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The Perfect Process Is the Enemy of the Good Tax: Tax's Exceptional Regulatory Process

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THE PERFECT PROCESS IS THE ENEMY OF THE GOOD TAX: TAX'S EXCEPTIONAL REGULATORY PROCESS

Stephanie Hunter McMahon *

Many courts and academics critique existing tax exceptionalism or the ability of the federal income tax to be created, applied, or interpreted differently from other laws. Critics have successfully complained that the Treasury Department, and the IRS as a bureau of the Department, issues guidance implementing the Internal Revenue Code using different processes from those required by the Administrative Procedure Act (APA). At the same time, courts are increasing the level of deference given to this guidance to conform to that given other agencies. This article responds to these critics by urging they re-focus their attention on the objectives of administrative law and comparisons to other agencies' procedures as opposed to limiting their assessment to the APA. Moreover, this article examines some risks of forcing procedural uniformity on the tax system. First, the agency would risk being inundated with information to comply with the APA. The agency could be captured by those submitting information, be forced to reduce the amount of guidance it issues, and be thwarted in its ability to accomplish other agency directives. Second, pushing the agency to develop *ex ante* regulations responsive to commentators, including those seeking to use the procedure to secure personal tax reduction, threatens established heuristics implementing the complicated Internal Revenue Code. To satisfy the APA's procedures risks minimizing the agency's use of its expertise to carry out its congressional-established mission.

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I. INTRODUCTION

Many courts and academics critique tax exceptionalism and disagree that there is something different or exceptional about the federal income tax.¹ Critics often complain that the Treasury Department, and the Internal Revenue Service (Service) as a bureau of the Department, issues guidance implementing the Internal Revenue Code using different processes than those used by other agencies. Its ability to use special processes and have its guidance respected by the courts may not be long lived. The Supreme Court recently stated that, absent a justification to do so, it was “not inclined to carve out an approach to administrative review good for tax law only.”² The D.C. Circuit subsequently noted in another case that “[t]he IRS is not special” with respect to the application of general administrative law.³ Because of its unique procedures, the Tax Court has held Treasury regulations invalid.⁴ This movement to conformity pleases many of the tax professors who have written on this topic.⁵

¹ Lawrence Zelenak defined tax exceptionalism as “the notion that tax law is somehow deeply different from other law.” Lawrence Zelenak, *Maybe Just a Little Bit Special, After All?*, 63 DUKE L.J. 1897, 1901 (2014). There have been several conferences on anti-tax exceptionalism (ATPI’s Tax Law and Administrative Law: The Implications of *May Foundation v. U.S.* (2016); Duke Law School’s Taking Administrative Law to Tax (2014); Tax Policy Center’s American Corporate Tax Exceptionalism (2009)).

² *Mayo Foundation for Education and Research v. United States*, 562 U.S. 44, 55 (2011).

³ *Cohen v. United States*, 650 F.3d 717, 723 (D.C. Cir. 2011) (en banc).

⁴ See e.g., *Altera Corp. v. Commissioner*, 145 T.C. No. 3 (2015).

⁵ See *infra* note 25. Professor Paul Caron, of the TaxProf.blog, once criticized “tax myopia” and the “myth that tax law is fundamentally different from other areas of law.” Paul Caron, *Tax Myopia, or Mamas Don’t Let Your Babies Grow Up To Be Tax Lawyers*, 13 VA. TAX REV. 517, 518, 531 (1994).

Despite this attack on tax exceptionalism, the wide reach of the federal tax system makes many taxpayers feel there is something unique about it.⁶ In 2014, over 240 million federal tax returns were filed, of which over 147 million were individual returns.⁷ Over 118 million individual taxpayers received refunds, including almost 24.5 million who received refunds through the earned income tax credit, the largest redistribution program in the United States.⁸ Almost 1.4 million returns were audited.⁹ Compare this to the 1.34 million active military personnel,¹⁰ the 963,739 bankruptcy petitions,¹¹ the 376,576 civil and criminal cases filed in the U.S. district courts,¹² the 214,149 total federal inmates.¹³ More people interact with the tax system than with any other part of the federal government. This is not to minimize the importance of other areas of the federal government but to underscore the expansive reach of the federal income tax.

Since the federal income tax's enactment in 1913, the number of tax returns filed annually has increased dramatically. Between 2003 and 2013 alone, the number of individual tax returns was up eleven percent and business returns up twenty-three percent.¹⁴ In addition, Congress has added new initiatives to the Service's burdens, such as implementing national responses to taxpayer identity theft, monitoring foreign bank accounts and offshore assets, and administering credits and penalties under the Patient Protection and Affordable Care Act.¹⁵ Taxpayer questions are to be answered, tax returns processed, some returns audited, and refunds paid as a bevy of social, economic, and political policies operate through the tax

⁶ Zelenak, *supra* note 1, at 1901.

⁷ INTERNAL REVENUE SERVICE, 2014 DATA BOOK, at 4, tbl 2, <https://www.irs.gov/pub/irs-soi/14databk.pdf>.

⁸ *Id.* at 17, tbl. 7.

⁹ *Id.* at 23, tbl. 9a.

¹⁰ U.S. DEFENSE MANPOWER DATA CENTER, ACTIVE DUTY MILITARY STRENGTH BY SERVICE, HISTORICAL REPORTS FY 2013 – 2015, https://www.dmdc.osd.mil/appj/dwp/dwp_reports.jsp.

¹¹ ADMINISTRATIVE OFFICE OF UNITED STATES COURTS, JUDICIAL BUSINESS 2014, <http://www.uscourts.gov/statistics-reports/judicial-business-2014>.

¹² *Id.*

¹³ FEDERAL BUREAU OF PRISONS, STATISTICS, https://www.bop.gov/about/statistics/population_statistics.jsp#old_pops (last visited Mar. 19, 2016).

¹⁴ Jeremy Temkin, *Internal Revenue Service Budget Cuts Spell Trouble*, N.Y. L.J. vol 253–no.14 (Jan. 22, 2015) (in nominal terms, the 2005 budget was \$10.2 billion and 2015 budget was \$10.9 billion).

¹⁵ *IRS Actions to Reduce Improper Payments, Hearings Before the Subcomm. on Gov't Operations of the H. Comm. On Oversight and Government Reform*, 113th Cong. 61–76 (July 9, 2014) (statement of John A. Koskinen, Commissioner, Internal Revenue Service); 26 U.S.C. § 1471 (2012); Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119, 145 (2010).

system.¹⁶

Notwithstanding its importance to the federal government, “[n]o member of Congress ever got a single vote by telling his constituency that he got more resources for the IRS.”¹⁷ The Service’s budget has had a twelve percent reduction over the last ten years when adjusted for inflation, although the nominal budget has increased modestly.¹⁸ Since 2010, there have been substantial staff reductions in auditing and collection (an 11.9% and 21.4% decline, respectively).¹⁹ As it currently operates, the tax system is forced to do much with little.

In order to facilitate tax filings and the implementation of congressional initiatives, the Treasury Department issues significant amounts of guidance to taxpayers and Service personnel. Certainly there remain imperfections in published tax guidance, but most tax practitioners are pleased with the guidance that is issued.²⁰ “[I]f a regime is designed to give bureaucrats flexibility and hold them accountable for their results — a management technique taught in many business schools . . . — then Treasury’s administrative model might seem to be an exemplar rather than a problem.”²¹

Tax guidance is created using a relatively small percentage of department resources. In its last budget report, the Treasury Department estimated it spends approximately 3.5% of its enforcement budget issuing guidance.²² Recently, while using fewer employee hours, the Department has continued to publish significant amounts of guidance.²³ Nevertheless, budget pressure may threaten the production of guidance even as reduced funding increases guidance’s importance for facilitating accurate tax filings and tax compliance.²⁴

Despite the Treasury Department’s success in interpreting the tax on a

¹⁶ NATIONAL TAXPAYER ADVOCATE, ANNUAL REPORT TO CONGRESS, at vii–ix (2014).

¹⁷ George Guttman, *The IRS’s Fiscal 2004 Budget: More or Less*, 98 TAX NOTES 486, 488 (2003) (quoting Larry Levitan).

¹⁸ Temkin, *supra* note 14.

¹⁹ *Id.*

²⁰ See Roundtable on *Taxes and the Guidance Problem: How to Address the Growing Problem of Inadequate Guidance*, 2011 TNT 142-100 (July 22, 2011); Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury’s (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 NOTRE DAME L. REV. 1727, 1800 (2007).

²¹ David Zaring, *Administration by Treasury*, 95 MINN. L. REV. 187, 241 (2010).

²² U.S. DEPT. OF THE TREAS., THE BUDGET IN BRIEF 13–14 (2015), https://www.treasury.gov/about/budget-performance/budget-in-brief/Documents/Treasury_FY_2015_BIB.pdf.

²³ *Tax Administration: Letting Practitioners Help Write Guidance Poses No More Risk of Influence, TIGTA Says*, Daily Tax Rep. (BNA), No. 48 at G-6 (Mar. 12, 2008).

²⁴ Rev. Proc. 2013-32, 2013-28 I.R.B. 55 (restricting the issuance of private letter rulings).

limited budget, critics prefer that generally applicable regulatory rules be imposed more completely on the tax process.²⁵ They complain that “changes in administrative law doctrine . . . have not penetrated fully into IRS practice or judicial precedents concerning IRS rules and regulations.”²⁶ Professor Kristin Hickman has been most prolific on this topic, writing that the Treasury Department fails to comply with the Administrative Procedure Act (APA).²⁷ According to this argument, failing to comply with procedural requirements should prevent tax guidance from being given the force of law.

However, other scholars argue that “the rules that apply trans-substantively across the rest of the legal landscape do not, or should not, apply to tax.”²⁸ To the extent tax is exceptional, the Treasury Department requires exceptional procedures to accomplish all that it is tasked with accomplishing. This argument is consistent with the claim that each substantive area of law should have different procedures catered to the agency’s mission.²⁹ Professors Ernest Gellhorn and Glen Robinson object to imposing particular procedures on all agencies because they fear the misapplication of procedure in different administrative contexts.³⁰ An

²⁵ See Kristin E. Hickman, *Unpacking the Force of Law*, 66 VAND. L. REV. 465 (2013); Kristin E. Hickman, *Agency-Specific Precedents*, 89 TEX. L. REV. 89 (2010); Kristin Hickman, *The Need for Mead*, 90 MINN. L. REV. 1537 (2006); Steven R. Johnson, *Preserving Fairness in Tax Administration in the May Era*, 32 VA. TAX REV. 269 (2012); Leandra Lederman, *The Fight Over ‘Fighting Regs’ and Judicial Deference in Tax Litigation*, 92 B.U. L. REV. 643 (2012); Shannon Weeks McCormack, *Tax Abuse According to Whom?*, 15 FLA. TAX REV. 1 (2013); Toni Robinson, *Retroactivity: The Case for Better Regulation of Federal Tax Regulators*, 48 OHIO ST. L.J. 773, 775 (1987). But see Bryan Camp, *A History of Tax Regulation Prior to the Administrative Procedure Act*, 63 DUKE L.J. 1673, 1682 (2014); Richard Murphy, *Pragmatic Administrative Law and Tax Exceptionalism*, 64 DUKE L.J. ONLINE 21, 21 (2014); Richard J. Pierce, Jr., *Which Institution Should Determine Whether an Agency’s Explanation of a Tax Decision is Adequate?: A Response to Steve Johnson*, 64 DUKE L.J. ONLINE 1, 12 (2014); James Puckett, *Structural Tax Exceptionalism*, 49 GA. L. REV. 1067 (2015); Zelenak, *Maybe Just a Little Bit Special*, *supra* note 1. Professor Zaring notes not only the Service’s exceptionalism but that of the entire Treasury Department (although potentially comparable to Department of Defense and Department of State). Zaring, *Administration by Treasury*, *supra* note 21, at 238.

²⁶ Richard Levy & Robert Glicksman, *Agency-Specific Precedents*, 89 TEX. L. REV. 499, 500 (2011).

²⁷ Hickman, *Agency-Specific Precedents*, *supra* note 25; Kristin E. Hickman, *A Problem of Remedy: Responding to Treasury’s (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 76 GEO. WASH. L. REV. 1153 (2008); Hickman, *Coloring Outside the Lines*, *supra* note 20; Hickman, *Unpacking the Force of Law*, *supra* note 25.

²⁸ Zelenak, *supra* note 1, at 1901.

²⁹ Connor Raso, *Agency Avoidance of Rulemaking Procedures*, 67 ADMIN. L. REV. 65 (2015); Ernest Gellhorn & Glen O. Robinson, *Perspectives on Administrative Law*, 75 COLUM. L. REV. 771, 787 (1975).

³⁰ Gellhorn & Robinson, *supra* note 29, at 787–88, 793.

alternative way to evaluate procedures, according to Professor Ellen Aprill, is for courts to focus on whether the agency's resulting substantive position is consistent with what Congress tasked the agency to do.³¹

Instead of forcing all agencies to conform to one set of principles, Congress and the courts should figure out which principles work in different contexts to accomplish administrative law's underlying objectives. Tax has some notable "atypical features"³² and no system is perfect, but the Treasury Department and the Service have developed ways to address many of the pervasive concerns in administrative law. Though it operates on a relatively low budget and has little public or congressional support, the tax administration provides taxpayers a tremendous amount of guidance in various levels of specificity to facilitate agency consistency and taxpayer compliance. Examining the process the government uses to create tax guidance with an eye to the final product, as opposed to comparing the process to the directives of the APA, provides a better means of evaluating what the government does correctly and what could be improved.

This article proceeds in three parts. In Part II, the article examines what is currently known about the Treasury Department's procedures for issuing tax guidance and what deference courts attribute to that guidance. Many questions remain to be answered. The Treasury Department's process should be researched empirically, with comparison to processes used by other agencies. As a result of incomplete information, this article fails to quantify the degree to which taxpayers participate in the process or the consideration the agency gives to input from various groups of taxpayers.

This lack of agency-specific information might explain some of the critiques of the tax system's procedure. It is easier (although still a commendable task) to quantify adherence, or the lack thereof, to the mechanics of the notice and comment process than to assess whether the guidance-creating process accomplishes underlying policy goals. Courts have listed many requirements for documentation under notice and comment that can be verified. However, it is impossible to quantify the value of each step of the increased process, especially as compared to the undocumented process that is currently used.

Building on the limited research that is available, Part III analyzes what critics fail to admit. Critics of the Treasury Department often lambast the process for creating tax guidance without including in their analysis the APA's well-known problems and the impact that these problems might have

³¹ Ellen P. Aprill, *Muffled Chevron: Judicial Review of Tax Regulations*, 3 FLA. TAX REV. 51, 87 (1996).

³² *Id.* at 53; see also Joana Que, Note, *The State of Treasury Regulatory Authority After Mayo Foundation: Arguing for an Intentionalist Approach at Chevron Step One*, 85 S. CAL. L. REV. 1413 (2012).

on the creation of tax guidance or the operation of the tax system. By comparing the tax system's procedures to the APA without a review of the APA's problems, such as ossification in the creation of guidance, it is possible critics will make the idea of an impossibly perfect process the enemy of good tax guidance. In doing so, critics might even thwart seemingly unrelated congressional objectives by making it impossible for the Treasury Department to achieve all of its mandates.

In the binary discussion of tax guidance procedures versus the APA, critics also fail to examine whether the process for creating tax guidance is exceptional vis-à-vis that used by other agencies. In other words, tax-centric critics may be holding tax to a uniquely high standard. Instead of critiquing tax as an isolated area of law, tax scholars should integrate federal taxation into larger administrative debates. It is insufficient to merely incorporate broad administrative overviews into a tax analysis. Failing to challenge or add to existing theory denies administrative law the opportunity of seeing tax procedures as an alternative. Moreover, it fails to prevent the problems identified in administrative law from being imported into the tax system. Dean Erwin Griswold wrote in the 1940s, "It is high time that tax lawyers rise up to defend themselves against the charge that tax work is narrowing and stifling."³³ Tax has much expertise to offer other areas of law, including its rather nimble creation of guidance.

Part IV discusses two specific challenges that the Treasury Department is able to overcome using the current process of tax guidance formation. These benefits are at risk of being lost through a standardization of process. First, tax guidance faces many attempts at information capture by which interested parties may purposely (or not) control the content of regulatory guidance. The theory of information capture suggests wealthy and organized taxpayers could gain an advantage in the creation of favorable tax guidance by flooding the Treasury Department with information. The Department must filter massive amounts of information to create fair guidance.

Although more input from the poor and other relatively less organized groups is needed, the Treasury Department demonstrates some means of filtering information and balancing views despite a widespread perception that tax is too complex for anyone to understand. Attempting to increase participation at the cost of a more formalized process might result in reduced or less meaningful participation from those who are currently least likely to participate in tax discussions. Focusing on the goal of balanced participation leads to different solutions than focusing on the APA.

Second, tax currently operates with reasonable heuristics, or rules of thumb, that guide revenue agents, taxpayers, and courts to interpret

³³ Erwin N. Griswold, *The Need for a Court of Tax Appeals*, 57 HARV. L. REV. 1153, 1183 (1944).

complicated tax statutes. These heuristics are necessary because, despite the Code being a complex statute that creates a complex regime, it fails to provide specific guidance for every circumstance. Congress vests significant discretion in the Treasury Department to administer the system, and one means of construing that discretion is through the use of heuristics that facilitate decision-making.

Increasing procedure would require the Treasury Department to exercise its discretion before the application of the law, nullifying one of the Treasury Department's strengths. Responding to comments that would almost certainly have the goal of tax minimization through explicit rules that can be planned around would threaten the heuristics that can counteract tax planning. Instead of procedure-laden, complex rules, rules of thumb have historically helped the system function and allowed the government to respond to changing laws and taxpayer activities.

Part V concludes that to the extent the processes used to create tax guidance accomplish the goals of administrative law, its exceptionalism offers a way of producing guidance without some of the problems associated with compliance with the APA. Congress and courts should be wary of importing procedures from other areas of law into the tax system unless they are prepared to incorporate imperfections, which may be worse than the problems tax already suffers. It may be unpopular to argue that the Service is doing something right, but, with respect to the issuance of tax guidance, the Service's good is better than the less exceptional alternative.

II. THE CURRENT PROCESS

Congress is responsible for creating the Internal Revenue Code, which the president signs into law, but it falls to the Treasury Department to interpret and apply the statute in the first instance. The Treasury Department, and the Service within it, creates a regime that must be used by hundreds of millions of taxpayers. They create this regime through regulations and other guidance that either explains or supplements the Code. Once made, this guidance is granted varying levels of deference by the courts. Both the creation of tax guidance and the deference given it are subject to exceptionalism critiques that, if successful, would limit its creation or application to taxpayers.

A. Creating Tax Guidance

The Treasury Department and the Service issue numerous forms of tax guidance, and there are different procedures for the creation of each type. Only broad outlines of those procedures are made public, but it is clear that Treasury Department procedures receive varying amounts of internal and external review. These procedures developed not out of the agency's

founding statute but from a need to provide information to Service employees and the public. Because the Treasury Department is a large organization with many functions, not everything that is produced is given extensive review. This longstanding Treasury Department practice favoring the prompt creation of guidance predates the APA and has continued even after changes in general administrative law.³⁴

Treasury regulations are the most authoritative form of tax guidance but, nonetheless, only skeletal outlines are available for how they are developed or even how issues are targeted for guidance. Under current procedures, the Service annually solicits taxpayer input as to what guidance is most needed.³⁵ However the process by which the Assistant Secretary of Tax Policy puts those proposals into a semiannual agenda is not described. And new legislation or events might change listed priorities on the agenda without notice. During his extensive career as a tax attorney and at accounting firms, Phillip Gall noted that how and why projects appear on that list is “somewhat mysterious.”³⁶ This may be in, in part, because for much of the last decade, there was no confirmed Assistant Secretary for Tax Policy to guide this process.³⁷ After being placed on the agenda, initiated projects are assigned to the Office of the Chief Counsel of the Internal Revenue Service, effectively the Service’s internal law firm, to being the drafting process.³⁸

The public may be alerted to the agency’s interpretation of an issue at different times in the drafting process. Early in the rulemaking process, the Treasury Department may issue an Advance Notice of Proposed Rulemaking. Such a notice describes a problem or situation about which the agency is considering issuing published guidance, describes the anticipated approach, and solicits public feedback on that approach.³⁹ Whether or not an Advance Notice of Proposed Rulemaking is issued, a Notice of Proposed Rulemaking announces proposed regulations published in the Code of Federal

³⁴ Levy & Glicksman, *supra* note 26, at 554.

³⁵ *Transcript Available of Tax Analysts’ Roundtable on ‘Taxes and the Guidance Problem,’* 2011 TNT 142-100 (Jul. 22, 2011); *Tax Administration: Letting Practitioners Help Write Guidance Poses No More Risk of Influence, TIGTA Says*, Daily Tax Rep. (BNA), No. 48 at G-6 (Mar. 12, 2008). In the 1950s, the Assistant Secretary to Treasury explained then-current procedures. See Laurens Williams, *Preparation and Promulgation of Treasury Department Regulations Under Internal Revenue Code of 1954*, in 8 MAJOR TAX PLANNING 733, 748–50 (1956).

³⁶ Phillip Gall, *Phantom Tax Regulations: The Curse of Spurned Delegations*, 56 TAX LAW. 413, 416 (2003).

³⁷ Amy S. Elliott, *Roundtable Panelists Bemoan Tax Guidance Processes*, 132 TAX NOTES 473 (2011).

³⁸ Treas. Reg. § 601.601(a)(1).

³⁹ I.R.M. 32.1.1.2.1 (Sept. 23, 2011).

Regulations with draft language.⁴⁰

The method by which proposed regulatory language is drafted is described in the Service's Internal Revenue Manual.⁴¹ A drafter and a reviewer from the same Office of Chief Counsel that created the regulatory agenda and an attorney from the Treasury Department Office of Tax Policy (the agency that establishes policy criteria) consider projects slated for regulations. These three, possibly joined by others, jointly identify issues, informally exchange drafts of regulations, and hold guidance briefings as needed. Before being proposed to the public, the draft language is submitted to various constituents within the Treasury Department in order to build widespread internal acceptance of its content.⁴² Only when the language reaches the highest level of internal review is input received from outside the Department, the executive's Office of Management and Budget.⁴³ If the Assistant Secretary for Tax Policy signs off on the proposed language, it becomes a proposed regulation ready to be published and sent to the Service. This first internal step takes anywhere from months to years.⁴⁴

Once published in proposed form, the group of drafters solicits public comments. According to the Internal Revenue Manual, although the public may voice its opinion on regulatory topics at any time, the public is not to see the draft language until a proposed regulation is released and comments publicly solicited. The public may then comment in writing via the notice and comment process, but only if that process is available.⁴⁵ This is the only official time the Department receives feedback on regulations from taxpayers or their representatives.⁴⁶

Notwithstanding this formal process, many scholars argue that the majority of comments received on tax regulations are informal and delivered

⁴⁰ I.R.M. 32.1.1.2.2 (Sept. 23, 2011).

⁴¹ I.R.M. 32.1.1 (Sept. 23, 2011); *see also* MICHAEL SALTZMAN & LESLIE BOOK, IRS PRACTICE AND PROCEDURE ¶3.02[2] (2016); Michael Asimow, *Public Participation in the Adoption of Temporary Tax Regulations*, 44 TAX LAW 343, 366–68 (1991); Gall, *supra* note 36, at 416; Monte A. Jackel, *Is There Anything Wrong With the Guidance Process?*, 132 TAX NOTES 935 (2011); Williams, *supra* note 35, at 748–50.

⁴² *Transcript Available of Tax Analysts' Roundtable on 'Taxes and the Guidance Problem'* 2011 TNT 142-100 (Jul. 22, 2011), at 7–12 (remarks by Mike Desmond).

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ I.R.M. 32.1.7.2 (Aug. 19, 2011).

⁴⁶ There are other, less-participatory means of rulemaking not used in the tax area. Direct final rulemaking permits the agency to publish a rule and then solicit public feedback; if objections are received the rule is normally withdrawn and submitted for notice and comment. *See* Ronald M. Levin, *Direct Final Rulemaking*, 64 GEO. WASH. L. REV. 1 (1995); Ronald M. Levin, *More on Direct Final Rulemaking: Streamlining, Not Corner-Cutting*, 51 ADMIN. L. REV. 757 (1999). *But see* Lars Noah, *Doubts about Direct Final Rulemaking*, 51 ADMIN. L. REV. 401 (1999).

over the phone, seemingly violating the process outlined in the Internal Revenue Manual.⁴⁷ Without describing the public's involvement in detail, Professor Wendy Wagner states that most administrative agencies give interest groups extensive influence before notice and comment begins because agencies are aware that they must work closely with potential critics for rules to make it through the process.⁴⁸ It is clear that more information needs to be obtained regarding the amount and timing of public involvement that exists, especially informally, in the creation of tax guidance.

After the public comment period has lapsed, the group within the Treasury Department that proposed the regulation drafts issues memoranda summarizing the issues.⁴⁹ Assuming no major changes are required in response to comments, the group also prepares final regulations. The Commissioner (or Deputy Commissioner) of the Service and an Assistant Secretary (or Deputy Assistant) for Tax Policy sign the final proposal. If major changes are required, the process may begin again with another notice and comment period.

One concern with this process is that it is slow.⁵⁰ There are complaints about the lack of staffing and funding for those who draft and review regulations, as is undoubtedly common throughout the government; and the complaint regarding tax guidance is often that "being 'cheap' at the front end results in much more cost at the back end."⁵¹ Cost does constrain the issuance of guidance. For example, the Service recently announced it is restricting the issuance of one type of guidance in order to conserve agency resources.⁵²

Using this process, regulations can be initiated for any tax provision. Procedure may depend upon which provision is the source of authority for their issuance. Unlike other areas of law, tax persists in distinguishing between specific and general regulatory authority for guidance. This exceptionalism perseveres although the Code is not the only statutory system with both forms of authority.⁵³

Although the source of authority for particular regulations may have

⁴⁷ Asimow, *Public Participation*, *supra* note 41, at 366 n.104. Hickman, *A Problem of Remedy*, *supra* note 27, at 1205. Would commentators provide less of this free service if they needed to submit written documentation rather than just lift the phone?

⁴⁸ Wendy Wagner, *Administrative Law, Filter Failure, and Information Capture*, 59 DUKE L.J. 1321, 1381–83 (2010).

⁴⁹ I.R.M. 32.1.8.6 (Aug. 11, 2004).

⁵⁰ Jackel, *supra* note 41, at 936.

⁵¹ *Id.* at 935.

⁵² Rev. Proc. 2013-32, 2013-28 I.R.B. 1 (restricting the issuance of private letter rulings).

⁵³ See, e.g., Communications Act of 1934, Pub. L. No. 73-416, § 220, 48 Stat. 1067, 1068, 1078–80; Securities Act of 1933, Pub. L. No. 73-22, § 10(b)(4), 48 Stat. 74, 81 (containing both specific and general rulemaking authority).

little impact on the content of the final guidance, the Treasury Department maintains that it is important to link guidance back to the source of authority. As a broad grant of general regulatory authority, section 7805(a) gives the Treasury Department the power to develop “all needful rules and regulations for the enforcement of” the Code.⁵⁴ Additionally, some Code sections grant extremely broad specific authority. For example, section 1502 provides the Treasury Department the authority to develop whatever regulations are necessary to ensure affiliated corporations’ returns properly reflect income, and the regulations under section 1502 have become a web of law in their own right.⁵⁵ Finally, there are narrowly tailored specific delegations of authority that give the Department greater guidance as to Congress’s desires. For example, section 168(i)(5) calls for regulations to guide the determination of depreciation deductions with respect to tangible property if the property changes status during the year.⁵⁶

One reason the source of authority is considered important is that the Treasury Department contends guidance issued under general authority demands less formal procedures for its creation. Under the APA, regulations may be categorized as either legislative or interpretive,⁵⁷ and the Treasury Department often traces this classification to the source of authority. Legislative regulations provide operational rules for specific Code provisions and have the same authority as the law itself. The Treasury Department’s position is that legislative regulations normally originate from specific authority.⁵⁸ On the other hand, interpretive regulations merely explain the government’s position and, according to the Treasury Department, are issued under general authority.⁵⁹ Because the latter type of regulations merely interprets the law, instead of making it, the Treasury Department argues that these regulations are not subject to the same stringent procedural requirements as the former. Despite the importance of distinguishing between legislative and interpretive guidance, all administrative agencies find it difficult to draw the distinction.⁶⁰

Congress is aware, at least in some instances, that the Treasury Department retains this distinction between authorities and procedures. Pursuant to the Regulatory Flexibility Analysis Act (FRAA),⁶¹ agencies must

⁵⁴ I.R.C. § 7805(a) (2016).

⁵⁵ Treas. Reg. § 1.1502-0 through 1.1502-100.

⁵⁶ I.R.C. § 168(i)(5) (2016).

⁵⁷ 5 U.S.C. § 553; *see also supra* note 28.

⁵⁸ I.R.M. 32.1.1.2.8 (Sept. 23, 2011).

⁵⁹ *Id.*

⁶⁰ Camp argues that all early regulations were considered interpretive. Camp, *supra* note 25, at 1709–10.

⁶¹ 5 U.S.C. § 603(a) (2012).

analyze the impact of proposed rules on small businesses. The requirement generally applies only to rules that go through the APA's notice-and-comment procedures, which the Treasury Department contends only applies to specific authority or legislative regulations. Congress added a special requirement to the FRAA applicable only to tax to include interpretive rules as well as legislative ones.⁶² In doing so, Congress recognized that the Treasury Department makes a distinction and chose to override that distinction for a limited purpose without eliminating it.

Nevertheless, critics contend the Treasury Department's distinction between general and specific authority and, therefore, legislative and interpretive guidance should no longer apply.⁶³ Focusing on the potential penalties taxpayers face if they fail to follow interpretive regulations, Professor Kristin Hickman argues the distinction reflects a historical understanding no longer consistent with changes in administrative law doctrine, which push toward greater procedure for regulations.⁶⁴ According to this argument, all tax regulations need more arduous public review. Permitting the Treasury Department to maintain this distinction allows the Department to create law without undertaking the procedural steps required to do so. This also raises questions of agency overreaching. When the Treasury Department claims general authority as its basis for regulations, there is increased risk the Department creates guidance beyond the will of Congress and without a specific congressional mandate to do so.⁶⁵

In addition to deriving from different legal bases, tax regulations also come in three different forms: final, temporary, and proposed. Final regulations are the most authoritative and have completed all internal and external review. Proposed regulations are those that have completed internal review but have not yet completed the public's review. Proposed regulations provide insight into how the Service interprets the law. Taxpayers cannot rely on proposed regulations to support a tax position or for planning purposes unless the Service clearly states otherwise, and proposed regulations are not

⁶² *Id.* (The requirement applies to a general notice of proposed rulemaking or a "notice of proposed rulemaking for an interpretative rule involving the internal revenue laws of the United States . . .").

⁶³ Asimow, *Public Participation*, *supra* note 41, at 357–58; Steve Johnson, *Intermountain and the Importance of Administrative Law in Tax Law*, 128 TAX NOTES 837 (2010).

⁶⁴ Richard E. Levy & Robert L. Glicksman, *Agency-Specific Precedents*, 89 TEX. L. REV. 499, 520 (2011).

⁶⁵ With increased procedure, there may be hope for judicial intervention against Treasury Department overreach, but that is limited by standing and pre-enforcement litigation restrictions. Mark E. Berg, *Judicial Deference to Tax Regulations: A Reconsideration in Light of National Cable, Swallows Holding, and Other Developments*, 61 TAX LAW. 479, 481 (2008).

binding on the Service, even though the Service's policy is to follow them.⁶⁶ Finally, temporary regulations are issued simultaneously with proposed regulations.⁶⁷ Temporary regulations have the same authority as final regulations despite rarely going through notice and comment.⁶⁸

It is temporary regulation's combination of speedy publication without public review that subjects this form of regulations to criticism but makes the form popular with the Treasury Department.⁶⁹ And they are pervasive. The Treasury Department has issued a significant number of temporary regulations since a backlog of statutes needing guidance was enacted in the 1980s.⁷⁰ In a study of 232 regulatory projects, from January 1, 2003 through December 31, 2005, more than one-third were issued with only post-promulgation notice and comment.⁷¹ The Treasury Department claimed more than 90 percent of these were interpretive and that public comment was not required.⁷² Some complain that temporary regulations' lack of procedure "obliterates the APA's notice-and-comment procedures."⁷³ In 1991, Professor Michael Asimow predicted "the inevitable waive of litigation" about the validity of temporary regulations that has yet to occur.⁷⁴

By law, temporary regulations are only effective for three years,⁷⁵ requiring the Treasury Department to finalize these regulations or they lose their authority. Despite current procedures, a question remains whether temporary regulations also need the same process of ex ante public comment as final regulations. The Treasury Department has argued, unsuccessfully,

⁶⁶ I.R.M. 32.1.1.2.2 (Sept. 23, 2011); I.R.S. Gen. Couns. Mem. CC-2003-014 (May 8, 2003).

⁶⁷ Section 7805(e) of the Code requires the Treasury Department to issue proposed regulations when it issues temporary regulations, and proposed regulations presumably are subject to notice and comment. I.R.M. 32.1.1.2.2 (Sept. 23, 2011).

⁶⁸ I.R.S. Gen. Couns. Mem. CC-2003-014 (May 8, 2003).

⁶⁹ See Asimow, *Public Participation*, *supra* note 41, at 363–64; Johnson, *Intermountain*, *supra* note 63, at 838; Kristin Hickman & Mark Thomson, *Open Minds and Harmless Errors: Judicial Review of Post-Promulgation Notice and Comment*, 101 CORNELL L. REV. 216, 282 (2016); Hickman, *Unpacking the Force of Law*, *supra* note 25, at 496 n.168; Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Regulations: An Analysis of the Administrative Procedure Act, Legislative Reenactment Doctrine, Deference, and Invalidity*, 3 HOUS. BUS. & TAX L.J. 248, 253 (2003). One can think of temporary regulations as either (1) a prelude to a final regulation or (2) as permitting the parties to see potential problems, debate solutions, and mitigate the problems.

⁷⁰ Asimow, *Public Participation*, *supra* note 41, at 343; Hickman, *Unpacking the Force of Law*, *supra* note 25, at 498.

⁷¹ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1748–51.

⁷² *Id.*

⁷³ Vasquez & Lowy, *Challenging Temporary Regulations*, *supra* note 69, at 253.

⁷⁴ Asimow, *Public Participation*, *supra* note 41, at 370.

⁷⁵ I.R.C. § 7805(e).

that Congress provided the short period of effectiveness and required the simultaneous issuance of proposed regulations as a political trade off permitting the continued, shorter-term use of temporary regulations without notice and comment.⁷⁶ According to this interpretation, Congress authorized a tax-specific exception to notice-and-comment for temporary regulations for three years.⁷⁷

It is plausible, but unproven, that Congress was aware of the backlog of statutes and taxpayers' desire for guidance and expected the Treasury Department to continue issuing temporary legislative regulations but with post-promulgation notice and comment. If that was the case, Congress did not say so, and Congress has been explicit about trade-offs in other contexts. For example, Congress explicitly permitted regulations with post-promulgation comments with respect to the Health Care Portability and Accountability Act of 1996.⁷⁸

Even with the existence of proposed and temporary regulations, regulations are not written for every statute that requires them. Guidance projects may "linger or die" as a result of changes in Treasury Department personnel or the project's politicization.⁷⁹ The Treasury Department's failure to issue regulations, when given a congressional mandate to do so, can be as deleterious as drafting inappropriate regulations.⁸⁰ When Congress delegates specific authority to the Treasury Department to issue regulations but regulations are not forthcoming, courts may be forced to invoke phantom regulations as though some form of regulation had been issued in order to apply the law.⁸¹

The issue of phantom regulations is not without debate. The Tax Court once concluded that "the Secretary may not prevent implementation of a tax benefit provision simply by failing to issue regulations."⁸² The alternative would give the Treasury Department the power to defeat a congressionally-mandated tax provision "merely by failing to discharge the statutorily

⁷⁶ *Intermountain Ins. Serv. of Vail, LLC v. Commissioner*, 134 T.C. 211, 245 (2010), *rev'd on other grounds*, 650 F.3d 691 (D.C. Cir. 2011).

⁷⁷ *Id.* at 245–46. Judges Halpern and Holmes of the Tax Court rejected this interpretation.

⁷⁸ I.R.C. § 9833, Pub. L. No. 04-191, title IV, § 401(a) (1996).

⁷⁹ Jackel, *supra* note 41, at 936.

⁸⁰ See Michael Livermore & Richard Revesz, *Regulatory Review, Capture, and Agency Inaction*, 101 GEO. L.J. 1337, 1341 (2013).

⁸¹ *But see* *Temco Helicopters, Inc. v. United States*, 409 Fed. Appx. 64, 67–68 (2010); *Francisco v. Commissioner*, 119 T.C. 317, 322–23 (2002), *aff'd*, 370 F.3d 1228 (D.C. Cir. 2005); *Hillman v. Commissioner*, 114 T.C. 103, 110 (2000); *Estate of Neumann v. Commissioner*, 106 T.C. 216, 220–21 (1996).

⁸² *Francisco*, 119 T.C. at 324.

imposed duty to promulgate the required regulations.”⁸³ Courts can also seek to compel the creation of regulations but, with limited agency resources, only so much can practically be done.

As the Treasury Department fails to issue all requisite regulations, the Service issues many other forms of guidance that are made public as a result of the Freedom of Information Act.⁸⁴ These other forms of tax guidance are given less high-level internal evaluation and often lack formalized external review. Revenue Rulings are public administrative rulings that apply to particular factual situations. Revenue Procedures are akin to Revenue Rulings but traditionally focus on procedural, rather than substantive, aspects of the tax system. Public notices are viewed by the Service as equivalent to rulings but tend to be issued more quickly in response to public concerns.⁸⁵ Less general are private letter rulings issued to particular taxpayers seeking binding guidance for proposed transactions and numerous types of guidance issued to Service agents in the process of audits or on particular matters.

It is one of the latter, less general forms of guidance that incorporates the greatest amount of taxpayer information in its creation and is currently threatened by budget cuts.⁸⁶ When a taxpayer requests a private letter ruling, the taxpayer begins an extensive dialogue with the Service as the taxpayer must provide satisfactory information to receive the ruling.⁸⁷ This dialogue is necessary because these rulings function akin to an audit prior to the submission of a tax return. Although it is not necessarily indicative of taxpayer involvement in the creation of other guidance and it is only binding on the Service and the taxpayer making the request, private letter rulings illustrate departmental capacity for interpreting information received from taxpayers.

Historically, there has been little complaint from practitioners about any of the forms of tax guidance, particularly on procedural grounds. “Most members of the tax community believe that Treasury does a decent job in drafting regulations and instead focus their grumbling on issues where guidance is lacking.”⁸⁸ With respect to Treasury Department and Service guidance, Linda Stiff, Managing Director with PricewaterhouseCoopers and former Acting Commissioner of the Service, stated, “I personally believe that the process is neither fundamentally or [sic] inherently bad or [sic] failed or

⁸³ *Occidental Petroleum Corp. v. Commissioner*, 82 T.C. 819, 829 (1984); *see also Int'l Multifoods Corp. v. Commissioner*, 108 T.C. 579, 587 (1997).

⁸⁴ John F. Coverdale, *Court Review of Tax Regulations and Revenue Rulings in the Chevron Era*, 64 GEO. WASH. L. REV. 35, 51–52 (1995).

⁸⁵ Rev. Rul. 87-138, 1987-2 C.B. 287.

⁸⁶ *See* Rev. Proc. 2013-32, 2013-28 I.R.B. 1.

⁸⁷ I.R.M. 32.3.2 (Jul. 9, 2014); Rev. Proc. 2015-1, 2015-7 I.R.B. 1.

⁸⁸ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1800.

[sic] completely ineffective as I've heard some say."⁸⁹ That sense may be changing. Professor Hickman argues that the reason for the past failure to complain stemmed not from not a rational ignorance of administrative law or a love for the guidance itself but from procedural limitations as to what a taxpayer may gain from such a challenge. Those limits reduce taxpayers' desire to bring procedural suits.⁹⁰

Unlike with other agencies, public challenges to (as opposed to comments on) tax guidance are explicitly limited. Almost all legal challenges to tax guidance are deferred until after a taxpayer is audited, is found to owe tax, and has completed the agency's appeals process. The source of this bar is, first, the Tax Anti-Injunction Act and the Declaratory Judgment Act that isolate Treasury Department rules from pre-enforcement challenges, whether on substantive or procedural grounds. The Anti-Injunction Act denies injunctive relief by generally prohibiting "suit for the purpose of restraining the assessment or collection of any tax . . . whether or not such person is the person against whom such tax was assessed."⁹¹ The Declaratory Judgment Act contains a tax exception that prevents courts from providing pre-enforcement declaratory relief for controversies "with respect to Federal taxes."⁹²

Courts have interpreted the Tax Anti-Injunction Act and the Declaratory Judgment Act coextensively⁹³ and broadly.⁹⁴ Neither provision's legislative history provides much evidence of congressional intent,⁹⁵ but the Supreme

⁸⁹ Transcript Available of Tax Analysts' Roundtable on 'Taxes and the Guidance Problem,' 2011 TNT 142-100 (Jul. 22, 2011).

⁹⁰ Hickman, *Agency-Specific Precedents*, *supra* note 25; Hickman, *A Problem of Remedy*, *supra* note 27, at 1156.

⁹¹ See Ellen Aprill, *The Impact of Agency Procedures and Judicial Review on Tax Reforms*, 65 NAT'L TAX J. 917 (2012); Paul H. Asofsky, *Injunctions and Declaratory Judgments in Federal Tax Controversies*, 28 RUTGERS L. REV. 785, 786 (1975); Hickman, *A Problem of Remedy*, *supra* note 27, at 1165-81; James Lenoir, *Congressional Control over Suits to Restrain the Assessment or Collection of Federal Taxes*, 3 ARIZ. L. REV. 177 (1961); Richard Murphy, *Pragmatic Administrative Law and Tax Exceptionalism*, 64 DUKE L.J. ONLINE 21, 23 (2014); Gale Ann Norton, *The Limitless Federal Taxing Power*, 8 HARV. J.L. & PUB. POL'Y 591, 622-23 (1985). The Supreme Court has not declared that cases regarding procedural rules cannot be litigated pre-enforcement. Hickman, *Agency-Specific Precedents*, *supra* note 25, at 99-100. Scholars note two common law exceptions that permit litigation but generally find the exceptions insufficient. Hickman, *A Problem of Remedy*, *supra* note 27, at 1169-73.

⁹² 28 U.S.C. § 2201(a) (2012).

⁹³ Hickman, *A Problem of Remedy*, *supra* note 27, at 1166.

⁹⁴ *Id.* at 1167. As a specific enactment, § 7421 trumps the APA as a general statute.

⁹⁵ Paul H. Asofsky, *Injunctions and Declaratory Judgments in Federal Tax Controversies*, 28 RUTGERS L. REV. 785, 787-88 (1975); Note, *Enjoining the Assessment and Collection of Federal Taxes Despite Statutory Prohibition*, 49 HARV. L. REV. 109, 109 (1935).

Court often identifies a revenue-raising function.⁹⁶ As a result, these statutes often prevent pre-enforcement legal challenge to tax statutes and, therefore, are likely to increase government revenue. Even when injunction and declaratory judgment actions occur, they are rarely successful.⁹⁷

Recently, the Supreme Court circumvented these limitations on pre-enforcement litigation in a way that might reduce tax's exceptionalism in the future. A case regarding the individual mandate in the Patient Protection and Affordable Care Act of 2010 seemed to present a conflict between the penalty as a tax to establish its constitutional basis and as a tax for these statutory prohibitions on pre-enforcement litigation.⁹⁸ Two former Service commissioners, Mortimer Caplin and Sheldon Cohen, filed an *amici curiae* brief arguing the Anti-Injunction Act and Declaratory Judgment Act prevented pre-enforcement judicial review of the mandate.⁹⁹ Nevertheless, the Supreme Court distinguished between a "tax" for statutory and constitutional purposes, denying the application of the Anti-Injunction Act and the Declaratory Judgment Act.¹⁰⁰

Similarly, the Circuit Court narrowed its reading of these limitations in *Cohen v. United States*.¹⁰¹ The Supreme Court has denied certiorari, leaving the precedent in the Circuit Court of allowing pre-enforcement litigation when several taxpayers challenged special refund procedures from an invalidated telephone excise tax. The Service had issued those refund procedures in Notice 2006-50 without notice and comment.¹⁰² The taxpayers did not request a refund but challenged the Notice under with the APA. Narrowly reading the Anti-Injunction Act as not covering refunds, the court refused to create a broader tax exception from the challenges allowed by the APA.¹⁰³ Arguing for administrative law uniformity, the D.C. Circuit's majority concluded "[t]he IRS is not special in this regard; no exception exists shielding it – unlike the rest of the Federal Government – from suit under the APA."¹⁰⁴ The court permitted the challenge and, on remand, the District Court determined the notice was invalid per the APA.¹⁰⁵

⁹⁶ *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1, 7 (1962).

⁹⁷ Asofsky, *supra* note 95, at 786.

⁹⁸ Steve R. Johnson, *The Anti-Injunction Act and the Individual Mandate*, 135 Tax Notes 1395 (Dec. 12, 2011).

⁹⁹ *Id.*

¹⁰⁰ *Nat'l Fed'n of Indep. Bus. v. Sebelius*, 132 S.Ct. 2566 (2012).

¹⁰¹ *Cohen v. United States*, 650 F.3d 717 (D.C. Cir. 2011), *cert. denied* 135 S.Ct. 946 (2015).

¹⁰² I.R.S. Notice 2006-50, 2006-25 I.R.B. 1141.

¹⁰³ *Cohen*, 650 F.3d at, at 723–24 (holding that § 702 of the APA waives sovereign immunity for APA procedural challenges).

¹⁰⁴ *Id.* at 723.

¹⁰⁵ *In re Long-Distance Tel. Service Fed. Excise Tax Refund Litig.*, 853 F.Supp.2d 138

In addition to these statutory limitations, common law sovereign immunity and standing doctrine discourage or prohibit most pre-enforcement tax challenges, although these common law limitations are also under challenge.¹⁰⁶ Justiciability doctrines, such as standing and ripeness, complicate the prospects for tax litigation, even though these have been infrequently raised in the tax context because of the statutes described above.¹⁰⁷ Standing is more generally a problem for third parties seeking judicial action against Service guidance that is intended to apply to other taxpayers.¹⁰⁸ Cases on these common law limits are rare.

Notwithstanding the timing restrictions for procedural challenges to tax guidance, courts appear increasingly sympathetic to them. In *Dominion Resources Inc. v. United States*,¹⁰⁹ the Federal Circuit invalidated a regulation governing the capitalization of interest (as opposed to its current deductibility) on the grounds that it was not a reasonable interpretation of the statute.¹¹⁰ It troubled the court that the regulation was premised on a fiction that about the inability to sell component parts of a larger item. Not basing its decision on its evaluation of the fiction, the court concluded the regulation was arbitrary and capricious because the promulgation of the regulation did not have the judicially mandated reasoned explanation of the Treasury Department's decision-making.¹¹¹ From the tone of the opinion, it is unlikely any explanation would have satisfied the majority who disliked the particular fiction on which the regulations were based, even though the concurrence pointed out some fiction was likely inevitable.

(D.D.C. 2012). The case potentially opens the Treasury Department to significant, although not unlimited, litigation because it narrowly reads the Anti-Injunction Act's limitation as not involving the refund of taxes already collected. The practical result was that the Service did not create new procedures through notice and comment and the statute of limitations has closed for taxpayers who could be affected.

¹⁰⁶ Patrick Smith, *Standing Issues in Direct APA Challenges to Tax Regulations*, 149 TAX NOTES 1033 (Nov. 23, 2015).

¹⁰⁷ Karl Coplan, *Ideological Plaintiffs, Administrative Lawmaking, Standing, and the Petition Clause*, 61 ME. L. REV. 377 (2009); Hickman, *A Problem of Remedy*, *supra* note 27, at 1174–76; Lynn Lu, *Standing in the Shadow of Tax Exceptionalism*, 66 ADMIN. L. REV. 73 (2014); Elizabeth Magill, *Standing for the Public*, 95 VA. L. REV. 1131 (2009); Richard Stewart, *Standing for Solidarity*, 88 YALE L.J. 1559, 1568 (1979).

¹⁰⁸ Hickman, *A Problem of Remedy*, *supra* note 27, at 1175. The case-or-controversy requirement of Article III of the Constitution requires litigants to show an “injury in fact,” causation, and redressability. *Id.* at 1175–76. Ripeness requires that the issue be fit for judicial decision and that the parties experience hardship absent court consideration. *Id.* at 1179.

¹⁰⁹ *Dominion Resources Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012). For a discussion of this case, see Aprill, *Impact of Agency Procedures*, *supra* note 91, at 923.

¹¹⁰ Treas. Reg. 1.263A-11(e)(1)(ii)(B) (1995).

¹¹¹ *Dominion Resources, Inc.*, 681 F.3d at 1319. These problems existed before, but not as often. See *American Standard, Inc. v. United States*, 602 F.2d 256, 267 (Ct. Cl. 1979).

And in *Altera Corp. v. Commissioner*, a unanimous Tax Court invalidated certain transfer pricing regulations used by multi-national corporations.¹¹² When issuing the final regulations, the Treasury Department's files did not contain expert opinions, empirical data, or papers that supported its position, and its preamble, while responding to some comments, was held not to justify the final rule. Invalidating the regulations, the Tax Court disagreed with the Treasury Department that the APA did not apply and found the Treasury Department failed to engage in reasoned decision-making by not producing this evidence and not responding to several comments. As a result, the Treasury Department was found to have engaged in arbitrary and capricious decision-making.

Arguments against tax guidance's procedural exceptionalism are likely to continue. On the basis that the Code's general authority has the force of law and are, therefore, legislative, courts are likely to require the Treasury Department to follow notice and comment procedures absent an exemption. The result, however, is unlikely to be widespread invalidation of regulations. Under existing law, these regulations would likely, although not definitively, be remanded without vacatur.¹¹³ Nevertheless, even with additional time to comply with procedure, additional process for all tax guidance would threaten agency administration.

B. Deference thereto

Courts have devoted significant attention to the question of the appropriate level of deference to be given to agency-created guidance.¹¹⁴ They have a long history of deferring to agencies because, as the Supreme Court has concluded, courts are "not at liberty to substitute [their] own discretion for that of administrative officers who have kept within the bounds of their administrative powers."¹¹⁵ Unlike with older, tax specific precedent, today courts and most academics argue that the Treasury Department should enjoy the deference generally applicable to other administrative agencies. This results in significant deference to final, legislative regulations.¹¹⁶ It does

¹¹² *Altera Corp. v. Commissioner*, 145 T.C. No. 3 (2015). The government has filed notice of appeal.

¹¹³ Recent Case, *Administrative Law-Judicial Review of Treasury Regulations*, 126 HARV. L. REV. 1747, 1752-53 (2013).

¹¹⁴ Ellen Aprill, *A Case Study of Legislation vs. Regulation*, 63 DUKE L.J. 1636, 1642 (2014).

¹¹⁵ *AT&T Co. v. United States*, 299 U.S. 232, 236-37 (1936).

¹¹⁶ Jeremiah Coder, *Year in Review: Tax Law's Vanity Mirror Shattered*, 134 TAX NOTES 35 (2012). The reenactment doctrine might have held on the longest in tax with the Treasury Department arguing for departmental interpretations if Congress re-enacted a statute without adjusting for the agency's interpretation. In *Newark Morning Ledger Co. v. United States*, 507

not clarify the amount of deference that should be given other types of regulations — interpretive, proposed, temporary — and deference to other tax guidance is even more uncertain.¹¹⁷

Generally applicable standards of deference to administrative guidance have evolved in fits and starts over the years. This leaves agencies, courts, and taxpayers struggling to determine what deference to apply in a given situation. In 1944, the Supreme Court adopted a moderately deferential role in reviewing agency action in *Skidmore v. Swift & Co.*,¹¹⁸ denying that an agency's interpretation would control a court's decision. In theory, deference has been expanded. Under *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*,¹¹⁹ decided in 1984, the Court required mandatory deference to an agency's reasonable interpretation of an ambiguous statute. Congressional delegations of authority are held to reflect a presumptive evaluation that the agency is better positioned, possesses more expertise, and is more politically responsive than the courts. Notwithstanding *Chevron's* broad language, courts often struggle applying its standard and agencies are unsure of how it will be applied in each particular instance as they create guidance.¹²⁰

Unfortunately, courts do not clearly or consistently apply any of the deference standards, and scholars debate the effect deference has on the outcome of cases.¹²¹ For example, under the lesser *Skidmore* test, empirical studies found that agency actions were upheld between thirty percent and sixty percent of the time.¹²² On the other hand, when using *Chevron* review,

U.S. 546 (1993), the majority rejected the Service's argument that the reenactment of the Code with this long-standing regulation gave it the force and effect of law. The dissent relied on the reenactment doctrine to rule for the force of the regulations.

¹¹⁷ For example, Professor Coverdale argues there were three types of deference for Treasury guidance. John F. Coverdale, *Chevron's Reduced Domain*, 55 ADMIN. L. REV. 39 (2003). Andre L. Smith argues for greater deference to Tax Court decisions. See Andre Smith, *Deferential Review of the United States Tax Court, after Mayo Foundation v. United States*, 58 TAX LAW. 361 (2005).

¹¹⁸ *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944).

¹¹⁹ *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).

¹²⁰ Ellen P. Aprill, *The Interpretive Voice*, 38 LOYOLA OF L.A. L. REV. 2081 (2005); Lisa S. Bressman, *How Mead Has Muddled Judicial Review of Agency Action*, 58 VAND. L. REV. 1443 (2005); Mark Seidenfeld, *Chevron's Foundation*, 86 NOTRE DAME L. REV. 273 (2011). *Chevron* states that deference is not contingent upon the existence of notice and comment. For a statement of the government's "elaborate" rulemaking process, see MAEVE P. CAREY, CONGRESSIONAL RESEARCH SERVICE, THE FEDERAL RULEMAKING PROCESS: AN OVERVIEW (June 17, 2013).

¹²¹ Kristin Hickman & Matthew Krueger, *In Search of the "Modern" Skidmore Standard*, 108 COLUM. L. REV. (2007); Richard J. Pierce, Jr., *Democratizing the Administrative State*, 48 WM. & MARY L. REV. 559, 568–69 (2006); Amy Wildermuth, *Solving the Puzzle of Mead and Christensen*, 74 FORDHAM L. REV. 1877, 1898–99 (2006); Eric Womack, *Into the Third Era of Administrative Law*, 107 DICK. L. REV. 289, 325–28 (2002).

¹²² Hickman & Krueger, *supra* note 121; Wildermuth, *supra* note 121, at 1898–99;

courts upheld agency actions between sixty percent and seventy percent of the time.¹²³ Not focusing on tax, Professor David Zaring argues that different standards of review can really be boiled down to the reasonableness of the agency's guidance.¹²⁴

Despite the existence of generally applicable rules, courts often follow tax specific precedent, as they do with other specialized areas of law. “[S]pecialized practices . . . prefer their particular deference precedents and continue to cite them, often leading the Court to follow suit. The best example of this phenomenon is tax (always a special case, concededly).”¹²⁵ Tax regulations have always received deference from courts, but not to the extent demanded by *Chevron* in the case of ambiguous statutory language.¹²⁶ The leading case establishing deference in taxation is *National Muffler Dealers Association v. United States*.¹²⁷ In *National Muffler*, the Supreme Court held that courts should defer to a Treasury regulation only if it “implement[s] the congressional mandate in some reasonable manner.”¹²⁸ At least one popular secondary source still cites to tax’s *National Muffler* standard.¹²⁹

The tax-specific standard makes it harder to secure deference for tax guidance. Although *Chevron* requires a rather passive review of reasonableness, under *National Muffler* the determination for whether tax guidance is reasonable is made through a weighing of factors asking “whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose.”¹³⁰ Under the latter test, the Treasury Department’s special expertise in the field of tax may be used as a factor. On the other hand, that much of tax litigation occurs in the specialized Tax Court where judges have their own knowledge may mitigate against special deference based on expertise.¹³¹ Certainly, a significant amount of tax guidance is only given

Womack *supra* note 121, at 325–28.

¹²³ David Zaring, *Reasonable Agencies*, 96 VA. L. REV. 135, 170–76 (2010). Courts have decided issues of deference and the validity of Treasury regulations on multiple grounds. *See e.g.*, *Intermountain Ins. Serv. of Vail LLC v. Commissioner*, 134 T.C. 11 (2010). There were three different opinions in support of denying deference to Treasury regulations in *Intermountain*.

¹²⁴ Zaring, *Reasonable Agencies*, *supra* note 123, at 137.

¹²⁵ William Eskridge & Lauren Baer, *The Continuum of Deference*, 96 GEO. L.J. 1083, 1108 (2008).

¹²⁶ Noel Cunningham & James Repetti, *Textualism and Tax Shelters*, 24 VA. TAX REV. 1, 46 (2004).

¹²⁷ *National Muffler Dealers Ass’n v. United States*, 440 U.S. 472 (1979).

¹²⁸ *Id.* at 476.

¹²⁹ 1 CASEY FED. TAX PRAC. § 1.40 n.1 (2015).

¹³⁰ *National Muffler Dealers Ass’n*, 440 U.S. at 477.

¹³¹ Mitchell M. Gans, *Deference and the End of Tax Practice*, 36 REAL PROP. PROB. & TRUST J. 731, 757, 788–89 (2002). Agency expertise was not included in *Skidmore*’s list of factors, but expertise played a role in that opinion. *Skidmore v. Swift & Co.*, 323 U.S. 134,

deference to the extent it had the power to persuade. But with the balancing, the Court in *National Muffler* concluded that the “choice among reasonable interpretations is for the Commissioner, not the courts.”¹³²

The conflict between *Chevron* and *National Muffler* was partially abated in 2001. In *United States v. Mead Corp.*,¹³³ the Supreme Court limited *Chevron* deference in the tax context, although the limits and how they would apply remained unclear. In *Mead*, the corporation challenged the classification of its diaries, notebooks, and day planners for tariff purposes. Thousands of similar tariff decisions are made each year and have no precedential value and, according to the majority, should not be given *Chevron* deference. Despite resolving the case, *Mead* failed to clarify when *Chevron* or another standard would apply. The American Bar Association (ABA) complained that “[r]eaders of the Court’s post-*Chevron* tax opinions are left wondering whether the Court applies a unique analysis when deciding cases involving deference to IRS interpretations of tax law.”¹³⁴

The Supreme Court again reached the issue of deference to tax guidance in 2011. The Court unanimously extended *Chevron* to tax regulations in *Mayo Foundation for Medical Education & Research v. United States*.¹³⁵ In *Mayo*, taxpayers challenged the Treasury Department’s regulatory interpretation that changed a long-standing agency interpretation.¹³⁶ Although claiming the rules resulted from the Department’s general authority to issue needful rules and regulations, the Department did use notice and comment procedures, a fact noted by the Court. Siding with the government, the Court followed *Chevron* rather than *National Muffler*, as the taxpayer had urged. Thereafter, the Court ruled that the Treasury Department “certainly did not act irrationally” in its regulations as it upheld their application.¹³⁷

Chevron deference has not always resulted in victory for the government; often courts fail to find the necessary statutory ambiguity to entitle guidance to deference. For example, in 2012, in *United States v. Home Concrete & Supply, LLC*,¹³⁸ the Supreme Court reviewed final regulations

137–40 (1944). *Mead* expressly included expertise as a factor. *United States v. Mead Corp.*, 533 U.S. 218, 228 (2001). Hickman and Krueger lament that courts’ references to expertise are often “mere throwaway lines tacked onto independent decisions to defer to the agency.” Hickman & Kreuger, *supra* note 121, at 1289, 1293–94.

¹³² *National Mufflers Deal Ass’n*, 440 U.S. at 488.

¹³³ *Mead Corp.*, 533 U.S. 218 (2001).

¹³⁴ Irving Salem et al., *ABA Section of Taxation Report of the Task Force on Judicial Deference*, 57 TAX LAW. 717, 763 (2004).

¹³⁵ *Mayo Foundation for Medical Education & Research v. United States*, 562 U.S. 44 (2011).

¹³⁶ *Id.*

¹³⁷ *Id.* at 60.

¹³⁸ *United States v. Home Concrete & Supply, LLC*, 132 S.Ct. 1836 (2012).

extending the statute of limitations to apply to a well-known abusive tax shelter involved in the litigation. The Code provides a six-year, as opposed to the general three-year, statute of limitations for gross understatements of income.¹³⁹ The case involved overstated basis and the use of that basis to eliminate tax on gains. Judicial precedent predating the regulations held that overstatement of basis was not the same as the understatement of income despite having the same economic effect.¹⁴⁰ Based on this precedent, the Court found there was no statutory ambiguity and therefore no need to defer to the Treasury Department. Congress has since changed the statute to overturn *Home Concrete*.¹⁴¹

Showing even greater disregard for agency guidance, courts may side step granting deference despite admitting the application of *Chevron*. In 2014, in *King v. Burwell*,¹⁴² the Supreme Court refused to defer to Treasury Department regulations interpreting provisions of the Patient Protection and Affordable Care Act. The regulations denied tax credits to persons who purchased health insurance from exchanges not directly established by a state. Despite finding the language ambiguous, the first step of *Chevron*, the Court then interpreted the provision in a manner “that is compatible with the rest of the law.”¹⁴³ Taking power from the agency to interpret the law, the Court created its own operational rules on the grounds that, if Congress wanted to assign such power over the new healthcare system to the agency, Congress “surely would have done so expressly.”¹⁴⁴

Thus, courts appear reluctant to defer to the Treasury Department notwithstanding *Chevron*. This makes the appropriate deference to tax guidance other than regulations even more uncertain. Revenue Rulings have received some deference in the past, but their future is indeterminate. Rulings have less weight than regulations but, according to the Service, “may be used as precedents” by both taxpayers and the Service.¹⁴⁵ In 2014 in *United States v. Quality Stores Inc.*,¹⁴⁶ a taxpayer raised the deferential value of Revenue Rulings but the Supreme Court decided not to rule on this issue, finding a conclusion on the issue unnecessary to resolve the case. As such, the issue remains ripe for decision. Some deference is likely, but it is implausible that a clear standard will be developed.

¹³⁹ I.R.C. § 6501(a), (e)(1)(A) (2016).

¹⁴⁰ *Colony, Inc. v. Commissioner*, 357 U.S. 28 (1958).

¹⁴¹ Surface Transportation and Veterans Healthcare Choice Improvement Act of 2015, Pub. L. No. 114-41, 129 Stat. 443.

¹⁴² 135 S.Ct. 2480 (2015).

¹⁴³ *Id.* at 2492.

¹⁴⁴ *Id.* at 2483.

¹⁴⁵ Rev. Proc. 89-14, 1989-8 I.R.B. 20; I.R.M. 32.2.2.10 (Aug. 11, 2004).

¹⁴⁶ *United States v. Quality Stores, Inc.* 134 S.Ct. 1395, 1405 (2014).

This issue of deference creates a circular problem with the process required for guidance's creation. To the extent that tax guidance is given deference, there is greater administrative concern for its creation. The more procedure adopted, the greater deference sought. Because *Chevron* deference may (although often does not) tip the scales in favor of the government over the taxpayer in tax litigation,¹⁴⁷ it is possible that such deference should only be given to guidance created with significant administrative procedure.

III. BEWARE WHAT YOU ASK FOR

The existence of various forms of tax guidance is not exceptional as most agencies promulgate guidance and many agencies have different forms to meet different needs. Critics contend that the process used to create these various forms of tax guidance is exceptional for failing to comply with the APA's stipulated processes.¹⁴⁸ Unfortunately, their analysis compares the tax system's method against the APA as opposed to other agencies' methods. This part examines how these critics not only fail to consider problems inherent in the APA as they advocate stamping the APA's procedures onto the tax system, they fail to confirm whether other agencies achieve their APA-based ideal.

A. *Objectionable objectives*

The APA contains broadly applicable and (ironically labeled) informal procedural rules that originated in response to waves of New Deal legislation and the seemingly all-powerful executive.¹⁴⁹ The procedures are to promote public deliberation, reasoned agency decision-making with fewer errors, and agency accountability to the public and Congress.¹⁵⁰ The APA attempts to accomplish these goals by encouraging public participation in the rulemaking process.¹⁵¹ However, the procedures the APA imposes, which critics want to be expanded into the creation of tax guidance, do not always accomplish these goals and may inadvertently make it harder for agencies to do so. Therefore, the focus for agencies should be whether the agency's process

¹⁴⁷ Mitchell M. Gans, *Deference and the End of Tax Practice*, 36 REAL PROP. PROB. & TRUST J. 731, 735 (2002).

¹⁴⁸ See *supra* note 25. For a history of the APA and the creation of tax guidance, see Camp, *supra* note 25.

¹⁴⁹ Martin Shapiro, *A Golden Anniversary?: The Administrative Act of 1946*, 19 REG. 40, 40-41 (1996).

¹⁵⁰ Lisa Schultz Bressman, *Procedures as Politics in Administrative Law*, 107 COLUM. L. REV. 1749 (2007).

¹⁵¹ U.S. DEP'T OF JUSTICE, ATTORNEY GENERAL'S MANUAL ON THE ADMINISTRATIVE PROCEDURE ACT, 26 (1947).

accomplishes the goals of administrative law rather than whether the agency satisfies the process itself, particularly if the goals are met and there is a colorable explanation why the APA's process should not apply.¹⁵²

Unless Congress explicitly legislates otherwise, the APA requires the public be given notice of all federal agencies' proposed rules and the agency consider the public's response after a reasonable comment period.¹⁵³ There remains ambiguity as to what this actually requires. The APA mandated notice-and-comment procedure has developed a life beyond the strict statutory requirements, but what that requires is not always clear *ex ante*. Additionally, the APA's processes apply to all agency rules that have the force of law, although what has the force of law is also debated.¹⁵⁴

Fundamentally, the APA's command that "the agency shall give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments" is an inviolate principle of agency rule-making.¹⁵⁵ This notice is to "fairly apprise interested parties of the issues involved, so that they may present responsive data or argument."¹⁵⁶ Courts treat this notice requirement seriously, invalidating rules that fail to provide sufficient notice.¹⁵⁷ This process encourages open doors for any and all to participate with any information they choose to share.

The agency must consider all comments the public chooses to submit, which is generally accepted to mean the agency must process all, and respond to all relevant, comments.¹⁵⁸ Perhaps more importantly, despite the need to respond to comments, the agency cannot change the rule substantially in response to comments without starting the notice-and-comment process over again.¹⁵⁹ This last requirement, and the various forms of intellectual lock-in that accompany it, caused Professor Stephanie Stern to conclude that notice-and-comment actually reduces the value of public participation by prematurely committing agencies to proposed rules.¹⁶⁰

Notwithstanding the reluctance to substantially change language, unless the agency responds to almost all comments, the agency risks the guidance's invalidation. Although administrative law requires the public's comments to

¹⁵² The author will argue in another paper why the good cause exemption should apply in the tax context.

¹⁵³ 5 U.S.C. § 553(b)-(c) (2012).

¹⁵⁴ Hickman, *Unpacking the Force of Law*, *supra* note 25.

¹⁵⁵ 5 U.S.C. § 553(c) (2012).

¹⁵⁶ S. REP. NO. 79-752, at 200 (1945).

¹⁵⁷ *See e.g.*, *Global Van Lines, Inc. v. Interstate Commerce Comm'n*, 714 F.2d 1290 (5th Cir. 1983) (holding that the Interstate Commerce Commission's failure to articulate the legal basis for a rule "effectively deprived the petitioners of the opportunity to present comments.").

¹⁵⁸ 5 U.S.C. § 553(c) (2012).

¹⁵⁹ *Wagner*, *supra* note 48, at 1354.

¹⁶⁰ Stephanie Stern, *Cognitive Consistency*, 63 U. PITT. L. REV. 589, 620-630 (2002).

cover “the waterfront of their concerns and ideally do so in detail” before the agency’s failure to respond to the comment would form the basis of a successful legal challenge, the perception of agency discretion and agency capture motivated courts to impose stringent requirements on agencies.¹⁶¹ The hard look doctrine emerged in the early 1970s to require an agency to consider all comments and to explain why it was not persuaded by all but frivolous comments. Hard look review imposes close judicial scrutiny on the rulemaking process to ensure an agency’s rule has adequately considered all comments and adequately supported its contested assumptions.¹⁶²

One difficulty with hard look review is that the doctrine imposes no limits on the size, number, detail, or technicality of the issues that can be raised.¹⁶³ Moreover, the level of review that is required for an agency rule to be upheld is not predictable; Professor Jerry Mashaw argues that courts function as “robbed roulette wheels” when reviewing agency guidance.¹⁶⁴ Agencies must decide whether to devote resources to the rebuttal of possibly meaningless comments without knowing courts’ expectations, so agencies may rationally devote too much or too little resources to the process from a judicial perspective.

The notice and comment procedure, coupled with hard look review, makes some experts question whether federal rulemaking has ossified.¹⁶⁵ Ossification is the idea that procedural constraints imposed on federal agencies have the undesirable consequence of making the process so burdensome that agencies routinely delay or defer issuing guidance.¹⁶⁶ Agencies understand that the process after notice has been filed may take years. Pre-notice rulemaking may even be longer; some estimate more than twice as long because of the risk of judicial invalidation if a final regulation is not in essentially the same form as the proposed rule.¹⁶⁷ This requires a

¹⁶¹ Wagner, *supra* note 48, at 1352.

¹⁶² *Id.* at 1357.

¹⁶³ RICHARD PIERCE, ADMINISTRATIVE LAW TREATISE at 447–50 (4th ed. 2002); Edward Rubin, *It’s Time to Make the Administrative Procedure Act More Administrative*, 89 CORNELL L. REV. 95, 116–18 (2003); Wagner, *supra* note 48, at 1352.

¹⁶⁴ Wagner, *supra* note 48, at 1360 (citing JERRY MASHAW, GREED, CHAOS, AND GOVERNANCE 181 (1999)).

¹⁶⁵ Edward Rubin, *It’s Time to Make the Administrative Procedure Act More Administrative*, 89 CORNELL L. REV. 95 (2003); Jason Webb Yackee & Susan Webb Yackee, *Testing the Ossification Thesis: An Empirical Examination of Federal Regulatory Volume and Speed, 1950–1990*, 80 GEO. WASH. L. REV. 1414 (2012) (testing rulemaking at the Department of the Interior); see also Richard Pierce, Jr., *Rulemaking Ossification is Real*, 80 GEO. WASH. L. REV. 1493 (2012) (responding to Yackee & Yackee).

¹⁶⁶ *Id.*

¹⁶⁷ Asimow, *supra* note 41, at 345; Pierce, *supra* note 25, at 12. In the tax context, this means that some important regulations “are inevitably slow in coming” and often create a “premium on being the first to market” with tax abusive transactions. Committee on

serious commitment of agency resources to undertake the issuance of guidance.

Examples of ossification abound. The Occupational Safety and Health Administration takes an average of ten years to develop and promulgate a health or safety standard.¹⁶⁸ A study of the Environmental Protection Agency found it required approximately five and a half years to issue each of ninety rules, including many that were not economically significant.¹⁶⁹ Even after twenty years, the EPA has failed to issue judicially satisfactory rules regarding the interstate transportation of pollution.¹⁷⁰ Unfortunately, experts cannot explain why some issues ossify and others do not.¹⁷¹

Even after the added delay of ossification, rules that complete the notice and comment process are not free from judicial invalidation. Courts reject thirty percent of rules that go through notice and comment because the agency did not adequately respond to one or more submitted comments.¹⁷² And lawyers of interested parties critical of the proposed rules have learned to submit voluminous comments.¹⁷³

Thus, the risk to published guidance of requiring notice and comment is substantial because it may delay its creation. Moreover, the process may not address existing concerns about guidance. At one high-level roundtable talk, the complaint was not the lack of notice and comment in the making of tax guidance but the Treasury Department and the Service's fear of "getting it wrong" and therefore delaying guidance,¹⁷⁴ a problem likely exacerbated if notice and comment were used more robustly. Fear of guidance being overturned is likely increased by the formal procedures of the APA, which, as stated above, results in thirty percent of rules being invalidated on procedural grounds. "The nation simply cannot afford to allow courts to delay interminably the process of issuing tax rules."¹⁷⁵

That procedural challenges to tax guidance context generally occur only

Partnerships, NY State Bar Association, *Report on the proposed Partnership Antiabuse Rule*, 64 TAX NOTES 233, 235 (July 11, 1994).

¹⁶⁸ MAEVE P. CAREY, CONG. RESEARCH SERVICE, *THE FEDERAL RULEMAKING PROCESS: AN OVERVIEW* 3 (2013).

¹⁶⁹ Wendy Wagner et al., *Rulemaking in the Shade*, 63 ADMIN L. REV. 99, 143–45 (2011).

¹⁷⁰ *EME Homer City Generation, L.P. v. EPA*, 696 F.3d 7, 24 n.18 (D.C. Cir. 2012).

¹⁷¹ See Jacob E. Gersen & Anne O'Connell, *Deadlines in Administrative Law*, 156 U. PA. L. REV. 923 (2008); Anne Joseph O'Connell, *Political Cycles of Rulemaking*, 94 VA. L. REV. 889 (2008); Sidney A. Shapiro & Richard W. Murphy, *Eight Things Americans Can't Figure Out About Controlling Administrative Power*, 61 ADMIN. L. REV. 5 (2009).

¹⁷² Pierce, *supra* note 25, at 10.

¹⁷³ *Id.* at 9–10.

¹⁷⁴ Amy S. Elliott, *Roundtable Panelists Bemoan Tax Guidance Processes*, 132 TAX NOTES 473 (August 1, 2011).

¹⁷⁵ Pierce, *supra* note 25, at 18.

after the guidance has been applied to taxpayers through the audit process is especially troubling.¹⁷⁶ Long-term uncertainty regarding the validity of guidance threatens the credibility of the tax system. If guidance has the force of law, their validity needs to be assured. The required delay before taxpayers may litigate procedural issues risks legitimating the regulations' underlying policies even though the litigation may render regulations invalid for those who want to rely on the guidance for planning purposes.¹⁷⁷

Recognizing that notice and comment procedures are not always in the public's best interest, the APA contains exemptions from notice and comment.¹⁷⁸ One exemption from the notice and comment requirement is the good cause exemption.¹⁷⁹ Under the good cause exemption, agencies are permitted to issue binding guidance immediately but must explain why adhering to the default notice and comment process is "impracticable, unnecessary, or contrary to the public interest."¹⁸⁰ Courts often interpret this exemption narrowly and skeptically.¹⁸¹

The Treasury Department often relies on the good cause exemption to issue tax regulations without the required explanation of why the regulations should be issued without antecedent notice and comment.¹⁸² Although approximately twenty-five percent of all federal agency actions invoke the good cause exemption, Professor Juan Lavilla notes the comparatively egregious misuse of the good cause exemption in the area of tax regulations is "particularly remarkable."¹⁸³ Focusing only on tax regulations, Professor Hickman concludes that "courts are unlikely to find Treasury's blanket assertions of APA section 553(b)'s inapplicability [or its more explicit assertions of the good cause exemption] sufficient explanation to sustain a

¹⁷⁶ If procedural challenges become the norm, the Anti-Injunction Act and the Declaratory Judgment Act might need to be repealed.

¹⁷⁷ Paul G. Chevigny, *Fairness and Participation*, 64 N.Y.U. L. REV. 1211, 1219–22 (1989); Jessica Mantel, *Procedural Safeguards for Agency Guidance*, 61 ADMIN. L. REV. 343, 348–351 (2009).

¹⁷⁸ Mantel, *supra* note 177, at 346–47.

¹⁷⁹ 5 U.S.C. § 553(b)(3) (2012).

¹⁸⁰ 5 U.S.C. § 553(b)(3)(B) (2012).

¹⁸¹ Hickman, *Unpacking the Force of Law*, *supra* note 25, at 493–94.

¹⁸² Treasury spokesman Andrew DeSouza took issue with Hickman's conclusion that the Treasury Department does not comply with the APA. Jeremiah Coder, *Study Finds Treasury Isn't Complying with Procedure Act*, 116 TAX NOTES 636 (Aug. 20, 2007). DeSouza stated, "Treasury and the IRS take the Administrative Procedure Act very seriously and fully comply with it and all other procedural requirements when issuing regulations and other published guidance." *Id.* at 637.

¹⁸³ Juan Lavilla, *The Good Cause Exemption to Notice and Comment Rulemaking Requirements Under the Administrative Procedure Act*, 3 ADMIN. L.J. 317, 338–341 (1989) (stating incorrectly that the Service creates the regulations, rather than the Treasury Department); see also Asimow, *Public Participation*, *supra* note 41, at 347–50.

claim of good cause.”¹⁸⁴ Arguing the “circumstances in which Treasury issues temporary regulations typically are not particularly dire,” Professor Hickman dismisses most uses of this regulatory exemption as currently employed by the Treasury Department.¹⁸⁵

However, good arguments can be made for the good cause exemption to apply widely in the tax context. Currently, tax provisions are tied to the federal government’s budget and there are restrictions on both deficit spending and the national debt.¹⁸⁶ As a part of federal fiscal planning, tax provisions are almost always estimated to have immediate effect, and that estimation is necessary in order to accomplish other goals of federal budgeting. In other words, if tax provisions were given delayed effective dates to permit time for notice and comment, this delay would alter the cost calculation of the federal budget. Instead, the existence of a workable regime is presumed; the alternative conditions budgeting on Treasury Department action.

Because of the assumption that tax provisions are immediately effective and their effect is built into the budgeting process, Congress implicitly demands quick (before fiscal year end) issuance of implementing rules.¹⁸⁷ Therefore, the good cause exemption from notice and comment should arguably apply any time that revenue estimates for tax legislation are incorporated by Congress into the budget. If Congress expects tax provisions to operate immediately, the Treasury Department, as an executive agency tasked with making it operational, must create guidance quickly. Under this theory, the strongest case for the good cause exemption can be made for new legislation because the revenue raised in new legislation is used to balance spending in the current year’s budget bills. However, even with long-established legislation, current year budgetary consequences demand implementation of a workable regime.

A second APA exemption from notice and comment that the Treasury Department frequently relies upon is for guidance that is not legislative but merely interprets the law or provides agency policy.¹⁸⁸ This argument is used

¹⁸⁴ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1780.

¹⁸⁵ *Id.* at 1783.

¹⁸⁶ DEP’T OF TREASURY, DEBT LIMIT, <https://www.treasury.gov/initiatives/Pages/debtlimit.aspx> (last visited Mar. 30, 2016); CONGRESSIONAL BUDGET OFFICE, BASELINE BUDGET AND ECONOMIC PROJECTIONS, <https://www.cbo.gov/about/products> (last visited Mar. 30, 2016).

¹⁸⁷ BORIS BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES & GIFTS ¶ 16.3 (2016).

¹⁸⁸ For more on interpretive rulemaking, see Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1760–63, 1796–97; Stephen Johnson, *In Defense of the Short Cut*, 60 U. KAN. L. REV. 495, 509 (2012); Thomas Merrill & Kathryn Watts, *Agency Rules with the Force of Law*, 116 HARV. L. REV. 467, 570–576 (2002).

extensively by the Treasury Department because it claims all of its guidance issued under its general authority are interpretive. In other areas of law, however, courts have determined that the historical basis of the distinction between legislative and interpretive guidance no longer applies. Instead, under current administrative law, general grants of rulemaking authority are regularly construed as conferring on the agency the power to promulgate rules with the force of law and are thus legislative.¹⁸⁹ Nevertheless, the Treasury Department claims more than ninety percent of tax regulations are interpretive and excepted from notice and comment on that basis.¹⁹⁰ Because of this divergence from administrative law precepts, the Treasury Department's argument is increasingly under threat in the move away from tax exceptionalism.

When not excepted from notice and comment procedures, agencies face significant costs associated with compliance. Although it is impossible to calculate all of the costs of rulemaking because data is unavailable or immeasurable,¹⁹¹ Professor David Franklin notes, "Congress, the President, and the courts have all taken steps that have made the notice-and-comment rulemaking process increasingly cumbersome and unwieldy."¹⁹² Even critics of tax exceptionalism note that the "procedures are quite burdensome."¹⁹³ Many federal agencies have responded by foregoing notice and comment and issuing interpretive tools, policy statements, and informal guidance.¹⁹⁴ "[B]usy staffs, tight budgets, and a variety of competing priorities" may affect how agencies weigh the choice of rulemaking tools.¹⁹⁵

Because of the significant costs of compliance with the APA, some have already noted that requiring notice and comment for all tax guidance would

¹⁸⁹ Asimow, *Public Participation*, *supra* note 41, at 358. Focusing on the potential for penalties through failure to follow even interpretive regulations, Professor Hickman argues to eliminate tax's exceptionalist grasp on interpretive regulations. 89 TEX. L. REV. 499, 520 (2011). One tax attorney complained of "[t]he Treasury Department's apparent inclination, to a much greater degree than would have been imaginable previously, to take on the role of lawmaker in the absence of a specific congressional mandate to do so." Mark E. Berg, *Judicial Deference to Tax Regulations*, 61 TAX LAW. 481, 483 (2008).

¹⁹⁰ See Asimow, *Public Participation*, *supra* note 41, at 370.

¹⁹¹ Jerry Mashaw, *Improving the Environment of Agency Rulemaking*, 57 LAW & CONTEMP. PROBS. 185, 188 (1994); Mark Seidenfeld, *Playing Games with the Timing of Judicial Review*, 58 OHIO ST. L.J. 85 (1997).

¹⁹² David Franklin, *Legislative Rules, Nonlegislative Rules, and the Perils of the Short Cut*, 120 YALE L.J. 276, 283 (2010).

¹⁹³ Hickman, *Unpacking the Force of Law*, *supra* note 193, at 473; Kristin Hickman, *A Problem of Remedy*, *supra* note 27, at 1203.

¹⁹⁴ Stephen M. Johnson, *Good Guidance, Good Grief!*, 72 MO. L. REV. 695, 695 (2007).

¹⁹⁵ Michael Asimow, *Interim-Final Rules*, 51 ADMIN. L. REV. 703, 711 (1999); see also Michael Asimow, *Nonlegislative Rulemaking and Regulatory Reform*, 1985 DUKE L.J. 381, 404-09 (1985).

be “ridiculously wasteful” of scarce agency resources and “could dry up this important tool for communicating with taxpayers.”¹⁹⁶ Professor Richard Pierce, historically a proponent of notice and comment for binding rules despite a concern for ossification,¹⁹⁷ worries that the Treasury Department lacks the resources to comply with the APA for its fifty-thousand to fifty million decisions each year.¹⁹⁸ The cost is likely to affect all Treasury Department guidance. Expecting the Treasury Department to recognize, in advance, which guidance is likely to face challenge from an unknown taxpayer fighting a determination of liability is asking the agency to anticipate challenges in ways other agencies have failed to do. If, in response to fears of litigation and invalidation by courts, other agencies produce reams of paperwork, it is unreasonable to assume the Treasury Department would not follow the same pattern.

What is worse is that, despite its costs, notice and comment often does not accomplish its objectives. Notice and comment may not guarantee any more meaningful public participation than exists in the current process for formulating tax guidance. “Notice-and-comment does not always provide genuine public participation in legislative rulemaking; it is useful primarily as a record-making device and is generally employed when a rule is in near-final form.”¹⁹⁹ After noting that no administrator uses notice-and-comment if they are “genuinely interested” in input, Professor Donald Elliott explained, “[n]otice-and-comment rulemaking is to public participation as Japanese Kabuki theater is to human passions — a highly stylized process for displaying in a formal way the essence of something which in real life takes place in other venues.”²⁰⁰ Informal meetings, roundtables, speeches and leaks, advisory committees, and negotiated rulemaking are better ways to obtain feedback from the public.²⁰¹

If the goal is to increase public access to and accountability for the resulting tax guidance, requiring notice and comment might have the opposite effect. Currently, much of the government’s actions with respect to federal income taxation are open to the public (or more accurately their tax advisors) through published guidance. Slowing publication or discouraging the production of published guidance may hide the agency’s decision-making. In other words, increasing the costs or difficulty of producing guidance threatens to push agency decision-making out of public view. This

¹⁹⁶ Hickman, *Unpacking the Force of Law*, *supra* note 25, at 471–472, 531.

¹⁹⁷ Richard Pierce, Jr., *Seven Ways to Deossify Agency Rulemaking*, 47 ADMIN L. REV. 59, 82–86 (1995).

¹⁹⁸ Pierce, *supra* note 25, at 1–2.

¹⁹⁹ E. Donald Elliott, *Re-Inventing Rulemaking*, 41 DUKE L.J. 1490, 1490 (1992).

²⁰⁰ *Id.* at 1492.

²⁰¹ *Id.* at 1492–93.

is particularly important in tax matters because litigation often occurs only after audit. Guidance is needed before tax filing in order for taxpayers to have a sense of the government's position and in audit to ensure consistent positions among agency personnel.

A side effect of APA procedures is that wealthy or informed participants may find it easier to capture the Service in the traditional sense of manipulating the agency to advance the interest group's objectives. Regulatory capture occurs when interest groups dominate the agency in ways that are detrimental to the public purpose for which the agency was created.²⁰² Public choice theorists argue this should be expected when a small number of interested parties have more at stake than the general public. This is often the case in taxation. As shown in one model of regulatory capture, "asymmetric information is the source of regulatory discretion, making capture possible."²⁰³ An interest group has more power when the group's interest lies in inefficient, rather than efficient, ties between Congress and the agency.²⁰⁴ The more interested parties isolate the agency, the easier it is for them to directly influence the agency's work. Consequently, creating additional process and slowing down the production of published guidance may increase the opportunity for capture by hiding the internal workings of the agency from the public and their representatives.

In addition to concerns about interested parties' ability to shape regulatory procedures, these groups may be able to divert agency resources from other agency activities. To the extent an agency is tasked both with creating published guidance and with overseeing the application of the law, the ability to tie up limited agency resources in the creation of guidance would minimize oversight of tax returns. Put simply, taxpayers can capture the Service's auditing function by forcing the agency to devote its resources to providing guidance that can withstand judicial scrutiny. And by limiting the amount of guidance that can be produced, taxpayers put themselves in a better position on audit because they are not arguing against an agency's published position but merely its litigation strategy.

Despite concerns that the APA procedures have significant costs, issues of procedure have been articulated (and won) in court and have gained traction in scholarly debate.²⁰⁵ Now that the debate is begun, it produces a

²⁰² Arthur Wilmarth, *Turning a Blind Eye*, 81 U. CIN. L. REV. 1283, 1417 (2013); see also Ernesto Dal Bo, *Regulatory Capture: A Review*, 22. OXFORD REV. OF ECON. POL'Y 203, 203 (2006); Jean-Jacques Lafont & Jean Tirole, *The Politics of Government Decision Making*, 106 Q. J. OF ECON. 1089 (1991); Michael Levine & Jennifer Forrence, *Regulatory Capture, Public Interest, and the Public Agenda*, 6 J. L. ECON. & ORG. 167 (1990).

²⁰³ Dal Bo, *supra* note 202, at 210.

²⁰⁴ Lafont & Tirole, *supra* note 202, at 1109–10.

²⁰⁵ For example, *Mead* and then *Mayo* fanned the flames of debate on regulatory procedure. See *supra* part IV.

cycle for debate, litigation, and change. But if what critics want is greater public participation in the creation of tax guidance that should be the focus around which tax guidance is judged and not compliance with a statute that might fail to accomplish that goal. Thus the question should be reframed to a review of whether the creation of tax guidance incorporates the public's concerns or, possibly, unrepresented portions of the public's concerns, as opposed to whether the guidance is APA compliant. If this change in framing were made, it would make more acceptable a broad tax-specific good cause exemption from notice and comment as a result of budgeting expectations.²⁰⁶

B. No One is Perfect

As critics of tax exceptionalism import administrative law into the study of taxation, they often fail to examine whether other agencies are any better than the Treasury Department at satisfying the APA's elaborate processes. One reading of these critiques is that, while siloing tax, they hope, or expect, that the tax system can be made a better one through the incorporation of new ideas. An alternate interpretation, however, is that every agency but for those associated with tax must have it right. This latter interpretation deprecates the tax system and risks fueling anti-tax politicians and public sentiment. Comparing the tax system to an ideal instead of other agencies may paint the tax system as a worse offender than it actually is.

Instead of situating the Treasury Department's potentially invalid approach as one of many such failures to live up to the APA, today's tax critics look only to the Treasury Department. This isolation portrays tax as particularly egregious in flaunting federal law. Even Professor Hickman's more comparative work with non-tax norms fails to compare how guidance in different agencies is created, viewed, and interpreted.²⁰⁷ This is not to suggest that Professor Hickman and others are unaware that failure to live up to the APA occurs in areas other than tax,²⁰⁸ but tax scholarship fails to analyze the degree to which other agencies get away with not complying with the APA. Thus, critics further tax exceptionalism even as they attack it.

For example, despite criticism within tax circles for its exceptionalism, tax regulations have retroactive effect in certain circumstances, including if they were filed or issued within eighteen months of a statute's enactment or if necessary "to prevent abuse."²⁰⁹ Nevertheless, no comparative research has

²⁰⁶ There may be limits to this argument. Because the public does not otherwise participate when the Service grants someone a tax break, notice and comment may be the only time that those who seek to prevent a benefit can complain.

²⁰⁷ Hickman, *Need for Mead*, *supra* note 25, at 1564–372.

²⁰⁸ Hickman, *Unpacking the Force of Law*, *supra* note 25, at 467.

²⁰⁹ Before 1996, tax regulations were presumed retroactive, but Congress reversed the presumption as part of a Taxpayers Bill of Rights unless the regulations were filed or issued

been done with respect to retroactive regulations. To date, no one has asked whether the need for deference is more likely in tax than in other areas of the law²¹⁰ or whether other agencies adopt similar practices.²¹¹

Studies from outside of tax show that the Treasury Department is not exceptional in its dismissal of notice and comment. Possibly as a result of its cost, agencies often avoid notice and comment. The Government Accountability Office found that, between 2003 and 2010, thirty-five percent of major rules and forty-four percent of nonmajor rules did not use the notice of proposed rulemaking.²¹² Of these, the Treasury Department was by no means the largest abstainer from the process.²¹³ Not looking at tax specifically, Professor Connor Raso concludes that agencies avoid notice and comment procedures as the threat of lawsuits decline.²¹⁴ If there is a low threat of lawsuit, agencies avoid the procedures ninety percent of the time.²¹⁵ This move away from notice and comment pervades agency action. No longer restrained by the nondelegation doctrine, which prevented Congress from delegating legislative power to agencies, agencies have increasingly issued rules that have the force of law and are doing so with informal procedures.²¹⁶

The limits of comparative work extend to the appropriate deference given to tax guidance. For most non-tax specialists, tax is included in broader studies of deference without concern for any exceptionalist underpinnings.²¹⁷ Tax specialists, on the other hand, often question whether *Chevron* deference

within eighteen months of the statute's enactment or if necessary "to prevent abuse." Pub. L. No. 104-168, § 1101, 110 Stat. 1462, 1469 (1996). Congress neither defined abuse nor expressly delegated the power to define this term. *Id.* at 1468-69; *see also* Bowen v. Georgetown Univ. Hosp., 488 U.S. 204, 208 (1988) (rejecting retroactive rulemaking by agencies absent express congressional authorization). *But see* Geoffrey C. Weien, Note, *Retroactive Rulemaking*, 30 HARV. J.L. & PUB. POL'Y 749 (2007).

²¹⁰ Shannon Weeks McCormack, *Tax Abuse According to Whom?*, 15 FLA. TAX REV. 1 (2013).

²¹¹ Lederman, *supra* note 25.

²¹² U.S. GOV'T ACCOUNTABILITY OFFICE, FEDERAL RULEMAKING: AGENCIES COULD TAKE ADDITIONAL STEPS TO RESPOND TO PUBLIC COMMENTS GAO 13-21 (2012). The good cause exception was cited in 77% of major and 61% of nonmajor rules. *Id.* at 37.

²¹³ *Id.* at 11-13. Forty-seven percent of all major final rules and 8% of nonmajor rules were interim rules that permitted comments after issuance.

²¹⁴ Connor Raso, *Agency Avoidance of Rulemaking Procedures*, 67 ADMIN L. REV. 65 (2013).

²¹⁵ *Id.*

²¹⁶ Hickman, *Unpacking the Force of Law*, *supra* note 25, at 476-77. This is not a new concern. *See* Kenneth Culp Davis, *A New Approach to Delegation*, 36 U. CHI. L. REV. 713, 713 (1969).

²¹⁷ *See* Davis, *supra* note 216; Hickman, *Unpacking the Force of Law*, *supra* note 25, at 470; Raso, *supra* note 214.

is appropriate for tax guidance generally and, in particular, for different types of guidance.²¹⁸ In doing so, tax specialists often fail to consider deference given to the array of guidance issued by other agencies. Throughout them all, discussion regarding tax remains siloed from other agencies' actions.

In the face of limited comparative work, an alternate approach recognizes the exceptional features of each agency. Not all scholars, including this one, accept that administrative law's goal should be a broadly applicable procedural law. Every area of law has attributes that may require exceptional powers or processes.²¹⁹ Instead of the current one-size-fits-all format, procedure should be designed to recognize "varying levels of expertise, different levels of public interest, and types of responses that typify the government regulatory process."²²⁰ In this view, determining the proper procedures for each government agency would require an understanding of the agency's substantive mandate.²²¹

Thus, exceptionalism is not exclusive to the tax system. Despite administrative law "assum[ing] the existence of core statutes and principles that apply consistently across agencies," subject-matter exceptionalism is recognized to occur throughout administrative law.²²² Professors Richard Levy and Robert Glicksman attribute agency-specific precedents to the silo effect. In the field of organizational management, the silo effect is recognized as the "propensity of departments or divisions within a large organization to become isolated, with a resulting failure to communicate and pursue common goals."²²³ There are at least three types of costs that drive silos: agency costs (through which agencies pursue goals different from those of the government as a whole), transaction costs (which make it difficult for agencies to cooperate with one another), and information costs (which make it difficult to share information among agencies). It is information costs that cause courts to rely on attorneys representing the parties and for attorneys to be

²¹⁸ John Coverdale, *Chevron's Reduced Domain: Judicial Review of Treasury Regulations and Revenue Rulings After Mead*, 55 ADMIN. L. REV. 39 (2003); Mitchell M. Gans, *Deference and the End of Tax Practice*, 36 REAL PROP. PROB. & TR. J. 731, 792–95 (2002); Hickman, *The Need for Mead*, *supra* note 25, at 1538. By arguing Congress only delegates legislative authority with explicit delegation, Coverdale seeks to influence how non-tax statutes are interpreted. John Coverdale, *Court Review of Tax Regulations and Revenue Rulings in the Chevron Era*, 64 GEO. WASH. L. REV. 35, 38 (1995); *see also* Lederman, *supra* note 25, at 648.

²¹⁹ Raso, *supra* note 214.

²²⁰ Dorit Rubinstein Reiss, *Tailored Participation: Modernizing the APA Rulemaking Procedures*, 12 N.Y.U. J. LEGIS. & PUB. POL'Y 321, 324 (2009).

²²¹ Gellhorn & Robinson, *supra* note 29, at 787.

²²² Glicksman & Levy, *supra* note 26, at 500.

²²³ *Id.* at 510.

specialists.²²⁴ Gaining information beyond a narrow specialty is costly.

Because tax law is highly specialized and large in the sense that there is a vast body of law and guidance, subject matter specialization should be more pervasive than in less specialized areas of law.²²⁵ “[T]he difficulty of keeping up with even in-field legal developments leaves practitioners with little time for a hunt — seemingly unnecessary in any event — for relevant cases from outside the field.”²²⁶ This specialization is not without cost. The marketplace of ideas is smaller because of silos, harming both tax and other areas of administrative law.²²⁷ The issue to consider before dismantling the silo around tax is the relative value of an open market of ideas which may decrease the ability of anyone to fully comprehend the tax system or a comprehensive tax system built on the recognition that silos are a necessary part of a complex administrative state.

Simply shoehorning tax (or any other area of administrative law) into a general administrative procedure without assessing either the risks or likelihood of success for that shoehorning is dangerous. As it stands, the desire to eliminate tax exceptionalism and to integrate tax more fully into the legal system is proceeding without the necessary comparative work to show if this is truly warranted. Any issue for which tax is recognized as receiving different treatment than other areas of law may be subject to criticism that demands consistency, and perhaps costly or impossible, change.

V. WHAT TAX MIGHT LOSE (MORE THAN REVENUE)

The federal tax system raises more than \$2.5 trillion in revenue from almost 240 million taxpayers on a budget of approximately \$11.6 billion.²²⁸ To do so, the Treasury Department crafts guidance to facilitate consistent application of the law, both by taxpayers and Service employees. Ignoring the addition of new burdens on the tax system risks reducing this guidance or lessening its value to its users. The choice to change the method of producing tax guidance should only be made after evaluating all possible consequences.

This is not to suggest all of tax’s procedures are successful. As the Treasury Department struggles to apply complicated and often vilified taxes, the federal government crafts approaches to regulatory matters, some of which work better than others. In the process, the Treasury Department illustrates the need to beware the threat of information capture and the need

²²⁴ *Id.* at 561.

²²⁵ Zelenak, *supra* note 1, at 1912 (mentioning the number of cases).

²²⁶ *Id.*

²²⁷ Glicksman & Levy, *supra* note 26, at 576.

²²⁸ INTERNAL REVENUE SERVICE, 2014 INTERNAL REVENUE SERVICE DATA BOOK, at 3 tbl. 1, 4 tbl. 2, 67 tbl. (2014), <https://www.irs.gov/pub/irs-soi/14databk.pdf>.

for reasonable heuristics to facilitate implementation of a complicated statutory regime. These approaches and their consequences deserve greater study with an eye to preserving the benefits the Treasury Department now enjoys.

A. Protection from information capture

The breadth and density of tax law make it natural that interested parties, already influential in the political process that creates the law, should seek to influence the creation of guidance that implements the Internal Revenue Code. From the agency's perspective, in order to issue guidance as well as to complete most other regulatory tasks, the Treasury Department depends upon information.²²⁹ Therefore, one means for interested parties to exercise influence is by controlling the information available to an agency.

As mentioned in Part IV, interested parties may seek to influence the content of agency guidance in ways that are not in the public's interest.²³⁰ As a result, the government must be concerned that interested parties unduly shape rules and force the shifting of agency resources to activities that are less taxing on interested parties. With means that are not entirely clear and deserve further research, the tax process currently addresses this concern, of course imperfectly. Treasury Department procedures plus statutory and common law rules serve a filtering function that reduce some threats of capture in federal taxation.

Interested parties could pursue many types of capture to shape implementation of the notoriously complicated Internal Revenue Code. Beyond the scope of this discussion are the financial capture of regulators based on their material self-interest and cultural capture in which regulators begin to think like the regulated parties.²³¹ This Part is concerned with three different forms of information capture. First, a taxpayer might inundate the Treasury Department with arguments and evidence with the goal of shaping guidance, possibly by drowning out other interested parties' voices. Second, a taxpayer might inundate the Department without the intent of capturing guidance but the result might shift the final guidance and reduce other activities required of the Department, such as providing customer service or auditing returns. Third, a taxpayer supplying too much information might drive out underrepresented parties as the material and discussion becomes too complex for these groups to engage with. Simply put, more information

²²⁹ Cary Coglianese et al, *Seeking Truth for Power: Informational Strategy and Regulatory Policymaking*, 89 MINN. L. REV. 277 (2004).

²³⁰ See Asofsky, *supra* note 95.

²³¹ Nicholas Bagley, *Agency Hygiene*, 89 TEX. L. REV. 1, 2 (2010); Michael E. Levine & Jennifer L. Forrence, *Regulatory Capture, Public Interest, and the Public Agenda: Toward a Synthesis*, 6 J.L. ECON. & ORG. 167, 179 (1990).

risks raising the threshold for participation.

Information capture is different than other forms of agency capture and the iron triangle in which interested parties, congressional committees, and agencies form mutually beneficial alliances. Instead, through information capture interested parties determine government agencies' activities and outcomes by deluging the agency with information and information-related costs.²³² In the battle to capture an agency in this fashion, Professor Wendy Wagner argues that the "player need not convince his opponents of the merits of his case; he need only wear them down enough to cause them to throw in their towels and give in."²³³ The audience, rather than the speaker, is the person who suffers the true cost of information.

Agencies risk being swamped with information because the APA fails to require the filtering of information.²³⁴ Nothing within administrative law ensures interested parties provide the right level of information for the intended audience or purpose. Even assuming no interested party has a bad intent, a system that seeks maximum participation encourages the creation of information, despite each additional word or participant adding little to the process.²³⁵ As a consequence of the resulting deluge, information itself becomes an externality for the agency receiving comments.²³⁶ When confronting the externality of too many words and too much data, the agency must synthesize information, something the APA does not recognize as critical or as something difficult for agencies to accomplish.

Therefore, more information is not unambiguously good in the creation of guidance; its benefit depends both on the cost of interpreting the information and the quality of the information provided.²³⁷ The APA does not recognize that attention, and not information, is the limiting factor in producing good guidance. The greater need is to "conserve the critical scare resource – the attention of managers."²³⁸ The risks of this form of capture is greatest when technical issues dominate rulemaking, a problem that pervades the tax system.²³⁹

If an interested party can win simply by inundating the agency with information, the agency begins the guidance-creation process on the

²³² Wagner, *supra* note 48, at 1325.

²³³ *Id.* at 1329.

²³⁴ *Id.* at 1323–26.

²³⁵ *Id.* at 1329.

²³⁶ ROBERT ASH, INFORMATION THEORY (1965); CLAUDE SHANNON & WARREN WEAVER, THE MATHEMATICAL THEORY OF COMMUNICATION 31–35 (1949); Henry Smith, *Language of Property*, 55 STAN. L. REV. 1105, 1115, 1137–38 (2003).

²³⁷ Elizabeth Garrett, *Harnessing Politics*, 65 U. CHI. L. REV. 501, 558 (1988).

²³⁸ HERBERT SIMON, ADMINISTRATIVE BEHAVIOR 241–43 (4th ed. 1997).

²³⁹ Wagner, *supra* note 48, at 1326.

defensive. This complicates the agency's goal of creating good guidance. The Treasury Department's starting position cannot be focusing on developing the best language in the abstract but how to defend the most acceptable language in an inevitable legal attack. That attack will come in courts, only one of which specializes in taxation and is likely to fully understand the complexities of the issues.²⁴⁰

This threat is made worse because comments are likely only to come from those directly facing an increased tax burden from the proposed regulation. Public choice theory warns that it is the wealthy or informed and cooperative taxpayers who are likely to capture the rulemaking process and squeeze out other participants.²⁴¹ In addition to collective action barriers for unorganized voices in the regulatory context, Professor Wagner worries that the increased information costs created by this information may prevent underrepresented participants from participating. As a result, the agency can face an onslaught by one side of a particular issue and a dearth of information from the other. The agency is then left to face off against a barrage of information from an unopposed, highly engaged interest group, as opposed to the ideal of a vigorous conflict among interest groups.²⁴² Even if the agency is able to withstand the assault, it nonetheless has a lopsided administrative record and the threat of a procedural lawsuit.²⁴³

Administrative law encourages these threats of capture despite the recognition in other areas of law that open-ended communication is not required to produce just results. Property law, jury trials, and appellate review require speakers to synthesize the information they present and limit the parties that can speak in order to prevent perversion of the outcome.²⁴⁴ Contract law even more severely limits the parties to those in the contract and limits their speech to that allowed by opposing parties.²⁴⁵ Through these rules, these other areas of law have created filtering mechanisms. Filtering in administrative law is no less necessary to save agencies from capture and produce the most just outcomes.

When an interested party speaks to inadvertently or strategically win control over regulatory outcomes, costs are incurred whether or not control is in fact gained. Stretching an agency's resources threatens its ability to process information and risks the reduction in published guidance. Published

²⁴⁰ Unlike in most areas of the law, taxpayers have a choice of forum to litigate their tax controversies: the Tax Court, the District Court, the Court of Federal Claims, and, at times, the Bankruptcy Court.

²⁴¹ STEVEN P. CROLEY, REGULATION AND PUBLIC INTERESTS 29–52 (2008).

²⁴² Wagner, *supra* note 48, at 1332.

²⁴³ *Id.* at 1333–34.

²⁴⁴ Smith, *supra* note 236, at 1155–56; Wagner, *supra* note 48, at 1329–30.

²⁴⁵ Smith, *supra* note 236, at 1177–90; Wagner, *supra* note 48, at 1329–30.

guidance may be especially important in taxation because few cases litigate underlying statutory issues and litigation occurs after tax filing.²⁴⁶ According to Professor Asimow, the issuance of guidance is “quite sensitive to the bureaucratic costs of adopting them.”²⁴⁷ For example, the number of published revenue rulings declined between 1974 and 1984 by seventy percent because of the recognition that the process was costly and slow and the Service needed to divert personnel to higher urgency tasks.²⁴⁸ The less information that is publicly available creates the potential for discrimination among taxpayers, advantages former Service employees who can market their information, and delays resolution of tax audits and litigation.

Another cost of information deluge is that increasing the cost to the agency of producing guidance without a specifically targeted increase in funding (not politically likely) requires resources be diverted from other, equally legitimate agency efforts. Limited funding strains the myth of agencies’ unlimited capacity. Because the Treasury Department operates in a world of limited budgets, in order to provide the same level of guidance, finite resources must be reallocated from other activities the more information (no matter how trivial) is received. In the tax context, to produce the same amount of guidance, resources must come from creating new guidance, the audit of tax returns, or customer service. The potential impact of shifting resources from more politically salient groups or issues, such as the concern that the elderly and handicapped could not leave messages for the Service in the last tax filing cycle, risks forcing the Service to reduce the creation of guidance or the number of audits in order to appease political constituents.²⁴⁹ The American public is not especially sympathetic to the Service or to taxes, which should aggravate the choice of allocating scarce resources among the agency’s numerous tasks.

These costs also explain why tax guidance needs to receive some level of judicial deference, although the cost of production does not determine the exact level of deference required for each type of guidance.²⁵⁰ The cost of creating guidance (and thereby diverting resources from other Service activity) is offset by reducing audit activity if taxpayers follow the guidance

²⁴⁶ Allowing pre-enforcement substantive review of non-legislative rules would permit litigation without concrete situations and would significantly frustrate the production of guidance and the operation of the tax system.

²⁴⁷ Asimow, *Nonlegislative Rulemaking and Regulatory Reform*, *supra* note 195 at 406.

²⁴⁸ *Id.* at 407.

²⁴⁹ See e.g., AMS. FOR TAX REFORM, *IRS Watchdog: Elderly and Disabled Taxpayers Not Allowed to Leave Messages*, (Jan. 14, 2015, 4:42 PM), <http://www.ATR.org/irs-watchdog-elderly-and-disabled-taxpayers-not-allowed-leave-message>.

²⁵⁰ Acknowledging that taxpayers want as much guidance as possible, Professor Hickman questions why guidance is binding on taxpayers. Hickman, *A Problem of Remedy*, *supra* note 27, at 1202 n. 218.

or enforcement costs if they do not. This potential offsetting of costs may make it cost effective to shift resources to the creation of guidance to the extent the guidance reduces the agency's burdens on audit. If on audit or litigation, guidance is ignored or is merely persuasive as to its argument, the guidance's relative cost increases by reducing its benefit, possibly making its production prohibitive. Making guidance optional for taxpayers denies the government the benefit of trading the guidance that taxpayers want for planning purposes with an understanding the guidance must guide that planning.

Considerations of costs to the Treasury Department and the Service are critical because of the way people respond to the tax regime. The income tax as a whole is salient to the public, as evidenced by political threats to abolish the Service.²⁵¹ For the part of taxes that are salient, the Treasury Department must find technically defensible and politically acceptable solutions as it engages in crisis management.²⁵² These issues receive significant press attention, and it may be hard to create lopsided guidance favoring particular groups. On the other hand, most tax provisions, other than those establishing tax rates, gain relatively little of the public's attention. This may impact how and who makes tax policy.

In salient and complex fields there is pressure for both accountability and expertise but, as salience drops off, so does the push for accountability.²⁵³ Thus, with respect to individual tax provisions, experts have significant influence but the public has little interest in their operation. As a result, the risk of agency capture increases to the extent interested parties can utilize experts.²⁵⁴ Because of the relative lack of public pressure coupled with the use of experts, politicians are more likely to enact procedural reforms, rather than substantive ones, as a means to show the public they are taking action but without grappling with the difficult issues the public does not really care about.²⁵⁵ Thus, procedure may merely be a means to side step difficult issues and feed into capture.

This article is not arguing that recognizing the potential threat of information capture validates all processes that stifle the flow of information.

²⁵¹ Richard Rahn, *Abolish the IRS*, WASH. TIMES (Apr. 13, 2015), <http://www.washingtontimes.com/news/2015/apr/13/richard-rahn-abolishing-the-irs>; David Drucker, *Ted Cruz Gets Specific on 'Abolishing the IRS,'* WASHINGTON EXAMINER (Apr. 27, 2015), <http://www.washingtonexaminer.com/ted-cruz-gets-specific-on-abolishing-the-irs/article/2563631>; *Abolish the IRS!*, THE TEAPARTY.NET, <http://act.theteaparty.net/10184/abolish-irs> (last visited Mar. 30, 2016).

²⁵² William T. Gormley, Jr., *Regulatory Issue Networks in a Federal System*, 18 POLITY 595, 618 (1986).

²⁵³ *Id.* at 606.

²⁵⁴ *Id.* at 616.

²⁵⁵ *Id.* at 611–13.

The Treasury Department's procedures are only superior to notice and comment to the extent they manage the risk of information capture by requiring a filtering of information without losing the benefit of public participation. Tax currently has several mechanisms that operate as filters. First, there are greater external filters in taxation than in other areas of law. As discussed in Part II, Congress enacted the Anti-Injunction Act and the Declaratory Judgment Act and courts impose a limited standing rule, which together limit the ability and the timing to challenge regulations and thereby to supply information. Second, the process for creating tax guidance adopts many less formal procedures, such as round tables and meetings, and limit ex ante notice and comment so that those who participate are vested in tax issues, although not necessarily as interested parties. This process is not sufficiently transparent and needs greater scrutiny. Nevertheless, experimentation with filters, not without concerns, might produce gains for all of administrative law.

To be supportable, these filters must appropriately respond to concerns for public participation. Filters should limit or require synthesizing of information but not thwart the larger objectives of administrative law. This puts pressure on what the filter does. Filters can affect the timing of public comments, the number and type of commentators, or the content itself.²⁵⁶ The latter type of filter is difficult under the APA because the APA encourages unlimited content. This focuses filters on the timing and number of commentators. The timing of comments is critical because the public needs guidance not to be delayed in order to comply with the law but the public also needs the guidance to be well thought out and not change in response to comments that could have been gained earlier. The number and types of commentators is important because some are more organized than others.

For the creation of good tax guidance, the absolute number and types of commentators is less important than that the Treasury Department is presented with, and properly evaluates, diverse points of view and relevant data. Representative voices among varied participants need to be heard. Professor William Gormley argued that professionals, including tax professionals, should have greater influence in complex areas, such as the tax system,²⁵⁷ but that does not mean these professionals should be limited to representing opinions of certain interested groups. Tax professionals are organized in relatively unbiased groups that often provide evidence for decision-making in taxation. The American Bar Association Section of Taxation frequently testifies before Congress and provides studies for the government.²⁵⁸ In addition, the Tax Executives Institute, the American

²⁵⁶ Wagner, *supra* note 48, at 1323–26.

²⁵⁷ Gormley, *supra* note 255, at 606.

²⁵⁸ *Section on Taxation*, AMERICAN BAR ASSOCIATION, <http://www.americanbar.org>

Institute of Certified Public Accountants, the American College of Tax Counsel, and the American Tax Policy Institute educate members and provide feedback to the government.²⁵⁹ Additionally, large taxpayers participate through their advocates.²⁶⁰

Because of the participation of organized interests, the concern should be narrowed to those times when organized and unorganized taxpayers' interests diverge, in particular when this divergence can result in isolation of the uninformed and ill connected.²⁶¹ Beneficiaries of the tax regime, or those who enjoy the benefits paid for with tax revenue, often fail to submit comments when guidance goes through the formulistic system.²⁶² Interested taxpayers, rather than revenue recipients or even uninterested taxpayers, predominately provide comments to agencies.²⁶³ The focus of procedural change should not be on the voice of those already disposed to comment but on finding the voices of those not inclined to submit comments. Unfortunately, it is unknown whether these voices are silent because of the lack of a desire to voice opposition to policy choices (in which case no procedure will produce participation) or because of an inability or unwillingness to voice opinions through the current system.

An increase in process alone is unlikely to increase the voice of the underrepresented. Indeed, increasing the need to understand voluminous and technical information before this group can thoughtfully participate in notice and comment is likely to reduce, rather than encourage, participation.²⁶⁴ Therefore, even if the government is able to prevent control of the notice and comment process by highly vocal groups, changes to existing procedure might actually decrease the participation of those intended to be encouraged.

One alternative is to empower group representation of underrepresented voices in the creation of tax guidance. Professor Leslie Book suggests this as a new role for the Taxpayer Advocate Service (TAS) and Low Income

/groups/taxation/policy.html.

²⁵⁹ TAX EXECUTIVES INSTITUTE, INC., <https://www.tei.org/Pages/default.aspx> (last visited Mar. 30, 2016); AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS, <http://www.aicpa.org/About/Pages/About.aspx> (last visited Mar. 30, 2016); AMERICAN COLLEGE OF TAX COUNSEL, <http://www.actconline.org/other-government-submissions/> (last visited Mar. 30, 2016); AMERICAN TAX POLICY INSTITUTE, <https://www.americantaxpolicyinstitute.org/conferences/> (last visited Mar. 30, 2016).

²⁶⁰ Meg Shreve & Michael M. Gibson, *Tax Analysts Picks Washington's Top 5 Tax Lobbyists*, TAX ANALYSTS (Oct. 23, 2012).

²⁶¹ Hickman, *A Problem of Remedy*, *supra* note 27, at 1205.

²⁶² Nina A. Mendelson, *Regulatory Beneficiaries and Informal Agency Policymaking*, 92 CORNELL L. REV. 397 (2007).

²⁶³ Leslie Book, *A New Paradigm for IRS Guidance*, 12 FLA. TAX REV. 517, 554 (2012).

²⁶⁴ Wagner, *supra* note 48, at 1335 n.41.

Taxpayer Clinics (LITCs).²⁶⁵ Currently, the TAS is not given the authority to engage in rulemaking and federally funded LITCs are prohibited from doing so even though low-income and disadvantaged taxpayers may not personally be in the position to monitor the development of guidance.²⁶⁶ Empowering advocates for these taxpayers would further the goals of the APA, although not as part of the APA procedure itself. If nothing else, this would help ensure a more balanced approach to notice and comment if it were adopted, although not sufficiently to outweigh the likelihood of a skewed record favoring powerful taxpayers.

Creating countervailing interest groups would also better represent the public in those instances when tax guidance favors particular groups, a problem unlikely to be resolved by notice and comment alone. Open debates alone may accomplish little unless opponents can be empowered. In a world where people do not always recognize tax favoritism as a zero sum game, guidance that favors a particular group may not have a natural opponent. Other agencies may not struggle with this problem to the same degree. For example, the Environmental Protection Agency has the Natural Resources Defense Council and the Sierra Club on one side versus corporations and farmers on the other. The creation of tax guidance would benefit by having representatives of unrepresented groups and the revenue-needing public participate, although such participation is not conditioned on, or possibly even furthered by, notice and comment procedures.

There is evidence that the Treasury Department responds to comments received through the formal notice and comment process. This issue is particularly relevant in the tax context because of the agency's use of temporary regulations coupled with proposed regulations. The question arises whether the use of temporary regulations, which are binding when issued, coupled with proposed regulations, which must complete notice and comment to be binding, have a chilling effect on the submission of comments for the proposed regulations.²⁶⁷ Temporary regulations may entrench the

²⁶⁵ Book, *supra* note 263, at 529. For a good discussion of the Taxpayer Advocate Service program, see Bryan Camp, *What Good is the National Taxpayer Advocate*, 126 TAX NOTES 1243 (2010).

²⁶⁶ Book, *supra* note 263, at 529.

²⁶⁷ As mentioned in Part II, the Treasury Department is not the only agency to use temporary regulations and even the Administrative Conference of the United States endorsed the use of interim-final rules. Administrative Conference of the United States, Notice: Adoption of Recommendations, 60 Fed. Reg. 43108, 43111 (Aug. 18, 1995). Professor Hickman concludes that temporary regulations violate the APA unless they qualify for an exception. Hickman, *Unpacking the Force of Law*, *supra* note 25, at 493. Professor Asimow argues that interim-final rules that invite comment thereafter can be valid if the "agency meets normal APA standards by giving consideration to material public comments." Asimow, *Interim-Final Rules*, *supra* note 195, at 726.

Treasury Department's views and render notice and comment for proposed regulations less influential to the final guidance. This result is not yet proven. From interviews, Professor Asinow concludes that Treasury Department and Service officials and private-sector professionals cannot discern a difference in the quality and quantity of public input as between proposed and temporary regulations, although "nobody can say for sure."²⁶⁸

The main indication that comments are responded to is through a review of changes to published guidance. Professor Hickman, a critic of tax's procedural exceptionalism, concludes from her empirical data that the Treasury Department often responds to comments by modifying proposed regulations.²⁶⁹ But many proposed regulations, almost twenty-four percent, received no comments, and a little more than three percent received only approval or urges to finalize the proposed regulations.²⁷⁰ Numbers alone only say so much. Without assessing whether the regulations that received no comments were of the type likely to be contested, it is impossible to know whether the Treasury Department responds more or less often to contentious issues or responds to substantive comments more often than less substantive ones.

The Treasury Department does make changes to temporary regulations, which receive greater deference than proposed regulations. Professor Hickman has found that the Department "[o]ften, though not always" changes its temporary regulations in response to comments.²⁷¹ The Department has even issued successive rounds of temporary regulations in response to perceived failings.²⁷² Although its procedures need further research, it is possible that the Treasury Department is supplying a workable solution to the problem of public participation for temporary regulations.

Consider, for example, a set of temporary regulations critiqued by Professor Hickman.²⁷³ In response to a 2001 Supreme Court opinion, *United Dominion Industries v. United States*,²⁷⁴ the Treasury Department began the rulemaking process in September 2003, issuing a full set of temporary regulations governing the application of a statutory exclusion from gross income when a member of a consolidated group realizes discharge of

²⁶⁸ Asinow, *Public Participation*, *supra* note 41, at 367. The Treasury Department's receptivity to comment might differ if temporary regulations have been issued. *See id.* However, receptivity might be similarly limited for proposed regulations because of the need to restart the process if significant changes are made.

²⁶⁹ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1747.

²⁷⁰ *Id.* at 1758. These numbers provide no information regarding the effectiveness of informal communication in the guidance-creation process.

²⁷¹ Hickman, *Unpacking the Force of Law*, *supra* note 25, at 531.

²⁷² *Id.* at 533.

²⁷³ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1802.

²⁷⁴ *See United Dominion Industries v. United States*, 532 U.S. 822 (2001).

indebtedness income, a complicated issue from a tax perspective.²⁷⁵ Included in the notice was a request for comment. The Treasury Department concluded that a good cause exemption from notice and comment was warranted for the temporary regulations because of “current circumstances” that made issues of the discharge of indebtedness “an issue that needs to be addressed at this time” and because consolidated groups might be taking positions inconsistent with the principles underlying *United Dominion*.²⁷⁶

Three months later, in December 2003, based on comments it had received on the temporary regulations, the Treasury Department amended those temporary regulations by clarifying a list of tax attributes that might be affected.²⁷⁷ Although the change was a substantive correction, it was consistent with the theory of the prior regulation and was only made proactively enforceable, unless the taxpayer’s tax year had not yet closed. The Treasury Department should not have made the first omission, but that is no reason to prohibit the Department from making a timely correction when it was drawn to the Department’s attention.

Additionally, in its December 2003 amendment, the Service noted that it was “aware that there are a number of other technical issues that have been identified” and which were under study.²⁷⁸ After three more months, the Treasury Department again amended the regulations to address one of the technical issues referenced before, regarding the interaction of these rules with depreciation recapture in the larger context of these new regulations, a very refined and targeted issue.²⁷⁹ This was less a change to the temporary regulations than expanding the guidance that was provided.

Finally, in March 2005, the Treasury Department revised and finalized the regulation and removed all the earlier temporary regulations.²⁸⁰ If the Treasury Department had, instead, used proposed regulations to issue this guidance, taxpayers would not have been able to rely on the regulations when filing their returns. Each change to the temporary regulations applied prospectively to transactions that had not yet occurred and taxpayers were able to rely on each set. Moreover, if proposed regulations had been used, the Treasury Department would not have been able to update its rule without incurring significant cost. To make substantive changes to proposed regulations risks restarting the notice and comment process.

Because it chose to use the temporary regulations format, in the eighteen months before the regulations were finalized, the Department could make

²⁷⁵ T.D. 9098, 68 Fed. Reg. 52487 (Sept. 4, 2003).

²⁷⁶ *Id.*

²⁷⁷ T.D. 9098, 68 Fed. Reg. 69024 (Dec. 11, 2003).

²⁷⁸ *Id.*

²⁷⁹ T.D. 9117, 69 Fed. Reg. 12069 (Mar. 15, 2004).

²⁸⁰ T.D. 9192, 70 Fed. Reg. 14395 (Mar. 22, 2005).

four changes in guidance to give taxpayers its most accurate understanding of the law and gave taxpayers the ability to rely on that guidance as they finalized their tax returns. These changes in response to the identification of problems might be a sign of the agency's responsiveness to taxpayers without employing an unreasonable amount of resources to provide that response.

The many iterations of this guidance illustrate the larger point that process in and of itself is not the objective. Despite only receiving one written comment and two participants in a public hearing,²⁸¹ the tax system sifted information and generated public responses to a proposed regulation on uncertain tax positions in what one professor called "an example of the triumph of the public participation ideal in administrative rulemaking."²⁸² Formed following various announcements predating the notice of proposed regulations, this proposed guidance "generated a significant amount of concern and public comment in the corporate tax community."²⁸³ The public participated in the press, at conferences, and "in the hallways of the IRS itself."²⁸⁴ Even if not everyone loves the final product, the final regulations resulted from "a process reflective of public participation, open deliberation, and forthright agency explanation."²⁸⁵

On the other hand, the formal process can fail to solicit sufficient public comment to accomplish the underlying purposes of the APA. For example, guidance as to innocent spouse relief, a type of tax relief used by married taxpayers who filed joint tax returns, failed to gain feedback until after the guidance was finalized. Innocent spouse relief was announced as a notice, then revenue procedure, and finally a proposed regulation.²⁸⁶ Those proposed regulations generated no formal public comment, and there is no evidence of comment along the way.²⁸⁷

When the Treasury Department once actively sought the advice of

²⁸¹ T.D. 9510, 2001-6 I.R.B. 453.

²⁸² Book, *supra* note 263, at 521.

²⁸³ *Id.* at 521.

²⁸⁴ *Id.*

²⁸⁵ *Id.* at 522.

²⁸⁶ See I.R.S. Notice 98-61, 1998-2 C.B. 758; Rev. Proc. 2000-15, 2000-5 I.R.B. 447 (*superseded* by 2003-32 I.R.B. 296); Relief From Joint and Several Liability, 66 Fed. Reg. 3888, T.D. 9003, 2002-2 C.B. 294. Although the Treasury Department's view was that the regulations were exempt from notice and comment, in the preamble the Service noted it had requested comments from the public in its subregulatory guidance and offered the public the opportunity to comment again following the issuance of proposed regulations.

²⁸⁷ See Book, *supra* note 263, at 521-22. In the case of innocent spouse relief, the Service resisted complaints that came after the guidance was finalized until losing legal challenges and then changed its interpretation to be consistent with the courts. Rev. Proc. 2013-34, 2013-43 I.R.B. 397; I.R.S. Notice 2012-8, 2012-4 I.R.B. 309; *Lantz v. Commissioner*, 132 T.C. 131 (2009), *rev'd*, 607 F.3d 479 (7th Cir. 2010); *Manella v. Commissioner*, 132 T.C. 196 (2009), *rev'd*, 631 F.3d 115 (3d Cir. 2011).

interested taxpayers in the creation of tax guidance, Congress criticized the solicitation, even though the solicitation yielded minimal results (three submissions within the first year).²⁸⁸ As part of this solicitation, the Treasury Department announced a plan for interested parties to propose draft regulations and policy memoranda. This pilot program was “to solicit greater input from the public in the initial development of certain guidance projects,”²⁸⁹ beginning with consideration of a narrow rule governing real estate mortgage investment conduits, popularly referred to as REMICs. To facilitate comprehensive submission, submitting parties were permitted to meet informally with Treasury Department personnel. Congress quickly terminated the program as granting too much power to participating interested parties.²⁹⁰

This article should not be read to suggest there are no shortcomings with the Treasury Department’s process for crafting tax guidance. But these shortcomings are unlikely to be resolved with stricter adherence to APA procedure. For example, for many years academics have worried about tax guidance creating taxpayer-friendly rules or exclusions from gross income (so the carving out of certain items from taxation).²⁹¹ Arguably the Treasury Department extending these favors to taxpayers is an undemocratic exercise of power that violates rule of law principles.²⁹² Without notice and comment or the ability to challenge the guidance before its application, those who do not benefit from a particular piece of tax guidance have no recourse except to Congress. While true, there is little reason to think APA procedures will eliminate targeted tax benefits often adopted for administrative convenience because, as mentioned above, the procedures do not create opposing parties. As shown in the earlier discussion of innocent spouse relief, parties do not always participate in their own interest, so it is unlikely that they will coalesce

²⁸⁸ *Tax Administration: Letting Practitioners Help Write Guidance Poses No More Risk of Influence, TIGTA Says*, Daily Tax Rep. (BNA), No. 48 at G-6 (Mar. 12, 2008).

²⁸⁹ I.R.S. Notice 2007-17, 2007-12 I.R.B. 748 (Feb. 28, 2007).

²⁹⁰ Baucus, *Grassley Oppose IRS Plan to Outsource Writing of Agency Rules*, 2007 TNT 52-32 (Mar. 15, 2007); *Tax Administration: Letting Practitioners Help Write Guidance Poses No More Risk of Influence, TIGTA Says*, Daily Tax Rep. (BNA), No. 48 at G-6 (Mar. 12, 2008); Memorandum from Michael R. Phillips & Nancy A. Nakamura, Deputy Inspector General for Audit, *The Published Guidance Program Needs Additional Controls to Minimize Risks*, No. 2008-10-075, (Mar. 4, 2008), <https://www.treasury.gov/tigta/auditreports/2008reports/200810075fr.html>.

²⁹¹ JAMES LANDIS, REPORT ON REGULATORY AGENCIES TO THE PRESIDENT-ELECT 49–51 (1960); William T. Gormley, Jr., *Regulatory Issue Networks in a Federal System*, 18 POLITY 595 (1986) (omitting tax regulations from his list of regulatory issue areas); Louis L. Jaffe, *The Effective Limits of the Administrative Process*, 67 HARV. L. REV. 1105, 1113–19 (1954); Roger Noll, *The Economics and Politics of Regulation*, 57 VA. L. REV. 1016, 1028–30 (1971).

²⁹² Lawrence A. Zelenak, *Custom and the Rule of Law in the Administration of the Income Tax*, 62 DUKE L.J. 829 (2012).

as a group to denounce complicated guidance that favors others but without direct harm to the groups' members.

Moreover, to the extent groups of taxpayers not directly harmed by a piece of guidance participate in the creation of that guidance, the risk of information deluge and capture intensifies. Thus, while underrepresented groups should be encouraged to participate in the formation of guidance, their message also needs to be filtered. Potential participants in tax debates could be limitless. We might agree that minority students should be able to argue that tax-exempt private schools exclude them, but we might be less supportive of businesses arguing that accelerated depreciation for other businesses decrease opportunities or of renters challenging the home mortgage interest deduction as inequitable. When the public as a group shares concerns about unfair agency administration, courts routinely dismiss their generalized grievances to prevent overuse of the court system as "no more than a vehicle for the vindication of the value interests of concerned bystanders."²⁹³ Administrative process and litigation over that process should not replace legislative or administrative choice.

In a world of unintended consequences, opening the door to speakers does not guarantee their voices are meaningful to debate. Too much information can become counterproductive. Participants in the creation of guidance or litigants over that guidance can usurp courts in a "kind of private conscription of public resources . . . that undermines a fully democratic efforts . . . to allocate . . . limited [agency] resources to the most serious problems."²⁹⁴ Perhaps unknowingly, tax has experimented with filtering information, both through its process of creating guidance and through limits on pre-enforcement litigation. Rather than ignore the concern of information capture, agencies should be encouraged in the endeavor to find constructive ways to filter information.

B. Reasonable Heuristics

Capture is a particular problem in the tax system because, while the Internal Revenue Code is a complex statute, the Code fails to answer every question or provide guidance for every scenario. Because of its combination of complexity and incompleteness, Congress must vest significant discretion in the Treasury Department to administer the tax system.²⁹⁵ How the

²⁹³ *United States v. Students Challenging Regulatory Agency Procedures*, 412 U.S. 669, 687 (1973). Moreover, requirements of particularized, concrete injuries are not as stringent as they used to be. Cass Sunstein, *Informational Regulation and Informational Standing*, 147 U. PA. L. REV. 613, 672 (1999); Gene Nichol, Jr., *Abusing Standing*, 133 U. PA. L. REV. 635, 657 (1985).

²⁹⁴ Jackel, *supra* note 41.

²⁹⁵ See the power of I.R.C. § 7805(a).

Treasury Department should exercise that discretion is part of the underlying debate over the process for creating tax guidance. By requiring increased process in the creation of guidance, the courts risk limiting guidance to an ex ante consideration of abstract facts rather than also permitting the ex post evaluation of taxpayers' own facts and circumstances with an evolving sense of the law. Instead of following current criticism, the agency should move in the opposite direction and create more first principles that can be imposed as best determined by the agency trusted to administer the law.

There are many ways to exercise the discretion vested in the Treasury Department. Complex regulations that spell out any eventuality before the law becomes effective are one method, arguably as unlikely to be complete as the statute that necessitated guidance. Alternatively, the agency could create reasonable heuristics that guide policy choice and, armed with these rules of thumb, the agency then determines the application of the statute on a case-by-case basis. Tax needs a combination of these two approaches. Even if there were no issue of ossification or any cost of notice and comment, there remains a benefit from an agency's ability to nimbly respond to changes in its governing statute and in regulated behavior. That nimbleness in agency discretion should be constrained by fundamental heuristics of tax policy.

Heuristics are strategies or tools that require little information to make complicated decisions. Streamlining the process of decision-making, these rules of thumb or first principles make choices easier and more effective. Thus, they provide a framework for making satisfactory decisions quickly.²⁹⁶ The goal of a good heuristic is to reduce the effort needed to make a decision by providing mental shortcuts. When applied on a system-wide basis, heuristics can permit the transmission of information to groups in the form of easier to apply rules that permit non-experts to participate.²⁹⁷

The value of nimbleness might seem surprising in a highly specialized area of law based on seemingly endless statutes. However, as the government and the public interact over the income tax, they are interacting over the most complicated and difficult of taxes. The tax places a premium on sensitivity to economic changes and to public attitudes. It demands high technical skills on the part of those who shape the legislative structure, who administer and interpret its provisions, who advise the public how to order its business and family affairs under the tax. It requires a literate citizenry with a respect for law and a willingness to shoulder fiscal burdens.²⁹⁸

²⁹⁶ Anuj Shah & Daniel Oppenheimer, *Heuristics Made Easy*, 134 PSYCHOL. BULL. 207 (2008).

²⁹⁷ Marta Berbes-Blazquez & Mathieu Feagan, *The Need for Heuristics in Ecosystem Approaches to Health*, 11 ECOHEALTH 290 (2014).

²⁹⁸ Stanley Surrey, *The Congress and the Tax Lobbyists*, 70 HARV. L. REV. 1145, 1145–46 (1957).

This creates an ideal situation for the government's employment of heuristics because of a widespread acceptance that there are special rules that must be learned but also a need to make the rules comprehensible by the public.

The sheer complexity of the law requires administrative flexibility. Several specialized tax statutes are enacted annually, which makes it almost impossible to build a system on exhaustive regulations expected to cover all scenarios. Additionally, taxpayers respond to the law (and changes to the law) as they attempt to minimize their tax burdens. The agency tasked with administering the tax system cannot anticipate all legal changes and taxpayers' responses. The agency needs to be able to respond to changes as they occur. Even while seeking to broaden standing for tax litigation, in one dissenting opinion, Justice John Paul Stevens wrote, "The Executive requires latitude to decide how best to enforce the law, and in general the Court may well be correct that the exercise of that discretion, *especially in the tax context*, is unchallengeable."²⁹⁹

The trend toward short-term legislation with sunset provisions only increases the need for heuristics and more rapidly issued tax guidance.³⁰⁰ The Treasury Department may find it difficult to issue even temporary guidance for an already effective tax break that will shortly expire. To require notice and comment would render the issuance impossible. This would mean guidance is likely never issued for an increasing number of tax provisions. Because the audit rate is low, most users of any given tax benefit will never be challenged, and case law may never develop to guide taxpayers. Cases of those few who are audited take time to move through the courts and so case law, limited as it is, might not develop until after the provision has expired. And these provisions, hastily written and often with the intent of changing behavior or meeting specific goals, may be the most in need of explication in order to be effective.

The creation of tax-specific heuristics is one means the agency has of guiding decision-making in a more flexible way than through the *ex ante* exercise of discretion in exhaustive regulations that wind their way through notice and comment. When required to make complicated decisions in order to comply with a complicated statute such as the Internal Revenue Code, people face psychological and behavioral barriers to making good decisions³⁰¹: "The central fact of our existence is that time is the ultimate

²⁹⁹ *Allen v. Wright*, 468 U.S. 737, 793 (1984) (Stevens, J., dissenting) (emphasis added).

³⁰⁰ See Victor Fleischer, *Tax Extenders*, 67 *TAX L. REV.* 613 (2014); Rebecca Kysar, *The Sun Also Rises*, 40 *GA. L. REV.* 335 (2006); Jason Oh, *The Pivotal Politics of Temporary Legislation*, 100 *IOWA L. REV.* 1055 (2015); Manoj Viswanathan, *Sunset Provisions in the Tax Code*, 82 *N.Y.U. L. REV.* (2007).

³⁰¹ See generally Antoinette Schoar, *The Power of Heuristics*, 42 *IDEAS 2* (2014); DANIEL

finite resource”³⁰² The use of heuristics makes it more likely that taxpayers and tax officials will make good decisions because simple information through rules of thumb is more easily absorbed and recalled.³⁰³

People use heuristics as indispensable psychological tools in all facets of their lives, and the tax system should be based on that reality. We know that taxpayers already utilize their own heuristics in understanding the tax system. Professors Edward McCaffery and Jonathan Baron observe systematic cognitive biases in a series of experiments involving tax and financial decision-making.³⁰⁴ Despite not always being accurate, subjects’ heuristics influenced their behavior. This finding has been found many times and neither education nor work experience alters the result.³⁰⁵ Even managers base financial decisions on salient information, such as average tax rates, rather than more accurate but less accessible information, such as marginal tax rates.³⁰⁶ Thus, taxpayers already have rules of thumb in assessing the tax system but the rules they use are not always the best.

If even experienced and educated professionals have need of heuristics, the need is particularly great for those with low levels of financial (and hence tax) literacy. A growing body of literature documents the low levels of financial literacy in the general population and its impact on decision making. Especially those with low levels of education, women, and ethnic minorities experience widespread lack of financial literacy, and this lack of literacy is, in turn, associated with poor financial decision-making.³⁰⁷ This likely

KAHNEMAN, THINKING, FAST AND SLOW (2011).

³⁰² KAHNEMAN, *supra* note 301, at 409.

³⁰³ Schoar, *supra* note 301.

³⁰⁴ Edward McCaffery & Jonathan Baron, *The Humpty Dumpty Blues*, 91 ORG. BEHAV. & HUM. DECISION PROCESSES 230 (2003); Edward McCaffery & Jonathan Baron, *Framing and Taxation*, 25 J. ECON. PSYCHOL. 679 (2004).

³⁰⁵ See Harold Amberger et al., *Heuristics and Tax Planning: Evidence From a Laboratory Experiment* (2015) (draft version), https://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Events/conferences/2015/Doctoral_mtg_2015/amberger-paper.pdf; see also Kay Balufus et al., *Decision Heuristics and Tax Perception*, 35 J. ECON. PSYCHOL. 1 (2013); Alejandro Drexler et al., *Keeping It Simple*, 6 AM. ECON. J. 1 (2014); John Scholz & Neil Pinney, *Duty, Fear, and Tax Compliance*, 39 AM. J. POL. SCI. 490 (1995); Michael Spicer & Rodney Hero, *Tax Evasion and Heuristics*, 26 J. PUB. ECON. 263 (1985); John Graham et al., *Tax Rates and Corporate Decision Making* (Working Paper, 2014).

³⁰⁶ Graham et al., *supra* note 305; Schoar, *supra* note 301, at 4; Claudia Townsend & Suzanne Shu, *When and How Aesthetics Influences Financial Decisions*, 20 J. OF CONSUMER PSYCHOL. 452 (2010).

³⁰⁷ Annamaria Lusardi & Olivia Mitchell, *Planning and Financial Literacy*, 98 AM. ECON. REV. 413 (2008); Annamaria Lusardi & Olivia Mitchell, *Financial Literacy and Retirement Preparedness*, 42 BUS. ECON. 35 (2007); van Rooij et al., *Financial Literacy and Stock Market Participation*, 101 J. FIN. ECON. 449 (2011); Victor Stango & Jonathan Zinman, *Exponential Growth Bias and Household Finance*, 64 J. FIN. 2807 (2009).

impacts their tax compliance. Easing compliance by recognizing the importance of heuristics should improve administration of the tax system.

Heuristics are only one of many tools being used by taxpayers and tax officials in addition to written guidance. With respect to taxes, as with other complicated choices, people are influenced by past experience, cognitive biases, age, and belief in their own personal relevance.³⁰⁸ Creating complicated written guidance following dense notice and comment procedures is unlikely to supplant other, easier means of decision-making by all but those most adept at tax law. Recognizing these tools permits policymakers to create better guidance that fosters compliance with the underlying statute.

This knowledge of how people understand tax should shape the acceptability of tax guidance. Tax guidance does not have to be all-inclusive. Except for the most aggressive tax planners and their representatives, those who currently seek more guidance are not necessarily seeking the ex ante application of the statute to all facts.³⁰⁹ Heuristics, as another form of guidance, enables agencies and their employees to be more accurate, consistent, and predictable. Moreover, heuristics permit taxpayers to determine for themselves the applicability of the law, which, in turn, conserves agency resources both by limiting taxpayer inquiries about the law in particular circumstances and deterring conduct that triggers audits and subsequent litigation.³¹⁰ Because guidance can come in many forms, those that are the most accessible to taxpayers are likely best able to achieve its objectives.

As alluded to in the prior paragraph, those engaged in aggressive tax planning and the creation of tax shelters are likely unhappy with the use of heuristics. These rules of thumb permit the agency to use discretion to ensure compliance with the spirit of the law rather than being limited to an evaluation of a taxpayer's deft maneuvering around specific lines in regulations. Because planners can most effectively structure deals around clearly demarcated lists and requirements, it is likely they would push for their creation in the notice and comment process. If the agency sought to

³⁰⁸ See Wandu de Bruin et al., *Individual Differences in Adult Decision-Making Competence*, 92 J. PERSONALITY & SOC. PSYCHOL. 938 (2007); Nicholas Epley & Thomas Gilovich, *The Anchoring-and-Adjustment Heuristic*, 17 PSYCHOL. SCI. 311 (2006); Daniel Golstein & Gerd Gigerenzer, *Models of Ecological Rationality*, 109 PSYCHOL. REV. 75 (2002); Keith Stanovich & Richard West, *On the Relative Independence of Thinking Biases and Cognitive Ability*, 94 J. PERSONALITY & SOC. PSYCHOL. 672 (2008); Richard West et al., *Heuristics and Biases as Measures of Critical Thinking*, 100 J. EDUC. PSYCHOL. 930 (2008).

³⁰⁹ See Transcript Available of Tax Analysts' Roundtable on 'Taxes and the Guidance Problem,' 2011 TNT 142-100 (Jul. 22, 2011).

³¹⁰ Jessica Mantel, *Procedural Safeguards for Agency Guidance*, 61 ADMIN. L. REV. 343, 393 (2009).

maintain heuristics following notice and comment, it would need to build a strong defense for the inevitable litigation and an explanation why these types of rules are necessary and the proposed lists inadequate.

The federal income tax currently operates with numerous heuristics that would likely be challenged in a system with regimented procedure because they were not developed through that process. Developed through common law and now incorporated into practice by the Service, tax lawyers know that gross income is interpreted broadly while deductions are construed narrowly as a matter of legislative grace,³¹¹ income is to be taxed to earners,³¹² substance prevails over form,³¹³ and (although possibly threatened by codification) transactions need economic substance.³¹⁴ These ideas, among others, guide the practice of law and the choices taxpayers make when they report the tax consequences of their activities. Without such guideposts, every new tax provision must be fully and singularly explicated, and any ambiguity litigated from scratch.

Those within the field of taxation are likely to know these, and other, tax heuristics. Because of technicalities pervading the field of tax, subject matter specialization is pervasive.³¹⁵ The difficulty of remaining up-to-date on tax developments means that most tax practitioners have little time for broader research.³¹⁶ The need for deep knowledge in this one area may preclude all but cursory knowledge of others, but the need for specialization is one reason heuristics are particularly useful and could be standardized to aid more taxpayers, advisors, and Service employees.

A legitimate concern is that people come to tax with diverse experiences and expertise. These differences might cause people to initially apply different heuristics.³¹⁷ It is for this reason that the system should work on disseminating workable heuristics rather than increasing procedural requirements for increasingly detailed rules. In other words, as the Treasury Department develops its first principles, it should work to make them known more widely.

As shown by the government's efforts during World War II, it is possible

³¹¹ *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955) (holding that “undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion” are taxable as gross income); *United States v. Wells Fargo Bank*, 485 U.S. 351, 354 (1988) (noting that “exemptions from taxation are not to be imposed; they must be unambiguously proved.”); *Knight v. Commissioner*, 128 S.Ct. 782, 790 (2008) (stating that “an income tax deduction is a matter of legislative grace”).

³¹² *Commissioner v. Banks*, 543 U.S. 426, 433–34 (2005).

³¹³ *Gregory v. Helvering*, 293 U.S. 465 (1935).

³¹⁴ *Id.*

³¹⁵ *See Zelenak, supra* note 1, at 1912 (mentioning the number of cases).

³¹⁶ *Id.*

³¹⁷ *See Berbes-Blazquez & Mathieu Feagan, supra* note 297.

to popularize tax heuristics. Professor Carolyn Jones illustrates the process the Treasury Department adopted to transition the income tax into a mass-tax with a “new culture of taxpaying.”³¹⁸ Adoption of popular culture tools, including songs and cartoons, were a tool to spread the message of one’s tax responsibilities. Donald Duck even provided instructions on how to comply with the income tax, such as stating “Don’t guess, it will solve a lot of trouble if you get it right.”³¹⁹ Currently, the Service focuses on creating heuristics regarding audit probabilities, tax penalties, and enforcement efficacy.³²⁰ The government has, and can, create general rules for taxpayers to apply, but those heuristics rarely have completed notice and comment.

The practical reliance on heuristics may help explain why so few practitioners raise claims of failed procedure in the creation of tax guidance.³²¹ If most taxpayers rely on heuristics only supplemented with technical guidance, taxpayers may accept guidance when it is consistent with their heuristics without questioning the procedure used for the guidance’s creation. It is beyond the scope of this article to determine whether the number of such challenges has increased and, if so, whether this is a statement regarding the efficacy of existing tax heuristics. Anecdotally, as discussed in part III, attacks on guidance on procedural grounds appears to have increased but possibly more from the perception these attacks are a means for individualized tax reduction rather than a claim that the rules were unreasonable or unexpected.

Valuing heuristics as a form of guidance does not mean that more detailed guidance is unimportant. Such guidance may be necessary when heuristics are insufficient. The long-standing debate over the merits of rules versus standards is not to be resolved in this article.³²² When particular guidance is necessary, the procedures behind its creation can have a legitimizing effect, and in some cases parties are more satisfied with results they perceive to be procedurally fair, even when the results are

³¹⁸ Carolyn Jones, *Mass-Based Income Taxation*, in *FUNDING THE MODERN AMERICAN STATE, 1941-1995*, at 107–08 (W. Elliot Brownlee ed., 1996); Carolyn Jones, *Class Tax to Mass Tax*, 37 *BUFF. L. REV.* 685 (1989).

³¹⁹ DISNEY, A NEW SPIRIT, <https://archive.org/details/TheNewSpirit> (1942); see also DISNEY, PAY YOUR INCOME TAX, https://archive.org/details/TheSpiritOf43_56 (1943).

³²⁰ Joshua Blank & Daniel Levin, *When Is Tax Enforcement Publicized?*, 30 *VA. TAX REV.* 1, 5 (2010).

³²¹ Hickman, *Coloring Outside the Lines*, *supra* note 27, at 1731; see also *Hosp. Corp. of Am. & Subsidiaries v. Commissioner*, 348 F.3d 136, 146 n.3 (6th Cir. 2003) (noting that taxpayers are not making procedural challenges).

³²² See generally RICHARD EPSTEIN, *SIMPLE RULES FOR A COMPLEX WORLD* (1995); Colin Diver, *The Optimal Precision of Administrative Rules*, 93 *YALE L. J.* 65 (1983); Ezra Friedman & Abraham Wickelgren, *A New Angle on Rules Versus Standards*, 16 *AM. L. & ECON. REV.* 499 (2014); Louis Kaplow, *Rules Versus Standards*, 42 *DUKE L. J.* 557 (1992).

unfavorable.³²³ Thus, procedure may make guidance more acceptable to taxpayers. On the other hand, procedure and ex ante rules can determine outcomes regardless of the merits of the case.³²⁴

It is enough to say that the hard and fast rules likely to be pushed through notice and comment are not always most just based on the particular facts of a particular case. At times, discretion can best be exercised after the facts are known. When all discretion is exercised ex ante, part of agencies' expertise may be underutilized and the agency loses its nimble ability to respond to changes in the law and taxpayer behavior. With reasonable heuristics, it is possible to defer to agency discretion with a reasonable judicial backstop.

The fear of heuristics and of agency discretion necessitates hard and fast rules that are nearly as easily made in Congress as in the specialized agency. Consider, for example, the taxation of fringe benefits in the 1970s. The Treasury Department exercised its discretion regarding their taxation through proposed regulations, circulated in draft rather than proposed form because the agency desired "the broadest possible public comment."³²⁵ Faced with numerous critics, the agency withdrew this proposed language.³²⁶ Furthermore, Congress enacted a statute imposing a moratorium on new regulations.³²⁷ A congressional task force then studied the issue, and Congress passed legislation governing fringe benefits in 1984.³²⁸ The need for detailed ex ante rules was as easily made by Congress as in the Treasury Department, but this limited the Service's ability to resolve particular cases based on its experience with claims for fringe benefits. This reallocation of responsibility back to Congress might be the correct answer in this instance,

³²³ See Paul G. Chevigny, *Fairness and Participation*, 64 N.Y.U. L. REV. 1211, 1217-23 (1989).

³²⁴ See *Herra v. Collings*, 506 U.S. 390, 411 (1993) (rejecting untimely claim that newly discovered evidence that exonerated defendant was sufficient to obtain relief); *Coleman v. Thompson*, 501 U.S. 722, 757 (1991) (rejecting claim of attorney error because no right to counsel and failure to make proper federal habeas appeal); *Schiavone v. Fortune*, 477 U.S. 21, 29 (1986) (dismissing libel claim because statute of limitations expired because complaint listed incorrect defendant); *Nat'l Hockey League v. Metro. Hockey Club, Inc.*, 427 U.S. 639, 643 (1976) (issuing sanction of dismissal for noncompliance with discovery).

³²⁵ Fringe Benefits: Notice of Publication of Discussion Draft of Regulations, 40 Fed. Reg. 41,118-19 (proposed Sept. 25, 1975); Fringe Benefits: Withdrawal of Discussion Draft of Proposed Regulations, 41 Fed. Reg. 56,334 (Dec. 28, 1976).

³²⁶ Fringe Benefits: Withdrawal of Discussion Draft of Proposed Regulations, 41 Fed. Reg. 56,334 (Dec. 28, 1976).

³²⁷ Act of Oct. 7, 1978, Pub. L. No. 95-427, 92 Stat. 996; see also Act of Dec. 29, 1979, Pub. L. No.

96-167, 93 Stat. 1275 (extending moratorium through May 31, 1981).

³²⁸ See generally Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 531, 98 Stat. 494, 877-87 (codified at I.R.C. § 132 (1984)); H.R. Rep. 95-1232 (1978), reprinted in 1978 U.S.C.C.A.N. 2508.

but it does dismiss the value of the agency's expertise.

If courts fear agency discretion to the degree that they necessitate ex ante exercise of it in the detailed and formulistic way likely to survive the notice and comment process, Congress should remove discretion entirely by changing the statute and congressional expectations of the agency. Consider the current regulations governing innocent spouse relief discussed earlier. The new regulations define how discretion is to be exercised for each potential claimant and how relief operates in all circumstances with an expectation of the need to withstand hard look review. The result is that there is no benefit of human evaluation of the applicant by agency personnel. Formulaic determinations of need and abuse replace an evaluation of honesty and circumstance. Moreover, in the creation of these regulations, the agency no longer administers the law but has become a mini-legislature for times when Congress failed to legislate fully.

There is a risk the nation is moving away from heuristics in tax with the codification movement and the move to increased APA procedures. For example, Congress codified the judicially created economic substance doctrine in March 2010.³²⁹ The heuristic demanded transactions have economic substance beyond tax savings in order for their tax effects to be respected. The issue of the codification of this rule was debated long before its enactment, and it remains unclear how far this provision moves the law from its heuristic start. Unlike the heuristic, the statute contains a two-prong mechanical test to determine whether economic substance exists. Therefore, it is likely codification will limit the flexibility of the doctrine as applied by the courts.³³⁰

The Treasury Department has proven unwilling to venture through notice and comment with rules implementing the statutory economic substance doctrine, although the Service has created less formal guidance. Because the doctrine "poses open-ended and unanswerable questions,"³³¹ it is doubtful the agency can create acceptable ex ante regulations as required by the APA to implement this rule. Concerns that it was "patently unfair" to apply the new codified provision without significant guidance as to how it should be applied necessitated some guidance but the format the Service has chosen has little authority but does provide much needed information to

³²⁹ Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, § 1409, 124 Stat. 1029, 1067 (2010) (codified at I.R.C. § 7701(o)).

³³⁰ Nomination of Pamela Olson, Hearing Before the Senate Finance Committee (2002) (statement of Pamela Olson, Assistant Secretary of Treasury, Tax Policy); Dennis Ventry, *Save the Economic Substance Doctrine from Congress*, TAX NOTES 1405, 1411 (Mar. 31, 2008).

³³¹ Joseph Bankman, *The Economic Substance Doctrine*, 74 S. CAL. L. REV. 5, 29 (2000); see also Sheryl Stratton, *Shelter Disclosure, Doctrine Codification Debated*, 2003 TNT 61-3 (Apr. 7, 2003).

taxpayers.³³²

In the face of a daunting notice and comment process, the Service has chosen to offer what is, in effect, its own nullification of the codified economic substance doctrine. After a brief interpretation of the new provision, the Service stated it would issue no guidance but requested comments as to disclosure requirements to avoid the provision's heightened penalties.³³³ Within six months, a directive was publicly issued that provided high level officials must approve any proposal to impose the codified economic substance doctrine and related penalties to ensure consistent administration.³³⁴ A second directive ten months later made public a series of inquiries that a Service employee must develop and analyze before seeking approval to raise the codified economic substance doctrine.³³⁵ A little more than a year later, the Service provided more basic, and still informal, guidance as to how this new statutory provision would be applied.³³⁶ Outside of formal procedure, the Service has made sure the public understands its position even if, in doing so, it fails to adopt the regime changes likely envisioned by those who wanted a more regimented law. Only time will tell whether this result terminates the heuristic underlying the statutory provision.

Perhaps more troubling than the threat to any particular tax heuristic is that the current criticism of tax exceptionalism may threaten tax's most basic heuristic, the understanding that tax is somehow different. Although a detailed discussion of this phenomenon must wait for another article, this rule of thumb allows practitioners and the government to limit the amount of information that they are accountable for knowing. It is possible that the increase in information that would result from breaking down the silo around taxation would further exacerbate the isolation of tax. This new tax order would demand (1) the continued understanding of tax specific rules (although less guidance is likely to be issued), plus (2) a newfound understanding of how those rules interact with other areas of the law. Few, perhaps many fewer, attorneys and advisors could hope to attain a working level of information in this un-siloed world.

Furthermore, the practical threat of eliminating this heuristic that tax is different might be particularly damaging for the government. In an environment where people do not want to pay taxes, this heuristic of

³³² Jackel Monte, *Subchapter K and the Codified Economic Substance Doctrine*, 2010 TNT 138-4 (July 20, 2010); see also Jeremiah Coder, *Treasury Official Reiterates Limited Scope of Economic Substance Guidance*, 2010 TNT 118-2 (June 28, 2010). But see Bret Wells, *Economic Substance Doctrine*, 10 FLA. TAX REV. 411 (2010).

³³³ I.R.S. Notice 2010-62, 2010-40 C.B. 411.

³³⁴ I.R.S. Treas. Dir. LMSB-04-0910-024 (Sept. 14, 2010).

³³⁵ I.R.S. Treas. Dir. LB&I-04-0711-015 (July 15, 2011).

³³⁶ I.R.S. Notice CC-2012-008 (Apr. 3, 2012); see also I.R.S. Notice 2014-58, 2014-44 I.R.B. 746.

different-ness can work for the government by limiting the procedures it must follow but also against the government by limiting the Service's budget and the regard in which its employees are held. To remove one part of the heuristic, a certain deference society gives to the operation of the tax system, without removing the other, resulting in a limited budget and widespread antagonism, would likely be catastrophic to raising revenue.

The likelihood that this threat would be outweighed by finding answers to taxing problems in other areas of law is remote. Encouraging the cross-pollination of ideas is beneficial only if doing so improves the chances the Treasury Department properly implements the tax law. Unfortunately, because it is impossible to know the availability of answers *ex ante*, it is impossible to know whether there would be sufficient benefit to outweigh the costs.

Thus, although taxpayers are proven to use heuristics when making their decisions regarding taxes, tax critics are reluctant to empower the agency to craft heuristics or to admit that these are often the basis of decisions. Instead of limiting agency power through extensive *ex ante* exercises of discretion in processes that can withstand the scrutiny of hard look review, when Congress desires to delegate discretion it should be delegated in a way that maximizes congressional objectives. It is the objectives that should drive the design of tax guidance, rather than a fear of agency power.

V. CONCLUSION

The exceptionalness of the tax system is an issue of degree and not of kind. The tax system is not better or worse or more important than other fields of law. It may or may not be more complicated. As with many other parts of our federal system, the tax system has a unique history and that difference has long-term consequences that cannot simply be undone. Ignoring that past or the different processes that have developed “runs the risk . . . of downplaying the virtues of pragmatism, flexibility, and realism.”³³⁷ We must be careful before we eliminate strengths our tax system is built upon.

This is not to suggest the Treasury Department's operation of the federal income tax is perfect. Nonetheless, it does do some things right, such as walk the line with information capture and struggling to define workable heuristics for taxpayers and its employees. These processes should be encouraged. Most certainly these attempts should not be ignored or jettisoned in the guise of eliminating tax exceptionalism.

Moreover, the tax system's exceptional processes should be made available to other agencies for review. As a kind of laboratory of

³³⁷ Richard Murphy, *Pragmatic Administrative Law and Tax Exceptionalism*, 64 DUKE L. J. ONLINE 21, 21 (2014).

administrative law experimentation, in much the same way that states operate within a federalist system, tax law exceptionalism can foster innovation or contain the spread of bad procedure. Current proposals to dismantle the exceptionalism surrounding the creation of tax guidance risks increasing information for its own sake without improving tax guidance and possibly leading to the capture of the tax administration. Before the courts impose requirements on the Treasury Department for the sake of doing so, there needs to be more comparative work with other agencies and a recognition that the APA's procedure, even in the abstract, is not without faults.

