

## **3M Ruling Highlights Loper Bright's Reach In Axing Tax Regs**

By **Natalie Olivo**

*Law360 (November 4, 2025, 6:15 PM EST)* -- A U.S. Supreme Court ruling that gutted deference to agencies took center stage in the Eighth Circuit's recent decision that backed 3M's challenge to transfer pricing rules, signaling the strict statutory analysis that courts may now apply to tax regulations.

An Eighth Circuit panel held last month that the Internal Revenue Service lacked the statutory authority to allocate nearly \$24 million in royalty payments that Minnesota-based multinational conglomerate 3M Co. said it was blocked from receiving under Brazilian law. In striking down transfer pricing regulations that underpinned the IRS' adjustment, the Eighth Circuit noted that "the legal landscape has changed" in light of the Supreme Court's June 2024 ruling in *Loper Bright Enterprises v. Raimondo*.

In *Loper Bright*, the high court's majority overruled *Chevron* deference, a 40-year-old doctrine that told judges to accept reasonable agency interpretations of ambiguous laws. *Chevron* deference was still in place when the U.S. Tax Court in February 2023 narrowly rejected 3M's challenge to the rules, which allow the IRS to ignore certain foreign legal restrictions when allocating payments from foreign affiliates.

Specialists say the Eighth Circuit's application of *Loper Bright* enabled the panel to eschew deference to the IRS and instead go straight to Internal Revenue Code Section 482, which dictates when the agency can transfer income within a corporate group. This approach could indicate how other courts may use a granular statutory lens as the main tool when scrutinizing tax regulations going forward.

According to Kevin Otero, a partner at Covington & Burling LLP, the Tax Court's decision was based in part on trying to sidestep what income means in Section 482 and letting the U.S. Treasury Department and IRS determine that. But the Eighth Circuit essentially said it knows what income means in certain contexts, and here it cannot mean blocked income.

"I think the critical aspect of the decision here is *Loper*, and invoking *Loper* in a way that substantially limited Treasury's ability to invoke a regulation under what it tried to say was a vague standard, at least at the Tax Court level," Otero said. "So I think *Loper* is pretty important."

### **The Loper Bright Analysis**

The justices held in *Loper Bright* that the *Chevron* court improperly prioritized the executive branch's legal interpretations over the judicial branch's. The decision handed a win to fishing industry groups, which had argued the National Marine Fisheries Service interpreted legislation too broadly when issuing

a 2018 rule requiring fishers to pay part of the cost of having federal compliance monitors aboard their ships.

The high court issued its ruling about a decade into 3M's litigation, which stemmed from the company's contention that a Brazilian tax law mandated fixed ceilings on royalty payments for trademarks and patents. Under this law, the royalty payments that could be allocated from the company's Brazilian affiliate were just under \$166,000, according to 3M, which claimed that the IRS in 2012 instead allocated nearly \$24 million from the affiliate by relying on what 3M argued were the invalid blocked income regulations.

According to the Eighth Circuit's Oct. 1 decision for 3M, Loper Bright frees courts to adopt the "best reading of the statute," or what the court would have reached if no agency were involved. The panel accordingly turned to the first sentence of Section 482, which says that the IRS can allocate income within a corporate group to "prevent evasion of taxes or clearly to reflect the income" of affiliates.

As the panel saw it, that definition of income didn't change in the second sentence of Section 482, which enables the IRS to allocate intercompany profits in ways that are "commensurate with the income" from intangibles when there are no comparable transactions between unrelated companies. Because 3M was blocked from receiving Brazilian royalty payments, "shifting income to 3M here would not 'clearly ... reflect [its] income,'" U.S. Circuit Judge David R. Stras wrote, citing the statute.

"The passage is dense, but the 'best reading' of it rules out what the IRS did here," Judge Stras said.

According to Crowell & Moring LLP partner S. Starling Marshall, Chevron deference had allowed the IRS to argue that it had clarified an ambiguous term in a statute.

"With that being set aside, we're going back to the more traditional methods of interpreting the statute," she said. "The IRS cannot ignore those statutory interpretation rules in making its argument."

### **Long-Standing Blocked Income Controversy**

As some see it, the blocked income rules were already vulnerable — as evidenced in part by the 9-8 Tax Court ruling that narrowly upheld them — but Loper Bright influenced how exactly the Eighth Circuit went about striking them down.

The Tax Court was divided in part on how to apply a 1972 Supreme Court decision that dealt with the topic of blocked income. In that decision, *Commissioner v. First Security Bank of Utah*, the high court ruled that the IRS couldn't allocate insurance commission income to two banks that were prohibited from receiving it under the National Bank Act.

According to Holland & Knight LLP partner Joshua Odintz, 3M had a stronger argument because of the First Security decision. But Loper Bright still provided "the easier path" to invalidate the blocked income rules, he said.

Similarly, Crowell & Moring associate Nicholas Roberti said the Eighth Circuit's decision to strike down the rules was not necessarily surprising, nor was its specific analysis.

"The fact that Judge Stras and the panel writ large focused on the statute itself and didn't pay too much attention to the IRS' interpretation of that statute, that's not a surprising analysis under Loper Bright,"

he said.

### **Possible Implications for Coca-Cola**

The Eighth Circuit's ruling raises questions about whether the Eleventh Circuit will apply a similar analysis to the same blocked income rules in Coca-Cola's long-running transfer pricing dispute with the IRS.

The Atlanta-based beverage giant's Brazilian income is only one portion of the company's challenge against its \$2.7 billion tax bill, which is before the appeals court. Tax Court Judge Albert Lauber in 2020 backed the IRS' method for pricing intangible assets that Coca-Cola licensed to several foreign affiliates, but he held off on addressing the company's Brazilian affiliate until the Tax Court ruled in the 3M case.

Following the Tax Court's decision against 3M, Judge Lauber in November 2023 sustained the agency's adjustment regarding Coca-Cola's Brazilian income. As part of his decision, he noted that the company's Brazilian affiliate could have legally paid dividends in lieu of royalties, meaning that the income was not actually blocked.

The Eighth Circuit's ruling for 3M did not directly address Coca-Cola's dispute, but the court did reject similar reasoning that the IRS offered in contending that 3M's Brazilian affiliate could have substituted dividends for royalties. According to the panel, this argument was "breathtaking in its potential reach" because under the agency's approach, a parent company could go as far as liquidating its subsidiary to get royalties it thinks should have been paid.

According to Clark Armitage, a member at Caplin & Drysdale Chtd., the court said that when it comes to blocked income, it's limited to that income item. The panel's view was that if a royalty is blocked, the focus is on that alone, and alternative methods for getting money back are irrelevant, he said.

"I think that the Eighth Circuit would have handled the Coke appeal in the same way it handled the 3M appeal," Armitage said.

### **Other Tax Rules on Potentially Unstable Ground**

The Eighth Circuit's decision has also put a new spotlight on other IRS regulations and policies that may get a closer look in the aftermath of Loper Bright.

Shortly after the Supreme Court issued its ruling, practitioners highlighted certain rules released under the 2017 Tax Cuts and Jobs Act as newly vulnerable in the wake of the high court's decision.

The tax overhaul bill spent less than two months in Congress, and often with limited legislative discussions during that time. Those circumstances have left room for companies to argue that Treasury's subsequent regulations don't always align with congressional intent.

Some challenges were successful even before Loper Bright. In March 2023, a Tennessee federal judge invalidated a rule that denied foreign tax credits on offshore income affected by a repatriation provision enacted under the TCJA. In the first ruling to strike down a TCJA regulation on substantive grounds, the judge sided with FedEx in concluding that the guidance contradicted the plain language of the law.

Two months after the Loper Bright decision, the Tax Court cited the high court's ruling when it invalidated another TCJA regulation that addressed an effective date mismatch under the statute in effort to prevent companies from claiming certain foreign income deductions. In siding with California-based medical device company Varian Medical Systems, the court held that "a plain reading of the statutory text" authorized the company to claim a deduction.

According to Crowell & Moring's Marshall, considering the speed at which the TCJA moved through Congress, even lawmakers would likely admit to the timing mismatch and other mistakes that Treasury had claimed it was fixing. But that's not what regulations are supposed to do, she said.

"They're supposed to implement and interpret, not fix things that were mistakenly passed," Marshall said. "And so I think there are some things in that scheme that might be vulnerable."

Beyond the TCJA, some practitioners have pointed to a generic legal advice memorandum, or GLAM, the IRS issued in January as another agency stance that may not pass muster under a Loper Bright analysis.

According to the GLAM, Section 482 — in particular, its "commensurate with income" language — authorizes the IRS to, on an ongoing basis, adjust the income associated with an intangible property transfer based on actual profits. The GLAM noted that pricing a transaction based solely on the information available at the time is not always the most reliable way to divide profits based on how unrelated parties would behave under the arm's-length principle.

As Caplin & Drysdale's Armitage saw it, there's nothing in Section 482 that says the IRS can ignore the statute of limitations for making assessments. Yet the GLAM says the agency can make periodic adjustments regarding transactions that took place years ago.

"I think it's very vulnerable," Armitage said of the GLAM. "And I think Loper Bright makes it more vulnerable."

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