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THE CURRENT TAX ENFORCEMENT ENVIRONMENT

By

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SESSION E

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Pam Olson is a consultant and the former US Deputy Tax Leader and Washington National Tax Services Leader for PwC. In her previous role with WNTS, Pam leads a team that includes many former senior government officials and policy advisers.

Prior to joining PwC, Pam led the Washington tax practice at Skadden, Arps, and served as assistant secretary for tax policy at the US Department of the Treasury.

Pam has represented clients in a broad range of matters, including IRS audits, appeals and litigation; congressional investigations; private letter ruling requests, proposed regulations, and other IRS and Treasury guidance; and in the legislative process. She has advised clients on tax and social security reform and on the structuring of financing, partnership, and M&A transactions. She is a frequent speaker on tax, economic and federal budget matters and has testified before several congressional committees, most recently before the Senate Finance Committee on international tax reform.

As assistant secretary for tax policy, Pam had supervisory responsibility for providing the secretary of the treasury with policy analysis and recommendations for all domestic and international issues of federal taxation, including legislative proposals, regulatory guidance, and tax treaties, and for providing the official estimates of all government receipts for the president's budget and treasury cash management decisions. Pam also held positions with the chief counsel's office of the Internal Revenue Service as special assistant to the chief counsel, attorney-adviser in the Legislation and Regulations Division and trial attorney in San Diego District Counsel.

In 2000 and 2001, Pam was the first woman to serve as chair of the American Bar Association Section of Taxation. She has served as tax and economic adviser to two presidential campaigns and as tax adviser to the National Commission on Economic Growth and Tax Reform. She has been included repeatedly in Chambers USA: America's Leading Lawyers for Business and The Best Lawyers in America for tax law. Pam served as a Regent of the American College of Tax Counsel and is on the board of several nonprofit organizations. She received the Treasury Department's highest award, distinguished service awards from the Federal Bar Association and Tax Executives Institute, and delivered both the Lawrence Woodworth and Erwin Griswold annual lectures.

Pam received her B.A., M.B.A., and J.D. from the University of Minnesota.

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I. IRS Workforce

A. Turnover at the Top

1. In the Commissioner's office, former Commissioner Billy Long was replaced after only two months on the job by Treasury Secretary Scott Bessent, now serving as Acting Commissioner of the IRS in addition to his Secretary responsibilities.

2. During 2025, the top rungs of the IRS have cycled through several departures and acting heads, presenting leadership challenges and opportunities.

3. Former IRS Chief Counsel Don Korb's nomination to return to the same position is pending confirmation by the Senate and, once confirmed, will bring welcome experience and continuity to the agency.

B. Reductions in Workforce

1. Between February and May 2025, there were significant IRS workforce departures: of its 103,000 employees, 25,386 departed. While these numbers are significant, they are against a baseline of a significant ramp up in workforce levels through funding provided under the Inflation Reduction Act of 2022.

2. Departures were variously due to reduction in force ("RIF") efforts or participation in the Deferred Resignation Program ("DRP"), Voluntary Early Retirement Authority ("VERA"), or Voluntary Separation Incentive Payment ("VSIP"). *See* Treasury Inspector Gen. for Tax Admin., Snapshot Report: IRS Workforce Reductions as of May 2025 ("July 2025 TIGTA Report") (Report No. 2025-IE-R027, July 18, 2025), https://www.tigta.gov/sites/default/files/reports/2025-07/2025ier027fr.pdf.

3. The reduction in the IRS's workforce impacted every aspect of the IRS. A substantial percentage of IRS personnel were retirement eligible prior to 2025, e.g., approximately 30% in the Large Business & International Division prior to the recent hiring ramp up. Certain functions in the workforce sustained notable reductions:

    a. A 27% reduction in tax examiners (4,180 personnel).

    b. A 26% reduction in revenue agents (3,070 personnel).

    c. A 23% reduction in contact representatives (5,931 personnel).

C. Rehiring Mixed with Additional Departures

1. The expedited efforts to reduce workforce led to almost immediate re-hiring efforts to fill "critical vacancies." Meanwhile, there have been more departures.

2. The IRS recently listed 3,500 open positions for which it is hiring across the country.

3. Additionally, it has been reported that the IRS is asking certain employees who accepted the DRP to return to the IRS to fill "critical vacancies." The precise details as to who is being asked to return and in what numbers are unclear. Other employees who were slated to be terminated have been told that they will be staying on. *See, e.g.*, Emily Peck, *IRS halts layoffs and plans to bring back workers as tax season looms*, Axios (Aug. 22, 2025) https://www.axios.com/2025/08/22/irs-layoffs-tax-season.

4. Notwithstanding the reports of re-hiring efforts, IRS employees on administrative leave were again offered the option to take a deferred resignation offer, remaining on paid administrative leave through December 31 before permanently leaving the IRS. Erin Slowey, *IRS Extends Deferred Resignation Offer to Workers on Admin Leave*, Bloomberg Law (Sept. 25, 2025), https://www.bloomberglaw.com/product/blaw/bloomberglawnews/bloomberg-law-news/BNA%2000000199-7377-d2f6-ad9f-f7f79fe10001.

D. Impact of Changes in IRS Workforce

1. Employee Morale

   a. Given the high staff turnover in the termination and re-hiring process, employee morale at the IRS is reported to be low in part because of the volume of work shifting from those employees who left to those employees who have remained. That said, IRS employees have long had an esprit de corps that has kept them committed to the mission of the IRS to collect the taxes owed that are necessary to fund the government.

   b. Shifting assignments means changes to exam teams. Accordingly, taxpayers may need to engage in a certain level of teaching with the new members of the exam team to ensure that they are up to date on the matter. To the extent that attorneys from the Office of Chief Counsel were assisting with an exam, taxpayers might also want to include them in education efforts. Similar considerations apply for cases pending in Appeals and reassignment of those cases to new Appeals officers.

2. Workload

   a. With fewer staff, there may be more limited interactions with exam teams.

   b. Reduced staff may also lead to a narrowing of scope for some existing audits.

c. Changes to the Code from the recently-passed One Big Beautiful Bill Act ("OBBBA"), Pub. L. 119-21 (July 4, 2025) will require implementing regulations and other guidance on new and amended provisions, including the treatment of research and experimental expenditures, green energy credits and the new "no tax on tips" deduction, Insight on this guidance should be forthcoming in the 2025-2026 Priority Guidance Plan, which is also expected to reflect the Administration's deregulatory agenda. Staff reductions, particularly in the Office of Chief Counsel, will present challenges for Treasury and the IRS in advancing this regulatory agenda.

d. OBBBA changes will also result in an increased demand for taxpayer assistance both in-person and via the IRS phone lines. However, reductions in the customer service workforce will affect the availability of assistance.

e. An open question is the extent to which the reductions in force and advent of new technologies, including AI, will allow the IRS to operate more efficiently and effectively, mitigating the effect of the staff reductions. E.g., other countries' have adopted technology that has allowed them to ensure compliance with far fewer resources, including on a more comprehensive basis.

3. Institutional Knowledge

a. With new exam and Appeals team members, taxpayers may also observe a shift in the level of experience.

b. Almost one-third of the reduction in revenue agents came from Large Business & International ("LB&I"). Given the experience level of most agents within LB&I, this represents a potentially significant reduction in institutional knowledge. Taxpayers subject to examination by this Division may experience a reduction in the number of audits, reduced scope of audits, and reduced availability of experts.

c. Given the percentage of examinations that result in no or insignificant adjustments, the most significant question is whether the IRS can take advantage of new technologies so that it improves its return selection, issue identification, and case management. To the extent that it can, it may reduce the number of audits that are essentially fruitless and instead produce better results with less burden to taxpayers whose returns shouldn't have been examined to begin with.

4. Increased Reliance on Specialists

a. If less experienced examiners and agents remain at the IRS, they may have a greater need to rely on issue specialists. A specialist backlog could make issue resolution and closing of examinations more time-consuming. That said, many specialists are in Chief Counsel's office or rely on Chief Counsel lawyers for advice. Since Chief Counsel has experienced fewer reductions in force, the burden may be shifted without

too much difficulty. Moreover, the Office of Chief Counsel is currently hiring, and the Chief Counsel nominee has a solid hiring track record from his first time in the role.

5. Computational Specialists

    a. Often one of the more time-consuming aspects of case resolution is coming to agreement on computation of the tax or refund due for agreed and unagreed issues, particularly in the context of large corporate and partnership audits. The reduction in force is expected to result in further delays in receiving and revising computations.

6. Processing Time

    a. With the reduction in customer service representatives, taxpayers may expect, among other things, slower processing of amended returns (which require manual intervention).

    b. Offsetting the staff reductions is the funds Treasury is directing to modernize IRS technology that are expected to lead to improved taxpayer service and streamlined filing processes. This represents a shift from the resources directed to increased enforcement personnel to expenditures that will improve taxpayer service and ease taxpayer interactions with the IRS.

7. Pre-Filing Assistance

    a. Staff reductions have impacted more than just post-filing functions. The IRS offers many pre-filing assistance programs, including:

        i. Advanced Pricing Agreements,

        ii. International Compliance Assurance Program,

        iii. Rulings from IRS Office of Chief Counsel,

        iv. Industry Issue Resolution,

        v. Pre-Filing Agreements, and

        vi. Compliance Assurance Program.

    b. These pre-filing assistance programs will be impacted not only by the number of staff departures, but specifically by *experienced* staff departures. Taxpayers who are able to get assistance from the reduced staff may encounter staff with reduced levels of expertise and experience.

    c. This reduction in workforce (and subsequent re-hiring, to an extent) is coinciding with increased demand for tax certainty from taxpayers via

pre-filing programs in the wake of OBBBA's many changes to the tax laws.

d. It is worth noting that the reductions in workforce open the possibility of a new leadership team at the IRS instituting more dramatic changes to its operations. Many experienced IRS personnel have observed over the years that long time employees with entrenched positions and set ways of operating have made implementation of more meaningful changes in IRS procedures more difficult or impossible. New hires with more experience in technology and more savvy on business operations could result in more effective examinations leading to swifter resolutions, an increase in the number of examinations, and more revenue collected per examination.

E. A Word of Caution

1. Given the impacts to the IRS workforce detailed above, certain taxpayers may try to take more aggressive return positions given there are fewer IRS employees focused on a narrower scope of issues. However, taxpayers should be wary and consider that the enforcement environment could shift within three-year or, where applicable six-year (or longer) statute of limitations.

2. It is worth noting that the Trump Treasury has already taken steps towards a more flexible approach to issues that have consumed an inordinate amount of IRS examination and Chief Counsel litigation resources. If successful, the change could result in freeing up resources to pursue other issues.

II. LB&I

A. Improvements to LB&I Exam Process

1. On July 25, 2025, the IRS issued an interim guidance "memorandum highlighting changes aimed at reducing case cycle times for corporate taxpayers, making examinations more customer-driven, consistent and efficient." IR-2025-77 (July 25, 2025). The memo provides guidance for:

   a. Phasing out Acknowledgement of Facts ("AOF") Information Document Request ("IDR") process in examinations by 2026,

   b. Expanding the use of Accelerated Issue Resolution ("AIR") to large corporate cases, and

   c. Stronger reviews of Fast Track Settlement ("FTS") denials.

B. Enforcement Campaigns

1. The LB&I Division identification of "currently active" campaigns provides insight on enforcement priorities and often drives selection of large businesses for examination. The full list may be found here: https://www.irs.gov/businesses/corporations/lbi-active-campaigns. A selection of currently active campaigns are highlighted below.

a. Allocation of Success-Based Fees

i. Focus on documentation requirements for deductibility of success-based fees under Treas. Reg. § 1.263(a)-5(a) where a safe harbor election under Rev. Proc. 2011-29 was not made.

b. Financial Service Entities Engaged in a U.S. Trade or Business

i. Considering whether foreign investors were subject to U.S. tax on effectively connected income from lending transactions engaged in through a U.S. trade or business. *See also YA Global Investments, LP v. Commissioner*, 161 T.C. No. 11 (2023).

c. Costs That Facilitate Section 355 Transactions

i. Evaluation of whether costs that facilitate a spin-off, split-off or split-up were properly capitalized and not currently deducted.

III. Independent Office of Appeals

A. New Alternative Dispute Resolution Program Manager Office

1. On April 24, 2024, Appeals announces the formation of a new Alternative Dispute Resolution Program Manager Office ("ADR PMO") to collaborate with LB&I, SB/SE, and other IRS operating divisions to help resolve tax disputes earlier and more effectively. IR-2024-119 (April 24, 2024), https://www.irs.gov/newsroom/irs-independent-office-of-appeals-forms-alternative-dispute-resolution-program-management-office#:~:text=Streamline%20and%20clarify%20existing%20guidance,Updated:%2029%2DMay%2D2025 (last reviewed or updated May 29, 2025).

2. The ADR PMO plans to:

a. Test ADR programs that allow Appeals to help resolve or mediate disputes earlier in the examination process;

b. Streamline and clarify existing guidance; and

c. Remove barriers to enable easier use of and access to ADR.

B. Compliance Personnel and Counsel at Taxpayer Appeals Conferences

1. On August 26, 2024, TIGTA released a report recommending that "The Chief, IRS Independent Office of Appeals, should update policies to require inviting compliance personnel and Counsel to the taxpayer conferences for those cases involving large multinational corporations." Treasury Inspector Gen. for Tax Admin., *The IRS Faces Challenges to Address Tax Avoidance Strategies of Large Multinational Corporations* ("August 2024 TIGTA Report") (Report No. 2024-400-045, Aug. 26, 2024), https://www.tigta.gov/sites/default/files/reports/2025-08/2024400045fr.pdf.

a. The August 2024 TIGTA Report conducted an evaluation of a 2017-2020 Appeals pilot program requiring participation of LB&I Exam teams and Counsel in the Appeals Conference held for large cases worked by Appeals Team Case Leaders ("ATCLs") before arriving at this recommendation.

b. IRS disagrees with the TIGTA recommendation, supporting current policy of providing discretionary flexibility in inviting Exam compliance personnel and Counsel to participate in Appeals conferences.

C. Final Section 7803 Regulations

1. In February 2025, the Treasury Department and IRS finalized regulations implementing Code section 7803(e), enacted as part of the Taxpayer First Act and codifying the role of Appeals and Appeals' mission statement and providing operating rules for Appeals personnel. *See* Treas. Reg. § 301.7803-2.

2. The regulation lists exceptions to the general availability of Appeals as a forum to resolve tax disputes, purporting to track historic (if unpublished) Appeals practices.

   a. Among those exceptions, the regulation carves out from Appeals jurisdiction challenges to the validity of Treasury regulations and subregulatory guidance absent a final, non-reviewable court decision.

IV. Expanding IRS Use of Economic Substance

A. *Liberty Global, Inc. v. United* States, Case No. 1:20-CV-03501 (D. Colo.).

1. *Liberty Global* involves two distinct proceedings, a refund action and a counter-claim by the government to collect taxes, each with significant implications for corporate taxpayers in that this is one of the first cases to address in detail the requirements of the codified economic substance doctrine in section 7701(o).

2. The transaction at issue in *Liberty Global was* designed to take advantage of an effective date mismatch between provisions of the Tax Cuts and Jobs Act ("TCJA") that made it possible for certain taxpayers to generate income that was exempt from the transition tax in section 965 and the GILTI tax in section 951A, but technically eligible for the dividends received deduction in section 245A (the "donut hole").

3. In the refund action, the Court found in 2022 that temporary regulations under section 245A intended to close the donut hole were invalid because they were issued without following the Administrative Procedure Act's ("APA") notice-and-comment requirements.

4. In the counter-claim brought by the United States, the Court later upheld the government's right to bring suit for collection of unassessed taxes. In considering the merits of that counter-claim on cross-motions for summary judgment, the Court held that irrespective of the validity of the section 245A regulations, the

codified economic-substance doctrine applied to disallow reported tax benefits from the transaction.

5. In a controversial aspect of the District Court's ruling on the government's counter-claim, it found that section 7701(o) did not require a threshold "relevance" inquiry to be made before the objective (economic substance) and subjective (non-tax purpose) prongs of the codified economic substance doctrine were applied and reviewed.

6. The case is currently on appeal to the Tenth Circuit. Docket No. 23-01410 (10th Cir.).

B. *Patel v. Commissioner*, Docket No. 24344-17 (U.S. Tax Court).

1. *Patel* follows *Liberty Global* in raising the question of whether courts are required to perform a threshold "relevance" inquiry before analyzing the substantive objective and subjective prongs of the codified economic substance doctrine.

2. The taxpayers in *Patel* entered into a micro-captive insurance arrangement that the IRS determined did not meet the requirements for "insurance" under section 831(b), disallowing deductions for premiums paid and imposing various accuracy-related penalties, including under section 6662(b)(6), finding that the transaction lacked economic substance under section 7701(o).

3. In T.C. Memo 2024-34, the Tax Court sustained the IRS's disallowance of a deduction for the insurance premiums paid, holding that the transaction did not comport with general insurance practices and procedures as required under section 831(b). Having analyzed the technical merit of the transaction under section 831 and disallowing the reported tax benefits under that analysis, the Court did not go on to rule on whether the tax benefits could also be disallowed under the economic substance doctrine.

4. Remaining pending before the Court in *Patel* is the applicability of several accuracy-related penalties proposed by the IRS for tax years 2014, 2015, and 2016, including penalties under section 6662(b)(6) for an under-payment of tax attributable to a transaction lacking in economic substance under section 7701(o).

    a. Because the Court's prior ruling did not entail an economic substance determination, in order for the Court to hold petitioners liable for the section 6662(b)(6) penalty, it must undertake an independent merits inquiry on whether the transaction lacked economic substance.

5. The Court invited *amicus* briefing on the economic substance issue, including whether (as the District Court held in *Liberty Global*), section 7701(o) includes a threshold "relevance" requirement.

    a. The amicus briefs filed generally supported the requirement for a threshold relevance determination but without taking a position on the merits or outcome of the case.

V. Deference to Administrative Rulemaking

A. *Loper Bright Enters. v. Raimondo*, 603 U.S. 369 (2024).

1. On June 28, 2024, the Supreme Court issued its long-awaited decision in *Loper Bright*, overruling the *Chevron* doctrine under which courts would give deference to an agency's "reasonable" interpretation of an ambiguous statute.

2. The plaintiff in *Loper Bright* is a small businesses engaged in herring fishing off the Atlantic coast that brought suit challenging a rule promulgated by the Department of Commerce that required it to pay for government-approved fishing monitors, which can reduce fishers' returns by up to 20%. The lawsuit argued that this rule was not authorized by the governing statute, which did not expressly say who should pay for these monitors. The district court below granted summary judgment to the Commerce Department, and the First Circuit affirmed, applying *Chevron* to hold that the agency had reasonably interpreted the statute.

3. The Supreme Court reversed the appellate court and held that "Chevron is overruled."

4. The effects of the *Loper Bright* decision will likely be most dramatic in the lower courts—including the Tax Court—which had continued to apply *Chevron* deference even as the Supreme Court has rarely invoked the doctrine over the past decade.

5. Going forward, agencies' interpretation of statutes will still be entitled to a lesser degree of "respect" under *Skidmore v. Swift & Co*., insofar as the agencies' views are persuasive. This may depend on factors such as whether the agency adopted the interpretation close in time to the statute's enactment and how consistently the agency has adhered to that interpretation since.

B. *Varian Medical Systems, Inc. v. Commissioner*, 163 T.C. 76 (2024).

1. *Varian* is the first Tax Court case to apply *Loper Bright* to the Treasury Department and IRS's interpretation of a tax regulation.

2. In a reviewed decision, the Court unanimously held that the plain language of the effective date provisions of the TCJA entitled a fiscal year taxpayer to a section 245A dividends received deduction for section 78 dividends that the taxpayer was deemed to receive during a one-time "gap period."

3. Relying on *Chevron*, the IRS initially argued that the Tax Court should defer to relevant Treasury Regulations that purported to bridge the gap period and disallow the deduction because even if the Court disagreed with the government's interpretation, the statute was ambiguous and the regulation was a reasonable interpretation of the statute. Finding that the plain language of the statute permitted the deduction, the Court held that the regulation had no legal effect.

4. Citing *Loper Bright*, the Court emphasized that with repeal of *Chevron*, statutes must have (and the courts must find) a "single, best meaning."

5. Thus, despite Congress delegating rulemaking authority to Treasury under the reviewed provision, the Court held that it was a failed attempt to "impermissibly…change an unambiguous provision of the statute" and so "the regulation falls outside the boundaries of any authority that Congress may have delegated under [the Code]."

6. In a September 13, 2024 Order entered in *Sysco Corp. v. Commissioner* (Docket No. 5728-23), the Court applied *Varian* to the same effect, allowing a reported dividends received deduction.

C. *Corner Post, Inc. v. Bd. of Governors of Fed. Reserve Sys.*, 603 U.S. 799 (2024).

1. In *Corner Post*, the Supreme Court held that an APA claim does not accrue for the purposes of 28 U.S.C. § 2401(a)'s six-year statute of limitations until the plaintiff is injured by final agency action.

2. The Court reasoned that because an APA plaintiff may not file suit and obtain relief until they suffer an injury from final agency action under 5 U.S.C. §§ 702 and 704, the statute of limitations does not begin to run until they are injured.

3. Combined with *Loper Bright*, *Corner Post*'s expanded time frame to bring suit against administrative agencies will likely lead to more litigation challenges to federal regulations.

VI. Recent and Pending Regulatory Validity Challenges

A. *3M Co. & Subsidiaries v. Commissioner,* 160 T.C. 50 (2023).

1. In *3M*, the Tax Court upheld and applied the "blocked income" regulations under Treas. Reg. § 1.482-1(h)(2) (addressing when a taxpayer may take into account foreign legal restrictions for determining the arm's-length amount in a transaction between controlled taxpayers) in connection with certain royalty income received by 3M from a Brazilian subsidiary for licensed intangible property (including intellectual property).

2. A Brazilian law imposed a 1% cap on royalties that a Brazilian licensee could remit to a foreign related-party licensor, and 3M complied with this limitation. The IRS argued that the royalty rate should have been 6%, in line with other related-party manufacturing arrangements, and adjusted 3M's income under section 482, notwithstanding the Brazilian domestic law. The Tax Court found in favor of the IRS on both the reallocation of income under section 482 and the validity of the requirements under Treas. Reg. § 1.482-1(h)(2).

3. The case is pending on appeal to the Eighth Circuit where, among other issues, the Court has asked for supplemental briefing on the impact of the Supreme Court's decision in *Loper Bright.*

B. ***FedEx Corp. & Subs. v. United States*, Case No. 2:20-cv-02794 (W.D. Tenn.).**

1. In *FedEx*, the court addressed Treasury's denial of foreign tax credits claimed by FedEx with respect to foreign taxes imposed on earnings that were offset by losses from other foreign subsidiaries. FedEx argued that its right to the credits was clearly supported under the plain language of section 960(a)(3), whereas the government argued that the credits were properly disallowed under the final transition tax regulations under section 965. The District Court ruled in favor of FedEx, holding the regulations invalid and ruling that, under the plain language of the Code, FedEx was entitled to the credits for the foreign taxes paid on offset earnings.

2. Following a 2023 ruling, the government argued for application of a different regulation issued under section 965 to deny judgment in favor of FedEx and further argued that the regulation should be afforded *Chevron* deference.

3. The Court ordered supplemental briefing in the case on the impact of the Supreme Court's decision in *Loper Bright*, and it rejected this alternative argument from the government in granting FedEx's motion for summary judgment. The Court confirmed that its prior ruling is unaffected by the Supreme Court's decision in *Loper Bright* to eliminate *Chevron* deference.