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The IRS as Tax Law Nonenforcer

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Lawrence Zelenak, *Custom and the Rule of Law in the Administration of the Income Tax*, 62 **Duke L.J.** 829 (2012).



Leigh Osofsky

In a recent essay, *Custom and the Rule of Law in the Administration of the Income Tax*, Larry Zelenak examines what he calls “customary deviations,” or “established practice[s] of the tax administrators . . . that deviat[e] from the clear dictates of the Internal Revenue Code.” Even though the IRS makes decisions every day about when not to enforce the tax law, tax scholarship does not typically examine this phenomenon systematically. By focusing on an aspect of IRS nonenforcement, Zelenak shines a much needed light on the topic. The essay, and the topic generally, should garner the attention of tax scholars, as well as scholars of enforcement discretion more generally.

Like other administrative agencies as well as prosecutors, the IRS has to make decisions all the time about when not to enforce the tax law. These decisions raise important questions about the legitimacy of different types of decisions not to enforce the tax law. For instance: Is it more or less legitimate for the IRS to decide not to enforce the law through a clear, customary deviation, or through a more opaque policy? If the IRS is somehow curtailed in its ability to use customary deviations, what alternatives might it use and would these be better or worse? By raising questions about customary deviations, Zelenak’s essay provides a jumping off point for a broader examination of tax law nonenforcement.

Zelenak’s story of customary deviations begins with the IRS’s nonenforcement of the tax law with respect to the personal use of frequent flier miles generated by an employer’s provision of travel. Zelenak explains that, despite the fact that the vast majority of commentators have assumed the statutory taxability of such miles, the IRS indicated that it “will not assert that any taxpayer has understated his federal tax liability by reason of the receipt or personal use of frequent flyer miles . . . attributable to the taxpayer’s business or official travel.” The implication of this example is broader than the example suggests. As Zelenak describes it, the IRS’s statement is a bald acknowledgement that it will not enforce the tax law, raising important questions about tax administration.

For Zelenak, customary deviations highlight an insoluble tension in tax administration. Customary deviations are often well-advised administrative responses to real enforcement difficulties and can help create more efficient administration of the tax system. And yet, Zelenak contends that such deviations threaten the rule of law. Zelenak makes the rule of law point most forcefully by arguing that the acceptance of customary deviations regarding frequent flier miles (and other customary deviations, such as exclusions for employee fringe benefits and deductions for Scientologists for “auditing” services) may have emboldened the IRS to provide customary deviations that he believes present a greater threat to the rule of law. The deviations that he believes present a

greater threat to the rule of law include the IRS's controversial declarations limiting the application of the loss-disallowance rules of section 382 of the Code in connection with bank acquisitions (at the time of bailout of the financial industry) and in connection with the Treasury Department's sale of General Motors shares to the public.

In all of these cases, Zelenak laments the difficulty in challenging customary deviations. He usefully explores how the pro-taxpayer nature of customary deviations and limitations on third-party taxpayer standing leave little room for outsiders to step in and prevent customary deviations from going too far. Zelenak leaves the reader with the sense that customary deviations can in some cases be desirable, in some cases problematic, but in all cases difficult to do anything about as a result of limitations on taxpayer standing and the real threat that allowing standing to challenge the deviations may pose to the administrability of the tax system. Zelenak's most concrete proposal is for "Congress to enact a new Code provision specifically authorizing the Treasury Department to issue regulations narrowing the statutory definition of gross income with respect to non-cash benefits received outside of an employment context, whenever the IRS decides that administrative concerns make such a narrowing advisable," and that "Congress might decide to give the Treasury Department similar authority to revise by regulation other specified Code sections" Zelenak leaves aside a full exploration of potential problems with this proposal. Rather, his contribution is to expose the conundrum of customary deviations, which form a subset of the broader set of strategies that the IRS uses to manage an enforcement mandate that exceeds its capacity. His essay thus points to the broader problem of the IRS's inevitable enforcement discretion and what, if anything, should be done about it.

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