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Unanimous High Court Rules Against IRS in Tax Reporting Dispute

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WASHINGTON (CN) — A tax law known as the Anti-Injunction Act does not preclude companies from challenging IRS reporting requirements laid out in that law before they are enforced, the U.S. Supreme Court ruled unanimously Monday.

CIC Services, a consulting firm that specializes in captive insurance companies, sued the IRS after the agency issued new reporting requirements for certain types of transactions related to that industry. A provision known as rule 2016-66 makes specific insurance micro-transactions reportable to the feds, who can issue notices to companies forcing them to provide more information.

The 2016 regulation comes with the threat of financial penalties for violating the new mandate, which the company contends amounts to a violation of the Administrative Procedure Act, in part based on the lack of a public comment period.

The district court ruled the challenge was precluded by the Anti-Injunction Act, or, AIA, because the penalty for not complying with the reporting requirement qualifies as a tax. The Sixth Circuit affirmed and CIC appealed to the Supreme Court, which agreed to hear the case last year.

“Allowing CIC’s suit to proceed will not open the floodgates to pre-enforcement tax litigation,” Justice Elena Kagan, a Barack Obama appointee, wrote for the unanimous court.

“When taxpayers challenge ordinary taxes, assessed on earning income, or selling stock, or entering into a business transaction, the underlying activity is legal,” she added. “In that scenario, the Anti-Injunction Act will always bar pre-enforcement review.”

Kagan said what sets CIC’s case apart is that it targets neither a regulatory tax or revenue-raising scheme, instead challenging a reporting mandate that doesn’t count as a traditional tax and is therefore out of the AIA’s reach.

In a concurring opinion, Justice Brett Kavanaugh, a Donald Trump appointee, further clarified what the opinion means for taxpayers.

“Pre-enforcement suits challenging regulatory taxes or traditional revenue-raising taxes are still ordinarily barred by the Anti-Injunction Act,” he wrote. “But pre-enforcement suits challenging

regulations backed by tax penalties are ordinarily not barred, even though those suits, if successful, would necessarily preclude the collection or assessment of what the tax code refers to as a tax."

Attempts to reach counsel for CIC and representatives with the IRS were not returned by press time.

Ilya Shapiro, vice president of the libertarian Cato Institute, which filed an amicus brief in the case in support of CIC, praised the high court's ruling in an emailed statement, calling it a big win for taxpayers.

"Congress intended that all agencies' substantive regulations would be subject to such review under the APA, and it certainly didn't intend for the IRS to be immune from accountability before federal courts," he said, adding the opinion enforces the right to know the difference between a tax and a regulation before engaging in "costly compliance efforts."

Shapiro argued the lower court's now-void interpretation would have required a violation and levied penalties before a legal challenge could be filed.

"That can't be right, so kudos to the unanimous Supreme Court for giving taxpayers their day in court," he added.

Meanwhile, Bryan T. Camp, a professor at the Texas Tech University School of Law who authored an amicus brief in support of the IRS, said Kagan's "floodgates" assessment might be a bit overstated. He suggested there could be a flurry of new cases aiming to use Monday's ruling to skirt tax laws.

"At the very least we will now need to see lots of litigation (the flood) to see how broad this new exception really is or is not," he said in an email, stressing taxpayers will want to know "how far they can go" and the only way to find that out is by filing suit. (Parentheses in original.)

He added, "We should reasonably expect to see a wave of pre-enforcement challenges, each of which will be claiming to be attacking a 'regulatory mandate' the restraint of which will not restrain the assessment or collection of tax."