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Thomas D. Bettge

Mark R. Martin

Hans Gerling

Thomas D. Bettge is a senior manager in the economic and valuation services group of the Washington National Tax (WNT) practice of KPMG LLP, Mark R. Martin is a principal in charge of the WNT economic and valuation services group as well as the WNT tax controversy and dispute resolution group, and Hans Gerling is a managing director in the WNT tax controversy and dispute resolution group.

In this article, the authors consider how the Supreme Court's decision in *Loper Bright* may affect the application of section 482, the first sentence of which serves as the basis for the entire U.S. transfer pricing system but does not squarely address one of *Loper Bright*'s guardrails — the question of delegation.



Transfer pricing practitioners spend so much time immersed in Treasury regulations that they can be forgiven for overlooking just how strange the underlying statute is. Consider that the first and original sentence of section 482 does not mention the arm's-length standard. It does not mention transfer pricing; it does not mention pricing at all, or intercompany transactions. It does not mention the hundreds of pages of regulations that transform it from a broad antiabuse power into a set of (mostly) coherent rules by which taxpayers arrange, and tax examiners police, intercompany relationships.

It says, in essence, that if two or more parties are subject to common control, the IRS "may distribute, apportion, or allocate gross income, deductions, credits, or allowances" if "necessary in order to prevent evasion of taxes or clearly to reflect the income of any of" those parties. To be sure, the statute has been amended, although only in a piecemeal fashion. The Tax Reform Act of 1986 added a second sentence, and the Tax Cuts and Jobs Act of 2017 added a third,[1] but both by their terms are restricted to transactions involving intangibles. This article focuses solely on the first sentence of section 482 — the basis for the entire U.S. transfer pricing system.

Tax certainty is an important goal. For all the work that goes into designing and improving tools to prevent and resolve disputes, the foremost source of certainty in tax matters is clear rules. We proceed from the assumption that, despite occasional governmental overreach, having reliable transfer pricing regulations is a good thing for just about everyone. *Loper Bright* has eliminated *Chevron* deference — which, despite a proliferation of exceptions and preliminaries, embraced a relatively simple two-step framework[2]

[1] Tax Reform Act of 1986, section 1231(e); TCJA, section 14221(b)(2).

[2] For discussion of judicial deference to agency action before *Loper Bright*, see Thomas D. Bettge, "Administrative Law Basics for Transfer Pricing Practitioners," *Tax Notes Federal*, Nov. 28, 2022, p. 1233.

— with a new framework that remains to be fully fleshed out.[3] At least for a while, we will be living in a less certain world. The crucial question is, once the dust settles, does section 482 have a *Loper Bright* problem?

## Delegation vs. Deference

Ascertaining the effect of *Loper Bright* is difficult because the Supreme Court, in eliminating *Chevron*, did not eliminate the possibility that an agency regulation may control — rather than simply inform — the outcome of a case. The Court said that "courts must exercise independent judgment in determining the meaning of statutory provisions" without deferring to agencies.[4] However, it acknowledged that in some cases, "the statute's meaning may well be that the agency is authorized to exercise a degree of discretion."[5]

In that case, under *Loper*, a court would not defer to the agency — it would, after all, be using its own judgment and expertise in statutory interpretation to discern that agency discretion was intended — but it would recognize and give effect to the intended delegation of discretionary authority subject to certain guardrails. In particular, courts will have to fulfill that role "by recognizing constitutional delegations, fixing the boundaries of the delegated authority . . . and ensuring the agency has engaged in reasoned decisionmaking within those boundaries."[6]

The first of these guardrails should not limit rulemaking under section 482. The constitutionality of the statute has already been challenged under the nondelegation doctrine without success. The Tax Court in *Foster* considered the contention that "section 482 is unconstitutional because it purports to vest in the Commissioner the discretion to disregard the statutory structure established by Congress for the taxation of corporations without setting forth a meaningful standard to guide him in the exercise of that discretion," and held that:

> Contrary to petitioners' apparent belief, section 482 does not delegate authority to respondent to reallocate income at his whim. Rather, he may do so only if he first determines that such reallocation is "necessary in order to prevent evasion of taxes or clearly to reflect the income" of two or more commonly owned or commonly controlled organizations, trades, or businesses. We think this is a meaningful standard.[7]

The third guardrail, reasoned decision-making, simply reiterates the need for Treasury to comply with background principles of administrative law. That can be problematic for section 482 regulations (witness the Tax Court's opinion in *Altera*[8]) but in ways that are dependent on the specific process behind each separate regulatory action and hence are outside the scope of this article.

The second guardrail — the need for the court to "fix the boundaries of the delegated authority" — is more novel. Because it seems to apply to the statutory delegation as a whole and thus to every regulation promulgated under that delegation, it is in a certain sense the most important of the *Loper Bright* guardrails once the low constitutional hurdle is cleared. We will consider what exactly the boundaries of a section 482 delegation might be — but first, we address a more basic question: Is there a delegation at all? Others have thoughtfully addressed this;[9] the problem is that they do not agree on the answer. Below we summarize a few of the arguments for and against a delegation in section 482. We leave to others the

[3] *Loper Bright Enterprises v. Raimondo*, 603 U.S. 369 (2024) (eliminating the deference framework established by *Chevron U.S.A. Inc. v. Natural Resources Defense Council Inc.*, 467 U.S. 837, 842 (1984)).

[4] *Loper Bright*, 603 U.S. at 395.

[5] *Loper Bright*, 603 U.S. at 395.

[6] *Loper Bright*, 603 U.S. at 372.

[7] *Foster v. Commissioner*, 80 T.C. 34, 141 (1983), *aff'd in part and vacated in part*, 756 F.2d 1430 (9th Cir. 1985). The Ninth Circuit did not disturb the Tax Court's holding on the constitutional issue. A prior constitutional challenge, *Asiatic Petroleum Co. v. Commissioner*, 79 F.2d 234 (2d Cir. 1935), *aff'g* 31 B.T.A. 1152 (1935), challenged then-section 45 — *i.e.*, the first sentence of present section 482 — on the grounds that it permitted a deprivation of property without due process. The taxpayer in that case was also unsuccessful.

[8] *Altera Corp. v. Commissioner*, 145 T.C. 91, 133 (2015) ("Because the final rule lacks a basis in fact, Treasury failed to rationally connect the choice it made with the facts found, Treasury failed to respond to significant comments when it issued the final rule, and Treasury's conclusion that the final rule is consistent with the arm's-length standard is contrary to all of the evidence before it, we conclude that the final rule fails to satisfy *State Farm*'s reasoned decisionmaking standard and therefore is invalid."), *rev'd*, 926 F.3d 1061 (9th Cir. 2019).

[9] *See, e.g.*, Ryan Finley, "Does *Chevron*'s Demise Matter in Transfer Pricing?" *Tax Notes Federal*, July 15, 2024, p. 401; Reuven S. Avi-Yonah, "Tax Delegation After *Loper Bright*," *Tax Notes Federal*, Oct. 7, 2024, p. 109.

question of whether section 7805's blanket authorization for regulations is a panacea or a nullity.

### Delegation: Arguments Against

*Loper Bright* seeks to give effect to "the command of the [Administrative Procedure Act] that 'the reviewing court' — not the agency whose action it reviews — is to 'decide *all* relevant questions of law' and 'interpret . . . statutory provisions'" (emphasis and ellipsis in original).[10] If the inquiry is to begin and end with the statute, the question seems a simple one — section 482 contains no delegation within the meaning of *Loper Bright*.

To be sure, section 482 delegates something, but what it delegates is enforcement discretion, not rulemaking authority. Where the text of section 1502 — another sparse provision fleshed out by mountains of regulations — directs the secretary of the Treasury to "prescribe such regulations as he may deem necessary," section 482 says nothing whatsoever about regulations; it merely authorizes the IRS to "distribute, apportion, or allocate" in appropriate cases. To be sure, the opinion in *Loper Bright* speaks of statutes "delegate[ing] discretionary authority" to an agency,[11] but from the context it is clear that the authority delegated must be the authority to fill in the statute's meaning (this is, after all, a regulatory validity standard) rather than merely the authority to exercise discretion in enforcing it. The government cannot bootstrap its way to regulatory deference simply because section 482 adjustments are reviewed for an abuse of discretion.

In fact, section 482 does not require regulations to operate. Its predecessor, section 45, was enacted as part of the Revenue Act of 1928 against a backdrop of earlier provisions authorizing the IRS to consolidate the accounts of related parties when needed to accurately reflect income and other tax items.[12] Regulations were issued under the 1928 act, but they merely restated the provisions of section 45 and hence were entirely tautological.[13] The first substantive transfer pricing regulations — and with them the arm's length standard — did not arrive until 1935.[14] Even then, the regulations spanned only about two pages and provided no methodological guidance concerning the determination of an arm's-length price.

For almost a decade, what is now the first sentence of section 482 operated without the regulatory substratum to which we have grown accustomed. This did not hamstring the IRS; the most prominent early case — *Asiatic Petroleum*[15] — shows how the IRS could effectively wield section 45 without regulations. There, the taxpayer sold stock to a foreign affiliate for an amount equal to its cost basis, and the foreign affiliate later sold the stock to a third party for a substantial gain. The Board of Tax Appeals and the Second Circuit upheld an adjustment allocating the gain realized to the taxpayer. Regulations, in short, were neither expressly contemplated by the statute nor required by the IRS.

### Delegation: Arguments in Favor

Looking at the early history of section 482 is all well and good, but if *Asiatic Petroleum* illustrates how the statute could operate without regulations, it also illustrates how dramatically different that sort of enforcement was from actual transfer pricing — a concept that today appears synonymous with section 482. The evolution of section 482 into a primarily pricing- and valuation-based enforcement mechanism took place through regulations, to be sure; what is perhaps less appreciated is that it also took place with the prodding and assent of Congress. A broader consideration of section 482 as it exists today and the inflection points at which Congress has considered and interacted with the statute during its long history shows that Congress intends for today's statute to operate through regulations.

[10] *Loper Bright*, 603 U.S. at 399 (quoting 28 U.S.C. section 706).

[11] *Loper Bright*, 603 U.S. at 372.

[12] The 1928 enactment was substantially identical to the first sentence of current section 482, with only minor differences.

[13] Reg. 74, art. 355, section 45.

[14] Reg. 86, art. 45 (1935).

[15] *Asiatic Petroleum*, 31 B.T.A. 1152, *aff'd*, 79 F.2d 234, *cert. denied*, 296 U.S. 645 (1935).

In 1962 the House passed a bill that would have added a formulary backstop to section 482 because "the difficulties in determining a fair price under this provision severely limit the usefulness of this power especially where there are thousands of different transactions engaged in between a domestic company and its foreign subsidiary."[16] The Senate did not adopt an analogous provision, and the conference committee demurred:

> The conferees on the part of both the House and the Senate believe that the objectives of section 6 of the bill as passed by the House can be accomplished by amendment of the regulations under present section 482. Section 482 already contains broad authority to the Secretary of the Treasury or his delegate to allocate income and deductions. It is believed that the Treasury should explore the possibility of developing and promulgating regulations under this authority which would provide additional guidelines and formulas for the allocation of income and deductions in cases involving foreign income.[17]

Arm's-length transfer pricing carried the day and Treasury took the hint, issuing final regulations in 1968. This marked the first substantive departure from the cursory 1935 regulations, and the first set of regulations to provide methodological transfer pricing guidance.

That worked well enough for a time. In 1986 Congress revisited section 482. This time it altered the statute, adding a second sentence containing the commensurate with income standard for transfers and licenses of intangibles.[18] Once again, the conference committee expressed a desire for updates to the regulations:

> The conferees are also aware that many important and difficult issues under section 482 are left unresolved by this legislation. The conferees believe that a comprehensive study of intercompany pricing rules by the Internal Revenue Service should be conducted and that careful consideration should be given to whether the existing regulations could be modified in any respect.[19]

Treasury undertook that study and released its white paper in 1988[20] which in turn led to new proposed regulations in 1992, temporary regulations in 1993, and final regulations in 1994.

In the meantime, Congress had acted again. After the fumbled initial adoption of transfer pricing penalties in 1990, it revamped the penalty regime in 1993.[21] In doing so, Congress removed the standard reasonable cause and good-faith defense, making penalty protection contingent on the preparation of documentation that (among other things) shows either that the taxpayer determined its transfer price "in accordance with a specific pricing method set forth in the regulations prescribed under section 482,"[22] or that "none of such pricing methods was likely to result in a price that would clearly reflect income."[23] Despite the absence of a specific mention in section 482 itself, the section 482 regulations are integral to the statutory framework of section 6662(e).

In 2017 Congress amended section 482 once again, adding the third sentence concerning the use of realistic alternatives and aggregate approaches for transactions involving intangibles. There is more legislative history displaying awareness that section 482 is administered through extensive regulations,[24] but perhaps more importantly there is another statutory enactment that directly depends on those regulations:

[16] H.R. Rep. No. 87-1447 at 28 (1962).

[17] H. Conf. Rep. 87-2508 at 18-19 (1962).

[18] Tax Reform Act of 1986, section 1231(e).

[19] H. Conf. Rep. 99-841 at II-638 (1986).

[20] Notice 88-123, 1988-2 C.B. 458.

[21] Omnibus Budget Reconciliation Act of 1993, section 13236. For additional discussion, see Mark J. Horowitz et al., "The Resurgence of Transfer Pricing Penalties," *Tax Notes Federal*, Jan. 8, 2024, p. 311.

[22] Section 6662(e)(3)(B)(i)(I).

[23] Section 6662(e)(3)(B)(ii)(I).

[24] *E.g.*, H. Conf. Rep. 115-466 at 574 (2017) ("Section 482 authorizes the Secretary of the Treasury to allocate income, deductions, credits, or allowances among related business entities when necessary to clearly reflect income or otherwise prevent tax avoidance, and comprehensive Treasury regulations under that section adopt the arm's-length standard as the method for determining whether allocations are appropriate.").

Section 59A exempts a payment from classification as a base erosion payment (to the extent of total services cost) if the payment is made for "services which meet the requirements for eligibility for use of the services cost method under section 482" apart from the business judgment rule.[25] The services cost method and the total services cost concept are nowhere to be found in the text of section 482 — they are creatures of reg. section 1.482-9.

## Boundaries

It is unclear whether section 482 should be understood as containing a delegation of rulemaking authority, but it is clear — we hope — that there are plausible arguments to be made on both sides. Ultimately, the answer may depend on whether a judge is an originalist in matters of statutory construction. It is therefore important to explore what "the boundaries of the delegated authority"[26] are in the event any such authority exists. If there is no delegation, it is similarly important to consider what boundaries exist within the statute itself.

For both of those inquiries, it is significant that while section 482 may have begun life back in 1928 as a nearly blank check granting enforcement authority to the IRS, that check has not stayed blank. The subsequent legislative developments summarized above all evince Congress's intent that the arm's-length standard be the lodestar for the first sentence of section 482. The defeat of a formulary approach in 1962 is an endorsement of arm's-length pricing. As for the 1986 amendment, Treasury explained in its 1988 white paper that "the commensurate with income standard is consistent with arm's length principles,"[27] but even if one were to disagree with this — something the government has flirted with in litigating positions — it would still be the case that the first sentence of section 482 remains dedicated to arm's-length pricing.[28] In enacting the penalty regime that it selected, Congress endorsed not only the arm's-length standard but also the methods-based approach taken by the regulations.

If those legislative actions are enough to breathe a colorable delegation into section 482, by the same token they should be enough to establish the arm's-length standard as an outer boundary for that delegation. Congress has expressed its wish that Treasury promulgate regulations under section 482 but only in furtherance of the fundamental arm's-length approach. If these actions do not rise to the level of a delegation, they nonetheless remain probative of how Congress intends that section 482 should operate.

In *Xilinx*, the Ninth Circuit upheld the arm's-length standard when in conflict with the specific requirement that stock-based compensation costs be shared; in doing so, it relied not only on the broad language of reg. section 1.482-1(b)(1)[29] but on the purpose of the regulations (and of the statute[30]). That is, to provide "parity between taxpayers in uncontrolled transactions and taxpayers in controlled transactions. The regulations are not to be construed to stultify that purpose."[31] Despite its absence from the face of the statute, there is good reason to believe the arm's-length standard is baked into section 482.

That is not to say the text of section 482 is without boundaries of its own. Its grant of enforcement discretion is tethered to a clear purpose: the prevention of tax evasion and the clear reflection of income. This provides a boundary marker beyond which the IRS's authority under section 482 cannot extend. Income and its clear reflection are not just words — they anchor section 482 in section 61 and the

[25] Section 59A(d)(5).

[26] *Loper Bright*, 603 U.S. at 372 (omitting alteration in original).

[27] Notice 88-123. For discussion of the consistency of the commensurate with income and arm's-length standards, see Mark R. Martin and Horowitz, "*Medtronic v. Commissioner*: A Taxpayer Win on Transfer Pricing, Commensurate With Income and Section 367 Issues," 45 *Tax Mgmt. Int'l J.* 651 (Nov. 11, 2016).

[28] *See also* AM 2025-001.

[29] Reg. section 1.482-1(b)(1) ("In determining the true taxable income of a controlled taxpayer, the standard to be applied in every case is that of a taxpayer dealing at arm's length with an uncontrolled taxpayer.").

[30] *See Commissioner v. First Security Bank of Utah*, 405 U.S. 394, 407 (1972) ("As stated in the Treasury Regulations, the 'purpose of section 482 is to place a controlled taxpayer on a tax parity with an uncontrolled taxpayer.'").

[31] *Xilinx Inc. v. Commissioner*, 598 F.3d 1191, 1196 (9th Cir. 2010).

judicial elaboration of what precisely constitutes income for purposes of the income tax. The Supreme Court articulated this connection in *First Security*,[32] and the Tax Court plurality in *3M* recognized this while failing to see its significance:

> Significantly the initial passage in *First Security Bank* involved the interpretation of the predecessors of section 61, not the predecessors of section 482. First, the principle identified in the initial passage was an application of the proposition that the income that is subject to a man's unfettered command and that he is free to enjoy at his own option may be taxed to him as his income. This proposition is a judicial interpretation of section 61 and its predecessors. Second, the initial passage also explained that the assignment-of-income doctrine concerned situations in which a taxpayer was taxed on income over which the taxpayer had control. The assignment-of-income doctrine too is an interpretation of the predecessors of section 61, not the predecessors of section 482. Indeed, the cases cited in the initial passage as examples of the application of the assignment-of-income doctrine were resolved under the predecessors of section 61, not the predecessors of section 482.[33]

In the view of the *3M* plurality, the happy circumstance that a separate code section was also at issue made *First Security*'s holding on the nature of income irrelevant, "the ultimate question in *Commissioner v. First Sec. Bank* involved respondent's authority under the predecessors of section 482, not section 61."[34] Yet the clear reflection of income language explicitly roots section 482 — and whatever discretion the IRS enjoys thereunder — in income and thus in section 61. If something cannot constitute income under section 61 — and the Court held in *First Security* that blocked income does not — then section 482 cannot authorize the IRS to mandate its inclusion in taxable income. However broad the grant under section 482, it has an explicit statutory tether separate from the indwelling arm's-length standard.

## At Stake

The foregoing discussion shows some of the possibilities for how courts may read section 482 under *Loper Bright* — and because statutory interpretation will proceed court by court, there is real potential for conceptual chaos. But other than headaches, what practically speaking is at stake here?

The recent and ongoing challenges to the blocked income rules and the regulations' treatment of stock-based compensation are well-known, obvious examples. Other provisions have not drawn prior challenges but can be difficult to square with the statutory text. Some provisions, for instance, add a prescriptive edge that departs from the regulations' basic approach of identifying the best method and arriving at the most reliable result; others impose unreasonably high hurdles for taking relevant factors into account. The market share strategy rules of reg. section 1.482-1(d)(4)(i) belong in the latter category alongside the blocked income rules of reg. section 1.482-1(h)(2).

Other issues can be less obvious and more troubling. The road to section 482 as we know it today is paved with the gravestones of issues, once pressing, that now appear quaint to the extent they appear at all. If *Loper Bright* throws the section 482 regulations back into the uncertain world of *Skidmore* deference,[35] who is to say what unexpected revenants will emerge?

## Conclusion

For a decision that prided itself on dispensing with the "byzantine set of preconditions and exceptions" that prevailed under *Chevron*,[36] *Loper Bright*'s own framework hardly seems like a simplification. There are reasons to think that

[32] *First Security Bank*, 405 U.S. 394.

[33] *3M Co. v. Commissioner*, 160 T.C. 50, at 257-258 (2023) (footnotes, quotation marks, and citations omitted).

[34] *3M Co.* at 258 (citation omitted).

[35] *Loper Bright*, 603 U.S. at 477 (citing *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944)). As summarized in a prior article, "*Skidmore* provides that a court will defer to agency guidance to the extent it is persuasive. In effect, this is no deference at all: It requires the court to consider an agency interpretation, but nothing more." Bettge, *supra* note 2.

[36] *Loper Bright*, 603 U.S. at 406.

section 482 does not contain a delegation of interpretive authority, and then again, there are reasons to think that it does. There is the entirely separate question, not addressed in this article, of whether section 7805 could supply a delegation if none can be found in section 482. But delegation or not, there is good reason to regard the arm's-length standard as an overarching principle that should inform both courts' interpretations of section 482 and the limits of any regulatory authority thereunder.[37] ■



[37] The foregoing information is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the author(s) only and does not necessarily represent the views or professional advice of KPMG LLP.