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Reflections on Home Concrete

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REFLECTIONS ON *HOME CONCRETE*: WRITING TAX REGULATIONS AND INTERPRETING TAX STATUTES

STEVE R. JOHNSON*

| | |
|------------------------------------------------|----|
| I. INTRODUCTION..... | 77 |
| II. HOME CONCRETE..... | 78 |
| III. LITIGATION BALANCE | 79 |
| A. <i>Generally</i> | 79 |
| B. <i>Reliance</i> | 82 |
| C. <i>Expertise</i> | 83 |
| IV. RETROACTIVITY..... | 83 |
| V. DEFERENCE DOCTRINE..... | 84 |
| A. <i>Chevron</i> | 84 |
| B. <i>Brand X</i> | 85 |
| VI. STATUTORY INTERPRETATION..... | 90 |
| A. <i>Elephants and Mouseholes</i> | 90 |
| B. <i>Stare Decisis</i> | 91 |
| C. <i>Continuing Dialogue</i> | 91 |
| D. <i>“Best Answer” Versus Deference</i> | 92 |
| VII. CONCLUSION..... | 93 |

I. INTRODUCTION

Positive statutory law—principally the Internal Revenue Code—is the most important source of tax rules. Despite its volume, however, the Code contains many gaps. Tax regulations promulgated by the Department of the Treasury are the principal vehicles for filling the most important gaps.¹

When consistent with the Code and issued pursuant to proper procedures, Treasury Regulations have the force of law.² The validity of Treasury Regulations has been a major battleground in contemporary tax litigation. In the last five years alone, the issue has arisen in high profile cases such as *Swallows*,³ *Mannella*,⁴

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1. The process by which Treasury regulations are drafted, reviewed, and promulgated is described in IRS Procedural Regulation § 601.601(a)-(c) (as amended in 1987). See also Mitchell Rogovin & Donald L. Korb, *The Four R's Revisited: Regulations, Rulings, Reliance and Retroactivity in the 21st Century: A View from Within*, TAXES, Aug. 2009, at 21; Paul F. Schmid, *The Tax Regulations Making Process—Then and Now*, 24 Tax Law. 541 (1971).

2. E.g., *Helvering v. R. J. Reynolds Tobacco Co.*, 306 U.S. 110, 115 (1939); *Boulez v. Comm'r*, 810 F.2d 209, 212 (D.C. Cir. 1987), cert. denied, 484 U.S. 896 (1987); *Union Elec. Co. v. United States*, 305 F.2d 850, 854 (Ct. Cl. 1962).

3. *Swallows Holding Ltd. v. Comm'r*, 515 F.3d 162 (3d Cir. 2008), rev'g 126 T.C. 6 (2006). See also Steve R. Johnson, *Swallows as It Might Have Been: Regulations Revising Case Law*, TAX NOTES, Aug. 28, 2006, at 773 [hereinafter *Swallows II*]; Steve R. Johnson,

Lantz,⁵ *Mayo*,⁶ *Dominion Resources*,⁷ and *Loving*.⁸

*United States v. Home Concrete & Supply, LLC*⁹ is the Supreme Court's most recent foray into the thicket of the validity of Treasury tax regulations. The decision disappointed some because the Court avoided many significant issues raised by commentators or briefed by the parties.¹⁰

Nonetheless, *Home Concrete* gives us much to digest.¹¹ Some reactions to the decision appear below. They are grouped under four headings: (1) litigation balance between the government and taxpayers, (2) retroactivity, (3) deference doctrine, and (4) statutory interpretation. These considerations are developed below after a brief description of the *Home Concrete* decision.

II. HOME CONCRETE

Home Concrete arose out of a long-running controversy. When the IRS believes that a taxpayer's return understates true tax liability, the IRS ordinarily must assess the additional liabilities within three years after the return was filed (or, if later, three years after the return was due to be filed).¹² A number of exceptions to this general rule exist, however. One of the exceptions allows the IRS a six-year assessment period when the return "omits from gross income an amount properly includible therein [which] is in excess of 25 percent of the amount of gross income stated in the return."¹³

The six-year rule obviously applies when the tax understatement results from complete omission of taxable receipts of sufficient amount. Does the six-year rule also apply when the

Swallows as It Is: *The Distortion of National Muffler*, TAX NOTES, July 24, 2006, at 351 (2006) [hereinafter *Swallows I*].

4. *Mannella v. Comm'r*, 631 F.3d 115 (3d Cir. 2011), *rev'g* 132 T.C. 131 (2009).

5. *Lantz v. Comm'r*, 607 F.3d 479 (7th Cir. 2010), *rev'g* 132 T.C. 131 (2009).

6. *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704 (2011). *See, e.g.*, Steve R. Johnson, *Mayo and the Future of Tax Regulations*, TAX NOTES, Mar. 28, 2011, at 1547.

7. *Dominion Res., Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012).

8. *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014). For discussion of *Loving*, see Steve R. Johnson, *Loving and Legitimacy: IRS Regulation of Tax Return Preparation*, 60 VILLANOVA L. REV. (forthcoming 2014).

9. 132 S. Ct. 1836 (2012).

10. *E.g.*, Patrick J. Smith, *What We Didn't Learn from Home Concrete*, TAX NOTES, June 25, 2012, at 1625. *See generally* *Comm'r v. Engle*, 464 U.S. 206, 227 (1984) ("In cases . . . where the effective and expeditious enforcement of our [n]ation's tax laws is at issue, what we do not decide is as important as what we do decide.")

11. For discussion of the decision generally, see Steve R. Johnson, *After the Cheering, Problems*, 31 ABA SEC. OF TAX'N NEWS Q. 1 (2012); William J. Wilkins, *Implications of Home Concrete*, 31 ABA SEC. OF TAX'N NEWS Q. 25 (2012); Shamik Trivedi & Jeremiah Coder, *Wilkins, Butler Give Their Takes on Home Concrete*, TAX NOTES, May 21, 2012, at 974.

12. I.R.C. § 6501(a) (2010).

13. I.R.C. § 6501(e)(1)(A) (2010).

understatement results from overstatement of basis on a sale reported on the return?¹⁴

The lower courts disagreed on this question,¹⁵ leading the Supreme Court to consider it in the 1958 *Colony* decision.¹⁶ The *Colony* Court acknowledged that the language of the statute¹⁷ was not “unambiguous.”¹⁸ Nonetheless, in an exercise of statutory interpretation, the Court held that the six-year limitations period did not extend to basis overstatements.¹⁹

Colony did not end the controversy, however. The IRS identified changes to the statute occurring after the years at issue in *Colony*, which, the IRS believed, modified the result. Lower courts disagreed as to the viability of the IRS’s contention.²⁰

Reflecting the difficulty of the issue, the *Home Concrete* Court itself was split. Justice Breyer delivered the opinion of the Court but could manage only a plurality as to his reinterpretation of the Court’s *Brand X* decision.²¹ Justice Scalia concurred in part and concurred in the judgment.²² Justice Kennedy, joined by three other justices, dissented.²³

III. LITIGATION BALANCE

A. Generally

Many taxpayers are pleased with the substantive outcome of the case. As a result of *Home Concrete*, it is clear (for the time being) that the six-year assessment limitations period under section 6501(e) of the Internal Revenue Code applies only to omitted taxable receipts. The amended regulations extending it to overstatements of basis have been invalidated, and *Colony* has been reaffirmed. Although the transaction at issue in *Home Concrete* involved a tax shelter, this holding applies as well to non-

14. Gain on sale is the difference between the amount the seller receives and the basis the seller had in the property. I.R.C. § 1001(a) (2012). Thus, claiming an inflated basis results in understatement of the gain and thus of tax liability.

15. Compare *Uptegrove Lumber Co. v. Comm’r*, 204 F.2d 570, 571-72 (3d Cir. 1953), with *Reis v. Comm’r*, 142 F.2d 900, 902-03 (6th Cir. 1944).

16. *Colony, Inc. v. Comm’r*, 357 U.S. 28, 31 (1958).

17. *Colony* interpreted a provision, 26 U.S.C. § 275(c) (1940), of the Internal Revenue Code of 1939, which was ancestral to current section 6501(e).

18. *Colony*, 357 U.S. at 33.

19. *Id.* at 32-37.

20. This was the case in *Home Concrete* itself. The trial court held for the IRS, to be reversed by the circuit court. *Home Concrete & Supply, LLC v. United States*, 599 F. Supp. 2d 678 (E.D.N.C. 2008), *rev’d*, 634 F. 3d 249 (4th Cir. 2011), *aff’d*, 132 S. Ct. 1836 (2012).

21. *Home Concrete*, 132 S. Ct. at 1843-44. See *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967 (2005); *infra* part V.B.

22. *Home Concrete*, 132 S. Ct. at 1846.

23. *Id.* at 1849.

shelter contexts.

However, this benefit may evanesce. If Treasury and the IRS decide that the stakes are sufficiently high, they could ask Congress to amend section 6501(e) to adopt the position rejected in *Home Concrete*.

Accordingly, more significant than *Home Concrete's* particular outcome may be the signal that it sends as to the future of tax litigation. *Home Concrete* adds to a positive trend that has been building in the aftermath of the Supreme Court's 2011 *Mayo* decision.²⁴ There are two principal types of tax regulations: specific authority²⁵ and general authority²⁶ regulations. In *Mayo*, the Court unanimously held that, no less than specific authority regulations, general authority tax regulations are tested under the *Chevron* standard when their validity is challenged.²⁷

Mayo inspired widespread concern in the taxpayer and taxpayer representatives community that the balance in litigation between taxpayers and the government had been dramatically tilted in favor of the government. This concern arose for two related reasons. First, *Mayo* dispensed with *National Muffler* as the guiding case when general authority regulations are challenged, and many considered *Chevron* more deferential to the government than *National Muffler*.²⁸ Second, *Mayo* disregarded a number of considerations listed in *National Muffler*, considerations on which taxpayers had staked their arguments in many prior cases. These included whether the IRS's current position is consistent with its prior positions, whether the IRS's interpretation is of long standing, whether the IRS took the position essentially contemporaneously with the enactment of the applicable IRS section, and whether the regulation at issue is a "fighting regulation," one promulgated in anticipation of litigation in order to bolster the government's prospects in that litigation.²⁹

24. *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704 (2011). For discussion of *Mayo*, see 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); Sebastian Watt, Note, *Abolishing the Shelter Ambiguity: A New Framework for Treasury Regulation Deference Clarifying Chevron and Brand X*, 117 PENN ST. L. REV. 617 (2012).

25. Specific authority delegations appear in hundreds of particular sections of the Internal Revenue Code. See, e.g., N.Y.S. Bar Ass'n Tax Section, *Report on Legislative Grants of Regulatory Authority*, 2006 TNT 215-22 (Nov. 3, 2006).

26. General authority regulations derive from the blanket delegation in Code § 7805(a), which allows Treasury to issue regulations "needful . . . for the enforcement of this title . . ."

27. *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 465 U.S. 837 (1984).

28. See *Nat'l Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979).

29. As to fighting regulations, see *Smiley v. Citibank*, 517 U.S. 735, 742-43 (1996); *Indianapolis Life Ins. Co. v. United States*, 115 F.3d 430, 436 (7th Cir. 1997); Leandra Lederman, *The Fight over "Fighting Reg" and Judicial Deference in Tax Litigation*, 92 B.U. L. REV. 643 (2012).

Many of these premises were simply wrong. First, *National Muffler*, properly understood, was a deferential case.³⁰ Second, *Chevron* is less deferential than some have assumed. Agency positions have often been invalidated at Step One as contrary to an unambiguous statute.³¹ Step Two is easier for agencies but still an occasional source of invalidation.³² Indeed, the current trend is towards more exacting, less agency-friendly application of *Chevron*.³³ Third, many of the specific considerations *Mayo* dispensed with clearly were disfavored, even under prior case law.³⁴

Moreover, the fears some had about *Mayo* have not been confirmed by experience. Taxpayers have not fared worse in tax litigation since *Mayo* was handed down than they had before *Mayo*. Indeed, taxpayers have prevailed in many cases which have cited *Mayo*.³⁵

The issue decided in *Home Concrete* had been controversial for many years, and the lower courts were divided. The taxpayer had prevailed in the circuit court below,³⁶ and in several other cases of the line citing *Mayo*.³⁷

The taxpayer's win in the Supreme Court in *Home Concrete*, although narrow (5-4 or 4-1-4), provides additional reassurance, as do the most recent major cases citing *Mayo*. These include *Dominion Resources*, in which a circuit court invalidated on Administrative Procedure Act ("APA") grounds a regulation under section 263A of the Internal Revenue Code,³⁸ and *Loving*, in which a district court invalidated on *Chevron* Step One grounds Treasury regulations regulating tax return preparers.³⁹

30. This point is developed in Steve R. Johnson, *Preserving Fairness in Tax Administration in the Mayo Era*, 32 VA. TAX. REV. 269, 286-87 (2012).

31. See, e.g., Mark Seidenfeld, *A Syncopated Chevron: Emphasizing Reasoned Decisionmaking in Reviewing Agency Interpretation of Statutes*, 73 TEX. L. REV. 83, 94-95 (1994).

32. E.g., *Dominion Res., Inc. v. United States*, 681 F.3d 1313, 1317-19 (Fed. Cir. 2012); *Goldenstein v. SEC*, 451 F.3d 873 (D.C. Cir. 2006).

33. See Linda Jellum, *Chevron's Demise: A Survey of Chevron from Infancy to Senescence*, 59 ADMIN. L. REV. 725, 781 (2007) ("Those judges and scholars who viewed *Chevron* as an agency-friendly decision have been proved wrong"); Johnson, *supra* note 8, at pt. II.B.1.

34. For a detailed discussion of the "agency inconsistency" consideration, see Johnson, *supra* note 8, at pt. II.B.3.c.

35. E.g., *Estate of Petter v. Comm'r*, 653 F.3d 1012, 1023 (9th Cir. 2011); *Cohen v. United States*, 650 F.3d 717, 736 (D.C. Cir. 2011); *Mass. Mut. Life Ins. Co. v. United States*, 103 Fed. Cl. 111 (2012); *Pullins v. Comm'r*, 136 T.C. 432 (2011).

36. *Home Concrete & Supply, L.L.C. v. United States*, 634 F.3d 257 (4th Cir. 2010).

37. E.g., *Burks v. United States*, 633 F.3d 347 (5th Cir. 2011); *Carpenter Family Invs., LLC v. Comm'r*, 136 T.C. 373 (2011). Of course, there were cases on the other side as well. The Supreme Court granted certiorari to resolve the circuit split.

38. *Dominion Res., Inc. v. United States*, 681 F.3d 1313 (Fed. Cir. 2012). For discussion of the APA as applied to tax, see David J. Shakow, *Who's Afraid of the APA?*, TAX NOTES, Feb. 14, 2012, at 825; Rimma Tsvasman, Note, *No More Excuses: A Case for the IRS's Full Compliance with the Administrative Procedure Act*, 76 BROOK. L. REV. 837 (2011).

39. *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013).

In short, the Court's decision in *Home Concrete* is yet another indication that fears about *Mayo* were exaggerated. Indeed, by forcing taxpayers' counsel to broaden their angle of vision to include APA arguments along with traditional arguments, *Mayo* and other recent cases may actually enhance taxpayers' abilities to challenge improper tax regulations and rulings.⁴⁰

B. Reliance

Taxpayers often challenge positional changes by Treasury or the IRS on the ground that the changes undercut taxpayers' reasonable reliance on the prior positions.⁴¹ *Home Concrete* provides additional support for reliance arguments.

Justice Scalia's opinion concurring in part and concurring in the judgment affords much of the ammunition. His opinion begins: "It would be reasonable, I think, to deny all precedential effect to *Colony* . . . to overrule its holding as obviously contrary to our later law that agency resolutions of ambiguities are to be accorded deference. Because of justifiable taxpayer reliance I would not take that course."⁴²

Similarly, the penultimate sentence of Justice Scalia's opinion is: "What is needed for the system to work is that Congress, the Executive, and the private parties subject to their dispositions, be able to predict the meaning that the courts will give to their instructions."⁴³

The four justices participating in Justice Kennedy's dissenting opinion also accepted the importance of taxpayer reliance although, under the circumstances, they felt that Treasury's "clarification of an ambiguous statute, applicable to these taxpayers, did not upset legitimate settled expectations."⁴⁴

Protecting reasonable reliance is among the core "rule of law" values.⁴⁵ *Home Concrete* supports such values in another way as well. Throughout the progress of *Home Concrete* and related cases through the courts, the government emphasized that the taxpayers' transactions were tax shelters. This should be

40. See Steve R. Johnson, *Preserving Fairness in Tax Administration in the Mayo Era*, 32 VA. TAX REV. 269 (2012).

41. See generally Jeffrey L. Jowell, LAW AND BUREAUCRACY: ADMINISTRATIVE DISCRETION AND THE LIMITS OF LEGAL ACTION 12-13 (1975) ("Those with business interests need reliable rules in order to achieve certainty and predictability in their operations.").

42. *United States v. Home Concrete & Supply, L.L.C.*, 132 S. Ct. 1836, 1846 (Scalia, J., concurring). See also *id.* at 1847 (speaking of the "justifiable reliance of taxpayers").

43. *Id.* at 1849.

44. *Id.* at 1853 (Kennedy, J., dissenting).

45. For discussion of rule-of-law considerations in tax, see Steve R. Johnson, *An IRS Duty of Consistency: The Failure of Common Law Making and a Proposed Legislative Solution*, 77 TENN. L. REV. 563, 592-93 (2010).

irrelevant when the issue is the statute of the limitations.⁴⁶ The government's argument was, in essence, that the end justifies the means. In ignoring this invitation to selective justice, the Court upheld the rule of law.

C. Expertise

One of the reasons courts defer to agencies is the agencies' superior technical expertise. However, *Home Concrete* reminds us that the courts' constitutional responsibility to interpret the laws does not admit unlimited deference, regardless of agency expertise. The *Home Concrete* majority noted that the *Colony* Court "was aware it was rejecting the expert opinion of the Commissioner,"⁴⁷ and it reaffirmed that approach.

IV. RETROACTIVITY

I note here one of the potentially important issues to which *Home Concrete* gave less than satisfactory shrift. Among the most interesting of the issues raised by the briefs in the case was whether the amended section 6501(e) regulations were retroactive and, if so, what effect that would have on their validity. Resolving the case on the ground of stare decisis, the *Home Concrete* majority did not reach these questions.⁴⁸

The dissent rejected the stare decisis argument, so it did engage with retroactivity analysis, although only briefly. Finding the current version of section 6501(e) to differ materially from the version constructed in *Colony*, the dissent thought that the amended regulations merely clarified an ambiguous statute. "Having worked no change in the law, and instead having interpreted a statutory provision without an established meaning, the . . . regulation does not have an impermissible retroactive effect."⁴⁹

Far from satiating our appetite, this morsel makes us hungry for hardier fare. Section 7805(b)(1) of the Internal Revenue Code generally prohibits retroactive application of tax regulations, but the remainder of section 7805(b) sets out exceptions and allows the IRS to "prescribe the extent, if any, to which any . . . [sub-regulation guidance] . . . shall be applied without retroactive effect."⁵⁰

46. Cf. *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 465 U.S. 837, 864 (1984); *SEC v. Johnson*, 650 F.3d 710, 715 (D.C. Cir. 2011); *Loving v. IRS*, 917 F. Supp. 2d 67, 79 (D.D.C. 2013) (all holding that policy arguments are irrelevant at *Chevron's* Step One).

47. *Home Concrete*, 132 S. Ct. at 1844.

48. *Id.* at 1841.

49. *Id.* at 1853 (Kennedy, J., dissenting).

50. I.R.C. § 7805(b)(8) (2004).

The issues unresolved by *Home Concrete* will, no doubt, be addressed in future cases. These issues include the following: (1) What does retroactivity mean and when is a regulation or ruling retroactive? (2) Are the section 7805(b) exceptions so expansive that they effectively swallow the section 7805(b)(1) prohibition of retroactive regulations? (3) How much broader, if at all, is the opportunity for retroactive rulings as opposed to retroactive regulations?

V. DEFERENCE DOCTRINE

A. *Chevron*

A growing chorus of voices, including mine, has urged the overthrow of *Chevron*.⁵¹ That will not happen overtly, but there is some movement in the direction of submerging *Chevron* into “arbitrary and capricious” review under the APA.⁵²

As long as *Chevron* is around, however, we will have to work with it. The famous *Chevron* “two step” is: whether the statute is unambiguous, in which case deference is not accorded to the agency's view (Step One) and, if the statute is ambiguous, whether the agency's interpretation of it is at least reasonable, in which case deference is afforded (Step Two).

One of the problems with *Chevron* is the unsatisfactory nature of this analytical format. If the regulation in question is contrary to an unambiguous statute, it cannot be reasonable. If it is consistent with an unambiguous statute, it cannot be unreasonable. Thus, the two steps merge.⁵³ In his *Home Concrete* opinion, Justice Scalia aligned himself with this view, noting that “‘Step 1’ has never been an essential part of *Chevron* analysis.”⁵⁴

If the “Step One versus Step Two” distinction is to be followed, a recurring question is: where, if at all, is legislative history to be considered?⁵⁵ Textualist judges would prefer to avoid legislative history entirely, as Chief Justice Roberts did in his opinion for the Court in *Mayo*.⁵⁶ Purposivist judges grant legislative history

51. *E.g.*, Johnson, *supra* note 30, at 280-85; Gary Lawson & Stephen Kam, *Making Law out of Nothing at All: The Origins of the Chevron Doctrine*, 65 ADMIN. L. REV. 1 (2013); Patrick J. Smith, *Chevron's Conflict with the Administrative Procedure Act*, 32 VA. TAX REV. 813, 814-16 (2013).

52. 5 U.S.C. § 706(2)(A). *See generally* Patrick J. Smith, *The APA's Arbitrary and Capricious Standard and IRS Regulations*, TAX NOTES, July 16, 2012, at 271.

53. *See, e.g.*, Matthew C. Stephenson & Adrian Vermeule, *Chevron Has Only One Step*, 95 VA. L. REV. 597 (2009).

54. *Home Concrete*, 132 S. Ct. at 1846 n.1 (Scalia, J., concurring).

55. *See, e.g.* Melinda Forte, Note, *May Legislative History Be Considered at Chevron Step One? The Third Circuit Dances the Chevron Two-Step in United States v. Geiser*, 54 VILL. L. REV. 727 (2009).

56. Briefs for the parties and amici in *Mayo* cited committee reports. *E.g.* Reply Brief for

considerable sway, as Justice Kagan did in her opinion for the Court in a non-tax case *Judulang v. Holder*.⁵⁷ If legislative history is to be taken into account, does it bear on Step One or Step Two? The majority opinion in *Home Concrete* was penned by Justice Breyer, a committed purposivist. In a portion of the opinion that was for a plurality only (because Justice Scalia did not subscribe to it), Justice Breyer addressed the contents of Step One. Emphasizing language from *Chevron*, he described Step One analysis as “employing traditional tools of statutory construction.”⁵⁸ For Justice Breyer, such traditional tools include legislative history. Indeed, in short order thereafter, Justice Breyer rehearsed *Colony's* reading of the legislative history.⁵⁹

None of the above opinions have carried the day, nor are they likely to. Whether legislative history is considered at Step One largely depends on the accident of which judge—a textualist or a purposivist—happens to pen the particular decision.⁶⁰

B. *Brand X*

In 2005, the Supreme Court took another major step (whether forward or backward) in deference doctrine in *National Cable & Telecommunications Association v. Brand X Internet Services*.⁶¹ The Court held that a subsequent regulation promulgated by an agency trumps prior judicial interpretation of a statute as long as two conditions are met: the regulation qualifies for *Chevron* deference and the prior cases did not base their results on an

Petitioners at 8 n.2, *Mayo Found. for Med. Educ. & Research v. United States*, 131 S. Ct. 704 (2011) (No. 09-837), 2010 WL 1775871, at *8 n.2; Brief for the United States in Opposition at 11, *Mayo*, 131 S. Ct. 704 (No. 09-837), 2010 WL 1557537, at *11; Brief of Georgetown Univ., Loyola Univ. Med. Center, St. Louis Univ., Univ. of Arkansas, Univ. of North Dakota, Univ. of Rochester, Univ. of Tennessee & Vanderbilt Univ. as Amici Curiae at 15 n.11, *Mayo*, 131 S. Ct. 704 (No. 09-837), 2010 WL 545704, at *15 n. 11. Nonetheless, Justice Roberts' opinion for the Court cited no committee reports. See *Mayo*, 131 S. Ct. at 711-16.

In a post-*Mayo* tax decision, the Court did not comment on committee reports generally, but it did unanimously condemn reliance on so called “Blue Books,” i.e., post-enactment reports on legislation prepared by Congress' Joint Committee on Taxation. *United States v. Woods*, 134 S. Ct. 557, 568 (2013).

There is some incongruity between some judges' disregard of committee reports and the fact that Treasury regulations provide that taxpayer reliance on committee reports – including the Blue Books – can preclude imposition of accuracy-related tax penalties. See *Treas. Reg. § 1.6662-4(d)(3)(iii)*.

57. 132 S. Ct. 476 (2011). See also Irving Salem, *Supreme Court Clarifies Mayo; or Is It Something Bolder?* TAX NOTES, Jan. 9, 2012, at 255 (discussing *Judulang*).

58. *Home Concrete*, 132 S. Ct. at 1844 (quoting *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 465 U.S. 837, 843 n.9 (2004)).

59. *Id.* at 1844.

60. See e.g., *Loving v. IRS*, 917 F. Supp. 2d 67, 79 (D.D.C. 2013) (the court took a textual approach to *Chevron* and gave legislative history short shrift at Step One).

61. 545 U.S. 967 (2005).

unambiguous statute.⁶²

It was clear from the start that internal tensions in *Brand X* would require that the Court modify this formulation in later cases. First, when the regulation seeks to oust a pre-*Brand X* decision, it often “will be incredibly difficult to determine whether the decision purported to be giving meaning to an ambiguous, or rather an unambiguous, statute.”⁶³ That is because, in such cases, the Court “had no inkling that it *must* utter the magic words ‘ambiguous’ or ‘unambiguous’ in order to (poof!) expand or abridge executive power Indeed, [the courts were] unaware of even the utility (much less the necessity) of making the ambiguous/nonambiguous determination in [such prior] cases”⁶⁴

Second, *Brand X* involved a subsequent regulation trumping a lower court (federal circuit court) decision. *Brand X* did not state whether its rule allows agencies to overthrow U.S. Supreme Court decisions. Taxpayers in some cases of the *Home Concrete* line argued that *Brand X* does not allow this result.⁶⁵

Third, *Brand X* did not speak to whether the prior court's opinion could be reexamined by a later court. For example, suppose the earlier decision said that the statute is unambiguous but that assertion is plainly incorrect. Would a later court (one reviewing a regulation purporting to oust the earlier decision) be bound by the earlier court's erroneous assertion, or could it probe the validity of the assertion?

Home Concrete did not answer these and other questions about *Brand X* because the plurality took the doctrine into new territory. According to the plurality, *Brand X* and prior cases (including *Chevron*) were based on “deciding whether, or when, a particular statute in effect delegates to an agency the power to fill a gap, thereby implicitly taking from a court the power to void a reasonable gap-filling interpretation.”⁶⁶

The plurality acknowledged “that judges today [might] use other methods to determine whether Congress left a gap to fill,” then added: “[b]ut that is beside the point. The question is whether the Court in *Colony* concluded that the statute left such a gap. And, in our view, [*Colony*] makes it clear that it did not.”⁶⁷

To Justice Scalia, this revised deference doctrine leads “in a

62. *Id.* at 982. See also Doug Geyser, Note, *Courts Still “Say What the Law Is”*: Explaining the Functions of the Judiciary and Agencies After *Brand X*, 106 COLUM. L. REV. 2129 (2006).

63. *Home Concrete*, 132 S. Ct. at 1846-47 (Scalia, J., concurring).

64. *Id.* at 1846 (emphasis in original).

65. See Mark E. Berg, *Practitioner Has Minor Quibble with Analysis of Home Concrete*, TAX NOTES, July 9, 2012, at 213.

66. *Home Concrete*, 132 S. Ct. at 1843.

67. *Id.* at 1844.

direction that will create confusion and uncertainty” because it adds “yet another lopsided story to the ugly and improbable structure that our law of administrative review has become,”⁶⁸ thus “making our judicial-review jurisprudence curiouser and curiouser”⁶⁹

To Justice Scalia, the answer to the conundrum is easy. He dissented in *Brand X* and remains unreconstructed. *Brand X* jurisprudence does not become byzantine if *Brand X* is discarded. Justice Scalia is clearly correct in his diagnosis, if not necessarily in his prescribed remedy. *Brand X* needed fixing from the start, but the approach of the plurality makes the doctrine more, not less, unwieldy.

The difference between Justice Breyer’s and Justice Scalia’s approaches to *Brand X* is illustrated by the line of cases testing the validity of the check-the-box regulations. The Code prescribes different income tax treatment of corporations as opposed to partnerships as opposed to trusts as opposed to disregarded entities such as sole proprietorships and divisions of corporations.⁷⁰ Thus, significant consequences turn on how an entity is classified.

The applicable statutes are of limited help in effecting such classifications.⁷¹ Thus, case law and Treasury regulations have long done the heavy lifting. In 1935, in the *Morrissey* case, the Supreme Court held that an entity organized as a trust under state law was nonetheless taxable as a corporation for federal income tax purposes.⁷² The Court reached its decision based on “the salient features” of trusts and corporations,⁷³ noting certain characteristics as typical of a corporation, including the existence of associates, continuity of the entity, centralized management, limited personal liability, ready transferability of ownership interests, and title to property.⁷⁴ *Morrissey* gave no indication that the Court considered classification a matter of option or election for the entity in question.

Subsequent cases, particularly the *Kintner* decision,⁷⁵ developed this approach. The Treasury Department promulgated

68. *Id.* at 1847 (Scalia, J., concurring).

69. *Id.* at 1848.

70. In general, C corporations are separate taxpayers from their shareholders while partnerships are pass-through entities subject to complex computational rules and disregarded entities have no independent status. *See, e.g.*, I.R.C. ch. 1, subchs. C & K.

71. *See, e.g.*, I.R.C. § 7701(a)(3) (2010) (providing a sketchy “definition” of corporation).

72. *Morrissey v. Comm’r*, 296 U.S. 344 (1935).

73. *Id.* at 359.

74. *Id.* at 359-61.

75. *United States v. Kintner*, 216 F.2d 418 (9th Cir. 1954).

regulations based on this case law—the so called *Kintner* regulations—which enshrined the mandatory approach, making classification depend upon the presence or absence of defined entity characteristics.⁷⁶

This mandatory approach was in place between at least 1935 (the date of *Morrissey*) and December 1996. On that latter date, the Treasury replaced the *Kintner* regulations with the check-the-box regulations, giving eligible entities substantial freedom to choose how they will be classified for tax purposes.⁷⁷ This change was based on the perception that the mandatory approach forced taxpayers and the IRS to expend excessive time and money applying the designated factors.⁷⁸

Some commentators challenged the validity of the check-the-box regulations.⁷⁹ Nonetheless, the regulations have been upheld by every court that has passed on them, first by the Sixth Circuit in the *Littriello* case,⁸⁰ then by a succession of other circuits and trial courts.⁸¹

How does the *Littriello* line of cases fit with *Brand X* as interpreted by *Home Concrete*? This question turns on whether *Morrissey* precluded the check-the-box regulations—just as the question in *Home Concrete* turned on whether *Colony* precluded the new section 6501(e) regulations. As seen below, one likely would answer this question differently under the plurality's approach than under Justice Scalia's approach.

The *Morrissey* Court noted the sparse statutory definition of "corporation,"⁸² and it traced the evolving case law and regulations attempting to give the definition greater content.⁸³ The court observed that

without further [statutory] definition, the Treasury Department was authorized to supply rules for the enforcement of the Act within the permissible bounds of administrative construction. Nor can this authority be deemed to be so restricted that the regulations, once issued, could not later be clarified or enlarged so as to meet administrative exigencies or conform to judicial decision We find no ground for the contention that by the

76. Treas. Reg. §§ 301.7701-1 to -3 (as effective up to December 1996).

77. Treas. Reg. §§ 301.7701-1 to -3 (2011).

78. *E.g.*, *Pierre v. Comm'r*, 133 T.C. 24, 30 (2009); *Dover Corp. v. Comm'r*, 122 T.C. 324, 330 (2004).

79. *E.g.*, Gregg D. Polsky, *Can Treasury Overrule the Supreme Court?*, 84 B.U. L. REV. 185 (2004).

80. *Littriello v. United States*, 484 F. 3d 372 (6th Cir. 2007).

81. *E.g.*, *McNamee v. Dep't of Treasury*, 488 F.3d 100 (2d Cir. 2007); *Med. Practice Solutions, LLC v. Comm'r*, 132 T.C. 125 (2009).

82. "The term 'corporation' includes associations, joint-stock companies, and insurance companies." Revenue Act of 1924 § 2(a)(2), 43 Stat. 253.

83. *Morrissey v. Comm'r*, 296 U.S. 344, 349-52 (1935).

enactment of the Revenue Act of 1924 the Department was limited to its previous regulations as to associations We think that the Department did not exceed its powers in rewriting its regulation, in the light of [judicial decisions].⁸⁴

But *Morrissey* did not rest on the regulations. “The difficulty with the regulations as an exposition was that they themselves required explication; that they left many questions open with respect both to their application to particular enterprises and to their validity as applied.”⁸⁵

Accordingly, *Morrissey* rested not upon the regulations but upon the Court’s construction of the statute.⁸⁶ Although acknowledging that “it is impossible in the nature of things to translate the statutory concept of ‘association’ into a particularity of detail that would fix the status of every sort of enterprise or organization which ingenuity may create,”⁸⁷ the *Morrissey* decision—in the construction of ordinary and accepted commercial meanings—elaborated criteria to resolve the classificatory dispute. And those criteria ultimately gave rise to the *Kintner* regulations.

In *Home Concrete*, the plurality and Justice Scalia took different approaches to the degree of administrative flexibility that exists after judicial interpretation of a statute. Those different approaches likely would mean different views as to whether the *Littriello* cases were correctly decided.

For the plurality, the controlling question under *Brand X* is whether Congress left a gap for the agency to fill. It found no such gap as to the section 6501(e) regulations.⁸⁸ Perhaps *Colony* could more or less plausibly be read to find no gap in the statute. The same could not be said of *Morrissey*. The above quoted language makes plain that the *Morrissey* Court found gaps aplenty in the statutory definition of “corporation.” Thus, the approach of the *Home Concrete* plurality, if applied to the *Littriello* context, would uphold the validity of the check-the-box regulations under *Brand X*.

In contrast, Justice Scalia’s *Home Concrete* concurrence repeated his position—rejected by the majority in *Brand X*—that: “Once a court has decided upon its *de novo* construction of the statute, there no longer is a different construction that is consistent with the court’s holding and available for adoption by

84. *Id.* at 354-55.

85. *Id.* at 356.

86. *Id.*

87. *Id.*

88. *United States v. Home Concrete & Supply, LLC*, 132 S. Ct. 1836, 1844 (2012) (“The question is whether the Court in *Colony* concluded that the statute left such a gap. And, in our view, the opinion . . . makes clear that it did not [T]here being no gap to fill, the Government’s gap-filling regulation cannot change *Colony*’s interpretation of the statute.”).

the agency.”⁸⁹ Accordingly, Justice Scalia concurred in *Home Concrete* “because it is indisputable that *Colony* resolved the construction of the statutory language at issue here, and that construction must therefore control.”⁹⁰ *Morrissey* construed the 1924 Revenue Act, adducing operative criteria from which classification was mandatory.⁹¹ Nothing whatever in *Morrissey* suggested that classification is elective.⁹² Application of Justice Scalia’s approach would call into question the validity of the check-the-box regulations.

We have not seen the end debate about the effect of *Home Concrete* on *Brand X*.⁹³ The doctrinal “clarifications” in *Home Concrete* will require their own clarifications in future cases, tax and non-tax.

VI. STATUTORY INTERPRETATION

A. *Elephants and Mouseholes*

This title derives from a principle of statutory interpretation that appears in *Home Concrete*. Under this principle, a court will require clear legislative evidence before it holds that a statute was intended to effect a major substantive change. Inferences from wisps of textual or other evidence will not suffice. “Congress . . . does not alter the fundamental details of a regulatory scheme in vague terms or ancillary provisions—it does not, one might say, hide elephants in mouseholes.”⁹⁴ This principle, a relative of the “plain statement” canon of construction, has been invoked in many

89. *Id.* at 1846 (Scalia, J., dissenting) (quoting Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs., 545 U.S. 967, 1018 n.13 (2005)).

90. *Id.* at 1848.

91. The *Morrissey* Court classified the entity at issue by analysis of the entity’s “salient features.” 296 U.S. at 359. The language of the applicable statute—an ancestor of current I.R.C. § 7701(a)(3)—was sparse, but the Court developed its analysis from the connotations and implications of the statutory terms. *See id.* at 295-97.

92. The Court acknowledged that Treasury had room to interpret the statute and to later to revise its interpretation. But the Court did not accord Treasury unlimited flexibility. To be valid, the interpretation or reinterpretation had to conform to the statute and judicial decisions; they could not supplant them with a wholly novel approach of Treasury’s rule devising. *Id.* at 354-55 (“[T]he Treasury Department was authorized to supply rules for the enforcement of the act *within the permissible bounds* of administrative construction. Nor can this authority be deemed to be so restrictive that the regulations, once issued, could not later be clarified or enlarged so as to meet administrative contingencies or conform to judicial decision.”) (emphasis added).

93. A recent Fourth Circuit case is an example. The court held that a Board of Immigration Appeals interpretation trumped a prior Fourth Circuit construction of a statute. The court acknowledged both the plurality’s and Justice Scalia’s *Home Concrete* views but distinguished *Home Concrete*. *Patel v. Napolitano*, 706 F.3d 370, 375-376 (4th Cir. 2013), *cert. denied*, *Patel v. Johnson*, 134 S. Ct. 1282 (2014).

94. *Whitman v. Am. Trucking Ass’ns*, 531 U.S. 457, 468 (2001).

federal and state cases, both tax⁹⁵ and non-tax.⁹⁶

In *Home Concrete*, the government argued that changes to what is now section 6015(e) which were made after the years at issue in *Colony*, required a different outcome.⁹⁷ The *Home Concrete* majority rejected this contention, finding the changes too weak to support the government's argument. Justice Breyer added to the metaphorical luxuriance of the precept: "to rely . . . on this solitary word change in a different subsection is like hoping that a new batboy will change the outcome of the World Series."⁹⁸

B. *Stare Decisis*

The majority/plurality opinion is inconsistent in its adherence to *stare decisis*. On the one hand, its reaffirmation of *Colony* was based on a strong invocation of the principle.⁹⁹

On the other hand, *Colony* states: "it cannot be said that the language [of even the old version of the statute] is unambiguous."¹⁰⁰ The plurality brushed this aside on the ground that "the Court decided [*Colony*] nearly 30 years before it decided *Chevron*. There is no reason to believe that the linguistic ambiguity noted by *Colony* reflects a post-*Chevron* conclusion that Congress had delegated gap-filling power to the [Treasury]."¹⁰¹

In other words, the plurality discounted what *Colony* did say in favor of what it thought *Colony* would have said had the *Colony* Court anticipated *Chevron* nearly 30 years later, *Brand X* nearly 50 years later, and *Home Concrete's* refinement of *Colony* nearly 55 years later. This is not adherence to *stare decisis*; it is imaginative reconstruction in the extreme.

C. *Continuing Dialogue*

Home Concrete contains interesting byplay between Justice Scalia's concurrence and Justice Kennedy's dissent as to a core question of statutory interpretation in tax: the respective roles of the branches of government.

The dissent advanced the proposition: "Our legal system

95. See Steve R. Johnson, *Elephants, Mouse Holes, Non-Barking Dogs, and Statutory Interpretation*, STATE TAX NOTES, June 25, 2012, at 911.

96. *E.g.*, *FDA v. Brown & Williamson Tobacco Corp.*, 529 U.S. 120, 159-60 (2000); *MCI Telecomm. Corp. v. Am. Tel. & Tel. Co.*, 512 U.S. 218, 231 (1994).

97. *Home Concrete*, 132 S. Ct. at 1841.

98. *Id.* at 1842. See also *id.* at 1849 (Scalia, J. concurring) (stating that a precedent should not "be overturned on the basis of statutory indications as feeble as those asserted here").

99. *Id.* at 1841 (majority opinion).

100. *Colony, Inc. v. Comm'r*, 357 U.S. 28, 33 (1958).

101. *Home Concrete*, 132 S. Ct. at 1844.

presumes there will be continuing dialogue among the three branches of Government on questions of statutory interpretation and application."¹⁰² This is a notion Justice Kennedy has urged before.¹⁰³ Some commentators have espoused similar views.¹⁰⁴

Justice Scalia, of course, has repeatedly inveighed against doctrines that liberate judges to substitute their preferences for those of Congress. Unsurprisingly, Justice Scalia rejected Justice Kennedy's "romantic, judge-empowering image," seeing it as inconsistent with *Vermont Yankee's* teaching "that Congress prescribes and we obey, with no discretion to add to the administrative procedures that Congress has created."¹⁰⁵

D. "Best Answer" Versus Deference

At the heart of the peculiarities of *Home Concrete* is its unsatisfactory attempt to cobble together two fundamentally inconsistent approaches to statutory interpretation: the "best answer" model versus the deferential model. A "best answer" court looks at all available evidence in the attempt to discover the single, true, or best meaning of the statute.¹⁰⁶

The deferential model, in contrast, is built on the premise that there may be several permissible interpretations of a statute. The role of the courts is not to enshrine the only or the best answer but merely to make sure that the interpretative answer the agency selects is within the range of the permissible.

Colony was a "best answer" exercise at a time when this model dominated. All three of the *Home Concrete* opinions acknowledged that we now are in a world in which, within limits, deference holds sway.¹⁰⁷

On the basis of an inconsistently applied notion of *stare decisis*, *Home Concrete* engrafted a "best answer" decision onto a deferential jurisprudence. As *Mead* muddled *Chevron*, so *Home Concrete* muddles *Brand X*.¹⁰⁸ Contemporary deference doctrine, and the

102. *Id.* at 1852 (Kennedy, J., dissenting).

103. See *Blakely v. Washington*, 542 U.S. 296, 326 (2004) (Kennedy, J., dissenting).

104. E.g., William D. Popkin, *The Collaborative Model of Statutory Interpretation*, 61 S. CAL. L. REV. 541, 543 (1988).

105. *Home Concrete*, 132 S. Ct. at 1848. See also *Vt. Yankee Nuclear Power Corp. v. Natural Res. Def. Council, Inc.*, 435 U.S. 519 (1978).

106. E.g., *Comm'r v. Engle*, 464 U.S. 206, 217 (1984) ("Our duty then is to find that interpretation which can most fairly be said to be imbedded in the statute, in the sense of being most harmonious with its scheme and with the general purposes that Congress manifested.") (punctuation omitted) (quoting *NLRB v. Lion Oil Co.*, 352 U.S. 282, 297 (1957) (Frankfurter, J., concurring in part & dissenting in part)); *Helvering v. Morgan's Inc.*, 293 U.S. 121, 126 (1934) (looking to related sections and the history of tax legislation in trying to ascertain "the true meaning [of a section] of the revenue acts").

107. *Home Concrete*, 132 S. Ct. at 1844 (plurality opinion); *id.* at 1846 (Scalia, J., concurring in part and concurring in the judgment); *id.* at 1851-52 (Kennedy, J., dissenting).

108. Lisa Shultz Bressman, *How Mead Has Muddled Judicial Review of Agency Action*,

statutory interpretation landscape of which it is a feature, is a house of cards. *Home Concrete* jerry-rigs another fix onto the system. The most fundamental question raised by *Home Concrete* is how long that system can endure before it collapses of its own weight.

VII. CONCLUSION

Administrative law principles have irreversibly established themselves as part of tax law.¹⁰⁹ The consequences of this “intrusion” will take decades to fully work out. Thus, the ongoing wave of litigation as to the validity of tax regulations is unlikely soon to abate.

Tax has always been about statutory interpretation. Perhaps no other body of substantive law engages principles of interpretation more often than does tax law. We are in an era of intense interest in, and controversy about, statutory interpretation.¹¹⁰

Home Concrete reflects the intersection of these administrative and statutory currents. What the Court did in *Home Concrete* is unlikely to put any issue to rest. Yet its insights as to those issues cannot be ignored and will be analyzed and debated for years in the case law and the commentary. And what the Court refrained from doing in *Home Concrete* will allow the pressure to continue to build on the issues, demanding eventual resolution. *Home Concrete* is a marker on a long and important road.

58 VAND. L. REV. 1443, 1444-45 (2005); see *United States v. Mead Corp.*, 533 U.S. 218 (2001).

109. See Steve R. Johnson, *Intermountain and the Importance of Administrative Law in Tax Law*, TAX NOTES, Aug. 23, 2010, at 837, 838 (2010).

110. See, e.g., Philip P. Frickey, *From the Big Sleep to the Big Heat: The Revival of Theory in Statutory Interpretation*, 77 MINN. L. REV. 241 (1992).