 12(a), 76 Stat. 1006-1027. Before Subpart F's enactment, the earnings of foreign subsidiaries escaped U.S. taxation unless those earnings were distributed to the U.S.-based parent corporation. See S. Rep. No. 1881, 87th Cong., 2d Sess. 78 (1962) (1962 Senate Report). That regime encouraged many corporations to shift income to foreign subsidiaries—generally in countries with lower tax rates—and thereby indefinitely defer U.S. taxation of such income. Pet. App. 2a. As President Kennedy explained in 1961, "more and more enterprises organized abroad by American firms have arranged their corporate structures * * * so as to exploit the multiplicity of foreign tax systems and international agreements in order to reduce sharply or eliminate completely their tax liabilities both at home and abroad." Message from the President of the United States Relative to Our Federal Tax System, Apr. 20, 1961, *reprinted in* H.R. Doc. 140, 87th Cong., 1st Sess., 6 (1961); see 1962 Senate Report 78-79.

That type of tax-avoidance practice can be illustrated with the potential operations of a U.S. corporation that has a manufacturing subsidiary in a foreign country with relatively cheap labor but a relatively high income-tax rate. See Staff of the Joint Comm. on Internal Revenue Taxation, *Tax Effects of Conducting Foreign Business Through Foreign Corporations*, JCS-5-61, at 23-24 (July 21, 1961). If the manufacturing subsidiary were to sell its products directly to the U.S. corporation (for distribution to consumers), the manufacturing subsidiary's income would be taxed at the relatively high rate. But if the U.S. corporation were to establish a second subsidiary in another country with lower taxes, then the manufacturing subsidiary could sell its products to the low-tax subsidiary at a price reflecting only the manufacturing costs, and the low-tax subsidiary—without adding any appreciable value to the products—could then sell the products to the U.S. corporation at the full (significantly higher) price. The firm could therefore reduce its overall tax payments by shifting sales income from the manufacturing subsidiary to the low-tax subsidiary. See *id.* at 23 (emphasizing that "a transfer of income" to "tax haven entities" "bring[s] about a substantial reduction in tax on the total income derived from the foreign operations").

b. Subpart F seeks to limit such tax-avoidance practices by taxing U.S. corporations directly on certain kinds of income earned by their foreign subsidiaries, *i.e.*, their "controlled foreign corporations" (CFCs). See 26 U.S.C. 954(d), 957(a). The kind of income at issue is called "foreign base company sales income" (FBCSI). 26 U.S.C. 954(a)(2), (d)(1) and (2); see 26 U.S.C. 952(a)(2). Section 954(d) defines FBCSI to include two primary types of income. First, Section 954(d)(1) provides that FBCSI includes income that the CFC derives from sales transactions between the CFC and a "related person," such as a wholly owned subsidiary of the CFC, involving personal property that is manufactured and sold for use outside the country of the CFC's incorporation. 26 U.S.C. 954(d)(1).

Second, Section 954(d)(2) provides in relevant part that, where the "carrying on of activities by a [CFC] through a [foreign] branch * * * has substantially the same effect as if such branch * * * were a wholly owned subsidiary," then, "under regulations prescribed by the Secretary the income attributable to the carrying on of such activities of such branch * * * shall constitute [FBCSI] of the [CFC]." 26 U.S.C. 954(d)(2). Section 954(d)(2) functions as a "failsafe provision," Pet. App. 5a, designed to prevent a CFC from circumventing Section 954(d)(1) by conducting activities (like selling or manufacturing) through branches located in a second foreign country, rather than through a "related person," *id.* at 55a-56a (citation omitted). Because some countries impose no taxes on corporate income sourced through a foreign branch, Congress recognized that, without Section 954(d)(2), CFCs would seek to conduct activities through such branches to "avoid taxation of income." *Id.* at 4a-5a.

c. Shortly after Congress enacted Subpart F, the Department of the Treasury promulgated regulations implementing Section 954(d) through notice-and-comment rulemaking. See 29 Fed. Reg. 6385, 6392-6399 (May 15, 1964). Among other things, those regulations provided that "[FBCSI] does not include income of a [CFC] derived in connection with the sale of personal property manufactured * * * by such [CFC] in whole or in part from personal property which it has purchased." 26 C.F.R. 1.954-3(a)(4)(i) (2009). Petitioners refer (Pet. 6) to that provision as the "manufacturing exception." The regulations provided an example (Example 2) of how the provision operated when a CFC's foreign branch manufactured products that the CFC then sold. 26 C.F.R. 1.954-3(b)(4) (2009) ("Branch B manufactures articles in country Y which are sold through the sales offices of C Corporation located in country X."). In that example, the CFC's sales income "constitutes [FBCSI]." *Ibid.*

In 2008, the Treasury Department revised the regulations implementing Section 954(d). See 73 Fed. Reg. 79,334 (Dec. 29, 2008); 73 Fed. Reg. 10,716 (Feb. 28, 2008). Among other things, the revised regulations "clarif[ied]" what was already apparent from the prior regulations and Tax Court decisions interpreting them, specifying "that in order to satisfy [the manufacturing exception] the relevant manufacturing activities must be performed by the CFC itself." 73 Fed. Reg. at 10,719 (citing *Electronic Arts P.R., Inc.* v. *Commissioner*, 118 T.C. 226, 265 (2002)); see 73 Fed. Reg. at 79,339 (explaining that any other view would be "contrary to existing law, and represents an incorrect reading"). The revised regulations thus state that a CFC "will have manufactured * * * property which the corporation sells only if such corporation [does so] through the activities of its employees." 26 C.F.R. 1.954-3(a)(4)(i). And the revised regulations retain the same example demonstrating how the provision operates when a CFC's foreign branch manufactures products that the CFC then sells. 26 C.F.R. 1.954-3(b)(4) (Example 2).

2. a. Petitioner Whirlpool Financial Corporation (Whirlpool) is a U.S. subsidiary of Whirlpool Corporation, a U.S. corporation that, through domestic and foreign subsidiaries, manufactures and distributes large household appliances.[1] Pet. App. 1a, 41a. At all times

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[1] Another Whirlpool Corporation subsidiary, Whirlpool International Holdings, S.a.r.l. (f/k/a Maytag Corporation & Consolidated Subsidiaries), is also a petitioner here. See Pet. ii. Whirlpool International Holdings is involved in this proceeding because a portion of the Whirlpool consolidated group's 2009 net operating loss that was reduced by the Internal Revenue Service's adjustments in this case was carried back to Whirlpool International Holdings's 2000 tax year. Pet. App. 42a. This brief refers to Whirlpool and Whirlpool International Holdings as "petitioners."

relevant here, Whirlpool owned 100% of Whirlpool-Mexico, a corporation organized under Mexican law. *Id.* at 5a. Before 2007, Whirlpool-Mexico manufactured appliances at two Mexican plants and sold them to Whirlpool. *Ibid.* Mexico taxed Whirlpool-Mexico's income from its manufacturing and sales at 28%. *Ibid.*

"Beginning in 2007, however, Whirlpool restructured its Mexican operations to avoid (or at least defer indefinitely) paying taxes on most of the income attributable to its Mexican operations." Pet. App. 6a. An internal Whirlpool presentation about the restructuring touted the "[d]eferral of U.S. taxation of profits earned." *Ibid.* (brackets in original). In seeking to achieve that deferral, Whirlpool created Whirlpool Overseas Manufacturing (Lux), a wholly owned subsidiary organized under Luxembourgian law (and a CFC under U.S. tax law). *Ibid.*; *id.* at 42a. Whirlpool also created a separate corporation under Mexican law, called Whirlpool Internacional (WIN), which Lux wholly owned. *Id.* at 6a. WIN had no employees, while Lux had one part-time employee in Luxembourg who "performed modest administrative functions." *Id.* at 45a; see *id.* at 6a.

Whirlpool-Mexico's existing Mexican plants then "subcontracted" their hourly employees, "seconded" their executives, sold parts and tools, and leased real estate, to WIN. Pet. App. 6a. The Mexican plants also sold machinery, equipment, and unfinished appliances to Lux. *Ibid.* Lux and WIN then entered an agreement, under which WIN would manufacture appliances using its subcontracted employees and Lux would supply the raw materials and own the finished goods. *Id.* at 6a-7a. Lux paid WIN an arm's-length fee for WIN's manufacturing services. *Id.* at 7a.

Next, Lux and Whirlpool entered their own agreement, under which Lux would supply Whirlpool with finished appliances and Whirlpool would pay Lux an arm's-length price for those appliances. Pet. App. 7a. Whirlpool would then distribute the appliances for sale to consumers. *Id.* at 42a.

"Meanwhile, on the ground in Mexico, nothing changed." Pet. App. 7a. The same plants paid the same workers to make the same appliances in the same factories. *Ibid.* "There is no evidence that the[] workers were aware of any change in their employment status after 2008." *Id.* at 61a. "Only the underlying corporate arrangements had changed." *Id.* at 7a.

b. Whirlpool deliberately adopted those corporate arrangements in order to obtain the tax benefits of Mexico's "Maquiladora Program." Pet. App. 7a. To qualify for that program, a foreign principal (here, Lux) had to engage a Mexican subsidiary—*i.e.*, the maquiladora (here, WIN)—to conduct manufacturing activities in Mexico. *Id.* at 7a-8a. If the principal and maquiladora met the relevant requirements (*e.g.*, the principal had to take title to and sell the finished goods), then Mexico would tax the maquiladora at a 17% rate, instead of the usual 28% rate. *Id.* at 8a. And it would treat the foreign principal as if it had no permanent establishment in Mexico—meaning that the principal would pay no Mexican taxes at all, instead of the usual 28% income tax applicable to foreign corporations with a permanent establishment in Mexico. *Ibid.*

Whirlpool's restructured operations fulfilled the Maquiladora Program's requirements. Pet. App. 8a. As a result, in 2009 (the tax year at issue here), WIN paid Mexico a 17% tax on its income earned from providing manufacturing services to Lux. *Id.* at 50a. And Lux paid Mexico no taxes at all on its approximately $45 million in profits from selling the manufactured appliances to Whirlpool and Whirlpool-Mexico. *Id.* at 8a-9a, 51a & n.3.

Lux not only avoided paying taxes on those profits in Mexico, but it also avoided paying taxes on those profits in Luxembourg. Pet. App. 9a. While Luxembourgian corporations normally paid a 28% income tax, Luxembourg and Mexico had a treaty under which a Luxembourgian corporation would pay no tax in Luxembourg on income attributable to the activities of a permanent establishment in Mexico. *Ibid.* In order to qualify for that treaty benefit, Lux represented to Luxembourgian authorities that it had a permanent establishment in Mexico, even though Lux had already obtained a determination from Mexico (under the Maquiladora Program) that it did not have a permanent establishment there. *Ibid.* "Lux did not disclose to the Luxembourgian authorities, however, that the Mexican authorities had made the opposite determination." *Id.* at 10a. Based on Lux's submission, Luxembourg (like Mexico) imposed no taxes on Lux's approximately $45 million in 2009 sales profits. *Ibid.*

c. On Whirlpool Corporation's 2009 U.S. consolidated tax return, it represented that Lux's income from Lux's sales to Whirlpool and Whirlpool-Mexico did not qualify as FBCSI. Pet. App. 10a. After an audit, the Internal Revenue Service (IRS) disagreed. *Ibid.* The IRS thus issued deficiency notices to petitioners, stating that the Whirlpool consolidated group had a "subpart F inclusion under [26 U.S.C.] 951(a) and 954(d)" because it engaged in "transactions giving rise to foreign base company sales income under [Section] 954(d)." C.A. App. 42, 81; see Pet. App. 51a.[2]

3. Petitioners sought redetermination of the IRS's deficiency determinations in the Tax Court, and the parties cross-moved for summary judgment. In a "meticulously reasoned 62-page opinion," Pet. App. 11a, the Tax Court granted summary judgment to the IRS on the ground that Lux's approximately $45 million in 2009 sales income was FBCSI under Section 954(d)(2), *id.* at 41a-92a.[3]

The Tax Court "beg[a]n with the text" of Section 954(d)(2). Pet. App. 69a. The court explained that "[t]he statute's first precondition is met because [Lux] carried on activities 'through a branch or similar establishment outside * * * [its] country of incorporation,'" and "the statute's second precondition is met because this manner of operation had 'substantially the same effect,' for U.S. tax purposes, as if the Mexican branch were a wholly owned subsidiary of [Lux]." *Id.* at 72a (asterisks and first set of brackets in original).[4] That was so, the court reasoned, because Lux's use of WIN

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[2] Although Lux derived $45,231,843 in income from selling appliances to Whirlpool and Whirlpool-Mexico, all of Lux's 2009 income ($51,326,345) is treated as Subpart F income under the "full inclusion" rule in 26 U.S.C. 954(b)(3)(B) if the $45,231,843 in sales income counts as FBCSI. C.A. App. 42, 81; Pet. App. 51a n.3. Petitioners have not challenged the IRS's application of the full inclusion rule.

[3] The Tax Court reserved the question whether that income also qualified as FBCSI under Section 954(d)(1), noting that the IRS had identified "factual uncertainties" related to that issue. Pet. App. 66a.

[4] WIN was deemed a "branch" under Section 954(d)(2), rather than a "related person" under Section 954(d)(1), because it had elected to be a "disregarded entity" for purposes of U.S. tax law, 26 C.F.R. 301.7701-2(a). See Pet. App. 10a; Pet. 11.

enabled it to "avoid[] any current taxation of its sales income," which "is precisely the situation that the statute covers." *Id.* at 73a. Accordingly, the court held, "even without the refinements supplied by the regulations implementing section 954(d)(2), the bare text of the statute, literally read, indicates that [Lux's] sales income is FBCSI that must be included in petitioners' income under subpart F." *Ibid.*

The Tax Court additionally held that application of the implementing regulations yielded the same result. Pet. App. 73a-79a. The court found that because the 2008 revision to the regulations had not become effective at the start of the 2009 tax year, the previous version of the regulations applied. *Id.* at 57a. The court applied those regulations and concluded that "[t]he sales income derived by [Lux] * * * constituted FBCSI." *Id.* at 79a.

4. The court of appeals affirmed the Tax Court's grant of summary judgment. Pet. App. 1a-40a.

a. In their appeal, petitioners did not contend that the Tax Court had erred by relying on Section 954(d)(2)'s "bare text," Pet. App. 73a, instead of exclusively applying the regulations. Rather, petitioners simply argued that they should prevail under the regulations and that those regulations were invalid in any event. Pet. C.A. Br. 27-48.

The court of appeals applied the terms of Section 954(d)(2), observing that the statute's "first condition—that Lux 'carr[ied] on' activities 'through a branch or similar establishment' outside its country of incorporation —is undisputedly met here." Pet. App. 13a. Turning to the phrase "substantially the same effect as if such branch * * * were a wholly owned * * * subsidiary," the court reasoned that "as a matter of historical and statutory context alike, an informed reader would naturally understand the 'effect' to which § 954(d)(2) refers to be a *tax deferral effect*." *Id.* at 16a-17a. The court thus concluded that Section 954(d)(2)'s conditions were met because "by carrying on its activities through a branch or similar establishment in Mexico, Lux avoided *any* taxation of its sales income." *Id.* at 17a (brackets and internal quotation marks omitted). "From these premises," the court explained, Section 954(d)(2) "expressly prescribes the consequences that follow": namely, the relevant income "'shall constitute [FBCSI] of' Lux." *Id.* at 17a-18a.

The court of appeals "acknowledge[d]" Section 954(d)(2)'s statement "that, if the provision's two conditions are met, then 'under regulations prescribed by the Secretary' the provision's two consequences 'shall' follow." Pet. App. 18a. "But," the court reasoned, "the agency's regulations can only implement the statute's commands, not vary from them." *Ibid.* The court stated that "the relevant command here—that Lux's sales income 'shall constitute [FBCSI] of' Lux—could hardly be clearer." *Ibid.* The court rejected the argument that its reading "would allow income from sources other than sales * * * to be treated as FBCSI," emphasizing that Section 954(d)(2) refers to "'foreign base company *sales* income'—which makes clear enough the provision is confined to income from sales." *Ibid.* Accordingly, the court "agree[d] with the Tax Court that, under the text of the statute alone, [Lux's] sales income is FBCSI." *Id.* at 19a (citation and internal quotation marks omitted). Unlike the Tax Court, the court of appeals did not proceed to articulate an alternative rationale based on the regulations.

b. Judge Nalbandian dissented. Pet. App. 21a-40a. At the outset, he described this as "a hard case," and he recognized that "[t]he majority thoughtfully engages with [the relevant text] and comes to a reasoned conclusion." *Id.* at 21a. But Judge Nalbandian was "not so sure" that "(d)(2)'s mandate is clear" because, in his view, "the statutory structure only makes sense if (d)(2) transactions filter back through (d)(1)'s framework." *Id.* at 26a. And, he maintained, the phrase "'under regulations prescribed by the Secretary'" gives the Department of the "Treasury a role in defining when branch transactions generate FBCSI." *Id.* at 27a. According to the dissent, the "Manufacturing Exception" in the agency's "*old* regulations" covered Lux, even though Lux "'*itself*'" did not "manufacture[] anything." *Id.* at 22a n.1, 24a, 37a. Judge Nalbandian reached that conclusion because he believed that the manufacturing exception in the former version of the regulations did not "require the CFC itself to manufacture the goods." *Id.* at 38a. At the same time, he suggested that Lux's income would now be FBCSI under "the *new* regulations" covering FBCSI after the 2009 tax year at issue here. *Id.* at 37a n.5.

5. Petitioners sought panel rehearing and rehearing en banc, contending for the first time that Section 954(d)(2)'s "'under regulations' command" precludes a court from relying on the statutory text "without considering the terms or validity of the implementing regulations." Pet. C.A. Reh'g Pet. 9. The court of appeals denied rehearing after no judge requested a vote. Pet. App. 93a-94a. Judge Nalbandian would have granted rehearing for the reasons given in his dissent. *Id.* at 94a.

ARGUMENT

Petitioners contend (Pet. 17) that 26 U.S.C. 954(d)(2) is "conditioned on the promulgation of regulations" by the Treasury Department and thus may not "be enforced without regard to such regulations." But as the court of appeals correctly held, Section 954(d)(2)'s text itself establishes clear "conditions" and "consequences," Pet. App. 12a, and when applied to this case, that text "mandate[s]" that the income at issue is FBCSI, *id.* at 18a. The phrase "'under regulations prescribed by the Secretary'" delegates to the Treasury Department authority to "implement the statute's commands," but not to "vary from them," *ibid.*, so the court permissibly declined to articulate a separate rationale in this case based on the implementing regulations. Petitioners concede (Pet. 33) that the decision below does not conflict with that of any other court of appeals. Nor does it conflict with this Court's precedent because petitioners' cited cases involved meaningfully distinct statutory schemes. And resolving the question presented lacks practical importance because the Treasury Department's former regulations would dictate the same result as the statutory text, and the revisions that were made to the regulations in 2008 removed any potential doubt about that result. This Court's review is unwarranted.

1. The court of appeals properly construed Section 954(d)(2)'s text, and its decision accords with this Court's precedent and administrative-law principles.

a. Petitioners contend (Pet. 17) that Section 954(d)(2) is "conditioned on the promulgation of regulations" by the Treasury Department and therefore cannot operate without reference to those regulations. But Section 954(d)(2)'s text makes clear that the provision is independently operative: It "specifies two conditions and then two consequences that follow if those conditions are met." Pet. App. 12a. In particular, if a CFC "carr[ies] on" activities "through a [foreign] branch" and that conduct "has substantially the same" tax-deferral "effect as if such branch * * * were a wholly owned subsidiary," then the "income attributable" to the relevant activities "shall constitute [FBCSI] of the [CFC]." 26 U.S.C. 954(d)(2); see Pet. App. 13a-18a. Considering the conditions and consequences in the statutory provision, the court of appeals correctly held that the result in this case—that Lux's relevant income qualifies as FBCSI—is "mandated by the statute itself." Pet. App. 18a. Although petitioners state that the Tax Court had "decided the case based on the regulations alone," Pet. 14, the Tax Court had in fact anticipated the court of appeals by concluding that "the bare text of the statute, literally read, indicates that [Lux's] sales income is FBCSI." Pet. App. 73a.

Section 954(d)(2)'s phrase, "under regulations prescribed by the Secretary," does not change the provision's self-executing nature. 26 U.S.C. 954(d)(2). Rather, that phrase—like countless other ordinary delegations of regulatory authority to agencies—simply authorizes the agency to promulgate regulations to "*implement* the statute's commands." Pet. App. 18a (emphasis added). Those implementing regulations can and do provide important guidance when the statute's application to a given case is ambiguous. For that reason, the "'under regulations'" phrase is by no means "superfluous." Pet. 25 (citation omitted). But petitioners' contention that the "'under regulations'" phrase makes Section 954(d)(2)'s entire operation turn on the regulations ignores Section 954(d)(2)'s own clear "command," Pet. App. 18a, that when the statutory conditions are met, the relevant income "*shall* constitute [FBCSI]." 26 U.S.C. 954(d)(2) (emphasis added). The dissent below suggested that such a reading could make income FBCSI "even if no sales transaction occurred," Pet. App. 28a (emphasis omitted), but the majority correctly concluded that Section 954(d)(2)'s express focus on "'foreign base company *sales* income' * * * makes clear enough the provision is confined to income from sales," *id.* at 18a.

Because Section 954(d)(2) is self-executing, and its application here is straightforward, the court of appeals permissibly declined to articulate a separate rationale based on the regulations. As the court recognized, those regulations "can only implement the statute's commands, not vary from them," and "the relevant command here * * * could hardly be clearer." Pet. App. 18a. That conclusion flows from the settled principle that where "the intent of Congress is clear, that is the end of the matter," and any agency regulations must "give effect to the unambiguously expressed intent of Congress." *City of Arlington* v. *FCC*, 569 U.S. 290, 296 (2013) (citation omitted). Indeed, petitioners argued in the court of appeals that the regulations contravened Section 954(d)(2) in certain respects, Pet. C.A. Br. 27-38—thereby undermining their current position that Section 954(d)(2) has no independent force without regard to those regulations.[5]

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[5] Contrary to petitioners' contention (Pet. 23), the IRS never suggested in the Tax Court that Section 954(d)(2) cannot be independently enforced. Rather, the IRS simply responded to petitioners' regulations-focused arguments by explaining why the relevant income here is FBCSI under the regulations, C.A. App. 2555-2579, and why those regulations permissibly implement the statutory

Of course, Congress does sometimes "expressly condition[]," Pet. 1, the operation of a statute on agency regulations. For instance, the Tax Court has held that a provision stating that it "shall apply *only to the extent* provided in regulations prescribed by the Secretary" cannot apply absent promulgation of such regulations. *Alexander* v. *Commissioner*, 95 T.C. 467, 473 (1990) (emphasis added); see 26 U.S.C. 465(c)(3)(D); see also, *e.g.*, 26 U.S.C. 170(a)(1) ("A charitable contribution shall be allowable as a deduction *only if verified* under regulations prescribed by the Secretary.") (emphasis added). But the court of appeals never questioned that certain provisions may fall into that category. It simply held that Congress did not use such expressly conditional language in Section 954(d)(2), and that Section 954(d)(2) itself establishes clear "conditions" as well as the "consequences that follow if those conditions are met." Pet. App. 12a. That statute-specific holding does not warrant this Court's review.

b. Petitioners contend (Pet. 17-20) that the decision below conflicts with this Court's precedent, but the purportedly conflicting cases that they cite involved statutes with distinct language that *expressly* conditioned the provisions' operation on agency regulations. Petitioners have therefore not identified any case in which this Court has held a statute that is "structurally identical" (Pet. 3) to Section 954(d)(2) to be non-self-executing.

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text, *id.* at 2579-2593. Nor has the IRS suggested that "structurally identical statutes," Pet. 23, are non-self-executing. In the case that petitioners cite, Pet. 24, the IRS argued on appeal that "[e]ven if the regulations were invalid, or had never been promulgated in the first instance, the statutory language of § 956(d) is still operative and supports the income inclusions here," Gov't Br. at 49, *SIH Partners LLLP* v. *Commissioner*, 923 F.3d 296 (3d Cir. 2019) (No. 18-1862).

Petitioners emphasize this Court's 123-year-old decision in *Dunlap* v. *United States*, 173 U.S. 65 (1899), which the Court last cited in 1917, see *United States* v. *M.H. Pulaski Co.*, 243 U.S. 97, 107. In *Dunlap*, the statute at issue provided that "[a]ny manufacturer finding it necessary to use alcohol in the arts, or in any medicinal or other like compound, may use the same under regulations to be prescribed by the Secretary of the Treasury, and on satisfying the collector of internal revenue * * * that he has complied with such regulations * * * , shall be entitled to receive from the Treasury of the United States a rebate or repayment" of taxes paid on such alcohol. 173 U.S. at 70. The Court held that the statutory rebate right "was not absolute," *id.* at 71, but rather "was conditioned on use [of alcohol] in compliance with regulations to be prescribed, in the absence of which the right could not vest," *id.* at 76.

Section 954(d)(2) is critically different from the statute in *Dunlap*. The statute in *Dunlap* "conditioned" the manufacturer's right to a rebate on showing "that he ha[d] *complied with* [the Secretary's] regulations." 173 U.S. at 70-71 (emphasis added). That compliance requirement meant that without any regulations (and the ability to comply therewith), the rebate "right could not vest." *Id.* at 76. In contrast, Section 954(d)(2) does not condition any right or obligation on a showing related to the Secretary's regulations. It does not say, for instance, that income shall constitute FBCSI only if certain conditions prescribed by the Secretary are met, or that income is exempt from FBCSI status if the taxpayer complies with the Secretary's regulations. Rather, the statute itself prescribes the relevant conditions that make income FBCSI and the consequences that flow from the fulfillment of those conditions. See

Pet. App. 12a. Accordingly, unlike the statute in *Dunlap*, it can be applied by its own terms.

Petitioners also cite (Pet. 18-19) *Campbell* v. *United States*, 107 U.S. 407 (1883), but *Campbell* supports the court of appeals' reasoning here. In *Campbell*, the statute provided a "drawback" of duties paid on certain imported materials "to be ascertained under such regulations as shall be prescribed by the Secretary of the Treasury." *Id.* at 407. After the regulations had been prescribed, a customs officer refused (at the Secretary's direction) to comply with those regulations when adjudicating a manufacturer's drawback request. *Id.* at 409. The Court held that the customs officer's conduct was unlawful, reasoning that "[i]t is the *law* which gives the right [to a drawback]" and "the fact that the customs officers refuse to obey the[] regulations cannot defeat a right which the act of Congress gives." *Id.* at 411. *Campbell* thus shows that a statute using the phrase "under such regulations"—analogous to the phrase in 26 U.S.C. 954(d)(2)—*can* be self-executing. See *Dunlap*, 173 U.S. at 72 (noting that in *Campbell*, "the right to the drawback depend[ed] on the statute, and not on the Secretary's regulations"). And while *Campbell* observes that agencies must follow their regulations to the extent they apply, it also recognizes that regulations are "invalid" if they contravene a governing statute. 107 U.S. at 410. Similarly, the court of appeals here held that the Treasury Department's regulations could not "vary" from the result "mandated by the statute itself." Pet. App. 18a.

The decision below is likewise consistent with the other cases on which petitioners rely. See Pet. 19. None of the statutes involved in those cases contained the language at issue here or articulated any clear "conditions" and following "consequences" for courts to apply in the absence of implementing regulations. Pet. App. 12a. Rather, unlike Section 954(d)(2), each of them used imperative language to expressly condition a provision's operation on agency regulations and otherwise lacked any judicially administrable standard.[6]

c. Petitioners also contend (Pet. 26) that the decision below conflicts with "bedrock principles of administrative law," *viz.*, that courts must review administrative actions based on the grounds given by the agency, and that agencies are bound by their own regulations. Neither of those principles was violated here.

As an initial matter, the first cited principle does not apply to tax-deficiency proceedings at all. Under *SEC* v. *Chenery Corp.*, 332 U.S. 194 (1947), "a reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to

[6] See *United Dominion Indus., Inc.* v. *United States*, 532 U.S. 822, 826 (2001) (26 U.S.C. 1501 provided that "[t]he making of a consolidated return *shall be upon the condition* that all corporations which * * * have been members of the affiliated group consent to all the consolidated return regulations prescribed under section 1502" (emphasis added)); *Good Samaritan Hosp.* v. *Shalala*, 508 U.S. 402, 405 (1993) (42 U.S.C. 1395x(v)(1)(A) provided that "[t]he reasonable cost of any services * * * *shall be determined in accordance with regulations* establishing the method or methods to be used" (emphasis added)); *Commissioner* v. *Portland Cement Co.*, 450 U.S. 156, 159 (1981) (26 U.S.C. 611(a) provided that a "reasonable allowance [for depletion in mineral investments] *in all cases* [*is*] *to be made under regulations* prescribed by the Secretary" (emphasis added)); *California Bankers Ass'n* v. *Shultz*, 416 U.S. 21, 64-66 (1974) (statute required domestic banks to report currency transactions "in such amounts, denominations, or both, or under such circumstances, *as the Secretary shall by regulation prescribe*," Act of Oct. 26, 1970, Pub. L. No. 91-508, § 221, 84 Stat. 1122 (emphasis added)).

make, must judge the propriety of such action solely by the grounds invoked by the agency." *Id.* at 196. But here, there is no "determination or judgment which an administrative agency alone is authorized to make," *ibid.*, because the non-Article-III Tax Court redetermines the IRS's tax-deficiency determinations de novo, see *Dobson* v. *Commissioner*, 320 U.S. 489, 501 (1943); 26 U.S.C. 6214(a). And "[b]ecause the tax court is not critiquing the Commissioner's deficiency determination, there is no agency decision to review, and *Chenery* is therefore inapplicable." *Estate of Streightoff* v. *Commissioner*, 954 F.3d 713, 720 (5th Cir. 2020); accord *QinetiQ US Holdings, Inc.* v. *Commissioner*, 845 F.3d 555, 560 (4th Cir.) (explaining that "the Code's provisions for de novo review in the tax court permit consideration of new evidence and new issues not presented at the agency level"), cert. denied, 138 S. Ct. 299 (2017); *Ax* v. *Commissioner*, 146 T.C. 153, 159-160 (2016) (explaining that the *Chenery* principle does not apply in tax-deficiency proceedings).

In any event, the court of appeals' application of Section 954(d)(2)'s terms was consistent with the IRS's deficiency determinations and with the Tax Court's deficiency redetermination, both of which also relied on Section 954(d). The IRS's deficiency notices stated that the Whirlpool consolidated group had a "subpart F inclusion under [26 U.S.C.] 951(a) and 954(d)" because it engaged in "transactions giving rise to foreign base company sales income under [Section] 954(d)." C.A. App. 42, 81. And the Tax Court resolved the case based on Section 954(d)(2)'s "bare text," before reaching the same result as an alternative holding under the regulations. Pet. App. 73a. Accordingly, petitioners are incorrect that the court of appeals allowed the IRS to "collect

[a] tax based on a theory different from the one on which it relied in imposing the tax." Pet. 15. And petitioners' "fair notice" concerns are misplaced because they had ample opportunity to "brief and argue [their] case under the statute" in both the Tax Court and the court of appeals. Pet. 28-29.

Petitioners' contention (Pet. 26-28) that the IRS failed to follow the regulations is likewise unfounded. The IRS relied on both the statute and the regulations in arguing that the income at issue qualifies as FBCSI. See, *e.g.*, C.A. App. 2555 (summary-judgment motion arguing that "[s]ection 954(d)(2) and the regulations thereunder * * * prevent taxpayers from circumventing the FBCSI rules by separating manufacturing and sales income through use of a branch"). Petitioners' suggestion (Pet. 27-28) that "the income at issue is *not* FBCSI under the regulations" rests exclusively on Judge Nalbandian's dissent—which adopted a novel reading of those regulations that petitioners did not even press below.[7] The IRS, however, read the regulations differently than did Judge Nalbandian. It applied them accordingly, and the Tax Court agreed with the IRS's reading. Pet. App. 78-79a & n.11.

2. Petitioners concede (Pet. 33) that there is no "circuit conflict on the meaning of [Section] 954(d)(2)." Indeed, petitioners cite no other court of appeals decision even interpreting Section 954(d)(2). To the extent the Court were ever inclined to review the question

[7] Whereas Judge Nalbandian's dissent concluded that Lux itself qualified for the manufacturing exception, Pet. App. 36a-38a, petitioners argued below that "the only potential 'sale' was by the Mexican [manufacturing] branch," and that the Mexican branch qualified for "the manufacturing exception," Pet. 14 (describing the argument).

presented, such review would be premature at this time given the absence of lower-court consideration of that question.

Though not in the context of Section 954(d)(2), other courts of appeals have addressed the general interaction between tax statutes and regulations, and those decisions accord with the decision below. Contra Pet. 33 (contending that the decision below "creates two different tax regimes"). For instance, in *Pittway Corp.* v. *United States*, 102 F.3d 932 (1996), the Seventh Circuit considered a provision stating that "[u]nder regulations prescribed by the Secretary, methane or butane shall be treated as a taxable chemical." 26 U.S.C. 4662(b)(1). The Secretary had never issued regulations implementing that provision, but the Seventh Circuit nonetheless held that the statutory "language directs us to a single conclusion: that [the petitioner], as the user of the butane, is the manufacturer responsible for the excise tax imposed on the butane." *Pittway*, 102 F.3d at 936. "Even if there were regulations," the court observed, "we would have to question them if they suggested a different result." *Ibid.*; accord Pet. App. 18a ("[T]he agency's regulations can only implement the statute's commands, not vary from them.").

Similarly, in *Temsco Helicopters, Inc.* v. *United States*, 409 Fed. Appx. 64 (2010), the Ninth Circuit considered a statute providing that, "if the Transportation Tax is not collected from the purchaser, 'under regulations prescribed by the Secretary,' the carrier shall pay the tax to the government." *Id.* at 67 (quoting 26 U.S.C. 4263(c)). The Secretary had never prescribed regulations implementing that provision, but the Ninth Circuit still affirmed the imposition of a tax based on the statute's "straightforward requirement," noting that "[t]he language of the statute and its legislative history do not establish that regulations are a precondition." *Ibid.*

3. Petitioners incorrectly claim (Pet. 29) that this case raises issues of "exceptional importance."

a. Petitioners principally submit (Pet. 30, 33) that many taxpayers have relied on the Treasury Department's Section 954(d)(2) regulations, and they will now face "great uncertainty" about whether those regulations apply. The amici supporting petitioners echo that submission. See Nat'l Ass'n of Mfrs. Amicus Br. 14-20; PricewaterhouseCoopers et al. Amici Br. et al. 7-9; Silicon Valley Tax Dirs. Grp. et al. Amici Br. 9-16. But the court of appeals did not question the validity of the regulations. Nor did it suggest that they will not govern many (or even most) cases. To the contrary, the court expressly recognized that the agency can use regulations to "implement the statute's commands" while simply observing that the regulations may not "vary from" those commands. Pet. App. 18a. That principle could not have surprised taxpayers, because this Court has long held that agency regulations may not "alter the clearly expressed intent of Congress." *Board of Governors* v. *Dimension Fin. Corp.*, 474 U.S. 361, 368 (1986).

Petitioners' narrower concern (Pet. 31) about the effect of the decision below on "maquiladora companies, and branch structures like those at issue in this case," is also unfounded. Although the former version of the regulations applies in this case, Pet. App. 57a, the current regulations—which took effect after the 2009 tax year began—remove any doubt that may have been raised by the dissent below about whether the sales income produced by such a branch structure counts as the CFC's FBCSI, see pp. 4-5, *supra*; Pet. App. 37a n.5 (Nalbandian, J., dissenting) (observing that "the new regulations covering FBCSI contain the language the Commissioner tries to read into the old regulations") (emphasis omitted). The resolution of this case therefore lacks prospective importance for taxpayers who use branch structures like the one here.

b. Resolving the question presented will not even make a difference in petitioners' own case, which arises under the now-obsolete former regulations. As the Tax Court's thorough opinion shows, the 2009 income at issue is FBCSI even under the former version of the regulations. See Pet. App. 73a-85a. The former regulations state that FBCSI "does not include income of a [CFC] derived in connection with the sale of personal property manufactured * * * by *such corporation* in whole or in part from personal property which it has purchased." 26 C.F.R. 1.954-3(a)(4)(i) (2009) (emphasis added). As petitioners observe, that provision excluded from FBCSI the "income that a foreign subsidiary earns from selling goods that it manufactures *itself*." Pet. 6 (emphasis added). Here, Lux is the relevant CFC, so income that Lux derived from selling personal property manufactured *by Lux itself* would not count as FBCSI. But Lux itself engaged in no manufacturing: It had only one part-time administrative employee and relied on WIN to produce appliances in Mexico. See p. 6, *supra*. So Lux cannot qualify for the manufacturing exception, and its sales income was therefore FBCSI under the former version of the regulations.

That result is confirmed by Example 2 in the former regulations. See 26 C.F.R. 1.954-3(b)(4) (2009). That example contemplates a CFC (here, Lux) being "incorporated under the laws of foreign country X" (here, Luxembourg) and maintaining a branch (here, WIN) in "foreign country Y" (here, Mexico). *Ibid.* The branch "manufactures articles in country Y which are sold through the sales offices of [the CFC] located in country X." *Ibid.* Under Example 2, "[i]ncome derived by [the CFC] * * * from the sale * * * outside country X of the personal property produced in country Y * * * constitutes foreign base company sales income." *Ibid.* Applying that logic here, the income Lux derived from selling appliances produced by WIN constitutes FBCSI.[8]

Judge Nalbandian's contrary reading (Pet. App. 36a-39a) of the former regulations is flawed. His dissenting opinion relies heavily on "passive language" (*id.* at 38a) in the former regulations, but that passive language speaks principally to the circumstances under which property will be deemed to be "manufactured, produced, or constructed"—specifically, when "the property sold is in effect not the property which [the foreign corporation] purchased," *id.* at 98a. That passive language does not answer the question of *which entity* must do the manufacturing, producing, or constructing to qualify for the manufacturing exception. Only the first sentence in the former regulations' manufacturing exception answers that question, making clear that the manufacturing activities must be performed "by such corporation"—*i.e.*, by the CFC itself. 26 C.F.R.

[8] The government's reading of the former regulations has also been adopted by tax commentators, including one cited in Judge Nalbandian's dissent, Pet. App. 34a. See, *e.g.*, Mary F. Voce, *Foreign Base Company Sales Income: A Primer and an Update*, 53 Tax Law. 327, 338 (2000) (observing that "the Manufacturing Exception applies only if the *same* corporation that is doing the selling also does the manufacturing"); 3 Boris I. Bittker & Lawrence Lokken, *Federal Taxation of Income, Estates and Gifts* ¶ 69.5.5, at 69-47 (rev. 3d ed. 2005) (illustrating that only the manufacturing branch, not the selling CFC, may claim the manufacturing exception).

1.954-3(a)(4)(i) (2009). The dissent also fails even to mention—let alone explain away—Example 2 and its clear application to the facts of this case. And the dissent's construction of the former regulations would have rendered Section 954(d)(2) largely toothless while those regulations were in effect. That is because transactions under Section 954(d)(2) frequently involve manufacturing performed by either the CFC or its branch, so allowing both entities to claim the manufacturing exception (as the dissent would) means that Section 954(d)(2) transactions would rarely result in FBCSI.

Yet even if the former regulations had to be applied and Judge Nalbandian's construction of those regulations were correct, that would not still not suffice to support a final judgment in petitioners' favor. As he recognized, there is "[a]t the very least, * * * a question of fact over whether LUX 'manufactured' the appliances," which would require resolution on remand. Pet. App. 39a. Similarly, the Tax Court reserved the question whether Lux's income qualifies as FBCSI under Section 954(d)(1), citing "factual uncertainties" on that issue. *Id.* at 66a. The question presented is therefore not even "outcome-determinative" (Pet. 2) in petitioners' own case.

c. Petitioners also claim (Pet. 32) that the decision below "has serious implications for other statutory and regulatory schemes" involving "'under regulations' language." See Pet. 5. As explained above, however, the court of appeals established no categorical rule about which statutes referencing agency regulations are self-executing. See pp. 14-16, *supra*. It held merely that Section 954(d)(2) is self-executing because it prescribes clear conditions, with consequences, that courts may apply. See Pet. App. 18a. At the same time, the court of appeals recognized that Section 954(d)(2) gives agency regulations a role in *implementing* the provision's commands. *Ibid.* Because the court's rationale turns on Section 954(d)(2)'s particular language, the decision below is unlikely to have consequences for other statutes.

4. Finally, this case is an unsuitable vehicle for considering the question presented because petitioners failed to adequately raise their current argument in the court of appeals. Although the Tax Court issued alternative holdings under Section 954(d)(2) and the Treasury Department's regulations, petitioners did not argue at the panel stage that the Tax Court erred by engaging in any independent statutory analysis at all. See p. 10, *supra*. Rather, petitioners argued that the Tax Court misapplied the regulations and that those regulations were invalid. See Pet. C.A. Br. 27-48. They did not press their current argument until their rehearing petition. See Pet. C.A. Reh'g Pet. 9. If the question presented were ever to warrant review, a case where the petitioner squarely raised the question in the court of appeals would provide a more suitable vehicle.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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