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## The Future of American Tax Administration: Conceptual Alternatives and Political Realities

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# ARTICLES

## **THE FUTURE OF AMERICAN TAX ADMINISTRATION: CONCEPTUAL ALTERNATIVES AND POLITICAL REALITIES**

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When their environments change markedly, individuals and species adapt or they cease to be. This principle holds institutionally as well as biologically. History is littered with both discarded enterprises (such as the Children's Crusade, the Hanseatic League, and the Golden Horde) and successful transformations (such as the evolution of much of the Holy Roman Empire into modern Germany).

The Internal Revenue Service now stands at the precipice of an uncertain future. With considerable justification, the IRS considers itself as being among the most successful revenue collection organizations in the world.<sup>1</sup> Whether that characterization will remain accurate in the future will depend on how the IRS deals, and is allowed to deal, with intersecting trends threatening to cripple the ability of the IRS to perform its core mission of revenue collection.

Part I of this article describes this intersection, which has reached crisis proportions.<sup>2</sup> The workload of the IRS—both in revenue collection and especially in adventitious missions Congress has chosen to assign to the IRS—has burgeoned in recent decades. At the same time, the resources allocated to the IRS by successive Congresses and Administrations—never fully adequate—have declined in inflation-adjusted terms and, in recent years, even in nominal terms. Part I also notes the most visible manifestations of the intersection of these trends: decreases in key IRS activities and results almost across the board, with consequent substantial losses to the federal fisc.

Two obvious and “easy” possible fixes immediately leap to mind: (1) the IRS should become more efficient and/or (2) Congress should appropriate more money for the IRS. Both of these approaches have roles to play. However, Part II explains why neither alone nor the two together can be fully satisfactory.

Theoretically, there are a number of different ways to relax the anaconda grip of the IRS's workload and budget squeeze. Some would require legislation. Others could be implemented without statutory change. Part III sketches some of the alternatives. It also notes precedents for some of them as well as obstacles to and potential disadvantages of their adoption.

Part IV examines reasons why desirable reforms have not yet been implemented. There are plenty of plausible ideas. Our failure to implement the best ideas results in part from intellectual failures (clinging to policy preferences and ways of thinking that make little sense in the current environment) but in larger part from political and bureaucratic realities. Reforms advantageous to the country would forfeit privileges and opportunities cherished by key congressional and executive actors.

While it would be naive to discuss tax administration without awareness of the hampering realities, it would be unduly pessimistic to quit the field in despair. Constellations in the political firmament are in constant motion. Changes not currently

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<sup>1</sup> Two decades ago, former Commissioner Cohen wrote: “With all of its faults, and there are many, [the modern IRS] is still one of the best systems of administration in the world. I have gone all over the world . . . and everywhere our system is admired. Only here is it derided.” Sheldon S. Cohen, *The Erwin N. Griswold Lecture*, 14 AM. J. TAX POL'Y 113, 115 (1997). More recently, current Commissioner Koskinen describes the IRS as “the world's largest financial institution, [which] continues to play a pivotal role in funding the United States government and enforcing the nation's tax laws.” John A. Koskinen, Letter from the Commissioner, in INTERNAL REVENUE SERVICE DATA BOOK 2014, at iii.

<sup>2</sup> Rhetorical inflation is a hallmark of our age in which events even mildly felicitous are described as “great” or “awesome” and events only mildly inconvenient are considered to be “devastating.” The word “crisis” drips from American lips far too cavalierly. Yet I believe it is an appropriate description of the subject at hand. See text accompanying notes 45 to 48, *infra*.

feasible may become feasible later. Recent history has shown that long-blocked changes can suddenly become politically viable. That being so, how should the tax community proceed? I suggest two principles. First, tax administrators, practitioners, and scholars should continue to think and talk about the merits of ideas unhampered by the thought that they might not be feasible. In public policy generally, and in tax policy in particular, realities are temporary, not perpetual. We should build the intellectual case for good ideas in preparation for the time when changing political or economic dynamics redefine the boundaries of feasibility.

Second, bad ideas as well as good ones can suddenly emerge as serious candidates for adoption. The tax community must be alert to these threats and respond to them rapidly and energetically. If accepted as an excuse for inertia, the notion that it would never be adopted may be the precursor to a professional lifetime of regret when the terrible idea, unopposed, actually wins adoption.

## I. INTERSECTING FORCES AND CURRENT CRISIS

This Part I explores two dimensions. First, it describes the “perfect storm” that has produced the current crisis in tax administration in the United States. Second, it charts the consequences, the particular harms inflicted by this perfect storm.

### A. The Perfect Storm

It is often said that the mission of the IRS is to collect the revenue needed to run the federal government, but this is imprecise. It is not the IRS’s role to wring every dollar it can out of the citizenry by whatever means necessary, fair or foul. Instead, as the IRS itself acknowledges:

[I]t is the duty of the Service to carry out [tax] policy by correctly applying the laws enacted by Congress; to determine the reasonable meaning of various [Internal Revenue] Code provisions in light of the Congressional purpose in enacting them; and to perform this work in a fair and impartial manner, with neither a government nor a taxpayer point of view.<sup>3</sup>

Properly executing this duty requires the IRS to balance many desiderata, including:

- Providing “taxpayers top quality service by helping them understand and meet their responsibilities,”<sup>4</sup>
- “[A]pplying the tax law with integrity and fairness to all,”<sup>5</sup>
- Collecting “the proper amount of tax revenue at the least cost,”<sup>6</sup>
- “[C]ontinually improving the quality of [its] products and services,”<sup>7</sup>
- “[P]erforming in a manner warranting the highest degree of public confidence in [the IRS’s] integrity, efficiency and fairness,”<sup>8</sup> and
- Being “vigorous in requiring compliance with law and . . . relentless in [attacking] unreal tax devices and fraud.”<sup>9</sup>

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<sup>3</sup> Rev. Proc. 64-22, 1964-1 C.B. 689.

<sup>4</sup> 2002-2 C.B. ii.

<sup>5</sup> *Id.*

<sup>6</sup> 1996-1 C.B. ii.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> 1976-1 C.B. ii.

No human institution ever achieves its goals perfectly.<sup>10</sup> But the ability of the IRS to achieve even satisfactory levels of performance has been put into severe question by the confluence of three trends: (1) substantial declines in the IRS's budget, (2) expansion of workload in the IRS's core revenue collection function, and (3) ever-expanding other responsibilities placed by Congress on the IRS, that is, responsibilities not essentially connected to revenue collection but deriving instead from non-revenue priorities. These trends are described below.

### 1. *Declining Budget*

We are not accustomed to the budgets of government agencies—especially key government agencies<sup>11</sup>—declining. But the budget of the IRS has dropped, not just in real (that is, inflation-adjusted) terms but also in nominal (stated dollar amount) terms.<sup>12</sup>

Agencies cry for greater funding more frequently than newborns cry for milk. Sometimes agencies' budgetary wails are valid, sometimes they are not. It is fair to say, however, that the underfunding of the IRS is not new but is of long standing.<sup>13</sup>

What is new is the severity of budget cuts suffered recently by the IRS. In the period 2010 to 2015, the IRS's budget was slashed by a total of \$1.2 billion, more than 17%.<sup>14</sup> In a joint letter to the Senate Committee on Appropriations and the House Committee on Appropriations, seven former Commissioners of Internal Revenue stated: "None of us ever experienced, nor are we aware of, any IRS appropriations reductions of this magnitude over such a prolonged period of time."<sup>15</sup>

The most recent budget, enacted in the Consolidated Appropriations Act of 2016,<sup>16</sup> "freezes most funding for the IRS at the fiscal year 2015 level," although it does provide "an additional \$290 million targeted solely for taxpayer services to ensure that the agency

<sup>10</sup> Certainly, that is true of taxation. "The wisdom of man never yet contrived a system of taxation that operates with perfect equality." Andrew Jackson, *quoted by* Peter J. Reilly, *Some Presidential Words on Federal Income Taxes*, FORBES, Aug. 15, 2012, at 7, <http://www.forbes.com/sites/peterjreilly/2012/08/15/some-presidential-words-on-federal-income-taxes> [<https://perma.cc/JT6B-EH2V>].

<sup>11</sup> The critical significance of the IRS to the enterprise of governing the United States cannot be doubted. *Bull v. United States*, 295 U.S. 247, 259 (1935) ("[T]axes are the life-blood of government, and their prompt and certain availability an imperious need."); *see also* *United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 734 (1979) ("That collection of taxes is vital to the functioning, indeed existence, of government cannot be denied."). The IRS collects about 93% of federal receipts. U.S. GOV'T ACCOUNTABILITY OFFICE, *IRS 2016 BUDGET: IRS IS SCALING BACK ACTIVITIES AND USING BUDGET FLEXIBILITIES TO ABSORB FUNDING CUTS 1* (2015).

<sup>12</sup> For a chart comparing IRS funding (1) as recommended by the IRS Oversight Board, (2) as requested by the President, and (3) as actually appropriated by Congress, all for fiscal years 2009 to 2015, see TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, *REDUCED BUDGETS AND COLLECTION RESOURCES HAVE RESULTED IN DECLINES IN TAXPAYER SERVICE, CASE CLOSURES, AND DOLLARS COLLECTED 1* (May 8, 2015).

<sup>13</sup> "Historically, the lack of a political constituency has contributed to a level of funding for [United States] tax administration which almost certainly is far less than optimal." Michael C. Durst (reporter), *REPORT OF THE SECOND INVITATIONAL CONFERENCE ON INCOME TAX COMPLIANCE 12* (1988). I have been beating this drum for over a decade. *See* Steve Johnson, *The 1998 Act and the Resources Link Between Tax Compliance and Tax Simplification*, 51 U. KAN. L. REV. 1013 (2003).

<sup>14</sup> Letter from Mortimer M. Caplin, Sheldon S. Cohen, Lawrence B. Gibbs, Fred T. Goldberg, Jr., Shirley D. Peterson, Margaret M. Richardson & Charles O. Rossotti to Senators Thad Cochran and Barbara A. Mikulski & Representatives Harold Rogers and Nita M. Lowey (Nov. 9, 2015) (on file with author) [hereinafter *Seven Commissioners Letter*]. Collectively, the seven former Commissioners served for fifty years in Administrations of both major political parties.

<sup>15</sup> *Id.*

<sup>16</sup> H.R. 2029, 114th Cong. (1st Sess. 2016).

responds to taxpayer questions in a timely manner, and to improve fraud detection and prevention and cybersecurity.”<sup>17</sup> However, this increase is contingent on the IRS reporting to Congress quarterly on the IRS’s plans for the use of these funds.<sup>18</sup> In any event, \$290 million does not come close to offsetting pre-2016 IRS budget cuts.

## 2. *Increasing Revenue Responsibilities*

The IRS’s workload in its core revenue functions has grown and will continue to grow. First, even if the Internal Revenue Code (the “Code”) changed not a wit, the population of the United States grows every year and the number of businesses in the United States grows in most years. “[I]n real terms, [the Fiscal Year 2016 projected] funding level is less than the IRS’s enacted level in FY 1991, 25 years ago, when there were 38 million fewer individual taxpayers, only about half as many business tax returns, and a far less complicated tax code.”<sup>19</sup>

Second, the Code does change—a lot.<sup>20</sup> Every year, Congress adds numerous new Code provisions and substantially modifies numerous existing provisions.<sup>21</sup> Each change requires creation or alteration of IRS forms and explanatory publications, sometimes necessitates revised regulations or other guidance,<sup>22</sup> and compels training or retraining of IRS employees throughout the organization.<sup>23</sup>

Third, globalization guarantees that transnational tax enforcement and administration will be a major and enduring part of the IRS’s future. Over a trillion dollars a day flow across international boundaries.<sup>24</sup> The ease with which international capital flows can be effected guarantees that some taxpayers—both Americans and others—will attempt to evade their tax obligations through concealed foreign arrangements.<sup>25</sup> In addition, of course, legal transactions involving both inbound and outbound economic

<sup>17</sup> HOUSE APPROPRIATIONS COMMITTEE, FY 2016 OMNIBUS – FINANCIAL SERVICES APPROPRIATIONS 1 (2016), <http://appropriations.house.gov/> [<https://perma.cc/JMN7-NREA>].

<sup>18</sup> H.R. 2029, *supra* note 16, at Division E, Title I.

<sup>19</sup> Letter from Anne Wall, Assistant Treas. Sec’y for Legislative Affairs, to Sen. Robert P. Casey, at 3 (Nov. 12, 2015) (on file with author).

<sup>20</sup> The changes may be to either the substantive or procedural tax law. For discussion of the demands created by the procedural changes enacted in the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685 (1998) (partially codified in scattered sections of the Code), see Johnson, *supra* note 13, at 1039-44.

<sup>21</sup> See, e.g., Cohen, *supra* note 1, at 114-15; *supra* note 3; Seven Commissioners Letter, *supra* note 14, at 4.

<sup>22</sup> In 1974, there were 1,500 pages in the Code compared to about 5,500 pages in 2014. In 1974, there were about 12,100 pages of Treasury tax regulations compared to over 44,000 pages in 2014. Jonathan H. Adler, *How the IRS has Changed Since 1974*, WASH. POST (Apr. 2, 2014), <https://www.washingtonpost.com/news/volokh-conspiracy/wp/2014/04/02/how-the-irs-has-changed-since-1974/> [<https://perma.cc/XW2N-Z2DM>].

<sup>23</sup> See, e.g., Nicole Duarte, *New Programs Strain IRS Resources, Budget*, TAX NOTES, Jan. 3 2011, at 63 (“Congress in 2010 enacted numerous tax law changes and new tax-related programs and enforcement initiatives. . . . Congress’s work managed to leave the [IRS] with a potentially overwhelming slate of new initiatives to administer.”).

<sup>24</sup> See Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1585-86 (2000) (citing studies); see also Peter D. Sutherland, *Sharing the Bounty*, THE BANKER, Nov. 1998, at 16 (estimating that international capital flows exceed trade flows by 60 to 1).

<sup>25</sup> The IRS is embroiled in a long-running effort to crack down on Americans evading U.S. taxes through use of undisclosed foreign bank accounts. For part of the saga, see Kathryn Keneally & Charles P. Rettig, *The End of an Era: The IRS Closes in on Offshore Bank Accounts*, J. TAX PRAC. & PROC., Apr.-May 2009, at 11.

activity pose challenging transfer pricing,<sup>26</sup> Subpart F,<sup>27</sup> sourcing,<sup>28</sup> foreign tax credit,<sup>29</sup> and other tax issues.<sup>30</sup> Often these issues involve disparities between U.S. and foreign tax regimes or conflicting interpretations of bilateral tax treaties.<sup>31</sup> The United States has responded to the challenges of cross-border tax issues through more aggressive use of IRS summonses,<sup>32</sup> information exchange provisions in tax treaties and agreements,<sup>33</sup> and an expanding array of Code provisions.<sup>34</sup>

As necessary as serious international enforcement is, one must recognize its costs. Because of distance, political sensitivities, and the uncertainties of where principal targets are located, overseas efforts are more time-consuming and expensive.<sup>35</sup> A major current initiative, the Foreign Account Tax Compliance Act (FATCA),<sup>36</sup> is consuming vast amounts of IRS resources.<sup>37</sup>

### 3. Increasing Non-Revenue Responsibilities

We think of the IRS as a revenue-raising agency, but that monocular image does not reflect current reality. A binocular view is more accurate. The IRS collects revenue, to be sure, but it also expends a substantial part of its energy, money, and human resources on administering a host of initiatives having no essential connection with its revenue functions.<sup>38</sup> For example:

The continual enactment of targeted tax provisions leaves the IRS with responsibility for the administration of policies aimed at the environment, conservation, green energy, manufacturing, innovation, education, saving, retirement, health care, child care, welfare, corporate governance, export promotion, charitable giving, governance of tax exempt organizations, and economic development, to name a few.<sup>39</sup>

<sup>26</sup> I.R.C. § 482.

<sup>27</sup> I.R.C. §§ 951-964.

<sup>28</sup> I.R.C. §§ 861-865.

<sup>29</sup> I.R.C. §§ 901-909.

<sup>30</sup> See, e.g., Yariv Brauner, *An International Tax Regime in Crystallization*, 56 TAX L. REV. 259 (2003); Diane M. Ring, *One Nation Among Many: Policy Implications of Cross-Border Arbitrage*, 44 B.C. L. REV. 79 (2002).

<sup>31</sup> See, e.g., S. Rep. 445, 100th Cong., 2d Sess. pt. XII H1, *Technical Corrections to the Tax Reform Act of 1986* (discussing the relationship between U.S. tax treaties and the Code).

<sup>32</sup> See, e.g., *United States v. Bank of Nova Scotia*, 691 F.2d 1384 (11th Cir. 1982), cert. denied, 462 U.S. 1119 (1983), further proceedings, 722 F.2d 657 (11th Cir. 1983), appeal after remand, 740 F.2d 817 (11th Cir. 1984), cert. denied, 469 U.S. 1106 (1985).

<sup>33</sup> For example, Article 26 of the U.S. Model Income Tax Treaty provides for exchange of information and administrative assistance between the IRS and the treaty partner's tax authority. The United States has tax treaties of varying degrees of coverage with approximately 70 other countries.

<sup>34</sup> See, e.g., I.R.C. §§ 982 (formal document requests), 6038A (information as to certain foreign-owned corporations) & 6038C (information with respect to foreign corporations engaged in U.S. business). For discussion of these and other devices, see JOHN A. TOWNSEND, LARRY A. CAMPAGNA, STEVE JOHNSON & SCOTT A. SCHUMACHER, *TAX CRIMES* 327-30 (2d ed. 2015).

<sup>35</sup> See, e.g., U.S. Dep't of State Circular, *Obtaining Evidence Abroad*, 739 PLI/LIT 1095, 1098 (2006).

<sup>36</sup> Pub. L. No. 111-147, 124 Stat. 71, 97 (codified at IRC §§ 1471 et seq.).

<sup>37</sup> See, e.g., Seven Commissioners Letter, *supra* note 14, at 3.

<sup>38</sup> See, e.g., Kristin E. Hickman, *Administering the Tax System We Have*, 63 DUKE L.J. 1717 (2014).

<sup>39</sup> Pamela F. Olson, *Woodworth Memorial Lecture: And Then Cnut Told Regan . . . Lessons from the Tax Reform Act of 1986*, 38 OHIO N.U. L. REV. 1, 12-13 (2011) (citations omitted); see also Lawrence B. Gibbs, *Loving v. IRS: Treasury's Authority to Regulate Tax Return Preparers*, TAX NOTES, Oct. 21, 2013, at 331, 334 ("One of the biggest changes in the Federal tax area in the last twenty-five years has been the

The IRS has been charged with vast additional burdens of rulemaking, information processing, and enforcement with respect to the Affordable Care Act (“ACA”), enacted in 2010.<sup>40</sup> This program “contains an extensive array of tax law changes that, absent added funding, will present budgetary challenges for the IRS in the coming years.”<sup>41</sup>

It is now more accurate than alarmist to warn that “Congress’s repeated utilization of the IRS to serve functions beyond its traditional revenue raising mission has reached a tipping point that threatens to undermine substantially the viability of the IRS’s primary mission as the nation’s tax collector.”<sup>42</sup>

#### 4. Cumulative Impact

Could the IRS meet its revenue-collection responsibilities without significantly enhanced funding? Probably yes—if it were able to shed its non-revenue functions. Could the IRS shoulder both its revenue duties and its currently assigned adventitious duties? There would be agency expertise, organization, and institutional culture concerns, but probably yes—if Congress were to greatly increase funding for the IRS.

The problem is the simultaneity and compounding effects of the three trends. According to former Commissioners, “these reductions in IRS appropriations are difficult to understand in light of the fact that, at the same time these reductions have occurred, the Congress repeatedly has passed major tax legislation to substantially increase the IRS workload.”<sup>43</sup> Commissioner Koskinen offered this example: “The disconnect between our funding levels and our responsibilities is illustrated by the fact that, just three days after cutting our budget by almost \$350 million, Congress passed legislation requiring the IRS to design and implement two new programs by [a designated date].”<sup>44</sup>

#### B. Consequences

The “terrible trifecta” described above sounds ominous, but is it really? What, if any, have been the particular, adverse repercussions of the current trends?

Seven former Commissioners of Internal Revenue have said that currently “the IRS is stretched to the breaking point to cope with tax enforcement challenges attributable to global and domestic changes that are impacting our tax system.”<sup>45</sup> The current Commissioner has warned that “now, we are at the point of having to make very critical

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increasing number of socio-economic spending programs that have been run through the Internal Revenue Code.”).

<sup>40</sup> Patient Protection and Affordable Care Act of 2010, Pub. L. No. 111-148, 124 Stat. 119 (2010) (codified as amended in scattered sections of the United States Code), *amended by* the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

<sup>41</sup> TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, IMPLEMENTATION OF FISCAL YEAR 2013 SEQUESTRATION BUDGET REDUCTIONS 5 (June 12, 2014); *see also* Letter from Representatives Jason Chaffetz, Jim Jordan & Mark Meadows to John Koskinen (Jan. 29, 2014) (on file with author); William Hoffman, *IRS May Miss 12 Million Taxpayer Calls in 2015*, TAX NOTES, June 16, 2014, at 1263, 1264 (according to John Dalrymple, IRS Deputy Commissioner for Services and Enforcement, the IRS anticipated receiving 11 million calls in 2015 from taxpayers confused by ACA provisions) (“This is complicated stuff. . . . [It] is complicated for us; it’s complicated for taxpayers.”).

<sup>42</sup> Kristin E. Hickman, *Pursuing a Single Mission (or Something Closer to It) for the IRS*, 7 COLUM. J. TAX L. 169, 173 (2016).

<sup>43</sup> Seven Commissioners Letter, *supra* note 14, at 3.

<sup>44</sup> Prepared remarks of John A. Koskinen, Commissioner, Internal Revenue Service, before the Tax Executives Inst. 65th Mid-Year Conference 4 (Washington, D.C.) (Mar. 24, 2015) (on file with author).

<sup>45</sup> *Id.*

performance tradeoffs”<sup>46</sup> and has stated, “I am deeply concerned about the ability of the IRS to continue to fulfill its mission if the agency lacks adequate funding.”<sup>47</sup> Another Treasury official echoed: “This reduced funding has directly led to deterioration in the ability of the IRS to conduct its mission . . . . A sustained deterioration in taxpayer services combined with reduced enforcement activity creates serious long-term risk for the U.S. tax system.”<sup>48</sup>

But, of course, “the sky is falling” rhetoric is central to the playbook of administrative agencies trying to defend or enhance their budgets. With how large a pinch of salt, then, should we take the above dire assessments?

Seven dimensions suggest that the Commissioners’ concerns should not be dismissed out of hand. They involve (1) formal guidance, (2) informal guidance, (3) enforcement, (4) workforce, (5) training, (6) technology, and (7) revenue.

### I. Formal Guidance

Treasury and the IRS provide critical guidance to taxpayers through both force-of-law regulations and a variety of guidance documents, such as revenue rulings, revenue procedures, notices, announcements, and private letter rulings.<sup>49</sup> Resource constraints in recent years have caused the IRS to delay or abandon important regulation projects<sup>50</sup> and to scale back substantially its issuance of revenue rulings<sup>51</sup> and private letter rulings.<sup>52</sup>

This contraction may well continue.

Relating to legal guidance, [the IRS has] had to limit what [it] can do on business tax issues, and guidance needed for specialized areas may suffer as a result . . . . [I]t should be clear to everyone that Chief Counsel’s Office will have to reprioritize projects as it continues to lose staff. [Chief Counsel is] down about 200 attorneys since 2009.<sup>53</sup>

<sup>46</sup> Written Testimony of Commissioner John A. Koskinen before Senate Finance Comm. on IRS Budget & Current Operations 3 (Feb. 3, 2015).

<sup>47</sup> Written Testimony of Commissioner John A. Koskinen before House Oversight and Government Reform Comm. on IRS Operations 1-2 (Mar. 26, 2014), <https://www.irs.gov/uac/Newsroom/Written-Testimony-of-Commissioner-Koskinen-before-the-House-Oversight-and-Government-Reform-Committee-on-IRS-Operations>.

<sup>48</sup> Letter from Anne Wall, Treas. Assistant Sec’y for Legislative Affairs, to Sen. Michael B. Enzi 2 (Aug. 19, 2015) (on file with author).

<sup>49</sup> For discussion of these and other types of IRS guidance, see STEVE JOHNSON, JEROME BORISON & SAMUEL ULLMAN, *CIVIL TAX PROCEDURE* ch. 1 (3d ed. forthcoming 2016).

<sup>50</sup> See, e.g., Alison Bennett, *Foreign Tax Credit Splitter Rules Slowed by Resource Constraints*, *IRS Official Says*, 33 TAX MGMT. WKLY. REP. 1696 (Dec. 11, 2014); Lydia Beyoud, *Staffing Declines in Passthroughs Division Likely to Result in Smaller Guidance Plan*, 33 TAX MGMT. WKLY. REP. 694 (May 16, 2014).

<sup>51</sup> IRS issued 636 revenue rulings in 1974, but only 50 in 2013. See Adler, *supra* note 22. The slack was partly taken up by issuance of more notices, although notices typically receive somewhat less exacting review. In the early 1980s, the IRS issued between 200 and 400 revenue rulings, but only 10 to 20 notices each year. Recently, the IRS has been issuing around 50 revenue rulings, but around 100 notices each year. The IRS considers notices to be on the same plane of authority as revenue rulings. Rev. Rul. 90-91, 1990-2 C.B. 262. Courts, however, seem to give notices less weight. See, e.g., *BMC Software, Inc. v. Comm’r*, 780 F.3d 669, 675-76 (5th Cir. 2015); *Costantino v. TRW, Inc.*, 13 F.3d 969, 980-81 (6th Cir. 1994) (both refusing to defer to IRS notices).

<sup>52</sup> The IRS issued about 14,000 private letter rulings in 1974 but fewer than 2600 in 2013. *Id.* See also Rev. Proc. 2003-48, 2003-2 C.B. 86 (adding “business purpose” to the list of topics on which the IRS will not rule).

<sup>53</sup> Koskinen, *supra* note 44, at 4-5.

## 2. *Informal Guidance*

According to Ken Armstrong, “the reduction in IRS toll-free phone lines, walk-in Taxpayer Assistance Centers . . . in all areas of taxpayer correspondence, and a decrease in its workforce along with reductions in training and information technology have significantly diminished service to taxpayers.”<sup>54</sup> In Fiscal Year 2013, only 61% of taxpayers seeking to reach an IRS customer service representative by telephone got through, down from 87% in Fiscal Year 2004.<sup>55</sup> By 2015, the figure dropped to under 50%.<sup>56</sup> Almost 20 million phone calls from taxpayers to the IRS went unanswered in 2013.<sup>57</sup>

Those that did get through had long wait times, [which] rose from 12.8 minutes in 2013 to 20.3 minutes during the first four months of 2014. . . .

Those expecting correspondence did not fare better. During 2013, the IRS was unable to process 53 percent of its adjustments correspondence within 45 days, its standard timeframe.<sup>58</sup>

The Practitioner Priority Service used to be a popular device by which taxpayers’ representatives could obtain information on an expedited basis. But “[t]he PPS level of service has been frustrating to say the least. Many [enrolled agents] report frequently receiving messages that due to high volume, IRS cannot accept their calls and others have waited hours for service.”<sup>59</sup>

As always, of course, one must ask whether the numbers tell the whole story. A standard ploy in the strategy of agencies conducting guerrilla warfare against budget cuts is to cut good—or at least visible and popular—programs rather than wasteful ones, that is, to pare muscle rather than fat, as a way of leveraging howls of constituent indignation into restoration of funding. One cannot say with certainty whether and to what extent the IRS has slashed taxpayer service rather than other activities as part of such a strategy, but the possibility exists.<sup>60</sup>

## 3. *Enforcement*

No one knows for sure how much tax that should have been paid goes uncollected. The IRS estimates that the annual tax gap—the difference between what taxpayers should have paid and what they paid timely—is \$450 billion. The largest component (\$376 billion) reflects taxpayers underreporting their liabilities on their returns. An additional

<sup>54</sup> Ken Armstrong, *Service Matters*, 33 TAX MGMT. WKLY. REP. 1646 (2014); *see also* National Taxpayer Advocate, *2013 Annual Report to Congress* (Dec. 31, 2013).

<sup>55</sup> Catherine Rampell, *Charting the Decline in Service at the IRS*, N.Y. TIMES (Jan. 11, 2014), [http://taxprof.typepad.com/taxprof\\_blog/2014/01/ny-times-2.html](http://taxprof.typepad.com/taxprof_blog/2014/01/ny-times-2.html) [<https://perma.cc/M22W-BED3>].

<sup>56</sup> Koskinen, *supra* note 44, at 3. During the 2015 filing season, “the IRS answered only 38 percent of calls and those taxpayers able to reach the IRS experienced average wait times of over 23 minutes.” Wall, *supra* note 19, at 2.

<sup>57</sup> National Treasury Employees Union, Press Release, June 17, 2014, at 2 (on file with author).

<sup>58</sup> *Id.*

<sup>59</sup> Letter from Lonnie Garry, President of Nat’l Ass’n of Enrolled Agents, to Commissioner John A. Koskinen, Sept. 18, 2014 (on file with author). The average wait was 32.5 minutes. NTEU Press Release, *supra* note 57, at 2.

<sup>60</sup> The IRS has told Congress that “the only way to address these issues [of the impact of budget cuts on the quality of taxpayer services] is for Congress to provide the IRS with the additional funding.” Wall, *supra* note 19, at 1. Well, maybe not. The IRS has considerable, though not unlimited, flexibility in how it allocates appropriated funds and splits funds among activities. *See* GOVERNMENT ACCOUNTABILITY OFFICE, *supra* note 11, at 5-6.

\$28 billion is based on taxpayers who are legally obligated to, but do not, file returns. The remaining \$46 billion consists of reported but unpaid tax liabilities.<sup>61</sup> In short, there are abundant targets for more robust tax enforcement.

Yet key enforcement activities have contracted, not expanded, in recent years. Overall, between 2010 and 2015, IRS enforcement dropped by 20%.<sup>62</sup> For example:

- As noted in Subpart I.A. above, information gathering and enforcement involving transnational activities are of great and growing importance. FATCA is a central strategy for reducing cross-border evasion of U.S. taxes. The IRS has enough resources to accept the tsunamis of forms and reports that FATCA requires—but perhaps not enough to actually read, process, and act on the information contained in the FATCA reports.<sup>63</sup>
- Similarly, to facilitate cross-border enforcement, the IRS has long stationed employees in key global commerce hubs, but, for budgetary reasons, the IRS has closed its offices in Beijing, London, Paris, and Frankfurt.<sup>64</sup>
- In 2014, the IRS performed 100,000 fewer examinations of individual taxpayers, dropping individual audit coverage rates to historic lows.<sup>65</sup>
- The Appeals Office is a critical part of the IRS because it resolves numerous cases that otherwise would have to be docketed for trial. Because of budget cuts, however, some cases now are handled by offices remote from the taxpayer’s residence, without face-to-face contact, and less expeditiously.<sup>66</sup>
- In Fiscal Year 2013, “[c]ollection activities initiated by the IRS, such as taxpayer liens, levies, and property seizures, declined by approximately 33 percent.”<sup>67</sup>

#### 4. Workforce

Like most organizations, the IRS’s biggest expense is compensation of its employees. This is hardly surprising. “In order to perform the Service’s critical functions, in the face of complex and constantly changing tax laws, a sufficient staff must be recruited and properly trained.”<sup>68</sup>

Yet the IRS has “been forced to significantly reduce the size of its workforce. . . . Between FY 2010 and the end of FY 2014, the number of IRS employees has been reduced

<sup>61</sup> TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, *supra* note 12, at 2 & n.3.

<sup>62</sup> *House Approves Broad Spending Plan with Cuts to IRS*, 33 TAX MGMT. WKLY. REP. 1695 (Dec. 11, 2014).

<sup>63</sup> Jennifer DePaul, *Koskinen Says Budget Cuts Affect FATCA Administration*, TAX NOTES, at 1408 (Mar. 31, 2014).

<sup>64</sup> IRS Statement, Jan. 14, 2015 (on file with author).

<sup>65</sup> Written Testimony of Commissioner John A. Koskinen, Internal Revenue Service, Before the House Ways and Means Comm., Subcomm. on Oversight, *The 2014 Filing Season and Improper Payments* (May 7, 2014) (on file with author).

<sup>66</sup> *See, e.g.*, Letter from Michael Hirschfeld, Chair of the American Bar Ass’n Section of Taxation, to Senators Tom Udall and Mike Johanns & Representatives Ander Crenshaw and Jose E. Serrano (July 21, 2014) (on file with author) (“The ability of taxpayers to resolve cases administratively has also been negatively affected by decreased funding”).

<sup>67</sup> TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, *supra* note 12, at 2.

<sup>68</sup> Hirschfeld, *supra* note 66, at 3.

by approximately 13,000 full-time positions, with about 9,500 coming from front-line enforcement personnel.”<sup>69</sup>

Demographic trends make these losses particularly difficult to absorb.

[They] come at a time when the IRS workforce is aging, with nearly 52% of IRS employees now over the age of 50 and 24% already eligible to retire. Three years from now, 38% of IRS employees will be eligible to retire. This loss of IRS knowledge and experience is alarming, particularly in light of the fact that, out of a present workforce of about 85,000 employees, the IRS has only about 3,400 employees under the age of 30 and only 384 employees under the age of 25 . . . .<sup>70</sup>

### 5. *Training*

Having a large workforce will not suffice (and indeed may create more problems than it solves) if employees lack relevant knowledge. Knowledge may come from experience or from training. Yet many of the IRS’s most senior personnel are choosing retirement,<sup>71</sup> and the IRS has suffered “dramatic curtailments in training, travel, office space, and outside contracts.”<sup>72</sup> This country’s tax laws have not become 85% less complicated.<sup>73</sup> Yet, between 2009 and 2014, the IRS’s training budget was slashed by 85%.<sup>74</sup>

### 6. *Technology*

Each year, the IRS processes around 145 million tax returns, issues over 100 million refunds,<sup>75</sup> makes hundreds of millions of assessments, and generates untold millions of audit letters, collection letters, notices, bills, and other correspondence. To operate effectively, the IRS needs efficient and reliable information systems.

However, as a result of its own poor performance as well as lean budgets,<sup>76</sup> the IRS is forced to rely on aging, outmoded IT systems that sometimes do not interface with each other.<sup>77</sup> Inadequate technology also imperils the IRS’s ability to effectively execute

<sup>69</sup> TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, *supra* note 12, at 2. The seven former Commissioners put this attrition at 15,000. *See* Seven Commissioners Letter, *supra* note 14, at 2. The workforce of the IRS’s Criminal Investigation Division has dropped to its lowest level in four decades. *See Exclusive: IRS Enforcement Agent Numbers Could Drop to Lowest Levels Since 1970s*, REUTERS (Aug 25, 2014), <http://finance.yahoo.com/news/exclusive-irs-enforcement-agent-numbers-111711058.html> [<https://perma.cc/YA2G-ZEMA>].

<sup>70</sup> Seven Commissioners Letter, *supra* note 14, at 2-3. John Dalrymple, IRS Deputy Commissioner for Services and Enforcement, described the ongoing “brain drain” of retiring IRS employees as “a real critical problem.” Quoted by Hoffman, *supra* note 41, at 1264; *see also* Duarte, *supra* note 23, at 63 (“[E]xperienced IRS staff, and especially managers, are in short supply.”).

<sup>71</sup> Hirschfeld, *supra* note 66, at 3.

<sup>72</sup> TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION, *supra* note 12.

<sup>73</sup> Indeed, “Congress almost annually over the last 25 years has passed legislation that has imposed additional burdens on IRS tax collection and administration.” Seven Commissioners Letter, *supra* note 14, at 4.

<sup>74</sup> Written Statement of Nina E. Olson, National Taxpayer Advocate, Hearing on Identity Theft-Related Tax Fraud, Before the House Comm. on Oversight and Government Reform, Subcomm. on Government Operations 4 (Aug. 2, 2013).

<sup>75</sup> Wall, *supra* note 19, at 2 (citing information from the National Taxpayer Advocate).

<sup>76</sup> *See* Armstrong, *supra* note 54 (“Throwing money at IT and staffing won’t solve the impending . . . administration burdens on the IRS unless it has direction.”).

<sup>77</sup> Wall, *supra* note 19, at 2; Duarte, *supra* note 23, at 63; *see also* Koskinen, *supra* note 44, at 4 ([The IRS is] “experiencing delays to critical IT projects, with very old technology running alongside more modern systems.”).

the non-revenue functions Congress has chosen to vest in the IRS. For example, “without proper technology and staffing, the [ACA] reporting and funding system is doomed to failure.”<sup>78</sup>

The threat is not just to the IRS. It potentially implicates the peace and financial security of most of the adult population of the United States: the Americans who deal with the IRS. Combatting tax-based identity theft and fraud is a major goal of the IRS.<sup>79</sup> In 2015, there were unauthorized attempts to access taxpayer information using the agency’s “Get Transcript” online application.<sup>80</sup> This was the most publicized incident but far from the only one. “[T]he IRS continues to experience about one million attempts each week to hack into its main information technology system. Although the IRS has so far successfully thwarted these attacks, [they emphasize] that the IRS taxpayer assistance and IRS information technology resources are severely underfunded.”<sup>81</sup>

### 7. Revenue

Viewed from the traditional perspective, raising revenue—the correct amount of revenue determined by Congress—is the central criterion on which IRS performance should be evaluated. The “perfect storm” intersection of trends described above has eroded the IRS’s ability to collect tax liabilities and threatens more damage in the future.

Supporters of the IRS find it ironic that Congress has reduced funding for the main federal agency that actually turns a profit. The rule-of-thumb statistic is “that for every \$1 invested in the IRS budget, it produces \$4 in enforcement revenue, which is a \$4-to-\$1 return on investment.”<sup>82</sup> Accordingly, the IRS estimates that, for 2014, “it would have returned to the Federal government over \$2 billion more in collections had we received the remaining \$500 million that our budget was cut as a result of the sequester.”<sup>83</sup>

The 4-to-1 ratio is neither a ceiling nor a floor. Everything depends upon the particular use to which the IRS will put additional funds, which may explain why the IRS sometimes offers different return-on-investment figures.<sup>84</sup> Some in Congress, however,

<sup>78</sup> Armstrong, *supra* note 54.

<sup>79</sup> See, e.g., Prepared Remarks of Commissioner of Internal Revenue John Koskinen, Before the National Press Club 7 (Apr. 2, 2014).

<sup>80</sup> See, e.g., Michael S. Schmidt, *Hacking of Tax Returns More Extensive than First Reported IRS Says*, N.Y. TIMES (Aug. 17, 2015), <http://www.nytimes.com/2015/08/18/us/politics/hacking-of-tax-returns-more-extensive-than-first-reported-irs-says.html> [<https://perma.cc/VVE5-7YTT>] (“[H]ackers had gained access to the tax returns of more than 300,000 people, a far higher number than the agency had reported previously.”).

<sup>81</sup> Seven Commissioners Letter, *supra* note 14, at 4.

<sup>82</sup> Written Testimony of Commissioner John A. Koskinen, Internal Revenue Service, Before the Subcommittee on Financial Services and General Government on the FY 2015 IRS Budget 11 (Apr. 7, 2014).

<sup>83</sup> *Id.* See also Written Testimony of John A. Koskinen, Commissioner, Internal Revenue Service, Before the House Ways and Means Comm., Subcomm. on Oversight, *The 2014 Filing Season and Improper Payments* 5 (May 7, 2014) (estimating a revenue loss of almost \$3 billion). The 4 to 1 ratio was derived by dividing the additional revenue brought in by the IRS as a result of enforcement activities by the IRS’s budget. Thus, in Fiscal Year 2013, IRS enforcement collected about \$53 billion from a budget of about \$12 billion, a rate of return somewhat over 4 to 1. See *id.* at 1-2.

<sup>84</sup> E.g., John Koskinen, *Commissioner’s Message on the Budget 2* (Feb. 2, 2015) (“For every dollar invested in these programs, there can be returns ranging from 6-to-1 and even up to 20-to-1 for some initiatives”); John Koskinen, quoted by Senator Ron Wyden, *Statement on Budget Challenges 2* (Jan. 14, 2015) (7 to 1).

have lost faith in these oft-repeated figures, and it may be the path of wisdom to eschew precise quantification.<sup>85</sup>

The other possible effect is more subtle and conjectural but—were it to come to fruition—would be even more grave. The IRS examines only a small percentage of returns filed, typically under one percent.<sup>86</sup> At such low coverage, it is essential that the returns taxpayers file bear some reasonable correlation to economic reality.<sup>87</sup>

What causes taxpayers to comply or not comply with the tax laws is a complex web of self-interest, social signal, and personal morality.<sup>88</sup> Even a gradual deterioration of compliance would be dangerous.<sup>89</sup> Each 1% drop in compliance costs the federal treasury about \$30 billion annually.<sup>90</sup>

The “tipping point” theory posits that a point can be reached at which taxpayer alienation from the system or taxpayer disdain for tax enforcement becomes so pervasive that a general culture of tax compliance could flip “virtually overnight” into a general culture of noncompliance.<sup>91</sup> Some fear we are at, or near, that point now.<sup>92</sup> I do not share that fear, but the magnitude of the stakes inspires caution. Commissioner Koskinen has warned that the budget-driven “erosion in audit coverage . . . is deeply worrisome . . . especially for a system like ours that depends on voluntary compliance.”<sup>93</sup>

## II. DOUBTING OBVIOUS SOLUTIONS

In an increasingly complicated and thoroughly politicized society, few things are more treasured by Americans than simplistic explanations that allow us to keep, indeed fortify, our preconceptions. The woes of the IRS have been on the radar screen of public discourse long enough that two camps have formed as to what the appropriate solution to them might be.

Committed members of both camps may have the same reaction—although for quite different reasons. The common reaction may be “there’s no need to overthink this. There’s a pretty easy answer to the perfect storm problem.” For those in the anti-IRS camp,

<sup>85</sup> See, e.g., Hirschfeld, *supra* note 66, at 3 (stating simply that IRS enforcement produces “a substantial increase” in collections and that reduced funding may yield “significantly lower tax collections”); see also National Taxpayer Advocate, *2013 Annual Report to Congress*, Executive Summary 21 (Dec. 31, 2013).

<sup>86</sup> In Fiscal Year 2014, for example, the IRS examined seven tenths of one percent of all returns filed. *IRS Data Book* tbl. 9a (2014).

<sup>87</sup> Such “self-assessment” is the bedrock of our system of taxation. See, e.g., *United States v. Rodgers*, 461 U.S. 677, 683 (1983); IRS Proc. Reg. § 601.103(a) (2009).

<sup>88</sup> The literature on tax compliance is immense. See, e.g., Robert Boylan, Richard J. Cebula, Maggie Foley & Douglass IZard, *Implications of Recent Federal Personal Income Tax Increases for Income Tax Evasion, Tax Revenues, and Budget Deficits*, 6 WM. & MARY POL’Y REV. 1 (2014); Sarah B. Lawsky, *Modeling Uncertainty in Tax Law*, 65 STAN. L. REV. 241 (2013); Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO ST. L. J. 1453 (2003); J. Manhire, *Toward a Perspective-Dependent Theory of Audit Probability for Tax Compliance Models*, 33 VA. TAX REV. 629 (2014).

<sup>89</sup> See, e.g., Cohen, *supra* note 1, at 117 (“The audit rate in 1964-68 was about 4.5 to 5 percent, compliance was over 90 percent; today the audit rate is less than one percent and compliance is only about 80 percent. Think there is a correlation? I do.”).

<sup>90</sup> John Koskinen, quoted by William Hoffman, *Koskinen Warns of House IRS Budget Impact in 2015*, TAX NOTES, at 919 (Aug. 25, 2014).

<sup>91</sup> See Eric Kroh, *U.S. Seen as in Danger of Tumbling Over “Compliance Cliff”*, TAX NOTES, at 909 (Aug. 25, 2014) (quoting Richard Lavoie).

<sup>92</sup> See Jeremy Scott, *The Precarious State of Voluntary Compliance*, TAX NOTES, at 893 (Aug. 25, 2014).

<sup>93</sup> Koskinen, *supra* note 44, at 5.

the easy answer might be “despite budget cuts, the IRS still has a big budget. It just has to use it better by prioritizing and becoming more efficient.” For those in the pro-IRS camp, the easy answer might be “just open the purse strings. Congress should give the IRS the budget it needs.”

There is a kernel of truth in both of these views. Neither simplistic approach can provide the full answer, however. The anti-IRS agenda lacks flexibility: most easy efficiencies already have been wrung out of the system. The pro-IRS agenda could perpetuate bad behavior: the agency’s recent woes reflect serious management failures, as well as budgetary and workload pressures. To open wide the appropriations spigot would remove pressures and incentives for constructive change within the agency. This is not to suggest that the IRS be put on a budgetary starvation diet, but rather to suggest that the “just throw more money at it” approach which is often preferred in this country would be shortsighted in this context.

#### A. “Just Become More Efficient”

Recent budget and workload stresses have caused the IRS to improve its efficiency in a number of ways.<sup>94</sup> No doubt, some additional opportunities for efficiencies exist, but there are practical limits. No organization of 85,000 (or even fewer) participants—whether public or private—has yet or ever will achieve perfect efficiency. It flouts experience to demand that which has never been attained. The seven former commissioners observed:

Some have argued that the IRS can solve these problems by simply becoming more efficient. This argument ignores the reality that the IRS is already, by far, the most efficient tax collection agency among large countries in the world. . . . [T]he amount the IRS spends to collect a dollar in taxes is approximately half the average amount spent by all OECD countries. Germany, France, England, Canada and Australia all spend as much as two or three times the amount the IRS does to collect a dollar of revenue.<sup>95</sup>

#### B. “Just Give the IRS More Money”

In light of the harms described in Part I of this article one might, at first glance, be deeply puzzled as to why Congress has been decreasing the IRS’s budget. This behavior could seem extremely short-sighted, the government “cutting off its nose to spite its face.” Writing to the chairs and ranking members of Congress’s principal tax-writing committees, seven former commissioners of the IRS remarked with evident exasperation:

[W]e fail to understand how it makes any logical sense to continue to reduce, rather than increase, the IRS budget . . . . [W]e do not understand why anyone with present and projected debts and annual losses as large as

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<sup>94</sup> “The IRS does need to be as efficient as possible and we now saved over \$200 million a year as a result of efficiencies instituted over the past few years.” Koskinen, *supra* note 44, at 4. The commissioner added: “But we’re now at a point where further cuts may make us seem more efficient, but we’re actually going to be a lot less effective.” *Id.* For details as to recent efficiencies, see Written Testimony of John A. Koskinen, Commissioner, Internal Revenue Service, Before the Senate Finance Committee, *IRS Budget and Current Operations* 3 (Feb. 3, 2015) (describing real estate management, printing, postage, and other reforms).

<sup>95</sup> Seven Commissioners Letter, *supra* note 14, at 5 (citing the 2013 biannual comparative analysis of tax administration by the Organization for Economic Cooperation and Development); *see also* John Koskinen, quoted by William Hoffman, *Koskinen Warns of House IRS Budget’s Impact in 2015*, TAX NOTES, at 919-20 (Aug. 25, 2014) (“We’re beyond the stage where we can pretend we can keep doing the same amount of work with less resources”).

those of the United States would refuse to pay for telephone assistance to people trying to fulfill their tax obligations, would turn their back on \$8 billion annually in additional revenue, or would fail to make an investment that offers a return equal to at least four times the amount invested. For those reasons, we respectfully call upon each of you to support and work to accomplish the passage of [significantly enhanced] IRS appropriations.<sup>96</sup>

Anyone who cares about good tax administration will understand the former commissioners' view, but there is another side of the story. The IRS has had a string of embarrassing, damaging, and highly publicized failures in recent years attributable to its institutional culture, management structure, and incompetence, not just to inadequate resources. It is at least arguable that Congress should use its "power of the purse" to induce bureaucratic reforms within the IRS. These points are developed below.

In 2013, controversy erupted about alleged IRS targeting of conservative and libertarian groups for special, burdensome review of their applications for tax-exempt status.<sup>97</sup> Accusations, apologies, firings, and investigations occupied much of the news cycles for years thereafter.<sup>98</sup> Criminal charges have not been brought. Whether overt or subtle political influences led to "targeting" of these groups is beyond the possibility of conclusive proof or disproof.

But our interest should go deeper. Assume no criminality or partisan motivation of any kind. We are still left with appalling incompetence by the IRS, both in the training and supervision that caused poor handling of the applications and especially in the inept or deceptive nature of the IRS responses to the investigations.<sup>99</sup>

Responsible persons on both sides of the political aisle accept this. Senator Orrin Hatch, chair of the Senate of Finance Committee, finds in the scandal "gross mismanagement at the highest levels of the IRS."<sup>100</sup> Senator Ron Wyden, ranking member of that committee, concurred: "[T]he two of us [Senators Hatch and Wyden] certainly agree that there is evidence of vast bureaucratic bumbling at the IRS."<sup>101</sup>

As damaging as that saga was, it has had company. For example, in any organization of size, some employees will violate the rules or even break the law. The IRS cannot fairly be criticized for human failings of its employees. It can, however, properly be taken to task for failing to properly discipline miscreant employees. Yet, "[i]n recent years, the IRS has paid millions of dollars in bonuses and given tens of thousands of paid vacation hours to employees with recently substantiated conduct issues and disciplinary actions, including bonuses to 1,100 employees owing back taxes."<sup>102</sup> In addition, the IRS has rehired hundreds of seasonal employees despite their prior misconduct, including

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<sup>96</sup> Seven Commissioners Letter, *supra* note 14, at 5-6.

<sup>97</sup> See I.R.C. § 501(c)(4).

<sup>98</sup> For detailed discussion of the controversy, see Leandra Lederman, *IRS Reform: Politics as Usual?*, 7 COLUM. J. TAX L. 36 (2016).

<sup>99</sup> "The agency's performance during the Tea Party scandal has been defensive, dilatory, and less than fully honest." Joseph J. Thorndike, *Stop Blaming the IRS for Problems It Didn't Create*, TAX NOTES, at 115 (July 14, 2014).

<sup>100</sup> Quoted in Committee Press Release, *Finance Committee Releases Bipartisan IRS Report 2* (Aug. 5, 2015) (on file with author).

<sup>101</sup> Wyden Floor Statement on Finance Committee Investigation of IRS Handling of Applications for Tax-Exempt Status, at 2 (Aug. 5, 2015) (on file with author).

<sup>102</sup> Letter from Senator Orrin Hatch to John Koskinen (Jan. 29, 2015) (on file with author).

willfully failing to file their own returns, gaining unauthorized access to taxpayer information, falsifying official forms, and misusing IRS property.<sup>103</sup>

Other IRS failures have included:

- Sending incorrect information to 800,000 taxpayers as to ACA,<sup>104</sup>
- Multiple examples of waste in IRS conferences and training programs,<sup>105</sup>
- Paying millions to contractors who have failed to pay large tax debts they owe to the federal government,<sup>106</sup> and
- Failing to effectively monitor claims for deductions and credits in widely abused programs.<sup>107</sup>

The IRS sometimes is criticized unjustly, but “[i]n recent years, its list of failures and transgressions is long and serious.”<sup>108</sup> Commissioner Koskinen acknowledged that “there has been a loss of confidence among taxpayers and particularly within Congress in regard to the way we manage operations.”<sup>109</sup>

When an agency performs badly and the Administration fails to impose the appropriate corrections, the most important tool available to Congress is the power of the purse. It was in the exercise of that constitutional authority<sup>110</sup> that Congress says it acted to rein in IRS abuses.<sup>111</sup>

One may fairly ask whether Congress’ parsimony was proportional to the IRS’s derelictions. The harms described in Part I may involve too much pain for too little gain.

<sup>103</sup> Treasury Inspector General for Tax Administration, *Additional Consideration of Prior Conduct and Performance Issues is Needed When Hiring Former Employees* (Feb. 5, 2015).

<sup>104</sup> See, e.g., Peter Sullivan & Sarah Ferris, *Feds Sent Incorrect Tax Information to People on ObamaCare*, THE HILL (Feb. 20, 2015), <http://thehill.com/policy/healthcare/233315-incorrect-tax-information-sent-to-800000-people-on-obamacare> [<https://perma.cc/DA3B-PJHJ>].

<sup>105</sup> See, e.g., Prepared Remarks of Danny Werfel, Principal Deputy Commissioner, Before the 2013 IRS Nationwide Tax Forum, at 4 (July 30, 2013) (on file with author).

<sup>106</sup> See, e.g., Stephen Dinan, *IRS Breaking Federal Law in Paying Contracts to Tax Cheats: Audit*, WASH. TIMES (June 24, 2015), <http://www.washingtontimes.com/news/2015/jun/24/irs-breaks-federal-law-paying-contracts-tax-cheats/?page=all> [<https://perma.cc/8EB5-7JTZ>].

<sup>107</sup> See, e.g., Hadley Malcolm, *IRS Flubs \$5.6B in Tax Credits*, USA TODAY, May 6, 2015, at 5B (reporting a Treasury Inspector General for Tax Administration study finding that the IRS issued more than \$5.6 billion in faulty education tax credits to about 3.6 million taxpayers in 2013).

<sup>108</sup> Thorndike, *supra* note 99, at 115; see also Dave Camp, former Chair of the House Ways and Means Committee, quoted by William Hoffman, *Koskinen Achieving Mixed Results So Far*, TAX NOTES, at 233 (July 21, 2014) (“Since my time in Congress, I have never seen an IRS so broken.”)

<sup>109</sup> Written Testimony of John A. Koskinen, Commissioner, Internal Revenue Service, Before the House Oversight and Government Reform Comm. on IRS Operations 2 (Mar. 26, 2014).

<sup>110</sup> See U.S. CONST. art. I, § 8, cl. 1 & § 9, cl. 7; see, e.g., *Helvering v. Davis*, 301 U.S. 619, 908 (1937).

<sup>111</sup> [T]he IRS has exhibited a litany of questionable practices and expenses over the past five years . . . .

[A]fter five years of budget cuts or freezes, I would hope that the IRS has turned a new leaf . . . .

. . . .

We deliberately lowered the IRS’ funding to a level to make them think twice about what they were doing and why.

Ander Crenshaw, Chair, Subcomm. on Financial Services and General Government, House Comm. on Appropriations, Opening Statement as Prepared, *Oversight Hearing—Internal Revenue Service 2* (Feb. 25, 2015).

That question is hard to answer. The principle, however, stands. Control of the budget is the traditional and most effective means available to Congress to punish agency failures and to encourage improvements. In light of the IRS's dubious recent performance, surrender of this tool would be unwise. That being so, "just give the IRS whatever it wants or needs" may be an obvious, but not necessarily a desirable, response to the current crisis.

### III. OTHER THEORETICALLY AVAILABLE SOLUTIONS

We saw in Part II that two "obvious" solutions—increased IRS efficiency and appropriating more money without fixing the IRS's bureaucratic problems—are not by themselves reliable pathways out of the current morass. In this Part III, we consider other approaches which may, as substitutes for or complements to the obvious approaches, move our tax system forward.

One could float armadas on the oceans of ink that have been spent describing the countless proposals that have been offered to improve the substantive and procedural rules of federal taxation.<sup>112</sup> Identifying, explaining, and evaluating the numerous suggestions (meritorious and not) would be an encyclopedic effort, well beyond the limits of this article. Here, it will suffice to note the families of alternatives and sketch the approaches that, by design or happy accident, might ease the current crisis.

The families of proposals discussed below are (1) radical tax revision, that is, replacing some or all existing federal taxes with other taxes, (2) eliminating or modifying features of existing taxes, (3) moving non-revenue functions outside the IRS, (4) harmonizing U.S. and foreign tax rules, (5) revamping tax lawmaking, (6) changing incentives, and (7) relying more heavily on technology.

#### A. Radical Tax Revision

Wholesale or partial replacement of the income tax or other current major federal taxes is a perennial topic in tax discourse. Interest in the topic crests and falls in waves, but the sea is never wholly still. Most suggested alternatives are one or another version of a consumption tax, such as the value-added tax, progressive consumption tax, and some versions of the so-called flat tax.<sup>113</sup>

It is hard to become extremely excited about the prospects for fundamental reform. Anyone experienced in taxation has heard many times "this time, it's really going to happen!" But it almost never does, making it hard to join the parade when the next banner of supposed inevitability sallies past.<sup>114</sup>

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<sup>112</sup> Some of the many possibilities are discussed in Jonathan Barry Forman & Roberta F. Mann, *Making the Internal Revenue Service Work*, 17 FLA. TAX REV. 725 (2015) (enumerating both changes that would require congressional action and administrative actions that could be taken by either Treasury or the IRS without legislation, with the goal of designing a tax system administrable at even modest levels of funding); Steve R. Johnson, *Reforming Federal Tax Litigation: An Agenda*, 41 FLA. ST. U. L. REV. 205 (2013) (detailing proposed changes as to tax trial and appellate structure and doctrine).

<sup>113</sup> For a discussion of several such alternatives, see Alan Viard, *Fundamental Tax Reform: A Comparison of Three Options*, TAXPROF BLOG (Jan. 25, 2016) [http://taxprof.typepad.com/taxprof\\_blog/2016/02/viard-presents-fundamental-tax-reform-a-comparison-of-three-options-today-at-georgetown.html](http://taxprof.typepad.com/taxprof_blog/2016/02/viard-presents-fundamental-tax-reform-a-comparison-of-three-options-today-at-georgetown.html) [<https://perma.cc/59TH-B9JZ>].

<sup>114</sup> From a distance, tax reform reflects the shimmering frontier of American economic policy . . . .

Up close, however, the picture dims. For reasons both economic and political, the idea of a fundamental overhaul that closes loopholes, lowers rates and simplifies the tax code faces a deeply uncertain future regardless of who controls the White House and Congress in 2017.

The issues typically debated with respect to replacements for the income tax involve progressivity, revenue-raising capacity, and effect on economic growth. Presumably, the ultimate decision as to whether to embrace replacements will turn on those considerations more than on their effect on administrability. However, administrability is part of the debate.<sup>115</sup>

Would a consumption-based partial or complete alternative to the income tax ameliorate the current crisis? In the short term, no. The enormous transitional challenges of moving from one system to another would exacerbate immediate stresses.<sup>116</sup> The long-term effect would depend on design choices. Our income tax does entail mind-numbing complexity. In part, this is because “a neutral, scientific measure of taxable income is a mirage. . . . [T]he income tax structure cannot be discovered, but must be constructed; it is the final result of a multitude of debatable judgments.”<sup>117</sup>

But that would also be true of any alternative system. The choices made can produce complexity regardless of the starting point. The current income tax is complicated in part because of so called “tax expenditures,” in effect, subsidies to various persons or activities necessitated by defining ability to pay.<sup>118</sup> Similar pressures would likely find outlets in any replacement system.<sup>119</sup> For example, persons and activities could be favored in a consumption tax through elaborate exemptions, different rates of tax, timing rules, and rebate or credit mechanisms.

The current income tax also is complicated by the engrafting of consumption-based features, such as deferring the imposition of tax on retirement savings.<sup>120</sup> Indeed, what we call our “income” tax actually is a mix of income-based and consumption-based provisions in roughly equal measure.<sup>121</sup> If an income tax can be hybridized, so can a consumption tax. It all depends on design details, which can change over time.<sup>122</sup> Nothing guarantees that a fundamental alternative to the income tax would ultimately be easier to administer than the present system.

## B. Feature Modification

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John Harwood, *Despite Pledges, Tax Reform Remains an Elusive Goal*, N.Y. TIMES (Feb. 2, 2016), <http://www.nytimes.com/2016/02/03/us/politics/despite-pledges-tax-reform-remains-an-elusive-goal.html> [<https://perma.cc/3YU9-Y346>].

<sup>115</sup> For example, Michael Graetz has argued for partial replacement of the income tax by a value added tax in order to eliminate the need for low- and middle-income taxpayers to prepare, and for the IRS to process, 100 million tax returns each year. MICHAEL J. GRAETZ, *100 MILLION UNNECESSARY RETURNS: A SIMPLE, FAIR AND COMPETITIVE TAX PLAN FOR THE UNITED STATES* (2008).

<sup>116</sup> See, e.g., Cohen, *supra* note 1, at 124 (noting “the god-awful task of how to move from the old system to the new”); Viard, *supra* note 113, at 33-45.

<sup>117</sup> Boris I. Bittker, *A “Comprehensive Tax Base” as a Goal of Income Tax Reform*, 80 HARV. L. REV. 925, 925, 985 (1967).

<sup>118</sup> See generally Douglas A. Kahn, *A Proposed Replacement of the Tax Expenditures Concept and a Different Perspective on Accelerated Depreciation*, 41 FLA. ST. U. L. REV. 143 (2013). Approximately one quarter of the spending of the federal government consists of tax expenditures. National Taxpayer Advocate, *2 Annual Rep. to Congress*, 2010, at 101-04 (Dec. 31, 2010). They exceed \$1 trillion a year. Nina E. Olson, *More than a “Mere” Prepare: Loving and Return Preparation*, TAX NOTES, at 767 (May 2, 2013).

<sup>119</sup> See, e.g., Cohen, *supra* note 1, at 118, 122.

<sup>120</sup> See, e.g., I.R.C. §§ 219, 401-420.

<sup>121</sup> See, e.g., William D. Andrews, *A Consumption-Type or Cash Flow Personal Income Tax*, 87 HARV. L. REV. 1113, 1117 (1974); Lawrence A. Zelenak, *Will the Federal Income Tax Have a Bicentennial?*, 41 FLA. ST. U. L. REV. 275, 275 (2013).

<sup>122</sup> Similarly, were Congress to enact a “flat” tax, one wonders how long it would remain flat.

Simplifying tax burdens on the IRS might be too costly if doing so seriously eroded other important tax values. However, numerous proposed changes to aspects of our current tax system would arguably improve the substance of the law as well as facilitate administration. Here are some candidates.

### 1. *Reduce the Number of Pass-Through Regimes*

So-called C corporations are separate taxpayers from their shareholders,<sup>123</sup> creating the possibility of double taxation of corporate profits paid out to shareholders as dividends. This can be avoided if the entity is formed instead as an S corporation or as a partnership. Under Subchapters S and K of the Code, S corporations and partnerships generally do not themselves pay tax on their profits but instead pass the tax through to the shareholders or partners.<sup>124</sup>

Why do we need two pass-through regimes? There are situations in which S corporations have advantages partnerships do not, and there are other situations in which partnerships (including multi-member limited liability companies, which are usually taxed as partnerships) have advantages over S corporations.<sup>125</sup> Thus, eliminating one or the other pass-through form (or melding the two forms) would be unpopular with the politically potent small business sector.

Nonetheless, one may well ask whether the extra flexibility is important enough to saddle the tax system with considerable costs in terms of administrability. Subchapter K is hideously complex, indeed is often beyond the capacity of taxpayers to understand and of the IRS to enforce.<sup>126</sup> For that reason, I would abolish Subchapter K (in the main) and keep Subchapter S.<sup>127</sup>

Some others would make the opposite choice—abolishing Subchapter S and retaining Subchapter K.<sup>128</sup> The absence of consensus is one factor propping up the current regime of two pass-through systems. Whichever approach were taken, the tax system would be improved by paring the number of pass-through regimes.

### 2. *Eliminate the Ordinary Income-Capital Gains Distinction*

For individual taxpayers, long-term capital gains are usually treated favorably compared to ordinary income.<sup>129</sup> For all taxpayers, capital losses are usually treated unfavorably compared to ordinary losses.<sup>130</sup> The advantages and disadvantages of treating capital gains and losses differently from ordinary gains and losses have been debated for

<sup>123</sup> See I.R.C. § 11.

<sup>124</sup> I.R.C. §§ 701 (partnerships), 1363(a) (S corporations).

<sup>125</sup> The choice-of-entity literature is vast. See, e.g., John W. Lee, *Choice of Small Business Tax Entity: Facts and Fictions*, 87 TAX NOTES 417 (2000).

<sup>126</sup> The distressingly complex and confusing nature of the provisions of Subchapter K present a formidable obstacle to the comprehension of these provisions without the expenditure of a disproportionate amount of time and effort even by one who is sophisticated in tax matters with many years of experience in the tax field.

Foxman v. Comm’r, 41 T.C. 535, 551 n.9 (1964), *aff’d*, 352 F.2d 466 (3d Cir. 1965). In the half century since the Tax Court penned this gloomy assessment, Subchapter K has become more, not less, impenetrable.

<sup>127</sup> See Steve R. Johnson, *The E.L. Wiegand Lecture: Administrability-Based Tax Simplifications*, 4 NEV. L.J. 573, 589-96 (2004).

<sup>128</sup> See, e.g., Walter D. Schwidetzky, *Integrating Subchapters K and S—Just Do It*, 62 TAX LAW 749 (2009).

<sup>129</sup> Compare I.R.C. § 1(h), with I.R.C. § 1(a)-(d).

<sup>130</sup> See I.R.C. §§ 1211-12.

generations,<sup>131</sup> and different judgments have been made at different times. The distinction did not exist in our tax law until 1921. In 1986, the distinction was repealed but was reinstated a few years later. At other times, the requisite holding period for long-term status, the size of the differential, and limiting rules all have varied.<sup>132</sup> My own preference—a minority view<sup>133</sup>—would be to abolish the differential.

Capital gains policy is determined principally by considerations other than administrability. But it is worth noting that, were we ever to bury the distinction and not later exhume it, the burdens on the IRS would be greatly eased. The Code is festooned with provisions that exist only to keep in some state of repair the fence between ordinary and capital.<sup>134</sup> These sections require regulations, revenue rulings, private letter rulings, audits, and litigation. Abolition of the distinction would be a major move in obviating the current crisis.

### 3. *Abolish the Accumulated Earnings Tax*

The accumulated earning tax (AET) imposes a penalty tax on corporations that accumulate profits beyond the reasonable needs of the business instead of paying them out as dividends.<sup>135</sup> Determining what constitutes such reasonable needs requires extensive factual inquiry. At the end of the day, the IRS often loses because (1) the taxpayers have superior access to the facts and (2) courts are often reluctant to second-guess the business judgment of the taxpayer.<sup>136</sup>

As a result, it is likely that, on net, the IRS loses money when it tries to enforce the AET, at least when opportunity costs are taken into consideration. The IRS often invests hundreds of agent hours in AET examinations, appeals, and litigation, yet recovers little or nothing.

Relevant statistics may not exist and, if they do, have not been publicly released. It is likely, however, that the IRS's assumed "\$4 of extra tax collected for every \$1 of extra IRS budget" return on investment<sup>137</sup> is not achieved in AET examinations. Instead, the IRS should invest its time in other audit areas where that return on investment can be achieved. The AET wastes the time of the IRS, and because of opportunity costs, it hurts the federal fisc. Therefore, the AET should be abolished.<sup>138</sup>

### 4. *Revise Treatment of Tax-Exempt Entities*

Certain organizations are generally exempt from the federal income tax.<sup>139</sup> "Originally, only two types of organizations—charities and fraternal benefit societies—were exempt . . . Today, there are more than 29 different types of tax-exempt entities in section 501(c) alone and by some counts more than 70 in all."<sup>140</sup>

<sup>131</sup> See, e.g., WILLIAM D. POPKIN, INTRODUCTION TO TAXATION 45-49 (5th ed. 2008).

<sup>132</sup> For this history in brief, see *id.* at 46-47.

<sup>133</sup> But I have some illustrious company. See, e.g., Daniel Halperin, *Commentary: A Capital Gains Preference Is Not EVEN a Second-Best Solution*, 84 TAX L. REV. 381 (1993); Edward J. McCaffery, *The Holy Grail of Tax Simplification*, 1990 WIS. L. REV. 1267, 1295-95; Joseph A. Snoe, *Tax Simplification and Fairness: Four Proposals for Fundamental Tax Reform*, 60 ALB. L. REV. 61, 66-85 (1996).

<sup>134</sup> Among scores, if not hundreds, of examples, see I.R.C. §§ 1211-1259.

<sup>135</sup> I.R.C. §§ 531-537.

<sup>136</sup> See, e.g., *Welch v. Helvering*, 290 U.S. 111, 113 (1933).

<sup>137</sup> See *supra* text accompanying notes 83-86.

<sup>138</sup> For a more detailed discussion, see Johnson, *supra* note 127, at 603-8.

<sup>139</sup> See I.R.C. §§ 501-513.

<sup>140</sup> David S. Miller, *Reforming the Taxation of Exempt Organizations and Their Patrons*, 67 TAX LAW. 451, 451 (2014).

The area is huge, and policing it places heavy burdens on the IRS.<sup>141</sup> Yet the area remains a trouble spot in tax administration. The very size of the enterprise is daunting; key definitions sometimes are vague;<sup>142</sup> and there are recurring tensions between enforcement and other important values, such as privacy, free expression of ideas and of religion, and facilitation of socially useful work.<sup>143</sup>

Befitting the importance of the issues, a large literature has arisen. Numerous proposals—some complementary, some not—have been offered, including narrowing the categories of exemption, less rigorous oversight, more rigorous oversight, and increasing the transparency of IRS regulation of the area.<sup>144</sup> Where the needle stops in reform of this area will have significant implications for the amelioration or exacerbation of the current crisis.

### 5. Other Proposals

Numerous other simplification proposals are advanced on a frequent basis. Helpful sources include the following:

- Academic commentary,<sup>145</sup>
- “Blue ribbon” commission reports,<sup>146</sup>
- Bar reports,<sup>147</sup>
- Accounting society reports,<sup>148</sup>
- The annual reports to Congress by the National Taxpayer Advocate,
- The so-called Greenbooks issued by the Treasury explaining tax changes in the Administration’s annual budget proposals,<sup>149</sup>

<sup>141</sup> In 2013, there were nearly 1.5 million organizations recognized under § 501(c), and the IRS devoted 842 full-time equivalent employees to the area. Lloyd Hitoshi Mayer, “*The Better Part of Valour Is Discretion*”: *Should the IRS Change or Surrender Its Oversight of Tax-Exempt Organizations?*, 7 COLUM. J. TAX L. 80, 84, 87 (2016).

<sup>142</sup> See, e.g., *ABA Retirement Funds v. United States*, 759 F.3d 718, 721 (7th Cir. 2014).

<sup>143</sup> The scandal involving IRS review of § 501(c)(4) applications from conservative-leaning groups, see *supra* text accompanying notes 97-101, reflects the sensitivity of these trade-offs.

<sup>144</sup> See, e.g., Roger Colinvaux, *Political Activity and Tax Exemption: A Gordian Knot*, 34 VA. TAX REV. 1 (2014); Mayer, *supra* note 141; Miller, *supra* note 140; Donald B. Tobin, *The Internal Revenue Service and a Crisis of Confidence: A New Regulatory Approach for a New Era*, 16 FLA. TAX REV. 429 (2014); George K. Yin, *Saving the IRS*, 2014 TAX NOTES TODAY 87-5 (May 6, 2014).

<sup>145</sup> See, e.g., Joseph M. Dodge, *Some Income Tax Simplification Proposals*, 41 FLA. ST. U. L. REV. 71 (2013) (advancing over 50 suggestions).

<sup>146</sup> See Report of the President’s Advisory Panel on Federal Tax Reform, *Simple, Fair and Pro-Growth: Proposals to Fix America’s Tax System* (Nov. 2005); Report of the National Commission on Fiscal Responsibility and Reform, *The Moment of Truth* (Dec. 1, 2010). Nothing came of these reports. Perhaps this is unsurprising. Commissions usually are for kicking the can down the road, not for solving problems. See, e.g., Cohen, *supra* note 1, at 118 (“When a problem is too difficult to solve, punt to a commission”).

<sup>147</sup> The American Bar Association Section of Tax, New York State Bar Tax Section, and other tax professional organizations and individuals submit numerous proposals to Congress, the Treasury, and the IRS. The government submissions of the ABA Tax Section are available at <http://www.americanbar.org/groups/taxation/policy.html> [<https://perma.cc/M73R-K3ML>].

<sup>148</sup> See, e.g., American Inst. of Certified Public Accountants Press Release, *AICPA Sends Tax Reform Suggestions Concerning Individuals to Senate Finance Committee Working Group* (Mar. 19, 2015) (on file with author).

<sup>149</sup> See, e.g., Department of the Treasury, *General Explanations of the Administration’s Fiscal Year 2017 Revenue Proposals* (2016).

- Occasional study reports by the President, Treasury, and IRS,<sup>150</sup> and
- Congressional reports.<sup>151</sup>

### C. Moving Non-Revenue Functions Outside IRS

Subpart I.A.3. above noted that one aspect of the “terrible trifecta” is the imposition on the IRS of the burdens of administering legions of initiatives that, although lodged in the Code, have no essential connection with revenue collection.

A direct response would be to remove these initiatives from the purview of the IRS, lodging them instead in agencies more natural to the programs in question. This may not always be the right course. For instance, the Earned Income Tax Credit (“EITC”)<sup>152</sup> is one of the federal government’s largest anti-poverty programs.<sup>153</sup> Because it is directed at the working poor, who have received wages and have paid taxes, it may be that the easiest way to administer the EITC is through tax returns, putting the program in the IRS’s court.

Nonetheless, the EITC is problematic from an administrative standpoint. Because of the complexity of the EITC, there is a high error rate, including innocent error and outright fraud. The IRS estimates that 24% of all EITC payments are made in error, resulting in improper payments of between \$124 billion and \$148 billion between Fiscal Year 2003 and 2013.<sup>154</sup> The Code may be the best home for the EITC, but it is not a good home.

The case for lodging other non-revenue initiatives in the Code may be weaker. As noted in Subpart I.A.3., the ACA is creating immense strains on the IRS.<sup>155</sup> There is no programmatic logic under which the ACA is naturally linked to the Code. The shared responsibility payment<sup>156</sup> could have been structured as a penalty outside the Code.<sup>157</sup> As an alternative to fully shifting some non-revenue functions to other agencies, in some instances, program administration might be improved by more cooperative interaction between the IRS and other relevant agencies.<sup>158</sup>

Other concerns about IRS administration of the ACA also have been expressed. It requires IRS employees to make decisions “unrelated to [their] traditional expertise and skill set.”<sup>159</sup> Moreover, “[f]or important and well-understood reasons, the IRS operates with a great deal of independence from other agencies. . . . [D]irect participation of the

<sup>150</sup> See, e.g., *President’s Tax Proposals to the Congress for Fairness, Simplicity, and Growth* (1985).

<sup>151</sup> See, e.g., House Comm. on Ways & Means, *Tax Reform Act of 2014, Discussion Draft, Section-by-Section Summary* (2014).

<sup>152</sup> I.R.C. § 32.

<sup>153</sup> The EITC and the related Additional Child Tax Act engender refunds exceeding \$90 billion a year. Treasury Inspector General for Tax Administration, *Existing Compliance Processes Will Not Reduce the Billions of Dollars in Improper Earned Income Tax Credit and Additional Child Tax Credit Payments* 5 (Sept. 29, 2014).

<sup>154</sup> *Id.*

<sup>155</sup> See also Staff Report, House Comm. on Oversight and Government Reform, *Making Sure Targeting Never Happens: Getting Politics Out of the IRS and Other Solutions* 14-16 (July 29, 2014).

<sup>156</sup> I.R.C. § 5000A.

<sup>157</sup> This fact is underlined by the odd rules governing enforcement of the shared responsibility payment. Unlike normal tax provisions, the IRS is prohibited from asserting criminal penalties on account of willful nonpayment of the shared responsibility payment and may not use liens or levies to collect it. I.R.C. § 5000A(g)(2).

<sup>158</sup> Government Accountability Office, *Low-Income Housing Tax Credit: Joint IRS-HUD Administration Could Help Address Weaknesses in Oversight* (July 2015).

<sup>159</sup> National Taxpayer Advocate, *2010 Annual Rep. to Congress* 20 (Dec. 31, 2010).

Service in a major non-tax Administration initiative has the potential to erode the historic independence of the Service.”<sup>160</sup>

Divesting the IRS of at least some of its non-revenue functions would liberate resources for improved IRS administration of its core functions. Hopefully, this would obviate unwise attempts to shift core duties out of the IRS. 2004 legislation authorized the IRS to enter into contracts with private companies to collect assessed but unpaid taxes.<sup>161</sup> The program was discontinued in 2009. Given the unimpressive results the first time around, occasional calls to reinstate private tax collection at the federal level should be disregarded.<sup>162</sup>

The proper role of the IRS in administering the ACA and other non-revenue initiatives<sup>163</sup> entails many questions beyond the scope of this Article. However, the possibility of shifting non-revenue initiatives outside the IRS requires serious discussion as a response to the current crisis in tax administration.

#### D. Harmonizing U.S. and Foreign Tax Rules

Historically, countries showed little enthusiasm for helping other countries enforce their tax laws.<sup>164</sup> However, in a relatively short span of time, attitudes have changed. The world’s economically leading countries all realize that, by legal or illegal means, many of their nationals are using transnational transactions to avoid or evade domestic tax liabilities.

Recognition of the common interest in preventing this evasion has led to increasing international tax cooperation. Regular and ad hoc bilateral and multilateral contacts are being established, and information exchange among revenue authorities grows apace.<sup>165</sup> Therefore, the question naturally arises whether cooperation in enforcing national laws should and will morph into some degree of harmonization of tax laws. To the extent their laws are the same, countries will find cooperation easier and more fruitful.<sup>166</sup>

A prominent experiment along these lines is the Base Erosion and Profit Shifting (BEPS) initiative of the Organization for Economic Cooperation and Development, an attempt to overcome divergences of national tax systems in order to better control transfer pricing abuses by multinational enterprises. Formidable obstacles to such efforts exist, including notions of national sovereignty and divergent national economic interests.<sup>167</sup> In

<sup>160</sup> Statement of Mark W. Everson, former Commissioner, Internal Revenue Service, *IRS: Enforcing Obama Care’s New Rules and Taxes*, hearing before House Comm. on Oversight and Government Reform, 112th Cong. (2012).

<sup>161</sup> American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 881(e), 118 Stat. 1418, 1625 (2004).

<sup>162</sup> See, e.g., National Taxpayer Advocate, *2013 Annual Rep. to Congress* 97-99 (2013).

<sup>163</sup> For example, the IRS’s administration of energy-related tax expenditures has not been especially impressive and has imposed significant burdens on the IRS. See Forman & Mann, *supra* note 112, at 775-79.

<sup>164</sup> One manifestation of this was the so-called revenue rule followed, in law or in fact, in most countries. See, e.g., Pasquantino v. United States, 544 U.S. 349, 360-68 (2005).

<sup>165</sup> Some of these efforts are described by Koskinen, *supra* note 44, at 5-7.

<sup>166</sup> For an ambitious move in this direction, see Henry Ordower, *Utopian Visions Toward a Grand Unified Global Income Tax*, 14 FLA. TAX REV. 361 (2013).

<sup>167</sup> For a description of the BEPS project and barriers to its success, see Ali Qassim, *Analysts: BEPS Project Won’t Work Without U.S.*, 34 TAX MGMT. WKLY. REP. 1042 (Aug. 17, 2015); see also Mindy Herzfeld, *A Quick Overview of the BEPS Project*, TAX NOTES, June 2, 2014, at 987.

a survey of 2500 businesses in 38 countries, only 23% of respondents thought that BEPS will be successfully implemented.<sup>168</sup> Others are more optimistic.<sup>169</sup>

International legal harmonization, even if it ultimately gains momentum, will take too long and will be too piecemeal to provide immediate help with the current crisis. However, in the long term, it will be interesting to see whether converging international tax administration interests trump or yield to diverging national economic and political interests.

#### E. Revamping Tax Lawmaking

Congress in writing Code sections and Treasury in writing regulations sometimes cling to habits that, over time, compromise efficient tax administration. Numerous examples could be adduced. Here are some possible changes to achieve attitudinal or structural correction of the processes of writing tax rules.

##### 1. *Choosing Feasibility over Theoretical Perfection*

Often, the rule maker—whether it be Congress writing a tax statute or Treasury writing a tax regulation—must choose between two competing conceptions of the enterprise. One approach is to create so detailed and nuanced a rule that, if it is accurately understood by taxpayers and the IRS, will fully and precisely capture the balancing of interests chosen by the decision maker. The second approach is to write a simpler rule that is a bit less nuanced and precise but is more readily understandable by taxpayers, their advisers, and the IRS.

Congress and the Treasury sometimes choose the former approach and other times choose the latter.<sup>170</sup> In my view, Congress and the Treasury too often choose the former. The assumption behind this choice seems to be that the way something is written inside the Washington beltway is the way it is applied by taxpayers, their representatives, and IRS field agents outside the Beltway. This assumption is a flight from reality. In many instances, the complexity of the rule as written defies the comprehension and the ability to implement of mere mortals. When that happens, taxpayers make the best guess they can. This best guess may not accord with the best guess of IRS agents, leading to unnecessary and wasteful administrative appeals and litigation.

Consider three examples, all drawn from Subchapter K, governing income taxation of partnerships and their partners. First, when a person renders services to a partnership and receives a profits-only interest in the partnership as compensation, does that person have an immediate inclusion into income? This issue has generated confusion—inside the government as well as outside it—for decades. In one case, the IRS asserted additional tax in such a case on a particular theory and won in the Tax Court. Defending against the ensuing appeal, the Department of Justice conceded that the theory that had prevailed in the Tax Court was erroneous but defended the result on a different theory. The circuit court rejected that new theory and held for the taxpayer.<sup>171</sup>

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<sup>168</sup> See Qassim, *supra* note 167 (reporting on a survey by Grant Thornton); see also Jeremy Scott, *BEPS Project Faces Rough Future in Congress*, TAX NOTES, June 9, 2014, at 1063; Lee A. Sheppard, *The BEPS Hybrid Draft and the Euro*, TAX NOTES, June 9, 2014, at 1085.

<sup>169</sup> See Qassim, *supra* note 167 (BEPS “is a thoughtful and impressive response” to “overcoming divergence of tax systems” and “shows international tax cooperation at its best.”) (quoting British tax consultant Stephen Fiamma).

<sup>170</sup> As examples of the latter approach (less precise but more understandable), see I.R.C. §§ 63(c), 102(c), and 152(e), all discussed by Johnson, *supra* note 127, at 584-88.

<sup>171</sup> *Campbell v. Comm’r*, 59 T.C.M. 236 (1990), *rev’d*, 943 F.2d 815, 818 (8th Cir. 1991).

Second, when a partner engages in transactions with her partnership, the tax treatment depends on which characterization under Code section 707 applies. In one case, the IRS prevailed in the Tax Court on the basis of the particular categorization it argued for.<sup>172</sup> However, in a later revenue ruling involving similar facts, the IRS held that that categorization—the one the IRS had persuaded the Tax Court to accept—is wrong.<sup>173</sup>

Third, when liquidating payments are made to a retired partner or the estate of a deceased partner, the tax treatment depends on the characterization under section 736. According to the Tax Court, to dispel “any lingering doubt [about] the distressingly complex and confusing nature of . . . Subchapter K . . . one has only to reread section 736 in its entirety.”<sup>174</sup>

Congress and the Treasury would materially ease the IRS’s burdens in administering the tax laws by more frequently giving up a mote of nuance, of theoretical perfection in the statute or regulation in favor of a rule that taxpayers and IRS agents can more readily understand and apply.<sup>175</sup> “[T]he most ingenious tax policy proposal really isn’t worth very much if it cannot be successfully administered by the IRS.”<sup>176</sup>

## 2. *Improving the Legislative Process*

Our traditional conception is that “[t]axation is a legislative function, and [at the federal level] Congress . . . is the sole organ for levying taxes.”<sup>177</sup> Not surprisingly, there is no end of criticism of how Congress has performed this function.<sup>178</sup>

The literature is not wanting for suggestions for how Congress can improve this performance. By way of example and not necessarily of endorsement, Professors Forman and Mann propose (1) creating a permanent loophole-closing commission and (2) requiring Congress to provide greater detail in tax statutes, instead of delegating the task to the Treasury for regulation-writing.<sup>179</sup> These and other proposals are not uncontroversial. For example, Professors Hines and Logue propose that Congress delegate more, not less, of the tax lawmaking power to Treasury.<sup>180</sup>

### F. Changing Incentives

Ends can be achieved by commands supported by coercive power. Or they can be achieved through attitudinal changes, by aligning incentives and perceptions so that self-interest and the public interest walk together. Below are some proposals of the latter type that might be useful in easing the current crisis.

#### 1. *Attitudes of Taxpayers*

Numerous aspects of current American tax administration make life harder on taxpayers than is warranted by the resulting benefit to the government. Among the bolder

<sup>172</sup> *Pratt v. Comm’r*, 64 T.C. 203 (1975), *aff’d in part & rev’d in part*, 550 F.2d 1023 (5th Cir. 1977).

<sup>173</sup> Rev. Rul. 81-300, 1981-2 C.B. 143, 144.

<sup>174</sup> *Foxman v. Comm’r*, 41 T.C. 535, 551 n. 9 (1964), *aff’d*, 352 F.2d 466 (3d Cir. 1965).

<sup>175</sup> See Johnson, *supra* note 127, at 582-88; see also Forman & Mann, *supra* note 112, at 803-04 (urging the Treasury to issue simplifying regulations).

<sup>176</sup> George K. Yin, *The Most Critical Issue Facing Tax Administration Today—And What To Do About It* 1 (June 27, 2014), <http://ssrn.com/abstract=2459592> [<https://perma.cc/AP53-AW69>].

<sup>177</sup> *Nat’l Cable Television Ass’n v. United States*, 415 U.S. 336, 340 (1974); see U.S. CONST. art. I, § 8, cl. 1.

<sup>178</sup> See, e.g., Michael Doran, *Tax Legislation in the Contemporary U.S. Congress*, 67 TAX L. REV. 555 (2014).

<sup>179</sup> Forman & Mann, *supra* note 112, at 789-92.

<sup>180</sup> James R. Hines, Jr. & Kyle D. Logue, *Delegating Tax*, 114 MICH. L. REV. 235 (2015).

possible changes is “presumptive taxation.” Under this approach, a taxpayer’s liability would be computed not on actual income but on various “easily verifiable external factors” that would serve as proxies for income.<sup>181</sup> For instance, “a tax on some percentage of a business’s gross receipts or its asset values rather than a precise measure of income might be considered a rough proxy for a business income tax.”<sup>182</sup>

The approach could be employed as the legally conclusive measurement, or the result of its use could establish a rebuttable presumption, allowing taxpayers to prove actual taxable income to overcome the proxy-based presumption.<sup>183</sup> If used only presumptively, the expectation is that many taxpayers would simply go along with the proxy result, as a way to avoid the expense and annoyance of maintaining records and preparing returns.<sup>184</sup>

Another approach would be moving to a “return free” system. Under it, at least some taxpayers—such as those whose income is captured fully by withholding on wages reported on Form W-2—could have their liabilities computed by the IRS from the reported sources.<sup>185</sup> The effort of that calculation by the IRS likely would be offset by savings in avoiding the need to process the now unnecessary returns.

Penalty reform also could be guided by putative effects on policy. Some have argued that current penalties are badly designed both in amount and in application, with the result that they do not encourage, and may even undercut, taxpayer compliance.<sup>186</sup> In addition, the reasonable cause defense to tax penalties<sup>187</sup> may encourage taxpayers to take aggressive tax return positions, relying on dubious advice from lawyers or accountants to deflect possible penalties. The defense may need to be adjusted to curb this possibility.<sup>188</sup>

## 2. Attitudes of Third Parties

Knowledgeable third parties can be important allies for the IRS. This already is reflected in the tax “whistleblower” initiative,<sup>189</sup> which, after a slow start, appears to be growing.<sup>190</sup> In a somewhat parallel vein, commentators have proposed authorizing *qui tam* suits in tax matters,<sup>191</sup> creating a climate in which tax advisers will discourage taxpayers from participating in tax shelters,<sup>192</sup> and applying pressure against aggressive tax planning

<sup>181</sup> Kathleen Delaney Thomas, *Presumptive Collection: A Prospect Theory Approach to Increasing Small Business Tax Compliance*, 67 TAX L. REV. 111, 114 (2013).

<sup>182</sup> Kyle D. Logue & Gustavo G. Vettori, *Narrowing the Tax Gap Through Presumptive Taxation*, 2 COLUM. J. TAX L. 100, 105 (2011).

<sup>183</sup> Victor Thuronyi, *Presumptive Taxation*, in 1 TAX LAW DESIGN AND DRAFTING (1996).

<sup>184</sup> Just as some taxpayers under the present income tax select the standard deduction even though itemizing might yield somewhat higher deductions.

<sup>185</sup> See, e.g., Forman & Mann, *supra* note 112, at 804-06.

<sup>186</sup> See, e.g., National Taxpayer Advocate, *2008 Annual Rep. to Congress* 2 (2008).

<sup>187</sup> See, e.g., I.R.C. § 6664(c). See generally Leandra Lederman, Stephen Mazza & Steve Johnson, *Surcharges and Penalties in Tax Law: United States* (2015), <http://ssrn.com/abstract=2635133> [<https://perma.cc/24LL-EFZP>].

<sup>188</sup> See, e.g., Steve R. Johnson, *A Modest Proposal to Improve Tax Compliance: Curbing Penalty Protection Opinions* (2008), <http://ssrn.com/abstract=1285282> [<https://perma.cc/7NU7-VWTE>].

<sup>189</sup> I.R.C. § 7623; see, e.g., Matthew R. Stock, Note, *Tax Whistleblower Statute: Obtaining Meaningful Appeals Through the Appropriate Scope of Review*, 42 FLA. ST. U. L. REV. 819 (2015).

<sup>190</sup> Total awards paid under the program grew from about \$344 million and \$310 million in Fiscal Years 2013 and 2014, respectively, to over \$501 million in Fiscal Year 2015. IRS Whistleblower Office, *Fiscal Year 2015 Report to Congress* (2016).

<sup>191</sup> See, e.g., Joshua D. Rosenberg, *The Psychology of Taxes: Why They Drive Us Crazy, and How We Can Make Them Sane*, 16 VA. TAX REV. 155, 209-18 (1996).

<sup>192</sup> See, e.g., Richard Lavoie, *Deputizing the Gunslingers: Co-Opting the Tax Bar into Dissuading Corporate Tax Shelters*, 21 VA. TAX REV. 43 (2001).

and reporting by removing privacy protections from some corporate tax return information.<sup>193</sup> Similarly, the IRS's attempt to bring unregulated tax return preparers "in from the cold" first by an invalidated mandatory regulation<sup>194</sup> and now by a voluntary (incentivized) program<sup>195</sup> attempts to adjust the knowledge and the motivation of such preparers to prepare and file accurate returns.

### 3. *Attitudes of IRS*

It is hard to change institutional culture. However, as a small silver lining in a large dark cloud, the substantial personnel turnover the IRS has been experiencing<sup>196</sup> may facilitate this change. "Responsive tax administration" focuses on "regulatory tools and approaches designed to move beyond a one-size-fits-all framework [hopefully to] gain voluntary compliance by regulated parties."<sup>197</sup> A large literature on it already exists.<sup>198</sup>

Especially in the current environment, the big objection, of course, is that limited resources are incompatible with tailored, contextualized treatment of taxpayers. Some scholars have addressed this concern, offering approaches to allow better targeting without the cost of case-by-case discretionary enforcement.<sup>199</sup>

#### G. Greater Use of Technology

Technology, of course, is already central to tax administration. Two of the pillars of the current income tax are withholding<sup>200</sup> and third-party information reporting.<sup>201</sup> "Technological improvements have made [these] more efficient, which has allowed these mechanisms to become more pervasively used."<sup>202</sup> Technology links to other possible avenues, described above, of response to the current crisis. For example, the BEPS project<sup>203</sup> "should consider automating the exchange of country-by-country reporting data to avoid overburdening tax administrators with the task of evaluating thousands of individual requests per year."<sup>204</sup>

<sup>193</sup> Joshua D. Blank, *Reconsidering Corporate Tax Privacy*, 11 N.Y.U. J.L. & Bus. 31 (2014).

<sup>194</sup> *Loving v. IRS*, 742 F.3d 1013 (D.C. Cir. 2014), *aff'g* 917 F. Supp. 2d 67 (D.D.C. 2013); *see e.g.*, Steve R. Johnson, *Loving and Legitimacy: IRS Regulation of Tax Return Preparation*, 59 VILL. L. REV. 515 (2014).

<sup>195</sup> Annual Filing Season Program, FS-2014-8, IR-2014-75 (June 2014).

<sup>196</sup> *See* text accompanying notes 68 to 70 *supra*.

<sup>197</sup> Leigh Osofsky, *Some Realism About Responsive Tax Administration*, 66 TAX L. REV. 301 (2012).

<sup>198</sup> *Id.* at 301-02.

<sup>199</sup> *See, e.g.*, Leandra Lederman & Ted Sichelman, *Enforcement as Substance in Tax Compliance*, 70 WASH. & LEE L. REV. 1679 (2013) (advocating probabilistic enforcement); Alex Raskolnikov, *Revealing Choices: Using Taxpayer Choice to Target Tax Enforcement*, 109 COLUM. L. REV. 689 (2009) (urging differentiating taxpayers based on their taxpaying motivation and urging creation of two different enforcement regimes, inducing taxpayers to choose between them).

<sup>200</sup> *See* Ajay K. Mehrotra, "From Contested Concept to Cornerstone of Administrative Practice": *Social Learning and the Early History of U.S. Tax Withholding*, 7 COLUM. J. TAX L. 144 (2016).

<sup>201</sup> Compliance rates correlate closely with how robust information reporting is. *See* IRS, *Tax Gap for Tax Year 2006*, Overview (2012), [https://www.irs.gov/pub/newsroom/overview\\_tax\\_gap\\_2006.pdf](https://www.irs.gov/pub/newsroom/overview_tax_gap_2006.pdf) [<https://perma.cc/S3TW-ZQ8H>]. Most proposals for better tax compliance urge expansion of such reporting. *See, e.g.*, Forman & Mann, *supra* note 112, at 792-94.

<sup>202</sup> Jeffery H. Kahn & Gregg D. Polsky, *The End of Cash, the Income Tax, and the Next 100 Years*, 41 FLA. ST. U. L. REV. 159, 159 (2013).

<sup>203</sup> *See* text accompanying notes 167 to 169 *supra*.

<sup>204</sup> John Koskinen, quoted by William Hoffman, *Koskinen Urges OECD to Consider Tax Administrations in BEPS*, TAX NOTES, June 9, 2014, at 1096.

The IRS believes that technological innovation is central to the future of tax administration.<sup>205</sup> In particular, it is looking to “big data” analytics to improve IRS services in a range of areas,<sup>206</sup> and even more innovative applications may become possible.<sup>207</sup>

But a snake or two may lurk even in a new technology-driven Garden of Eden. First, of course, the heavier the reliance on technology, the greater the harms if that technology is compromised. Achieving and maintaining a first-class maintenance and security apparatus will be essential.

Second, technology must be kept the servant and not allowed to become the master. The goal must be to use the capabilities to allow the IRS to better adapt to taxpayers—in all their variety—not to demand that taxpayers take on uniform shape most congenial to systems design and parameters. The poor and powerless too often are not present in, and are ignored by, conversations about tax reform.<sup>208</sup>

The IRS has assured us of its intention to, “[t]hrough the use of sophisticated analytics, . . . uncover insights that will allow us to better serve underserved populations.”<sup>209</sup> However, the IRS also says that “[t]axpayer expectations and behaviors indicate a preference towards online self-service.”<sup>210</sup> No doubt many taxpayers have such a preference. But not all do. For various reasons, some do not want, or want but cannot obtain, modern computing capability, and some will actually want to talk with a real, live person. Hopefully, the IRS will not use the preferences of some to relegate others to tax service oblivion.<sup>211</sup>

#### IV. REALITIES AND NEW REALITIES

Part III sketched general directions and some specific proposals that might, if properly designed, ease the crisis created by the perfect storm intersection of flat or declining IRS budgets, growing IRS revenue-related workloads, and foisting upon the IRS major responsibilities not essentially connected to the IRS’s revenue-collection function. In the context of particular possibilities, Part III noted relevant political considerations.

We now turn to political realities on a more general plane, considering them from three perspectives: (1) acknowledging the reality of perverse political incentives, (2) noting

<sup>205</sup> See, e.g., Douglas Shulman (former Commissioner of Internal Revenue), *Shulman Addresses Major Trends Affecting Tax Administrations*, TAX NOTES, May 19, 2014, at 835.

<sup>206</sup> *New IRS Strategic Plan Emphasizes Better IT, “Big Data” to Improve Taxpayer Services*, 33 TAX MGMT. WKLY. REP. 887 (July 7, 2014) [hereinafter *Big Data*].

<sup>207</sup> See, e.g., Kahn & Polsky, *supra* note 202, at 171 (“On the one hand, the increasing prevalence of electronic payment systems should bolster the income tax by substantially reducing the tax gap and mitigating the distortions caused by the cash economy. On the other hand, technological innovation and the corresponding evolution of attitudes towards privacy could make a progressive retail sales tax quite feasible, which might spell the end of the income tax.”).

<sup>208</sup> See, e.g., Cohen, *supra* note 1, at 119-20 (“We don’t even know average taxpayers. We are only dealing with the upper three or four percentage of taxpayers. Yet we all seem to assume that what we see is the universe.”).

<sup>209</sup> See *Big Data*, *supra* note 206, at 887. Other goals are to “improve our demand planning capabilities, identify potential fraud schemes and more quickly detect noncompliance.” *Id.* (quoting IRS 2014-2017 Strategic Plan).

<sup>210</sup> See *id.*; see also IRS Electronic Tax Administration Advisory Comm., *Annual Rep. to Congress* 2 (June 2015) (“The nature of this demand [by taxpayers for IRS services] is also changing, as taxpayers increasingly prefer digital self-service to phone and paper methods.”).

<sup>211</sup> Lest a future version of William Jennings Bryan be forced to deliver a jeremiad: “You shall not press down upon the brow of labor this Web of Wireless Thorns. You shall not crucify humankind upon a Cross of Cyber Conformity.” (I apologize to the memory of the Great Commoner and to all who hold dear his July 9, 1896 “Cross of Gold” speech).

that, given the impermanence of everything political, today's reality may be tomorrow's memory, and (3) in light of the above, suggesting an appropriate role for those interested in the solvency of tax administration in the United States now and in the future.

#### A. Realities

Everywhere and always, public policy is driven in part by the public interest and in part by personal interest (what is sometimes called "public choice").<sup>212</sup> It is of course true that ideas with much public interest merit fail because of public choice perversities.<sup>213</sup> Examples abound. Congress often "strings out" desirable changes rather than implementing a whole agenda at one time because doing so is a way to raise PAC contributions over many years, not just one.

Part of Congress' recent hostility to the IRS may well be based on principle,<sup>214</sup> but the unscrupulous have incentive to keep the issue alive rather than solve it. Inadequate IRS technology and training budgets guarantee future IRS "screw-ups," and each such event is the chance for media exposure, new fund-raising letters, and guaranteed applause lines in stump speeches.

Nearly everyone speaks urgently of the need to simplify our tax laws.<sup>215</sup> But "[t]ax simplification has no constituency."<sup>216</sup> When a lawyer or politician is put to the choice of supporting (1) a simple tax rule that does nothing for, or even hurts, a client or important constituent or (2) a complicated rule that is very much in the client's or constituent's pocketbook interest, the "smart money" knows where to place its bet.<sup>217</sup>

And, of course, self-interest does not stop at the water's edge. BEPS faces and future international tax harmonization initiatives will face great pressure from parochial, national interests.<sup>218</sup>

#### B. "Realities"

Only an incorrigible optimist would ignore the preceding barriers to the making and maintaining of good tax policy. But only an incorrigible defeatist—and one with little knowledge of tax history—would assume that obstacles are forever. Political forces are always in motion, so political realities are always temporary. Even enduring tendencies can be swamped, if only for a brief window of opportunity, but the march of events.

Consider some examples:

- The "bracket creep" phenomenon (tax bills rising because of the effects of inflation) offered real benefits to politicians: (1) rising revenues not requiring voting for tax increases and (2) the chance to be a hero to the voters by periodically voting for tax cuts only partly offsetting bracket

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<sup>212</sup> A classic study of this interaction as to the historic Tax Reform Act of 1986 is Daniel Shaviro, *Beyond Public Choice and Public Interest: A Study of the Legislative Process as Illustrated by Tax Legislation in the 1980s*, 139 U. PA. L. REV. 1 (1990). See also Julie A. Roin, *United They Stand, Divided They Fall: Public Choice Theory and the Tax Code*, 74 CORNELL L. REV. 62 (1988).

<sup>213</sup> See, e.g., Cohen, *supra* note 1, at 123 n.10 (noting the demise of one tax legislative process reform which "like all really good ideas was left fallow").

<sup>214</sup> See Subpart III.B. *supra*.

<sup>215</sup> *But see, e.g.*, Samuel A. Donaldson, *The Easy Case Against Tax Simplification*, 22 VA. TAX REV. 645 (2003).

<sup>216</sup> Cohen, *supra* note 1, at 118.

<sup>217</sup> See *id.* at 115-16.

<sup>218</sup> See text accompanying notes 167 to 169 *supra*.

creep. And yet bracket creep was banished from the Code a generation ago and has not returned.<sup>219</sup>

- Politicians benefit (in the form of campaign contributions) from annually renewing annually popular tax breaks. Yet Congress recently voted to make some renewals permanent.<sup>220</sup>
- The value-added tax was once considered political poison. Yet many Presidential candidates—Republican Presidential candidates—now are proposing them.<sup>221</sup>

### C. What To Do

Many a fair flower of reform has been crushed under the hard heels of selfish interest and callous indifference. But there is personal satisfaction in fighting the good fight, even if it is against long odds.<sup>222</sup> And the good does sometimes triumph despite the odds. If major reform is unlikely, piecemeal gains can be won.<sup>223</sup>

Those who are friends of good tax administration might find the following course realistic without being fatalistic: (1) continue to advocate for good ideas, creating an intellectual record that can justify change at the opportune moment; (2) when the winds of public choice opposition blow hard, husband energy and avoid discouragement; (3) when the gale subsides or when political circumstances direct the wind in favorable direction, seize the moment to push hard for the changes already justified intellectually; and (4) compromise but not to the point of sacrificing core principles of taxation.

What are those principles? Many sets have been offered. Professor, later Judge, Sneed's seven principles of taxation are always worth remembering.<sup>224</sup> Other commentators have offered different or more particularized lists.<sup>225</sup> So have political leaders of both parties.<sup>226</sup> The IRS has established a ten-part Taxpayer Bill of Rights.<sup>227</sup>

Regardless of the stresses of the moment, even those as acute as the current "perfect storm," tax discourse and action should always trench firmly in solid principles. To endure, to flourish over the long term, so pervasive and crucial a function as financing the government must rest on principles, not expediency. Despite the crisis, we should eschew anything momentarily seductive that would imperil the enduringly sound.

<sup>219</sup> See I.R.C. §§ 1(f), 63(c)(4).

<sup>220</sup> H.R. 2029, Protecting Americans From Tax Hikes Act, 114th Cong. (1st Sess. Dec. 2015).

<sup>221</sup> See Paul Caron, *Value-Added Tax Catches on in Republican Presidential Race*, WALL ST. J. (Nov. 12, 2015), <http://www.wsj.com/articles/value-added-tax-catches-on-in-republican-presidential-race-1447374891> [<https://perma.cc/SD69-6RSS>].

<sup>222</sup> "The idea of tax nirvana seems always to elude us. But like Don Quixote, the quest is the thing." Cohen, *supra* note 1, at 122.

<sup>223</sup> See *id.* at 123 (for this reason, seeing himself as "a raging incrementalist" in tax policy).

<sup>224</sup> (1) Adequate revenue, (2) Administrability, (3) Horizontal fairness, (4) Economic stability, (5) Distributional fairness, (6) Market-oriented economy, and (7) Political order. Joseph T. Sneed, *The Criteria of Federal Income Tax Policy*, 17 STAN. L. REV. 567, 568 (1965).

<sup>225</sup> See, e.g., Johnson, *supra* note 112, at 244-46 (criteria as to tax procedural reform).

<sup>226</sup> See, e.g., President's Framework for Business Tax Reform 1 (Feb. 2012) (five elements of business tax reform); Kevin Brady, Chair, House Ways and Means Comm., *Keynote Address*, Tax Council Policy Institute Symposium 3-4 (Feb. 12, 2016) (on file with author).

<sup>227</sup> IRS Pub. 1, *Your Rights as a Taxpayer* (rev. Dec. 2014).