Section 179D Deduction for Energy Efficient Commercial Building Property: IRS Attacks Allocations as Part of Compliance Campaign

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Taxpayers yearn for certainty, as they need it to make informed, intelligent decisions about tax-related issues. Unfortunately, doubt has arisen recently in connection with Section 179D, a provision that incentivizes taxpayers to make commercial buildings more energy efficient. This unsettled state of affairs can be attributed to various factors, including the attempt by the U.S. Internal Revenue Service ("IRS") to disregard its long-standing guidance directly on point.

This article provides an overview of Section 179D, identifies the related Compliance Campaign, explains the IRS[esq]s aggressive position about allocation of the Section 179D deduction in situations involving government-owned buildings, and analyzes authorities that counter the IRS's position.

Overview of Section 179D

Congress enacted the Energy and Policy Act of 2005, which was a broad energy research and development program.[1] The law featured a long list of new energy-related tax incentives. Among them was a special deduction in Section 179D for expenses incurred by taxpayers in connection with the installation of energy efficient commercial building property ("EECBP").[2] This provision contemplated unique allocation rules for Section 179D deductions linked to public property, but Congress did not have all the specifics at the outset. Therefore, it tasked the IRS with working out the details. Specifically, Section 179D(d)(4) states that, in the case of EECBP in-

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stalled on or in property owned by a federal, state or local government, the IRS "*shall promulgate a regulation* to allow the allocation of the deduction *to the person primarily responsible for designing* the [EECBP] in lieu of the owner of such property."[3]

This seems straightforward enough, but problems have arisen. Why? Well, despite the clear congressional mandate from way back in 2005, the IRS has never issued any proposed, temporary or final regulations regarding Section 179D. Indeed, based on the Priority Guidance Plans published by the Treasury Department annually, the IRS never planned to issue regulations, and never devoted resources to the matter after 2012.[4] Instead of going to the effort to formulate regulations and comply with the normal public-notice-and-comment requirements, the IRS released what it called "interim guidance" in the form of three Notices.[5] One of them, Notice 2008-40, addresses Section 179D(d)(4) in detail. It is the focus of this article.[6]

Compliance Campaign

After Congress creates a benefit, the IRS often starts to suspect that certain taxpayers are engaged in wrongdoing, deriving an advantage to which they are not entitled. This is what happened with Section 179D. The IRS initiated a Compliance Campaign in November 2017 directed at Section 179D(d)(4) and allocation of the deduction in situations involving government-owned buildings. The IRS's website says as much.[7]

Authorities Confirming Multiple Designers

In carrying out the Compliance Campaign, some IRS personnel have started narrowly reading Section 179D(d)(4). They argue that, based on a literal and strict reading of the provision, there can be only one "person primarily responsible for designing the property." This idea seems logical at first glance, but it quickly becomes dubious when one starts reviewing relevant authorities. A partial list of the authorities contradicting the IRS's position is analyzed below.[8]

Notice 2006-52

Congress introduced in 2005 energy-efficiency standards for lighting that would reign "[u]ntil such time as the [IRS] issues final regulations."[9] The IRS released Notice 2006-52 less than one year later. It contained "interim guidance" for all components of EECBP, not just lighting systems. Notice 2006-52 expressly states that it applies to EECBP that is installed as part of the (i) interior light systems, (ii) heating, cooling, ventilation, and hot water systems, or (iii) the building envelope or exterior. The rules undoubtedly contemplate the involvement of multiple Designers and the allocation of the Section 179D among them. Notice 2006-52 states the following in this regard:

> *Application to Multiple Taxpayers. If two or more taxpayers* install [energy-efficient lighting property, heating, cooling, ventilation, or hot water property, or building envelope property] on or in the same building, *the aggregate amount* of the Section 179D *deductions allowed to all such taxpayers* with respect to the building shall not exceed the amount determined under [the relevant portion of Notice 2006-52].[10]

Notice 2008-40

Next came Notice 2008-40. The IRS told the public that Notice 2008-40 "clarified and amplified" Notice 2006-52, contained "additional guidance," and was "intended to be used with Notice 2006-52."[11] In other words, Notice 2008-40 did not supersede Notice 2006-52; it expanded on it. Notice 2008-40 unveils the special rules related to government-owned buildings, which purchase EECBP, and which are eligible for a Section 179D deduction. It begins with the general rule that, in the case of EECBP installed on or in a government-owned building, the owner can allocate the deduction to "the person primarily responsible for designing the property."[12] For these purposes, a "Designer" is a person that creates the "technical specifications" for the installation of the EECBP for which a Section 179D deduction is allowed.[13] The non-exhaustive list of potential Designers includes architects, engineers, contractors, environmental consultants, and energy-service providers who create "technical specifications" for a new building, or for an addition to an existing building, which incorporates EECBP.[14] However, cautions the IRS, a person that merely installs, repairs, or maintains the property is not considered a Designer.[15]

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1 Energy Policy Act of 2005, Public Law 109-58, August 8, 2005.

2 U.S. Joint Committee on Taxation. Description and Technical Explanation of the Conference Agreement of H.R., Title XII, Energy Tax Incentives Act of 2005. JCX-60-05 (July 28, 2005), pgs. 78-81.

3 Section 179D(d)(4) (emphasis added).

4 U.S. Treasury Department. 2007-2008 Priority Guidance Plan (April 22, 2008) (although full of instances where the government explicitly planned to release proposed, temporary or final regulations, the government only anticipated issuing "guidance" regarding Section 179D in the form of a Notice). *See also* U.S. Treasury Department. 2011-2012 Priority Guidance Plan (November 19, 2012).

5 Notice 2006-52, Notice 2008-40, and Notice 2012-16.

6 Other articles about Section 179D exist, but they do not wrangle with allocation of the Section 179D deduction to multiple Designers. *See, e.g.,* Larry R. Garrsion, "New Law Creates, Expands, and Extends Energy-Related Tax Incentives," 18(6) Practical Tax Strategies 351 (Dec. 2008); Robyn L. Dahlin and Alex R. Pederson, "Energy Act Offers Tax Benefits to Developers," 33(3) Journal of Real Estate Taxation (Second Quarter 2006); Charles R. Goulding et al, "Strategic Thinking: Seven Years of Code Sec. 179D EPAct," 13(12) Corporate Business Taxation Monthly 9 (2012); Pat McLaughlin, "Commercial Buildings: Achieving Energy Efficiency," Construction Accounting and Taxation (May/June 2009).

7 www.irs.gov/businesses/corporations/lbi-retired-campaigns

8 The IRS has published other authorities regarding Section 179D, but they do not address the key issue of allocation of deductions to Designers pursuant to Section 179D(d)(4). *See, e.g.,* Chief Counsel Advice 201451028; Chief Counsel Advice AM 2010-07; IRS INFO 2007-0031; IRS INFO 2011-0072, Revenue Procedure 2011-14, Appendix, Section 8; Revenue Procedure 2012-39, Section 1.09 through 1.11; Revenue Procedure 2016-29, Section 8; Revenue Procedure 2018-31, Section 8.01.

9 Section 179D(f). This provision cross-references Section 179D(d)(1)(B), which states that the IRS, after consultation with the Secretary of Energy, shall establish energy-efficiency targets.

10 Notice 2006-52, Section 2.03(2)(a)(ii), Section 2.04(2)(b), and Section 2.05(2)(b) (emphasis added). *See also*, Notice 2012-26, Section 3.04(2).

11 Notice 2008-40, Section 1.

12 Notice 2008-40, Section 3.01.

13 Notice 2008-40, Section 3.02.

14 Id.

15 Id.

Notice 2008-40 then contemplates the existence of multiple Designers collaborating on a single project. It explains that, if "more than one Designer is responsible for creating the technical specifications" in connection with a government-owned building, then the owner of such building can do one of two things. The owner can figure out which of the several Designers is the one "primarily responsible" and allocate 100 percent of the Section 179D deduction to that Designer. Alternatively, the owner, using its own discretion, can allocate the deduction "among several Designers."[16]

Process Unit – Audit Guide

The IRS issued guidance to its audit personnel in the form of a Process Unit focused on Section 179D deductions.[17] In light of the fact that the IRS never published regulations, the Process Unit directs IRS personnel to consult various types of guidance, including Notice 2008-40.[18] Later, consistent with the special rules featured in Notice 2008-40, the Process Unit instructs IRS personnel to verify whether the government-building owner allocated the Section 179D deduction to multiple Designers. It then reminds IRS personnel that, in situations involving more than one Designer, the owner "must" either identify the Designer primarily responsible and fully allocate the deduction to that one Designer or, using its own discretion, "allocate the deduction among several Designers."[19] The Process Unit also presents IRS personnel with the following questions to answer during the audit process, all of which infer the participation by multiple Designers: "Are there other Designers? If so, how many and why are they considered Designers? Did other Designers receive an allocation of the [Section] 179D deduction?"[20]

The Process Unit also contains interesting perspectives from the IRS about the significance of Notice 2008-40. It explains that a Notice is a "public announcement" that may contain "substantive interpretations" of tax provisions, such as Section 179D. Expanding on this notion, it goes on to state that "Notices can be used to relate what regulations will say in situations where the regulations may not be published in the immediate future."[21]

Bulletin Published in Federal Register

The General Services Administration ("GSA") published a bulletin in the Federal Register in 2011 notifying all agencies incurring expenses related to EECBP in government-owned buildings of useful information available to them.[22] Among other things, the GSA bulletin stated that IRS "guidance on the allocation of the [Section 179D deduction] for government-owned buildings is set forth in Notice 2008-40." More importantly, the bulletin said that the owners "may allocate [the Section 179D] deduction *to the person or persons primarily responsible*" for designing the EECBP.[23]

Only Case on Point

Several cases involve Section 179D in one way or another, but the specific issue of allocation of deductions to multiple Designers appears in only one, *United States v. Quebe.*[24]

Decision by District Court

There are two major issues in *Quebe*, one of which was whether the property was "placed in service" during the years that the taxpayer claimed the deduction. That has no bearing on this article. The second issue in *Quebe* was whether the taxpayer, QHI, was a Designer for purposes of Section 179D. The District Court determined that QHI was merely an installer, such that it was not a Designer, and was thus not eligible for an allocation of the Section 179D deduction. Despite the ultimate holding in *Quebe*, the reasoning and statements by the District Court contain several items that strengthen the position that a government-building owner can allocate some of the Section 179D deduction among many parties, provided that they all qualify as Designers. For instance, the District Court explained that the DOJ argued that "QHI did not collaborate *with the architects and engineers who designed the buildings* it was not a designer, but merely installed the lighting pursuant to *their* specifications." The District Court then clarified that the relevant projects involved at least six different architectural and engineering companies.[25]

Citing Notice 2008-40, the District Court also said that "while the Notice recognizes that [EECBP] *may have more than one designer*, it specifically excludes a contractor who "merely installs" property." By doing so, the District Court necessarily recognized the validity and authority of Notice 2008-40. This is because the rule about excluding persons who merely install items from the definition of Designer is *only* found in Notice 2008-40; it is *not* found in Section 179D(d)(4). In other words, the District Court based its entire decision on Notice 2008-40. The District Court again acknowledged the possibility of multiple Designers in concluding that QHI "failed to create a genuine issue of material fact regarding their assertion that QHI *was one of the persons primarily responsible for designing the schools.*"

Legal Brief Submitted by U.S. Government to District Court

The Department of Justice ("DOJ"), as representative of the U.S. government, filed a Reply Brief with the District Court in *Quebe*, opposing the earlier Motion for Summary Judgment submitted by QHI. As seen below, the DOJ argued that (i) more than one Designer can receive an allocation of the Section 179D deduction, (ii) the District Court and taxpayers can rely on Notice 2008-40, and (iii) Section 179D(d)(4) and Notice 2008-40 can be interpreted consistently.

The DOJ presented the following reasoning to the District Court:

> [QHI and other taxpayers] argue incorrectly that Section 3.02 of Notice 2008-40 expanded the scope of the persons eligible to receive an allocation of the deduction. Notice 2008-40 did not do so, and does not purport to do so. Section 3.01 of Notice 2008-40 provides that "the owner of the property may allocate the [Section] 179D deduction to the person primarily responsible for designing the property (the designer)." This is wholly consistent with [Section 179D]. *It is clear from the statute and from Section 3.01 that Section 3.02 provides additional color on how the person "primarily responsible for designing the property" can be identified, and Section 3.03 provides*

a procedure if several persons are together "primarily responsible" for the design. The Notice [2008-40] cannot, and does not purport to, expand the deduction beyond what was authorized by Congress that the deduction be allocated *only to persons "primarily responsible" for the design.* It must be read in that context.

The DOJ went on to explain to the District Court in *Quebe* that two parties were the "persons primarily responsible," the architects and the engineers, and each was entitled to an allocation of the Section 179D deduction. The DOJ was simply urging the District Court not to make QHI another party, a third one, receiving an allocation. The DOJ stated the following in this regard:

> [QHI and other taxpayers] do not dispute that they are not primarily responsible for the design of the lighting systems in the school buildings. Indeed, *the persons primarily responsible for these designs are clearly the architects and engineers. [Section 179D] plainly allows the deduction to the architects and engineers*, not [QHI and other taxpayers].

Another Legal Brief Submitted by U.S. Government to District Court

The DOJ filed a Memorandum of Law with the District Court in support of its Motion for Summary Judgment. As seen below, the DOJ again argued that (i) more than one Designer can receive an allocation of the Section 179D deduction, (ii) the District Court and taxpayers can rely on Notice 2008-40, and (iii) Section 179D(d)(4) and Notice 2008-40 can be interpreted consistently. The DOJ explained that Congress, in enacting Section 179D(d)(4), provided that a government-building owner may allocate the deduction only to "the person primarily responsible for designing" the EECBP. However, "Notice 2008-40 [Section] 3.01-3 *expands on this requirement*," allowing the owner to allocate the deduction among several parties when more than one Designer is responsible for creating the technical specifications. Demonstrating its support for the idea that it is acceptable for a government-building owner to allocate the Section 179D deduction to all parties considered Designers, the DOJ stated the following to the District Court:

> *The Notice [2008-40] thus recognizes that more than one person can be primarily responsible for the design, as when an architect and engineer work together to create the specifications, but specifically excludes a contractor who 'merely installs' the property. The architects and engineers who worked on each school building are the persons primarily responsible for designing the lighting systems.* QHI, as the electrical contractor, was [merely] responsible for installing the lighting system.

Extending the reasoning of the DOJ featured above, if QHI had been able to prove to the District Court that it, too, was a Designer, then allocation of the Section 179D to the architects, engineers, *and* QHI (instead of just to the architects and engineers) would have been fine.

Chief Counsel Advice AM 2018-005

Chief Counsel Advice ("CCA") AM 2018-005 perhaps provides the most extensive guidance, from the IRS itself, about the ability of taxpayers to allocate the Section 179D deduction to multiple parties that qualify as Designers. The CCA describes the evolution of Section 179D and the special rules applicable to government-owned buildings under Section 179D(d)(4). In doing so, the CCA acknowledges that the IRS has never promulgated regulations, as mandated by Congress in 2005, but has issued three Notices, including Notice 2008-40. The CCA concedes that Notice 2008-40 offers "substantial guidance" on the

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16 Notice 2008-40, Section 3.03.

17 U.S. Internal Revenue Service. LB&I Process Unit. IRC 179D Energy Efficient Commercial Buildings Deduction. COR-P-002 (Revised June 19, 2020).

18 U.S. Internal Revenue Service. LB&I Process Unit. IRC 179D Energy Efficient Commercial Buildings Deduction. COR-P-002 (Revised June 19, 2020), pg. 6.

19 U.S. Internal Revenue Service. LB&I Process Unit. IRC 179D Energy Efficient Commercial Buildings Deduction. COR-P-002 (Revised June 19, 2020), pg. 26.

20 U.S. Internal Revenue Service. LB&I Process Unit. IRC 179D Energy Efficient Commercial Buildings Deduction. COR-P-002 (Revised June 19, 2020), pg. 30.

21 U.S. Internal Revenue Service. LB&I Process Unit. IRC 179D Energy Efficient Commercial Buildings Deduction. COR-P-002 (Revised June 19, 2020), pg. 38.

22 Federal Register, Volume 76, Number 49, page 13617 (March 14, 2011).

23 Id.

24 *United States v. Quebe*, 123 AFTR 2d 2019-543; *See also University of Texas v. Alliant Group, LP*, 124 AFTR 2d 2019-5779, *Konkel v. Commissioner*, Tax Docket No. 4609-12W, 2012 WL 864737 (2012), *Hellmuth, Obata & Kassabaum, LP v. Efficiency Energy, LLC*, 2015 WL 4126911 (DC SD Tx 2015) and 2016 WL 164112 (DC SD Tx 2016).

25 *United States v. Quebe*, 123 AFTR 2d 2019-543. The District Court listed Fanning/Howey Associates, Moody-Nolan, Allied Toledo Architects, Munger Munger & Associates Architects, Vision Mechanical, and Freytag & Associates.

26 INFO 2009-0226 (Nov. 25, 2009).

27 INFO 2012-0004 (Feb. 1, 2012).

28 www.irs.gov/businesses/corporations/lbi-retired-campaigns

29 *See, e.g., Middle Rio Grande Conservancy Dist. v. Babbitt*, 206 F. Supp. 2d 1156, 1176 (N.M. 2000) ("[W]hen a statute uses the word 'shall', Congress has imposed a mandatory duty upon the subject of the command."); *Commonwealth of Pa. v. Weinberger*, 367 F. Supp. 1378, 1381 (D.C. 1973) ("Statutory language that an official 'shall' perform an act has been repeatedly held to be mandatory in nature."); *Campbell v. Pan American World Airways, Inc.*, 668 F. Supp. 139, 142 (E.D. N.Y. 1987) ("*Will*, like *shall*, is a mandatory word."); *In re Davenport*, 175 B.R. 355, 358 (E.D. Ca. 1994) ("There is perhaps no less ambiguous word used in statutes than 'shall.'); *Keith v. Rizzuto*, 212 F.3d 1190, 1193 (10th Cir. 2000) ("It is a basic canon of statutory construction that use of the word 'shall' indicates a mandatory intent."); *Lexecon Inc. v. Milberg*, 523 U.S. 26, 35 (1998) ("The [statute's] instruction comes in terms of the mandatory "shall," which normally creates an obligation impervious to judicial discretion."); *In re Barbieri v. Raj Acquisition Corp.*, 199 F.3d 616, 619 (2nd Cir. 1999) ("The term 'shall,' as the Supreme Court has reminded us, generally is mandatory and leaves no room for the exercise of discretion by the trial court."); *McMullen v. United States*, 50 Fed. Cl. 718, 725 (2001) ("As a matter of statutory construction, the word 'may' usually connotes permissive discretion, as opposed to the word 'shall,' which connotes a mandatory task."); *Ace Prop. & Cas. Ins. Co. v. Federal Crop Ins. Corp.*, 357 F. Supp. 2d 1140, 1150 (S.D. Iowa 2005) ("The term 'shall' is mandatory in nature."); *International Data Products Corp. v. United States*, 64 Fed. Cl. 642, 650 (2005) ("It is well settled that 'shall' indicates a command."); *Association of Civilian Technicians v. Federal Labor Relations Auth.*, 22 F.3d 1150, 1153 (D.C. 1994) ("The word 'shall' generally indicates a command that admits of no discretion on the part of the person instructed to carry out the directive."); *Plaut v. Spendthrift Farm, Inc*. 1 F. 3d 1487, 1490 (6th Cir. 1993) ("Where the word 'shall' appears in a statutory directive, "Congress could not have chosen stronger words to express its intent that [the specific action] be mandatory."); *Forest Guardians v Babbitt*, 174 F.3d 1178, 1187 (10th Cir. 1999) ("The Supreme Court and this circuit have made it clear that when a statute uses the word 'shall,' Congress has imposed a mandatory duty upon the subject of the command."); *United States v. Myers*, 106 F.3d 936, 941 (10th Cir. 1997) ("It is a basic canon of statutory construction that use of the word 'shall' indicates a mandatory intent.").

special rule for government-owned buildings. The CCA then explains Sections 3.01, 3.02 and 3.03 of Notice 2008-40, which confirm that the owner of a government building can allocate the Section 179D deduction among multiple parties "if more than one Designer is responsible for creating the technical specifications." Finally, the CCA offers eight scenarios whose sole issue is which parties, among several, are entitled to an allocation of the Section 179D deduction. The scenarios are discussed below.

Scenario 1 involved a "design team," consisting of two separate persons, an architect and an engineer. It is also involved a general contractor, who aspired to join the team in hopes of getting an allocation of the Section 179D deduction. The work of the general contractor did not rise to the level of technical specifications, such that it was not part of the "design team." In Scenario 1, the IRS held that two persons, the architect and the engineer, jointly constituted the "person primarily responsible" and thus were both Designers. Moreover, the IRS stated in Scenario 1 that "[a]lthough Section 3.03 of the Notice [2008-40] gives the government-building owner discretion to allocate the [Section] 179D deduction among several Designers, it does not give [it] discretion to allocate the [Section] 179D to a person who is not a Designer."

Scenario 2 involved an architect, design firms, and a construction manager. At the end of the project, the architect requested and received the full allocation of the Section 179D deduction. Later, the design firms requested allocations, too, but were denied. The IRS determined that the architect was a Designer because he provided technical specifications for the building envelope. The IRS further explained that, because the architect was one of the Designers, the government-building owner had discretion under Notice 2008-40 to allocate the entire Section 179D deduction to the architect. Importantly, the IRS confirmed that if the other Designers were to later claim an allocation of the Section 179D deduction, they would not be entitled to any because the government-building owner already allocated the full amount to the architect.

Scenario 3 involved an architect and a construction manager. Only the architect created technical specifications, so he was the only Designer for purposes of Section 179D. The implication of Scenario 3 is that multiple parties, such as the architect and construction manager, could have each received a portion of the Section 179D if they had both qualified as Designers.

Scenario 4 involved an engineer and a contractor. Only the engineer created technical specifications, so he was the only Designer. The implication of Scenario 4 is that multiple parties, such as the engineer and contractor, could have each received a portion of the Section 179D if they had both qualified as Designers. This IRS confirms this by repeating its mantra that "[a]lthough Section 3.03 of the Notice [2008-40] gives the government-building owner discretion to allocate the [Section] 179D deduction among several Designers, it does not give [it] discretion to allocate the [Section] 179D to a person who is not a Designer."

Scenario 5 involved an engineer, contractor, and subcontractor. Only the engineer created technical specifications; therefore, he was the only Designer. The inference of Scenario 5 is that multiple parties, such as the engineer, contractor and subcontractor, could have each received a portion of the Section 179D if they had all qualified as Designers. Again, the IRS confirms that by underscoring that "[a]lthough Section 3.03 of the Notice [2008-40] gives the government-building owner discretion to allocate the [Section] 179D deduction among several Designers, it does not give [it] discretion to allocate the [Section] 179D to a person who is not a Designer."

Scenario 6 involved an engineer and a contractor. Only the engineer created technical specifications, such that he was the only Designer. The significance of Scenario 6, like many of its predecessors, is that more than one party, like an engineer and a contractor, could have received a portion of the Section 179D deduction, provided that each independently qualified as a Designer.

Scenario 7, which is particularly noteworthy, involved a lighting firm and an architect. Both parties created technical specifications and were thus Designers. However, the government-building owner allocated all the Section 179D deduction to the lighting firm and none to the architect. The IRS explained the following, fortifying the notion that multiple persons could, together, form the "person primarily responsible" under Section 179D(d)(4) and Notice 2008-40:

> While it seems more appropriate for the lighting firm to receive a partial [Section] 179D deduction so that Designers of the other EECBP systems can also receive partial [Section] 179D deductions, Section 3.03 of the Notice [2008-40] gives the government-building owner discretion to allocate either the full deduction to the primary Designer or to allocate portions of the deduction among several Designers. Unless the [IRS] has evidence that a government-building owner's allocation of the [Section] 179D deduction was improper, such as when the person to whom the deduction was allocated was not a Designer or when the government-building owner allocated more than the maximum amount of the [Section] 179D deduction among one or more Designers, the [IRS] should respect the owner's allocation.

Scenario 8 involved a mechanical engineer, who is part of the design team, and a specialty subcontractor hired to design and install various building systems ("Energy Management System"). The subcontractor did not design the EECBP system, but the Energy Management System manages the EECBP for peak performance. The IRS determined that, if the Energy Management System were part of the EECBP, then both the mechanical engineer and the subcontractor would be Designers and entitled to an allocation of the Section 179D deduction. By contrast, if the Energy Management System were not part of the EECBP, then only the mechanical engineer would be a Designer.

The CCA contained the following conclusion: "If a building owner could have qualified for the maximum [Section] 179D deduction . . . then the gov-

ernment-building owner has discretion to allocate the full . . . deduction to the primary Designer of one system of such property *or to allocate the . . . deduction among several Designers.*"

IRS National Office Correspondence to Lawmakers

Over the years, various lawmakers have explicitly asked the IRS, in writing, to issue regulations regarding Section 179D, as Congress instructed it to do in 2005. In response, attorneys from the IRS's National Office told one lawmaker, again in writing, that the IRS issued Notice 2006-52 and Notice 2008-40, they addressed "key issues" regarding Section 179D, and although such IRS guidance came in the form of Notices instead of regulations, "taxpayers may rely with confidence in those Notices.[26] Similarly, in addressing other questions about the application of Section 179D to efficient lighting, another attorney from the IRS's National Office told lawmakers, via a published document, that the IRS issued Notice 2006-52 and Notice 2008-40 "to provide guidance" about the deduction, the two Notices contain "in depth information" about various qualifications and procedures, and taxpayers "should refer to the Notices in their entirety."[27]

Compliance Campaign

As explained earlier in this article, the IRS, suspecting potential wrongdoing by taxpayers, initiated a Compliance Campaign in late 2017. In warning the public about its plan to audit Section 179D deductions allocated to Designers pursuant to Section 179D(d)(4), the IRS confirmed that "[i]f the equipment is installed in a government-owned building, the deduction is allocated *to the person(s) primarily responsible for designing the EECBP.*"[28]

Musings on Interpretation of Rules

The current mess, for lack of a better word, arguably results from the fact that the IRS has outright ignored Congress for over 15 years. Section 179D(d)(4) states that, in the case of EECBP installed on or in a government-owned building, the IRS "shall promulgate a regulation" to permit the allocation of the Section 179D deduction. The IRS disseminated three Notices, including Notice 2008-40, instead of releasing a regulation. As one might expect, the IRS, other governmental agencies, and the courts then followed Notice 2008-40 in making determinations.

This article is not the place for a comprehensive discussion of statutory interpretation. It is enough to simply introduce a few relevant notions. First, courts have consistently held that when Congress uses the term "shall" in a statute, it means "shall," not "might" or "should."[29] Congress told the IRS in 2005 that it "shall" issue a regulation to clarify allocation of the Section 179D deduction, but the IRS never did.

Second, courts agree that a *specific* rule prevails over a *general* one.[30] The *general* mandate that government-building owners can allocate the deduction is found in Section 179D(d)(4), while the *specific* directions originate in Notice 2008-40. The latter says, with remarkable precision, that one of the options available to government-buildings owners is to divide the Section 179D deduction, using their own judgment, "among several Designers."

Third, courts have a duty to interpret statutes such that, whenever possible, no provision, clause, sentence, or word becomes superfluous, void or meaningless.[31] Reading Notice 2008-40, as the IRS suggests, to mean that government-building owners can allocate the deduction to only one Designer would require the general rule, set forth in Section 3.01 of Notice 2008-40, to effectively oblit-

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[30] *See, e.g., Bulova Watch Co. v. United States*, 365 U.S. 753, 758 (1961). ("[I]t is familiar law that a specific statute controls over a general one 'without regard to priority of enactment.'"); *HCSC-Laundry v. United States*, 450 U.S. 1, 6 (1981) ("[I]t is a basic principle of statutory construction that a specific statute . . . controls over a general provision . . ."); *Edmond v. United States*, 520 U.S. 651, 657 (1997) ("Ordinarily, where a specific provision conflicts with a general one, the specific governs."); *Doe v. National Board of Medical Examiners*, 199 F.3d 146, 155 (1999) ("[I]t is a commonplace of statutory construction that the specific governs the general." This principle has special force when Congress has targeted specific problems with specific solutions in the context of a general statute."); *In re Gledhill*, 76 F.3d 1070, 1078 (10th Cir. 1996) (It is a "fundamental tenet of statutory construction that a court should not construe a general statute to eviscerate a statute of specific effect."); *Witt v United States*, 100 F.3d 915, 919 (Fed. Cir. 1996) ("It is a standard rule of construction that "a specific statute controls over a general one 'without regard to priority of enactment.'").

[31] *See, e.g., United States v. Menasche*, 348 U.S. 528, 538-539 (1955) ("The cardinal principle of statutory construction is to save and not to destroy. It is our duty to give effect, if possible, to every clause and word of a statute, rather than to emasculate an entire section, as the Government's interpretation requires.") (citations omitted); *TRW Inc. v. Andrews*, 534 U.S. 19, 31 (2001) ("It is "a cardinal principle of statutory construction" that "a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant."); *Crawford v. United States*, 376 F.2d 266, 272 (Ct. Cl. 1967) ("It is a cardinal principle of statutory construction to give effect to every clause, sentence and word of a statute, if possible, rather than to distort the language so as to defeat the plain intent of the Congress."); *Little Six, Inc. v. United States*, 210 F.3d 1361, 1365 (Fed. Cir. 2000) ("[I]n construing a statute we must give effect and meaning to all of its terms if possible . . . the interpretation proposed by the government would render language in the statute superfluous, a result that we must attempt to avoid."); *Estate of Magnin v Commissioner*, 184 F.3d 1074, 1078 (9th Cir. 1999) ("To read the statute otherwise would be to render the parenthetical exception meaningless surplusage . . . We must interpret the statute to give effect to all of its parts.")

[32] *See, e.g., United States v, Merriam*, 263 U.S. 179, 187-188 (1923) ("But in statutes levying taxes the literal meaning of the words employed is most important for such statutes are not to be extended by implication beyond the clear import of the language used. If the words are doubtful, the doubt must be resolved against the government and in favor of the taxpayer."); *United States v. Maryland Casualty Co.*, 49 F.2d 556, 558 (7th Cir. 1931) ("[Tax] statutes are not to be extended by implication beyond the clear import of the language used. If the words are doubtful, the doubt must be resolved against the government and in favor of the taxpayer. Such acts, including provisions of limitation embodied therein, are to be construed liberally in favor of the taxpayer. There must be certainty as to the meaning and scope of language imposing any tax, and doubt in respect to its meaning is to be resolved in favor of the taxpayer.")(citations omitted); *Commissioner v. Bryson*, 79 F.2d 397, 402 (9th Cir. 1935) ("It is familiar doctrine that taxing acts, including provisions of limitation embodied therein [are] to be construed liberally in favor of the taxpayer.); *Holmes Limestone Co. v. United States*, 946 F. Supp. 1310, 1319 (N.D. Ohio 1996) ("These rules of construction guide this court in most situations, however, materially different rules have been adopted for the interpretation of a revenue statute . . . [A]s a special rule in tax cases, 'if doubt exists as to the construction of a taxing statute, the doubt should be resolved in favor of the taxpayer.'")

[33] Section 7430(a).

[34] Section 7430(c)(4)(A).

[35] Section 7430(c)(4)(B)(i).

[36] Section 7430(c)(4)(B)(ii).

[37] Section 7430(c)(4)(B)(iv); Treas. Reg. § 301.7430-5(c)(3).

erate the precise rules about multi-Designer allocations, described in Section 3.03.

Fourth, just as courts ordinarily construe a contract in favor of the party that did *not* draft it, numerous tax cases have held that tax provisions should be resolved in favor of taxpayers.[32] This supports the idea that any haziness concerning the allocation rules, or any alleged inconsistencies between the language in Section 179D(d)(4) and Notice 2008-40, should be resolved in favor of the taxpayers. Specifically, they should be read to favor government-building owners and multiple Designers, not the government.

Conclusion

The "prevailing party" in any administrative proceeding before the IRS, or in any litigation that is brought by or against the IRS, may be awarded reasonable administrative and/or litigation costs.[33] The term "prevailing party" means the one that substantially triumphs with respect to either the amount in dispute or the most significant issues presented, and meets the net worth thresholds.[34] Even if a taxpayer meets these two criteria, it nonetheless will *not* be the "prevailing party" if the IRS can establish that its position was "substantially justified."[35] Stated another way, if the IRS can prove that the arguments it raised during the dispute were substantially justified, then the taxpayer cannot recover costs.

There is a rebuttable presumption that the IRS's position is *not* substantially justified if the IRS failed to follow "applicable published guidance" during a proceeding.[36] Such guidance includes, but is not limited to, regulations, revenue rulings, information releases, *notices*, announcements, private letter rulings, technical advice memos, and determination letters.[37]

One might contend that the current position advanced by the IRS that government-building owners can allocate the Section 179D deduction to only one Designer is not "substantially justified" because it is contrary to Notice 2006-52, Notice 2008-40, the Process Unit, the GSA bulletin, the District Court holding in *Quebe*, various briefs filed by the DOJ in *Quebe*, CCA AM 2018-55, letters from IRS National Office attorneys to lawmakers, and the express language of the Compliance Campaign. Additionally, one might argue that the IRS's position contravenes several long-standing rules of statutory interpretation. Secured by this foundation, one might suggest that, if the IRS insists on pressing its one-Designer-only theory in Section 179D disputes, taxpayers are obligated to challenge matters with the Appeals Office and later in Tax Court, and the taxpayers prevail, then the taxpayers might be poised to seek recoupment of all reasonable costs. ●