The President's Power To Tax

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Existing statutes give the President and his Treasury Department broad authority to implement important elements of the administration's tax agenda without further congressional action. And yet only occasionally does the Executive Branch exercise this statutory "power to tax." Instead, the President often asks Congress to pass revenue-raising measures achieving what the President and his Treasury Department already could accomplish on their own. And even when Congress rebuffs the President's request, past administrations only rarely have responded by exercising the regulatory authority they already possess. All the while, past Presidents have stretched the limits of executive authority in a taxpayer-friendly direction—even over Congress's expressed preferences.

This article attempts to explain the peculiar patterns of executive action and inaction observed in the tax policymaking domain. It draws on public choice theory and game theory to build a strategic model of interactions between the Executive and Legislative Branches. The model generates several counterintuitive implications. Among others: a strong anti-tax faction in Congress may increase the probability that revenue-raising regulatory measures are implemented; judicial deference to Treasury regulations may reduce lawmakers' willingness to pass revenue-raising fixes to existing tax statutes; and statutory rules requiring legislation to be "deficit-neutral" may discourage the administration from taking deficit-closing regulatory actions.

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Introduction

In April 2016, Treasury Secretary Jack Lew announced new temporary regulations making it more difficult for a foreign company to acquire a larger American company without triggering the adverse tax consequences of an "inversion." [1] At the same time, Treasury published proposed regulations addressing so-called "earnings stripping" transactions that shift corporate profits from the United States to lower tax jurisdictions; the proposed rules characterize certain interests as stock instead of indebtedness to prevent U.S. corporations from claiming interest deductions on payments to their foreign affiliates. [2] President Obama told reporters at a White House press conference the following day that he "wanted to make sure that we highlighted the importance of Treasury's action." He also used the occasion as an opportunity to lambaste lawmakers for their inaction on inversions. "I want to be clear," President Obama said. "While the Treasury Department actions will make it more difficult and less lucrative for companies to exploit this particular corporate inversions loophole, only Congress can close it for good, and only Congress can make sure that all the other loopholes that are being taken advantage of are closed. . . . So far, Republicans in Congress have yet to act."[3]

Reaction was swift. Hours after the President's press conference, news leaked that the pharmaceutical giant Pfizer had called off its plans to merge with the Irish-headquartered Allergan—a transaction that was initially structured to avoid the inversion rules but that would have been caught up in the new temporary regulations' sweep.[4] Pfizer's chief executive officer, Ian Read, took to the op-ed page of the *Wall Street Journal* to assail the Obama administration's "ad hoc and arbitrary" action as "unprecedented, unproductive and harmful to the U.S. economy."[5] Inches away, the *Journal*'s editorial board said that Treasury's "rewrite of longstanding U.S. tax law" was "lawless" and "would almost surely be thrown out if it were challenged in court." Defending Pfizer and other firms involved in transactions targeted by the new rules, the *Journal* board said that "these companies

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[1] Press Release, U.S. Dep't of the Treasury, Treasury Announces Additional Action to Curb Inversions, Address Earnings Stripping (Apr. 4, 2016), available at https://www.treasury.gov/press-center/press-releases/Pages/jl0405.aspx [https://perma.cc/9XLE-RUH9]. *See* Inversions and Related Transactions: Final and Temporary Regulations, Treas. Dec. 9761, 81 Fed. Reg. 20858 (Apr. 8, 2016).

[2] Treatment of Certain Interests in Corporations as Stock or Indebtedness, 81 Fed. Reg. 20912 (proposed Apr. 8, 2016) (to be codified at 26 C.F.R. pt. 1).

[3] White House, Office of the Press Sec'y, Transcript, Remarks by the President on the Economy (Apr. 5, 2016), available at https://www.whitehouse.gov/the-press-office/2016/04/05/remarks-president-economy-0 [perma.cc/DPC8-ZHBM].

[4] Michael J. de la Merced & Leslie Picker, *Pfizer and Allergan Are Said To End Merger as Tax Rules Tighten*, N.Y. TIMES, Apr. 5, 2016, http://www.nytimes.com/2016/04/06/business/dealbook/tax-inversion-obama-treasury.html [https://perma.cc/LZ7C-9UHZ].

[5] Ian Read, Opinion, *Treasury Is Wrong About Our Merger and Growth*, WALL ST. J., Apr. 6, 2016, http://www.wsj.com/articles/treasury-is-wrong-about-our-merger-and-growth-1459983997 [perma.cc/5JYB-H6DR].

are acting legally and behaving rationally under the law that Congress has written."[6]

In fact, the laws that Congress has written delegate broad power to the Treasury Department to take the sorts of actions that President Obama and Secretary Lew announced in April. Section 7874 of the Internal Revenue Code, which addresses inversions, authorizes the Treasury Secretary to promulgate "regulations providing for such adjustments to the application of this section as are necessary to prevent the avoidance of the purposes of this section."[7] Section 385, the statute that Treasury invoked in its earnings stripping proposal, authorizes the Treasury Secretary "to prescribe such regulations as may be necessary or appropriate to determine whether an interest in a corporation is to be treated for purposes of this title as stock or indebtedness."[8] On the one hand, these statutory provisions undermine President Obama's claim that Congress has failed to take action against inversions: a Republican-led Congress *did* act in 2004 by passing section 7874, which gave the Treasury Secretary the power to close loopholes.[9] (A Democratic-majority Congress also acted in 1969 by passing section 385, although it is doubtful that inversions were on anyone's mind at the time.[10]) On the other hand, these statutory provisions also undermine the *Wall Street Journal* editorial board's claim that the Obama administration is "rewrit[ing]" the tax laws. The laws themselves give the administration wide leeway to define the rules of the game.[10a]

But in at least one sense, Pfizer's CEO was quite right to say that the Obama administration's approach was "unprecedented"—or close to it. (I will leave it to others to assess Ian Read's claims that the April 2016 actions were "unproductive" and "harmful to the U.S. economy";[11] my goal here is not to explore the merits of the administration's actions but instead to focus on the form those actions took.) Rarely, if ever, has a President publicly taken ownership of a tax-related Treasury decision, much less a decision that moved the dial in a taxpayer-unfriendly direction.[12] In this respect, the Obama administration's April 2016 actions on inversions and earnings stripping were indeed "unprecedented"—or, more precisely, unprecedented in the history of tax policy.

Of course, presidential administrations oftentimes take unilateral action in areas other than tax, and Presidents oftentimes take personal and political ownership of such measures. The Obama administration also has used regulatory

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[6] Opinion, *Jack Lew's Corporate Tax Ambush*, WALL ST. J., Apr. 6, 2016, http://www.wsj.com/articles/jack-lews-corporate-tax-ambush-1459900261 [https://perma.cc/SHY8-VT7A].

[7] 26 U.S.C. § 7874(g).

[8] § 385(a).

[9] American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 801(a), 118 Stat. 1562.

[10] Tax Reform Act of 1969, Pub. L. No. 91-172, § 415(a), 83 Stat. 613.

[10a] *Jack Lew's Corporate Tax Ambush*, *supra* note 6.

[11] *Compare, e.g.*, Editorial, *A Corporate Tax Dodge Gets Harder*, N.Y. TIMES, Apr. 6, 2016, http://www.nytimes.com/2016/04/07/opinion/a-corporate-tax-dodge-gets-harder.html [https://perma.cc/XD57-5QQ8], *with* Diana Furchtgott-Roth, Opinion, *Free Pfizer! Why Inversions Are Good for the U.S.*, N.Y. TIMES, Apr. 7, 2016, http://www.nytimes.com/2016/04/08/opinion/free-pfizer-why-inversions-are-good-for-the-us.html [https://perma.cc/9A3W-B3JY].

[12] In conversations with the author, Treasury officials from the past six administrations could name no similar example of a President claiming credit for a revenue-raising regulatory measure.

authority to nearly double fuel economy standards for cars and light-duty trucks,[13] to implement "commonsense" gun safety measures,[14] to ban "trans fat" from most food products,[15] to restrict carbon emissions from power plants,[16] to extend overtime pay to millions more workers,[17] and to grant "deferred action" status to hundreds of thousands of undocumented immigrants who came to the United States as children.[18] (The carbon emissions regulations have been stayed by the Supreme Court,[19] and the Justices by a 4-4 vote recently affirmed a lower court decision striking down the deferred action expansion.[20]) The administration of George W. Bush, for its part, used its regulatory authority with particular vigor in the waning days of Bush's second term, acting to ease rules on strip mining and coal power plant construction, open millions of acres to oil shale drilling, and allow individuals to carry concealed and loaded weapons in national parks, among other measures.[21] The Clinton administration acted unilaterally to outlaw smoking in federal buildings, ban the importation of dozens of types of semiautomatic weapons, and turn millions of acres in the West and Southwest into national monuments, among other measures.[22] Indeed, at the end of the Clinton years then-professor Elena Kagan already could declare that "[w]e live today in an era of presidential

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[13] Press Release, White House Office of the Press Sec'y, Obama Administration Finalizes Historic 54.5 MPG Fuel Efficiency Standards (Aug. 28, 2012), https://www.whitehouse.gov/the-press-office/2012/08/28/obama-administration-finalizes-historic-545-mpg-fuel-efficiency-standard [https://perma.cc/6JQ7-7NC7].

[14] White House, Office of the Press Sec'y, Fact Sheet: New Executive Actions to Reduce Gun Violence and Make Our Communities Safer (Jan. 4, 2016), available at https://www.whitehouse.gov/the-press-office/2016/01/04/fact-sheet-new-executive-actions-reduce-gun-violence-and-make-our [https://perma.cc/AQN3-FK5F]. Among other measures, the President announced that the Bureau of Alcohol, Tobacco, and Firearms would finalize a rule requiring background checks for additional gun purchases; the Social Security Administration would begin a rulemaking process with the goal of allowing mental health information regarding beneficiaries to be incorporated into the background check system; and the Department of Health and Human Services would finalize a rule amending privacy protections under the Health Insurance Portability and Accountability Act (HIPAA) so that state health officials could share mental health records of potential gun purchasers with the Federal Bureau of Investigation.

[15] Final Determination Regarding Partially Hydrogenated Oils, 80 Fed. Reg. 34650 (June 17, 2015).

[16] Carbon Pollution Emission Guidelines for Existing Stationary Sources: Electric Utility Generating Units—Final Rule, 80 Fed. Reg. 64,662 (Oct. 23, 2015).

[17] *See* Jonelle Marte, *Millions More Workers Will Be Eligible for Overtime Pay Under New Federal Rule*, WASH. POST, May 18, 2016, https://www.washingtonpost.com/news/get-there/wp/2016/05/17/millions-more-workers-would-be-eligible-for-overtime-pay-under-new-federal-rule (noting that President Obama would announce the new rules alongside his Labor Secretary).

[18] Memorandum from Janet Napolitano, Sec'y, Dep't of Homeland Sec., to David V. Aguilar et al., Exercising Prosecutorial Discretion with Respect to Individuals Who Came to the United States as Children (June 15, 2012), https://www.dhs.gov/xlibrary/assets/s1-exercising-prosecutorial-discretion-individuals-who-came-to-us-as-children.pdf [https://perma.cc/QDP9-6QFY].

[19] *See* West Virginia v. EPA, No. 15A773, 577 U.S. __ (Feb. 9, 2016).

[20] *See* United States v. Texas, 579 U.S. __ (June 23, 2016).

[21] Paul Harris, *Bush Sneaks Through Host of Laws To Undermine Obama*, THE GUARDIAN (London), Dec. 13, 2008, http://www.theguardian.com/world/2008/dec/14/george-bush-midnight-regulations [https://perma.cc/2DBJ-HYRR].

[22] *See* WILLIAM G. HOWELL, POWER WITHOUT PERSUASION: THE POLITICS OF DIRECT PRESIDENTIAL ACTION 5–6 (2003).

administration,"[23] and her claim is—if anything—truer today than it was a decade and a half ago.

Tax, though, has followed a somewhat different pattern. Rather than acting on their own or through their Treasury Secretaries, the last three Presidents repeatedly asked Congress to close "loopholes"[24] in the tax laws—even when existing statutes gave them ample (or at least arguable) authority to enact a desired change, and even when legislative gridlock made it exceedingly unlikely that Congress would act.[24a] Each year, each President since George H.W. Bush has presented a set of suggested tax law reforms to Congress—compiled in a single volume colloquially known as the "Greenbook" because of its distinctive green cover.[25] Almost invariably, the Greenbook includes proposals that the President plausibly could carry out on his own—without any congressional action—by directing the Treasury Department to promulgate appropriate regulations. Recent examples include:

- Requiring managers of private equity, venture capital, and hedge funds to pay tax on carried interest profits at ordinary income rates rather than capital gains rates;[26]
- Restricting the use of "check-the-box" rules to create stateless income;[27]
- Preventing oil and gas companies and other taxpayers from claiming foreign tax credits where the relevant foreign country imposes no general tax;[28]
- Repealing the lower-of-cost-or-market (LCM) inventory accounting method;[29]
- Preventing taxpayers from avoiding gift taxes through "zeroed-out" grantor retained annuity trusts (GRATs);[30]

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[23] Elena Kagan, *Presidential Administration*, 114 HARV. L. REV. 2245, 2246 (2001).

[24] As Joseph Pechman noted, "A provision which is regarded as a loophole for one group is often justified as a major improvement in equity or as essential to promote economic growth by another." Joseph A. Pechman, *Comprehensive Income Taxation: A Comment*, 81 HARV. L. REV. 63, 66–67 (1967). This article avoids the term from here on out.

[24a] *See infra* Sections I.D–E.

[25] Greenbooks from fiscal year 1990 to the present are available at U.S. Dep't of Treas., Administration's Fiscal Year Revenue Proposals, https://www.treasury.gov/resource-center/tax-policy/Pages/general_explanation.aspx (last updated Mar. 3, 2016) [https://perma.cc/D4S7-ZSJM]. The Greenbook is not to be confused with the Bluebook, which is prepared by the Staff of the Joint Committee on Taxation at the end of each Congress and which explains all tax provisions actually enacted during the previous congressional session. See Joint Committee Bluebooks, Joint Comm. on Tax'n, https://www.jct.gov/publications.html?func=select&id=9 (last visited Dec. 11, 2015) [https://perma.cc/842L-AXHX].

Complicating matters somewhat, the administration of George W. Bush used a blue cover for its books of revenue proposals. *See* Warren Rojas, *Bush Tax Credit Aims To Make Housing Dreams Come True*, TAX NOTES, Apr. 16, 2001, at 375. The Obama administration restored the cover to the color green. *See* Tim Tuerff et al., *Obama Proposals Would Topple Long-Standing Tax Framework*, TAX NOTES INT'L, May 25, 2009, at 657.

[26] *See infra* Section I.E.1.

[27] *See infra* Section I.E.2.

[28] *See infra* Section I.E.3.

[29] *See infra* Section I.E.4.

[30] *See* infra Section I.E.5.

- Disallowing deductions for "charitable" contributions of rights to airspace above historic homes;[31] and
- Denying a deduction for payment of punitive damages.[32]

Several of these measures have appeared in multiple years' Greenbooks: the proposal to eliminate the carried interest preference, for example, appeared in the Greenbook every year of the Obama administration.[33] Year after year, Congress rebuffed the President's request.[34] Surely by the last year of the Obama administration, Treasury officials harbored no illusions that Congress would pass these measures. Why did the administration not act on its own?

To be sure, if the Executive Branch acted alone to implement these tax law changes, its actions would likely face challenge in court. On some of the above issues (e.g., limiting the ability of oil, gas, and other companies to claim foreign tax credits where no foreign tax was paid), the administration would almost certainly prevail; on other issues (e.g., carried interest and punitive damages) the administration's authority is somewhat less clear.[34a] And yet the risk of litigation hardly explains the Obama administration's reluctance to act on its own: after all, the administration routinely faces (and sometimes loses) challenges to unilateral action in other areas, ranging from immigration[35] to air pollution[36] to corporate governance.[37] What explains the reluctance of this and past administrations to raise revenue via executive action when the path to legislative reform was obstructed?

This article offers a first cut at answering that question. I say it is a "first cut" because the question has thus far gone almost entirely unasked.[38] While others

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[31] *See* infra Section I.E.6.

[32] *See* infra Section I.E.7.

[33] *See* U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2010 Revenue Proposals 23–24 (May 2009) [hereinafter FY 2010 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2011 Revenue Proposals 91–92 (Feb. 2010) [hereinafter FY 2011 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2012 Revenue Proposals 61–62 (Feb. 2011) [hereinafter FY 2012 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals 134–35 (Feb. 2012) [hereinafter FY 2013 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2014 Revenue Proposals 159–60 (Apr. 2013) [hereinafter FY 2014 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2015 Revenue Proposals 177–78 (Mar. 2014) [hereinafter FY 2015 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2016 Revenue Proposals 163–64 (Feb. 2015) [hereinafter FY 2016 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals 162–63 (Feb. 2016) [hereinafter FY 2017 Greenbook].

[34] *See* Jackie Calmes, *Carried-Interest Tax Break Divides Again, After Trump Revives the Issue*, N.Y. TIMES, Sept. 18, 2015, http://www.nytimes.com/2015/09/19/business/carried-interest-tax-break-divides-again-after-trump-revives-the-issue.html [https://perma.cc/QRU2-CQTZ].

[34a] *See infra* Section I.E.

[35] *See* Texas v. United States, 809 F.3d 134 (5th Cir. 2015), *cert. granted*, 136 S. Ct. 906 (2016).

[36] *See* Michigan v. EPA, 135 S. Ct. 2699 (2015).

[37] *See* Bus. Roundtable v. SEC, 647 F.3d 1144 (D.C. Cir. 2011).

[38] Daniel Berman and Victoria Haneman briefly address the question in their otherwise-comprehensive overview of tax policymaking. *See* DANIEL M. BERMAN & VICTORIA J. HANEMAN, MAKING TAX LAW 196 (2014) ("[W]hy would the Administration submit a legislative proposal to override regulations issued by its own Treasury Department, when the Treasury Department

have noted that the administration likely could end the carried interest preference without Congress,[39] this article shows that the carried interest example is part of a larger pattern. Recent Greenbooks are replete with proposals that could be accomplished by regulation: in many cases, the President asks Congress to fix a flaw *created* by Treasury rules—rules which the administration has authority to repeal.[40] Moreover, this pattern is not specific to the Obama administration: a review of Greenbooks since 1990 turns up numerous examples in which the President has asked Congress to do what his administration could do on its own.[41]

Part I of the article lays out the legal and institutional landscape. Part II offers several possible reasons why a President and his administration might decline to pursue revenue-raising regulatory measures—even when the same President supports legislation that would accomplish the same result. I start with a rudimentary model in which politicians take actions when the political costs exceed the political benefits. I then complicate the model by envisioning two actors—the President and Congress—whose political fortunes are separate. Voters and interest groups allocate credit and blame between the President and Congress based on each actor's role in the policymaking process: when the Executive Branch acts unilaterally, the President reaps all the credit but bears all the blame; when Congress passes legislation that the President signs, Congress and the President share credit and blame proportionally. I add the further constraint that the President cannot spend government funds on his own; all appropriations legislation must go through Congress. With this additional constraint, the two-branch model suggests an asymmetry between non-tax and tax matters. On the non-tax side, any policy that the President is willing to sign into law is also a policy that he would implement via regulation—i.e., any policy for which the political benefits exceed the political costs. On the tax side, however, the President bears all the political costs of executive actions that raise revenue but shares the political benefits of additional spending with Congress. The model predicts that there will be some revenue-raising measures that the President would sign if they came to his desk in the form of legislation (because he would then share the political costs with Congress) but that he would not want to implement via regulation (because he would then bear the political costs all himself). The model also predicts an additional asymmetry *within* tax law: the President will be less willing to promulgate

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could simply and quickly change the regulations on its own?"). Berman and Haneman suggest that the answer has to do with the fact that "[n]either the Joint Committee on Taxation nor the Treasury Department prepares a revenue estimate for a proposed regulation." *Id.* So while "the Treasury Department has the authority to simply revise or revoke regulations," Berman and Haneman posit that "the Administration may want to capture the measurable increase in revenue . . . and to do so, the change or revocation must be enacted by statute." *Id.*

Berman and Haneman's explanation is illuminating but incomplete. The Treasury Department could solve the problem identified by Berman and Haneman by generating its own revenue estimates for regulations. (Indeed, Treasury already estimates the revenue effects of each legislative proposal in the Greenbook.) The fact that Treasury refrains from estimating the revenue effects of regulations may be a consequence of its reluctance to implement revenue-raising regulations *sua sponte*; but given that Treasury could easily reverse this policy, it is difficult to see how the lack of revenue estimates for regulations could play a significant causal role.

[39] *See, e.g.*, Victor Fleischer, *Two and Twenty Revisited: Taxing Carried Interest as Ordinary Income Through Executive Action Instead of Legislation* (unpublished manuscript).

[40] *See infra* notes 105, 124–133, 137–139, 146–149 and accompanying text.

[41] *See infra* notes 140–141, 148, 198, 204, 212 and accompanying text.

(or to instruct his Treasury Secretary to promulgate) regulations that increase tax revenue than to promulgate regulations that reduce tax revenue. Indeed, the prospect of promulgating regulations that reduce revenue will be quite attractive to the President: if his administration acts on its own to reduce taxes, the President will reap all the political benefits, while he and Congress will share the political costs of spending cuts.

The rudimentary model yields a partial explanation for patterns of presidential action (and inaction) in the tax domain, but the account is incomplete in several respects. For one, the model envisions a single decisionmaker (the President) making a one-time decision (whether to promulgate regulations or request legislation). More realistically, outcomes are the product of strategic interactions between the Executive and Legislative Branches across a range of tax law issues. A game-theoretic model helps to describe these interactions. The President decides whether or not to regulate, and Congress decides whether or not to legislate. All else equal, the President would prefer to share the political costs of raising revenue with Congress, while Congress would prefer that the President bear all the political costs of raising revenue himself.

The game-theoretic model yields a number of additional implications. First, the model suggests that the President may ask Congress to pass revenue-raising legislative proposals even when the political costs to the President of implementing the proposal via regulation are less than his portion of the shared political benefits from additional spending. In more colloquial terms, the President may ask Congress to share the dirty work of raising revenue even though, push comes to shove, the administration would be willing to act on its own. Second, and symmetrically, the model suggests that Congress may rebuff the President's requests for revenue-raising legislation even when Congress's share of the political costs of raising revenue is less than Congress's share of the political benefits from the additional spending that revenue-raising would allow. In other words, members of Congress may try to call the President's bluff—they may reject the President's recommendations for revenue-raising legislation in the hope that if they do not act, the Executive Branch will proceed on its own. In his ideal world, the President could credibly commit *not* to implement certain revenue-raising regulations, thus spurring Congress to act. And in its ideal world, Congress could credibly commit *not* to pass certain revenue-raising measures, thus spurring the President to act on his own. Absent the possibility of such credible commitments, however, some revenue-raising measures that could be implemented via regulation or via legislation may not be implemented at all.

Part II goes on to discuss further implications of the game-theoretic model. First, I consider the role of ideology in bargaining between the President and Congress. If the political costs of revenue-raising measures are higher for Republicans than for Democrats, divided government will affect bargaining outcomes. When the President is a Democrat and Congress is controlled by Republicans, the Democratic President will discount the probability of revenue-raising legislative action; accordingly, the Democratic President may be more willing to raise revenue unilaterally. Meanwhile, when the President is a Republican and Congress is controlled by Democrats, then the President will assign a higher value to the probability of revenue-raising legislation, and Congress will discount the probability of unilateral executive action. Perhaps a more surprising implication is that a wider divergence between the President's preferences and Congress's does not necessarily reduce the probability of revenue-raising action, because Presidents will be more willing to raise revenue unilaterally when Congress is strongly tax-averse, and Congress will be more willing to pass revenue-raising legislation when the President is strongly tax-averse.

Next, I examine the role of doctrine in defining the terms of interactions between the President and Congress. Judicial deference to the Executive Branch's interpretations of tax statutes will, intuitively, expand the universe of revenue-raising measures that the Executive Branch can implement on its own. Less intuitively, judicial deference may make Congress more reluctant to adopt revenue-raising legislation: after all, Congress would prefer not to bear the political costs of revenue-raising measures if it does not have to. The latter observation suggests that the Supreme Court's decision in *Mayo Foundation for Medical Education & Research v. United States*, to the extent that it increased judicial deference to Treasury regulations, may have been a double-edged sword: *Mayo Foundation* empowered the Executive Branch to act unilaterally, but it also may have discouraged Congress from raising revenue via legislation.[41a]

Part II then considers the role of congressional "deficit hawks" in the tax policymaking process. I assume that some members of Congress are reluctant to vote for legislation unless it is revenue neutral. (Congress has periodically adopted "PAYGO" rules that attempt to codify this revenue neutrality constraint.) PAYGO has the potential to discourage the Executive Branch from adopting a revenue-raising measure on its own, because by doing so, it loses the ability to include those revenue raisers in legislation as offsets for the expenditures or tax cuts that the President supports.[41b] The irony is that lawmakers' emphasis on revenue neutrality may discourage the Executive Branch from pursuing regulatory actions that would raise revenue and reduce the deficit. The article thus draws attention to a potential unintended consequence of PAYGO rules.

Having previewed the aims of the article, I should add a word about what the article does not aspire to do. This article does not seek to offer a comprehensive account of the regulatory or legislative process in tax law.[42] Rather, my objective is to present a tractable model of strategic interactions between the Executive Branch and Congress—a model that, I hope, sheds light on some otherwise puzzling aspects of tax policymaking. Like any model, it inevitably oversimplifies. But such oversimplification is a necessary aspect of the modeling enterprise—and perhaps not an entirely unfortunate one.[43]

I. The President's (Largely Latent) Power To Tax

[41a] *See* Mayo Found. for Med. Educ. & Res. v. United States, 131 S. Ct. 704 (2011).

[41b] *See e.g.* DAVID EPSTEIN & SHARYN O'HALLORAN, DELEGATING POWERS: A TRANSACTION COST POLITICS APPROACH TO POLICY MAKING UNDER SEPARATE POWERS 127 (1999) (explaining how PAYGO constricts the policy choices available to both the President and Congress).

[42] For one such account, *see* BERMAN & HANEMAN, *supra* note 38.

[43] *See generally* KENNETH N. WALTZ, THEORY OF INTERNATIONAL POLITICS 7 (1979) ("Explanatory power . . . is gained by moving away from 'reality,' not by staying close to it. A full description would be of least explanatory power. . . . Departing from reality is not necessarily good, but unless one can do so in some clever way, one can only describe and not explain.").

A. Presidential Administration Outside of Tax

The President wields broad power to pursue policy objectives via executive action.[44] One source of presidential power is the Constitution's Appointments Clause, which requires all principal executive officers of the United States to be appointed by the President (with the Senate's advice and consent).[45] The Appointments Clause generally allows the President to choose agency heads who share his policy preferences (though, to be sure, this mechanism of presidential control may break down when Congress repeatedly refuses to confirm the President's nominees). A second source of presidential power arises from his removal authority: as a general rule, the President may fire executive officers who disobey his commands.[46] The Supreme Court has recognized an exception to the general rule where Congress has "conferr[ed] good-cause tenure on the principal officers of certain independent agencies"; the Federal Trade Commission is one example.[47] However, the President has the power to fire any Cabinet secretary at will. Past Presidents have exercised this power relatively rarely, but the firing of a Cabinet secretary is not an unheard-of occurrence.[48] Moreover, Executive Branch officials labor in the shadow of the President's removal power: the President's authority to fire his underlings may have a significant effect on their conduct even if firings are infrequent.

Beyond controlling the identities of agency heads, Presidents also pursue policy objectives by issuing executive orders and presidential memoranda directing

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[44] The phrase "executive action" does not refer to a "special legal category." It is, as Eric Posner puts it, "more like a layman's term for anything the executive branch does." *See* Julie Percha, The Nuance You May Have Missed in Obama's Gun Control Plan, PBS NewsHour (Jan. 5, 2016), http://www.pbs.org/newshour/updates/whats-the-difference-between-an-executive-order-and-action (quoting Posner) [https://perma.cc/ZAK5-X7Q4]. The term "executive order" does appear in the U.S. Code: the Federal Register Act requires publication of most "executive orders" in the Federal Register (though executive orders need not be published if they lack "general applicability and legal effect" or if they are effective only against federal officials). *See* 44 U.S.C. § 1505(a). As a practical matter, though, many presidential pronouncements that are not labeled "executive order" nonetheless appear in the Federal Register, and many executive orders appear in the Federal Register even though they technically fall within one of § 1505(a)'s exceptions. A recent report from the Congressional Research Service observes that "[t]he distinction between these instruments—executive orders, presidential memoranda, and proclamations—seems to be more a matter of form than of substance," given that any such document "may be employed to direct and govern the actions of government officials and agencies." VIVIAN S. CHU & TODD GARVEY, CONG. RESEARCH SERV., EXECUTIVE ORDERS: ISSUANCE MODIFICATION, AND REVOCATION 2 (Apr. 16, 2014). This article will use the term "executive action" throughout to refer to actions by the Secretary of the Treasury and other administration officials to implement the President's policies.

[45] U.S. Const. art. II, § 2, cl. 2; *see also* Free Enter. Fund v. Pub. Co. Accounting Oversight Bd., 561 U.S. 477, 492 (2010).

[46] *See* Free Enter. Fund, 561 U.S. at 492.

[47] *Id.*, at 492; Humphrey's Executor v. United States, 295 U.S. 602 (1935).

[48] *See, e.g.*, *Firing of Presidential Cabinet Members a Rarity*, NPR: ALL THINGS CONSIDERED (Dec. 15, 2013), http://www.npr.org/templates/story/story.php?storyId=251330321 [https://perma.cc/Q9LR-TGE4] (explaining why presidents only occasionally fire cabinet members).

Executive Branch officials to take specific actions.[49] Often these directives instruct Cabinet secretaries or other agency heads to promulgate particular regulations. Examples of presidential memoranda from President Obama's second term include: a memorandum instructing the Secretary of Defense, Attorney General, and Secretary of Homeland Security to conduct and sponsor research into gun safety technology that will reduce the risk of accidental discharge or unauthorized use of firearms and that will improve the tracing of lost and stolen guns;[50] a memorandum requiring that federally employed physicians undergo training regarding prescription opioid paid medication misuse;[51] a memorandum instructing the Secretary of Education to propose regulations allowing certain borrowers to cap their federal student loan payments at 10% of income;[52] a memorandum instructing the Secretary of Labor to propose regulations expanding overtime protections for workers in the private and public sectors;[53] and a memorandum instructing the EPA Administrator to issue a final rule setting standards for greenhouse gas emissions from power plants.[54] While President Obama has issued memoranda to agencies more frequently than his predecessors, he is not the first chief executive to use such memoranda as a means of pursuing policy objectives.[55] Then-Professor Kagan noted that the Clinton administration was a turning point in the use of presidential memoranda to catalyze agency action: by her count, President Reagan issued 9 directives to heads of domestic policy agencies regarding substantive regulatory policy; the first President Bush issued 4 such directives; President Clinton issued 107.[56] (According to another tally, the second President Bush issued approximately 150 during his two terms and President Obama had almost reached the 200 mark by the end of his first six years in office.[57])

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[49] *See, e.g.*, Kagan, supra note 23, at 2993–99. On the distinction (or lack thereof) between executive orders and presidential memoranda, *see supra* note 44 (comparing and contrasting the usage of executive orders and memoranda by the Reagan and Clinton administrations).

[50] Memorandum—Promoting Smart Gun Technology (Jan. 4, 2016), available at https://www.whitehouse.gov/the-press-office/2016/01/05/memorandum-promoting-smart-gun-technology [https://perma.cc/E77Q-6AXU].

[51] Presidential Memorandum—Addressing Prescription Drug Abuse and Heroin Abuse (Oct. 21, 2015), available at https://www.whitehouse.gov/the-press-office/2015/10/21/presidential-memorandum-addressing-prescription-drug-abuse-and-heroin [https://perma.cc/ASB7-TY6N].

[52] Presidential Memorandum—Federal Student Loan Repayments (June 9, 2014), available at https://www.whitehouse.gov/the-press-office/2014/06/09/presidential-memorandum-federal-student-loan-repayments [https://perma.cc/D2MT-586T].

[53] Presidential Memorandum—Updating and Modernizing Overtime Regulations (Mar. 13, 2014), available at https://www.whitehouse.gov/the-press-office/2014/03/13/presidential-memorandum-updating-and-modernizing-overtime-regulations [https://perma.cc/WY2E-WTYY].

[54] Presidential Memorandum—Power Sector Carbon Pollution Standards (June 25, 2013), https://www.whitehouse.gov/the-press-office/2013/06/25/presidential-memorandum-power-sector-carbon-pollution-standards [https://perma.cc/Q3JP-XJ8A].

[55] *See* Kenneth S. Lowande, *After the Orders: Presidential Memoranda and Unilateral Action*, 44 PRES. STUD. Q. 724, 730 fig. 1 (2014) (depicting graphically the number of executive orders and presidential memoranda issued from 1960 to 2012).

[56] Kagan, *supra* note 23, at 2294.

[57] *See* Gregory Korte, *Obama Issues 'Executive Orders by Another Name,'* USA TODAY, Dec. 17, 2014, http://www.usatoday.com/story/news/politics/2014/12/16/obama-presidential-memoranda-executive-orders/20191805 [perma.cc/5FR2-CYLY]; White House, Presidential Memoranda,

Presidents also exercise power over executive agencies through a formal process of "presidential review" of proposed regulations.[58] Every President since Reagan has required agencies to submit all proposed rules to the Office of Information and Regulatory Affairs, a part of the Office of Management and Budget within the White House.[58a] Agencies also must submit a "regulatory impact analysis" accompanying any rule that is "major" or "significant," with "major" or "significant" defined to include rules likely to result in an "annual effect on the economy of $100 million or more."[59] That analysis generally (but not always) involves some quantification of the regulation's costs and benefits.[60] If OIRA determines that a proposed rule is not cost-justified, OIRA "returns" the rule to the agency for further consideration.[61] Recent Presidents have used the OIRA review process to block regulations that diverged from their policy objectives. In September 2011, President Obama "requested" that the EPA Administrator withdraw draft rules setting national ambient air quality standards for ozone.[62] (The EPA Administrator, who serves at the President's pleasure, unsurprisingly complied with the request.)[62a] For its part, the administration of George W. Bush "returned" 42 rules to the agency after OIRA review.[63]

Once a rule passes through the OIRA review process and is promulgated by an agency, it still may be challenged in the courts. Judicial review of agency regulations interpreting statutes is generally governed by the two-step *Chevron* framework. Under *Chevron*, the court first determines "whether Congress has directly spoken to the precise question at issue" in the relevant statute.[64] If yes, then Congress's unambiguous statement is controlling. Conversely, "if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute"—or, phrased differently, whether the agency arrived at a "reasonable interpretation."[65]

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https://www.whitehouse.gov/briefing-room/presidential-actions/presidential-memoranda (last visited Apr. 20, 2016) [https://perma.cc/8BW3-H78Y].

[58] *See* Jennifer Nou, *Agency Self-Insulation Under Presidential Review*, 126 HARV. L. REV. 1755, 1767 (2013).

[58a] *Id.*

[59] *See* Exec. Order No. 12,291, § 1(b) (1982) (revoked 1993); Exec. Order No. 12,866, § 3(f)(1) (1993).

[60] *See generally* Jonathan S. Masur & Eric A. Posner, Unquantified Benefits and Bayesian Cost-Benefit Analysis (Univ. of Chi. Law Sch., Public Law Working Paper No. 538, Aug. 17, 2015), http://ssrn.com/abstract=2646063 [https://perma.cc/7V7Q-9G2R] (noting that regulators oftentimes fail to quantify the costs and benefits of a major rules).

[61] Exec. Order 12866, § 6(b)(3) (Sept. 30, 1993).

[62] White House, Office of the Press Sec'y, Statement by the President on the Ozone National Ambient Air Quality Standards (Sept. 2, 2011), https://www.whitehouse.gov/the-press-office/2011/09/02/statement-president-ozone-national-ambient-air-quality-standards [https://perma.cc/ABU5-GAKV].

[62a] Gabriel Nelson, *EPA Reveals Jackson's Preferred Path on Ozone Rule*, NEW YORK TIMES (Oct 4, 2011) http://www.nytimes.com/gwire/2011/10/04/04greenwire-epa-reveals-jacksons-preferred-path-on-ozone-r-23864.html [https://perma.cc/8MBG-3XEU].

[63] Nina Mendelson, *Disclosing "Political" Oversight of Agency Decisions*, 108 MICH. L. REV. 1127, 1150 (2010).

[64] Chevron v. Natural Res. Def. Council, 467 U.S. 837, 843 (1984).

[65] *Id.* at 843, 844.

The *Chevron* framework is no doubt familiar to most readers, and I will not pause here to comment on its various exceptions and limits.[66] The key takeaways from the discussion of presidential administration outside of tax are as follows: The President can pursue his policy objectives by appointing loyal agency heads and removing disloyal ones, by directing agencies to take specific actions such as promulgating regulations, and by blocking agencies from issuing regulations that diverge from his agenda. Moreover, when an executive agency does issue a regulation interpreting a statute, that regulation is (at least as a doctrinal matter) generally reviewed under the deferential *Chevron* framework. This is true even when the regulation reverses the view adopted by a previous administration (or adopted previously by the same administration).[67] To be sure, the President also can pursue his policy goals by submitting legislative proposals to Congress and by using his "bully pulpit" to put pressure on Congress for action.[68] And, of course, he has the power to veto legislation at odds with his own preferences. But Presidents can—and do—carry out significant elements of their agenda on their own, without congressional participation.

B. Presidential Administration and Tax Law

Formally, the President's powers with respect to tax law look very similar to his powers in most other areas. Both the Secretary of the Treasury and the Commissioner of Internal Revenue serve at the pleasure of the President: he appoints them (with the advice and consent of Congress), and can remove them at will.[69] The same is true for the Assistant Secretary of the Treasury for Tax Policy and the IRS Chief Counsel, the officials most directly responsible for drafting regulations that interpret the Internal Revenue Code.[70] The Constitution also imposes no constraints on Congress's ability to delegate authority to the Executive Branch in tax law beyond the constraints that apply in other areas. (The Origination Clause constrains Congress with regard to revenue measures,[71] but the Supreme

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[66] For a more comprehensive treatment, *see* Thomas W. Merrill & Kristin E. Hickman, *Chevron's Domain*, 89 GEO. L.J. 833 (2000).
[67] See Nat'l Cable & Telecomm'cns Ass'n v. Brand X Internet Servs., 545 U.S. 967, 981 (2005) ("Agency inconsistency is not a basis for declining to analyze the agency's interpretation under the *Chevron* framework. . . . [T]he whole point of *Chevron* is to leave the discretion provided by the ambiguities of a statute with the implementing agency.") (internal quotation marks omitted).
[68] *See generally* George C. Edwards III & B. Dan Wood, *Who Influences Whom? The President, Congress, and the Media*, 93 AM. POL. SCI. REV. 327 (2014) (analyzing the ability of presidents to use public pressure to spur Congress to their preferred policies).
[69] President George W. Bush's first Treasury Secretary, Paul O'Neill, technically "resigned" but by almost all accounts "was fired." *See* Edmund L. Andrews, *Bush, in Shake-Up of Cabinet, Ousts Treasury Leader*, N.Y. TIMES, Dec. 7, 2002, http://www.nytimes.com/2002/12/07/politics/07ONEI.html [https://perma.cc/DG2D-MEJJ]; John F. Dickerson, *Confessions of a White House Insider*, TIME (Jan. 10, 2004), http://content.time.com/time/magazine/article/0,9171,574809,00.html [https://perma.cc/CCU4-6DTX].
[70] On the role of the Assistant Secretary and the IRS Chief Counsel in the regulatory process, *see* Internal Revenue Manual § 32.1.6.9 (2016). *See also* 26 U.S.C. § 7803 (providing for presidential appointment and removal of the IRS Chief Counsel, with the IRS Commissioner providing recommendations to the President on both points).
[71] See U.S. Const. art. I, § 7, cl. 1 ("All bills for raising revenue shall originate in the House of Representatives; but the Senate may propose or concur with amendments as on other Bills."). In

Court has said that the Origination Clause does not affect the ability of Congress to delegate authority to the President regarding tax matters.[72]) And at least in theory, the President can exercise the same authority with respect to the Treasury Department and the Internal Revenue Service through memoranda and return letters as he can with respect to other Cabinet agencies and sub-agencies.

Here, however, theory and practice diverge. It does not appear that the President has *ever* issued a memorandum directing Treasury or the IRS to take regulatory action on a tax-specific issue.[73] Moreover, none of the OIRA return letters (or, at least, none of the publicly disclosed return letters) relate to tax regulations. And a recent study by the Government Accountability Office turned up only two instances in which OIRA has determined that an IRS regulation has an annual effect on the economy of $100 million or more.[74]

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practice, the Origination Clause rarely imposes a binding constraint: "With increasing frequency, the Senate takes a revenue bill passed by the House (the 'shell bill'), strikes the language of the bill entirely, and replaces it with its own revenue bill unrelated to the one that began in the House." (internal citation omitted). Rebecca M. Kysar, *The 'Shell Bill' Game: Avoidance and the Origination Clause*, 91 WASH. U. L. REV. 659, 661 (2014). So far this "shell bill" maneuver has passed muster in federal court. *See id.* at 662 n.10.

[72] A unanimous Court addressed this issue in *Skinner v. Mid-America Pipeline Co.*:

> We discern nothing in [the structure of Article I] that would distinguish Congress' power to tax from its other enumerated powers—such as its commerce powers, its power to "raise and support Armies," its power to borrow money, or its power to "make Rules for the Government"—in terms of the scope and degree of discretionary authority that Congress may delegate to the Executive in order that the President may "take Care that the Laws be faithfully executed." . . . It is, of course, true that "all Bills for raising Revenue must originate in the House of Representatives." But the Origination Clause . . . implies nothing about the scope of Congress' power to delegate discretionary authority under its taxing power once a tax bill has been properly enacted. . . . We find no support . . . for [the] contention that the text of the Constitution or the practices of Congress require the application of a different and stricter nondelegation doctrine in cases where Congress delegates discretionary authority to the Executive under its taxing power. . . . Congress may wisely choose to be more circumspect in delegating authority under the Taxing Clause than under other of its enumerated powers, but this is not a heightened degree of prudence required by the Constitution.

490 U.S. 212, 220-23 (1989) (alterations and citations omitted).

[73] President Obama has issued one memorandum addressed to the Commissioner of Internal Revenue, although the memo did not direct the Commissioner to take regulatory action. Rather, the memo responded to reports from the Government Accountability Office indicating that tens of thousands of federal contractors had failed to pay their federal taxes. *See, e.g.*, U.S. Gov't Accountability Office, GAO-07-742T, Tax Compliance: Thousands of Federal Contractors Abuse the Federal Tax System (Apr. 19, 2007), available at http://www.gao.gov/new.items/d07742t.pdf [perma.cc/4LFA-557K]. The memo directed the Commissioner to "conduct a review of certifications of non-delinquency in taxes that companies bidding for Federal contracts are required to submit," and to "report to [the President] within 90 days on the overall accuracy of the contractors' certifications." Memorandum for the Heads of Executive Departments and Agencies (Jan. 20, 2010), available at https://www.whitehouse.gov/the-press-office/memorandum-heads-executive-departments-and-agencies-1 [https://perma.cc/9M2G-HGLE].

[74] U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-16-720, REGULATORY GUIDANCE PROCESSES: TREASURY AND OMB NEED TO REEVALUATE LONG-STANDING EXEMPTIONS OF TAX REGULATIONS AND GUIDANCE 18-19 (Sept. 2016). One of these was a 2011 rule regulating paid preparers, Regulations Governing Practice Before the Internal Revenue Service, 76 Fed. Reg. 32,286 (June 3, 2011), subsequently set aside by a federal court. *See* Loving v. IRS, 917 F. Supp. 2d

The IRS, for its part, maintains that tax-related regulations are "[g]enerally" exempt from the requirements of Executive Order 12866, which sets forth the details of the presidential review process.[75] That exemption claim is questionable. The Service says that "[m]ost IRS/Treasury regulations are not significant regulatory actions for two key reasons."[74a] The first reason is that "the economic effect of a regulation under [Executive Order] 12866 is not determined by the amount of taxes imposed or collected under the regulation."[74b] The second is that "most IRS/Treasury regulations merely implement a statute"; thus, "[t]he effect from a rule in most IRS/Treasury regulations is almost always a result of the underlying statute, rather than the regulation itself."[76] Neither assertion holds up under scrutiny.

The IRS's first point seems to rely on the notion that an agency, in calculating the "annual effect on the economy" of a proposed regulation, ought not include revenues raised. To be sure, if a regulation requires one party to transfer $100 million to another, the $100 million should not be considered a net benefit or a net cost for purposes of cost-benefit analysis.[77] But OIRA has clearly stated that the "annual effect on the economy" calculation "includes *benefits, costs, or transfers*."[78] Other agencies routinely include transfers when calculating a regulation's effect on the economy. For example, in determining that a regulation adjusting patent fees qualified as a "significant" action under Executive Order 12866, the Patent and Trademarks Office considered the additional fees that the regulation would generate.[79] Likewise, in determining whether a recent rule on registration fees qualified as "significant," the Drug Enforcement Agency calculated the additional fees that the rule would raise and factored those into its estimate of the regulation's annual economic effect.[80] The IRS's interpretation of "annual effect on the economy" is thus at odds with White House pronouncements and with the practices of other agencies.

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67 (2013), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014). The other was the proposed rule on earnings stripping mentioned above. *See supra* notes 1-2 and accompanying text.

[75] See Internal Revenue Manual § 32.1.5.4.7.5.3(4) (2015).

[74a] *Id.*

[74b] *Id.*

[76] *Id.*

[77] *Cf.* Eric A. Posner, *Transfer Regulations and Cost-Effectiveness Analysis*, 53 DUKE L.J. 1067, 1069 (2003) (noting that if transfer regulation "pays $100 to farmers" and "also costs taxpayers $100," then "the costs and benefits wash out," and the only term that would enter into a cost-benefit calculation is the administrative cost of the transfer).

[78] White House Office of Information & Regulatory Affairs, Regulatory Impact Analysis: Frequently Asked Questions (FAQs) 1 (Feb. 7, 2011), available at https://www.whitehouse.gov/sites/default/files/omb/assets/OMB/circulars/a004/a-4_FAQ.pdf [https://perma.cc/7CV6-J2XL].

[79] Dep't of Commerce, Patent & Trademark Office, Setting and Adjusting Patent Fees—Final Rule, 78 Fed. Reg. 4212, 4282 (2013).

[80] U.S. Dep't of Justice, Drug Enforcement Administration, Economic Impact Analysis of Final Rule on Controlled Substances and List I Chemical Registration and Reregistration Fees, DEA-346, at 18 (Feb. 2012), available at http://www.deadiversion.usdoj.gov/fed_regs/rules/2012/reg_csa_fees/2012-03-08_economic_impact_analysis.pdf [https://perma.cc/KKL5-ZH7N].

The IRS's second argument is even more perplexing. Most regulations promulgated by *any* agency implement a statute—after all, statutes are the source of agencies' authority. The same rationale would seem to justify exemptions from Executive Order 12866 for EPA regulations implementing the Clean Air Act—the bread and butter of OIRA review.[81] And the IRS cites no source for its claim that regulations implementing statutes are exempt from Executive Order 12866.[82]

Indeed, a 1983 memorandum of agreement between Treasury and OMB, recently released under the Freedom of Information Act, would seem to suggest that "major" or "significant" IRS regulatory actions are indeed subject to OIRA review. The memorandum exempts from OIRA review all revenue rulings and non-"major" regulations, with the negative implication that "major" regulations enjoy no such exemption.[83] OIRA Administrator Howard Shelanski further confirmed in testimony before a Senate subcommittee in September 2016 that "the IRS is in fact not exempt from OIRA review."[84]

In any event, the IRS's exemption claim cannot be challenged in court. Executive Order 12866, by its own terms, "is intended only to improve the internal management of the Federal Government and does not create any right or benefit, substantive or procedural, enforceable at law or equity by a party against the United States, its agencies or instrumentalities, its officers or employees, or any other person."[85] In other words, only the President can enforce the order. Successive Presidents have declined to demand that the IRS submit its significant regulations for White House review.[86] So while the President's formal power with respect to the IRS is no different than with respect to other parts of the Executive Branch, past

[81] *But see* Dep't of Labor, Wage & Hour Div., Defining and Delimiting the Exemptions for Executive, Administrative, Professional, Outside Sales and Computer Employees 80 Fed. Reg. 38,516 (proposed July 6, 2015) (to be codified at 29 C.F.R. pt. 541) (regulatory impact analysis pursuant to Executive Order 12866 for proposed rule interpreting FLSA); Regulatory Impact Analyses, U.S. Env'tl Protection Agency http://www3.epa.gov/ttn/ecas/ria.html (last updated Nov. 17, 2015) (compiling RIAs for EPA regulations implementing the Clean Air Act).

[82] The IRS's exemption claim is particularly perplexing because Executive Order 12866 does *not* exempt regulations with an annual effect on the economy of less than $100 million from the cost-benefit analysis requirement; rather, regulations that fall below the $100 million threshold (and that do not otherwise qualify as "significant") are exempt from the requirement of OIRA review. A recent comment from the U.S. Chamber of Commerce in a tax-related rulemaking emphasizes this point. *See* Comment from U.S. Chamber of Commerce, RE: Supplemental Notice of Proposed Rulemaking on Minimum Value of Eligible Employer-Sponsored Health Plans (Nov. 2, 2015), available at https://www.uschamber.com/sites/default/files/documents/files/uscc_minimum_value_supp_nprm.pdf [https://perma.cc/QH6A-U9NT].

[83] Memorandum of Agreement: Treasury and OMB Implementation of Executive Order 12991 (Apr. 29, 1983), https://www.whitehouse.gov/sites/default/files/omb/inforeg/memos/2016/omb_moa_83_93.pdf.

[84] Alison Bennett, *New Tax Rule Challenges May Follow Memorandum Release*, BLOOMBERG BNA DAILY TAX REPORT (Sept. 27, 2016), http://www.bna.com/new-tax-rule-n57982077591.

[85] Exec. Order 12866, § 10 (Sept. 30, 1993).

[86] The IRS's noncompliance with Executive Order 12866 thus offers another example of "tax exceptionalism." On tax exceptionalism, *see generally* Kristin E. Hickman, *The Need for* Mead*: Rejecting Tax Exceptionalism in Judicial Deference*, 90 MINN. L. REV. 1537 (2006) (articulating the case against tax exceptionalism in judicial deference); Lawrence Zelenak, *Maybe Just a Little Bit Special After All?*, 63 DUKE L.J. 1897 (2014) (observing that in tax, as in other areas of law, subject matter-specific rules and norms are widespread, though arguably more so in tax than elsewhere).

Presidents have not sought to exercise this power (or, at least, have not sought to exercise this power through presidential review of tax regulations).

C. Judicial Review of Treasury Regulations

While Executive Order 12866 is not judicially enforceable, Treasury's tax regulations are judicially reviewable. And until recently, judicial review of tax regulations offered another example of tax exceptionalism. As noted above, the Supreme Court set forth a two-step framework for judicial review of agency statutory interpretations in the *Chevron* case, decided in 1984. Five years earlier, though, in *National Muffler Dealers Association v. United States*,[87] the Court set out a somewhat different test for judicial review of IRS interpretations of the tax code.

National Muffler laid out a multifactor test for determining whether an interpretation of a tax statute in a Treasury regulation would pass judicial muster. The first factor was whether the regulation "is a substantially contemporaneous construction of the statute by those presumed to have been aware of congressional intent," or whether "the regulation dates from a later period."[88] (Regulations issued immediately after the statute was passed would carry greater force.)[85a] Other factors included "the length of time the regulation has been in effect," "the reliance placed on it," "the consistency of the Commissioner's interpretation," and "the degree of scrutiny Congress has devoted to the regulation during subsequent re-enactments of the statute."[89] For decades, the Supreme Court oscillated between citing *National Muffler* and *Chevron* without any acknowledgement of the gap between the two.[90] The Tax Court, for its part, also went back and forth: in the 1985-2010 period, it cited *Chevron* but not *National Muffler* in 48 cases; cited *National Muffler* but not *Chevron* in 54 cases; and cited both *Chevron* and *National Muffler* in 27 cases.[91]

Finally, in 2011, the Supreme Court stepped in to resolve the confusion. In *Mayo Foundation*, the Court unanimously rejected *National Muffler* and announced that *Chevron* would apply to tax. As Chief Justice Roberts wrote for the Court, "[t]he principles underlying our decision in *Chevron* apply with full force in the tax context."[92] *Mayo Foundation* laid to rest any notion that Treasury and IRS interpretations of tax statutes might deserve less deference than agency interpretations in other contexts.

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[87] 440 U.S. 472 (1979).
[88] *Nat'l Muffler*, 440 U.S. at 477.
[85a] *Id.*
[89] *Id.*
[90] *See Mayo Foundation*, 131 S.Ct. at 712 (collecting cases).
[91] These numbers are drawn from searches of the LexisNexis database and restricting results to U.S. Tax Court cases. A search for citations to *Chevron* turns up 75 citing cases for the period from January 1, 1985, to December 31, 2010. A search for citations to *National Muffler* with the same restrictions turns up 81 citing cases. Twenty-seven Tax Court cases in that period cite both *Chevron* and *National Muffler*.
[92] *Id.* at 713. Chief Justice Roberts's majority opinion in *King v. Burwell* has injected additional uncertainty into the tax deference debate. *See* Kristin E. Hickman, *The (Perhaps) Unintended Consequences of* King v. Burwell, 2015 PEPP. L. REV. 56, 71 (suggesting that the Chief Justice's opinion in *Burwell* "may now have inadvertently opened the door to a new, de facto version of tax exceptionalism in judicial review of tax cases").

To be sure, *Chevron* deference does not mean that the IRS will win every statutory interpretation case. Recent IRS losses in the Federal Circuit and the Tax Court make that much clear.[93] Moreover, win rates are a flawed measure of success because of selection at the filing and settlement stages.[94] What we do know is that in court of appeals cases between 2003 and 2013 in which the court has applied *Chevron*, the IRS's win rate is approximately 83%—higher than the overall agency average for *Chevron* cases.[95]

D. Executive Action or Legislation

Unilateral executive action is, of course, not the only way that Presidents can pursue their policy objectives.[96] A President also can submit a legislative proposal to Congress and can then use his bully pulpit to put pressure on Congress to pass the proposal. One advantage of the legislative route is that statutes are more durable than regulations and executive orders: a future administration with a different set of policy preferences can rescind a rule or order, but it cannot repeal a statute without the support of majorities in the House and Senate.[97] And where the relevant statutes limit the President's latitude to pursue policy objectives via executive action, the legislative route may be the only one available.

Nonetheless, recent Presidents have used regulations and other executive actions to pursue policy objectives on many occasions, often testing the limits of executive authority. As noted above, the Obama administration pursued major policies regarding guns, health, the environment, labor, and immigration via regulatory action. Examples from the administration of George W. Bush, in addition to those mentioned in the introduction, include an FDA rule compelling food manufacturers to label products for trans-fat content[98] and an EPA rule setting

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[93] *See* Dominion Res., Inc. v. United States, 681 F.3d 1313 (Fed. Cir. 2012); Altera Corp. v. Comm'r, 145 T.C. No. 3 (July 27, 2015). The IRS's appeal from the *Altera* decision is currently pending before the Ninth Circuit. *See* Altera Corp. v. Comm'r, Nos. 16-70496, 16-70497 (9th Cir. appeal filed Feb. 9, 2016).

[94] *See* Leandra Lederman, *Which Cases Go To Trial?: An Empirical Study of Predictors of Failure To Settle*, 49 CASE W. RES. L. REV. 315, 318–19 (1999).

[95] Kent Barnett & Christopher J. Walker, Chevron *in the Circuit Courts*, 115 MICH. L. REV. (forthcoming 2017) (manuscript at 51 tbl. 3), http://ssrn.com/abstract=2808848 [https://perma.cc/JZ83-3B57].

[96] Moreover, regulations are not the only way that Presidents can pursue policy objectives through executive action. On sub-regulatory mechanisms outside tax, *see* Robert A. Anthony, *Interpretive Rules, Policy Statements, Guidances, Manuals, and the Like—Should Federal Agencies Use Them to Bind the Public?*, 41 DUKE L.J. 1311 (1992). On sub-regulatory mechanisms in tax law, see BERMAN & HANEMAN, *supra* note 38, at 192. On presidential control over sub-regulatory mechanisms, *see* Nou, *supra* note 58 at 1757–59. This article analyzes the choice between executive action and legislation without focusing on the varieties of executive action. The question of when—and why—Treasury and the IRS use regulations as opposed to revenue rulings, general counsel memoranda, and other documents is a significant but separate question.

[97] On the benefits to interest groups of durable laws, *see generally* SAUL LEVMORE, THE TIMING OF LAWMAKING: INTEREST GROUPS AND THE DURABILITY OF LAW, IN THE TIMING OF LAWMAKING (Saul Levmore and Frank Fagan, eds., Edward Elgar Publishing, forthcoming).

[98] *See* John D. Graham, *Saving Lives Through Administrative Law and Economics*, 157 U. PA. L. REV. 395, 461–62 (2008).

stricter limits on particle pollution[99]—both of which followed from OIRA "prompt" letters instructing the relevant agency to act.[100] Examples from the Clinton years are even more numerous: from extending Medicare to cover clinical trials, to bolstering regulations for the testing and labeling of children's prescription drugs, to imposing new safety standards for imported foods.[101] This list is far from exhaustive.

Tax policymaking, though, follows a different pattern. As noted above, the President submits a set of tax proposals to Congress each year along with his budget. And each year, Congress fails to act on many (generally, most) of the proposals in the President's Greenbook. Yet only occasionally do the President and his Treasury Department then pursue Greenbook goals via regulation. This is so even though, as detailed in the next section, many failed Greenbook proposals could be carried out through executive action.

E. The President's Greenbook and the Regulatory Road Not Taken

In February 2016, President Obama submitted his eighth and final Greenbook to Congress. As with every other Greenbook produced by the Obama administration, this one included a number of proposals that the President—through Treasury and the IRS—likely could have implemented on his own. This section provides a partial list of those proposals, several of which also appeared in Clinton administration Greenbooks.[102] To be sure, if the President and Treasury sought to enact these measures via regulation, taxpayers might have challenged those regulatory actions in court. But in other areas of law, President Obama—like his predecessors—has been more than willing to act unilaterally even in the face of certain court challenges (and uncertain results).

The following summaries are written for readers with only a basic understanding of tax law. Scholars and practitioners primarily focused on tax will find that some nuances are addressed in only broad brushstrokes. The goal of this section is to offer an introduction to the sorts of proposals that presidential administrations could carry out on their own but instead include in their

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[99] Env'tl Protection Agency, National Ambient Air Quality Standards for Particulate Matter—Final Rule, 71 Fed. Reg. 61144 (Oct. 17, 2006).

[100] *See* Letter from John D. Graham, Administrator, Office of Information & Regulatory Affairs, to Tommy G. Thompson, Sec'y of Health & Human Servs. (Sept. 18, 2001), available at http://www.reginfo.gov/public/prompt/hhs_prompt_letter.html [https://perma.cc/WD3E-SFLS]; Letter from John D. Graham, Administrator, Office of Information & Regulatory Affairs, to Christine Todd Whitman, Administrator, U.S. Env'tl Protection Agency (Dec. 4, 2001), available at http://www.reginfo.gov/public/prompt/epa_pm_research_prompt120401.html [https://perma.cc/Q3JU-ZQET].

[101] *See* Kagan, *supra* note 23, at 2295, 2304–05.

[102] Victor Fleischer has generated a separate list of tax law reforms that Treasury could accomplish via regulatory action. *See* Victor Fleischer, *8 Tax Loopholes the Obama Administration Could Close*, N.Y. TIMES: DEALBOOK (Feb. 18, 2015), http://dealbook.nytimes.com/2015/02/18/8-tax-loopholes-the-obama-administration-could-close [https://perma.cc/GJX4-7Y2Q]. My list differs from Fleischer's insofar as the proposals listed here are all proposals that the President has already endorsed in the Greenbook. Fleischer identifies measures that are "consistent with President Obama's renewed interest in business tax policy," rather than measures that the President is already on the record as supporting.

Greenbooks. It does not provide a comprehensive treatment of any one such proposal.

1. Taxing Carried Interests as Ordinary Income

A partnership profits interest—colloquially known as a "carried interest"—is the right to receive a percentage of a partnership's future profits. Unlike a capital interest, a profits interest does not entail a right to receive money or other property in the event that the partnership is liquidated.[103] The typical private equity fund, hedge fund, and venture capital fund is organized as a partnership, with the managers as general partners. The standard formula for determining the managers' compensation is known as "two and twenty": the manager receives an annual fee equal to 2% of the fund's total assets plus 20% of any profits. The 2% management fee is taxable as ordinary income. By contrast, managers generally pay no income tax when they receive the profits interest at the time the fund is formed; instead, profits are taxed as investment income as they are realized. If profits take the form of dividends or long-term capital gains, then managers are taxed at a top statutory rate of 20% instead of the 39.6% top statutory rate on ordinary income.[104]

The current state of affairs is largely the consequence of a revenue procedure issued by the IRS in the first year of the Clinton administration.[105] It is not an inevitable result of the existing statutory scheme. Section 707 of the Internal Revenue Code, which dates back to 1954, empowers the Treasury Secretary to promulgate regulations addressing circumstances in which "a partner performs services for a partnership."[106] The statute authorizes the Treasury Secretary to treat those transactions as if they "occurr[ed] between the partnership and one who is not a partner."[107] That provision would at least arguably allow the Secretary to characterize allocations to the manager of an investment partnership such as a private equity, venture capital, or hedge fund as ordinary income—without any further action by Congress. (Indeed, one prominent tax law scholar has written a model regulation with specific language that the Treasury Secretary could copy.[108])

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[103] Staff of the Joint Comm. on Tax'n, JCS-4-09, Description of Revenue Provisions Contained in the President's Fiscal Year 2010 Budget Proposal—Part One: Individual Income Tax and Estate and Gift Tax Provisions 110–11 (Sept. 2009).

[104] *See generally* Victor Fleischer, *Two and Twenty: Taxing Partnership Profits in Private Equity Funds*, 83 N.Y.U. L. REV. 1 (2008) (explaining the typical compensations structure for fund managers). For many hedge fund managers, a significant share of carried interest income comes from short-term capital gains, in which case hedge fund managers face the same statutory rates as for ordinary income. For this reason, private equity and venture capital fund managers, not hedge fund managers, appear to be the primary beneficiaries of the carried interest status quo. *See* Victor Fleischer, *Why Hedge Funds Don't Worry About Carried Interest Tax Rules*, N.Y. TIMES: DEALBOOK (May 14, 2014), http://dealbook.nytimes.com/2014/05/14/why-hedge-funds-dont-worry-about-carried-interest-tax-rules [https://perma.cc/R5GY-EHUE].

[105] Rev. Proc. 93-27, 1993-2 C.B. 343.

[106] 26 U.S.C. § 707(a)(2)(A).

[107] *Id.* § 707(a)(1).

[108] Fleischer, *supra* note 39. In addition, Steven Rosenthal, a former tax partner at the law firm of Ropes & Gray and now a senior fellow at the Urban-Brookings Tax Policy Center, has suggested that the Treasury Department could reform the taxation of carried interest profits for private equity fund managers by promulgating regulations that clarify that the income of a private equity fund is income from a "trade or business" for purposes of the Internal Revenue Code—and thus

Yet instead of using Treasury's existing authority under section 707, President Obama asked Congress in his first Greenbook to pass legislation that would lead to ordinary income treatment for carried interest profits.[109] President Obama has included similar proposals in each of his seven Greenbooks since then.[110] This could not be because Obama administration officials are unaware of their section 707 authority: writers in mainstream media outlets have noted the President's power to change the tax treatment of carried interests via regulation.[111] And whatever the (non-political) costs of drafting regulations under section 707, those costs pale in comparison to the revenues that such a change would generate. The most recent Greenbook estimates that taxing carried interests as ordinary income would raise an additional $19.3 billion over the next decade.[112] Others have estimated that the revenues would be an order of magnitude greater: Victor Fleischer calculates that a change in the tax treatment of carried interests would raise roughly $180 billion over a decade.[113]

To be sure, Treasury regulations ending the preferential treatment of carried interest would face court challenges (although as noted above, the specter of litigation did not prevent President or his administration from taking unilateral action in other areas[114]). Elsewhere, I have suggested that well-written regulations on carried interest would have a reasonable likelihood of surviving judicial review, but it is far from a certainty.[115] Moreover, the analysis here does not suggest that the President *ought* to alter the tax treatment of carried interests through executive action: as David Weisbach has argued, "[t]here are sound reasons, many deeply embedded in partnership tax law, for retaining [the status quo]."[116] At least for the purposes of this article, I remain agnostic on the normative question. President

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ineligible for capital gains treatment. *See* Steven M. Rosenthal, *Private Equity Is a Business:* Sun Capital *and Beyond*, TAX NOTES, Sept. 23, 2013, at 1467–70.

[109] *See* FY 2010 Greenbook, *supra* note 33, at 23.

[110] *See supra* note 33.

[111] *See, e.g.*, Victor Fleischer, *How Obama Can Increase Taxes on Carried Interest*, N.Y. TIMES: DEALBOOK (June 12, 2014), http://dealbook.nytimes.com/2014/06/12/how-the-president-can-increase-taxes-on-carried-interest [https://perma.cc/2QH6-9NE6] (claiming the president "could change the tax treatment of carried interest with a phone call to the Treasury Department); David Lebedoff, *Why Doesn't Obama End the Hedge Fund Tax Break?*, SLATE (June 2, 2014), http://www.slate.com/articles/business/moneybox/2014/06/taxation_of_carried_interest_the_loophole_for_hedge_fund_managers_could.html [https://perma.cc/CSD6-SQ44] (claiming the president "could disable one of the most powerful sources of wealth and income inequality in our country"). Senator Bernie Sanders also has called on the Obama administration to address the carried interest issue through regulatory action. *See* Letter from Sen. Bernie Sanders to President Barack Obama (Feb. 27, 2015), available at http://www.budget.senate.gov/democratic/public/_cache/files/7a8dbc99-3850-4760-be3a-2361c1ec4208/sanders-letter-to-white-house-on-tax-loopholes.pdf [https://perma.cc/8RWF-XR3W].

[112] FY 2017 Greenbook, *supra* note 33, at 269 tbl.1.

[113] Victor Fleischer, *An Income Tax on Carried Interest Couldn't Be Avoided*, N.Y. TIMES: DEALBOOK (July 9, 2015), http://www.nytimes.com/2015/07/10/business/dealbook/an-income-tax-on-carried-interest-couldnt-be-avoided.html [https://perma.cc/2QH6-9NE6].

[114] *See supra* notes 19–20 and accompanying text.

[115] Daniel Hemel, Two-and-Twenty and Fifty-Fifty, Whatever Source Derived (May 12, 2016), http://bit.ly/29BUEtp [https://perma.cc/5FH5FNBT].

[116] David A. Weisbach, *The Taxation of Carried Interests in Private Equity*, 94 VA. L. REV. 715, 764 (2008).

Obama, however, is not agnostic: he and his administration staked out a position that carried interest profits ought to be taxed as ordinary income.[112a] The puzzle is why President Obama, notwithstanding his expressed view, declined to implement his preferred policy through executive action.[117] And as discussed in the remainder of this section, the puzzle is in no way unique to carried interest.

2. Restricting the Use of Structures That Generate Stateless Income

The check-the-box rules allow certain "eligible entities" to choose whether to be taxed as corporations or as partnerships (or, in the case of entities with a single owner, to be "disregarded" and treated as though part of the owner). The check-the-box regime has facilitated the phenomenon of "stateless income," a term used to describe business income of a multinational group that is not taxed in the country where the group's customers reside, nor in the country where the group's factors of production are located, nor in the country where the group's parent company is domiciled.[118] One method of generating stateless income that has attracted significant attention from the media and from members of Congress in recent years is the "Double Irish Dutch Sandwich"[114a]—a technique that Apple, Google (now "Alphabet"[119]), and many other high-tech companies have employed.[120]

The basic structure of the sandwich is as follows: ABC Inc., a U.S. corporation with a popular mobile app, incorporates a holding company in Ireland (the top piece of bread) and puts cash inside the holding company. The Irish holding company then acquires ABC's intangible rights to its app for Europe. Although the holding company is incorporated in Ireland, it is headquartered in Bermuda and

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[112a] *See* Fleischer, *supra* note 109.

[117] After a *New York Times* columnist suggested that the Obama administration could "close the so-called carried interest loophole" via regulation, a Treasury spokesperson told a reporter for the publication *Tax Notes* that "it's the department's position that 'only Congress can fully close the carried interest loophole.'" Amy S. Elliott, *IRS Official Addresses Carried Interest Speculation*, TAX NOTES, May 16, 2016, at 857; *see* Gretchen Morgenson, *Ending Tax Break for Ultrawealthy May Not Take an Act of Congress*, N.Y. TIMES, May 6, 2016, http://www.nytimes.com/2016/05/08/business/ending-tax-break-for-ultrawealthy-may-not-take-act-of-congress.html [https://perma.cc/8QXT-WXJ9]. Democratic presidential candidate Hillary Clinton subsequently told a reporter that if she is elected, and if Congress does not pass carried interest reform on its own, she will direct her Treasury Department to take regulatory action on carried interest. *See* Heidi M. Przybyla, *USA Today Interview: Clinton Says She'll Call Trump Unfit To Handle Economy*, USA TODAY, June 16, 2016, http://www.usatoday.com/story/news/politics/elections/2016/06/15/hillary-clinton-donald-trump-economy/85928334 [https://perma.cc/5ERY-UV7S].

[118] *See* Edward D. Kleinbard, *Stateless Income*, 11 FLA. TAX. L. REV. 699, 701 (2011).

[114a] See *id.* at 706–713

[119] *See* Conor Dougherty, *Google to Reorganize as Alphabet to Keep Its Lead as an Innovator*, N.Y. TIMES, Aug. 10, 2015, http://www.nytimes.com/2015/08/11/technology/google-alphabet-restructuring.html [https://perma.cc/4LF6NWK2].

[120] *See* Kleinbard, *supra* note 116 at 707–08; Charles Duhigg & David Kocieniewski, *How Apple Sidesteps Billions in Taxes*, N.Y. TIMES, Apr. 28, 2012, http://www.nytimes.com/2012/04/29/business/apples-tax-strategy-aims-at-low-tax-states-and-nations.html [https://perma.cc/B49S-VRQM]. On Google's continued use of the "Double Irish" structure, *see* Toby Sterling & Tom Bergin, *Google Accounts Show 11 Billion Euros Moved via Low Tax 'Dutch Sandwich' in 2014*, REUTERS, Feb. 19, 2016, http://www.reuters.com/article/us-google-tax-idUSKCN0VS1GP [https://perma.cc/A7WV-S4ZF].

recognized as a Bermuda resident for purposes of Irish tax law. The holding company elects to be treated as a corporation for U.S. tax purposes pursuant to the check-the-box regime.

Next, the holding company licenses its regional rights to a Dutch subsidiary (the middle layer of the sandwich), which then licenses those rights to a lower-tier Irish subsidiary (the bottom piece of bread). Both the Dutch subsidiary and the Irish subsidiary are treated as corporations under local law but "check the box" to be treated as disregarded entities under U.S. law. The Irish subsidiary then earns royalties from European users of the app.

The arrangement yields favorable tax consequences for ABC. The lower-tier Irish subsidiary has virtually no net income taxable in Ireland: its revenues from European customers are almost entirely offset by its royalty payments to the Dutch subsidiary. The Dutch subsidiary, in turn, has virtually no net income taxable in the Netherlands: its royalty payments from the lower-tier Irish subsidiary are almost entirely offset by its payments back to the Irish holding company. And the Irish holding company's income is not taxable under Irish law because Ireland considers the company to be a resident of Bermuda. Bermuda, for its part, imposes no corporate tax. And from the U.S. Treasury's perspective, the Irish holding company's income is the income of a foreign corporation, which is not taxable in the United States until ABC repatriates the earnings.[121]

The sandwich arrangement is facilitated by Treasury's decision to allow ABC to treat the Dutch subsidiary as a disregarded entity under check-the-box. If the Dutch subsidiary were considered a corporation for U.S. tax purposes, then the royalty payment from the Dutch subsidiary to the Irish holding company could be taxable immediately in the United States. That is because under Subpart F of the Internal Revenue Code, royalties earned by a foreign corporation that ABC owns (a "controlled foreign corporation," or CFC) are included in ABC's income for U.S. tax purposes if the royalties originate in a country other than the country in which the foreign corporation is organized.[122] So under Subpart F, royalties from a Dutch corporation to an Irish corporation controlled by ABC are part of ABC's taxable income, regardless of when ABC repatriates the income. ABC can get out from under Subpart F because the Dutch subsidiary and the Irish holding company are considered the same entity under check-the-box.[123]

As discussed in more detail below, the check-the-box rules are creatures of regulation,[124] and so presumably could be amended by regulation as well.[125]

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[121] *See* Kleinbard, *supra* note 118, at 706–13.

[122] 26 U.S.C. §§ 954(c)(1)(A), (3)(A).

[123] The Dutch corporation is necessary because Ireland imposes a withholding tax on royalties paid by an Irish corporation to a Bermuda company. Since Ireland considers the lower-tier Irish subsidiary to be an Irish corporation and considers the holding company to be a Bermuda entity, Ireland would impose a withholding tax if not for the Dutch layer of the sandwich. *See* Kleinbard, *supra* note 118, at 713.

[124] *See infra* Section I.I.

[125] There is an important exception to this claim: If the royalties earned by the lower-level Irish subsidiary are "derived in the active conduct of a trade or business" and received from an unrelated person, then the royalty income would not be Subpart F income. 26 U.S.C. § 954(c)(2). And under the "look-thru" rule, royalties received by higher-level subsidiaries would not constitute Subpart F income to the extent attributable to the non-Subpart F income of the lower-level Irish subsidiary. *Id.* at § 954(c)(6).

Indeed, shortly after promulgating the check-the-box rules, the Treasury Department under President Clinton published Notice 98-11 in February 1998 announcing its intention to issue regulations addressing the use of "hybrid branch" arrangements similar to the Double Irish Dutch.[126] (The Dutch layer of the sandwich is a "hybrid branch" because it is considered a corporation under Dutch and Irish law but a branch of its Irish parent under the U.S. check-the-box regime.) Two months later, Treasury published proposed and temporary regulations under which payments from a hybrid branch to a CFC would give rise to Subpart F income (i.e., income immediately taxable by the United States) when certain conditions are present: specifically, the payment by the hybrid branch reduces the foreign tax of the payor; the payment consists of dividends, interest, royalties, or rents that would have qualified as Subpart F income if the payment had been made by one corporation to another; and the effective tax rate of the payee is significantly lower than that of the payor.[127] (The last condition would be satisfied in the Double Irish Dutch example if Bermuda's corporate income tax rate is less than 90% of, and at least 5 percentage points lower than, that of the Netherlands.[128])

Notice 98-11 was not long lived. In May 1998, the Senate passed a bill that would have imposed a six-month moratorium on any final rule with respect to Notice 98-11, and that expressed "the sense of the Senate" that Treasury should withdraw the notice.[129] Less than two months later, Treasury withdrew the notice

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Yet as important as this exception is, there are three reasons to believe that Treasury still has the ability to restrict hybrid branch arrangements like the Double Irish Dutch in significant ways. First, while the "active conduct of a trade or business" rule in § 954(c)(2) is statutory, the term "active conduct of a trade or business" is not self-defining. Treasury can (and to some extent has) defined the term so as to exclude subsidiaries whose activities are insubstantial in comparison to the royalties they receive. *See* Temp. Treas. Reg. § 1.954-2T (2015).

Second, the "look-thru" rule of § 954(c)(6)—while statutory—is also temporary. Originally added in 2006 and set to expire at the end of 2008, it has since been extended five times, and is now scheduled to lapse at the end of 2019. *See* 26 U.S.C.S. § 954 (LexisNexis 2016). This means that check-the-box reform today would indeed limit the ability of U.S. multinationals to avoid Subpart F tax through the use of hybrid branches—but the effects would only be felt starting in 2020.

Third, the successive extensions of the look-thru rule are politically more palatable because of the check-the-box regulations in the background. Each extension has a limited effect on the budget—according to the Joint Committee on Taxation's calculations—because JCT takes for granted the continuity of the current check-the-box regime. Thus, JCT scored the most recent five-year extension of the look-thru rule as reducing revenues by $7.8 billion. Joint Comm. on Tax'n, JCX-143-15, Estimated Budget Effects of Division Q of Amendment #2 to the Senate Amendment to H.R. 2029 (Rules Committee Print 114-40), for the "Protecting Americans from Tax Hikes Act of 2015," at 2 (Dec. 16, 2015). That figure would be much larger if U.S. multinationals did not already have the ability to avoid Subpart F through hybrid branch arrangements like the Double Irish Dutch.

[126] Notice 98-11, 1998-1 C.B. 433 (Feb. 9, 1998).

[127] Guidance Under Subpart F Relating to Partnerships and Branches, Treas. Dec. 8767, 1998-1 C.B. 875 (Apr. 20, 1998).

[128] It is. Bermuda imposes no corporate income tax, while the top corporate income tax rate in the Netherlands is 25%. *See* Brian O'Keefe & Marty Jones, *How Uber Plays the Tax Shell Game*, FORTUNE, Oct. 22, 2015, http://fortune.com/2015/10/22/uber-tax-shell [https://perma.cc.S5JZNN93].

[129] Internal Revenue Service Restructuring and Reform Act of 1998, H.R. 2676, 105th Cong., § 3713 (as passed by the Senate, May 7, 1998).

as well as the proposed and temporary regulations addressing hybrid branches.[130] The withdrawal notice never suggested that Treasury lacked the authority to act under existing law. Rather, it stated:

> The purpose of this action is to allow Congress an appropriate period to review the important policy issues raised by the regulations, including the continuing applicability of the policy rationale of subpart F, and, if appropriate, address these issues by legislation.[131]

Nearly two decades have passed since Notice 98-11, and Congress still has yet to pass legislation addressing the Double Irish Dutch. Yet the Obama administration, rather than reviving Notice 98-11, continued to ask Congress for a bill to restrict the use of the sandwich structure and similar mechanisms that generate stateless income.[132] The most recent Greenbook estimates that such legislation would raise $2.5 billion over the next decade.[133]

3. Limiting Foreign Tax Credits Claimed by Dual-Capacity Taxpayers

Section 901 of the Code allows U.S. taxpayers to claim a credit for income taxes paid to a foreign country."[134] Section 903 extends the credit to taxes "paid in lieu of a tax on income."[135] Questions often arise with respect to payments made by oil and gas companies to foreign governments in exchange for specific benefits such as the right to drill for oil on government land. If such payments are creditable, they can reduce the companies' U.S. tax bill dollar-for-dollar. If those payments are merely deductible business expenses, though, they reduce the companies' U.S. tax bill by approximately 35 cents on the dollar (a $1 deduction from taxable income multiplied by a 35% corporate tax rate).[136]

In regulations promulgated in 1983, the Treasury Department addressed the application of the foreign tax credit provisions to so-called "dual capacity taxpayers"— taxpayers who are "subject to a levy of a foreign state" and who also receive "a specific economic benefit from the state."[137] The regulations spell out a

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[130] Notice 98-35, 1998-2 C.B. 34 (July 6, 1998).
[131] *Id.*
[132] *See, e.g.*, FY 2016 Greenbook, *supra* note 33, at 36 (Obama administration proposal to restrict the use of hybrid arrangements that create stateless income). Ireland has announced changes to its tax laws that would prevent multinational firms from using the "Double Irish with a Dutch Sandwich" structure described above. Existing arrangements such as Alphabet's would be exempt from the new rules until 2020 under a grandfather clause. Moreover, multinational firms could replicate the arrangement under the new laws by replacing the Bermuda company with a company headquartered in Malta or the United Arab Emirates, thus keeping all the key ingredients of the sandwich structure in place. *See* Jeffrey L. Rubinger & Summer Ayers Lepree, *Death of the "Double Irish Dutch Sandwich"? Not So Fast, Taxes Without Borders* (Oct. 23, 2014), http://www.taxeswithoutbordersblog.com/2014/10/death-of-the-double-irish-dutch-sandwich-not-so-fast [https://perma.cc/PXQ8-AFL9].
[133] FY 2017 Greenbook, *supra* note 33, at 265 tbl.
[134] 26 U.S.C. § 901(b)(1).
[135] 26 U.S.C. § 903.
[136] *See, e.g.*, John P. Steines, Jr., *The Foreign Tax Credit at Ninety-Five: Bionic Centenarian*, 66 TAX L. REV. 545, 554 (2013) (describing the mechanics of the foreign tax credit).
[137] 26 C.F.R. § 1.901-2(a)(2)(ii).

facts-and-circumstances test for determining whether a foreign levy qualifies as a creditable tax or as a deductible expense.[138] The regulations also establish a safe harbor for dual capacity taxpayers who want to claim a foreign tax credit without going through the trouble of proving that the levy qualifies as a tax under the facts-and-circumstances test.[134a] The safe harbor allows the taxpayer to compute the creditable tax based on the general tax rate in the foreign country, or—if the foreign country does not impose a general tax—based on the applicable U.S. federal tax rate.[139]

In the Greenbook for fiscal year 1998, the Clinton administration proposed a change to the dual capacity rules: under the Clinton proposal, dual capacity taxpayers would not be able to claim a credit for payments to a foreign government if the foreign country has no general tax.[140] The Clinton administration repeated the proposal in its Greenbook for fiscal years 1999, 2000, and 2001.[141] The Obama administration included similar proposals in the Greenbooks for fiscal years 2010 through 2017.[142] Treasury's most recent estimate is that the proposal, if implemented, would raise revenues by more than $9.6 billion over the next decade.[143]

While both President Clinton and President Obama asked Congress to amend the rules for dual capacity taxpayers, it seems that the Treasury Department could adopt this proposal unilaterally if it chose. No statute unambiguously allows a dual capacity taxpayer to claim a credit for payments made to a foreign country with no general tax. If anything, section 903 suggests that such payments should *not* be creditable: if there is no general tax, then the payment is not made "in lieu of a tax on income . . . generally imposed by [the] foreign country."[144] The safe harbor that the last two Democratic Presidents sought to eliminate is a safe harbor created by regulations that Treasury could rescind. Nonetheless, the Clinton and Obama administrations declined to act on their own, even though their statutory authority to do so seems to be quite clear.

4. Repealing the Lower-of-Cost-or-Market Inventory Accounting Method

Taxpayers that sell goods as part of an active trade or business can claim a deduction for the cost of goods sold that tax year. Rather than tracking inventory on an item-by-item basis, taxpayers can determine the cost of goods sold by adding the value of their inventory at the start of the year to the value of purchases made

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[138] 26 C.F.R. § 1.901-2A(b)-(c).
[134a] § 1.901-2A(c)(3),(e).
[139] § 1.901-2A(e).
[140] U.S. Dep't of the Treasury, General Explanations of the Administration's Revenue Proposals 74 (Feb. 1997) [hereinafter FY 1998 Greenbook].
[141] *See* Staff of the Joint Comm. on Tax'n, JCS-2-00, Description of Revenue Provisions Contained in the President's Fiscal Year 2001 Budget Proposal 539 (Mar. 6, 2000) (discussing proposal's history).
[142] *See* FY 2010 Greenbook, *supra* note 33, at 39–40; FY 2011 Greenbook, *supra* note 33, at 49–50; FY 2012 Greenbook, *supra* note 33, at 49–50; FY 2013 Greenbook, *supra* note 33, at 94–95; FY 2014 Greenbook, *supra* note 33, at 55–56; FY 2015 Greenbook, *supra* note 33, at 51–52; FY 2016 Greenbook, supra note 33, at 26-27; FY 2017 Greenbook, supra note 33, at 16-17.
[143] FY 2017 Greenbook, *supra* note 33, at 265 tbl.1.
[144] *See* 26 U.S.C. § 903.

during the year and subtracting the value of their end-of-year inventory.[140a] Congress has delegated authority to the Treasury Secretary to prescribe methods for inventory accounting. The relevant statute, section 471, reads:

> Whenever in the opinion of the Secretary the use of inventories is necessary in order clearly to determine the income of any taxpayer, inventories shall be taken by such taxpayer on such basis as the Secretary may prescribe as conforming as nearly as may be to the best accounting practice in the trade or business and as most clearly reflecting the income.[145]

One of the approaches allowed by Treasury is the "lower-of-cost-or-market" (LCM) method.[146] Under the LCM method, a taxpayer values inventory at the end of the year by taking the lower of (1) the cost of goods and (2) the market value. LCM thus allows taxpayers to take a write-down when the market value of inventory goods has declined. This means that taxpayers can recognize losses even before goods are sold or exchanged—in marked contrast to the general tax law principle of realization.[147]

No statute specifically authorizes taxpayers to use LCM. The ability of taxpayers to use LCM arises due to Treasury regulations, and section 471 gives broad discretion to the Treasury Secretary. Nonetheless, both President Clinton and President Obama asked Congress to repeal LCM, rather than amending the inventory regulations on their own.[143a] Proposals to repeal LCM have appeared in the Greenbooks for fiscal years 1997 through 2001 and every year in which President Obama has been in office.[148] The Treasury Department now estimates that repealing LCM would raise revenue by approximately $6.8 billion over the next decade.[149]

5. Modifying the Gift Tax Rules for Grantor Retained Annuity Trusts

Section 2702 governs the gift tax treatment of transfers of interests in trusts among family members. As a general rule, when one family member (e.g., a mother)

140a *See* Staff of the Joint Comm. on Tax'n, JCS-2-12, Description of Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal 521 (June 2012).

145 26 U.S.C. § 471(a).

146 26 C.F.R. § 1.471-2(c).

147 *See* Staff of the Joint Comm. on Tax'n, JCS-2-12, Description of Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal 521–22 (June 2012).

143a *See* FY 1997 Greenbook, *supra* note 140, at 77; Staff of the Joint Comm. on Tax'n, JCS-2-12, Description of Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal 52122 (June 2012).

148 *See* FY 1997 Greenbook, *supra* note 140, at 77; U.S. Dep't of the Treasury, General Explanations of the Administration's Revenue Proposals 106 (Feb. 1998) [hereinafter FY 1999 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Revenue Proposals 148–49 (Feb. 1999) [hereinafter FY 2000 Greenbook]; U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2001 Revenue Proposals 161–62 (Feb. 2000) [hereinafter FY 2001 Greenbook]; FY 2010 Greenbook, *supra* note 33, at 118; FY 2011 Greenbook, supra note 33, at 96; FY 2012 Greenbook, supra note 33, at 64; FY 2013 Greenbook, *supra* note 33, at 131; FY 2014 Greenbook, *supra* note 33, at 89; FY 2015 Greenbook, *supra* note 33, at 94; FY 2016 Greenbook, supra note 33, at 110; FY 2017 Greenbook, supra note 33, at 106.

149 FY 2017 Greenbook, *supra* note 33, at 267 tbl. 1.

sets up a trust for the benefit of another family member (e.g., her son) but retains an interest in the trust herself, the value of the retained interest is treated as zero for gift tax purposes.[150] Section 2702 also creates an exception to the general rule: if the interest retained by the mother is a "qualified interest," then the value of the mother's interest "shall be determined under section 7520."[151] A "qualified interest" includes "any interest which consists of the right to receive fixed amounts payable not less frequently than annually."[152] Section 7520, in turn, directs the Treasury Secretary to publish tables setting forth interest rates based on the interest rates for federal debt.[153] These provisions give rise to a well-known gift tax avoidance opportunity: the grantor retained annuity trust (GRAT).[149a]

To see how an individual can avoid gift taxes through a GRAT, imagine that the mother transfers 175 shares of Facebook stock to a trust, with the trust set to distribute all of its assets to the son after two years. As of this writing, shares of Facebook were trading for around $114, so 175 shares would be worth roughly $20,000. Normally, the transfer would be treated as a gift from mother to son; if the mother had exhausted her lifetime gift tax exemption ($5.45 million) and her annual gift tax exclusion ($14,000), then the gift would be taxed at a 40% rate.[154] Now imagine that the trust also transfers a note to the mother obligating the trust to make annual payments to the mother of $10,271.04 for two years. Under the IRS's most recent section 7520 tables, the note would be valued (as of this writing) at $20,000.[155] The transfer of the note from the trust to the mother would "zero out" the transfer of the Facebook stock from the mother to the trust, resulting in no gift tax liability.

Readers familiar with the valuation of options but unfamiliar with GRATs may find this result peculiar. If Facebook's share price drops and the trust is unable to make payments to the mother, then the son is not liable: the mother gets whatever is remaining in the trust and the GRAT is said to have "failed."[156] But if Facebook's share price rises and the trust has assets left over after satisfying its obligations to the mother, then the gains go to the son. The arrangement essentially amounts to the transfer of a set of call options on Facebook stock from mother to son. As of this writing, the market value of the call options would be in the range of $3,000.[157] Yet

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[150] 26 U.S.C. § 2702(a)(1)-(2).
[151] *Id.* at § 2702(a)(2)(B).
[152] *Id.* at § 2702(b)(1).
[153] *Id.* at § 7520(a).
[149a] *See* Staff of the Joint Comm. on Tax'n, *supra* note 145 at 269–71.
[154] *E.g.*, Internal Revenue Serv., What's New—Estate and Gift Tax, https://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Whats-New-Estate-and-Gift-Tax [https://perma.cc/ELP7-KTMA] (last updated Feb. 12, 2016).
[155] *See* Internal Revenue Serv., Section 7520 Interest Rates, https://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Section-7520-Interest-Rates [https://perma.cc/6687-4SVE] (last updated Feb. 18, 2016). The section 7520 interest rate for March 2016 is 1.8%.
[156] *See* Andrew Katzenstein & Stephanie Zaffos, *When Assets Given to a GRAT Decline in Value*, 2010 EMERGING ISSUES 5244, 5246 (LexisNexis).
[157] As of this writing, a call option on one share of Facebook stock with a strike price of $115 and a January 2017 expiration date was roughly $13; the value of an otherwise-identical option with a January 2018 expiration date was about $21. See NASDAQ, Facebook, Inc. (FB) Option Chain, http://www.nasdaq.com/symbol/fb/option-chain [https://perma.cc/Z9Y9-6D27] (last updated Apr. 1, 2016). The GRAT described in text is a combination of a one-year and two-year call.

under sections 2702 and 7520, the options worth $3,000 transferred from mother to son would be valued at zero for gift tax purposes.

Does the text of the Internal Revenue Code require this anomalous result? Not necessarily. Section 7520(b) states that "[t]his section shall not apply for purposes of . . . any . . . provision specified in regulations."[158] And section 7805 authorizes the Treasury Secretary to "prescribe all needful rules and regulations for the enforcement of this title."[159] Exercising his authority under these provisions, the Secretary might—for instance—promulgate a rule stating that the section 7520 tables should not be used to value a retained interest if the interest consists of the right to receive fixed amounts but there is a substantial risk of nonpayment because the trust is thinly capitalized. The Secretary might set forth specific criteria to assess whether a trust is thinly capitalized (e.g., if the remainder interest is less than 25% of the trust's assets). The Secretary might point to the language in the definition of "qualified interest"—"the right to receive fixed amounts"[160]—and say that an interest does not qualify if the trust's liabilities are so high relative to its assets that the "fixed" payments are subject to significant uncertainty. The Secretary might also invoke his authority under section 7520(b) to limit the use of the tables, as well as his general authority to promulgate anti-abuse regulations under section 7805.[156a]

To be sure, the Secretary's authority to crack down on undercapitalized GRATs is not entirely certain. When the IRS under President Clinton sought to challenge the Walton family's use of zeroed-out GRATs, the Tax Court ruled in favor of the Waltons and against the Service.[161] Yet in that case, the Tax Court emphasized that the IRS had not promulgated a legislative rule restricting zeroed-out GRATs, and the court suggested that IRS might receive greater deference if it had followed the legislative-rule route.[162] But instead of initiating a notice-and-comment process and promulgating new rules, the Obama administration repeatedly asked Congress to intervene. The past two Greenbooks, for example, have included a proposal to deny "qualified interest" status when a GRAT is undercapitalized.[163]

6. Disallowing the Deduction for Upward Development Easements

Whatever the uncertainty regarding the President's ability to restrict the use of zeroed-out GRATs, his power to crack down on abuse of section 170(h) seems

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[158] 26 U.S.C. § 7520(b).
[159] *Id.* at § 7805(a).
[160] *Id.* at § 2702(b)(1).
[156a] *See id.* at §§ 7520(b), 7805(b)(3).
[161] *See* Walton v. Comm'r, 115 T.C. 589, 603–04 (2000).
[162] *See id.* at 597 ("The regulations at issue here are interpretative regulations . . . . Hence, while entitled to considerable weight, they are accorded less deference than would be legislative regulations issued under a specific grant of authority to address a matter raised by the pertinent statute.").
[163] *See* FY 2017 Greenbook, *supra* note 33, at 181 ("The proposal also would include a requirement that the remainder interest in the GRAT at the time the interest is created must have a minimum value equal to the greater of 25 percent of the value of the assets contributed to the GRAT or $500,000 (but not more than the value of the assets contributed)."); *accord* FY 2016 Greenbook, *supra* note 33, at 198.

quite clear. That provision allows taxpayers to claim a deduction for a contribution of a partial interest in real property to a qualified organization if the contribution is "exclusively for conservation purposes." [164] Section 170(h) also defines "conservation purpose" to include "the preservation of an historically important land area or a certified historic structure."[165] Under this provision, a taxpayer who lives in a house listed in the National Register of Historic Places or located in a registered historic district might donate an easement to an architectural trust that prevents the taxpayer or any future owner of the house from substantially altering the exterior or interior of the home; the taxpayer could claim a deduction for the value of the easement (subject to certain conditions regarding appraisal and public access).[166] Some taxpayers have sought to claim a deduction for contributing an "air rights" easement to an architectural trust—that is, an easement restricting development in the air space above a historic structure they own.[167] The Treasury Department has expressed concerns about "abuses" of section 170(h), specifically in cases in which taxpayers "have taken large deductions for contributions of easements restricting the upward development of historic urban buildings even though such development was already restricted by local authorities."[168]

President Obama repeatedly asked Congress to pass legislation that would address abuses of the deduction for conservation easements. In the Greenbook for fiscal year 2014, the President included a proposal to "disallow a deduction for any value of an historic preservation easement associated with forgone upward development above an historic building."[169] The President reiterated this proposal in his Greenbooks for fiscal years 2015, 2016, and 2017.[170] The President did not, however, instruct the Treasury Department to take regulatory action against deductions for upward development easements, even though the Executive Branch likely has the authority to prohibit such deductions on its own.

Recall that the relevant statutory definition of "conservation purpose" is "the preservation of an historically important land area or a certified historic structure."[171] Treasury could promulgate regulations stating that restrictions on upward development do not "preserv[e]" an important land area or historic structure.[167a] A taxpayer challenging the regulation would have a difficult time arguing that the term "historically important land area" unambiguously includes air rights: after all, at least for easements applying to air space above an existing

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164 26 U.S.C. § 170(h)(1)(C) (defining "qualified conservation contribution" to include a contribution "exclusively for conservation purposes"); *see also id.* at § 170(f)(3)(A) (denying a deduction for certain contributions of partial interests in property); *id.* at § 170(f)(3)(B)(iii) (allowing an exception for a "qualified conservation contribution").

165 *Id.* at § 170(h)(4)(A)(iv).

166 *E.g.*, 26 C.F.R. § 1.170A-14 (d)(5)(v) (2016), example 1.

167 *See, e.g.*, Herman v. Comm'r, No. 14005-07, T.C. Memo 2009-205, 2009 Tax Ct. Memo LEXIS 209 at *12 (2009) (involving a taxpayer who sought to claim a deduction for contributing an air rights easement to preserve a certified historic structure).

168 *See* FY 2014 Greenbook, *supra* note 33, at 162.

169 FY 2014 Greenbook, *supra* note 33, at 162.

170 *See* FY 2015 Greenbook, *supra* note 33, at 196; FY 2016 Greenbook, *supra* note 33, at 188–89; FY 2017 Greenbook, *supra* note 33, at 216.

171 26 U.S.C. § 170(h)(4)(A)(iv) (2012).

167a *Herman*, *supra* note 163 at *12.

structure, the land is already covered by a building.[167b] A taxpayer would also have trouble convincing a court that the term "certified historic structure" unambiguously includes air space above the structure.[167c] In one case, Tax Court Judge David Gustafson noted that "[i]t might be argued that the appearance of a structure is 'preserved' in an aesthetic sense by an easement that prevents vertical development above its existing height," but Judge Gustafson's opinion does not suggest that this argument would prevail. (He ultimately concluded that the deduction claim failed on other grounds, even "[a]ssuming arguendo that there can be circumstances in which an 'air rights' easement accomplishes the preservation of a 'structure.'"[172]) And if there is any ambiguity as to whether an air rights easement "preserv[es]" a historic "structure," the only question in court would be whether the Treasury regulation "is a 'reasonable interpretation' of the enacted text."[173] On that standard, it is difficult to see how Treasury would lose.

7. Denying a Deduction for Payment of Punitive Damages

Section 162(a) allows taxpayers to claim a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business."[174] In 1969, Congress added a new section 162(f) that denies a deduction for "any fine or similar penalty paid to a government for the violation of any law."[175] The IRS, applying the rule of *expressio unius est exclusio alterius*, has interpreted the 1969 law to mean that payments of punitive damages *are* deductible, at least where such damages are "incurred by the taxpayer in the ordinary conduct of its business operations."[176] The Obama administration called on Congress each year since 2009 to change this rule and deny a deduction for punitive damages paid upon a judgment or in settlement of a claim.[177] Disallowing the deduction entirely would raise, according to Treasury's most recent estimate, $741 million over a decade.[178]

In a 1996 law review article, Kimberly Pace, then a law clerk to a judge on the Federal Circuit, suggested that section 162 as it stands does not require the conclusion that punitive damages are deductible.[179] (Kimberly Pace is now Kimberly Moore, and she is no longer a clerk to a Federal Circuit judge but a Federal Circuit judge herself.) Pace's article pointed to two paths that Treasury and the IRS might follow if they sought to argue against deductibility. First, Pace suggested that payments of punitive damages might fall within the ambit of section

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[167b] *Id.*
[167c] *Id.*
[172] *Id.*, at *23.
[173] *Id.* at 12; Mayo Found. for Med. Educ. & Research v. United States, 562 U.S. 44, 58 (2011).
[174] 26 U.S.C. § 162(a).
[175] Tax Reform Act of 1969, Pub. L. No. 91-172, § 902(f), 83 Stat. 710.
[176] Rev. Rul. 80-221, 1980-2 C.B. 57.
[177] *See* FY 2010 Greenbook, *supra* note 33, at 117; FY 2011 Greenbook, *supra* note 33, at 95; FY 2012 Greenbook, *supra* note 33, at 63; FY 2013 Greenbook, *supra* note 33, at 139; FY 2014 Greenbook, *supra* note 33, at 95; FY 2015 Greenbook, *supra* note 33, at 101; FY 2016 Greenbook, *supra* note 33, at 116; FY 2017 Greenbook, *supra* note 33, at 111.
[178] FY 2017 Greenbook, *supra* note 33, at 267 tbl.
[179] Kimberly A. Pace, *The Tax Deductibility of Punitive Damage Payments: Who Should Ultimately Bear the Burden for Corporate Misconduct?*, 47 ALA. L. REV. 825, 828 (1996).

162(f): they may amount to a "fine or similar penalty paid to a government for the violation of any law."[180] This argument runs into the obvious obstacle that punitive damages are generally paid to private plaintiffs and not "paid to a government," although there are important exceptions. Certain statutes, such as the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (the "Superfund" law), allow the federal government to seek punitive damages.[181] When punitive damages are paid to a federal or state government plaintiff, the IRS might reasonably argue that such damages are a "penalty . . . for the violation of the law" and thus the section 162(f) exception applies. Moreover, eight states currently have "split-recovery" statutes providing for partial payment of punitive damages awards to state funds.[182] The IRS might argue (again, quite reasonably) that the portion of punitive damages awards payable to the state is nondeductible for federal tax purposes.[183]

Another possible—though more controversial—approach would be for Treasury and the IRS to argue that punitive damages are not "ordinary and necessary" business expenses under section 162(a). As the Supreme Court recently noted, "[p]unitive damages have long been an available remedy at common law for wanton, willful, or outrageous conduct."[184] Pace asks: "How could a corporation claim, or a court hold, that behavior which rises to that egregious level is a necessary part of doing business, or that such an expense is an ordinary, unavoidable part of business?"[185] Note, moreover, that if Treasury promulgated regulations interpreting section 162 to disallow a deduction for punitive damages, the relevant question under *Chevron* and *Mayo Foundation* would be whether Treasury's interpretation of the phrase "ordinary and necessary" is "permissible"—not whether Treasury's interpretation of the statutory language is the *best* reading of the text.

To be sure, the argument that Treasury has authority to disallow deductions for punitive damages under section 162 is far from airtight. In addition to the *expressio unius* implication from section 162(f), the Senate Finance Committee report accompanying the 1969 law is inconvenient: the report states that the statutory exceptions to the general rule of deductibility under section 162 are "intended to be all inclusive."[186] Treasury might argue that the *expressio unius* canon is a guide rather than an ironclad rule[187] and that one-house legislative history is not

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[180] *Id.* at 827, 872–78.

[181] 42 U.S.C. § 9607(c)(3); *see also, e.g.*, 10 U.S.C. § 2207(a) (if Secretary of Defense finds that contractor "offered or gave any gratuity . . . to an officer, official, or employee of the United States to obtain a contract or favorable treatment . . . concerning the . . . contract," United States "is entitled to exemplary damages in an amount at least three, but not more than 10 . . . , times the cost incurred by the contractor in giving gratuities"); 33 U.S.C. § 1514(c) (punitive damages payable to the United States for willful violation of statutes and regulations related to deepwater ports).

[182] Skyler M. Sanders, Note, *Uncle Sam and the Partitioning Punitive Problem: A Federal Split-Recovery Statute or a Federal Tax?*, 40 PEPP. L. REV. 785, 833–35 app. A (2013).

[183] *See* Pace, *supra* note 179, at 876.

[184] Atl. Sounding Co. v. Townsend, 557 U.S. 404, 409 (2009).

[185] Pace, *supra* note 179, at 879–80.

[186] Senate Comm. on Finance, Tax Reform Act of 1969, S. Rep. No. 552, 91st Cong., 1st Sess. 274 (1969).

[187] *See, e.g.*, Barnhart v. Peabody Coal Co., 537 U.S. 149, 168 (2003) ("[T]he canon *expressio unius est exclusio alterius* does not apply to every statutory listing or grouping; it has force only when the items

determinative.[188] The point here is simply that the administration would have a plausible (though admittedly not rock solid) basis for regulations that either partially or fully disallow deductions for punitive damages payments under the existing section 162, without further legislative action.

F. Cases of Congressional Action

The examples above all were instances in which the President asked Congress for a legislative change instead of proceeding through regulation and Congress rebuffed the President's request. The Greenbook is not, however, an entirely empty exercise: sometimes Congress *does* act on the President's proposals—including proposals that the President, through Treasury and the IRS, could have implemented on his own. This section discusses some instances in which Congress has adopted Greenbook proposals that the administration likely could have implemented via regulation.

1. Preventing Taxpayers from "Splitting" Foreign Income and Foreign Tax Credits

One such example involves the "splitting" of foreign income and foreign tax credits. The "technical taxpayer rule," promulgated by the Treasury Department in 1983, provides that the person who can claim the foreign tax credit is "the person on whom foreign law imposes legal liability for such tax," even if another person actually pays the tax.[189] Until recently, the technical taxpayer rule allowed a U.S. taxpayer to claim a foreign tax credit for the current year even though the income on which that foreign tax was paid might not be subject to U.S. income tax until a future year (or, in some cases, might never be subject to U.S. income). In a typical "splitting" arrangement, a U.S. corporation (the grandparent) would establish an entity in Luxembourg (the parent) that would be disregarded under U.S. check-the-box rules; however, the parent would qualify as a corporation for Luxembourg tax purposes.[185a] The parent, in turn, would own another Luxembourg entity (the child), which would generate income subject to tax in Luxembourg.[185b] Since Luxembourg law imposes legal liability for the tax on the parent entity rather than the child corporation, the parent entity would be considered the "technical taxpayer" under the Treasury rule.[185c] Because the parent entity was a disregarded entity under the U.S. check-the-box regime, the U.S. grandparent would be able to claim the foreign tax credit. But the income earned by the child corporation would not be subject to U.S. tax unless and until it was repatriated. The arrangement thus allowed the U.S. grandparent to split the foreign tax credit (which it would claim

expressed are members of an 'associated group or series,' justifying the inference that items not mentioned were excluded by deliberate choice, not inadvertence.").

[188] *See, e.g.*, Hoffman Plastic Compounds, Inc. v. NLRB, 535 U.S. 137, 149–150 n.4 (2002) ("a single Committee Report from one House of a politically divided Congress . . . is a rather slender reed"). The 91st Congress was not politically divided, but a court disinclined to follow legislative history could no doubt find reason to disregard such history here.

[189] 26 C.F.R. § 1.901-2(f); *see* Treas. Dec. 7918, 48 Fed. Reg. 46,272 (Oct. 12, 1983).

[185a] *See, e.g.*, Guardian Industries Corp. v. United States, 477 F.3d 1368, 1369–70 (Fed. Cir. 2007) (describing a typical splitting arrangement).

[185b] *See id.*

[185c] *See id.* at 1374.

immediately) from the corresponding income (on which it potentially could defer U.S. tax indefinitely).[190]

The Treasury Department under President George W. Bush proposed regulations addressing credit splitting arrangements, but the Treasury Department did not finalize those regulations.[191] Then in the fiscal year 2010 Greenbook, President Obama asked Congress to pass legislation to prevent credit splitting, even though the opportunity for splitting was an opportunity created by the Treasury Department's own technical taxpayer rule rather than by statute.[192] At the time, the staff of the Joint Committee on Taxation asked "whether congressional action is necessary" or "whether, instead, the IRS and Treasury Department could simply finalize the proposed regulations . . . in the desired form."[193] Nonetheless, Congress passed—and President Obama signed—legislation providing that taxpayers cannot claim a foreign tax credit until the related income is taken into account.[194]

2. Matching OID Deductions with Income Inclusions

The Deficit Reduction Act of 1981 amended the statutory rules regarding original issue discount to add a special rule for OID on obligations to related foreign persons. The amendment prevented the obligor (i.e., borrower) from claiming a deduction until the obligee (i.e., lender) has been paid.[195] In January 1993, shortly before President George H.W. Bush left office, the Treasury Department finalized regulations carving out an exemption from the special rule for cases in which the related foreign person is a foreign personal holding company (FPHC), a controlled foreign corporation (CFC), or a passive foreign investment company (PFIC).[191a] The 1993 rule allowed a taxpayer to claim a deduction for OID as of the day on which a corresponding amount is includible in the income of the FPHC, CFC, or PFIC, without waiting until the amount is paid.[196] However, an amount may be includible in the income of an FPHC, CFC, or PFIC before it is includible in the income of the entity's U.S. owners. This meant that U.S. taxpayers, in some cases, could claim a deduction for OID on debt to a related foreign person even though no money changed hands and no other U.S. taxpayer included that amount in income.[197]

Since the opportunity for mismatch of deductions and income inclusions had been created by a Treasury regulation, the Clinton administration could have prevented mismatch by rescinding that regulation. Instead, the Clinton administration asked Congress in the Greenbooks for fiscal years 2000 and 2001 to

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[190] *See id.* at 1375 (holding that the U.S. grandparent corporation could claim an immediate foreign tax credit under similar circumstances).
[191] See 71 Fed. Reg. 44,240 (Aug. 4, 2006).
[192] See FY 2010 Greenbook, supra note 2, at 31.;
[193] Staff of the Joint Comm. on Tax'n, JCS-4-09, Description of Revenue Provisions Contained in the President's Fiscal Year 2010 Budget Proposal—Part Three: Provisions Related to the Taxation of Cross-Border Income and Investment 100 (Sept. 2009).
[194] Pub. L. No. 111-226, § 211(a), 124 Stat. 2394 (2010).
[195] Pub. L. No. 98-369, § 128(c), 98 Stat. 494, 654 (1981); *see* 26 U.S.C. § 163(e)(3)(A).
[191a] *See* Treas. Dec. 8465, 58 Fed. Reg. 235 (Jan. 5, 1993).
[196] *See id.*
[197] Staff of the Joint Comm. on Tax'n, JCS-2-00, Description of Revenue Provisions Contained in the President's Fiscal Year 2001 Budget Proposal 315–17 (Mar. 6, 2000).

override the Treasury rule by statute.[198] Congress took no action for several years. Ultimately, the American Jobs Creation Act of 2004 did away with exemption for obligations to CFCs and PFICs; now, taxpayers can only claim deductions for OID on obligations to related CFCs and PFICs when a corresponding amount is included in the income of a U.S. person who owns stock in the CFC or PFIC.[199]

3. Requiring Information Reporting on Payments to Corporations

Since 1954, section 6041 of the Code has imposed information reporting requirements with respect to payments of $600 or more in the course of a taxpayer's trade or business. Specifically, section 6041 states that "[a]ll persons engaged in a trade or business and making payment in the course of such trade or business to another person . . . of $600 or more in any taxable year . . . shall render a true and accurate return" notifying the IRS of the amount of the payment and the name and address of the recipient.[200] By its terms, the reporting requirement covers payments made to corporations; the Code has long defined "person" to include "an individual, a trust, estate, partnership, association, company or corporation."[201] However, Treasury regulations dating back to 1960 carved out an exemption for "[p]ayments of any type made to corporations."[202]

The reporting exemption for payments to corporations opened up opportunities for tax evasion. As the National Taxpayer Advocate noted in her 2007 annual report to Congress, "[o]ne possible justification for the corporate exception to the information reporting requirements is that large corporations are less likely to underreport income than sole proprietors because they must account to unrelated shareholders for business earnings and expenses," but "these safeguards may not be present in many closely-held corporations." [203] The Taxpayer Advocate called for repeal of the exemption, and the Treasury Department under President George W. Bush agreed. But rather than instructing his Treasury Department to repeal the regulations that created the exemption, President Bush instead asked Congress to act legislatively.[204]

Why would the President ask Congress to change the tax statutes in order to require reporting for payments of $600 or more to corporations, when a statute requiring reporting for such payments had been on the books for more than a half-century? The Bush administration briefly addressed this question in the Greenbook for fiscal year 2009: "Although the exception for information reporting to corporations is set forth in existing regulations, because it has been in place for many years and because Congress, during that time period, has made numerous changes

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[198] FY 2000 Greenbook, *supra* note 148, at 114; FY 2001 Greenbook, *supra* note 148, at 133–34.

[199] Pub. L. No. 108-357, § 841, 118 Stat. 1418, 1597 (codified at 26 U.S.C. § 163(e)(3)(B)(i)). The 2004 Act also eliminated the FPHC status for future tax years.

[200] 26 U.S.C. § 6041(a); *see* Internal Revenue Code of 1954, 68A Stat. 3, 745.

[201] 26 U.S.C. § 7701(a); *see* Internal Revenue Code of 1954, 68A Stat. 3, 911.

[202] 26 C.F.R. § 1.6041-3(c) (1960). The 1960 regulations made an exception to the exception (i.e., required reporting for) certain rebates and refunds to patrons. 26 C.F.R. §§ 1.6044, 1.6044-1 (1960). Nonetheless, the vast majority of payments to corporations were exempt from reporting under the 1960 rules.

[203] 1 Taxpayer Advocate Serv., 2007 Annual Report to Congress 495 (2007).

[204] *See* U.S. Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2009 Revenue Proposals 63 (Feb. 2008).

to the information reporting rules, elimination of the exception should be made by legislative change."[205] The Bush administration estimated that repeal of the exemption would raise more than $8.2 billion in revenue over the next decade due to greater compliance, but it declined to take action without congressional cooperation.[206]

Ultimately, Congress did eliminate the exemption for payments to corporations as part of the Affordable Care Act of 2010. The ACA added a new subsection (i) to section 6041, which read: "Notwithstanding any regulation prescribed by the Secretary before the date of the enactment of this subsection, for purposes of this section the term 'person' includes any corporation that is not an organization exempt from tax under section 501(a)."[207] But subsection (i) was short-lived: Congress repealed it the following year; President Obama signed the repeal legislation; and payments to corporations remain exempt from the section 6041 reporting requirement.[208]

G. Back on the Regulatory Road

The inclusion of a proposal in the Greenbook does not, of course, preclude the same President or a successor from implementing the proposal via executive action. In at least three cases, Treasury and IRS have used their authority under existing statutes to implement a Greenbook proposal that previous Congresses rebuffed.

1. *Treating Signing Bonuses as "Wages" for FICA Taxes*

Since 1954, section 3402 has required employers to withhold tax on payments of "wages."[209] In 1958, the IRS issued a revenue ruling that addressed the application of section 3402 to bonus payments made to baseball players.[205a] The IRS concluded that a bonus "paid to a new player solely for signing his first contract, without any requirement of subsequent service," did not constitute "wages," and thus the baseball club was not required to withhold tax on the bonus.[210] The Federal Insurance Contributions Act (FICA) uses a definition of "wages" similar to the withholding statute, and thus the 1958 ruling indicated that signing bonuses would be exempt from Social Security and Medicare taxes as well if there was no subsequent-service requirement.[211]

In the Greenbooks for fiscal years 2000 and 2001, the Clinton administration included a proposal that would effectively override the 1958 revenue ruling and clarify that signing bonuses are "wages" for withholding and employment tax purposes, regardless of whether the bonus is conditioned on

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205 *Id.*
206 *See id.*
207 Pub. L. No. 111-148, § 9006(a), 124 Stat. 148, 855 (2010).
208 Pub. L. No. 112-9, § 2(a), 125 Stat. 36, 36 (2011).
209 26 U.S.C. § 3402.
205a Rev. Rul. 58-145, 1958-1 C.B. 360
210 *Id.*
211 *See* 26 U.S.C. § 3121.

subsequent service.[212] However, congressional action is generally not necessary to reverse a revenue ruling; the IRS can simply revoke the revenue ruling and issue a new one. Indeed, the IRS did exactly that in 2004: it issued a new revenue ruling revoking the 1958 decision and interpreting the term "wages" to include signing bonuses broadly. The 2004 ruling provided a straightforward justification for the IRS's revised interpretation: "amounts an employer pays an employee as remuneration for employment are wages"; "[e]mployment encompasses the establishment . . . of the employer-employee relationship"; so signing bonuses are wages if paid "in connection with establishing the employer-employee relationship."[213] The revenue ruling accomplished what the Greenbook proposal would have: signing bonuses are now considered wages for FICA and withholding purposes even if the bonuses are not contingent upon subsequent service.

The signing bonus change likely had a modest effect on revenues: according to the Clinton administration's last Greenbook, a reform along the same lines as the 2004 IRS ruling would raise receipts by $28 million over a decade.[214] What is more remarkable is how rare it was before the Obama administration's April 2016 inversion actions for Treasury to respond to the rebuff of a Greenbook request by implementing the measure via regulation.

2. Restricting Earnings Stripping by Expatriated Entities After an Inversion

Section 7874, enacted in 2004, sets forth specific rules that apply when a U.S. corporation is acquired by a foreign corporation and, after the acquisition, at least 60% of the stock of the combined entity is held by shareholders of the former U.S. corporation.[215] The U.S. corporation—now a subsidiary of the foreign parent—is treated as an "expatriated entity," and for the first 10 years after the inversion it is limited in its ability to claim deductions and credits for U.S. tax purposes.[216] These limitations do not, however, apply when the new multinational group created by combining the foreign parent and the U.S. corporation has "substantial business activities in the foreign country in which [the foreign parent] is created or organized, when compared to the [group's] total business activities."[217] Moreover, the limitations do little to prevent the U.S. subsidiary from reducing its U.S. tax liabilities through "earnings stripping" following an inversion. To see how an earnings-stripping strategy might work, imagine that a U.S. corporation inverts by merging with an Irish corporation and then issues a note as a dividend to the new Irish parent; the U.S. corporation would then pay interest on the note to the Irish parent and deduct those interest payments from U.S. income. The interest payment would be exempt from U.S. withholding tax under the U.S.-Ireland tax

[212] FY 2000 Greenbook, *supra* note 148, at 183; FY 2001 Greenbook, supra note 148, at 191-92.
[213] Rev. Rul. 2004-109, 2004-2 C.B. 958.
[214] FY 2001 Greenbook, *supra* note 148, at tbl.
[215] 26 U.S.C. § 7874(a)(2). The provision also applies to the acquisition of U.S. partnerships by foreign corporations.
[216] *See id.* at § 7874(a)(1), (d), (e). If shareholders of the former domestic corporation hold 80% or more of the combined entity after the inversion, the transaction is essentially disregarded and the foreign parent is subject to U.S. tax as if it were a U.S. corporation. *See id.* at § 7874(b).
[217] *See id.* at § 7874(a)(2)(B)(iii).

treaty and subject to only a 12.5% Irish corporate tax.[218] The net result would be to reduce the multinational group's tax rate on U.S. income from 35% (the top U.S. corporate income tax rate) to 15% (the U.S. withholding rate).[219]

The Obama administration took a number of relatively modest regulatory measures to limit corporate inversions prior to 2016.[220] Meanwhile, the President asked Congress to act to pass legislation limiting earnings stripping in connection with corporate inversions. President Obama's first Greenbook included a proposal that would limit the ability of "expatriated entities" to engage in earnings-stripping transactions with their foreign affiliates; under that proposal, a U.S. corporation that engages in an inversion could not reduce its taxable income by more than 25% through intragroup debt.[221] For the next four years, the President's Greenbook included the same proposal;[222] every time, Congress failed to act. Meanwhile, more than two dozen U.S. corporations completed inversion transactions.[223]

Outside the administration, several tax lawyers and academics—most notably Harvard Law School lecturer Stephen Shay—argued that Treasury already had ample authority to limit earnings stripping by U.S. corporations that invert.[224] One important source of Executive Branch authority is section 385 of the Code, which authorizes the Treasury Secretary to "prescribe such regulations as may be necessary or appropriate" to determine whether an interest in a corporation should

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[218] *See* Willard B. Taylor, Letter to the Editor, *A Comment on Eric Solomon's Article on Corporate Inversions*, 68 TAX NOTES INT'L 101 (Oct. 1, 2012); Interval Revenue Serv., Publication 901 tbl.1, https://www.irs.gov/publications/p901/ar02.html [https://perma.cc/TE3T-9WWZ] (last visited Mar. 5, 2016).

[219] Section 163(j) is designed to limit earnings stripping, but in practice it has failed to prevent U.S. corporations from using related party debt to zero out their U.S. income tax liabilities following an inversion. *See* Jim A. Seida & William F. Wempe, *Effective Tax Rate Changes and Earnings Stripping Following Corporate Inversion*, 57 NAT'L TAX J. 805, 807 (2004); U.S. Dep't of the Treasury, Report to the Congress on Earnings Stripping, Transfer Pricing and U.S. Income Tax Treaties 29 (2007).

[220] In 2012, the Treasury Department promulgated temporary regulations interpreting the term "substantial business activities" in section 7874 to mean that at least 25% of the employees, assets, and income of the multinational group must be located in or derived from the relevant foreign country. *See* Treas. Dec. 9592, 77 Fed. Reg. 34,785 (June 12, 2012). The 25% figure marked a change from temporary regulations promulgated by the Bush Treasury Department in 2006 that interpreted the term "substantial business activities" to mean at least 10% of employees, assets, and income. Treasury and the IRS promulgated additional rules regarding inversions in 2014 and 2015, but none of these measures materially limited earnings stripping by inverted firms. *See* IRS Notice 2014-52; IRS Notice 2015-79.

[221] *See* FY 2010 Greenbook, *supra* note 33, at 33.

[222] FY 2011 Greenbook, *supra* note 33, at 46; FY 2012 Greenbook, *supra* note 33, at 47; FY 2013 Greenbook, *supra* note 33, at 92; FY 2014 Greenbook, *supra* note 33, at 53.

[223] Jesse Drucker & Zachary R. Mider, *Tax Inversion: How U.S. Companies Buy Tax Breaks*, BLOOMBERG QUICKTAKE (Nov. 13, 2015), https://www.bloomberg.com/quicktake/tax-inversion [https://perma.cc/TE3T-9WWZ].

[224] Stephen E. Shay, *Mr. Secretary, Take the Tax Juice Out of Corporate Expatriations*, TAX NOTES, July 28, 2014, http://www.taxanalysts.org/content/mr-secretary-take-tax-juice-out-corporate-expatriations [https://perma.cc/7KN6-ZF36] ; *see also* Victor Fleischer, *How Obama Can Stop Corporate Expatriations, for Now*, N.Y. TIMES: DEALBOOK, Aug. 7, 2014, http://dealbook.nytimes.com/2014/08/07/how-obama-can-stop-corporate-expatriations-for-now [https://perma.cc/9DHK-AWFW]; Steven M. Rosenthal, *Professor Shay Got It Right: Treasury Can Slow Inversions*, TAX NOTES, Sept. 22, 2014, http://www.taxanalysts.org/content/professor-shay-got-it-right-treasury-can-slow-inversions [https://perma.cc/CH8F-N6LG].

be treated as debt or equity.[225] Shay argued that Treasury could use its authority under section 385 to classify as "equity" any debt issued by a U.S. corporation to a foreign affiliate as part of an earnings-stripping transaction.[226]

In April 2016, the Obama administration took up a version of Shay's proposal. (As noted in the introduction, the action came after pharmaceutical giant Pfizer announced plans to merge with Irish counterpart Allergan—a transaction that Pfizer said would reduce its tax bill by $1 billion a year.[227]) Perhaps most significantly, the Treasury Department published proposed regulations providing that when a U.S. corporation issues a note to a foreign affiliate as part of a dividend distribution, the note will be treated as equity rather than debt (and thus the U.S. corporation's "interest" on the note will be nondeductible).[228] The proposed regulation and other temporary and final regulations promulgated in April 2016[229] substantially limit the tax benefits for U.S. corporations that merge into foreign counterparts.

3. Curbing Valuation Discounts in Family Limited Partnerships

For decades, wealthy individuals have used "family limited partnerships" (FLPs) to avoid estate and gift taxes on transfers to children and other relatives. To see how taxpayers can accomplish this objective through FLPs, consider the following example: A mother forms a corporation to which she contributes $1. The mother then forms a limited partnership with herself as the limited partner and the corporation as the general partner; the limited partnership holds $100 in assets, with $1 from the corporation and $99 directly from the mother. The mother then transfers half her limited partnership interest to her son and half to her daughter. But instead of reporting the value of the gift to each child as $49.50 (half of $99), the mother reports that the value of each gift is $33 (two-thirds of $49.50). She claims that the value of each child's limited partnership interest is less than $49.50 because neither child can force the partnership to be liquidated: the corporation, as the general partner, remains in charge.[230] This maneuver allows the mother to transfer more to her children than she otherwise could without incurring gift tax liabilities.

Section 2704, enacted in 1990, authorizes the Treasury Secretary to promulgate regulations disregarding restrictions on liquidation of a partnership in determining the amount of a gift if the restriction "does not ultimately reduce the value of such interest to the transferee."[231] Yet instead of exercising this authority initially, the Obama administration sought congressional support for changes to the

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[225] 26 U.S.C. § 385(a) (2012).
[226] *See* Shay, supra note 224.
[227] *See* Michael Hiltzik, *Pfizer Shows That Its Allergan Merger Was Only a Tax Dodge*, L.A. TIMES, Apr. 6, 2016, http://www.latimes.com/business/hiltzik/la-fi-hiltzik-pfizer-allergan-20160406-snap-htmlstory.html [https://perma.cc/H62Y-72AT].
[228] Treatment of Certain Interests in Corporations as Stock or Indebtedness, 81 Fed. Reg. 20912 (proposed Apr. 8, 2016) (to be codified at 26 C.F.R. pt. 1).
[229] *See* Inversions and Related Transactions: Final and Temporary Regulations, Treas. Dec. 9761, 81 Fed. Reg. 20858 (Apr. 8, 2016).
[230] For a similar example, *see* Karen C. Burke & Grayson M.P. McCouch, *Family Limited Partnerships: Discounts, Options, and Disappearing Value*, 6 FLA. TAX. REV. 649, 650–51 (2004).
[231] 26 U.S.C. § 2704(b)(4).

FLP rules. A proposal in the President's Greenbook for fiscal year 2013 would have curbed valuation discounts for FLP interests where another family member has the authority to lift any restrictions on liquidation.[232] The Treasury Department estimated that the change would save more than $18 billion over the course of a decade.[233]

The Obama administration's FLP proposal went nowhere in Congress. Finally, in August 2016, the Treasury Department published proposed regulations that utilize the authority granted to Treasury under section 2704.[234] The details of the proposal lie beyond the scope of this article, but suffice it to say (as the Assistant Secretary of the Treasury for Tax Policy announced in a blog post) that the new rules "significantly reduce the ability of [wealthy] taxpayers and their estates to use [FLP] techniques solely for the purpose of lowering their estate and gift taxes."[235]

The Obama administration's April 2016 actions on inversions and the August 2016 proposed rules on FLPs are important exceptions to the claim that the President rarely resorts to regulation when Congress rebuffs his requests for revenue-raising regulation. Yet as argued below,[236] the timing of these measures is consistent with a model of executive-legislation interactions that also accounts for the general reluctance of President Obama and his predecessors to implement revenue-raising tax measures unilaterally. For now, keep in mind the facts that (a) the Obama administration ultimately did act without Congress to implement two important measures previously on the President's legislative agenda and (b) these actions occurred in the last year of the President's second term, at a time of legislative gridlock, and as polls and prediction markets showed a very high likelihood of the President's party retaining the White House.[237]

H. Congressional "Overrides" of Revenue Raising Regulations

Even when the President and his Treasury Department do decide to act unilaterally, that is not necessarily the end of the story. Congress still may seek to prevent Treasury from finalizing or implementing regulations. On several occasions, Congress has passed measures that stopped the Treasury Department from moving forward with a regulatory initiative. The year 1978 was a high

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[232] *See* FY 2013 Greenbook, *supra* note 33, at 79.
[233] *Id.* at 202 tbl.1.
[234] Estate, Gift, and Generation-skipping Transfer Taxes; Restrictions on Liquidation of an Interest: Notice of Proposed Rulemaking and Notice of Public Hearing, 81 Fed. Reg. 51413 (Aug. 4, 2016).
[235] Mark J. Mazur, *Treasury Issues Proposed Regulations to Close Estate and Gift Tax Loophole*, TREASURY NOTES, Aug. 2, 2016, https://www.treasury.gov/connect/blog/Pages/Treasury-Issues-Proposed-Regulations-to-Close-Estate-and-Gift-Tax-Loophole.aspx [https://perma.cc/V7UZ-NA8U].
[236] *See infra* notes __-__ and accompanying text.
[237] *See* HuffPost Pollster, 2016 General Election: Trump vs. Clinton, http://elections.huffingtonpost.com/pollster/2016-general-election-trump-vs-clinton [https://perma.cc/54ZK-3RUQ] (last visited Aug. 15, 2016) (showing Hillary Clinton leading Donald Trump by 9 percentage points on April 4, 2016, the date the inversion actions were announced, and by 8 percentage points on August 2, the date the proposed FLP rules were announced); Iowa Electronic Markets, Market Quotes: Pres16_WTA, https://iemweb.biz.uiowa.edu/quotes/Pres16_quotes.html [https://perma.cc/FM3Y-LDG3] (last visited Aug. 15, 2016) (showing that the prediction-market odds of Clinton beating Trump were about 69% on April 4 and 73% on August 2).

watermark for congressional action of this sort. In that year, Congress passed legislation temporarily prohibiting Treasury from issuing regulations regarding the definition of "fringe benefits,"[238] the deductibility of commuting expenses,[239] and the classification of workers as "employees" or "independent contractors" for employment tax purposes.[240] (The moratorium on regulations addressing the employee/independent contractor distinction was later extended to be a permanent ban.[241]) Congress also enacted a prohibition on regulations regarding the timing of taxes on non-qualified deferred compensation plan payments in the private sector.[242] That measure was aimed at blocking an unpopular proposed Treasury regulation,[243] and the prohibition lasted for a quarter century.[244] Similarly, the Taxpayer Relief Act of 1997 imposed an 11-month moratorium on Treasury regulations regarding the definition of "limited partner" for purposes of federal self-employment income taxes.[245] And in December 2015, Congress passed an appropriations rider barring the Treasury Department from using any funds to finalize proposed regulations regarding the involvement of tax-exempt organizations in political campaigns.[246]

These congressional "overrides" might lead some readers to question whether the Executive Branch really has the authority to implement revenue-

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[238] Act of Oct. 7, 1978, Pub. L. No. 95-427, § 1, 92 Stat. 996, 996. The moratorium was initially set to expire at the end of 1979 but was extended through 1983. *See* 26 U.S.C. § 61 note.

[239] Act of Oct. 7, 1978, Pub. L. No. 95-427, § 2, 92 Stat. 996, 996. The IRS had sought to limit the deductibility of certain commuting expenses in a 1976 revenue ruling. *See* Rev. Rul. 76-453, 1976-2 C.B. 86. The 1978 legislation, as later amended, prevented the IRS from implementing the ruling until the end of May 1981. *See* 26 U.S.C. § 62 note.

[240] Revenue Act of 1978, Pub. L. No. 95-600, § 530, 92 Stat. 2763, 2886 (codified as amended at 26 U.S.C.A. § 3401 note); *see also* William Hays Weissman, Nat'l Ass'n of Tax Reporting and Prof'l Mgmt., *Section 530: Its History and Application in Light of the Federal Definition of the Employer-Employee Relationship for Federal Tax Purposes*, (Feb. 28, 2009), available at https://www.irs.gov/pub/irs-utl/irpac-br_530_relief_-_appendix_natrm_paper_09032009.pdf [https://perma.cc/BGY7-EZY9] (discussing history of ban on employee/independent contractor regulations and revenue rulings).

[241] 26 U.S.C. § 3401 note.

[242] Revenue Act of 1978, Pub. L. No. 95-600, § 132, 92 Stat. 2763, 2782. Specifically, the Revenue Act of 1978 said that "[t]he taxable year of inclusion in gross income of any amount covered by a private deferred compensation plan shall be determined in accordance with the principles set forth in regulations, rulings, and judicial decisions . . . which were in effect on February 1" of that year. The statutory language effectively made any subsequent Treasury action on the subject null and void.

[243] Proposed Treas. Reg. § 1.61-16, 43 Fed. Reg. 4638 (1978).

[244] *See* American Jobs Creation Act of 2004, Pub. L. No. 108–357, § 885, 118 Stat. 1418, 1634 (2004) (codified at 26 U.S.C. § 409A); Michael Doran, *Time To Start Over on Deferred Compensation*, 28 VA. TAX. REV. 223, 224.

[245] Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788, 882. The 1997 legislation came in response to a controversial notice of proposed rulemaking, *see* 62 Fed. Reg. 1702 (Jan. 13, 1997); rather than waiting for the 11-month period to pass, Treasury declined to finalize the proposed rules even after the moratorium ended. *See* Lucia Nasuti Smeal & Tad D. Ransopher, *LLC Material Participation Policy Shift: New Regulations Focus on Management Rights*, 2 J. LEGAL ISSUES & CASES IN BUS. 1, 8 (2013).

[246] *See* Consolidated Appropriations Act of 2016, Pub. L. No. 114-113, § 127, 129 Stat. 2242, __ (2015). The regulations would have denied tax-exempt status to organizations that engage in "candidate-related political activity." 78 Fed. Reg. 71,535 (Nov. 29, 2013). *See* Paul C. Barton, *Confusion Over Judging Political Activity Still Reigns at IRS*, TAX NOTES, Feb. 4, 2016, http://www.taxnotes.com/featured-article/confusion-over-judging-political-activity-still-reigns-irs [https://perma.cc/BT3 V-EE27].

raising measures on its own. Note, though, that in the 1978, 1997, and 2015 cases, the President signed the bill imposing a moratorium or ban on regulatory action. Presidents Carter (in 1978), Clinton (in 1997), and Obama (in 2015) were unwilling to use their veto power in order to defend the Treasury Department's revenue-raising efforts. Of course, if the President had exercised his veto power in any of these instances, members of Congress might have sought to override the veto. However, veto overrides with respect to tax bills are rarer than lightning strikes: the last time that Congress overrode a President's veto of tax-related legislation was in 1948, when Harry Truman was in the White House.[247]

To be sure, Congress has other tools to express its opposition to revenue-raising executive action—and has ways aside from a veto override to punish the President for proceeding unilaterally. The Senate can refuse to confirm the President's nominees for Treasury posts[248] and also can refuse to ratify tax treaties that the President supports.[249] Moreover, both the House and the Senate can summon the administration's top tax officials before committees for time-consuming hearings.[245a] Note, though, tax is not unique in this regard: in other areas, Congress likewise can hold up nominations and haul administration officials before oversight committees for grueling hearings.[250] And yet recent Presidents have not been reluctant to proceed unilaterally in the face of potential congressional opposition—and retaliation—on a wide range of non-tax matters.

I. The Tax Cutter in Chief

Some of the examples above involved a President asking Congress to override a prior administration's action that had tested the limits of executive authority. Consider the decision by the first Bush administration to exempt obligations to FPHCs, CFCs, and PFICs from the rules otherwise applicable to OID debt (a decision ultimately overridden by Congress in 2004).[251] Treasury acknowledged in the notice announcing the proposed regulation that the special treatment of FPHCs, CFCs, and PFICs was "a substantial exception to the

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[247] Revenue Act of 1948, 62 Stat. 110; *see* U.S. Senate, Summaries of Bills Vetoed—1789-Present, http://www.senate.gov/reference/Legislation/Vetoes/vetoCounts.htm [https://perma.cc/7Z5X-9SMK] (last visited Apr. 3, 2016).

[248] *See* Shamik Trivedi, *Top Tax Nominees in Limbo, with Politics To Blame*, TAX NOTES, Jan. 30, 2012 at 522 (noting that for the first three years of the Obama presidency, the Senate refused to confirm President Obama's nominees to the posts of Assistant Secretary of the Treasury for Tax Policy and Assistant Attorney General in charge of the Justice Department's Tax Division).

[249] Indeed, Senate rules empower a single Senator to effectively block a nomination or treaty from going through. *See* Ryan Finley & William Hoke, *Tax Treaty Awaiting U.S. Senate Vote Face Uncertain Future*, TAX ANALYSTS WORLDWIDE TAX DAILY, Nov. 12, 2015 (noting that Senator Rand Paul, a Kentucky Republican, has held up eight pending tax treaties due to concerns about taxpayer privacy protections).

[245a] *See, e.g.*, Alan Rappaport, *I.R.S. Commissioner John Koskinen, on Hot Seat, Has History of Bureaucratic Rescue Jobs*, N.Y. TIMES, July 1, 2014, http://www.nytimes.com/2014/07/02/us/irs-commissioner-john-koskinen-on-hot-seat-has-history-of-bureaucratic-rescue-jobs.html (noting that IRS Commissioner John Koskinen "absorbed cascades of verbal salvos" from members of Congress at one hearing lasting "nearly four hours").

[250] The need for Senate ratification of tax treaties is one distinguishing feature of tax law—there is no obvious equivalent with respect to, e.g., health or labor policy.

[251] *See supra* Section I.F.2.

otherwise applicable general rule" for OID debt, but it cited no statutory provision supporting such an exception, nor did it point to any part of the relevant legislative history indicating that the exemption was consistent with congressional intent.[252]

Several other Treasury actions addressed above seem to fit this mold: examples include the exemption from section 6041 for corporations carved out by the Treasury Department under President Eisenhower,[253] the safe harbor for dual capacity taxpayers created by the Treasury Department under President Reagan,[254] and—arguably—the decision by the Treasury Department at the start of the Clinton administration allowing carried interest profits to be taxed at preferential rates.[255] For present purposes, I will focus on three Treasury actions—one from each of the past three administrations—that represent particularly bold assertions of executive power in a taxpayer-friendly direction. The first, alluded to above, is the 1996 rule promulgated by Treasury under President Clinton establishing the check-the-box regime. The second is a set of rules promulgated under the second President Bush and commonly known as the "*INDOPCO* regulations" though perhaps better termed the "anti-*INDOPCO* regulations" because they effectively overturn the Supreme Court's decision in *INDOPCO, Inc. v. Commissioner*.[256] The third is the Treasury Department's decision under President Obama allowing General Motors to make use of $45 billion in net operating loss carryforwards despite statutory restrictions that would seem to go against General Motors' position.

1. The Clinton Administration's Check-the-Box Regulations

Since 1924, federal tax law has defined the term "corporation" as "includ[ing] associations, joint-stock companies, and insurance companies."[257] While that definition is somewhat Delphic, the Supreme Court shed light on the scope of the term "corporation" in the 1935 case *Morrissey v. Commissioner*.[258] The "salient features" of a corporation, according to *Morrissey*, are (1) perpetual life, (2) centralized management, (3) free transferability of beneficial interests "without affecting the continuity of the enterprise," and (4) limited liability for owners.[259] A

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[252] Deduction of Amounts Owed to Related Foreign Persons—Notice of Proposed Rulemaking, 56 Fed. Reg. 11531 (Mar. 19, 1991).
[253] *See supra* text accompanying notes 200–202.
[254] *See supra* text accompanying notes 134–139.
[255] *See supra* text accompanying note 105.
[256] 503 U.S. 79 (1992).
[257] 26 U.S.C. § 7701(a)(3).
[258] 296 U.S. 344, 359 (1935).
[259] *Id.* at 359; *see* Gregg D. Polsky, *Can Treasury Overrule the Supreme Court?*, 84 BOS. U. L. REV. 185, 216 (2004). Note that Polsky's article preceded two Supreme Court decisions that likely place Treasury's actions on firmer ground. The first, *National Cable & Telecommunications Association v. Brand X Internet Services*, held that "[a] court's prior construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion." 545 U.S. 967, 982 (2005). Then in 2011, the Court clarified in *Mayo* that the *Chevron* framework applies to Treasury regulations. *See supra* Section I.C. The combination of holdings would seem to suggest that the Supreme Court's prior interpretations of the tax code in *Morrissey* and *INDOPCO* can be trumped by subsequent Treasury pronouncements. The argument in text here, though, is not that the check-the-box and *INDOPCO* regulations are illegal. Rather,

quarter century after *Morrissey*, the Treasury Department under President Eisenhower promulgated regulations codifying the *Morrissey* factors.[260] This test governed for the next three dozen years.

In 1996, however, the Clinton administration announced a dramatic change to the decades-old regime. The Treasury Department promulgated regulations allowing unincorporated business entities other than publicly traded enterprises to elect whether or not they will be taxed as corporations. Some foreign business entities are treated as "per se corporations" under check-the-box, but a wide variety of foreign entities enjoy freedom of choice.[261]

Several commentators have questioned Treasury's authority to promulgate the check-the-box rules.[262] The Supreme Court has held that "[o]nce we have determined a statute's meaning," that interpretation becomes "settled law," and agencies are no longer entitled to deference if they adopt a conflicting interpretation of the same provision.[263] *Morrissey*, moreover, interpreted the meaning of the term "corporation" for purposes of the tax statutes; that interpretation would now seem to be "settled law."[259a] Two courts of appeals, though, have held that the check-the-box regulations do not contravene *Morrissey*,[264] largely laying the issue to rest. But valid or not, the check-the-box regulations certainly represent a robust exercise of executive authority. In this regard, they stand in stark contrast to the modus operandi of past Presidents with respect to revenue-raising measures.

2. The Bush Administration's INDOPCO *Regulations*

The Supreme Court's *INDOPCO* decision construed Code provisions relating to the deductibility of business expenses.[265] In *INDOPCO* itself, a corporation formerly known as National Starch claimed deductions for fees paid to investment bankers and lawyers in connection with a friendly takeover of National Starch by Unilever.[261a] The Supreme Court ruled that the fees were capital expenditures rather than immediately deductible business expenses. The Court's narrow holding was that expenses "incurred for the purpose of changing the

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the argument is that at the time they were issued these regulations represented much more robust assertions of executive authority than is typical in the revenue-raising context.

[260] Treas. Dec. 6503, 1960-2 C.B. 409. The 1960 regulations stated that an enterprise would only be treated as a corporation if it exhibited at least three of the four corporate factors. On whether the 1960 regulations are themselves consistent with *Morrissey*, *see* Polsky, *supra* note 259, at 217–18.

[261] 61 Fed. Reg. 66584, 66845 (Dec. 18, 1996). Foreign entities that provide limited liability for their owners are treated as corporations by default, but can opt out of corporation status.

[262] *Compare* Polsky, *supra* note 259 (arguing that the regulations exceeded Treasury's authority), *with* Victor E. Fleischer, Note, *"If It Looks like a Duck": Corporate Resemblance and Check-the-Box Elective Tax Classification*, 96 COLUM. L. REV. 918 (1996) (arguing the opposite).

[263] *See, e.g.*, Neal v. United States, 516 U.S. 284, 295 (1996).

[259a] *See* Morrissey v. Comm'r, 296 U.S. 344, 359 (1935).

[264] *See* McNamee v. Dep't of the Treasury, 488 F.3d 100, 104–09 (2d Cir. 2007); Littriello v. United States, 484 F.3d 372, 378 (6th Cir. 2007).

[265] INDOPCO, Inc. v. Comm'r, 503 U.S. 79, 83–87 (1992); *see* 26 U.S.C. § 162(a) (deduction for "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business"); § 263(a)(1) (no deduction for "[a]ny amount paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate").

[261a] 503 U.S. 79 at 79–81, 88.

corporate structure for the benefit of future operations" must be capitalized;[266] the broader implication of the *INDOPCO* decision was that taxpayers must capitalize expenditures made for the "betterment" of the their business over a period of time "somewhat longer than the current taxable year."[267]

In 2004, a dozen years after *INDOPCO*, the Bush Treasury Department promulgated final regulations addressing the deductibility of amounts paid to create or acquire intangibles.[268] In several respects, the regulations deviated from the *INDOPCO* decision in a "taxpayer-favorable" direction.[269] For example, the regulations generally allow a taxpayer to immediately deduct amounts paid to create or acquire nonfinancial interests with a useful life of 12 months or less, even if the 12-month period extends over two taxable years.[270] The 12-month rule opens the door to planning opportunities that were well recognized even at the time of the regulations.[271]

Just as the 1996 check-the-box regulations raised the question of whether Treasury could effectively overrule *Morrissey*, the 2004 regulations raised the question of whether Treasury could effectively overrule *INDOPCO*.[272] Since the regulations are generally taxpayer-friendly, few potential litigants would have standing to challenge the validity of the 2004 rules.[273] The point here, though, is not to question the validity of the *INDOPCO* regulations; it is to note the asymmetry with respect to revenue-raising and revenue-reducing regulations. Over the course of several administrations, the President and his Treasury Department have sought congressional support for revenue-raising measures while adopting taxpayer-friendly regulations on their own (even when those taxpayer-friendly regulations require relatively bold assertions of executive power).

3. The Obama Administration's General Motors Decision

As a general rule, a company that incurs a net operating loss (NOL) in one year can claim that loss as a deduction from taxable income in a future year. Section 172 of the Code allows for NOL carryforwards over 20 years and NOL carrybacks over two years: that is, a taxpayer with a net operating loss in 2016 can use that loss to reduce its tax for 2014 or 2015 or for any year through 2036.[274] Section 382, however, limits the ability of a corporation to use NOLs following an ownership change. Most relevantly for present purposes, section 382(l)(5) applies when a corporation with NOLs goes through bankruptcy and the shareholders and creditors of the old corporation own at least 50% of the stock of the reorganized corporation.[270a] Under those circumstances, the new corporation *can* use the old corporation's NOLs, provided that the new corporation does not undergo another

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[266] *Id.* at 89.
[267] *Id.* at 90.
[268] Treas. Dec. 9107, 69 Fed. Reg. 436 (Jan. 5, 2004).
[269] Ethan Yale, *The Final* INDOPCO *Regulations*, TAX ANALYSTS, Oct. 25, 2004, at 435–36.
[270] *See* 69 Fed. Reg. at 440.
[271] *See generally* Calvin H. Johnson, *Destroying Tax Base: The Proposed* INDOPCO *Capitalization Regulations*, TAX NOTES, June 2, 2003, at 1381.
[272] *See* Polsky, *supra* note 259, at 243–44.
[273] *See id.* at 244 n. 347, 245.
[274] 26 U.S.C. § 172(a), (b)(1)(A).
[270a] *See id.* at § 382(1)(5)(A).

"ownership change" in the next two years. If, however, the new corporation undergoes an ownership change in the two years following the bankruptcy reorganization, it loses all of its NOLs.[275] The definition of "ownership change" is somewhat complicated, but such a change will occur if one or more large shareholders (i.e., shareholders with more than 5% of the corporation's stock) sell more than 50% of the corporation's stock over the next two years.[276]

In October 2008, Congress passed and President Bush signed the Emergency Economic Stabilization Act, which provided Treasury with authority to carry out the Troubled Assets Relief Program (TARP).[277] In June of the following year, General Motors filed for bankruptcy protection in federal court. By that point, the U.S. Treasury was GM's primary creditor, having acquired nearly $50 billion in GM senior debt through TARP. The bankruptcy court quickly approved a sale of GM's assets to a new corporation in which the U.S. Treasury would hold a 61% stake. The Canadian government would hold a 12% stake in the new corporation; the United Auto Workers would, through a trust, hold a 17.5% stake; and other unsecured creditors would hold the remaining stock in the new corporation. Because creditors of the old GM held at least half (indeed, all) of the stock in the new GM, section 382(l)(5) allowed the new GM to use the old GM's $45 billion in NOLs.[278]

There was, however, one potential wrench in the plan: if Treasury sold its stock in GM in the next two years—or if Treasury sold some of its stock and other owners of the new GM sold their stock such that an "ownership change" occurred—the new GM would lose all of its NOLs. And, indeed, Treasury had every intention to sell its stake expeditiously.[279] Treasury addressed this potential problem in January 2010 by issuing Notice 2010-2, which said that for stock and other financial instruments acquired by Treasury through TARP, any subsequent sale by Treasury would not trigger an "ownership change" under section 382.[280] With the swoop of a pen, GM's section 382 problem went away.

Notice 2010-2 cited three sources of statutory authority. First, section 382(m) authorizes the Treasury Secretary to "prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section."[281] Second, section 7805(a) authorizes the Treasury Secretary to "prescribe all needful rules and regulations for the enforcement" of the Internal Revenue Code.[282] Third, section 101(c)(5) of the Emergency Economic Stabilization Act gives the Treasury Secretary the power to "issu[e] such regulations and other guidance as may be necessary or

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[275] *See id.* at § 382(l)(5)(D).
[276] *See id.* at § 382(g).
[277] Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat. 3765.
[278] Mark Ramseyer & Eric B. Rasmusen, *Can the Treasury Exempt Its Own Companies from Tax? The $45 Billion GM NOL Carryforward,* 1 CATO PAPERS ON PUB. POL'Y 1, 7–9 (2011).
[279] *See* Zachary A. Goldfarb, *U.S. To Sell Off Its Remaining GM Shares*, WASH. POST, Dec. 19, 2012, https://www.washingtonpost.com/business/economy/us-to-sell-off-500-million-remaining-gm-shares/2012/12/19/6dfc345e-49fd-11e2-b6f0-e851e741d196_story.html [https://perma.cc/H8K5-XQK3] (quoting Assistant Secretary of Treasury for Financial Stability Timothy Massad as saying that "[t]he government should not be in the business of owning stakes in private companies for an indefinite period of time").
[280] Notice 2010-2, 2010-2 I.R.B. 251.
[281] 26 U.S.C. § 382(m).
[282] *See id.* at § 7805(a).

appropriate to define terms or carry out the authorities or purposes of this Act."[283] One can question whether these general grants of regulatory authority are sufficient to justify Notice 2010-2, though I will leave that debate to others.[284] What seems clear is that the statutory delegations cited by Treasury in Notice 2010-2 are no more specific (and indeed, much less so) than the provisions that Treasury might cite as authority for regulations addressing carried interest,[285] lower-of-cost-or-market accounting,[286] and grantor-retained annuity trusts[287]—all of which are cases in which the statutory grant of authority is quite explicit. Put differently, one might argue that Treasury lacked the statutory authority to promulgate Notice 2010-2, but if one thinks that Treasury *did* have the statutory authority to promulgate Notice 2010-2 (as the Obama administration claims it did), then Treasury most certainly has the authority to implement the revenue-raising measures listed in Section I.E through executive action.[288]

What is especially remarkable about Notice 2010-2 is how clearly it contravened the expressed wishes of members of the then-current Congress. In the midst of the fall 2008 financial crisis, the Bush Treasury Department issued a similar notice—Notice 2008-83—that effectively exempted the banking industry from the section 382 limitations.[289] Notice 2008-83, unlike the Obama administration's subsequent action addressing GM, asserted absolutely no statutory authority for such an exemption. The *Washington Post* quoted former Joint Committee on Taxation chief of staff George Yin as saying: "Did the Treasury Department have the authority to do this? I think almost every tax expert would agree that the answer is no."[290] But while the legal basis for Notice 2008-83 was dubious, the intention behind Notice 2008-83 was unambiguous: Treasury wanted to attract a buyer for Wachovia, then the fourth-largest bank holding company in the country, which was on the brink of collapse.[286a] And it worked: three days after the notice, Wells Fargo stepped in to buy Wachovia and its built-in NOLs.[291]

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[283] Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, § 101(c)(5), 122 Stat. 3765 (2008).

[284] *See* Ramseyer & Rasmusen, *supra* note 278 at 7–9; Lawrence Zelenak, *Custom and the Rule of Law in the Administration of the Income Tax*, 62 DUKE L.J. 829, 846–47 (2012).

[285] *See supra* text accompanying notes 106–107.

[286] *See supra* text accompanying note 145.

[287] *See supra* text accompanying note __.

[288] Treasury separately took actions ensuring that Fannie Mae, Freddie Mac, Wells Fargo, Citigroup, and AIG would not lose NOLs as a result of financial crisis bailouts. *See* RAMSEYER & RASMUSEN, *supra* note 278, at 20–21.

[289] *See* Notice 2008-83, I.R.B. 2008-42 (Oct. 20, 2008).

[290] Amit R. Paley, *A Quiet Windfall for U.S. Banks*, WASH. POST, Nov. 10, 2008, http://www.washingtonpost.com/wp-dyn/content/article/2008/11/09/AR2008110902155_pf.html [https://perma.cc/MK3H-G5BJ].

[286a] *See* Memorandum from Richard Delmar, Counsel to the Inspector General on Inquiry Regarding IRS Notice 2008-83 to Eric M. Thorson, Inspector General (Sept. 3, 2009) https://www.treasury.gov/about/organizational-structure/ig/Documents/Inquiry%20Regarding%20IRS%20Notice%202008-83.pdf [https://perma.cc/Q2CL-43A4] (positing that tax rules should not be obstacles to financial transactions and acquisitions that were otherwise good for the economy.").

[291] *See* Binyamin Applebaum, *After Change in Tax Law, Wells Fargo Swoops In*, WASH. POST, Oct. 4, 2008, http://www.washingtonpost.com/wp-dyn/content/article/2008/10/03/AR2008100301042.html [https://perma.cc/XZ9U-GENZ].

The reaction from Congress was almost as rapid. Republican Senator Charles Grassley of Iowa called for the Treasury Inspector General to investigate the "facts and circumstances surrounding the issuance of the Notice."[292] Democratic Senator Charles Schumer of New York also wrote to Treasury officials expressing concerns about the action.[293] Then in February of the following year, Congress passed the American Recovery and Reinvestment Act of 2009, which included a provision stating:

> Congress finds as follows:
>
> (1) The delegation of authority to the Secretary of the Treasury under section 382(m) of the Internal Revenue Code of 1986 does not authorize the Secretary to provide exemptions or special rules that are restricted to particular industries or classes of taxpayers.
>
> (2) Internal Revenue Service Notice 2008-83 is inconsistent with the congressional intent in enacting such section 382(m).
>
> (3) The legal authority to prescribe Internal Revenue Service Notice 2008-83 is doubtful.[294]

Acknowledging that "taxpayers should generally be able to rely on guidance issued by the Secretary of the Treasury," Congress declared that Notice 2008-83 would "have the force and effect of law with respect to any ownership change . . . occurring on or before January 16, 2009, and . . . shall have no force or effect with respect to any ownership change after such date."[295] Nonetheless, Notice 2010-2 extended the exemption from the section 382 limits to the GM transaction occurring four months *after* the American Recovery and Reinvestment Act became law. Whether or not Notice 2012-2 technically runs afoul of the American Recovery and Reinvestment Act, the contrast with revenue-raising regulations could not be more stark. Consider the example of Notice 98-11 above (the Clinton administration proposal to walk back check-the-box with respect to hybrid branches).[296] In the Notice 98-11 case, Treasury withdrew a proposed revenue-raising regulation for which it had virtually uncontested statutory authority based on murmurs of congressional disapproval.[292a] In the Notice 2010-2 case, Treasury went forward with a taxpayer-friendly regulatory action for which it had questionable authority notwithstanding shouts from Capitol Hill. To be sure, the financial crisis catalyzed (and perhaps justified) extraordinary measures. But the fact remains that Treasury has been willing to test the outer limits of its authority in one direction and not the other.

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[292] Michael Scherer, *The Silent Change to Section 382*, TIME, Nov. 15, 2008, http://swampland.time.com/2008/11/15/the-silent-change-to-section-382 [https://perma.cc/6UZU-XP9M].

[293] Letter from Senator Charles E. Schumer to Secretary Henry Paulson, Department of the Treasury and Doug Shulman, IRS Commissioner (Oct. 30, 2008), available at http://bit.ly/1O2U4gm [https://perma.cc/U5JL-56XS].

[294] American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, § 1261(a), 123 Stat. 115, 342–43 (2009).

[295] *Id*. § 1261(a)(4)–(b)(1), 123 Stat. at 342–43.

[296] *See supra* text accompanying notes 126–131.

[292a] *Id*.

II. Game Theory, Deficit Hawks, and Resource Constraints

Part I set forth the puzzle: Why does the President repeatedly ask Congress to enact revenue-raising measures that the Executive Branch already has the power to implement on its own—especially when it is clear that Congress will rebuff the President's request? One potential answer is that statutes are more durable than regulations: regulations are easily reversible by the next administration (especially after the *Brand X* decision[297]) while the process of repealing a statute is considerably more cumbersome. So too, statutes are less likely to be overturned on judicial review than regulations: a regulation, after all, can be set aside if it is inconsistent with the authorizing statute, whereas a statute need only satisfy the requirements of the Constitution. Also, a President who acts unilaterally may face charges of presidential imperialism from the press and other thought leaders.[298] While this last constraint has not prevented Presidents in recent years from engaging in robust exercises of executive authority, it may make legislation a first-best option and unilateralism a second-best response to legislative gridlock.

The puzzle, then, is not why the President *initially* asks Congress to enact revenue-raising measures via legislation: in light of the considerations listed in the previous paragraph, the President's preference for legislation over executive action might seem overdetermined. Rather, the puzzle is why the President fails to act *after* Congress already has rebuffed his requests. I do not claim to have found a single answer to the puzzle, and I doubt that a single answer exists. Instead, this part proposes three explanations and explores the implications of each. The three explanations, I argue, bring us closer to understanding patterns of presidential action and inaction in tax law. They do not, however, constitute a complete answer.

Before proceeding further, a caveat is in order: the analysis below generally treats the President, Treasury, and the IRS as an undifferentiated whole. Of course, the Executive Branch—like Congress—is a they, not an it.[299] IRS officials may have preferences that diverge from those of their counterparts at the Treasury Office of Tax Policy, and the top tax officials at Treasury may, in turn, have preferences that diverge from the President's. Why, then, treat the Executive Branch as the functional unit of analysis? First, the organizational structure of the Treasury Department (including the IRS, a bureau within Treasury) is both an independent and dependent variable. The regulation drafting process within Treasury may generate frictions that make it more difficult for the Executive Branch to take on a robust revenue-raising role, but at the same time, if the President had a strong interest in Treasury taking on a robust revenue-raising role, the regulation drafting process within Treasury might be much more streamlined. Analyzing the incentives of the President is a first step toward understanding why Treasury and the IRS are structured as they are. Second, and as noted above, simplification can allow us to

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297 *See supra* note 67.

298 *See, e.g.*, Ross Douthat, Opinion, *The Making of an Imperial President*, N.Y. TIMES, Nov. 22, 2014, http://www.nytimes.com/2014/11/23/opinion/sunday/ross-douthat-the-making-of-an-imperial-president.html [https://perma.cc/G7GP-9CRM] (characterizing President Obama's tenure as an "imperial presidency").

299 *See* Kenneth A. Shepsle, *Congress Is a "They," Not an "It": Legislative Intent as Oxymoron*, 12 INT'L REV. L. & ECON. 239, 240–42 (1992).

see potential relationships upon multiple variables in a complex environment.[300] Whether it does so here is a judgment I leave to the reader.

A. Taxation Across Two Branches: A Game-Theoretic Approach

This section uses public choice and game theory to generate a possible explanation to the puzzle presented in Part I. Subsection II.A.1 presents a simple model of presidential behavior. Subsection II.A.2 develops a game-theoretic framework for analyzing interactions between the President and Congress. Subsection II.A.3 incorporates ideological and doctrinal factors into the game-theoretic framework.

1. A Simple Model of Presidential Behavior

No single formula can capture all of the reasons why Presidents and members of Congress do what they do. But a serviceable first approximation is that politicians take actions for which the expected political benefits (B) exceed the expected political costs (C). The beneficiaries of regulation can reward a politician through votes, campaign contributions, political favors, and employment opportunities after the politician leaves office. The interests harmed by regulation channel votes, contributions, and favors to the politician's opponent. To be sure, this first approximation is just that—an approximation: politicians also act for reasons unrelated to a political cost-benefit calculus.[301] Yet even though not everyone in a position of power acts like Frank Underwood,[302] the basic model provides a useful set of analytical building blocks even if it does not describe every element of reality.

As noted above, in many circumstances Presidents have a choice between acting on their own and proposing legislation to Congress. When the President and Congress act jointly, voters may apportion credit and blame between the two branches. Let p represent the portion of credit (blame) for legislation that voters assign to the President, with $1-p$ representing the portion of credit (blame) for legislation that voters assign to Congress. Assume, for the sake of simplicity, that there are no veto overrides: any legislation passed by Congress must be signed by the President in order to become law.[303]

The introduction of a second branch does not (yet) alter the analysis significantly. If the President were the sole political actor, he would adopt regulations for which $B > C$. If he has to share credit and blame with Congress, he will support measures for which $pB > pC$. The set of regulations for which $B > C$ is identical to the set of measures for which $pB > pC$. So long as the President's proportion of credit is the same as his proportion of blame, then every regulation that he would support in the one-branch scenario is also a measure he will support in a two-branch world.

[300] *See supra* note 43,

[301] *See generally* JOHN F. KENNEDY, PROFILES IN COURAGE 1–21 (Harper Perennial Modern Classics, 1st ed., 2006) (1956).

[302] *See* HOUSE OF CARDS (Netflix 2013-2016).

[303] As previously noted, veto overrides with respect to tax legislation are exceedingly rare. *See supra* note 247 and accompanying text.

What about revenue-raising measures? I will assume for now that the only political benefit of raising revenue is the benefit that comes from spending that revenue. There may be cases in which voters affirmatively want other taxpayers to pay more;[304] for now, my focus will be on the majority of cases where revenue-raising measures yield only political costs and expenditures yield only political benefits. I will also assume that voters assign blame for revenue-raising measures to the political actors who enacted those measures, and will assign credit for expenditures to the political actors who approved the spending. So when the President takes executive action that results in more revenue being raised, he bears all the political costs himself. However, he cannot spend the funds himself; spending measures must go through Congress. Thus, the President internalizes all the political costs, C, but only a portion of the political benefits, pB.

The model so far has incorporated assumptions that are concededly contestable. First, it assumes that voters and/or interest groups are sufficiently well informed that they know whether it was the President and Congress who raised their taxes or the President who did so on his own. This assumption may appear implausible as applied to the general mass of voters, who may have difficulty determining whether the President or Congress is responsible for a particular policy change.[305] But the assumption is more viable with respect to some of the interest groups that benefit from specific features of the tax laws. For example, private equity managers who benefit from the taxation of carried interest profits at preferential rates have spent millions of dollars on sophisticated lobbying efforts and campaign contributions targeted at specific members of Congress and presidential candidates.[306] The same is true for the multinational firms that benefit from check-

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[304] One might think that earnings stripping—*see infra* Section I.E.2—would be one such case: Democrats and Republicans alike have criticized U.S. corporations that merge with foreign counterparts in an attempt to escape out from under the U.S. tax system. *See, e.g.*, Kevin Drawbaugh & Emily Stephenson, *Politicians Slam Tax-Avoiding Pfizer-Allergan Deal*, REUTERS, Nov. 24, 2015, http://www.reuters.com/article/us-allergan-m-a-pfizer-whitehouse-idUSKBN0TC24820151124 [https://perma.cc/X2L3-DQUG] (reporting statements by presidential candidates criticizing Pfizer's planner merger with Allergan); Carolyn Y. Johnson & Renae Merle, *Pfizer's Tax-Avoiding Megamerger with Allergan Sparks Outcry*, WASH. POST, Nov. 23, 2015, https://www.washingtonpost.com/business/economy/pfizers-tax-avoiding-megamerger-with-allergan-sparks-outcry/2015/11/23/cced417c-9218-11e5-b5e4-279b4501e8a6_story.html [https://perma.cc/S5DZ-PAWN] (quoting Senate Minority Leader Harry M. Reid's complaint that "[b]y nominally moving overseas while continuing to take all the benefits of a U.S. company, Pfizer is gaming the system and will avoid paying its fair share of U.S. tax dollars"). Note, though, that the Obama administration has *not* used the full measure of its executive power to crack down on earnings stripping by inverted firms. Perhaps this suggests that the earnings stripping case is not as exceptional as it initially appears.

[305] On political ignorance, *see generally* MICHAEL X. DELLI CARPINI & SCOTT KEETER, WHAT AMERICANS KNOW ABOUT POLITICS AND WHY IT MATTERS 62–105 (1996) (exploring "what Americans know—and don't know—about politics"); Ilya Somin, *Political Ignorance and the Countermajoritarian Difficulty: A New Perspective on the Central Obsession of Constitutional Theory*, 89 IOWA L. REV. 1287, 1308 tbl. 1 (2004) (assessing political ignorance of Americans through survey evidence). For example, only 55% of U.S. adults (though perhaps a higher percentage of *voters*) knew that Republicans had a majority in the House of Representatives before the 2000 election. *See id.*

[306] *See, e.g.*, Alec MacGillis, *The Billionaire's Loophole*, NEW YORKER, Mar. 14, 2016, http://www.newyorker.com/magazine/2016/03/14/david-rubenstein-and-the-carried-interest-dilemma [https://perma.cc/7JP4-2SVB] dilemma ("[T]he so-called carried interest tax loophole .

the-box treatment of single-member foreign-incorporated entities.[307] If the Obama administration took executive action to eliminate these features of the tax code, it is difficult to imagine that private equity managers and Fortune 500 CEOs would be confused as to whether the President or Congress was to blame.

At the same time, the model assumes that voters and/or interest groups are not *so* sophisticated that they can attribute the credit for expenditures to the actor who facilitated those expenditures through revenue-raising measures. This assumption strikes me as quite plausible even as applied to the most sophisticated interest groups. It is virtually impossible to know where the marginal dollar in the federal budget goes. (What would Congress cut if it had $1 less—or even $10 billion less?) It is doubtful that members of the House and Senate Appropriations Committees can answer that question—much less that anyone outside the Capitol office buildings can. For that reason, it seems unlikely that the beneficiary of a particular spending program will recognize that the money for that program came from a specific revenue-raising executive action. More plausibly, the beneficiary of the spending program will assign credit to the lawmakers who passed—and the President who signed—the spending measure.

Subject to these assumptions, the model generates a first-cut solution to the puzzle in Part I. The President will include a proposal in the Greenbook if $pB > pC$, which is to say, when $B > C$. In other words, the President will include a revenue-raising proposal in the Greenbook if the political benefits from additional spending (benefits he shares with Congress) offset the political costs from additional taxation (costs he also shares with Congress). By contrast, the President will act unilaterally to raise revenue only if $pB > C$—only if the shared political benefits from additional spending offset the political costs from additional taxation that the President must bear on his own. This suggests that there exists a set of revenue-raising proposals that the President is willing to include in the Greenbook but unwilling to pursue on his own: those for which $pC < pB < C$.

With respect to revenue-reducing measures, the model generates an opposite result. Assume that voters appreciate actions that reduce their own tax burden; the only political cost of such measures is that they leave less revenue to be spent. If the President acts unilaterally to reduce revenue, the political benefits, B, are all his, and the political costs of corresponding spending cuts are shared with Congress. This suggests that there exists a set of revenue-reducing measures that the President would be willing to enact on his own but not if he has to share the credit with Congress: those for which $pB < pC < B$.

One might think that the dynamics of tax lawmaking would change as a President approaches the end of his second term in office. And indeed, the Treasury

. . [a] tax break [that] has helped private equity become on of the most lucrative sectors of the financial industry"); Ctr. for Responsive Politics, Private Equity & Investment Firms, OpenSecrets.org, https://www.opensecrets.org/industries/indus.php?ind=F2600 [https://perma.cc/9JXL-7AWU] (last visited Mar. 11, 2016).

[307] *See, e.g.*, Kevin Drawbaugh & Andy Sullivan, *Insight: How Treasury's Tax Loophole Mistake Saves Companies Billions Each Year*, REUTERS, May 20, 2013, http://www.reuters.com/article/us-usa-tax-checkthebox-insight-idUSBRE94T17K20130531 [https://perma.cc/3MKH-UTS6] ("The 'check the box' loophole – which costs the United States about $10 billion per year, according to the White House – also has been a reflection of Washington's 'revolving door' culture of policy-making and lobbying.").

Department issued a series of revenue-raising "midnight regulations" in the last days before President Clinton left the White House. These midnight regulations included: regulations placing limits on the availability of the research and experimentation tax credit[308] (which were then suspended by the administration of George W. Bush after it took office[309]); regulations designed to prevent avoidance of rules regarding long-term contracts;[310] regulations aimed at stopping "abusive transactions" involving charitable remainder trusts;[311] regulations extending an anti-abuse rule to rental agreements involving payments of $2 million or less;[312] and regulations restricting the permissible terms for lifetime charitable lead trusts.[313] Even so, there are reasons why a President might be reluctant to act in his waning days in office. For one, an outgoing President will not be around to share in the political benefits from additional spending; thus, both terms in the President's cost-benefit calculus are reduced in the administration's last days. And perhaps more significantly, a President who is being followed by a member of the opposite party may worry that midnight revenue-raising regulations will allow his successor to score easy political points: the successor can rescind or suspend the midnight regulation (as President Bush did with respect to Clinton's R&E rule) and reap all the political benefits that follow.

As of this writing, voters had yet to go to the polls for the 2016 general election, and the results of the presidential race were still unknown (though they will be known by the time the article appears in print). Yet as noted above, the smart money was on the President's party retaining the White House,[314] rendering the latter concern somewhat less salient. Perhaps the Obama administration's more robust exercise of executive authority in a revenue-raising direction in mid-2016 can be attributed to this political reality: the administration might have been clearing the regulatory brush so that the next Democratic President could avoid the political costs of doing so. It should be emphasized, however, that at no prior point in the modern era has a President who generally supported higher taxes handed off power to a successor of the same political party.[315] Drawing any inferences about such a handover from President Obama's last year in office raises the risk of overextrapolating based on an *n* of 1.[316]

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[308] 66 Fed. Reg. 280 (Jan. 3, 2001).
[309] *See, e.g.*, Robert McIntyre, *The Taxonomist*, AM. PROSPECT, Jan. 3, 2002, http://prospect.org/article/taxonomist-36 [https://perma.cc/LGQ3-FNDZ].
[310] 66 Fed. Reg. 2219 (Jan. 11, 2001).
[311] 66 Fed. Reg. 1034 (Jan. 5, 2001).
[312] 66 Fed. Reg. 1038 (Jan. 5, 2001).
[313] 66 Fed. Reg. 1040 (Jan. 5, 2001).
[314] See supra note 237.
[315] The last time a living Democratic President handed off power to a Democratic successor was in 1857, before there was a federal income tax. Republican President William Howard Taft supported the ratification of the Sixteenth Amendment and Republican President Dwight D. Eisenhower held views about taxation that would be anathema to Republicans today, but both were succeeded by Presidents of the rival party.
[316] On midnight rulemaking generally, *see* Anne Joseph O'Connell, *Political Cycles of Rulemaking: An Empirical Portrait of the Modern Administrative State*, 94 VA. L. REV. 889, 956–58 (2008). O'Connell finds a significant uptick in rulemaking activity in a President's final year in office, *see id.* at 956 tbl.4, although it is difficult to know whether this is because the incentives of regulators shift in the final year, or because outgoing administration officials are racing to complete multiyear projects before they leave office.

Even though the model above is only rudimentary, it already sheds some light on the puzzle in Part I. On the one hand, the President may be willing to include revenue-raising proposals in the Greenbook but not to implement those proposals unilaterally because the political costs are too steep if he must bear those costs all on his own. On the other hand, the President may be quite willing to pursue revenue-reducing measures on his own: indeed, in some circumstances he may be willing to implement revenue-reducing measures via executive action even though he would not want the measure included in the Greenbook. Notably, the simple model does not suggest that the set of revenue-raising executive actions will be null: the President still may be willing to act on his own when $pB > C$. But while the basic model sheds light on the President's incentives, it fails to capture the strategic interactions between the President and Congress. The next subsection takes up that task.

2. The Strategic Model

With respect to revenue-raising measures, the model has identified a set of proposals that the President will choose to include in the Greenbook but is not willing to implement on his own. Yet the President's decision to include a proposal in the Greenbook is not the end of the story; it is his opening bid in bargaining with Congress. According to the model, the President will include a proposal in the Greenbook if $pC < pB < C$, and will not include a proposal in the Greenbook if $B < C$. When $pB > C$, though, the analysis is more complicated.

The complication arises from the fact that even if $pB > C$, it is still the case that $C > pC$. In other words, even if the shared political benefits of additional spending are high enough that the President would be willing to bear the political costs of raising revenue on his own, he would still prefer to share those costs with Congress. As a result, the President may include proposals in the Greenbook even though—if the prospect of legislation were off the table—the President would be willing to implement the proposal via executive action.

After Congress receives the Greenbook, it decides whether to adopt the President's proposal. (Of course, just as the Executive Branch is not a unitary actor, Congress is not of one mind either; for now, imagine a unified congressional leadership calling the legislative shots, though this assumption will be relaxed later on.) One might think that if the leadership in Congress shares the President's preferences (or shares his estimate of political costs and benefits), then Congress would adopt every proposal in the Greenbook. The outcome might change, though, if the leaders of Congress have political fortunes separate from the President. This is because the congressional leadership knows that the President may include some proposals in the Greenbook for which $pB > C$. (With perfect information, the leaders of Congress will be able to identify the proposals that fall into this set.) While the President would prefer to share political costs with Congress, the leaders of Congress would prefer that the President bear those costs himself.

How might we imagine this interaction playing out? The payoffs to the President and Congress resemble the well-known "hawk-dove" game.[317] If the President does not regulate and Congress does not legislate, then the payoff is zero to both sides. If the President does not regulate and Congress *does* legislate (with the President signing the legislation into law), then the payoff to the President is $p(B - C)$ and the payoff to Congress is $(1 - p)(B - C)$. In other words, the President and Congress share both the benefits and the costs. And if the President regulates while Congress does not legislate, then the payoff to the President is $pB - C$ while the payoff to Congress is $(1 - p)B$. That is, the President and Congress share the benefits, but the President bears all the costs. Figure 1 summarizes the analysis thus far. Note that the model excludes the possibility of unilateral congressional action: my assumption is that the President will never veto a revenue-raising proposal that he already has included in his own Greenbook. (Indeed, there do not appear to be any historical examples of such a veto.)

Figure 1. Hawk-Dove Game With One Missing Box

	Don't Legislate	**Legislate**
Don't Regulate	0, 0	pB - pC, (1 - p)(B - C)
Regulate	pB - C, (1 - p)B	--

Three points about Figure 1 are worth noting. First, the upper left box (*don't regulate, don't legislate*) is the worst of all worlds for both players. The President would prefer to regulate than to end up in the upper left box, even though that means he would bear all the political costs of revenue raising himself. And Congress, for its part, would prefer to legislate than to end up in the upper left box, even though that would mean it shares a portion of the political costs. Second, the President would prefer to end up in the upper right box (*don't regulate*, *legislate*) rather than the lower left box (*regulate*, *don't legislate*). This should track our intuitions: the President wants to share the political costs of revenue raising with Congress if he can. Third, and reciprocally, Congress would prefer to end up in the lower left box (*regulate, don't legislate*) rather than the upper right box (*don't regulate*, *legislate*). Again, this should be intuitive: Congress would prefer for the President to bear all the political costs of revenue raising rather than having those costs shared across branches.

What goes in the fourth box? What would it mean for the President to regulate *and* Congress to legislate? In theory, Congress could ratify a Treasury regulation by incorporating the regulatory language into a statute. However, once the Treasury Department has already promulgated a revenue-raising regulation, what incentive would Congress have to incur the political costs that come with codification (given that Congress is already set to share the benefits from the revenue raised)?[318] A more plausible interpretation of the fourth box is as follows: When the President includes a proposal in the Greenbook, the President decides

[317] *See* DOUGLAS C. BAIRD, ROBERT H. GERTNER & RANDAL C. PICKER, GAME THEORY AND THE LAW 303–04 (1994); Richard H. McAdams, *Beyond the Prisoner's Dilemma: Coordination, Game Theory, and Law*, 82 S. CAL. L. REV. 209, 223–24 (2009).

[318] Perhaps Congress would codify the regulation in order to shield it from attack in court as *ultra vires*. For present purposes, however, I focus on cases in which the relevant regulatory action lies within the Executive Branch's authority.

whether he is willing to proceed unilaterally and Congress decides whether it is willing to proceed legislatively. If the President decides to regulate and Congress decides to legislate, then the outcome is a tossup as to who acts first. The simplest representation of the tossup is to say that half the time the President acts first and half the time Congress acts first. The payoffs in the lower right box, then, are the averages of the payoffs in the upper right and lower left boxes. Thus when the President decides to regulate and Congress decides to legislate, there is a 50% probability that the President will regulate first—in which case Congress won't legislate, the President's payoff will be $pB - C$, and Congress's payoff will be $(1 - p)B$. Likewise, there is a 50% probability that Congress will legislate first—in which case the President won't regulate, his payoff will be $p(B - C)$, and Congress's payoff will be $(1 - p)(B - C)$. The terms in the lower right box in Figure 2 represent the averages of these payoffs.

Figure 2. Hawk-Dove Game With All Four Boxes Filled In

	Don't Legislate	**Legislate**
Don't Regulate	0, 0	pB – pC, (1 – p)(B – C)
Regulate	pB – C, (1 – p)B	pB – 0.5C – 0.5pC, B – pB – 0.5C + 0.5pC

A game has a Nash equilibrium when there exists a set of strategies such that each player's strategy is an optimal response to the other player's strategy.[319] (The name honors John Forbes Nash, Jr., the mathematician and Nobel prize winner of *A Beautiful Mind* fame.[320]) Here, the lower left and upper right boxes both represent Nash equilibria. In the lower left box, Congress never legislates and the President always regulates. (More precisely, the President unilaterally implements revenue-raising measures allowable under existing statutes for which $pB > C$.) Conditional on Congress not legislating, the President has no incentive to change his strategy because his payoff from (*regulate, don't legislate*) is higher than his payoff from (*don't regulate, don't legislate*). And conditional on the President regulating, Congress has no incentive to change its strategy because its payoff is higher when it does not legislate than when it does. Likewise, in the upper right box, the President never regulates and Congress always legislates. Again, the President has no incentive to change his strategy as long as Congress sticks to legislating, and Congress has no incentive to change its strategy as long as the President does not regulate. Both of these equilibria are considered "pure strategy" equilibria because they involve each player playing the same strategy each time.[321]

We can imagine, then, a lower-left-box world in which Congress *never* adopts any revenue-raising measure for which $pB > C$, and the President *always* proceeds unilaterally. We can also imagine an upper-right-box world in which Congress *always* adopts such measures and the President *never* proceeds on his own. Note that in either case, the President never moves unilaterally to adopt a measure for which

[319] *See* DREW FUDENBERG & JEAN TIROLE, GAME THEORY 11 (1991).
[320] *See* SYLVIA NASAR, A BEAUTIFUL MIND (1998); A BEAUTIFUL MIND (Imagine Entertainment 2001).
[321] *See* BAIRD ET AL., *supra* note 317, at 313.

$pB < C$; if the shared benefits from additional spending are less than the costs of acting alone, the President will not act alone.

Even readers unfamiliar with game theory will likely have an intuition at this point that the two pure strategy Nash equilibria are not the only possible outcomes of the hawk-dove game: the players might mix up their moves from time to time. And indeed, game theory shows that the players can arrive at a mixed strategy equilibrium as well. The mixed strategy equilibrium arises when the President's combination of moves makes Congress indifferent between legislating and not legislating, and Congress's combination of moves makes the President indifferent between regulating and not regulating. Formally, let r represent the probability that the President will regulate and let λ (the Greek letter lambda) represent the probability that Congress will legislate; a mixed strategy equilibrium arises when[322]:

$$r = \frac{B - C}{B - 0.5C}$$

and

$$\lambda = \frac{pB - C}{pB - 0.5C - 0.5pC}$$

What does this mean practically? The answer depends critically on the values of the unknown variables. Say, for example, that $p = 0.5$, $B = 2.01$, and $C = 1$. That is, the President and Congress share the political benefits and costs of joint action evenly, and the political costs of raising revenue are slightly less than half the political benefits of the spending that it enables. We can imagine the President and Congress interacting repeatedly with respect to revenue-raising measures that the President would be willing to adopt if the prospect of legislative action were off the table and that Congress would be willing to enact if the prospect of executive action were foreclosed. Given the parameter values above, the mixed strategy Nash equilibrium looks like the following: in about 66% of cases, the President ends up

[322] The mixed strategy Nash equilibrium arises in the hawk-dove game where both players are indifferent between their two strategies. The condition for Congress to be indifferent between *don't legislate* and *legislate* is:

$$0(1 - r) + [(1 - p)B]r = [(1 - p)(B - C)](1 - r) + [B - pB - 0.5C + 0.5pC]r$$

This equation can be solved for r with the result that:

$$r = (B - C)/(B - 0.5C)$$

The condition for the President to be indifferent between *don't regulate* and *regulate* is:

$$0(1 - \lambda) + (pB - pC)\lambda = (pB - C)(1 - \lambda) + (pB - 0.5C - 0.5pC)\lambda$$

This equation can be solved for λ with the result that:

$$\lambda = (pB - C)/(pB - 0.5pC - 0.5C)$$

regulating on his own; in 1% of cases, Congress enacts the measure via legislation; and in the remaining cases (slightly less than one-third), *neither* side acts and the measure goes unimplemented.[323]

Given that the values of p, B, and C are all unknown, it would be a mistake to place too much emphasis on any particular percentage figure. The more important point is this: Two-sided inaction may result in the hawk-dove game even in equilibrium. Combining this insight with the results of the simple model at the beginning of the section, we now have two explanations for the puzzle presented in Part I. Even when the President already has authority under existing statutes to implement some of his Greenbook proposals via unilateral action, the President may fail to do so because:

- The President's share of the political benefits from the spending that the revenue raising will allow is greater than the political costs of revenue raising if those costs can be shared, but less than the political costs of revenue raising if he must bear all of those costs himself ($pC < pB < C$); or

- The President's share of the political benefits from the spending that revenue raising will allow is greater than the political costs of revenue raising even if he must bear all of those costs himself ($pB > C$), but two-sided inaction is sometimes the result of a mixed strategy Nash equilibrium solution to the game played by the President and Congress.[324]

3. *Further Implications of the Hawk-Dove Model*

So far the model has made no accommodation for ideology: it assumes that the President and Congress have the same ideal point with respect to legislation. The model also has not addressed the role of doctrine in constraining or enabling executive action. Incorporating ideology and doctrine into the model yields additional insights into the dynamics of tax lawmaking.

a. *The Role of Ideology*

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[323] When $p = 0.5$, $B = 2.01$, and $C = 1$, then $r = 0.669$ (66.9%) and $\lambda = 0.020$ (2.0%). Thus, in 32.44% of cases the outcome is (*don't regulate*, *don't legislate*); in 0.66% of cases the outcome is (*don't regulate*, *legislate*); in 65.56% of cases the outcome is (*regulate, don't legislate*), and in 1.34% of cases the outcome is (*regulate*, *legislate*). When the President decides to regulate and Congress decides to legislate, it is a tossup a to who acts first: half of the 1.34% of cases end up as cases of unilateral executive action, and half of the 1.34% of cases end up with legislation.

[324] We can derive additional insights through comparative statics. Note that the (*don't regulate*, *don't legislate*) outcome arises with probability $(1-r)(1-\lambda)$. Substituting the values for r and λ derived above, we arrive at:

$$\frac{0.25C^2\,(1-p)}{pB^2 - 0.5BC - pBC + 0.25C^2 + 0.25pC^2}$$

As long as $pB > C$, the probability of a (*don't regulate*, *don't legislate*) result decreases over B, increases over C, and decreases over p. In other words, the probability of a (*don't regulate*, *don't legislate*) result is highest when the political costs of raising revenue are high relative to the political benefits and the President captures a relatively small share of the benefits.

What if the President and Congress assign different values to B and C? Such a scenario is likely in an era of divided government if one party's political base has a stronger taste for spending (or distaste for taxation) than the other's.

Begin with the case in which the President assigns a lower value to B (or a higher value to C) than Congress does. This means that for some set of potential proposals, $B > C$ from Congress's perspective but $B < C$ from the President's point of view. In other words, Congress would pass a revenue-raising measure but the President would not include it in the Greenbook or sign it into law. Revenue-raising measures of this sort will not be implemented.

At the same time, the difference between the President's and Congress's cost-benefit assessments also reduces the frequency with which $pB > C$. There are fewer revenue-raising proposals that the President would be willing to implement on his own. This narrows the range over which interactions between the President and Congress resemble the hawk-dove game. Knowing that the tax-averse President is unlikely to act on his own, Congress is more likely to adopt a strategy of legislation.

This analysis suggests that tax aversion on the part of the President or his political base has an ambiguous effect on the probability that revenue-raising legislation will be enacted. On the one hand, the President's tax aversion makes him less likely to include revenue-raising measures in his Greenbook (or to sign such measures into law). On the other hand, Congress—knowing that the President is tax-averse—is less likely to believe that he would be willing to implement revenue-raising measures on his own. In sum, the President's tax aversion reduces the number of revenue-raising proposals that the President will include in the Greenbook but increases the probability that Congress will enact any given revenue-raising measure that the President does include in the Greenbook.

The reverse scenario is potentially more interesting, as it more closely describes the present state of affairs in Washington. In this scenario, for a wide range of revenue-raising measures, $B > C$ from the President's perspective but $B < C$ from Congress's vantage point. This scenario would come about if, say, the political costs of revenue-raising measures are very high for the congressional leadership because of a strong anti-tax faction within the majority party. Congressional tax aversion will, unsurprisingly, make it less likely that any revenue-raising legislation will be passed. Yet that fact may make the President more likely to act unilaterally when $pB > C$. Recall that in the hawk-dove game, the President had an incentive to seek congressional support even for proposals that he would be willing to implement on his own absent the possibility of legislation. In effect, congressional tax aversion removes the possibility of legislation.

A perhaps-ironic implication of this analysis is that the rise of the anti-tax Tea Party in recent years may actually lead to more revenue being raised. This is because a President who knows that he cannot get any revenue-raising measure through Congress will implement such measures on his own whenever $pB > C$. The Tea Party, in other words, allows the President and Congress to avoid the uncooperative result (*don't regulate*, *don't legislate*) in the hawk-dove game.

b. The Role of Doctrine

The analysis above assumed that the President has the legal option of implementing revenue-raising measures via executive action. The availability of this option, however, depends on the deference regime. The option may be off the table under a less deferential regime (e.g., *National Muffler*) but available under a more deferential regime (*Chevron*).[318a]

One might initially expect that the shift to a more deferential regime would generally have positive revenue effects. This might be so if taxpayer-friendly regulations are likely to go unchallenged while taxpayer-unfriendly regulations are likely to be litigated. In the latter set of cases (the only cases that will make it to court in substantial numbers), more deference means it is more likely that the IRS will prevail. Yet the analysis changes when one considers the dynamic effects of deference regimes on the shape of tax law. Recall the observation in section II.B that when $pB > C$, an uncooperative outcome (*don't regulate, don't legislate*) is possible unless the President can credibly commit not to regulate or Congress can credibly commit not to legislate. A zero-deference regime would effectively eliminate the President's regulatory option, increasing the probability that Congress would act.

None of this is to say that a less deferential regime always results in more revenue. The static and dynamic effects of deference cut in different directions: deference makes it more likely that any particular Treasury regulation will pass judicial muster but less likely that Congress will act to raise revenues. What we can say is that the Supreme Court's shift from *National Muffler* to *Chevron* will not necessarily have a positive effect on revenue, because freedom of action for the Executive Branch may lead to inaction by Congress.

B. The Role of Deficit Hawks

So far the model has assumed an equality of revenues and expenditures: the possibility of deficit spending has not yet entered the picture. Incorporating the possibility of deficit spending generates additional insights—one of which might strike some readers as quite counterintuitive.

One way to conceptualize deficit spending is to think of it as just another form of taxation. Deficits impose a cost on future taxpayers, at least some of whom are also current voters (i.e., the relatively young).[325] Deficits are also sometimes said to impose a cost on savers through inflation, though there are strong theoretical reasons to doubt this claim[326] and little empirical evidence to support it.[327] Lawmakers and Presidents who support deficit-financed projects capture political

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[318a] *Compare National Muffler Dealers Assn., Inc. v. United States*, 440 U.S. 472 (1978) (articulating a multi-factor test that the courts must use to determine the validity of an IRS regulation) *with Chevron U.S.A. v. Natural Res. Def. Council*, 467 U.S. 837, 866 (1983) (holding that the courts must defer to the administrative agencies' reasonable interpretations of statutes).

[325] *See* David Romer, *What Are the Costs of Excessive Deficits?*, 3 NBER MACROECONOMICS ANN. 63, 108 (1988).

[326] *See, e.g.*, Robert J. Barro, *The Ricardian Approach to Budget Deficits*, 3 J. ECON. PERSPECTIVES 37, 49–50 (1989) (noting that the results of empirical studies about the effects of deficits on saving are "all over the map" because both deficits and saving have strong cyclical elements).

[327] *See, e.g.*, Marco Bassetto & R. Andrew Butters, *What Is the Relationship Between Large Deficits and Inflation in Industrialized Countries?*, FED. RESERVE BANK OF CHI. ECON. PERSPECTIVES—3RD QUARTER 83, 86–89 (2010) (discussing empirical data on the relationship between deficits and inflation).

benefits on the spending side but bear political costs from voters and interest groups adversely affected by deficits.

What happens if "deficit hawks" constitute a well-organized interest group?[328] (I do not intend the term "deficit hawk" to be pejorative in any sense—politicians seem to embrace the label readily.[329]) One possibility is that a President can implement a revenue-raising measure via regulation and advertise the fact that the measure will lower the deficit: presumably deficit hawks will give all the political credit for the deficit reduction to the President. On the other hand, a President may be reluctant to take this approach because it will also serve to underscore his responsibility for the measure in the minds of adversely affected taxpayers. Perhaps unsurprisingly, I have found no example of a President implementing a revenue-raising reform via regulation and then publicizing it as a deficit-reduction measure.

The existence of deficit hawks may affect the dynamics of tax lawmaking through another channel. In 1990, Congress adopted the so-called "PAYGO" rule requiring that any spending that increases the deficit must be offset by measures that raise revenue or reduce other spending by at least the same amount.[330] The PAYGO law lapsed from 2002 until 2010, and while a version of PAYGO was reenacted in 2010, the new law applies only to tax cuts and entitlement spending (not to the "discretionary" items—such as defense, education, and transportation, economic development—that together make up 32% of the federal budget).[331] PAYGO is not a binding constraint: Congress can turn it off for any bill at any time (as it did for the December 2015 package of tax breaks that will add $622 billion to the national debt).[332] And yet bills that violate revenue neutrality tend to generate at least some political blowback—especially from fiscally conservative members of the Republican caucus.[333] So while the requirement of revenue neutrality exists

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[328] The scenario is not entirely hypothetical: Blackstone Group co-founder Peter Peterson has spent more than a half billion dollars over the last several years in an effort to draw political attention to debt/deficit concerns. *See* Alan Feuer, *Peter G. Peterson's Last Anti-Debt Crusade*, Apr. 8, 2011, http://www.nytimes.com/2011/04/10/nyregion/10peterson.html [https://perma.cc/972S-EC76].

[329] *See, e.g.*, Ron Klein, Opinion, *Fiscal Responsibility Begins in Washington*, SUN-SENTINEL (Ft. Lauderdale, Fla.), Feb. 25, 2010, http://articles.sun-sentinel.com/2010-02-25/news/fl-deficit-reduction-klein-forum-20100225_1_fiscal-responsibility-deficit-budget [https://perma.cc/95XZ-JJ4J] (then-sitting Democratic congressman telling voters in his district that "[t]hose who know me know that I am a deficit hawk").

[330] *See* Elizabeth Garrett, *Harnessing Politics: The Dynamics of Offset Requirements in the Tax Legislative Process*, 65 U. CHI. L. REV. 501, 510 (1998).

[331] *See* Statutory Pay-As-You-Go Act of 2010, Pub. L. No. 111-139, 124 Stat. 8; Ctr. for Budget & Policy Priorities, Policy Basics: Introduction to the Federal Budget, http://www.cbpp.org/research/policy-basics-introduction-to-the-federal-budget-process [https://perma.cc/ZD68-8UMZ] (last updated Feb. 17, 2016).

[332] *See* Protecting Americans from Tax Hikes Act of 2015, Pub. L. No. 114-113, § 1001, 129 Stat. 3088, Division Q (Dec. 18, 2015); David M. Herszenhorn, *Under Wire, House Passes Big Package of Tax Cuts*, N.Y. TIMES, Dec. 17, 2015, http://www.nytimes.com/2015/12/18/us/politics/house-approves-huge-package-of-tax-breaks.html [https://perma.cc/F2L8-PULS]; Mark Bloomfield, *Tax Extenders on the Road to Tax Reform*, THE HILL, Dec. 21, 2015, http://thehill.com/blogs/pundits-blog/economy-budget/263889-tax-extenders-on-the-road-to-tax-reform [https://perma.cc/77W8-BMH9].

[333] *See, e.g.*, Rachel Bade, *Congress's Half-Trillion-Dollar Spending Binge*, POLITICO, Dec. 17, 2015, http://www.politico.com/story/2015/12/congress-spending-binge-tax-cuts-budget-deal-216883 [https://perma.cc/N8LJ-DBZY] (describing concerns voiced by some House Republicans when

only on paper, it remains the case that ceteris paribus, members of Congress (or at least some of them) would be more inclined to vote for legislation that is revenue neutral than legislation that is deficit increasing.

Why might this matter to the President when considering whether to implement revenue-raising measures unilaterally? One possibility is that Presidents will "save up" revenue-raising measures for future negotiations with Congress regarding the budget. Administration officials might realize that they could raise revenues by nearly $10 billion over the next decade through regulations preventing dual-capacity taxpayers from claiming foreign tax credits where the relevant foreign country imposes no general corporate income tax,[334] but might decide that those $10 billion also could be used to (partially) offset the cost of a tax break or spending provision that the President favors. And if the Executive Branch adopts the revenue-raising measure unilaterally now, it loses the ability to use the measure as a chip when bargaining with deficit hawks in Congress down the line. The irony is that congressional deficit hawks—*because* they are less willing to support measures that add to the deficit—may deter the President from taking steps that would raise revenue and reduce the deficit. PAYGO may be a double-edged sword.

One possible solution would be to amend the PAYGO law so as to require the Executive Branch to keep a running tally of revenues raised through regulatory action, and then to allow those revenues to be used as an offset the next time Congress passes deficit-increasing legislation. Yet if the objective is overall deficit reduction, it is not clear whether such a reform would bring the budget closer in line with that goal. After all, the analysis in Section II.A does not suggest that the number of revenue-raising regulations will be *zero*: a pure strategy equilibrium of (*regulate*, *don't legislate*) is possible and a mixed strategy equilibrium in which the President sometimes acts unilaterally is also possible. And while the analysis in this section suggests that the norm of revenue neutrality may *sometimes* deter the President from acting on his own, it does not suggest that the shadow of PAYGO will *always* have that effect. Allowing for the use of revenues raised by regulation as part of the PAYGO calculus might motivate the President to act unilaterally in some instances that he otherwise might not, but in other instances the President might have acted even in the absence of the proposed PAYGO reform. If, for example, the President would have implemented the foreign tax credit measure that raises revenue by $10 billion regardless of PAYGO, then allowing those $10 billion to offset other tax cuts or direct spending would simply serve to loosen the PAYGO constraint.

The takeaway, then, is not that PAYGO is a bad idea or that it ought to be amended. Rather, the implication is that norms of revenue neutrality in Congress (binding or not) may have an as-yet-unrecognized effect on the President's incentives to act unilaterally. [335] So while the analysis here does not yield a concrete

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Congress passed a $680 billion tax package that will add to the national debt in December of 2015).

[334] *See supra* Section I.E.4.

[335] For an example of a recent discussion of PAYGO that ignores this potential unintended consequence of the law, *see* Nancy Pelosi, Opinion, *Shouldn't Congress Tell Us How We'll Pay for Tax Cuts?*, N.Y. TIMES, Mar. 22, 2016, http://www.nytimes.com/2016/03/22/opinion/shouldnt-congress-tell-us-how-well-pay-for-tax-cuts.html [https://perma.cc/ZZG3- QNDS].

proposal with respect to revenue neutrality requirements, it does serve to shed light on one of PAYGO's hidden costs.

C. Cheap Talk

So far, the analysis in this part has assumed that the Greenbooks reflect the genuine preferences of the President. The very question "why doesn't the President use his power to accomplish X?" assumes that X is an outcome that the President desires. That assumption is arguably naïve: perhaps Treasury officials place proposals in the Greenbook with no intention that those proposals will ever come to fruition.

Yet if this is so, it is difficult to explain what exactly the Executive Branch gets out of putting a proposal in the Greenbook. Perhaps it is a way of mollifying progressives or deficit hawks without incurring the wrath of interest groups with a stake in the status quo. But for that strategy to work, it would require (1) that pro-tax constituencies are sophisticated enough to be paying attention to the Greenbook while (2) not being so sophisticated as to understand that the Greenbook is cheap talk, while at the same time (3) the interest groups with a stake in the status quo *are* sufficiently sophisticated to understand that Greenbook talk is cheap. This confluence of conditions is perhaps conceivable, but not particularly plausible.

Another sense in which Greenbook proposals might be "cheap talk" is that they are relatively cheap to write. That is, the time and resource costs borne by Treasury and IRS officials are likely lower with respect to Greenbook proposals than with respect to regulations that have the force of law. Since Greenbook proposals are only proposals, the language does not have to be airtight. And Treasury need not go through notice and comment or observe other procedural niceties with respect to the Greenbook each year.[336] But while Greenbook talk is no doubt cheaper than regulation writing, the costs of the latter are not prohibitive. When a policy goal becomes a top presidential priority, the Executive Branch is capable of acting expeditiously.[337] None of this is to deny that resource constraints play a very real role in the day-to-day operations of the Treasury Department. But it is to suggest that resource constraints are endogenous to the political dynamics of tax lawmaking.

Conclusion

So far, this article has argued that the President's "power to tax" under existing statutes is broad, but that notwithstanding this power, the President repeatedly asks Congress to pass revenue-raising measures that he and his Treasury Secretary could implement on their own. This article has presented several

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[336] To be sure, legislative drafting requires resources as well. But those costs potentially can be passed off to Hill staffers at the relevant congressional committees—the House Ways and Means Committee and the Senate Finance Committee, as well as the lawyers at the Joint Committee on Taxation and the House and Senate Offices of the Legislative Counsel who assist members of Congress in drafting statutes.

[337] *See, e.g.*, Elizabeth Kolbert, *Midnight Hour*, NEW YORKER, Nov. 24, 2008, http://www.newyorker.com/magazine/2008/11/24/midnight-hour [https://perma.cc/64B9-7JKE] (discussing "midnight regulations" promulgated by previous presidential administrations).

plausible explanations for presidential inaction in tax law. These accounts do not, however, tell us whether the President *ought* to assert executive authority more robustly in the tax domain.

The observations above do shed some light on a separate normative question: whether Congress ought to give the President some authority to set tax rates. In a recent article, James Hines and Kyle Logue suggest that delegation of rate-setting authority "might be normatively attractive." [338] The Hines-Logue argument for delegation of rate-setting authority resembles arguments for delegation in other areas of law: agencies "have comparative advantages" relative to Congress "in terms of expertise and time";[339] delegation gives agencies greater "flexibility" to respond to changes in the legal environment and the economy;[340] and "the President answers to a majority of the electorate in a way that no single legislator or even group of legislators does."[341] The analysis in Section II.A suggests, though, that delegation in the tax context might have different results than in other domains. Interest group politics push the President to exercise executive power over tax law largely in one direction: in favor of the taxpayer. That result may appear to be positive or negative depending on one's ideological commitments; at the very least, it makes us doubt whether a President with even broader delegated authority over tax law would act as a faithful agent of his congressional principals.

Congress, then, might be well advised to resist calls for delegation of rate-setting authority to the President. This does not mean, though, that the President ought to refrain from exercising the authority that Congress already has delegated. As a normative matter, it is difficult to see why the President ought to be any less willing to exercise his statutory authority in tax law than in other domains. Indeed, lawmakers likely would prefer for the President to exercise that authority—and to do so in a revenue-raising direction, so that Congress can share in the political rewards from spending without sharing the political costs of raising revenue. Moreover, the fact that Congress has failed to act on a proposal in the Greenbook does not imply congressional disapproval of the proposal. It may mean, to the contrary, that members of Congress *want* the President to implement those policies himself.

Finally, the analysis in this article identifies two features of the political environment that decrease the likelihood of unilateral executive action to raise revenue: (1) revenue-raising actions rarely yield political benefits except insofar as they facilitate additional spending; and (2) members of Congress are more likely to

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[338] *See* James R. Hines Jr. & Kyle D. Logue, *Delegating Tax*, 114 MICH. L. REV. 235 (2015). Hines and Logue cite work by political scientists David Epstein and Sharyn O'Halloran suggesting that Congress is less likely to delegate power to the President in the tax content than in other policy areas. *See id.* at 237 (citing DAVID EPSTEIN & SHARYN O'HALLORAN, DELEGATING POWERS: A TRANSACTION COST POLITICS APPROACH TO POLICY MAKING UNDER SEPARATE POWERS 196–203 tbl.8.2 (1999)). Note, though, that Epstein and O'Halloran's results are based on the *percentage* of public law provisions in particular areas that delegate discretion to the Executive. Results for tax may be skewed by the fact that a single provision, section 7805, authorizes the Treasury Secretary to "prescribe all needful rules and regulations for the enforcement of [the Internal Revenue Code]." 26 U.S.C. § 7805(a).

[339] Hines & Logue, *supra* note 338, at 261.

[340] *Id.*

[341] *Id.*; *cf.* Jerry L. Mashaw, *Prodelegation: Why Administrators Should Make Political Decisions*, 1 J. L. ECON. & ORG. 81, 95 (1985) (making similar arguments in the non-tax context).

support legislation if it is scored as revenue neutral. The first factor reduces the President's willingness to act when that means he will bear the political costs of revenue raising on his own; the second factor encourages the President to "save up" revenue-raising measures so that they can be used as offsets for future expenditures or tax cuts that he supports. Neither factor is necessarily a permanent feature of the political landscape.

As for the first factor, 63% of respondents in a recent Gallup poll said that wealth in the United States should be more evenly distributed, and 52% supported heavy taxes on the rich as a redistributive mechanism.[342] We may be nearing a time when a President can score political points through revenue-raising regulations that disproportionately affect large corporations and wealthy taxpayers. As for the second factor, concern about the deficit appears to be on the decline—both among members of the public and in the halls of Congress. Only 11% of respondents in a recent Wall Street Journal/NBC News poll ranked the deficit as a "top priority," down from 22% four years earlier.[343] Other surveys identify a similar trend.[344] And a tax deal that flunked the revenue neutrality test by a $622 billion margin nonetheless passed the House and Senate with large bipartisan majorities at the end of 2015.[345] If lawmakers are unconcerned with revenue neutrality, then the President has less of an incentive to save up revenue-raising measures for future bargaining with Congress. And if legislative gridlock makes any entitlement expansion or sweeping tax reform package unlikely, then the President has even less reason to save up revenue-raising measures for future bargaining with Congress because such bargaining is unlikely to bear fruit anyway.

These trends help us make sense of the Obama administration's April 2016 actions on corporate inversions. The simplifying assumption in the game-theoretic model is that the only political benefit from revenue-raising tax measures comes through the expenditures enabled by additional revenue, but that simplifying assumption probably does not hold true for the inversions case. Cracking down on U.S. corporations that seek to lower their tax bills by merging with foreign counterparts quite likely would be a politically popular endeavor,[346] even if the Treasury Department burned the additional cash generated by its actions. This is not necessarily a problem with the model as much as an additional implication: Presidents will be more willing to take revenue-raising actions unilaterally when those actions yield political benefits over and above the political benefits from spending.

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[342] Frank Newport, *Americans Continue to Say U.S. Wealth Distribution Is Unfair*, GALLUP (May 4, 2015), http://www.gallup.com/poll/182987/americans-continue-say-wealth-distribution-unfair.aspx [https://perma.cc/95T6- D6XG].

[343] *See* Janet Hook, *Deficit Concern Fades in Congress, Among Voters and on the 2016 Trail*, WALL ST. J., Dec. 22, 2015, http://blogs.wsj.com/washwire/2015/12/22/deficit-concern-fades-in-congress-among-voters-and-on-the-2016-trail [https://perma.cc/9DAK- P22L].

[344] *See, e.g.*, *Budget Deficit Slips as Public Priority*, PEW RESEARCH CTR., (Jan. 22, 2016), http://www.people-press.org/2016/01/22/budget-deficit-slips-as-public-priority [https://perma.cc/V76N- 25YS] (reporting results of a Pew Research Center survey finding that 56% of U.S. adults in 2016 say that the budget deficit is a "top priority," down from 64% in 2015).

[345] *See* Hook, *supra* note 345.

[346] For an unscientific poll showing 71% support for the Obama administration's April actions, *see* *Most Support Crackdown on Inversions*, ROCHESTER BUS. J., Apr. 15, 2016, http://www.rbj.net/article.asp?aID=226042 [https://perma.cc/FL46- J4YJ].

The inversions case is consistent with the comparative statics in Part II in still other ways. Conditions that make executive action more likely are present with respect to inversions. The congressional leadership is constrained by an anti-tax faction, which effectively rules out the (*don't regulate*, *legislate*) option. In those circumstances, regulation becomes the President's dominant strategy. Meanwhile, the low probability of election year tax reform means that the PAYGO deterrent is largely absent today: there are no significant entitlement expansions or tax cuts on the horizon that the Obama administration might want to offset. The likelihood that President Obama would be succeeded by another Democrat also reduced the risk that revenue-raising executive actions would be reversed by a successor of the rival party seeking to score political points. Perhaps it should not be surprising, then, that the President and his Treasury Secretary chose this time and this issue for unilateral action.

Does 2016 mark a turning point in the politics of taxation? The fact that the April 2016 actions were followed by proposed rules on FLPs four months later might suggest so: as voters become more concerned about inequality and less so about the deficit, the political calculus with respect to revenue-raising tax regulations may change. Or the Obama administration's last-year actions might suggest a fleeting confluence of circumstances—a second-term President likely to be succeeded by a political ally and facing an opposition party in Congress whose members can credibly commit the party leadership not to pass revenue-raising measures. "Prediction is difficult, especially about the future."[347] What does seem evident, though, is that if a future President decides to exercise the full range of his (or her) power to tax under existing statutes, he or she will find that long-latent power to be vast indeed.

[347] This quotation is often attributed, with slightly different phrasings, to both Niels Bohr and Yogi Berra, though its true origins are unclear. *See Letters to the Editor: The Inbox, The Perils of Prediction, June 2nd*, THE ECONOMIST (July 15, 2007), http://www.economist.com/blogs/theinbox/2007/07/the_perils_of_prediction_june [https://perma.cc/4B4F- 7DGX].