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## NOTES

HOLISTIC TAX REFORM: PROCEDURE, THE MISSING  
COMPANION TO THE TAX CUTS AND JOBS ACT'S SUBSTANTIVE  
LAW FOCUS

*Jake E. Balogh*



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# NOTES

## HOLISTIC TAX REFORM: PROCEDURE, THE MISSING COMPANION TO THE TAX CUTS AND JOBS ACT'S SUBSTANTIVE LAW FOCUS

*Jake E. Balogh\**

### I. INTRODUCTION

Substantive laws are important, but so too are procedural laws. Substantive laws determine tax liabilities, whereas procedural laws govern how disputed tax liabilities are resolved.<sup>1</sup> Both substantive and procedural laws can be modified through tax legislation. However, tax reform is often a proxy for “broadening the tax base, closing loopholes, and [stimulating] the economy.”<sup>2</sup> The substantive nature of this style of reform is arguably self-evident. Whereas, the procedural aspect of tax law is forgotten. Therefore, to aid the analysis of tax legislation, this Note proposes a new evaluation standard: holistic reform. This new standard of evaluation would build upon the comprehensive reform standard; there must be a meaningful congressional attempt to amend both substantive and procedural tax laws.

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\* Candidate for JD, 2019, University of Pittsburgh School of Law. Thanks to Charles Wakefield, a Pittsburgh Tax Review alumnus, for his invaluable help in developing this topic, and thanks to the Pittsburgh Tax Review faculty editors for their feedback and comments. Also, many thanks to my wife, Jaimee, and our daughter for their support while I have continued my education.

<sup>1</sup> Steve Johnson, *The 1998 Act and the Resources Link Between Tax Compliance and Tax Simplification*, 51 U. KAN. L. REV. 1013, 1013 n.1 (2003).

<sup>2</sup> Press Release, U.S. Dep’t of the Treasury, Unified Framework for Fixing Our Broken Tax Code (Sept. 27, 2017), <https://www.treasury.gov/press-center/press-releases/Pages/sm0166.aspx>. For more information about what the Republican Party hoped to accomplish with the TCJA, please refer to Stephen J. Pieklik et al., *Deducting Success: Congressional Policy Goals and the Tax Cuts and Jobs Act of 2017*, 16 PITT. TAX REV. 1 (2018).

Based upon this constructed definition of holistic tax reform, I argue that the Tax Cuts and Jobs Act of 2017<sup>3</sup> (TCJA or Act) does not rise to the level of holistic tax reform. Undoubtedly, the TCJA drastically adjusted substantive elements of the federal tax system. However, the TCJA did not meaningfully attempt to address the procedural elements of the federal tax system.

One example of procedural tax reform is the Bipartisan Budget Act of 2015 (BBA).<sup>4</sup> The BBA simplified the procedural tax laws that applied specifically to partnerships.<sup>5</sup> The methods used by the BBA to simplify partnership taxation procedure cannot be easily applied to other entity types.<sup>6</sup> Nevertheless, the wisdom behind the BBA exemplifies the attempt to curb the Internal Revenue Service's (Service) counterproductive behaviors. An example of an uncorrected counterproductive procedure would be offers in compromise.<sup>7</sup> Offers in compromise are the administrative settlement process used by many different types of taxpayers.<sup>8</sup> This Note, however, addresses offers in compromise only in the context of individual taxpayers.

Offers in compromise are procedurally inefficient because the denial of an administrative compromise can be subsequently overridden after the government devotes additional resources in the legal settlement process. There are three bases on which Service employees can enter into an administrative settlement. First, an administrative settlement can be based upon a legitimate dispute; in other words, the employee's determination that the taxpayer is not liable for a portion of the tax liability.<sup>9</sup> Second, an

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<sup>3</sup> Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017).

<sup>4</sup> Bipartisan Budget Act of 2015, Pub. L. No. 114-74, 129 Stat. 584.

<sup>5</sup> Michael Hauswirth et al., *Practical Implications of New Partnership Audit Rules*, TAX EXEC. (Feb. 2, 2017), <https://taxexecutive.org/practical-implications-of-new-partnership-audit-rules/>.

<sup>6</sup> *See id.*

<sup>7</sup> *See* Robert E. McKenzie, *IRS Relaxes Offer in Compromise Rules*, FORBES (Aug. 10, 2015, 9:03 PM), <https://www.forbes.com/sites/irswatch/2015/08/10/irs-relaxes-offer-in-compromise-rules>.

<sup>8</sup> *See* I.R.C. § 7122; *see also Offer in Compromise*, TAXPAYER ADVOCATE SERV., <https://taxpayeradvocate.irs.gov/get-help/offers-in-compromise> (last updated Apr. 6, 2018).

<sup>9</sup> Doubt as to Liability Offer in Compromise, I.R.M. 5.19.24 (Aug. 13, 2018); *see* Offers in Compromise and the Role of Counsel, I.R.M. 33.3.2.2(1)–(3) (Oct. 5, 2015); *see also* Review of Doubt as to Liability Offers, I.R.M. 33.3.2.3.1 (Aug. 11, 2004). This footnote, and many subsequent footnotes, include parallel citations to Part 5, Collecting Process, and Part 33, Legal Advice, of the Internal Revenue

administrative settlement can be based upon collection potential; the Service may concede a portion of the liability that will be uncollectable.<sup>10</sup> The third basis for administrative settlement is effective tax administration; the laws of taxation are not enforced if it would either cause a taxpayer to suffer economic hardship or if the action would undermine public confidence in the federal laws of taxation.<sup>11</sup>

In the initial tax deficiency dispute, when the taxpayer and the Service cannot reach an administrative outcome, the process typically progresses to litigation. Office of Chief Counsel (Chief Counsel) attorneys can enter into legal settlements based on the merits of the controversy; that is, they apply fact to law.<sup>12</sup> The taxpayer's ability to pay and the corresponding collection potential are not considered by Chief Counsel.<sup>13</sup> Thus, Chief Counsel attorneys, as compared to Service employees, have increased autonomy to enter into settlements.<sup>14</sup>

There are two possible ways to correct the incongruence between legal and administrative settlements: either legal settlements can be restricted to the same degree as administrative settlements, or administrative settlements can be relaxed to the same degree as legal settlements. Restricting legal settlements is not a viable option; it is incompatible with Chief Counsel's

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Manual. Part 33 of the Internal Revenue Manual addresses Chief Counsel's approval of offers in compromise. The attorney evaluation process is limited to ensuring that administrative compromise is appropriate and correctly produced: "[Administrative] determinations should ordinarily not be reexamined by Counsel unless patently erroneous. Asset valuations and necessary expense determinations are largely matters of administrative discretion and judgment and should not be questioned by Counsel." I.R.M. 33.3.2.2(3). Therefore, the parallel citations to Parts 33 and 35, Tax Court Litigation, of the Internal Revenue Manual are included to provide context and additional information.

<sup>10</sup> Doubt as to Collectibility, I.R.M. 5.8.4.3 (Jan. 18, 2018); *see* Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.3.2 (Nov. 4, 2010).

<sup>11</sup> Effective Tax Administration, I.R.M. 5.8.11 (Aug. 5, 2015); *see* Review of Effective Tax Administration Offers, I.R.M. 33.3.2.3.3 (Nov. 4, 2010).

<sup>12</sup> Settlement on the Merits, I.R.M. 35.5.2.4(1) (Dec. 31, 2012).

<sup>13</sup> *Id.*

<sup>14</sup> *See* I.R.M. 5.19.24; *see also* I.R.M. 33.3.2.3.1; I.R.M. 33.3.2.3.2; I.R.M. 33.3.2.3.3; I.R.M. 35.5.2.4(1).

operating procedures.<sup>15</sup> Moreover, maximizing tax liabilities produces paper judgments. It does not inherently ensure payment of maximized tax liabilities.

The better of these two options is to make administrative and legal settlements equally obtainable by relaxing the administrative settlement standards. To accomplish this, the motivation in the administrative settlement process, in situations other than intentional noncompliance,<sup>16</sup> should be to maximize settlement amounts. If the Service were to rely on increased employee discretion, then the Service should increase the number of employees and their abilities to shoulder greater responsibilities. The Service, however, is incapable of meeting increased expectations without appropriate funding and support.<sup>17</sup> How did we arrive at the current inefficient method of tax dispute resolution? The answer lies in the failure to consider the interplay between substantive and procedural tax laws.<sup>18</sup>

In Part II, I propose the new evaluation standard of holistic tax reform. Part III examines whether the TCJA satisfies this constructed definition of holistic tax reform. In Part IV, I use the BBA to provide an example of prior congressional action involving procedural tax laws. In Part V, I then examine a procedural tax law—offers in compromise—that was ripe for congressional intervention in 2017. Part VI addresses how remediation of the procedural problems associated with offers in compromise would require congressional reassessment of its commitment to the Service.

## II. HOLISTIC TAX REFORM: SUBSTANCE AND PROCEDURE

The TCJA was intended to be reform along the lines of the Tax Reform Act of 1986<sup>19</sup> (TRA); the purpose was to “broaden[] the tax base, clos[e]

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<sup>15</sup> General Principles for Handling Legal Work, I.R.M. 31.1.1.1(3) (Aug. 11, 2004). “We properly protect the revenue only when we ascertain and apply the true meaning of the statute.” *Id.*

<sup>16</sup> Johnson, *supra* note 1, at 1059–60. “The Code recognizes that fraud is special, and it treats it more harshly than it treats mere mistake or negligence.” *Id.* at 1060.

<sup>17</sup> *See id.* at 1013–14.

<sup>18</sup> *See id.* at 1013.

<sup>19</sup> Pub. L. No. 99-514, 100 Stat. 2085.

loopholes, and [stimulate] the economy.”<sup>20</sup> The Republican Party leadership based their subjective appraisals on the TCJA’s modification of substantive laws;<sup>21</sup> they gave procedural tax laws insufficient attention. The concern is that such an approach fails to properly assess the importance of both types of tax law. Therefore, this Note proposes the new evaluation standard of holistic reform. This new standard of evaluation builds upon the comprehensive reform standard. The holistic standard is only satisfied when Congress meaningfully attempts both substantive and procedural tax reform.

For many, the TRA serves as the prototype for tax reform. Some have argued that the TRA was the most important tax legislation since the enactment of the income tax.<sup>22</sup> Those who agree contend that “[t]he 1986 Tax Reform Act . . . broadened the tax base . . . [and] provid[ed] a roadmap on how to pass a major tax overhaul . . . .”<sup>23</sup> This is the conceptual framework that the Republican Party leadership operated within.

Before introducing the legislation, Republican Party leadership engaged in a campaign to “sell” the TCJA to voters.<sup>24</sup> *The Unified Framework for Fixing Our Broken Tax Code* was released on September 27, 2017,<sup>25</sup> roughly one month before the legislation was formally introduced. The framework indicated that the legislation would be tax reform in the sense that “[the TCJA] will deliver fiscally responsible tax reform by broadening the tax base, closing loopholes and growing the economy.” The framework went on to describe what this actually entailed. As it pertained to individual taxpayers, the TCJA would provide tax relief by adjusting the income amounts associated with the marginal tax brackets, lowering the corresponding marginal percentages, and revisiting deductions and credits.<sup>26</sup>

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<sup>20</sup> Press Release, *supra* note 2.

<sup>21</sup> *See id.*

<sup>22</sup> Kenneth Behle, *Repeal of the Corporate AMT as Part of Upcoming Tax Reform*, 155 TAX NOTES 133, 133 (2017).

<sup>23</sup> Jay Starkman, *Why Are Taxes So Complex?*, 155 TAX NOTES 1255, 1257 (2017).

<sup>24</sup> Press Release, *supra* note 2.

<sup>25</sup> *See id.*

<sup>26</sup> *Id.* The framework also mentioned that the legislation would alter retirement plan taxation and estate and gift taxation. *Id.*

President Trump's comments as he signed the Act followed the widened-tax-base, fewer-loopholes, and stimulated-economy approach to tax reform.<sup>27</sup> More specifically, he only referred to substantive tax law. The tax base would be widened by \$3 to \$5 trillion.<sup>28</sup> He said that it "tremendously cut regulations."<sup>29</sup> President Trump also commented that many businesses were expected to make capital investments in manufacturing and other industries as a result of the TCJA, thereby stimulating the economy.<sup>30</sup> Republican Party leadership in Congress and President Trump sold the TCJA as tax reform that would broaden the tax base, close loopholes, and stimulate the economy. There was, however, no mention of how the TCJA would affect procedural tax laws.<sup>31</sup>

This approach to tax reform is problematic. Tax laws can be assigned to one of two categories: substantive or procedural laws.<sup>32</sup> While it is true that both types of tax law are modifiable through legislation,<sup>33</sup> these types of tax law are not interchangeable. Substantive laws determine the amount of a taxpayer's liability,<sup>34</sup> which is the amount that the taxpayer owes to the federal government. Procedural laws determine how a taxpayer and the Service resolve disputes related to this liability amount.<sup>35</sup>

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<sup>27</sup> See *Remarks by President Trump at Signing of H.R. 1, Tax Cuts and Jobs Bill Act, and H.R. 1370*, THE WHITE HOUSE (Dec. 22, 2017), <https://www.whitehouse.gov/briefings-statements/remarks-president-trump-signing-h-r-1-tax-cuts-jobs-bill-act-h-r-1370/> [hereinafter *President's Remarks*].

<sup>28</sup> *Id.*

<sup>29</sup> *Id.* This can be interpreted to suggest that loopholes created by regulations were closed.

<sup>30</sup> *Id.*

<sup>31</sup> See *id.*; see also Press Release, *supra* note 2.

<sup>32</sup> See *id.* at 1013 n.1.

<sup>33</sup> Steve R. Johnson, *The Future of American Tax Administration: Conceptual Alternatives and Political Realities*, 7 COLUM. J. TAX L. 5, 10 n.20 (2016).

<sup>34</sup> Johnson, *supra* note 1, at 1013 n.1.

<sup>35</sup> *Id.* "[P]rocedural tax law[s] are] (i) the rules by which controversies as to the amount of substantive liability are resolved, (ii) the rules which govern collection of the liability once its amount has been determined, and (iii) civil and criminal penalty regimes to encourage prompt and accurate payment of tax." *Id.*

As stated above, substantive and procedural laws can both be modified by legislation.<sup>36</sup> One purpose of modifying tax laws is to increase taxpayer compliance.<sup>37</sup> “Self-reporting is the bedrock of our system of taxation . . . .”<sup>38</sup> It is easy to see why substantive tax laws affect taxpayer compliance.<sup>39</sup> If taxpayers believe that others are able to avoid paying their fair share of taxes, then these taxpayers begin to see their own compliance obligations as optional.<sup>40</sup>

Procedural tax laws are also important.<sup>41</sup> Procedural tax laws affect taxpayer compliance through the oversight of taxpayer noncompliance.<sup>42</sup> However, whereas the focus of substantive tax laws is on the conduct of taxpayers, procedural tax laws look to the Service’s conduct as it relates to the enforcement of substantive law.<sup>43</sup> Procedural tax laws ensure due process,<sup>44</sup> allowing taxpayers to “tell their side of the story.”<sup>45</sup> If procedural tax laws go uncorrected, then taxpayers will not feel fairly treated. Unfair treatment, perceived or actual, causes decreased taxpayer compliance, one of the primary purposes of tax legislation.

This Note therefore proposes a new standard for evaluating tax legislation, holistic tax reform, to guard against future failure to consider the importance of procedural tax law. Holistic tax reform builds upon the

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<sup>36</sup> Johnson, *supra* note 33, at 10 n.20.

<sup>37</sup> *Id.*

<sup>38</sup> Steve R. Johnson, *The Taxpayer’s Duty of Consistency*, 46 TAX L. REV. 537, 545 (1991) (citation omitted).

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> Leandra Lederman & Stephen W. Mazza, *Addressing Imperfections in the Tax System: Procedural or Substantive Reform?*, 103 MICH. L. REV. 1423, 1442 (2005) (reviewing DAVID CAY JOHNSTON, *PERFECTLY LEGAL: THE COVERT CAMPAIGN TO RIG OUR TAX SYSTEM TO BENEFIT THE SUPER RICH—AND CHEAT EVERYBODY ELSE* (2003)).

<sup>42</sup> *Id.*

<sup>43</sup> *Id.* at 1443.

<sup>44</sup> Leandra Lederman, *Tax Compliance and the Reformed IRS*, 51 U. KAN. L. REV. 971, 991 (2003).

<sup>45</sup> *Id.* at 991 n.97 (citing Kent W. Smith, *Reciprocity and Fairness: Positive Incentives for Tax Compliance*, in *WHY PEOPLE PAY TAXES* 224 (Joel Slemrod ed., 1992)).

comprehensive standard to consider the extent of both substantive and procedural tax reform.<sup>46</sup> Legislation cannot satisfy the holistic tax reform standard if it does not make a meaningful attempt to reform both substantive and procedural deficiencies in the federal system of taxation.<sup>47</sup> The extensive modification of either substantive or procedural tax law should not justify the failure to consider the other category of tax law.<sup>48</sup>

“Reform” may be subjective, but there should be limits on how we classify this subjective activity. In order to provide a more complete analysis of tax legislation, a new evaluation standard—holistic reform—is proposed. Holistic tax reform is the attempt to improve both substantive and procedural tax laws. It is a higher standard than comprehensive reform, which only requires modification of one category of tax law. Applying the holistic evaluation standard to the TCJA allows an observer to identify the missing procedural aspect, which would have been the first step in proposing a more complete “reform.”

### III. THE TAX CUTS AND JOBS ACT

On December 22, 2017, President Trump signed the TCJA into law.<sup>49</sup> The TCJA made numerous changes to existing substantive tax laws.<sup>50</sup> The main intent of the legislation was to reduce the amount of taxes paid by Americans.<sup>51</sup> An ancillary purpose of the legislation was to limit deductions and credits.<sup>52</sup> Minimal attention was given to how the laws of taxation are procedurally applied.<sup>53</sup> Based upon the constructed definition of holistic

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<sup>46</sup> See Lederman & Mazza, *supra* note 41, at 1433 n.27 (quoting DAVID CAY JOHNSTON, PERFECTLY LEGAL: THE COVERT CAMPAIGN TO RIG OUR TAX SYSTEM TO BENEFIT THE SUPER RICH—AND CHEAT EVERYBODY ELSE 298 (2003)).

<sup>47</sup> See *id.* at 1444–45.

<sup>48</sup> See *id.*

<sup>49</sup> Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017).

<sup>50</sup> See *President’s Remarks*, *supra* note 27.

<sup>51</sup> *Id.*

<sup>52</sup> See *id.*

<sup>53</sup> Tax Cuts and Jobs Act § 11071(a), 131 Stat. at 2091 (codified at § 6343(b)) (extending the time to contest a levy from nine months to two years).

reform, tax legislation should attempt comprehensive modification of both the substantive and procedural aspects of taxation if it is to be called “tax reform.”<sup>54</sup> The TCJA does not satisfy this holistic tax reform evaluation standard.

I will discuss four notable ways, selected because of the significant implications on everyday taxpayers, in which the TCJA interacted with the substantive laws governing tax rates and tax credits. First, the TCJA widened the income amounts of most of the individual, joint, and head of household income tax brackets.<sup>55</sup> It also reduced the marginal tax rates applicable to many of the widened tax brackets.<sup>56</sup> Second, the TCJA reduced the maximum corporate tax rate from thirty-five percent to twenty-one percent.<sup>57</sup> Third, the TCJA doubled the amount of the child tax credit, and it increased the phase-out income amount from \$75,000 to \$200,000 for single filers and \$110,000 to \$400,000 for joint filers.<sup>58</sup> Fourth, and finally, the standard deduction was

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<sup>54</sup> Even when done separately, substantive and procedural reform is difficult. However, this Note would deny that difficulty is a valid justification. If simultaneous reform is too arduous for those who determine the laws that we live by, then how can we reasonably expect taxpayers to comply with these same laws?

<sup>55</sup> Tax Cuts and Jobs Act, Pub. L. No. 115-97, § 11001(a), 131 Stat. 2054, 2054–56 (2017) (codified at § 1(j)).

<sup>56</sup> *Id.*

<sup>57</sup> *Id.* § 13001(a), 131 Stat. at 2096 (codified at § 11(b)).

<sup>58</sup> *Id.* § 11022(a), 131 Stat. at 2073 (codified at § 24(h)(3)). The impact of an increased child tax credit is marginal. Under the new law, the credit is \$2,000 while the refundable portion of the credit is capped at \$1,400. *Id.* (codified at § 24(h)(2), (5)(A)). The TCJA eliminated the personal exemption deduction for dependents, which had permitted a \$4,050 deduction from adjusted gross income in 2017 for each dependent. *Id.* § 11041(a), 131 Stat. at 2082 (codified at § 151(d)(5)(A)); Rev. Proc. 2016-55, § 3.24(1), 2016-2 C.B. 713. Comparing credits to deductions is akin to comparing apples to oranges. However, even when comparing apples to oranges you can approximate the effect. Consider the following example of a single dependent exemption for married taxpayers filing jointly. Without accounting for other changes elsewhere in the TCJA, the tax implications vary depending on the income level of the taxpayers. Due to the loss of the dependent exemption, the value of the increased child tax credit is discounted. The TCJA gave with one hand and took with the other, and it is possible for the TCJA to take more than it gives.

doubled.<sup>59</sup> It was increased to \$12,000 for single filers, \$18,000 for head of households, and \$24,000 for joint filers.<sup>60</sup>

The TCJA also greatly limited, or eliminated, deductions associated with certain expenses. For example, deductions for state and local taxes are now capped at \$10,000 for single filers and joint filers and \$5,000 for married taxpayers filing separately.<sup>61</sup> Deductions for mortgage interest payments were also drastically changed.<sup>62</sup> Under the preexisting framework, interest payments on up to \$100,000 of home equity loan indebtedness were deductible.<sup>63</sup> From 2018 through 2025, interest on home equity loan indebtedness will not be deductible.<sup>64</sup> Acquisition indebtedness will still be deductible, but the principal amount of such indebtedness that will give rise

Adjusted Gross Income	2017 Child Tax Credit	2018 Child Tax Credit	Change in Child Tax Credit	2017 Single Dependent Exemption Value	2018 Single Dependent Exemption Value	Change in Exemption Value	TCJA's impact on Combined Value
\$50,000	\$1,000.00	\$2,000.00	\$1,000.00	\$607.50	0.00	(\$607.50)	\$392.50
\$100,000	\$1,000.00	\$2,000.00	\$1,000.00	\$1,012.50	0.00	(\$1,012.50)	(\$12.50)
\$200,000	0.00	\$2,000.00	\$2,000.00	\$1,134.00	0.00	(\$1,134.00)	\$866.00
\$440,000	0.00	0.00	0.00	0.00	0.00	0.00	0.00

<sup>59</sup> Tax Cuts and Jobs Act § 11021(a), 131 Stat. at 2072–73 (codified at § 63(c)(7)(A)(ii)). Analogous to the tempered helpfulness of a child tax credit absent a personal exemption deduction for dependents, the impact of an increased standard deduction is offset by the inability to use personal exemptions to exclude \$4,050 from gross income not only for dependents but also for the taxpayer(s). *Id.* § 11041(a), 131 Stat. at 2082 (codified at § 151(d)(5)(A)).

<sup>60</sup> *Id.* § 11021(a), 131 Stat. at 2072–73 (codified at § 63(c)(7)). Consider two married taxpayers filing jointly, the 2018 standard deduction was \$24,000 and the 2017 standard deduction was \$12,700. This represents a standard deduction increase of \$11,300. However, the TCJA prevented the claiming of personal deductions. The taxpayer's two personal exemptions excluded \$8,100 from income in 2017 but none in 2018. Thus, specific to married taxpayers filing jointly and utilizing the standard deduction, the TCJA only caused \$3,200 of additional income to be excluded in 2018. The value of the expanded standard deduction was discounted by roughly seventy-one percent, due to the loss of the personal exemptions. Again, the TCJA gave with one hand while taking with the other.

<sup>61</sup> The state and local taxes that can give rise to federal deductions are real estate taxes, personal property taxes, sales taxes, and income taxes. *Id.* § 11042(a), 131 Stat. at 2085–86 (codified at § 164(b)(6)(B)).

<sup>62</sup> *See id.* § 11043(a), 131 Stat. at 2086 (codified at § 163(h)(3)(F)(i)(I)–(II)).

<sup>63</sup> I.R.C. § 163(h)(3)(C). Home equity interest refers to loans that are secured by a qualified residence, but where the loan proceeds were not used to acquire or substantially improve the property.

<sup>64</sup> Tax Cuts and Jobs Act, § 11043(a), 131 Stat. at 2086 (codified at § 163(h)(3)(F)(i)(I)).

to deductible interest was reduced from \$1,000,000 to \$750,000 during that same period.<sup>65</sup>

Miscellaneous itemized deductions are disallowed under the TCJA from 2018 through 2025.<sup>66</sup> Moving expenses, under the TCJA, are generally no longer deductible.<sup>67</sup> Similarly, alimony payments will no longer give rise to federal deductions by the payor or be includible in the income of the payee.<sup>68</sup> The TCJA will cap business interest payment deductions at either the business interest income or thirty percent of the adjusted income.<sup>69</sup> The provided information on tax rates, credits, and deductions is not intended to be inclusive of all of the TCJA's substantive law modifications. Rather, the intention, specifically as it relates to everyday taxpayers, is to exhibit the extent of the overwhelming focus of the TCJA on substantive, as opposed to procedural, tax law.

A single section, ten lines of the 185-page law, directly addressed the procedural application of taxation.<sup>70</sup> The single section increased, from nine months to two years, the amount of time that a taxpayer has to contest a levy.<sup>71</sup> This section does not address any other procedural issues that influence the enforcement of tax laws. Given the volume and scope of the substantive changes, this single alteration to levies does not represent meaningful congressional attention on procedural tax laws.

The TCJA's failure to address procedural deficiencies is not surprising. President Trump's earlier actions on tax reform also neglected procedural tax law.<sup>72</sup> For example, on April 21, 2017, President Trump issued Executive

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<sup>65</sup> *Id.* Home acquisition indebtedness refers to loans where the loan proceeds are used to either acquire or substantially improve a qualified residence.

<sup>66</sup> *Id.* § 11045(a), 131 Stat. at 2088 (codified at § 67(g)).

<sup>67</sup> *Id.* § 11049(a), 131 Stat. at 2088–89 (codified at § 217(k)). At the federal level, active members of the Armed Forces, and qualifying family members, might still be eligible to deduct nonreimbursed moving expenses. I.R.S. Pub. No. 521, Moving Expenses 2–4 (2018).

<sup>68</sup> Tax Cuts and Jobs Act, § 11051(a), 131 Stat. at 2089 (repeal of §§ 71, 215).

<sup>69</sup> *Id.* § 13301(a), 131 Stat. at 2117 (codified at § 163(j)(1)).

<sup>70</sup> *Id.* § 11071(a), 131 Stat. at 2091–92 (codified at § 6343(b)).

<sup>71</sup> *Id.*

<sup>72</sup> See, e.g., Exec. Order No. 13789, 82 Fed. Reg. 19,317 (Apr. 21, 2017).

Order 13,789.<sup>73</sup> This executive order tasked the Department of Treasury with locating tax regulations that “(i) impose an undue financial burden on United States taxpayers, (ii) add undue complexity to the Federal tax laws; or (iii) exceed the statutory authority of the Internal Revenue Service.”<sup>74</sup> The Department of Treasury issued two reports in response to Executive Order 13,789.<sup>75</sup> The reports recommended eight changes to the regulations.

Recommendation One proposed the complete withdrawal of “[p]roposed regulations, [that] through a web of dense rules and definitions, would have narrowed longstanding exceptions and dramatically expanded the class of restrictions that are disregarded under . . . the valuation, for wealth transfer tax purposes, of interests in family-controlled entities.”<sup>76</sup> Recommendation Two proposed the complete withdrawal of temporary regulations that limited the exclusion of state and local bond interest from a taxpayer’s gross income based upon the bond provider’s characteristics.<sup>77</sup>

Recommendation Three proposed the partial revocation of regulations that allowed the Service to “farm out” an audit to private contractors.<sup>78</sup> While accepting that an audit should not be shifted to nongovernmental accountants and lawyers, the Service retained the right to employ subject matter experts in complex litigation.<sup>79</sup> The Service indicated that it would not regularly retain private contractors, and when private contractors are utilized they will have a relatively minimal role.<sup>80</sup>

Recommendation Four proposed the partial repeal of temporary and permanent regulations on partnership allocation of liabilities in disguised

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<sup>73</sup> *Id.* (the Executive Order is titled “Identifying and Reducing Tax Regulatory Burdens”).

<sup>74</sup> *Id.*

<sup>75</sup> The two reports are substantively identical. The first was an interim report. I.R.S. Notice 2017-38, 2017-30 I.R.B. 174. The Secretary, in the second report, recommends the adoption of the initial report. Executive Order 13,789—Second Report to the President on Identifying and Reducing Tax Regulatory Burdens, 82 Fed. Reg. 48,013, 48,013 (Oct. 16, 2017) [hereinafter Second Report].

<sup>76</sup> Second Report, 82 Fed. Reg. at 48,013.

<sup>77</sup> *Id.* at 48,015.

<sup>78</sup> *Id.*

<sup>79</sup> *Id.* at 48,016.

<sup>80</sup> *See id.*

sales and on when it is necessary for a partnership to take into account the economic risk of a recourse liability.<sup>81</sup> Recommendation Five proposed the partial repeal of regulations that “address[ed] the classification of related-party debt as debt or equity for U.S. federal income tax purposes.”<sup>82</sup>

Recommendation Six called for the substantial revision of regulations to authorize an exception to taxpayers’ recognition of income from the transfer of tangible and intangible property to foreign corporations.<sup>83</sup> Recommendation Seven states that the regulation that causes C corporations to recognize gain upon transfers to REITs and RICs should be amended to lower the gain amounts.<sup>84</sup> Finally, Recommendation Eight states that the Service will revise how taxpayers calculate gain and loss on foreign currency translation.<sup>85</sup>

Only one of these recommendations, Recommendation Three, addressed the procedural aspects of tax compliance.<sup>86</sup> Moreover, the TCJA made no reference to this sole procedural deficiency identified six months prior to the Act’s enactment. Rather, independent from legislative oversight, the Service proposed new regulations.<sup>87</sup>

The substantive nature of the TCJA is self-evident. Excluding a single section of the Act, each change could be described as either the widening or restriction of preexisting substantive tax law. The TCJA did not meaningfully attempt to improve the procedural aspects of federal taxation. To reiterate, the new evaluation standard for tax legislation, holistic reform, would separately consider substantive and procedural tax reform. Therefore, while the TCJA made significant substantive adjustments to the federal tax system, the legislation was not holistic reform due to its procedural shortcomings.

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<sup>81</sup> *Id.*

<sup>82</sup> *Id.*

<sup>83</sup> *Id.* at 48,017.

<sup>84</sup> *Id.*

<sup>85</sup> *Id.* at 48,018.

<sup>86</sup> *See id.* at 48,015–16.

<sup>87</sup> Certain Non-Government Attorneys Not Authorized to Participate in Examinations of Books and Witnesses as a Section 6103(n) Contractor, Prop. Treas. Reg. § 301.7602-1, 2018-16 I.R.B. 503, 506.

There is no need to look far to locate an example of procedural tax reform, which is the missing element of the TCJA.

#### IV. THE BIPARTISAN BUDGET ACT OF 2015

One example of an effort to address procedural reform through legislation is the BBA.<sup>88</sup> The BBA reformed the procedural laws governing partnership examinations.<sup>89</sup> The specific methods of partnership procedural simplification are not applicable to other entity types.<sup>90</sup> Nevertheless, the BBA could serve as the inspiration to rectify counterproductive behavior produced by procedural requirements.

To understand the BBA, one should first start with the procedural laws for partnership taxation prior to the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA).<sup>91</sup> Prior to TEFRA, there was no mechanism for consolidating the tax proceedings of a partnership.<sup>92</sup> The assessment, administrative adjudication, and legal proceedings took place at the partner-level, not the entity-level.<sup>93</sup> To correct the tax liability of a partnership, each partner would require separate examination, administrative review, and court order.<sup>94</sup> A partnership of fifteen individuals might not unnecessarily burden the Service, but a partnership of over a hundred was a logistical quagmire.<sup>95</sup>

TEFRA was intended to reduce the administrative burden of partner-level corrections by shifting the focus to the entity that gave rise to the error.<sup>96</sup> The application of TEFRA did not, however, produce the intended result of

<sup>88</sup> Bipartisan Budget Act of 2015, Pub. L. No. 114-74, 129 Stat. 584.

<sup>89</sup> See Hauswirth et al., *supra* note 5.

<sup>90</sup> *Id.*

<sup>91</sup> Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324.

<sup>92</sup> I.R.S. Pub. No. 541, Partnerships 13 (2016).

<sup>93</sup> *Id.*

<sup>94</sup> *Id.*

<sup>95</sup> See Josh Ungerman, *TEFRA Partnership IRS Controversies: Now That the TEFRA Partnership Exam Is Complete with an FPPA, What Is a Partnership to Do?*, FORBES (July 22, 2013, 2:18 AM), <https://www.forbes.com/sites/irswatch/2013/07/22/tefra-partnership-irs-controversies-now-that-the-tefra-partnership-exam-is-complete-with-an-fppa-what-is-a-partnership-to-do/>.

<sup>96</sup> I.R.S. Pub. No. 541, Partnerships 13 (2016).

simplified governmental review of partnerships.<sup>97</sup> Under TEFRA, the examination, administrative adjudication, and some of the legal proceedings took place at the entity-level.<sup>98</sup> However, to collect on the tax adjustment, the Service needed to initiate separate partner-level proceedings.<sup>99</sup> Individual partners could then challenge their tax adjustments by arguing that the Service failed to provide them with information and notices applicable to the entity-level proceeding.<sup>100</sup> The entity-level proceedings did not eliminate the necessity of partner-level proceedings, and thus the Service's administrative burden was not meaningfully reduced.<sup>101</sup>

The BBA, in an effort to address this issue, revamped the procedural laws that govern partnership examinations and tax proceedings.<sup>102</sup> Partnerships of one hundred individuals or fewer can elect to be governed by the laws of individual examination and adjustment.<sup>103</sup> Partnerships that do not elect out, or are comprised of more than one hundred partners, have entity-level examination and adjustment.<sup>104</sup> Each partnership is required to designate a person, whether a partner or a nonpartner with substantial presence within the United States, to act on behalf of the partnership in interactions with the Service.<sup>105</sup> If the partnership fails to appoint a representative, then the Service is empowered to appoint a partnership representative.<sup>106</sup>

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<sup>97</sup> *Id.*

<sup>98</sup> Jennifer Villier, *Update: Partnership Audit Proceedings, Post-TEFRA*, WEALTH COUNSEL (Feb. 15, 2016, 5:00 AM), <https://info.wealthcounsel.com/blog/update-partnership-audit-proceedings-post-tefra> [<https://web.archive.org/web/20180810121027/https://info.wealthcounsel.com/blog/update-partnership-audit-proceedings-post-tefra>].

<sup>99</sup> *Id.*

<sup>100</sup> See Hauswirth et al., *supra* note 5.

<sup>101</sup> See *id.*

<sup>102</sup> *Id.*

<sup>103</sup> *Bloomberg BNA Analysis of the Bipartisan Budget Act of 2015*, BLOOMBERG (Oct. 30, 2015), <https://www.bna.com/bloomberg-bna-analysis-n57982062926/>.

<sup>104</sup> *Id.*

<sup>105</sup> Bipartisan Budget Act of 2015, Pub. L. No. 114-74, § 6223(a), 129 Stat. 584, 627.

<sup>106</sup> *Id.*

Only the partnership representative has the authority to act on behalf of the entity.<sup>107</sup> Additionally, all of the entity's partners are bound by the actions of the partnership representative.<sup>108</sup> Individual partners are no longer entitled to statutory notices as they were under TEFRA.<sup>109</sup> The partnership representative, not the Service, is responsible for ensuring that each partner is sufficiently informed.<sup>110</sup>

Furthermore, the BBA went on to correct the mistakes of TEFRA by providing that “[a]ny adjustment . . . of a partnership . . . shall be assessed and collected . . . at the partnership level.”<sup>111</sup> The separate entity-level and partner-level proceedings under TEFRA were abandoned; the partnership as a collective is now responsible for correcting any deficiency.<sup>112</sup> In addition, the responsible partners are not those for the tax year under review but rather the partners when the review occurs.<sup>113</sup> The Service is still responsible for policing a partnership's compliance with the tax laws, but the internal behavior of the partnership is now outside of the Service's purview.<sup>114</sup>

The BBA was a correction to TEFRA. There now should be just one taxpayer per partnership examination. This change in procedural law eliminates significant administrative burdens that are not directly related to tax controversies.<sup>115</sup> Unfortunately, the BBA is not directly applicable to the procedural laws for individual examination and tax litigation.<sup>116</sup> However,

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<sup>107</sup> *Id.*

<sup>108</sup> *Id.*

<sup>109</sup> Thereby eliminating a potential argument to prevent partner-level adjustment despite a valid entity-level adjustment. *See* Hauswirth et al., *supra* note 5.

<sup>110</sup> Eliminating a second potential argument to prevent a partner-level adjustment despite a valid entity-level adjustment. *See id.*

<sup>111</sup> Bipartisan Budget Act of 2015 § 6221(a), 129 Stat. at 625; *see* Hauswirth et al., *supra* note 5.

<sup>112</sup> *Id.*; Hauswirth et al., *supra* note 5.

<sup>113</sup> Eliminating a third argument against partner-level adjustment despite valid entity-level adjustment: the inability to locate or enforce judgments against former, but not current, partners. Bipartisan Budget Act of 2015 § 6225(a)(1)–(2), 129 Stat. at 628.

<sup>114</sup> *See* Hauswirth et al., *supra* note 5.

<sup>115</sup> *See* Bipartisan Budget Act of 2015 § 6223(a), 129 Stat. at 627.

<sup>116</sup> *See* Hauswirth et al., *supra* note 5.

the BBA does provide useful guiding insight:<sup>117</sup> if procedural laws do not reinforce taxpayer compliance, then the laws are counterproductive and should be rewritten.

#### V. THE PROCEDURAL DEFICIENCY OF OFFER IN COMPROMISE

Offers in compromise exemplify federal tax procedure that was ripe for congressional intervention in 2017 and remains ripe for intervention now. The offer in compromise process allows the Service and taxpayers to reach administrative settlements.<sup>118</sup> Congress delegated authority to the Secretary of Treasury to determine whether offers in compromise are adequate.<sup>119</sup> To assist with this determination, congress mandated that the Secretary of Treasury develop national and local allowances to allow taxpayers to cover basic living expenses.<sup>120</sup> An unintended result of the procedures for offers in compromise is that, like the TERA rules for partnerships, they are procedurally counterproductive.<sup>121</sup>

Section 7122 of the Code creates the current process that allows taxpayers to reach administrative compromises with the Service.<sup>122</sup> The Service cannot make the offer; the offer must come from the taxpayer.<sup>123</sup> The Service has the ability to accept or decline the taxpayer's offer.<sup>124</sup> The compromise can relate to any civil or criminal tax case.<sup>125</sup> Additionally, the

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<sup>117</sup> This Note is attempting to advance how we evaluate tax legislation. This is similar to, but distinct from, questioning whether legislation produces the intended results. Therefore, the implementation problems associated with the Bipartisan Budget Act of 2015 are outside of the current scope of discussion.

<sup>118</sup> See I.R.C. § 7122.

<sup>119</sup> *Id.* § 7122(d)(1).

<sup>120</sup> *Id.* § 7122(d)(2)(A).

<sup>121</sup> See McKenzie, *supra* note 7.

<sup>122</sup> I.R.C. § 7122(a). While the offer in compromise process has existed for roughly twenty years, the Secretary's ability to compromise dates back to at least 1868. *E.g.*, T.D. 8829, 1999-32 C.B. 235-37.

<sup>123</sup> I.R.C. § 7122(d)(1).

<sup>124</sup> See *id.*

<sup>125</sup> See *id.* § 7122(a).

terms of the compromise can set the amount of tax liability, interest, and penalties owed by the taxpayer to the federal government.<sup>126</sup>

Congress delegated authority to the Secretary of Treasury to determine if administrative compromise is acceptable.<sup>127</sup> However, Congress also required that the Secretary “publish schedules of national and local allowances designed to provide . . . taxpayers entering into a compromise [with] adequate means to provide for basic living expenses.”<sup>128</sup> The schedules exclude assets from the assessment of whether a taxpayer can pay the full amount due. Congress does not expect a taxpayer to fully pay outstanding taxes, interest, or penalties if it would cause a taxpayer to be unable to cover basic living expenses.<sup>129</sup>

The national and local allowances cover monthly expenses. There are two types of national allowances: (1) food, clothing, and other items;<sup>130</sup> and (2) healthcare.<sup>131</sup> The national allowance for food, clothing, and other items covers five sets of expenses: “food, housekeeping supplies, apparel and services, personal care products and services, and miscellaneous.”<sup>132</sup> Excluding miscellaneous expenses, the allowance for the other categories can potentially be increased if the taxpayer produces documentation that substantiates the necessity of the expense.<sup>133</sup> The amount of allowance is dependent on the size of the taxpayer’s family.<sup>134</sup> For a family size of one the total allowance is currently \$647, for a family of two it is \$1202, for a family

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<sup>126</sup> Treas. Reg. § 301.7122-1(a)(2) (2002).

<sup>127</sup> I.R.C. § 7122(d)(1).

<sup>128</sup> *Id.* § 7122(d)(2)(A).

<sup>129</sup> *Id.* § 7122(d)(2)(B).

<sup>130</sup> *National Standards: Food, Clothing and Other Items*, INTERNAL REVENUE SERV., <https://www.irs.gov/businesses/small-businesses-self-employed/national-standards-food-clothing-and-other-items> (last updated Mar. 26, 2018).

<sup>131</sup> *National Standards: Out-of-Pocket Health Care*, INTERNAL REVENUE SERV., <https://www.irs.gov/businesses/small-businesses-self-employed/national-standards-out-of-pocket-health-care> (last updated Feb. 28, 2019).

<sup>132</sup> *National Standards: Food, Clothing and Other Items*, *supra* note 130.

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

of three it is \$1384, for a family of four it is \$1694, and for each additional family member above four the allowance is increased by \$357.<sup>135</sup>

The second category of national expenses is healthcare.<sup>136</sup> The allowance is intended to cover out of pocket expenses such as “medical services, prescription drugs, and medical supplies.”<sup>137</sup> The allowance is not intended to cover the costs of elective cosmetic or dental procedures.<sup>138</sup> As with the allowance for food, clothing, and other items, taxpayers are entitled to the minimum allowance, but providing sufficient documentation establishing the necessity of the expense can increase the allowance.<sup>139</sup> Each member of the taxpayer’s family increases the allowance by \$52 if the family member is younger than sixty-five years old and \$114 if the family member is sixty-five years old or older.<sup>140</sup>

There are two types of local living expenses: “(1) housing and utilities and (2) transportation.”<sup>141</sup> Unlike the national allowances, taxpayers are allowed the lower of either the local standard or the amount paid by the taxpayer.<sup>142</sup> The local allowance for housing and utilities is intended to cover expenses such as monthly “mortgage or rent, property taxes, interest, insurance, maintenance, repairs, gas, electric, water, heating oil, garbage collection, residential telephone service, cell phone service, cable television, and Internet service.”<sup>143</sup> The specific amount of the local allowance for

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<sup>135</sup> *Id.* The Secretary provides the total allowance per family size and also the allowance for five different categories of expense. *Id.* The categories of expense are food, housekeeping supplies, apparel and services, personal care products and services, and miscellaneous. *Id.* Additionally, the Secretary’s table is somewhat illogical. For example, the housekeeping supply cost for two people is sixty-four dollars, whereas the housekeeping supply cost for three people is sixty-three dollars. *Id.*

<sup>136</sup> *National Standards: Out-of-Pocket Health Care*, *supra* note 131.

<sup>137</sup> *Id.*

<sup>138</sup> *Id.*

<sup>139</sup> *Id.*

<sup>140</sup> *Id.*

<sup>141</sup> Allowable Expense Overview, I.R.M. 5.15.1.8(5) (Aug. 29, 2018).

<sup>142</sup> *Id.*

<sup>143</sup> *Collection Financial Standards*, INTERNAL REVENUE SERV., <https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards> (last updated Feb. 28, 2019).

housing and utilities is dependent on the family size of the taxpayer and the specific county of residence.<sup>144</sup>

The second type of local allowance is transportation.<sup>145</sup> The allowance for transportation differentiates between taxpayers who use public transportation and those who own or lease vehicles.<sup>146</sup> Taxpayers who use public transportation are allowed a local allowance of \$178 per month.<sup>147</sup> Taxpayers who own or lease vehicles have the allowance subdivided into ownership costs and operating costs.<sup>148</sup> Ownership costs are the monthly lease or loan payments.<sup>149</sup> Operating costs are the expenses for “maintenance, repairs, insurance, fuel, registrations, licenses, inspections, parking and tolls.”<sup>150</sup> The allowable amount for ownership costs is \$497 for one car and \$994 for two or more cars.<sup>151</sup> The specific amount of the allowance for vehicle operation costs is set by the number of vehicles—either one or two or more—and the taxpayer’s geographic location.<sup>152</sup>

The allowances are well intended, but their practical application produces four problems that distort the evaluation of offers in compromise. First, the permissible allowances are based on national or local averages. There is no attempt to compare the specific taxpayer’s pre- and

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<sup>144</sup> 2018 Allowable Living Expenses Household Standards, INTERNAL REVENUE SERV. (Mar. 26, 2018), [https://www.irs.gov/pub/irs-utl/all\\_states\\_housing\\_standards.pdf](https://www.irs.gov/pub/irs-utl/all_states_housing_standards.pdf). The potential family sizes are one, two, three, four, and five or more individuals. *Id.*

<sup>145</sup> *Local Standards: Transportation*, INTERNAL REVENUE SERV., <https://www.irs.gov/businesses/small-businesses-self-employed/local-standards-transportation> (last updated June 1, 2018).

<sup>146</sup> *Id.*

<sup>147</sup> *Id.* The local allowance for public transportation does not attempt to assess the costs specific to unique localities. *Id.*

<sup>148</sup> Allowable Expense Overview, I.R.M. 5.15.1.8(5)(b) (Aug. 29, 2018).

<sup>149</sup> *Local Standards: Transportation*, *supra* note 145. If a taxpayer owns a vehicle unencumbered by a lease or loan then the ownership allowance amount is zero dollars. *Id.*

<sup>150</sup> *Id.*

<sup>151</sup> *Id.* Like the allowance for public transportation, there is no attempt to match vehicle ownership costs to specific localities. The amount of the allowance is the same for every taxpayer. *Id.*

<sup>152</sup> *Id.* There are twenty-three metropolitan cities. If the taxpayer does not reside in a metropolitan city then the allowance is determined based on one of four geographic regions. *Id.*

postcompromise spending.<sup>153</sup> Second, and similarly, the amounts of the allowances are not linked to a taxpayer's income.<sup>154</sup> Just as a minimum-wage earner and a corporate executive could be expected to have dissimilar spending habits, two taxpayers of similar income amounts may also have dissimilar spending habits. The allowances do not fully capture a taxpayer's specific financial situation.<sup>155</sup>

Third, while the allowance amounts are updated, the Service does not regularly consider new types of allowances, such as potential allowances for retirement savings and childcare expenses.<sup>156</sup> Taxpayers who set aside retirement funds do not consider this action discretionary and feel punished for their responsible planning. Similarly, other taxpayers with childcare costs might be faced with an unsolvable dilemma: should future income be devoted to satisfying the tax controversy or childcare costs?

Fourth, and most importantly, the Service's evaluation procedures for offers in compromise are counterproductive.<sup>157</sup> As discussed below, the Service's denial of an administrative compromise, an offer in compromise, could be bypassed after additional resources are devoted during subsequent legal negotiations with Chief Counsel. There are three bases for administrative compromise: "doubt as to liability,"<sup>158</sup> "doubt as to

<sup>153</sup> *IRS Allowable Living Expense Standards Do Not Provide Taxpayers with a Sustainable Standard of Living*, TAXPAYER ADVOCATE SERV. (Aug. 2, 2017), <https://taxpayeradvocate.irs.gov/news/irs-allowable-living-expense-standards-do-not-provide-taxpayers-with-a-sustainable-standard-of-living> [hereinafter *Sustainable Standard of Living*]. Taxpayers may be shocked and confused when they learn that while Congress allows taxpayers to retain enough assets to cover basic living expenses, "basic living" is an objective rather than subjective standard. *Id.*

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

<sup>155</sup> *Id.* Furthermore, the failure to capture a taxpayer's specific financial situation is inconsistent with other aspects of tax law. For example, the income tax is a progressive tax and not a flat tax. Rather than equally distribute the collective tax liability, taxes are distributed based on one's specific situation. Kelly Phillips Erb, *Our Current Tax v. the Flat Tax v. the Fair Tax: What's the Difference?*, FORBES (Aug. 7, 2015, 10:16 AM), <https://www.forbes.com/sites/kellyphillipserb/2015/08/07/our-current-tax-v-the-flat-tax-v-the-fair-tax-whats-the-difference>.

<sup>156</sup> *Sustainable Standard of Living*, *supra* note 153.

<sup>157</sup> See McKenzie, *supra* note 7.

<sup>158</sup> Doubt as to Liability Offer in Compromise, I.R.M. 5.19.24 (Aug. 13, 2018); see Offers in Compromise and the Role of Counsel, I.R.M. 33.3.2.2(1)–(3) (Oct. 5, 2015); see also Review of Doubt as to Liability Offers, I.R.M. 33.3.2.3.1 (Aug. 11, 2004).

collectibility,”<sup>159</sup> and “effective tax administration.”<sup>160</sup> Doubt as to liability exists when there is a “genuine dispute” about the tax liability.<sup>161</sup> Any portion of the liability can be settled for less than the full amount if the Service determines that the taxpayer is *genuinely*, or *legitimately*, not liable for that portion of the deficiency.<sup>162</sup> In other words, the Service will make concessions when its original position lacked validity.<sup>163</sup> This decision does not create a boon for an affected taxpayer. The Service’s concession is limited to the approximation of the “amount the Service would expect to collect through litigation.”<sup>164</sup> It is possible for the larger controversy to proceed absent the specific issues in which the Service had untenable positions.<sup>165</sup>

Doubt as to collectibility occurs when the taxpayer’s income and assets are less than the full amount of the liability.<sup>166</sup> The Service does not wholly concede the tax liability.<sup>167</sup> Rather, doubt as to collectibility offers are acceptable if they approximate the amount that could be collected by another method.<sup>168</sup> On the one hand, the Service expects the taxpayer to satisfy as

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<sup>159</sup> Doubt as to Collectibility, I.R.M. 5.8.4.3 (Jan. 18, 2018); *see* Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.3.2 (Nov. 4, 2010).

<sup>160</sup> Effective Tax Administration, I.R.M. 5.8.11 (Aug. 5, 2015); *see* Review of Effective Tax Administration Offers, I.R.M. 33.3.2.3.3 (Nov. 4, 2010).

<sup>161</sup> DATL Acceptances, I.R.M. 5.19.24.17(1) (June 1, 2017) (emphasis added); *see* I.R.M. 33.3.2.3.1(1). It is worth noting that doubt as to liability is only applicable before a deficiency judgment. A court order inherently substantiates the existence of the liability. Thus, this basis for administrative settlement is inapplicable to taxpayers faced with collection actions or collection due process disputes. I.R.M. 5.19.24.17(1); *see* I.R.M. 33.3.2.3.1(1).

<sup>162</sup> Centralized Doubt as to Liability (DATL) Offers in Compromise, I.R.M. 5.19.24.2(1) (July 24, 2016); *see* I.R.M. 33.3.2.3.1.

<sup>163</sup> *See* I.R.M. 5.19.24.2(1); *see also* I.R.M. 33.3.2.3.1.

<sup>164</sup> I.R.M. 5.19.24.17(2); *see* I.R.M. 33.3.2.3.1(2).

<sup>165</sup> I.R.M. 5.19.24.17(2); *see* I.R.M. 33.3.2.3.1(2).

<sup>166</sup> Doubt as to Collectibility, I.R.M. 5.8.4.3(2) (Jan. 18, 2018); Components of Collectibility, I.R.M. 5.8.4.3.1(1) (Apr. 30, 2015); *see* Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.3.2(1) (Nov. 4, 2010).

<sup>167</sup> *See* I.R.M. 5.8.4.3(3); *see also* I.R.M. 33.3.2.3.2(2).

<sup>168</sup> I.R.M. 5.8.4.3(3); *see* I.R.M. 33.3.2.3.2(2).

much of the liability as possible.<sup>169</sup> On the other hand, taxpayers are not expected to willingly choose an outcome that skirts the razor's edge of insolvency.<sup>170</sup>

There are two types of situations that warrant administrative settlement based on effective tax administration. The first, is when the collection of the liability would create economic hardship as defined by Treasury regulation section 301.6343-1.<sup>171</sup> In other words, the national and local allowances are applied to the taxpayer's specific financial situation, and the results are then compared against the tax liability in dispute.<sup>172</sup>

Despite claiming to be a subjective standard, economic hardship is an objective standard set by the Service.<sup>173</sup> Economic hardship occurs when a taxpayer is unable to meet basic living expenses, but this definition does not take into account the specific taxpayer's prior standard of living.<sup>174</sup> While accepting that taxpayers should not be subsidized for living beyond their means, this Note questions what the phrase signifies. A single approach to economic hardship fails to distinguish between taxpayers with truly affluent standards of living and those taxpayers with the mere appearance of luxurious lifestyles. Taxpayers who devote assets to champagne and caviar are fundamentally different from those who have equity, in excess of the allowance limits, in the family home or retirement accounts accumulated through careful planning and sacrifice.

Second, administrative settlement based on effective tax administration is permissible if there is a "compelling public policy or equity consideration."<sup>175</sup> Administrative compromise of this nature requires that the taxpayer establish that the collection of the liability would undermine

<sup>169</sup> See I.R.M. 5.8.4.3(3); *see also* I.R.M. 33.3.2.3.2(2).

<sup>170</sup> See I.R.M. 5.8.4.3(3); *see also* I.R.M. 33.3.2.3.2(2).

<sup>171</sup> Economic Hardship, I.R.M. 5.8.11.2.1(1)–(2) (Aug. 5, 2015); *see* Review of Effective Tax Administration Offers, I.R.M. 33.3.2.3.3(1)(a) (Nov. 4, 2010).

<sup>172</sup> Treas. Reg. § 301.6343-1(b)(4) (1995).

<sup>173</sup> *Id.* Cf. I.R.M. 5.8.11.2.1(2); I.R.M. 33.3.2.3.3(2).

<sup>174</sup> Treas. Reg. § 301.6343-1(b)(4) (1995); I.R.M. 5.8.11.2.1(2); *see* I.R.M. 33.3.2.3.3(2).

<sup>175</sup> Public Policy or Equity Grounds, I.R.M. 5.8.11.2.2(2) (Aug. 5, 2015); *see* I.R.M. 33.3.2.3.3(1)(b).

confidence in the federal tax laws.<sup>176</sup> An example of effective tax administration, as justification for an administrative settlement, would be a taxpayer's paralysis after a motor vehicle accident.<sup>177</sup> The taxpayer would devote assets to future care, and the taxpayer is expected to be unable to earn future income.<sup>178</sup>

Ultimately, the Service mechanically evaluates offers in compromise. Doubt as to liability is dependent on the Service perceiving flaws in its position,<sup>179</sup> which is something the Service might not readily disclose to an affected taxpayer. Doubt as to collectibility, as a justification for administrative settlement, is only a stone's throw away from the requirement that a taxpayer accept financial ruin.<sup>180</sup> The taxpayer will need to satisfy as much of the full liability as possible. Few taxpayers would facilitate a reduction in their own standard of living. Effective tax administration as grounds for administrative settlement is predicated on either the taxpayer accepting a low standard of living or the Service accepting that its enforcement action would erode public trust in the federal tax laws.<sup>181</sup> It is expected that in relatively few circumstances would the Service deem that its enforcement action would erode public trust in the tax laws. Taken as a whole, offers in compromise are only likely to provide effective results for taxpayers in a few narrow circumstances.

In the initial tax deficiency dispute, when the taxpayer and the Service cannot reach an administrative resolution, the process typically progresses to litigation. Chief Counsel maintains the position that all cases suitable for

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<sup>176</sup> I.R.M. 5.8.11.2.2(2); see I.R.M. 33.3.2.3.3(3); see Treas. Reg. § 301.7122-1(c)(3)(iii) (2002).

<sup>177</sup> See David M. Fogel, *The "Effective Tax Administration" Offer in Compromise*, 108 TAX NOTES 1015, 1017 (2005).

<sup>178</sup> *Id.*

<sup>179</sup> See Centralized Doubt as to Liability (DATL) Offers in Compromise, I.R.M. 5.19.24.2(1) (July 14, 2016); see also DATL Acceptances, I.R.M. 5.19.24.17(1) (June 1, 2017); Review of Doubt as to Liability Offers, I.R.M. 33.3.2.3.1 (Aug. 11, 2004).

<sup>180</sup> See Components of Collectibility, I.R.M. 5.8.4.3.1(1) (Apr. 30, 2015); see also Doubt as to Collectibility, I.R.M. 5.8.4.3(2)–(3) (Jan. 18, 2018); Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.3.2(1)–(2) (Nov. 4, 2010).

<sup>181</sup> Fogel, *supra* note 177, at 1016; see *Offer in Compromise*, *supra* note 8.

settlement should be settled.<sup>182</sup> More specifically, and based on Executive Order 12,988, Chief Counsel's policy is to settle or eliminate as much of the tax controversy as possible.<sup>183</sup> One unresolved issue does not require the adjudication of all undisputed issues.<sup>184</sup> Litigation is limited as much as facts and circumstances allow.<sup>185</sup>

Nuisance, whether for or against the government, can never be the justification for a legal settlement with Chief Counsel.<sup>186</sup> Nuisance would prevent a taxpayer's request, unrelated to the merits of the controversy, to lower the deficiency amount.<sup>187</sup> For example, if a request to lower a tax deficiency were only based upon a taxpayer's attempt to "make a deal," then Chief Counsel would be obligated to reject that request.<sup>188</sup> Similarly, Chief Counsel's litigation hazards cannot be avoided by settling for less than the taxpayer's litigation costs, since such an attempt would be little more than a nuisance.<sup>189</sup>

Merit is the only basis on which Chief Counsel may settle issues and tax controversies.<sup>190</sup> A settlement on the merits requires the examination of "pertinent facts [to] applicable case law."<sup>191</sup> For example, a Chief Counsel attorney may agree to settle an early IRA distribution penalty after the taxpayer provides documentation that a qualifying deposit was made.

Field attorneys for Chief Counsel are instructed to be impartial regarding the parties; that is, they should neither automatically support the

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<sup>182</sup> Settlement Negotiations, I.R.M. 35.5.2.2(1) (Aug. 11, 2004).

<sup>183</sup> Principles of Litigation, I.R.M. 31.1.1.1.3(4) (Aug. 11, 2004).

<sup>184</sup> *Id.*

<sup>185</sup> *Id.*

<sup>186</sup> Settlement on the Merits, I.R.M. 35.5.2.4(2) (Dec. 31, 2012).

<sup>187</sup> Settlement Letters Content Format, I.R.M. 34.8.2.5.1(10) (Aug. 5, 2014).

<sup>188</sup> *Id.*

<sup>189</sup> *Id.*

<sup>190</sup> I.R.M. 35.5.2.4(1)-(3).

<sup>191</sup> Settlement Letters Content Scope, I.R.M. 34.8.2.4.1(1) (Aug. 11, 2004).

government nor the taxpayer.<sup>192</sup> Rather, field attorneys are expected to apply the true statutory meaning of the laws of taxation.<sup>193</sup> “We properly protect the revenue only when we ascertain and apply the true meaning of the statute.”<sup>194</sup> Thus, in their respective functions, Service employees and Chief Counsel attorneys have vastly different responsibilities and priorities.<sup>195</sup>

Unfortunately, a direct comparison of administrative and legal settlement outcomes is not possible. One’s ability to compare and contrast is dependent on the availability of information. Although the Service releases data for each fiscal year, the Service is selective in the types of information that it releases.<sup>196</sup> For offers in compromise, the Service discloses the approximate number of offer in compromise requests made by taxpayers, the number of offer in compromise requests that the Service accepted, and the approximate monetary total of accepted offers in compromise.<sup>197</sup> The Service does not disclose information related to the precompromise liability total of either accepted or rejected offers in compromise, and the Service does not disclose the monetary amount of rejected offers in compromise.<sup>198</sup>

The Service selectively provides information addressing Chief Counsel’s success.<sup>199</sup> The data addresses the number of cases received, the number of cases closed, the amount of tax and penalties in dispute, and the monetary judgment totals attributable to specific litigation outcomes.<sup>200</sup> The Service makes no attempt to distinguish outcomes based on determinative characteristics such as the type of tax controversy.<sup>201</sup> More problematic, the

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<sup>192</sup> General Principles for Handling Legal Work, I.R.M. 31.1.1.1(3) (Aug. 11, 2004).

<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

<sup>195</sup> *See, e.g.*, Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.2(3) (Nov. 4, 2010) (“Counsel must rely upon factual determinations made by the Service. These determinations should ordinarily not be reexamined by Counsel unless patently erroneous.”).

<sup>196</sup> INTERNAL REVENUE SERV., INTERNAL REVENUE SERVICE DATA BOOK: 2017 (2018).

<sup>197</sup> *Id.* at 39.

<sup>198</sup> *See id.*

<sup>199</sup> *See id.* at 62.

<sup>200</sup> *Id.*

<sup>201</sup> *See id.*

Service's data does not track the number of cases resolved through each type of identified litigation outcome.<sup>202</sup>

At best, a direct comparison of administrative and legal settlement outcomes would be the comparison of apples to oranges. On the one hand, there is information addressing the acceptance rate of offers in compromise.<sup>203</sup> On the other hand, there is information addressing how much of the legal judgment total is attributable specifically to settlements.<sup>204</sup> These two types of percentages are fundamentally dissimilar. Rather than engage in a flawed comparison, the data provided by the Service can be used to demonstrate something simple, yet important.

In 2017, taxpayers submitted approximately 62,000 offers in compromise, and the Service accepted roughly 25,000 offers while rejecting nearly 37,000 offers.<sup>205</sup> Chief Counsel opened 26,856 new Tax Court cases.<sup>206</sup> The total number of case openings includes all types of cases, not just the types applicable to offers in compromise.<sup>207</sup> However, this Note expects that the controversies behind an undefined number of rejected offers in compromise became tax litigation. No part of the *Internal Revenue Manual* or the 2017 *Internal Revenue Service Data Book* demonstrates that a tax controversy is treated differently after a failed offer in compromise. If Chief Counsel reaches a legal settlement after a failed administrative settlement, then that legal compromise is obtained after additional resources are devoted to that specific controversy. This would be counterproductive and represent a waste of resources.<sup>208</sup>

The administrative and legal compromise processes are fundamentally different from the appellate review of a particular controversy. While

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<sup>202</sup> *See id.*

<sup>203</sup> *Id.* at 39.

<sup>204</sup> *Id.* at 62.

<sup>205</sup> *Id.* at 39.

<sup>206</sup> *Id.* at 62.

<sup>207</sup> *Id.* at 62. Additionally, it would be expected that some of the rejected offers in compromise were resubmitted. *See id.* at 39, 62.

<sup>208</sup> The quantification of the amount of wasted resources requires information not provided by the Service, and the Service is the only available source for this information.

appellate outcomes change in accordance with the judicial application of fact to law, in the compromise processes, outcomes can change based on the Service's internal transfer of a specific controversy. The government's change in position should be linked to the development of the application of fact to law. This argument should neither be viewed as a suggestion that the government's position be static and unmoving, nor does this argument suggest that Chief Counsel be bound by prior administrative decisions.<sup>209</sup> Rather, the argument is that administrative decisions should attempt to mirror expected legal positions; the government should attempt to speak with a single voice.

In the respective administrative and legal phases, Service employees and Chief Counsel attorneys do not have identical priorities and abilities to act.<sup>210</sup> For better or worse, Chief Counsel attorneys are not bound by the congressionally mandated national and local cost-of-living allowances.<sup>211</sup> Additionally, the taxpayer's ability to pay and the corresponding collection potential are only considered in the administrative settlement process, not in the legal settlement process.<sup>212</sup> Moreover, the expectations for taxpayers are relaxed after the administrative settlement process.<sup>213</sup> Whereas taxpayers are required to present a genuine dispute of the liability in the administrative phase, legal settlement merely necessitates the application of fact to law.<sup>214</sup>

The increased governmental autonomy to enter into legal settlements means that taxpayers might bypass an administrative settlement denial.<sup>215</sup> This type of tax game erodes public trust in taxpayer compliance.<sup>216</sup>

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<sup>209</sup> See *IRS Frequently Asked Questions Can Be a Trap for the Unwary*, TAXPAYER ADVOCATE SERV. (July 26, 2017), <https://taxpayeradvocate.irs.gov/news/irs-frequently-asked-questions-can-be-a-trap-for-the-unwary> [hereinafter *Trap for the Unwary*].

<sup>210</sup> See *supra* note 195.

<sup>211</sup> *Trap for the Unwary*, *supra* note 209.

<sup>212</sup> See *Settlement on the Merits*, I.R.M. 35.5.2.4 (Dec. 31, 2012).

<sup>213</sup> See *Review of Doubt as to Liability Offers*, I.R.M. 33.3.2.3.1 (Aug. 11, 2004); see also *Review of Doubt as to Collectibility Offers*, I.R.M. 33.3.2.3.2; *Review of Effective Tax Administration Offers*, I.R.M. 33.3.2.3.3 (Nov. 4, 2010); I.R.M. 35.5.2.4.

<sup>214</sup> See I.R.M. 35.5.2.4(1)–(3).

<sup>215</sup> See I.R.M. 33.3.2.3.1; see also I.R.M. 33.3.2.3.2; I.R.M. 33.3.2.3.3; I.R.M. 35.5.2.4.

<sup>216</sup> See *Lederman & Mazza*, *supra* note 41, at 1442.

Procedural tax rules should reinforce taxpayer compliance by limiting the types of games that taxpayers can play.<sup>217</sup> Thus, the procedural deficiency afflicting offers in compromise is that it is possible, and expected, for legal settlements to grow out of failed administrative settlements. Compromise might be more easily obtained after additional resources are devoted to the tax controversy.

Taxpayers have a limited right to enter into compromises with the Service.<sup>218</sup> The current procedural laws and practices applied to offers in compromise result in more than half of the offers being rejected. There is an overwhelming likelihood, as the *Internal Revenue Service Data Book* for 2017 demonstrates, that some number of failed administrative settlements become legal settlements.<sup>219</sup> Regardless of the precise number of legal settlements that grow out of failed administrative settlements, § 7122 is procedurally inefficient. It does not facilitate compromise, and it does not ensure that compromises are fair to all parties. The administrative procedures for administrative compromise are bypassed by Chief Counsel's autonomy and its enhanced ability to enter into settlements. This problem can be rectified by relaxing the administrative standards for offers in compromise.

## VI. INVESTING IN THE INTERNAL REVENUE SERVICE

The TCJA could have employed two possible solutions to rectify the procedural problems associated with offers in compromise. Chief Counsel's ability to enter into legal settlements could be restricted. This approach is ill advised; it would not necessarily produce positive results. Maximizing tax liabilities would require the alteration of Chief Counsel's operating principles,<sup>220</sup> and there is no guaranteed payment of a maximized tax liability.

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<sup>217</sup> *See id.*

<sup>218</sup> *See* I.R.C. § 7122(a); *see also* I.R.M. 35.5.2.4.

<sup>219</sup> *See* INTERNAL REVENUE SERVICE, *supra* note 196, at 39, 62.

<sup>220</sup> General Principles for Handling Legal Work, I.R.M. 31.1.1.1(3) (Aug. 11, 2004) (“We properly protect the revenue only when we ascertain and apply the true meaning of the statute.”). This operating principle is important. It encapsulates the Service's unique role in safeguarding the lifeblood of the federal government: revenue. *Id.* This operating principle should be preserved. Moreover, I would argue that it should not be limited to Chief Counsel. Every Service interaction with taxpayers should be rooted in revenue protection and proper interpretation of laws and regulations.

Alternatively, the Service's evaluation standards for offers in compromise could be reevaluated. The 2012 Fresh Start Program loosened the evaluation procedures for offers in compromise.<sup>221</sup> However, it was not enough. In situations other than intentional noncompliance with the laws of taxation,<sup>222</sup> the Service should strive to reach settlements for the maximum amount possible. This solution would expand the Service's responsibilities. Accordingly, the Service would require additional staff, funding, and congressional support.<sup>223</sup>

A potential solution to correcting the procedural deficiencies for offers in compromise is to alter Chief Counsel's ability to enter into legal settlements. If the incongruence between legal and administrative settlements were eliminated, then the procedural laws would not benefit taxpayers who attempt to play tax games. But there are crippling flaws associated with this potential solution. Requiring that Chief Counsel place the maximization of tax liabilities above all else is incompatible with the current position that settlement is preferred over unnecessary adjudication.<sup>224</sup> Similarly, the solution would stand in direct contrast to the general principles that Chief Counsel operates under. Chief Counsel states that it will not "adopt a strained construction with the goal of maximizing revenue," and that it will only apply the true meaning of the Code.<sup>225</sup> There is no simple way of reconciling the maximization of tax liabilities with the current operating framework of the Chief Counsel's Office.

Additionally, the maximization of tax liabilities does not necessarily eliminate the underlying problem of additional expenditure of resources. The maximization of tax liabilities at the legal settlement phase should, at minimum, absorb the additional costs generated by the failure to reach earlier

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<sup>221</sup> McKenzie, *supra* note 7. The 2012 Fresh Start Program was a Service initiative to help struggling taxpayers resolve disputes. *E.g.*, Press Release, Internal Revenue Serv., IRS Offers New Penalty Relief and Expanded Installment Agreements to Taxpayers Under Expanded Fresh Start Initiative (Mar. 7, 2012), <https://www.irs.gov/newsroom/irs-offers-new-penalty-relief-and-expanded-installment-agreements-to-taxpayers-under-expanded-fresh-start-initiative>.

<sup>222</sup> Johnson, *supra* note 1, at 1059–60. "The Code recognizes that fraud is special, and it treats it more harshly than it treats mere mistake or negligence." *Id.* at 1060.

<sup>223</sup> *See id.* at 1013.

<sup>224</sup> *See* Settlement Negotiations, I.R.M. 35.5.2.2(1) (Aug. 11, 2004).

<sup>225</sup> I.R.M. 31.1.1.1(3).

administrative settlements. If the maximization of the tax liabilities is not equal to or more than the costs of continued tax enforcement, then the cost of collection increases.<sup>226</sup> As a matter of policy, tax compliance is more important than the cost of collection. However, as a business matter, a collection action that costs more than it generates is impractical. Maximizing tax liabilities creates a right to payment, not actual payment. Paper judgments do not fill coffers. There is no guarantee that the federal government will receive any part of a maximized tax liability.<sup>227</sup>

The better solution would be to reevaluate the Service's motivation when it evaluates offers in compromise. The 2012 Fresh Start Program made headway in counterbalancing against the motivation that maximizes tax liabilities. More specifically, it limited how the Service calculates the taxpayer's assets that could be used to pay the liability.<sup>228</sup> The 2012 Fresh Start Program altered how future income is calculated, and it also required that taxpayers be left with sufficient assets to repay student loans and unpaid state and local taxes.<sup>229</sup> Additionally, the Service, as a result of permanent changes made to administrative procedures by the 2012 Fresh Start Program, excludes \$1000 of liquid assets and \$3450 of equity in motor vehicles from the determination of the taxpayer's total assets.<sup>230</sup>

The 2012 Fresh Start Program helped, but it did not go far enough. The program only addressed doubt as to collectibility, one of the three possible bases for offers in compromise. The different standards of evaluation

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<sup>226</sup> Currently, the Service spends thirty-four cents to collect one hundred dollars of taxes. INTERNAL REVENUE SERV., *supra* note 196, at 63.

<sup>227</sup> Maximizing paper judgments is not practical from a business perspective. But from a policy perspective there are some benefits to maximizing judgment amounts. It communicates to taxpayers that their compliance obligations are not discretionary. Additionally, it can be used to indicate the types of issues that Chief Counsel is likely to challenge and refuse to concede. These policy considerations are valid; however, I would argue that the Service already communicates this information through the Internal Revenue Manual and publications. *E.g.*, Identification of Frivolous Submissions, I.R.M. 25.25.10.2 (Sept. 15, 2017). Taxpayer's lack of knowledge, or refusal to comply, is not remedied through more information. I would argue that these policy implications are properly addressed through alternative methods of communication, not liability maximization.

<sup>228</sup> McKenzie, *supra* note 7.

<sup>229</sup> *Id.*

<sup>230</sup> *Id.*

between legal settlement and administrative settlement, based on doubt as to liability, remained unchanged. Legal settlements still require the application of fact to law and administrative settlements require that the taxpayer present a genuine dispute of the tax controversy. Similarly, the 2012 Fresh Start Program made no attempt to alter how effective tax administration offer in compromise requests are evaluated.<sup>231</sup> Moreover, the Service's evaluation of doubt as to collectibility offers in compromise is still the maximization of the tax liability amount.

The Service's motivation when evaluating offers in compromise should be the maximization of the settlement amount. The Service should not employ a one-size-fits-all approach to offers in compromise. The Service would not be obliged to agree to offers in compromise that are insufficient. Beyond ensuring that taxpayers do not intentionally violate the tax laws, the question should be: will the settlement decision produce more revenue—that the federal government is correctly entitled to and will actually receive—than nonsettlement? Therefore, Congress should enact legislation similar to the following.<sup>232</sup>

#### **SEC. 1. MODIFIED BASES OF ADMINISTRATIVE SETTLEMENT.**

(a) IN GENERAL.—Section 7122 is amended by inserting after (g) the following new paragraphs:

(h) When the basis of administrative settlement is doubt as to liability, the Service shall employ the evaluation standard used in the expected type of litigation and court system.

(1) The Service properly protects the revenue by ascertaining and applying the true meaning of federal tax laws.

(A) The Service's position shall be based on pertinent fact applied to relevant laws, regulations, and legal precedent.

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<sup>231</sup> See McKenzie, *supra* note 7.

<sup>232</sup> Some may argue that the proposed language is too ambitious. There is some validity to this concern. However, taxpayers are entitled to fair proceedings, both administrative and legal. Simply put, if the proposed language is truly too ambitious, then what basis is there to infer that taxpayers currently receive fair proceedings?

(i) When the basis of administrative settlement is doubt as to collectibility, the Service must safeguard the revenue.

(1) In situations other than intentional tax noncompliance, the Service shall attempt to reach settlements for the maximum amount possible.

(2) The Secretary shall develop and utilize internal standards for evaluating a taxpayer's unique circumstances.

(j) Effective tax administration:

(1) When the basis of administrative compromise is economic hardship, the Service shall exclude from consideration assets shielded under the doubt as to collectability administrative compromise standard.

(2) Compelling public policy or equity consideration—  
The Secretary shall publish:

(A) Examples of situations giving rise to the public policy or equity grounds of administrative compromise.

(i) A taxpayer may argue for public policy or equity compromise based on a situation not contained in the Secretary's published list.

(B) Examples of situations that cannot give rise to the public policy or equity grounds of administrative compromise.

(i) There is a rebuttable presumption that the examples included in this list fail to establish the public policy or equity grounds of administrative compromise.

To be capable of appropriate review of offers in compromise, the Service should be appropriately funded and staffed.<sup>233</sup> However, since 2010,

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<sup>233</sup> See Johnson, *supra* note 1, at 1013.

17%, or \$2,400,000,000, has been cut from the Service's annual budget.<sup>234</sup> As a result of underfunding, the Service is forced to limit training and the size of its workforce.<sup>235</sup> The number of enforcement staff has declined by 23% and the number of employees has declined by 14%.<sup>236</sup> If the Service is to adequately apply the discretion afforded by congress, then the Service should be appropriately funded and staffed.<sup>237</sup> It is imprudent to expand responsibilities absent the resources necessary for satisfactory performance.

The TCJA could have rectified the procedural problems associated with offers in compromise by either altering legal or administrative settlements. Chief Counsel's ability to enter into legal settlements could be restricted to situations in which the tax liability is maximized. This approach is not advised. Maximizing tax liabilities is inconsistent with the operating principles of Chief Counsel. Furthermore, maximizing the amount of tax liabilities does not guarantee that the amounts will ever be paid. The better solution would be to change how the Service evaluates offers in compromise. In situations other than intentional noncompliance with the tax laws, the motivation should be to maximize the settlement amount. This would require additional employees and increased employee expertise. To be capable of satisfactorily executing the discretion afforded by congress, the Service should be appropriately funded and staffed.<sup>238</sup> In the absence of appropriate funding, and the corresponding diminished workforce size, the procedural enforcement of substantive tax laws will be lacking.

## VII. CONCLUSION

The Republican Party leadership's approach to tax reform was based on expanding the tax base, eliminating loopholes, and stimulating the

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<sup>234</sup> Chuck Marr & Cecile Murray, *IRS Funding Cuts Compromise Taxpayer Service and Weaken Enforcement*, CTR. ON BUDGET & POLICY PRIORITIES, <https://www.cbpp.org/research/federal-tax/irs-funding-cuts-compromise-taxpayer-service-and-weaken-enforcement> (last updated Apr. 4, 2016).

<sup>235</sup> *Id.*

<sup>236</sup> *Id.* The enforcement staff size decreased by nearly 12,000 employees, and the overall size of the workforce has decreased by 13,000 employees. *Id.*

<sup>237</sup> See Johnson, *supra* note 1, at 1013.

<sup>238</sup> *Id.*

economy.<sup>239</sup> This approach only implicates substantive tax laws. The other type of tax law, procedural tax law, was an afterthought. Substantive tax laws determine the amount of a taxpayer's liability and procedural laws govern how the taxpayer and the Service resolve disagreements about this liability amount.<sup>240</sup>

Accordingly, this Note proposed a new evaluation standard, holistic reform, to improve the analysis of tax legislation. This new standard of holistic evaluation builds upon the comprehensiveness evaluation standard. Tax legislation may be holistic if it is a meaningful attempt to alter both substantive and procedural tax laws. Holistic reform is a higher standard than comprehensive reform.

As discussed above,<sup>241</sup> the TCJA made numerous, and sometimes far-reaching, changes to the system of taxation. However, the legislation almost exclusively addressed substantive aspects of taxation such as tax rates, deductions, credits, and the like.<sup>242</sup> The heavy focus on substantive law was not complemented by a meaningful attempt to improve the procedural enforcement of tax laws. "Reform" is in the eye of the beholder. However, every modification to a preexisting system does not inherently amount to reform. "Reform" ought to meet a higher standard.

The BBA was a legislative attempt to address procedural deficiencies in the federal system of taxation. Before the BBA there was TEFRA, which was an attempt to create partnership-level examination and adjustment.<sup>243</sup> TEFRA's procedural laws prevented the realization of this intent;<sup>244</sup> it required entity-level and then partner-level adjudication.<sup>245</sup> The BBA

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<sup>239</sup> See, e.g., Press Release, *supra* note 2.

<sup>240</sup> *Id.* at 1013 n.1.

<sup>241</sup> See *supra* Part III.

<sup>242</sup> Tax Cuts and Jobs Act, Pub. L. No. 115-97, §§ 11001, 11021, 11022, 11041, 11042, 11043, 11045, 11049, 131 Stat. 2054, 2054-56, 2072-73, 2082, 2085-86, 2088-89 (2017). There was a single section, ten lines of the 185-page document, which was procedural. *Id.* § 11071(a), 131 Stat. at 2091 (codified at § 6343(b)). This section altered the time length to contest a levy. *Id.*

<sup>243</sup> I.R.S. Pub. No. 541, Partnerships 13 (2016).

<sup>244</sup> Villier, *supra* note 98.

<sup>245</sup> *Id.*

corrected redundant and wasteful procedural requirements.<sup>246</sup> Under the BBA, partnership examinations and adjustments only occur at the entity-level, not the partner-level.<sup>247</sup>

The BBA might have served as the inspiration for the TCJA to identify and address other procedural deficiencies, such as those associated with offers in compromise. Offers in compromise are the administrative settlement process used by many different types of taxpayers.<sup>248</sup> Congress delegated authority to the Secretary of Treasury to determine whether offers in compromise are adequate.<sup>249</sup> Service employees have different priorities and abilities than Chief Counsel attorneys.<sup>250</sup> In the administrative settlement process with the Service, outside of the merits of the controversy, there is only a perfunctory attempt to consider the taxpayer's specific circumstances when evaluating doubt as to collectibility in offers in compromise.<sup>251</sup>

Regarding the merits of the controversy, the government's expectations are markedly different between legal and administrative settlements.<sup>252</sup> For an administrative settlement based on doubt as to liability, the taxpayer must genuinely or legitimately not be liable for the underlying portion of the deficiency.<sup>253</sup> For legal settlements, the application of fact to law should merely favor the taxpayer.<sup>254</sup> Thus, the government's expectations are markedly different between legal and administrative settlements, and this

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<sup>246</sup> Bipartisan Budget Act of 2015, Pub. L. No. 114-74, § 6221(a), 129 Stat. 584, 625–26.

<sup>247</sup> Hauswirth et al., *supra* note 5.

<sup>248</sup> I.R.C. § 7122.

<sup>249</sup> *Id.* § 7122(d).

<sup>250</sup> *See, e.g.*, Offers in Compromise and the Role of Counsel, I.R.M. 33.3.2.2(3) (Oct. 5, 2015) (“Counsel must rely upon factual determinations made by the Service. These determinations should ordinarily not be reexamined by Counsel unless patently erroneous.”).

<sup>251</sup> *See* Doubt as to Collectibility, I.R.M. 5.8.4.3 (Jan. 18, 2018); *see also* Review of Doubt as to Collectibility Offers, I.R.M. 33.3.2.3.2 (Nov. 4, 2010).

<sup>252</sup> *See* Doubt as to Liability Offer in Compromise, I.R.M. 5.19.24 (Aug. 13, 2018); *see also* Offers in Compromise and the Role of Counsel, I.R.M. 33.3.2.2(1)–(3) (Oct. 5, 2015); Review of Doubt as to Liability Offers, I.R.M. 33.3.2.3.1 (Aug. 11, 2004); Settlement on the Merits, I.R.M. 35.5.2.4 (Dec. 31, 2012).

<sup>253</sup> *See* I.R.M. 5.19.24; *see also* I.R.M. 33.3.2.2(1)–(3); I.R.M. 33.3.2.3.1.

<sup>254</sup> Settlement Letters Content Scope, I.R.M. 34.8.2.4.1(1) (Aug. 11, 2004); *see* I.R.M. 35.5.2.4.

breeds conflict and inefficiency. Finally, the Service rarely accepts offers in compromise based on effective tax administration.<sup>255</sup>

It is procedurally inefficient to make settlements easier to obtain after additional resources are devoted to the controversy. The TCJA could have made administrative and legal settlements equally obtainable. Either the ability to enter into legal settlements could be limited, or the ability to enter into administrative settlements could be expanded. Restricting legal settlements is not advisable. It would require the alteration of Chief Counsel's governing principle that prioritizes correct tax law interpretation over tax liability maximization.<sup>256</sup> This is ill-advised given both Chief Counsel's position in the Service, and the Service's unique role in society. Additionally, maximizing tax liabilities would be impractical if it does not produce enough revenue to offset the additional cost of revenue production. Maximizing tax liabilities produces paper judgments that are mere legal rights to payment. It does not inherently ensure payment of any judgment. Maximizing tax liabilities is thus not a viable motivation for either legal or administrative settlements.

The better solution, consistent with a holistic approach to tax reform, would be to alter the Service's motivation when it evaluates offers in compromise. Beyond preventing intentional noncompliance with tax laws,<sup>257</sup> the motivation should be to maximize the amounts of settlements. This would increase the Service's workload and the expertise required of Service employees. As a result, the Service should concomitantly receive appropriate funding to allow for increased training and employment.<sup>258</sup>

Yes, the TCJA "broaden[ed] the tax base, clos[ed] loopholes and [grew] the economy."<sup>259</sup> However, under the proposed holistic tax reform evaluation standard, substantive and procedural laws do not exist in isolation; reform of one should coincide with that of the other. The TCJA fails to satisfy the

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<sup>255</sup> See Fogel, *supra* note 177, at 1018.

<sup>256</sup> See *supra* note 220 and accompanying text.

<sup>257</sup> See *supra* note 222.

<sup>258</sup> See Johnson, *supra* note 1, at 1013.

<sup>259</sup> See, e.g., Press Release, *supra* note 2.

holistic reform standard, due to the missing procedural law focus. “Reform” may be subjective. At the same time, there should be limits on subjectivity. Sometimes, legislation, such as the TCJA, is better referred to as a modification, not as reform. Tax legislation should not merely “broaden[] the tax base, clos[e] loopholes, and [stimulate] the economy,”<sup>260</sup> the legislation should also be holistic tax reform.

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<sup>260</sup> *Id.*