

10-1-1974

Tax Reform and Tax Simplification

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university of miami law review

VOLUME 29

FALL 1974

NUMBER 1

TAX REFORM AND TAX SIMPLIFICATION

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I. INTRODUCTION

Neither "tax simplification" nor its mirror image, complexity, is a concept that can be easily defined or measured. I know of no comprehensive analytic framework for these ideas, nor are there any empirical studies supplying a "simplicity index" of particular areas of tax law and practice.¹ Journalists often ridicule the Internal Revenue Code by pointing to lengthy involuted provisions and to definitions that refer the reader to other definitions that in turn compel him to go even farther afield. A favorite example is the 554-word sentence that makes up Section 341(e)(1). But these statutory intricacies may in fact

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It is an honor, though a sad one, to contribute this article to an issue of the *University of Miami Law Review* in memory of Jack Chommie. Our acquaintance began with a letter written almost 21 years ago, when he had just begun his academic career at Dickinson School of Law, and continued throughout his unusually productive professional life, my last letter from him having arrived only a few weeks before his death. All who knew him in person, and the much larger group that was familiar with his written work, were impressed by the combination of technical competence, concern with broad issues, and personal idealism that his books and articles reflected.

1. For general discussions of this area, see Surrey, *Complexity and the Internal Revenue Code: The Problem of the Management of Tax Detail*, 34 LAW & CONTEMP. PROB. 673 (1969); Woodworth, *Tax Simplification and the Tax Reform Act of 1969*, 34 LAW & CONTEMP. PROB. 711; [hereinafter cited as Woodworth]; Roberts, *A Report on Complexity and the Income Tax*, 27 TAX L. REV. 325 (1972); Ginsburg, *Tax Simplification—A Practitioner's View*, 26 NAT'L TAX J. 317 (1973).

be of minor importance, if they are addressed to tax experts concerned with transactions that rarely occur; and they may even clarify the law, despite their initially baffling phraseology. Sections 671-675, for example, are intricate provisions. As compared with the pre-1946 law governing income-splitting trusts, however, their message is crystal-clear. The statutory language was simpler in earlier years, but the taxpayer and his adviser had to weigh the implications of hundreds of judicial decisions, most of which simply announced that all of the relevant facts and circumstances were to be weighed in determining whether the income of a trust was taxable to the grantor or to its trustee and beneficiaries. The 1945 regulations and 1954 statutory rules that replaced these judicial decisions were complex, but they made it much easier to find one's way through the wilderness. On the other hand, elaborate statutory verbiage *can* be a source of complexity and an obstacle to simplification; I will offer some instances later in this paper.

Simple language can also be a source of complexity. When the taxpayer is advised by Section 163 that he can deduct "all interest paid or accrued during the taxable year on indebtedness" and by Section 166 that he can deduct "any debt that becomes worthless within the taxable year," the terms "interest" and "debt" are disarmingly simple. But these words and others like them have been interpreted by thousands of administrative rulings and judicial opinions, without exhausting the possibilities. In some instances, it may be possible to simplify the law by defining terms like these, either in the Code or by Treasury Regulations; and occasionally the problem of ambiguity may be side-stepped by depriving concepts like these of operative significance. If scholarships were not exempt, for example, it would not be necessary to decide whether money received by a student from a university was a "scholarship" or a "salary." Often, however, there are valid reasons for using these slippery terms, and little prospect of defining them with precision.

It is unfortunately the fact that, by its very nature, a tax on income must take account of an almost infinite spectrum of business, investment, and personal events and transactions. When such a tax is imposed on tens of millions of taxpayers at rates yielding tens of billions of dollars, only an incorrigible optimist could expect the kind of simplicity that can be achieved with a poll tax, or that is characteristic of local real property and sales taxes. Income taxation entails a high level of irreducible complexity. In my opinion, the price is worth paying; but there is in any event no likelihood that the income tax will be repealed in the interest of achieving simplicity.

II. INHERENT STRUCTURAL COMPLEXITIES IN EXISTING TAX LAW

Quite aside from the irreducible complexity of even the simplest income tax, a host of additional complexities in existing law are the

result of policy decisions that are not likely to be reversed in the foreseeable future. I would like to mention these aspects of existing law, without discussing them in detail, simply to describe the context within which tax simplification must be considered. As economic and political decisions, they may be good or bad—I will not pause to debate them—but there can be no doubt about their contribution to complexity. These structural features of existing law, which may be modified in minor respects but seem in the main to be invulnerable to major change, include the following:

A. *The Concept of Realization*

Taxpayers are not taxed on appreciation in the value of their property, nor are they permitted to deduct a decline in value, until the property is sold or otherwise disposed of. Although the statutory requirement of a realization was given constitutional status by *Eisner v. Macomber*,² it is quite unlikely that the courts would impose this requirement today. If taxpayers were required to value their assets annually, and to take the current increase or decrease into account currently, a number of complexities in existing law would evaporate. Among them would be the elaborate rules regarding non-taxable exchanges, the separate tax status of the corporation, and the distinction between business expenses and capital outlays. Conversely, preservation of the concept of realization necessarily requires statutory, administrative and judicial rules to cover these areas, along with many others. I do not mean to imply that there would be no offsetting social costs in complying with an income tax law taking account of annual changes in the taxpayer's net worth. The appraisal industry would flourish, and its fees would no doubt be very considerable. I doubt, however, that they would approach the cost of administering the concept of realization as it operates in existing law. In any event, I see no disposition in Congress to abolish the concept of realization in order to achieve simplification of the tax law.

B. *Cash Basis Accounting*

A closely related structural feature of existing law is the privilege of reporting income on a cash basis, which is open to almost all individual taxpayers and to many corporations. This privilege creates many opportunities to postpone the recognition of income, opening the door to a variety of tax deferment schemes. Some are either blocked or, more frequently, inconvenienced by statutory or administrative counter-measures. If all taxpayers were required to report on an accrual basis, these complexities could be greatly reduced.

However, cash basis accounting is more convenient for millions of taxpayers whose only records consist of their bank statements and cancelled checks, and it brings tax liability into closer contact with the taxpayer's cash receipts than does accrual accounting. Here again, I

2. 252 U.S. 189 (1920).

see little prospect of a major reform, despite the contribution it could make to simpler rules of substantive tax law, especially since the cost and inconvenience of requiring millions of taxpayers to use accrual method would be an offsetting social burden.

C. *The Corporation as a Separate Entity*

Because the corporation is regarded as a separate taxable entity, rather than as a partnership of its shareholders, the Code must contain an elaborate set of rules to govern the distribution of dividends, unreasonable accumulations, stock redemptions, corporate liquidations, and other transactions between the corporation and its shareholders. Many of these rules could be abolished, and others could be simplified, if the corporation were treated as a partnership.³ A less drastic step, deserving more study than it has had so far, would be a requirement that closely-held corporations, but not publicly owned corporations, be compelled to elect Subchapter S treatment. Neither of these possibilities has emerged from the stage of academic discussion, however, with the result that the statutory rules based on the corporation's separate entity will not lose their importance, or their complexity, for the foreseeable future.

D. *Progression in the Rate Structure*

Although the effective rate of income taxation is not nearly as progressive as the schedule of marginal tax rates suggests, there is enough residual progression to stimulate income-splitting devices on a large scale, as well as to encourage other avoidance techniques. The exploitation of these opportunities, and the counter-measures adopted by Congress, the Internal Revenue Service and the courts in an effort to frustrate the most egregious of them, account for many complexities in existing law. But progression is a deeply entrenched feature of our income tax system, with its own rationale; and its preservation necessarily requires the payment of a price in terms of legal and accounting complexities. Speaking for myself, I would prefer more progression, despite the additional complexities it would entail, rather than less.

E. *Reduced Rate for Capital Gains*

The fact that long-term capital gains are subject to a lower tax rate than other types of income is perhaps the single most complicating aspect of existing law. Preservation of the differential, even if it is slightly narrowed by minor reforms, inevitably serves to perpetuate complexities that are, of course, well known to the architects of tax laws in Congress. Moreover, the differential rate for capital gains differs from some of the other structural features of existing law that I have mentioned (e.g., the concept of realization) in that its abolition would not create a new source of compliance expense.

3. See discussion in *Estate of Leonard E. Whitlock*, 59 T.C. 490 (1972).

F. *Multi-Purpose Tax Provisions*

In raising revenue, a tax necessarily pinches some people more than others, and in doing so affects everyone's behavior. Strictly speaking, therefore, no tax can be neutral. There are, however, varying degrees of non-neutrality; and as incentives, relief provisions and penalties are added to the Internal Revenue Code, complexities in interpreting and enforcing it are bound to multiply. For many if not most provisions of this type, however, plausible economic and social reasons can be advanced. Though every tax commentator asserts that we are attempting to accomplish too many objectives and has his own favorite list of unjustified incentive and relief provisions, few want to repeal all such adjustments; and there is in any event little likelihood that those who favor such draconic action could persuade Congress to accept their recommendations.

III. POSSIBLE AREAS OF SIMPLIFICATION

Against this background, a dramatic reduction in complexities is simply not in the cards. There are, however, some areas in which marginal improvement is possible, and others that will be the breeding grounds for new complexities unless we exercise great vigilance. I would like now to turn to an examination of these areas.

A. *Simplification of "Mass" Provisions*

I would attach primary importance, so far as simplicity is concerned, to "mass" provisions affecting millions of taxpayers, even if the dollar amount per taxpayer is small and the complexities are mild when compared with the trust and corporate areas.⁴ As an example of what I mean, let me refer to Form 2441, attached as Appendix A, which is to be filed by every taxpayer claiming a deduction under Section 214, the so-called dependency care provision. Because Section 214(c)(1) limits the deduction to \$400 per month, Form 2441 requires taxpayers to report their expenses on a monthly basis. This is annoying enough, but since the statute refers to expenses that are "incurred" during the month, taxpayers are put on an accrual basis in applying the \$400 limit, even though their income and other deductions are computed on a cash basis. Without doubt, however, many taxpayers think that the amount *paid* during the month is controlling. Some of them short-change themselves, for example, by deducting only \$400 for a month in which a domestic servant is paid \$600 for two months' work. Others inadvertently or deliberately violate the statute, for

4. When the standard deduction is increased in amount, the number of taxpayers who itemize their personal deductions is reduced, and this simplifies the law for them, as pointed out by Woodworth, *supra* note 1. But there is an offsetting cost. If a taxpayer with medical expenses, casualty losses, bad debts, etc. *should* pay less than a taxpayer with an equal amount of adjusted gross income who has not experienced these losses, an increase in the standard deduction reduces or eliminates the differential. Administrative convenience and fairness are, unfortunately, competing values.

example, by deducting \$400 a month for a servant who earns \$4,800 for 10 months of work but is paid at the rate of \$400 a month throughout the year. The \$400 a month limitation may serve a useful purpose in theory, but I very much doubt that it justifies requiring millions of taxpayers to shift from cash basis reporting to an accrual method in computing their monthly expenditures. Most of these taxpayers have no records other than their checkbooks and cancelled checks, which disclose their cash payments but do not allocate the cost of household services and dependent care to the particular months in which the services were rendered.

This departure from cash accounting in computing monthly expenditures under Section 214 is even more troublesome than it initially appears because the taxpayer is then required by Section 214(a) to shift back to cash accounting in ascertaining the aggregate amount that can actually be deducted for the year. This means, in some cases, that amounts paid in January for services rendered in December of the previous year (or, conversely, paid in December for services to be rendered in January) are not deductible in either year. In practice, many taxpayers no doubt add up their actual expenditures during the year for Section 214 items, divide by 12, and enter the resulting amount for each month on Form 2441. Unless the Internal Revenue Service demands an explanation from everyone who reports the same amount of Section 214 expenditures for every month of the year (an enforcement practice that would be both wasteful and abrasive), the accounting niceties of Section 214 may well become a dead letter except for the taxpayer who is unusually scrupulous, who is advised by an expert, or whose return happens to be audited by a particularly diligent revenue agent.⁵ A paradox of this type of statutory refinement is that its equity objective is often not attained because the intricate rules cannot be uniformly enforced, so that the result in practice—as distinguished from theory—is that some taxpayers get the relief intended, others do not even if they are similarly situated, and everyone pays the price of the extra complexity.

Another example of statutory requirements that overload both the taxpayer's capacity to comply and the Internal Revenue Service's capacity to enforce the law is the 1962 travel and entertainment rules. Section 274 is replete with fine distinctions (graphically portrayed by the "road map" in Appendix B) that might possibly be given meaning if applied to a limited number of very important transactions, but that, in my opinion, cannot possibly be enforced with an acceptable degree of uniformity in the area for which they are prescribed. I refer, for example, to the difference between entertainment that is "directly related" to the active conduct of the taxpayer's business and enter-

5. For the Internal Revenue Service's own difficulties with section 214, resulting in errors on Form 2441 as prescribed for the calendar year 1972, see *Panel Discussions*, *supra* note 1, in the footnote denoted by (*), at 125-26.

tainment that is only "associated" with the active conduct of the business, as well as to such phrases as "substantial and bona fide business discussion," "primarily for the furtherance" of business, and "circumstances . . . generally considered to be conducive to a business discussion." By themselves, any of these phrases might be enforceable, but the problem is that they are all imposed in addition to the general requirement of Section 162 that the expense be "paid or incurred . . . in carrying on [the taxpayer's] trade or business," and there is no objective measure of what they add to this threshold requirement. Except for the substantiation rules and the debatable dollar limit on business gifts, the elaborate verbiage does almost nothing that could not have been achieved by a simple presumption or a single hortatory adjective.⁶

A systematic study of the sources of misunderstanding and error in "mass" tax provisions would be illuminating. Such a study could well begin with a tabulation of the questions put by taxpayers to the taxpayer assistance offices of the Internal Revenue Service; and it would be equally useful to know whether some questions cannot be readily answered by agents assigned to this function because they themselves find it difficult to interpret the statutory provisions. Such a study ought to include an examination of a random sample of low income returns to identify recurring errors attributable to statutory intricacies. (For example, how often do taxpayers misapply the rules governing deductibility of medical insurance premiums?) The aim of the study should not be to ascertain whether taxes are overpaid or underpaid as a result of interpretive errors. It should be, rather, an evaluation of the interpretative problem itself, leading to a judgment on whether the statutory draftsman's ingenuity has outstripped the capacity of taxpayers to comply with the law and the Service's capacity to enforce it.⁷ Above all, the study should be conducted in collaboration with independent outside experts and on completion should be made available for public analysis.

B. "Token" Reform Measures

A second major problem in the area of tax simplification is the growing tendency to complicate the Code with token reform measures

6. See the recent comment by Judge Hall in *George Durgom*, P-H TAX CT. REP. & MEM. DEC. ¶ 74,058, at 74-265 n.3 (March 7, 1974) (mem.):

While it is this Court's role to construe and apply the Code and regulations and not to intrude its own notions as to tax policy, the extremely laborious task cut out for us by the application to the facts of this case of an almost unbearably prolix and convoluted set of regulations [under section 274] makes it difficult to resist the observation that the average citizen to whom these regulations are applicable could not realistically be expected to comprehend and follow them in every precise detail, if they are construed in the most rigorous possible sense. The Court has accordingly attempted to give the regulations as common-sense a construction as the rather astounding wording permits.

7. A "Readability Analysis" of the Instructions to Form 1040 (conducted by Dr. Roy J. Butz, Reading and Language Center, Pontiac, Mich.) reached the conclusion that a taxpayer would have to read at the college graduate level to understand these instructions. See also the Crossley Survey, commissioned by the Internal Revenue Service, 118 CONG. REC. 13195-204 (1972).

that pacify complainants rather than solve problems. An illustration is the minimum tax for tax preferences, enacted in 1969.⁸ This intricate provision imposes an actual tax liability on only a comparative handful of taxpayers (19,000 individuals in 1970), but it compels many more to work through its calculations to determine if it applies to them. In 1970, 76,000 taxpayers filed Form 4625, required of every taxpayer with more than \$15,000 of tax preference items, even if no minimum tax is due. It would be instructive to know how many more should have been filed.

If the minimum tax remains in force, we can anticipate an endless series of proposals to amend it. Some will wish to tighten it by enlarging the list of preferences, lowering the exempt floor and raising the rate. Others will propose to eliminate "inequities" by permitting tax preferences and taxable income to be averaged over a period of years, by stepping up the basis of property to reflect the minimum tax paid on accelerated depreciation, amortization, stock options, etc., and introducing other refinements. More important, the mere existence of the minimum tax will provide a permanent mechanism for avoiding fundamental reform, just as the mere existence of the special rate on long-term capital gains has invited the proliferation of provisions to give similar benefits to a host of other items.

According to former Undersecretary of the Treasury Cohen, more than 80% of the preference income reported by the 19,000 individuals subject to the minimum tax in 1970 was the excluded half of long-term capital gains; percentage depletion was evidently the second most important item when individuals and corporations are combined.⁹ In my opinion, a comparatively small change in the capital gain area—reducing the excluded portion, for example, or lowering the amount subject to the 25% rate ceiling—would accomplish more by itself, and would set a better precedent, than tinkering with the minimum tax.

Another illustration of tokenism is the "excess farm deduction account" established by section 1251, enacted in 1969. Section 1251 requires a taxpayer who deducts farm losses from non-farm income to establish an "excess deductions account" if his adjusted gross from non-farm sources exceeds \$50,000 and his net loss from farming exceeds \$25,000. The account is carried forward from year to year, reduced by any profits he may make from his farming activity. If there is a balance in the section 1251 account when the farm is sold, any profit on the sale must be reported pro tanto as ordinary income, rather than as long-term capital gain.

Section 1251, to be blunt, is either much ado about nothing, or

8. See Note, *The Minimum Tax for Items of Tax Preference . . . Movement Toward a Comprehensive Tax Base?*, 41 U. CIN. L. REV. 365 (1972); Schenk, *Minimum Tax for Tax Preferences*, 48 TAXES 201 (1970).

9. Remarks of Edwin Cohen to Tax Forum, United States Chamber of Commerce, Nov. 29, 1973 (Transcript at 13).

much ado about nearly nothing. If the taxpayer ultimately sells his farm at a loss, there will be no capital gain to be transmuted by section 1251 into ordinary income. If he passes the farm on to his heirs at death, it will get a new basis under section 1014, unless existing law is changed by enactment of a constructive realization or carryover-of-basis provision. If the farm is transferred by gift, incorporated or exchanged in a tax-free transaction, the taxpayer's "excess deductions account" will be inherited by the new owner. But it is a reasonable prediction that this theoretical carryforward will often be forgotten in practice, however ingenious it may be in theory. The transmutation of capital gain into ordinary income, in short, will occur in only a fraction of the cases in which excess farm losses are realized.

Even when section 1251 actually triggers a conversion of long-term capital gain into ordinary income, it will often be only a slap on the wrist. Assume, for example, that Farmer Brown had a farm net loss of \$125,000 in 1971, operates at a \$25,000 loss every year from 1972 to 1980, and sells his farm at the end of 1980 at a profit of \$1,000,000. Only \$100,000 of this long-term capital gain will be adversely affected by section 1251. Let us assume that section 1251 increases the tax on this \$100,000 of long-term profit from \$35,000 (capital gain rate of 35%) to \$70,000 (maximum ordinary income rate of 70%). This means, in effect, that as of 1971, when Farmer Brown incurred \$100,000 of "excess deductions," he saved \$70,000 of federal income tax, and was told that 10 years later he may have to pay an additional \$35,000 of taxes as retribution. The net result is that his \$70,000 of tax savings in 1971 is reduced by the discounted value of \$35,000 to be paid 10 years later, *viz.*, \$13,500 if the discount rate is 10%. If the taxpayer in question sold his farm at a profit in less than 10 years from the date when he enjoyed the excess deductions, or if the appropriate discount rate is less than 10%, section 1251's penalty would of course be more costly; but by the same token, if the holding period of the farm was longer than 10 years or the appropriate discount rate is greater than 10%, the penalty would be even more lenient than in my example.

Section 1251 is presumably addressed to two problems. One is the fact that some taxpayers with substantial amounts of non-farm income are able to persuade the Internal Revenue Service and the courts that their farms are bona fide businesses (and thus to escape section 183), when in fact they are hobbies. The other problem is that the Code permits farmers to deduct a variety of expenditures that add to the value of their farm properties and that, by ordinary accounting standards, should be capitalized rather than deducted. These are both genuine problems, but section 1251 is only a token response to them. Analyzed in isolation, section 1251 is innocuous; one might debate whether it is better than nothing, or worse. One might ask, for example, why losses on a citrus grove should escape section 1251 if the

taxpayer's other income is derived from a wheat farm, but fall into section 1251's grasp if his income comes from selling hardware or practicing law; or why soil conservation expenditures incurred and deducted in 1971 should be recaptured in 1980, if their usefulness was exhausted in prior years, so that the gain on selling the farm does not in any way reflect these expenditures; and so on.

But my complaint is not the scope of section 1251. It is, rather, that section 1251 may elicit more token responses to genuine problems. (Indeed, one might argue that this trend began with the recapture provisions of section 1245 and section 1250.) If accepted as a model, section 1251 might be followed by dozens of separate "excess deduction accounts," each posing as a "reform" of one of the numerous other statutory provisions for the current deduction of expenditures that, by normal tax accounting standards, should be capitalized. These include research and experimental expenditures, intangible drilling and development expenses, circulation expenses of newspapers and magazines, accelerated depreciation and many others—any of which may be deducted from income generated by other activities.¹⁰

In my opinion, each of these provisions should be dealt with head-on, not by establishing a mini-schedule that segregates its benefits for recapture when, as and if some event occurs in the future. If the provision serves a useful purpose, let it be accepted and defended wholeheartedly; if it is too generous, cut it back directly by imposing percentage, dollar or similar limits in the year when the deduction is taken; if it has outworn its usefulness, repeal it. The kind of tokenism that is typified by section 1251 needlessly complicates the Code, and its remedy, when it actually applies, is utterly erratic.

C. *Excessive Statutory Detail*

I have suggested earlier that detailed statutory provisions can simplify rather than complicate the law. Having acknowledged this, however, I want to go on to argue that the Code has far too many detailed provisions, but that this affliction, in a curious way, is a tribute to the extraordinary analytic skills that have been developed in the last few decades by both government and private tax experts. To illustrate my point, let me refer to the variety of constructive ownership rules in the Code, illustrated by the chart in Appendix C. (Though only seven years old, the chart would already have to be amplified to encompass all the refinements of today's Code.) Another illustration is the network of private foundation rules, enacted in 1969, which a leading tax practitioner has summarized in the chart in Appendix D. He has identified 14 categories of charitable organizations, which are subject to 34 different legal requirements, so that a

10. Other precedents for the segregation of income and deductions from a particular type of activity are sections 1211 and 1212 (capital losses) and section 163(d) (excess investment interest).

portrait of the way the rules apply to each category of organizations requires a chart with 476 cells.

While some of this statutory complexity is accidental, much of it results from the tax expert's analytic skill in sniffing out the potential abuses and potential inequities that can be generated by general rules, coupled with a utopian passion for eradicating both flaws. These talents are possessed in equal measure by lawyers in the Treasury, on the staff of the Joint Committee on Internal Revenue Taxation, in the practicing bar and in the academic world. The experts are of course not autonomous, and the substantive rules which they advocate reflect the deeper interests—financial, political, social, and intellectual—that they represent or reflect. But however divergent their motives and objectives, their common passion is a rule for every conceivable set of circumstances. Lest I be accused of treason to my profession, perhaps I should add that tax economists have a passion for macroeconomic concepts that can keep them from seeing the trees in the forest; if lawyers are overly preoccupied with statutory detail, economists too often discount its importance. Perhaps what we need is an exchange of roles.

The expert who represents the interests of clients wants to hobble every lever that might be used by a revenue agent or court to manipulate a proposed general rule, while the reformer cannot sleep easily unless he has blocked up every chink in the government's armor. These drives—which generate a common distrust of generalities—are unfortunately not counterbalanced by an equally powerful concern with the problems of interpreting and enforcing the resulting complex statute. Legislative deadlines discourage attention to anything other than a remedy for the potential abuse or inequity. It is easy to persuade oneself that the Treasury Regulations will clarify the intricacies, and the private practitioner who is trying to get a concession is not inclined to look a gift horse in the mouth. Thus, simplicity is like a lighthouse: everyone can attest to its value, but no one will pay the price voluntarily.

I find it easy to understand this important source of complexity, because I have contributed my share, and I am not sanguine about eliminating it, because I would not myself readily put my analytic and critical skills on the shelf. To suggest to tax lawyers that they should refrain from exercising their talents when the point of diminishing returns is reached is like asking doctors to suppress their impulse to keep patients alive by every available scientific device: we have no agreed or enforceable criteria to determine how far is too far. I regret that the best I can offer by way of prescription is a more self-conscious recognition of our passion for intricate detail and an acknowledgement that elaborate formulations are useless if they cannot be effectively enforced.

D. *Private Legislation Couched in General Terms*

The Code contains a number of provisions that were intended to provide relief for a particular taxpayer or institution, but that are couched in general terms. Because the tax adviser must pore over these provisions to see whether they may apply to his client, they add to the complexity of the law. Their contribution to this plague may not be substantial, but it is particularly galling because the provisions often make no redeeming contribution to the fairness or efficiency of the tax law. They are also irritating monuments to the importance of persuading the right legislator at the right time of one's case for special treatment—an opportunity that comes to few taxpayers among the many whose claims are equally valid.

It is possible, of course, to overstate this objection, since by drawing attention to a serious problem, a specific taxpayer's complaint may stimulate enactment of a provision that, though narrowly drawn, encompasses other taxpayers who are similarly situated. I disagree, for example, with the conventional criticism of the unlimited charitable deduction of section 170(b)(1)(C), and regret its repeal; though enacted to aid a particular taxpayer, its effect was in my opinion salutary. Moreover, when a specialized complaint seems to deserve a favorable legislative response, something can be said for legislation of general though narrowly confined applicability, rather than a private bill naming the particular taxpayer. Since there may be others unknown to the legislature who are similarly situated, there is an aura of unfairness about private legislation. Even so, the Congress ought to consider the imposition of chronological deadlines more frequently in legislation of this character, so that the provision will be outlawed by time at an early date, rather than carried forward interminably. It is easier to extend the date of legislation that is scheduled for expiration, if a longer life seems warranted, than to repeal a provision that has no time limit, and hence may create expectations and action in reliance, even when it has outlived its usefulness.

E. *Stylistic Discipline*

Although the involuted phraseology of the Code may be less of a problem than humorists and even experts sometimes allege, it is certainly not a blessing. Moreover, one need not turn to the corporate, fiduciary or private foundation provisions for language that needs pruning, guideposts, better cross-references and other revisions. It is not really necessary, for example, to employ the windy formula that appears in section 214 and elsewhere: "In the case of an individual, . . . there shall be allowed as a deduction" when one can say directly: "An individual may deduct" Anyone who has asked a class of law students to read and explain the sick pay and related provisions (sections 104(a)(3), 105, and 106) can testify to the need for

greater clarity in provisions that affect millions of taxpayers. In a tribute to President Johnson, published in the New York Times on January 26th 1974,¹¹ Bill Moyers describes a session at a 1966 international conference when a final memorandum was being prepared for release to the press. The President looked at the draft, described by Mr. Moyers as written in "flat, sterile, polysyllabic prose," and insisted on rewriting the preamble. His objective, he said, was a revised version that "can be read in the public square at Johnson City." I don't propose a Code that can be read at town meetings, but if a provision intended for mass consumption cannot be summarized in language that will be understood by the citizens of Johnson City, it ought to be re-examined with great suspicion. And if a provision of the Code cannot be understood by a good law student with a grounding in taxation, there should be an irrebutable presumption that it needs to be re-written.

11. New York Times, Jan. 26, 1973, § L, at 35, col. 2.

APPENDIX A

Form

2441

Department of the Treasury
Internal Revenue Service

Expenses for Household and Dependent Care Services

Attach to Form 1040 (See instructions on back)

Name(s) as shown on Form 1040 _____

Your social security number _____

Computation of deduction for household and dependent care services

1 Monthly amounts incurred for employment-related expenses in the household (see General Instruction B and Specific Instructions for Line 1):

- (a) Dependent under 15 years of age _____
- (b) Disabled dependent _____
- (c) Disabled spouse _____

2 Monthly amounts incurred for services outside the household for care of a dependent(s) under 15 years of age. Enter lesser of amount incurred or \$200 for one, \$300 for two, or \$400 for three or more _____

3 Total (add lines 1(a), 1(b), 1(c), and 2) _____

4 If you entered employment-related expenses for a disabled dependent on line 1(b), above, an additional amount received this year by that dependent is in excess of \$750, divide the excess over \$750 by the number of months for which you have listed amounts on line 1(b). Enter this result or the monthly amount on line 1(b), whichever is smaller, in each monthly column in which an amount is listed on line 1(b) (see Specific Instructions for Lines 4 and 5) _____

5 If you entered employment-related expenses for a disabled dependent on line 1(c), above, and your disabled spouse received disability payments, divide the total disability payments received this year by the number of months for which you have listed amounts on line 1(c). Enter this result or the monthly amount on line 1(c), whichever is smaller, in each monthly column in which an amount is listed on line 1(c) (see Specific Instructions for Lines 4 and 5) _____

6 Total (add lines 4 and 5) _____

7 Subtract line 6 from line 3 _____

8 Monthly limitation _____

9 Enter lesser of line 7 or line 8 _____

10 If your adjusted gross income (line 15, Form 1040) is larger than \$18,000, divide the amount over \$18,000 by 24. Enter this result in each monthly column in which you have an amount listed on line 3 _____

11 Subtract line 10 from line 9. If line 10 is greater than line 9, enter "0" _____

12 Add amounts on line 11 and enter total here _____

13 Total amounts listed on line 11 paid during this taxable year or a prior taxable year (see Specific Instructions for Line 13) _____

14 Enter lesser of line 12 or line 13 _____

15 Deductible household and dependent care expenses incurred in prior taxable year not paid until this taxable year (attach schedule showing computation of deduction—see Specific Instructions for Line 15) _____

16 Allowable deduction this taxable year (add lines 14 and 15). Enter total here and include on line 32 of Schedule A, Form 1040 _____

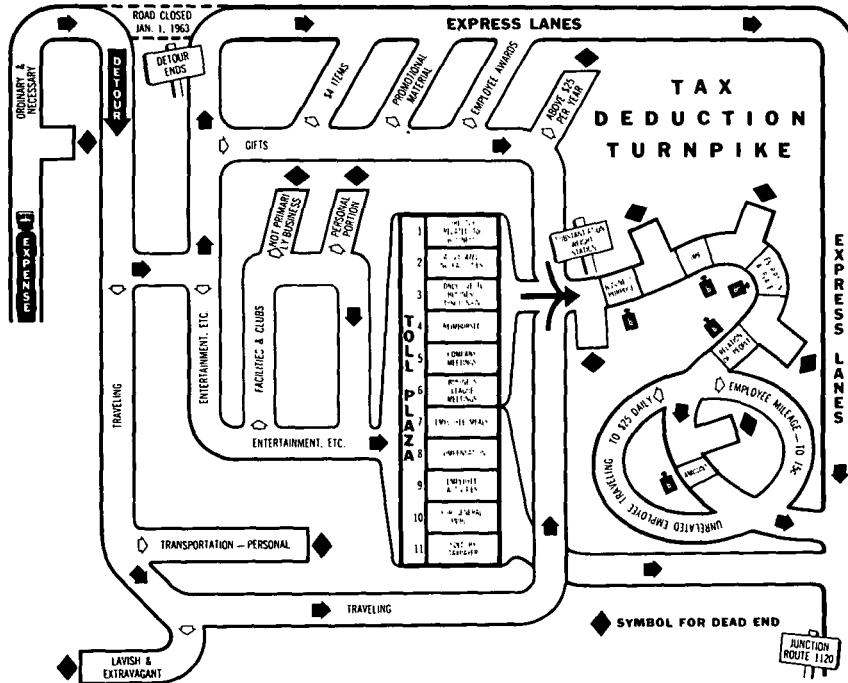
1973

APPENDIX B*

A New Road for T&E Expenses

THE FINAL travel and entertainment rules, despite "clarifying" attempts by the Commissioner, are still apt to be somewhat of a maze for the practitioner. To aid him in finding his way along the new route, we present a map of

the "Tax Deduction Turnpike," which has been prepared by Robert H. Monyek, CPA, of the Chicago office of Arthur Young & Company. In addition to giving an overall view of present rules, it may find popularity as a tax "Monopoly."



If an expense makes its way from the entrance to the road to its termination at Route 1120, (or Route 1040, as the case may be), it is deductible. However, in making the trip, a few words of explanation are needed:

1. Before January 1, 1963, all ordinary and necessary expenses proceeded onto the express lanes leading to Route 1120. Today, all such expenses must take the indicated detour, and only those ordinary and necessary expenses that are not required to take one of the three specific cut-offs find their way to the express lanes.

2. Traveling expenses must take the first cut-off, on which there are two potential dead ends which trap the personal portion of transportation expenses and expenses which are lavish and extravagant. The remaining traveling expenses continue on the cut-off to the junction leading into the weight station, where we shall rejoin these expenses at item 6 below.

3. Expenses for entertainment, amusement, and recreation take the second cut-

off, which leads into the toll plaza. Only those items which are permitted through one of the eleven toll gates may continue. Those passing through one of the last five gates go directly to the express lanes; the balance continue to the weight station.

4. The cost of facilities used for entertainment, amusement, and recreation must take an additional detour. Those not primarily for business run into a dead end, and even the personal portion of those used primarily for business must leave the road. The balance of the costs continue to the toll plaza, where all must pass through one of the gates. Note that gate two does not permit facilities to enter. After the toll plaza, the costs proceed either to the express lanes or to the weight station.

5. At the third cut-off, all gifts must turn. Gifts costing \$4 or less (containing taxpayer's name and widely distributed), gifts of promotional materials, and employee awards (tangible personal property costing \$100 or less, for service or safety achievement) are permitted to turn onto the ex-

press lanes, which lead directly to Route 1120. Gifts above \$25 per year per donee run into a dead end, and the balance continue on to the weight station.

6. At the weight station, the evidence in support of an item is measured. A diary entry is heavy enough to satisfy all the scalekeepers, except that a receipt is needed for items over \$25 and all expenses for lodging. The five scales require proof of the business purpose, time of expenditure, relation to business of all persons present at the expenditure, place and description of expenditure, and amount of expenditure. Note that mileage allowances to employees (up to 15¢) and travel expense reimbursements to employees unrelated to the employer (up to \$25 daily) may travel around the last scale.

7. Those expenses reaching the junction with Route 1120 are allowable as deductions.

8. While no speed limit is posted, the fact that the road is new and difficult indicates that we should travel it carefully.

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APPENDIX C

OUTLINE OF MAJOR ATTRIBUTION RULES

	SECTION 1363(e)	SECTION 267(c)	SECTION 318	SECTION 544(a)
A = Applicable		Applies to 257, 241(e), 707, Re;	Applies to 302, 304, 306(b) (1) (A), 334 (b) (3) (C), 382 (a) (3), 856(d), 958(b), 6038(d) (1) Re: Corporate Distributions and Adj., etc.	Applies to 341(d), 542, 543, Re; Collapsible Corporations and Personal Holding Companies
NA = Not applicable	Applies to 1551, 1561, 1562, 1563 Re: Surtax Exemptions, etc.	Disallowance of Losses and Unpaid Expenses & Interest		
1. Attribution from ownership of options:				
a. Option to acquire stock considered same as ownership of stock.	A	NA	A	A
b. Option to acquire option considered same as ownership of stock.	A	NA	A	A
2. Attribution from partnerships:				
a. Stock owned, directly or indirectly, by or for a partnership, is attributed to any partner with 5% or more interest in capital or profits, in proportion to his interest (greater of capital or profits).	A	NA	NA	NA
b. Stock owned, directly or indirectly, by or for a partnership, is attributed proportionately to each partner.	NA	A	A	A
3. Attribution from estates or trusts:				
a. Stock owned, directly or indirectly, by or for an estate or trust, is attributed to any beneficiary with 5% or more actuarial interest in such stock, to the extent of such actuarial interest.	A	NA	NA	NA
b. Stock owned, directly or indirectly, by or for a trust, is attributed to the grantor or other substantial owner of the trust.	A	NA	A	NA
c. These attributions do not apply to stock owned by a qualified employees' stock bonus, pension, or profit-sharing trust. ...	A	NA	A	NA
d. Stock owned, directly or indirectly, by or for an estate or trust, is attributed proportionately to each beneficiary.	NA	A	A	A
4. Attribution from corporations:				
a. Stock owned, directly or indirectly, by or for a corporation, is attributed to any stockholder who owns, actually or constructively, 5% or more in value of the corporation's stock, in proportion to the value of his stock interest.	A	NA	NA	NA
b. Stock owned, directly or indirectly, by or for a corporation, is attributed proportionately to each stockholder.	NA	A	NA	A
c. Stock owned, directly or indirectly, by or for a corporation, is attributed to any stockholder who owns, directly or indirectly, 50% or more in value of the corporation's stock, in proportion to the value of his stock interest.	NA	NA	A	NA
5. Attribution from spouse:				
a. General rule—individual is considered to own stock in a corporation owned, directly or indirectly, by or for his spouse.	A	A	A	A
b. Exception—general rule does not apply if each of the following conditions is satisfied for taxable year of corporation: ...				
(i) Individual does not at anytime during such taxable year own directly any stock in such corporation. (ii) Individual is not a director or employee and does not participate in management of corporation at any time during such taxable year. (iii) Not more than 50% of corporation's gross income for such taxable year was derived from royalties, rents, dividends, in-				

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OUTLINE <i>continued</i>	SECTION 1563(e)	SECTION 267(c)	SECTION 318	SECTION 544(a)
A = Applicable NA = Not Applicable				
terest, and annuities. (iv) Such stock in such corporation is not at any time in such taxable year, subject to conditions in favor of the individual or his minor children which substantially restrict or limit spouse's right to dispose of such stock.	A	NA	NA	NA
6. Attribution from children, grandchildren, parents and grand-parents.				
a. Children under 21 years of age:				
1. Individual is considered to own stock owned, directly or indirectly, by or for his minor children.	A	A	A	A
2. Individual under 21 years of age is considered to own stock owned, directly or indirectly, by or for his parents.	A	A	A	A
b. Adult children and grandchildren:				
1. Individual who owns, actually or constructively, more than 50% of total voting power of all stock or more than 50% of total value of all stock in a corporation is considered to own the stock in such corporation owned, directly or indirectly, by or for his parents, grandparents, grandchildren, and adult children.	A	NA	NA	NA
2. Individual is considered to own stock owned, directly or indirectly, by or for his ancestors and his lineal descendants.	NA	A	NA	A
3. Individual is considered to own stock owned, directly or indirectly, by or for his children, grandchildren, and parents. "Children" includes legally adopted children.	NA	NA	A	NA
4. For purposes of Section 341(d) only, an individual is considered to own stock owned, directly or indirectly, by or for the spouses of that individual's lineal descendants.	NA	NA	NA	A
7. Attribution from brothers and sisters:				
a. Individual is considered to own stock owned, directly or indirectly, by or for his brothers and sisters (whether by the whole or half-blood).	NA	A	NA	A
b. For purposes of Section 341(d) only, an individual is considered to own stock owned, directly or indirectly, by or for the spouses of his brothers and sister (whether by the whole or half-blood).	NA	NA	NA	A
8. Attribution from partners:				
a. Individual who owns, actually or constructively, any stock in a corporation (except for constructive ownership through a member of his family), is considered to own the stock owned, directly or indirectly, by or for his partner.	NA	A	NA	A
9. Attribution to partnerships:				
a. Stock owned, directly or indirectly, by or for a partner, shall be considered as owned by the partnership.	NA	NA	A	NA
10. Attribution to estates:				
a. Stock owned, directly or indirectly, by or for a beneficiary of an estate shall be considered as owned by the estate.	NA	NA	A	NA
11. Attribution to trusts:				
a. Stock owned, directly or indirectly, by or for a beneficiary of a trust (other than a qualified employees' stock bonus, pension, or profit sharing trust) shall be considered as owned by the trust, unless such beneficiary's interest in the trust is a remote contingent interest.	NA	NA	A	NA

(Outline continued next page)

OUTLINE continued

A = Applicable NA = Not Applicable	SECTION 1563(e)	SECTION 267(c)	SECTION 318	SECTION 544(a)
b. Stock owned, directly or indirectly, by or for the grantor or other substantial owner of any portion of a trust, shall be considered as owned by the trust.	NA	NA	A	NA
12. Attribution to corporations:				
a. If 50% or more in value of the stock in a corporation is owned, directly or indirectly, by or for any person, such corporation shall be considered as owning the stock owned, directly or indirectly, by or for such person.	NA	NA	A	NA
13. Operating rules:				
(i) General rule—except as provided in subparagraph (B), stock constructively owned by a person under Sections 1563(e) (1), (2), (3), (4), (5), or (6) shall, for purposes of applying such sections, be treated as actually owned by such person.	A	NA	NA	NA
(ii) Members of family—stock constructively owned by an individual under Sections 1563(e)(5) or (6) shall not be treated as owned by him for purposes of again applying such sections in order to make another the constructive owner of such stock.	A	NA	NA	NA
(iii) Stock constructively owned by a person under Section 267(c)(1) shall, for purposes of applying Sections 267(c)(1), (2), or (3), be treated as actually owned by such person.	NA	A	NA	NA
(iv) Stock constructively owned by an individual under Sections 267(c)(2) or (3) shall not be treated as owned by him for the purpose of again applying either of such sections in order to make another the constructive owner of such stock.	NA	A	NA	NA
v) Except as provided in Section 318(a)(5)(B) and (C), stock constructively owned by a person under Sections 318(a)(1), (2), (3), or (4), shall, for purposes of applying Sections 318(a)(1), (2), (3), and (4), be considered as actually owned by such person.	NA	NA	A	NA
(vi) Stock constructively owned by an individual under Section 318(a)(1) shall not be considered as owned by him for purposes of again applying Section 318(a)(1) in order to make another the constructive owner.	NA	NA	A	NA
(vii) Stock constructively owned by a partnership, estate, trust, or corporation shall not be considered as owned by it in order to make another person the constructive owner.	NA	NA	A	NA
(viii) Stock constructively owned by a person under Sections 544(a)(1) or (3) shall, for purposes of applying Sections 544(a)(1) or (2), be considered as actually owned by such person.	NA	NA	NA	A
(ix) Stock constructively owned by an individual under Section 544(a)(2) shall not be considered as owned by him for purposes of again applying Section 544(a)(2) in order to make another the constructive owner.	NA	NA	NA	A
(x) If stock may be considered as constructively owned by a person because such person owns an option to acquire stock or to acquire an option, and such stock may also be considered as constructively owned by such person under another provision of this section of the Code, then such stock shall be considered as constructively owned by such person by reason of the option.	A	NA	A	A
(xi) Under Section 544(b), outstanding securities convertible into stock shall be considered as outstanding stock for some purposes under Sections 542(a) and 543(a).	NA	NA	NA	A

APPENDIX D*

BENEFITS AND BURDENS AFFECTING FOUNDATIONS
(REFERRED TO AS F)*Requirements as to establishment or maintenance of
exempt status and classification of Foundation*

1. F is required to file an exemption application with IRS (if organized after 10/9/69). §508(a).
2. F is required to amend basic documents to avoid penalty taxes (§4942-45). §508(e).
3. F is required to file notice to IRS that it is not a private foundation. §508(b).
4. F is subject to penalty tax on termination of private foundation. §507(a).
5. F is specifically authorized to receive assets of a terminating private foundation, thereby enabling private foundation to avoid tax on termination of its status. §507(b).

Attributes affecting classification of Foundations

6. F's payments are treated as "public support" (not from disqualified persons) to recipient organizations for purposes of §509(a)(2).
7. Control by F is permitted over organization qualifying as public foundation under §509(a)(3).
8. F qualifies as an organization that can provide support (up to 25 per cent) of a Private Operating Foundation. §4942(j)(3)(B)(iii).

Restrictions on activities and holdings of Foundations

9. F's managers [trustees, officers, etc. defined in §4946(b)] are subject to penalty tax for failure to meet restrictions under §§4941-4945, 6684.
10. F is subject to tax on self-dealing. §4941.
11. F is subject to tax on failure to distribute. §4942.
12. F qualifies as organization to which distributions can freely be made by a Private Foundation. §4942(g)(1).
13. F qualifies as organization to which distributions can be made under §4942(g) only if an equivalent is distributed within the following year. §4942(g)(3).
14. F is subject to tax on excess business holdings. §4943.

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APPLICATION TO CATEGORIES OF ORGANIZATIONS *

	<i>A</i>	<i>B</i>	<i>C</i>	<i>D</i>	<i>E</i>	<i>F</i>	<i>G</i>	<i>H</i>	<i>I</i>	<i>J</i>	<i>K</i>	<i>L</i>	<i>M</i>	<i>N</i>
1.	N ^a _b	Y ^a _b	Y ^a _b	Y ^a _b	Y ^b	Y ^b	Y ^b	Y ^b	^d	N	N ^c	N	Y	Y
2.	N	N	N	N	Y	Y	Y	Y	^d	N	^d	Y	Y	Y
3.	Y ^a _b	Y ^a _b	Y ^a _b	Y ^a _b	*	*	*	*	^d	*	^d	*	*	*
4.	N	N	N	N	Y	Y	Y	Y	^d	N	^d	Y	Y	Y
5.	Y	N	N	N	N	N	^d	N	^d	N	^d	N	N	N
6.	Y	N	N	N	N	N	N	N	^d	N	^d	*	N	N
7.	Y	Y	N	N	N	N	N	N	^d	N	^d	N	N	N
8.	Y	Y	Y	Y	Y ^c	Y ^c	Y ^c	N	^d	^d	^d	N	Y	Y
9.	N	N	N	N	Y	Y	Y	Y	^d	N	^d	ⁱ	Y	Y
10.	N	N	N	N	Y	Y	^d	Y	^d	N	^d	Y	Y	Y
11.	N	N	N	N	N	Y	^d	^d	^d	N	^d	N	Y	Y
12.	Y	Y	Y	Y	Y	N	N	N	^d	^d	^d	N	N	N
13.	*	*	*	*	*	Y	Y	Y	^d	^d	^d	N	Y	Y
14.	N	N	N	N	Y	Y	^d	Y	^d	N	^d	Y ^h	Y	N ^h

* The letters *A-N* represent the 14 categories of organizations. Numbers 1-14 represent 14 of the 34 Benefits and Burdens. "Y" means "yes"; "N" means "no"; * means "not applicable"; lower case letters denote specific provisions affecting particular types of foundations.