

# TaxNewsFlash

## United States



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## Ninth Circuit reverses Tax Court, validity of cost-sharing arrangement regulations

The U.S. Court of Appeals for the Ninth Circuit today reversed a decision of the U.S. Tax Court, and the appeals court upheld the validity of the regulations under Code section 482 with respect to cost-sharing arrangements.

At issue was the validity of the Treasury regulations implementing section 482—the Code provision that provides for the allocation of income and deductions among related entities. Specifically, this case focused on Reg. section 1.482-7A(d)(2) that provides that related entities must share the cost of employee stock compensation in order for their cost-sharing arrangements to be classified as qualified cost-sharing arrangements. The Tax Court found this regulation was invalid under the Administrative Procedure Act.

The Ninth Circuit today reversed and held that:

- The IRS did not exceed the authority delegated by Congress under section 482.
- Section 482 does not speak directly to whether the Commissioner may require parties to a qualified cost-sharing arrangement (QCSA) to share employee stock compensation costs in order to receive the tax benefits associated with entering into a QCSA.
- Treasury reasonably interpreted section 482 as an authorization to require internal allocation methods in the QCSA context, provided that the costs and income allocated are proportionate to the economic activity of the related parties.
- The regulations were a reasonable method for achieving the results required by the statute and were afforded *Chevron* deference, and were not “arbitrary and capricious” under the Administrative Procedure Act.

The case is: *Altera Corp. v. Commissioner*, Nos. 16-70496 and 16-70497 (9<sup>th</sup> Cir. June 7, 2019). Read the Ninth Circuit’s [decision](#) [PDF 342 KB] (81 pages) that includes a dissenting opinion.

## Background

The Ninth Circuit in July 2018 reversed the 2015 decision of the Tax Court finding that the Treasury regulations—Reg. section 1.482-7A(d)(2) that requires related entities to share the cost of employee stock compensation in order for their cost-sharing arrangements to be classified as “qualified cost-sharing arrangements” and to avoid an IRS adjustment—were invalid. Then, in August 2018, the Ninth Circuit announced the withdrawal of the July 2018 decision “to allow time for the reconstituted panel to confer on this appeal.” Judge Reinhardt had fully participated in the July 2018 decision and formally concurred in the majority opinion prior to his death. The August 2018 order replaced him with Judge Graber. Read [TaxNewsFlash](#)

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