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PRE-ENFORCEMENT LITIGATION NEEDED FOR TAXING PROCEDURES

Stephanie Hunter McMahon*

Abstract: Courts have opened tax guidance to procedural attack. Consequently, taxpayers who are found to owe tax may challenge the validity of the guidance implementing the tax if the procedure used by the Treasury Department in adopting the guidance failed to comply with the Administrative Procedure Act, in particular, with notice-and-comment. This increased willingness to consider tax guidance's procedural defects offers little to most taxpayers unless they are also given a better means to raise procedural challenges. Under current law and in most circumstances, generally, taxpayers can bring a challenge only after they have been found to owe taxes in an audit and completed an internal IRS appeal process. This delay in the ability to challenge guidance reduces the likelihood taxpayers will challenge the procedure used to create a particular rule. Moreover, delayed litigation requires taxpayers to plan their affairs under the umbrella of guidance that might not survive a procedural challenge. To the extent procedural challenges are accepted in the tax context, this Article argues Congress should narrowly repeal its prior limitations on pre-enforcement litigation of those procedures. Everyone affected by the guidance should be permitted to litigate procedural questions for a period of time post-promulgation without the necessity of being found to owe taxes. This narrow exception would increase the certainty of tax guidance and encourage greater public participation in the guidance-formation process in a way that is sensitive to the fact that litigation imposes costs on the Treasury Department.

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INTRODUCTION

Politicians demand a more fair, more efficient, and simpler tax system as the press rails against problems plaguing the tax system's administration.¹ However, improving the tax system and making substantive change to tax administration, whether or not considered independently of the substance of the tax law, is not easy. Protecting taxpayer rights while raising the revenue necessary to fund our government is a complicated balancing act. That balancing requires compromise resulting from a sensitivity to the push and pull between taxpayers' rights (and some taxpayers' desire not to pay taxes) and the system's administration (and the need for revenue).

Balancing these competing interests in the complicated world of taxation is hard. It is made more difficult by the fact that tax is an area of law recognized as unique and yet bound by general systems of law. Historically, a silo evolved around taxation that allowed the tax system to develop its own answers to procedural questions; that silo is now being challenged. Those challenges often do not fully consider the unintended consequences that arise when tax administration is forced into ill-fitting procedures that work imperfectly for other government agencies and were certainly not created with the tax system in mind.²

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1. See Naomi Jagoda, *House Committee Votes to Censure IRS Head*, HILL (June 15, 2016), <http://thehill.com/policy/finance/283576-house-committee-votes-to-censure-irs-head> [<https://perma.cc/WK4W-BGPW>]; *National Taxpayer Advocate Identifies Priority Areas and Challenges in Mid-Year Report to Congress*, IRS (July 16, 2014), <https://www.irs.gov/uac/newsroom/national-taxpayer-advocate-identifies-priority-areas-and-challenges-in-mid-year-report-to-congress> [<https://perma.cc/Z7NP-UG3G>]; Jose Pagliery, *IRS Taxpayer Data Theft Seven Times Larger than Originally Thought*, CNN (Feb. 26, 2016), <http://money.cnn.com/2016/02/26/technology/irs-data-theft/index.html> [<https://perma.cc/5Q6E-FH9P>]; Hillary Clinton, *A Fair Tax System*, HILLARY CLINTON (Jan. 11, 2016), <https://www.hillaryclinton.com/issues/a-fair-tax-system/> [<https://perma.cc/6EYH-B6K2>] (“[r]estore basic fairness to our tax code” and “[s]implify and cut taxes for small businesses”); Donald Trump, *Tax Reform that Will Make America Great Again*, <https://www.donaldjtrump.com/positions/tax-reform> [<https://perma.cc/Y6NV-74AR>] (calling for “simpler, fairer brackets” that will “spur economic growth”). The TaxProf Blog was on Day 1563 of “The IRS Scandal” as of Aug. 19, 2017. Paul L. Caron, TAXPROF BLOG, http://taxprof.typepad.com/taxprof_blog/irs-scandal/ [<https://perma.cc/248D-S3Q3>].

2. See Bryan Camp, *A History of Tax Regulation Prior to the Administrative Procedure Act*, 63 DUKE L.J. 1673, 1682 (2014); Richard Murphy, *Pragmatic Administrative Law and Tax Exceptionalism*, 64 DUKE L.J. ONLINE 21, 21 (2014); Richard J. Pierce, Jr., *Which Institution Should Determine Whether an Agency's Explanation of a Tax Decision Is Adequate?: A Response to Steve Johnson*, 64 DUKE L.J. ONLINE 1, 12 (2014); Lawrence Zelenak, *Maybe Just a Little Bit*

This tension plays out in cases that would shoehorn tax guidance into the mold created by the Administrative Procedure Act (APA).³ The APA “afford[s] parties affected by administrative powers a means of knowing what their rights are and how they may be protected.”⁴ Unless specifically carved out, all agencies that create informal guidance, as opposed to formal rulemaking, are required to follow a procedure laid out in the APA popularly referred to as notice-and-comment.⁵ An agency is required to provide the affected public with notice of proposed rules and consider the public’s comments after a reasonable comment period.

The Treasury Department often summarily relies on statutory exceptions from the requirement for notice-and-comment when it issues tax guidance.⁶ Since 2011, when the Supreme Court warned in *Mayo Foundation for Medical Education & Research v. United States*⁷ that the Internal Revenue Service (IRS) will not be granted special exemption from administrative law, this reliance has come under attack.⁸ This is part of a wave of attacks against Treasury Department procedures that

Special, After All?, 63 DUKE L.J. 1897, 1901 (2014). See generally Stephanie Hunter McMahon, *The Perfect Process Is the Enemy of the Good Tax: Tax’s Exceptional Regulatory Process*, 35 VA. TAX REV. 553 (2016); James Puckett, *Structural Tax Exceptionalism*, 49 GA. L. REV. 1067 (2015).

3. Administrative Procedure Act of 1946, Pub. L. No. 70-404, 60 Stat. 237. For cases on the matter handed down in the last ten years, see *Mayo Found. for Med. Educ. & Research v. United States*, 562 U.S. 46 (2011); *Intermountain Ins. Serv. v. Comm’r*, 134 T.C. 211 (2010); *Stobie Creek Inv. LLC v. United States*, 83 Fed. Cl. 636, 668 (2008); *Lewis v. Comm’r*, 128 T.C. 48, 53–54 (2007); Complaint, Chamber of Commerce v. I.R.S., No. 1:16-cv-944 (W.D. Tex. Aug. 4, 2016).

4. S. REP. NO. 79-752, at 193 (1945); see also H.R. REP. NO. 79-1980 (1946).

5. 5 U.S.C. § 553 (2012).

6. More than forty percent of the 232 regulations published between January 1, 2003 and December 31, 2005 are susceptible to APA challenge for failure to comply with the notice and comment. Kristin E. Hickman, *Coloring Outside the Lines*, 82 NOTRE DAME L. REV. 1727, 1740–59 (2007).

7. 562 U.S. 44 (2011).

8. See *id.*; Ellen P. Aprill, *The Impact of Agency Procedures and Judicial Review on Tax Reform*, 65 NAT’L TAX J. 917 (2012); Kristin E. Hickman, *A Problem of Remedy*, 76 GEO. WASH. L. REV. 1153, 1778–86 (2008); Michael Livingston, *Reinventing Tax Scholarship*, 83 CORNELL L. REV. 365, 384–84, 387 (1998); Toni Robinson, *Retroactivity: The Case for Better Regulation of Federal Tax Regulators*, 48 OHIO ST. L.J. 773, 775 (1987). See generally Kristin E. Hickman, *Agency-Specific Precedents*, 89 TEX. L. REV. 89 (2010); Kristin E. Hickman, *The Need for Mead: Rejecting Tax Exceptionalism in Judicial Deference*, 90 MINN. L. REV. 1537 (2006); Kristin E. Hickman, *Unpacking the Force of Law*, 66 VAND. L. REV. 465 (2013); Steven R. Johnson, *Preserving Fairness in Tax Administration in the May Era*, 32 VA. TAX REV. 269 (2012); Leandra Lederman, *The Fight Over “Fighting Regs” and Judicial Deference in Tax Litigation*, 92 B.U. L. REV. 643 (2012); Shannon Weeks McCormack, *Tax Abuse According to Whom?*, 15 FLA. TAX REV. 1 (2013); Kristin E. Hickman, *Goodbye Tax Exceptionalism*, 12 ENGAGE 1 (2011), <http://www.fed-soc.org/publications/detail/goodbye-tax-exceptionalism> [<https://perma.cc/M4Q4-DHNX>].

are argued not to comply with the APA. As a result, what APA compliance looks like in the tax context has been a hot topic. Despite a need for clarity of the law, courts have yet to establish a coherent jurisprudence on this issue.⁹

In other areas of law, agencies often litigate the application of the APA to their guidance before the guidance is enforced against the public.¹⁰ Pre-enforcement litigation can isolate procedural issues and allow the public thereafter to focus on the substance of the rules as it applies to their facts. This process is not currently available in the tax context because of statutory and prudential prohibitions on pre-enforcement litigation on either substantive or procedural grounds.¹¹ Most challenges to tax guidance and the collection of tax are deferred until after a taxpayer is audited, is found to owe tax, and completes the agency's appeals process. These tax specific and general prudential doctrines minimize the number and type of attacks the Treasury Department faces even when the APA would otherwise permit the challenge.

Only those taxpayers who are found to be in violation of the tax guidance and who do not settle with the IRS have any ability to initiate a judicial challenge of the guidance's procedural history. In most instances, this potential tax litigation results from either refund or deficiency suits. Refund litigation occurs when a taxpayer has paid taxes or penalties and seeks to recover these payments.¹² Deficiency litigation challenges an IRS audit that determines taxes are owed but are not yet paid.¹³ With a three-year statute of limitations for assessing liability, this litigation may take place years after the tax return was filed.¹⁴ Moreover, only those who pursue litigation after this period of delay can initiate procedural challenges—a small subset of all taxpayers. What most

9. See generally *Balestra v. United States*, 803 F.3d 1363 (Fed. Cir. 2015) (discussed in Part II); *Altera Corp. v. Comm'r*, 145 T.C. 3 (2015).

10. See *Balestra*, 803 F.3d 1363; discussion *infra* Part II.

11. Judges could broaden the narrow exceptions so that some cases could be heard early. Hickman suggests revising judicial interpretation of the Anti-Injunction Act and Declaratory Judgment Act “to allow some greater amount of . . . judicial review of facial challenges to Treasury regulations seems likely to resolve the problems . . .”; however, she recognizes that “a legislative solution may be necessary” if that is insufficient. Hickman, *A Problem of Remedy*, *supra* note 8, at 1201–02. However, even after doing so the bulk of tax guidance would remain insulated from pre-enforcement judicial review. Moreover, the exceptions might increase taxpayer frustration and confusion over when they can and cannot secure judicial review.

12. See I.R.C. § 7422(a) (2012).

13. See *id.* §§ 6211(a), 6213(a), 6512(b).

14. *Id.* § 6501(a). The statute of limitations is extended to six years for substantial omission and indefinitely if a return is filed fraudulently or no return is filed. *Id.* § 6501(c), (e).

taxpayers may gain in that litigation is unlikely to offset the expense of the litigation itself.

While Congress only permits procedural challenges late in the tax collection process, this offers little to most taxpayers. The delay in litigating procedural complaints reduces what is challenged and affects taxpayer behavior throughout the period from its promulgation until someone, eventually, challenges the procedures. In the process, delayed litigation requires that taxpayers plan their affairs under the spectre of guidance that might not survive a procedural challenge. Moreover, in deciding whether to follow the tax guidance, taxpayers must not only assess its substance but also the procedures used to create it under procedural requirements that are not consistently interpreted by the courts. It is for these reasons this Article proposes two narrow statutory changes to permit pre-enforcement review of the procedures used to create tax guidance.

Thus, this Article accepts the reality that courts will permit certain procedural challenges to tax guidance, and with that acceptance argues that a new method for hearing those challenges needs to be developed. The right to procedural litigation should mean something. Instead of waiting until after enforcement of the guidance, this Article proposes that procedural challenges should be heard early, to the extent constitutionally permissible. Thereafter, taxpayers may undertake their tax compliance understanding what the law is. However, permitting this early litigation is likely to increase the amount of litigation and its cost.¹⁵ This cost requires constraining early and meaningful review so that it does not consume all of the agency's resources.

Unless the system balances permissive litigation with an awareness of limited agency resources, taxpayers have an incentive to overwhelm the agency in litigation. Today, as courts and academics struggle to determine exactly how application of the APA and notice-and-comment will change the process for challenging tax guidance, this litigation has been recognized as a means to change some tax outcomes. One Am-Law 100 law firm claims procedural challenges create “a unique opportunity” to challenge the IRS and Treasury Department.¹⁶ That these procedural

15. See Jerry L. Mashaw, *Improving the Environment of Agency Rulemaking*, 57 LAW & CONTEMP. PROBLEMS 185, 233–38 (1994).

16. Sena Akins & GERAL KAFKA, Latham & Watkins LLP, *A New Argument for Contesting IRS Audit Determinations*, 65 Tax Executive 171, 179 (2013); see also Roger Jones et al., *How to Challenge Tax Regs on Administrative Law Grounds*, LAW 360 (Oct. 16, 2015), <http://www.law360.com/articles/715380/how-to-challenge-tax-regs-on-administrative-law-grounds> [<https://perma.cc/L4QS-8DDF>]; J. Walker Johnson & Alexis A. MacIvor, *Tax Controversy Alert*, STEPTOE & JOHNSON LLP, <http://www.steptoel.com/assets/attachments/4472.pdf> [<https://perma.cc/J39D-98WS>].

challenges to the validity of tax guidance generally occur in the post-audit context risks breeding contempt for the tax system more than fixing procedural problems.¹⁷ Additionally, the structure of the litigation means that important procedural issues can never be brought in court. Therefore, some procedural problems will continue unless Congress steps in to protect taxpayer rights.

This Article proposes legislative changes to address some of the problems created by post-audit procedural challenges; however, it is important to know what this Article does not argue. It is beyond the scope of this Article to debate the value of applying notice-and-comment in the creation of tax guidance. There are good reasons to facilitate the publication of guidance and to limit judicial review of agency procedures, both generally and specifically in the tax context.¹⁸ The IRS's budget has been reduced by twelve percent over the last ten years when adjusted for inflation, and with the IRS's shrinking budget, there is only so much that can be accomplished by an underfunded agency.¹⁹ Increasing the amount of tax litigation for a greater number of procedural claims could have several unintended consequences, including impeding other agency activities that might be as important, if not more so, for the protection of taxpayers' rights and reducing government revenue. In a world of finite resources, it should not be assumed that increasing an agency's administrative burdens is in taxpayers' best interest.

Additionally, with the evolution of procedural litigation, it is possible that APA procedures will be required of all IRS and Tax Court activities; however, this Article limits itself to the creation of tax guidance.²⁰ The focus on guidance is because of the importance of this issue in litigation today and because this study can serve as a model for how a narrow procedural fix can address concerns without opening the floodgates to litigation. In doing so, this Article urges temperance, rather than broad sweeping changes of unknown consequence, to the administration of the

Academics are telling the bar to do so. See Steve Johnson, *Using Administrative Law to Challenge IRS Determinations*, 88 FLA. B.J. 81 (2014).

17. See *infra* Part I.

18. See *infra* note 59.

19. Jeremy H. Temkin, *Internal Revenue Service Budget Cuts Spell Trouble*, 253 N.Y. L.J. (Jan. 22, 2015).

20. For example, recent cases have questioned whether the IRS must comply with the APA when issuing determination letters assessing taxpayers' liability or in IRS programs operated to increase compliance with foreign-held assets. See *Maze v. IRS*, 206 F. Supp. 3d 1 (2016); Reply Brief for Appellant, *Qinetiq U.S. Holdings, Inc. v. Comm'r*, 845 F.3d 555 (4th Cir. 2016) (No. 15-2192), 2016 WL 1464112.

nation's revenue raising regime. The most persuasive form of tax guidance is regulations, but there is also lesser guidance, such as revenue rulings and private letter rulings, that assist taxpayers in complying with the tax law. In this Article, the broader term, "tax guidance," is used to encompass all types of agency-created rules governing tax matters.

This Article proceeds in four parts. Part I briefly describes the APA's procedures for agencies to create rules. The notice-and-comment rules are often considered onerous and do not perfectly accomplish their objectives. There are exceptions to these procedures, but courts interpret the exceptions narrowly.²¹ Part I also describes how tax guidance is created in comparison to the APA procedures.

Part II then examines when the APA permits pre-enforcement litigation of procedural issues and how a general presumption in favor of pre-enforcement litigation does not extend to the tax context.²² Congress enacted specific statutory limitations that prevent taxpayers from challenging most tax laws and tax guidance before enforcement. Additionally, prudential rules limit the ability to bring lawsuits against the government more generally. These limits effectively overturn the APA's default of early litigation over the procedures the APA requires and reduce the likelihood of pre-enforcement procedural challenges to tax guidance.

In Part III, the Article examines how, under current law, some procedural matters are never litigated. First, no one is in a position to challenge rules that favor small groups of taxpayers. Only those benefited have standing to sue and they have little incentive to challenge their own benefit, if this is even possible. Additionally, notices that promise future regulations are likely not final rules for APA challenge or ripe for litigation.²³ Unfortunately, there is a cost of these timing and scope of litigation limitations. Taxpayer rights and the law's consistency are both jeopardized through delayed or limited litigation of procedural violations.

Recognizing the importance of maintaining a workable tax system, Part IV proposes two narrow statutory changes to address these concerns about procedure. First, this Article proposes a statutory change to permit narrow procedural challenges to the validity of tax guidance before enforcement of the guidance is undertaken. The proposal permits

21. *See infra* Part I.

22. *See also* Hickman, *A Problem of Remedy*, *supra* note 8 (focusing on why people do not make APA claims in tax matters).

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

litigation over substantive issues only to the extent necessary to clarify that the regulations are consistent with the statutory language. To ensure the Treasury Department and IRS are not inundated with procedural claims and that rules are finalized, a limited time period should be established to constrain when this type of procedural litigation can occur, as currently required by some other agencies' rules.

This permissive approach to pre-enforcement litigation would settle procedural issues and permit the law to proceed subject only to substantive challenge. Although this would prevent some taxpayers from making procedural challenges after learning too late of the application of the guidance to their own circumstances, this proposal balances concerns over taxpayer rights to challenge procedure with the need for settled guidance to shape taxpayer activity. In the process, it should also encourage more public attention to the guidance-making process.

The second proposal expands the group that can engage in these legal challenges. To increase procedural review of favorable tax guidance, Congress should provide standing for those who do not benefit from tax expenditures by permitting "all persons" to sue over procedural claims. Moreover, Congress should acknowledge the injury that tax expenditures have on federal revenue and subsequently on the provision of national services. Because of the far-reaching consequences of narrowly tailored tax preferences beyond the immediate taxpayer, the procedures used for creating the guidance must be democratic. Failure to follow democratic procedures envisioned by the APA should be open to public challenge.

The success of this second proposal depends upon the judicial response. Courts may not accept that this latter proposal proves that a case or controversy exists if they do not accept there is a real injury for those not benefited by tax preferences. If courts do not accept this congressional interpretation of the injury, neither those not benefited nor those who are benefited have an injury. Therefore, those opposing the procedure used to create the rule would only have recourse to Congress. Appeals to Congress, however, would likely address the substance of the rule and ignore procedural concerns.

The Article concludes that changing the law in these limited ways has many benefits despite having some drawbacks. If Congress adopts these two changes, the public could litigate procedural questions without the necessity of being found to owe tax. This would validate the importance of procedural issues and encourage greater compliance with the APA by the Treasury Department. A limited window for those procedural complaints would encourage public participation in the creation of tax guidance when the ability to litigate remains open. Having early

litigation would then allow tax guidance to apply to taxpayers who may focus only on its substance. However, this proposal also means the IRS is likely to face a wave of new litigation and need to devote more of its dwindling resources to litigation. Despite this downside, in a world where procedural attacks will occur, litigating early maximizes benefits to both taxpayers and the government.

I. PROCEDURAL CLAIMS AGAINST TAX GUIDANCE UNDER THE APA

An agency does not have the discretion to develop rules using any method it chooses. Instead, Congress prescribes the procedures for creating rules in the APA, unless Congress expressly grants an agency an exception from the generally applicable requirements. These procedures were enacted in 1946, and since that time the rules have grown through judicial interpretation. Nevertheless, ambiguities remain and agencies must interpret the procedures for themselves as they craft their rules. These interpretations are then subject to review by courts.

The Treasury Department is an agency subject to the APA unless an exception applies. Therefore, general APA procedures are the backdrop against which Treasury Department procedures are to be measured. Although the Treasury Department says it complies with the APA, the degree to which it does so has been debated.

A. *The APA's Rules as a Backdrop for Tax Guidance*

The APA “afford[s] parties affected by administrative powers a means of knowing what their rights are and how they may be protected.”²⁴ To that end, when agencies forego formal hearings to create rules, section 553 of the APA requires federal agencies to provide the public with notice of a proposed rule as well as an opportunity to comment on the proposal.²⁵ The agency is then required to consider the public’s comments after a reasonable comment period before publishing the rule as final.²⁶ Unless specifically carved out, all agencies that create guidance, including tax agencies, are required to follow this procedure,

24. S. REP. NO. 79-752, at 193 (1945); *see also* H.R. REP. NO. 79-1980, at 250 (1946).

25. 5 U.S.C. § 553 (2012). For purposes of notice and comment procedures, a rule is defined broadly to encompass virtually any agency statement about what regulated parties must or should do. *Id.* § 551(4).

26. The resulting rule must be published at least thirty days before it takes effect unless there is good cause for a sooner effective date. *Id.* § 553(d).

popularly referred to as notice-and-comment. This process has many components that may be burdensome for agencies to satisfy.

The primary purpose of notice-and-comment procedures is to ensure the public has a voice in the creation of the rules. Exception from these procedures are limited in order to maintain a robust dialogue between agencies and the public, but exceptions do exist to ensure other public interests are not sacrificed in the quest for public participation. Many contemporary attacks on the Treasury Department's process for issuing tax guidance, regulations in particular, claim that the Department's process fails to comply with the APA's notice-and-comment requirements and does not fall within an exception.²⁷

The requirements of notice-and-comment are extensive. For example, notice is more than alerting the public to a proposed rule; it has many nuanced requirements. Notice must "fairly apprise interested parties of the issues involved in the proposed rule, so that [the public] may present responsive data or argument,"²⁸ and the "required specification of legal authority must be done with particularity."²⁹ Courts treat this notice requirement seriously, invalidating rules that fail to provide sufficient factual details and rationales to permit the public a "fair chance" to comment meaningfully.³⁰ Therefore, the Notice of Proposed Rulemaking (NPRM), typically published in the *Federal Register*, must include the terms or substance of the proposed rule or a description of the subjects and issues involved.³¹ An agency adding critical material to the record after the comment period risks judicial invalidation of the rule because the public did not have time to respond to that new material.³²

Notice opens the agency's doors for any and all to submit comments with any information they choose to share. There is no requirement that the commentator be a party in a more litigious sense. And while the APA does not establish a window for the submission of comments, a

27. See *supra* note 3.

28. S. REP. NO. 79-752, at 200.

29. H.R. REP. NO. 79-1980, at 258.

30. See, e.g., *Global Van Lines, Inc. v. Interstate Commerce Comm'n*, 714 F.2d 1290, 1298 (5th Cir. 1983) (the Interstate Commerce Commission's failure to articulate the legal basis for a rule "effectively deprived the petitioners of [the] opportunity to present comments").

31. 5 U.S.C. § 553(b) (2012); see also *Warshauer v. Solis*, 577 F.3d 1330 (11th Cir. 2009); *Chamber of Commerce v. SEC*, 443 F.3d 890, 906 (D.C. Cir. 2006); *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375 (D.C. Cir. 1973); *Penobscot Indian Nation v. U.S. Dep't. of Housing & Urban Dev.*, 539 F. Supp. 2d 40, 50 (D.D.C. 2008).

32. See *ConocoPhillips Co. v. EPA*, 612 F.3d 822, 833 (5th Cir. 2010); *Idaho Farm Bureau Fed'n v. Babbitt*, 58 F.3d 1392, 1402-04 (9th Cir. 1995).

reasonable amount of time must be provided.³³ Agencies typically allow sixty days for comments.³⁴

Following the comment period, the agency must consider “the relevant matter presented” in the comments.³⁵ The extent to which this exchange between the agency and the public becomes a dialogue is debated. For example, in *Prometheus Radio Project v. Federal Communications Commission*,³⁶ the majority treated the agency and commentators as opposing litigants so that process itself was emphasized to assure fairness to the commentators.³⁷ The dissent argued that the decision-making process should be reviewed in its entirety, in order to permit a long chain of public involvement to be evidence of compliance with the APA.³⁸ This debate over procedural versus substantive participation permeates discussion of the value to be given to each section of the APA.

The fundamental meaning of notice-and-comment is critical because an agency cannot substantially change a rule in response to comments without starting the notice-and-comment process over again. Only those changes that are a “logical outgrowth” of the proposed rule may be made without restarting the process for fear that the public did not have adequate notice or the opportunity to comment on the revised language.³⁹ If, and only if, the public “should have anticipated” the change is it unnecessary to restart notice-and-comment.⁴⁰ Any change that “materially alters the issues involved in the rulemaking” or substantially departs from the proposed language requires re-notice.⁴¹ An agency that fails to provide new notice-and-comment risks a court invalidating the rule based on procedural faults.

Two cases illustrate some of the difficulties of the logical outgrowth test. In *South Terminal Corp. v. Environmental Protection Agency*,⁴² the agency modified a proposed rule that reduced pollution from motor

33. See *Fla. Power & Light Co. v. United States*, 846 F.2d 765, 772 (D.C. Cir. 1988).

34. See JEFFREY S. LUBBERS, A GUIDE TO FEDERAL AGENCY RULEMAKING 251–52, 272–74 (5th ed. 2012). Agencies may accept late comments at their discretion. *Id.* at 252.

35. 5 U.S.C. § 553(c) (2012).

36. 652 F.3d 431 (3d Cir. 2011).

37. *Id.* at 445–47.

38. *Id.* at 473 (Scirica, J., dissenting).

39. See *Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 160 (2007); *Nat. Res. Def. Council Inc. v. EPA*, 279 F.3d 1180, 1186 (9th Cir. 2002).

40. See *Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 549 (D.C. Cir. 2006).

41. See *Chocolate Mfrs. Ass’n v. Block*, 755 F.2d 1098, 1105 (4th Cir. 1985).

42. 504 F.2d 646 (1st Cir. 1974).

vehicles by adopting specific measures, such as parking surcharges and travel restrictions.⁴³ The final rule eliminated the proposed measures and, instead, imposed other measures, such as reducing parking availability and increasing automobile inspections.⁴⁴ The First Circuit held the new measures were a logical outgrowth of the proposal because they were “in character with the original scheme” and the agency had announced in the notice that it would consider “all reasonable alternatives.”⁴⁵

On the other hand, in *Chocolate Manufacturers Ass’n v. Block*,⁴⁶ the Department of Agriculture responded to a congressional amendment to the federal food program that required supplemental foods for women, infants, and children to have nutritional value.⁴⁷ The Department proposed maintaining the substitution of flavored milk for whole milk but invited the public “to make recommendations for alternatives not considered in the proposed regulations.”⁴⁸ The final regulation prohibited the substitution, and the Fourth Circuit held that in “the specific circumstances of this case” the revision was not a logical outgrowth because the Department had previously permitted the substitution and had not suggested deleting flavored milk.⁴⁹ Therefore, in order to delete flavored milk, the agency was required to re-initiate the process, alerting the public to the proposed deletion.

The risk of invalidation for failing to restart the notice-and-comment process leads to some degree of intellectual lock-in with proposed language. Practical considerations of the cost and timing of redoing notice-and-comment are in addition to people’s natural propensity not to change their minds, described in depth in the bounded rationality scholarship.⁵⁰ This result caused Stephanie Stern to conclude that notice-and-comment actually reduces the value of public participation by prematurely committing agencies to proposed rules.⁵¹

43. *Id.* at 656–57.

44. *Id.* at 657–58.

45. *Id.* at 658–59.

46. 755 F.2d 1098 (4th Cir. 1985).

47. *Id.* at 1100.

48. *Id.* at 1101.

49. *Id.* at 1107.

50. See BOUNDED RATIONALITY (Gerd Gigerenzer & Reinhard Selten eds., 2002); MANCUR OLSON, JR., THE LOGIC OF COLLECTIVE ACTION 124 (1965); Herbert A. Simon, *Bounded Rationality and Organizational Learning*, 2 ORG. SCI. 125 (1991).

51. Stephanie Stern, *Cognitive Consistency*, 63 U. PITT. L. REV. 589, 620–30 (2002); see also Brian Galle & Mark Seidenfeld, *Administrative Law’s Federalism*, 57 DUKE L.J. 1933, 1954–61 (2008).

As a final step of notice-and-comment, the statute requires that final rules be submitted to the *Federal Register* with a concise general statement of its basis and purpose.⁵² Courts, however, have effectively eliminated “concise” from this APA requirement.⁵³ In *Citizens to Preserve Overton Park, Inc. v. Volpe*,⁵⁴ the Supreme Court urged lower courts to engage in a “searching and careful” review of agency actions.⁵⁵ To facilitate that review, agencies must provide courts with a contemporaneous administrative record of their decision-making in their statements accompanying final rules.⁵⁶ In later litigation over the procedure behind a rule, only those statements supplied with the final rule are reviewable in support of the agency.⁵⁷ Consequently, agencies can use their own expertise to supplement the comments in their rulemaking, but that expertise must become part of the administrative record in a way accessible to the courts.⁵⁸

This exchange between the public and the agency is to encourage public participation in the rulemaking process. Subjecting proposed regulations to public scrutiny is expected to foster rational and informed rulemaking.⁵⁹ However, the notice-and-comment procedures the APA imposes, which critics want to be applied more rigorously in the formation of tax guidance, do not always accomplish these goals and may inadvertently make it harder for agencies to move closer to the ideal by increasing the cost of issuing guidance.

Some scholars argue these procedures have become onerous to agencies and reduce the amount of rules and guidance that are produced.⁶⁰ Moreover, the level of review that is required for an agency rule to be upheld is not predictable; Jerry Mashaw argues that courts

52. 5 U.S.C. § 553(c) (2012).

53. *See* *Auto. Parts & Accessories Ass’n v. Boyd*, 407 F.2d 330, 338 (D.C. Cir. 1968).

54. *Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402 (1971).

55. *Id.* at 416.

56. *Id.* at 420.

57. *See* *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto Ins.*, 463 U.S. 29 (1983).

58. *See* *Balt. Gas & Elec. Co. v. Nat. Res. Def. Council, Inc.*, 462 U.S. 87, 103–04 (1983); *Nat’l Wildlife Fed’n v. Nat’l Marine Fisheries Serv.*, 422 F.3d 782, 798–99 (9th Cir. 2005).

59. *See* *Weyerhaeuser Co. v. Costle*, 590 F.2d 1011, 1028–31 (D.C. Cir. 1978); *Int’l Harvester Co. v. Ruckelshaus*, 478 F.2d 615, 648 (D.C. Cir. 1973).

60. *See* Richard J. Pierce, Jr., *Rulemaking Ossification Is Real*, 80 GEO. WASH. L. REV. 1493 (2012) (responding to Yackee & Yackee, *infra*); Edward Rubin, *It’s Time to Make the Administrative Procedure Act More Administrative*, 89 CORNELL L. REV. 95 (2003); Jason Webb Yackee & Susan Webb Yackee, *Testing the Ossification Thesis: An Empirical Examination of Federal Regulatory Volume and Speed, 1950–1990*, 80 GEO. WASH. L. REV. 1414 (2012) (testing rulemaking at the Department of the Interior).

function as “robed roulette wheels” when reviewing agency guidance.⁶¹ As a result, the notice-and-comment procedure is costly in terms of both time and agency resources, while the procedure does not guarantee the public good.

Recognizing a downside of notice-and-comment, even the APA does not claim notice-and-comment must be applied in all circumstances. Because notice-and-comment procedures are not always in the public’s best interest, the APA’s exceptions ensure other public interests are not sacrificed in the quest for public participation. Some exceptions are specific subject matter exceptions for national priority circumstances—military or foreign affairs—or for internal agency or government business—agency management, personnel, or public property, loans, grants, benefits, or contracts.⁶² These do not apply in the tax context discussed in this Article.

More broadly, there is an exception for interpretive or procedural rules and general statements of public policy.⁶³ These excepted rules do not have the force and effect of law, or alternatively, do not govern substantive rights.⁶⁴ Instead, they offer guidance as to the agency’s interpretation of the law. In this way, interpretive guidance is the agency’s view of the law but not the agency’s creation of law. The existence of interpretive rules raises questions of the appropriate level of deference courts should give this type of guidance. Agencies’ authority even to issue interpretive regulations is questioned, in part, because distinguishing between interpretive and legislative rules is difficult for agencies and even courts to do.

Finally, the APA recognizes an exception from notice-and-comment when agencies have good cause to do so.⁶⁵ Unlike interpretive rules, rules created under the good cause exception have full force and effect of law. Although not widely applied by courts, the good cause exception

61. JERRY L. MASHAW, GREED, CHAOS, AND GOVERNANCE 181 (1997); Wendy E. Wagner, *Administrative Law, Filter Failure, and Information Capture*, 59 DUKE L. J. 1321, 1360 (2010).

62. 5 U.S.C. § 553(a) (2012).

63. *Id.* § 553(b)(A).

64. *See* United States v. Mead Corp., 533 U.S. 218, 231–32 (2001); Christensen v. Harris County, 529 U.S. 576 (2000); Reno v. Koray, 515 U.S. 50, 61–62 (1995); EEOC v. Arabian Am. Oil Co., 449 U.S. 244, 256–58 (1991); LUBBERS, *supra* note 34, at 64–77; Antonin Scalia, *Judicial Deference to Administrative Interpretations of Law*, 1989 DUKE L.J. 511, 516–17.

65. 5 U.S.C. § 553(b)(B) (2012). There is a separate good cause exception to the standard thirty-day waiting period following their publication before regulations become effective. *Id.* § 553(d); *see also* Riverbend Farms Inc. v. Madigan, 958 F.2d 1479, 1485 (9th Cir. 1992) (analyzing differences between the good cause exception to the thirty-day waiting requirement and the good cause exception to notice and comment).

is authorized when compliance with the notice-and-comment procedure is “impracticable, unnecessary, or contrary to the public interest.”⁶⁶ Therefore, regulations promulgated within this narrow exception avoid notice-and-comment but have a similar effect as guidance that has gone through notice-and-comment. This exception can be, at least at times, a large “legal grey hole” through which agencies avoid judicial review of agencies’ procedure in making law.⁶⁷

B. *Tax Guidance’s Potential Violations*

The Treasury Department and the IRS, as a bureau within the Treasury Department, issue significant amounts of guidance that qualify as rules subject to the APA. Congress granted the Secretary of the Treasury Department, and subsequently the Secretary’s designees, the authority to “prescribe all needful rules and regulations for the enforcement” of the Code.⁶⁸ Although most tax regulations proceed through the notice-and-comment process, few adhere to a strict form of notice-and-comment before their issuance. Currently, the Treasury Department often summarily relies on the interpretive or good cause exceptions for the issuance of tax guidance and sometimes issues legally binding temporary regulations simultaneously with proposed regulations, which then proceed through notice-and-comment.⁶⁹ These procedures have come under legal and academic attack for failing to comply with proper procedure.

One critique is over the Treasury Department’s policy of often simultaneously issuing proposed and temporary regulations, resulting in a delayed comment period until after publication of guidance that is binding.⁷⁰ The Treasury Department issues proposed regulations that have completed internal review but still await public review at the same time it issues temporary regulations.⁷¹ These temporary regulations have

66. 5 U.S.C. § 553(b)(B) (2012).

67. Adrian Vermeule, *Our Schmittian Administrative Law*, 122 HARV. L. REV. 1095, 1125 (2009).

68. I.R.C. § 7805(a) (2012).

69. *See supra* note 2.

70. The Code requires the Treasury Department to issue proposed regulations when it issues temporary regulations, and proposed regulations presumably are subject to notice and comment. I.R.C. § 7805(e); *see also* I.R.M. § 32.1.1.2.2.

71. Taxpayers cannot rely on proposed regulations to support a tax position or for planning purposes unless the IRS clearly states otherwise, and proposed regulations are not binding on the IRS, even though the IRS’s policy is to follow them. I.R.M. § 32.1.1.2.2; I.R.S. Chief Couns. Mem. CC-2003-014 (May 8, 2003).

the same authority as final regulations that completed both internal and external review, despite rarely going through the notice-and-comment process.⁷² The speedy publication without public review subjects temporary regulations to criticism while making them popular with the Treasury Department.⁷³ Although subject to debate, the Treasury Department's modified form of notice-and-comment coupling temporary and proposed regulations is also used by other agencies.⁷⁴

The Treasury Department has argued, unsuccessfully, that Congress blessed this simultaneous issuance arrangement in the tax context.⁷⁵ Congress provided a three-year period of effectiveness for temporary tax regulations and required the simultaneous issuance of proposed regulations.⁷⁶ The Treasury Department argued before the Tax Court that this was a political trade-off permitting the continued, short-term use of temporary regulations without notice-and-comment. If Congress intended the trade-off, that intent was not made evident. Congress did not make any purpose explicit in this situation as it has done in other contexts.⁷⁷

An argument the Treasury Department also frequently makes to bolster its procedure is that most of its regulations are interpretative and therefore do not require notice-and-comment.⁷⁸ This is consistent with the Supreme Court's recent holding in *Perez v. Mortgage Bankers*

72. *Id.*

73. See Michael Asimow, *Public Participation in the Adoption of Temporary Tax Regulations*, 44 TAX LAW 343, 364 (1991); Hickman, *Unpacking the Force of Law*, *supra* note 8, at 496 n.168; Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Regulations*, 3 HOUS. BUS. & TAX L.J. 248, 253 (2003). See generally Kristin E. Hickman & Mark Thomson, *Open Minds and Harmless Errors*, 101 CORNELL L. REV. 261 (2016); Steve Johnson, *Intermountain and the Importance of Administrative Law in Tax Law*, 128 TAX NOTES 837 (2010) [hereinafter Johnson, Intermountain]. The Treasury Department has issued a significant number of them since a backlog of statutes needing guidance was enacted in the 1980s. Hickman, *Unpacking the Force of Law*, *supra* note 8, at 498. In a study of 232 regulatory projects, from January 1, 2003 through December 31, 2005, more than one-third were issued with only post-promulgation notice and comment. See Hickman, *Coloring Outside the Lines*, *supra* note 6, at 1748–51.

74. Michael Asimow, *Interim-Final Rules: Making Haste Slowly*, 51 ADMIN. L. REV. 703, 726 (1999). Even the Administrative Conference of the United States endorsed the use of interim-final rules. Notice: Adoption of Recommendations, 60 Fed. Reg. 43,108, 43,111 (Aug. 18, 1995).

75. See *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. 211 (2010), *rev'd on other grounds*, 650 F.3d 691 (D.C. Cir. 2011).

76. I.R.C. § 7805(e) (2012).

77. Congress explicitly permitted post-promulgation comments for regulations regulating the Health Care Portability and Accountability Act of 1996, Pub. L. No. 104-191 § 401(a), 110 Stat. 1936, 2073 (codified at I.R.C. § 9833 (2012)).

78. 5 U.S.C. § 553(b)(A) (2012).

*Ass'n*⁷⁹ that interpretive rules do not require notice-and-comment even if they significantly revise or change policies from a prior presidential administration.⁸⁰ Despite the holding, three separate concurrences in *Mortgage Bankers* stated concern that interpretive regulations were subject to agency abuse.⁸¹

The Treasury Department sources regulations to the authority for the regulation and claims this sourcing justifies its expansive use of interpretive regulations. Regulations can be initiated under any provision of the Internal Revenue Code, but the Treasury Department interprets the catchall provision that grants the Treasury Department the power to issue “all needful rules and regulations” as the source of interpretive regulations.⁸² Under this interpretation, the IRS believes that regulations only require notice-and-comment because they are legislative regulations when they originate from specific authority in a particular Code provision.⁸³ The Treasury Department claimed more than ninety percent of temporary regulations were interpretive and that public comment was not required.⁸⁴

This distinction between interpretive and legislative regulations may be invalid under administrative law.⁸⁵ Most other agencies recognize all regulations as legislative.⁸⁶ Focusing on the potential penalties taxpayers face if they fail to follow interpretive tax regulations, Kristin Hickman argues the distinction reflects a historical understanding no longer consistent with changes in administrative law doctrine.⁸⁷ According to this argument, all tax regulations except those issued under the good cause exception would need more arduous public review.

Congress is aware that the Treasury Department retains this distinction between authorities and procedures. For example, pursuant to the Regulatory Flexibility Analysis Act (RFAA), agencies must analyze the impact of proposed rules on small businesses.⁸⁸ The RFAA’s requirement generally applies only to rules that go through notice-and-comment, a process the Treasury Department contends only applies to

79. ___ U.S. ___, 135 S. Ct. 1199 (2015).

80. *Perez*, 135 S. Ct. at 1206.

81. *Id.* at 1210–25.

82. I.R.M. § 32.1.2.8.

83. *Id.*

84. Hickman, *Coloring Outside the Lines*, *supra* note 6, at 1748–51.

85. Asimow, *supra* note 73, at 358. *See generally* Johnson, *Intermountain*, *supra* note 73.

86. Hickman, *Agency-Specific Precedents*, *supra* note 8, at 520.

87. *Id.*

88. 5 U.S.C. § 603(a) (2012).

specific authority legislative regulations. Congress added a special requirement applicable only to tax to include interpretive rules as well as legislative ones.⁸⁹ In the limited context of the RFAA, Congress recognized that the Treasury Department makes a distinction and eliminated its effect without eliminating the distinction itself.

Additionally, the IRS issues a tremendous amount of tax guidance that receives less review than is given to regulations. Revenue Rulings apply the law to particular factual situations. Revenue Procedures are similar to Revenue Rulings but traditionally focus on procedural, rather than substantive, aspects of the tax system. Public notices are equivalent to rulings, but their value is derived from the fact they can be issued more quickly in response to public concerns.⁹⁰ Less general are Private Letter Rulings issued to particular taxpayers seeking binding guidance for proposed transactions and numerous types of guidance issued to IRS agents in the process of audits or on particular matters. These other forms of guidance are made public as a result of the Freedom of Information Act.⁹¹

There are claims that the Treasury Department and IRS fail to meet the APA's procedural requirements for the creation of regulations and these other forms of guidance. That failure is arguably subject to judicial challenge and invalidation. To the extent the Treasury Department and IRS are subject to the APA, they must meet its procedural requirements, even if the requirements are burdensome and may operate against the public's best interests. The question for the next Part is how the failure to follow proper procedure may be challenged.

II. CURRENT LIMITATIONS ON PRE-ENFORCEMENT TAX ATTACKS

In most instances the APA permits pre-enforcement litigation to ensure final rules comply with the Act's procedural requirements before the rules have far-reaching impact. In the tax context, however, specific statutes carve out procedural issues (as well as substantive ones) from litigation before the rules have been enforced against a particular taxpayer. Additionally, traditional prudential justiciability rules prevent

89. *Id.* (the requirement applies to a general notice of proposed rulemaking or a "notice of proposed rulemaking . . . for an interpretative rule involving the internal revenue laws of the United States").

90. Rev. Rul. 87-138, 1987-2 C.B. 287.

91. John Coverdale, *Court Review of Tax Regulations and Revenue Rulings in the Chevron Era*, 64 GEO. WASH. L. REV. 35, 79-89 (1995).

many people from litigating procedural issues regarding tax guidance. There were, and remain, good reasons for imposing these restrictive policies, but there are also costs of doing so. The need to use efficiently judicial and agency resources and the interests of taxpayers and the public often conflict in the midst of these challenges.

A. *APA Default Favors Pre-Enforcement Litigation*

Section 701 of the APA establishes a presumption in favor of judicial review of agency action.⁹² Only to the extent that “statutes preclude judicial review” or the action is “committed to agency discretion by law” are courts to abstain from evaluating the choices that agencies make.⁹³ Thus, generally only express congressional action eliminates judicial review of agency rulemaking. This broad pro-litigation floor does not, however, open up all issues to litigation at all times. The APA provides rules to guide a generally permissive pre-enforcement litigation process that encourages early evaluation of procedural, and other, claims.

Courts accept that the APA encourages litigation unless Congress expressly says otherwise or, alternately, in those rare instances where “statutes are drawn in such broad terms that in a given case there is no law to apply.”⁹⁴ Courts often narrowly interpret statutory language that might limit judicial review.⁹⁵ In *Citizens to Protect Overton Park v. Volpe*,⁹⁶ the Supreme Court found there was “law to apply” when the law said the Department of Transportation was not to build highways through parks if a “feasible and prudent” alternative existed.⁹⁷ The Court ruled the choice of going through a park was subject to judicial review

92. 5 U.S.C. § 701(a)(1)–(2) (2012). Other statutory rules and executive orders, outside the APA, also limit agency discretion in creating rules, but compliance with these requirements is not reviewable by courts. For example, the Unfunded Mandates Reform Act and Executive Order 12,866 work to improve management within the federal government and are not intended “to create any right or benefit, substantive or procedural, enforceable by any person in any judicial or administrative action.” 2 U.S.C. § 1571(b) (2012); Exec. Order 12,866, 58 Fed. Reg. 51,735, 51,744 (Oct. 4, 1993). Therefore, agencies cannot be sued for the violation of these requirements, although it might affect their future funding and congressional or executive support.

93. 5 U.S.C. § 701(a)(1)–(2).

94. S. REP. NO. 752, at 212 (1945). For example, in *Carolina Med. Sales, Inc. v. Leavitt*, 559 F. Supp. 2d 69, 75 (D.D.C. 2008), the court precluded judicial review on the grounds the provision in the law regarding the “selection of items and services for competitive acquisition” specifically insulated the decision from the courts.

95. See *Bowen v. Mich. Acad. of Fam. Physicians*, 476 U.S. 667, 674 (1986). But see *Block v. Cmty. Nutrition Inst.*, 467 U.S. 340 (1984).

96. 401 U.S. 402 (1971).

97. *Id.* at 413.

because there was no indication that Congress sought to limit the APA's judicial review. Congress must indicate with a "showing of 'clear and convincing evidence' of a . . . legislative intent . . . [to] restrict access to judicial review."⁹⁸

That pro-litigation perspective includes review of agency procedure often requiring notice-and-comment as discussed in the prior Part. This litigation may result in the court invalidating a rule if the agency acts "without observance of procedure required by law."⁹⁹ When an agency fails to comply with the APA's requirements, as alleged for violations of the notice-and-comment process, a court may conclude this warrants invalidation of the rule. There is a "harmless error rule" in the application of this judicial review, so that if a violation does not create hardship, the court will not overturn the violation.¹⁰⁰ However, "an utter failure to comply with notice and comment cannot be considered harmless if there is any uncertainty at all as to the effect of that failure."¹⁰¹

Despite a pro-litigation perspective, there are limits on when procedural claims can be brought under the APA. Cases alleging violations of the APA in the creation of rules cannot arise until the rules are "final."¹⁰² This requirement protects the integrity of the administrative process and prevents wasting judicial resources. The Supreme Court in *Bennett v. Spear*¹⁰³ set the test:

As a general matter, two conditions must be satisfied for agency action to be "final": First, the action must mark the "consummation" of the agency's decisionmaking process—it must not be of a merely tentative or interlocutory nature. And second, the action must be one by which "rights or obligations have been determined," or from which "legal consequences will flow."¹⁰⁴

This requirement makes it difficult to challenge a policy statement or a notice calling for further action. True policy statements may lack the requisite force of law to determine rights or obligations or lead to legal

98. *Abbott Labs. v. Gardner*, 387 U.S. 136, 141 (1967).

99. 5 U.S.C. § 706(2)(D) (2012).

100. *Id.*

101. *Sugar Cane Growers Coop. of Fla. v. Veneman*, 289 F.3d 89, 96 (D.C. Cir. 2002).

102. For more on the confusing law that is finality, see Gwendolyn McKee, *Judicial Review of Agency Guidance Documents: Rethinking the Finality Doctrine*, 60 ADMIN. L. REV. 371 (2008).

103. 520 U.S. 154 (1997).

104. *Id.* at 177–78 (citation omitted).

consequences.¹⁰⁵ Nevertheless, the form of the guidance itself is not definitive as to whether the rule is final.¹⁰⁶ Guidance has been held not final, so not subject to judicial review, despite having completed notice-and-comment.¹⁰⁷

However, recently the Supreme Court has defined final agency action permissively to permit judicial review. In *U.S. Army Corps of Engineers v. Hawkes Co.*,¹⁰⁸ the Court held that a determination that the property on which a company sought to mine contained regulated water was the consummation of the agency's decision-making process and, therefore, was a final rule permitting judicial review.¹⁰⁹ That the determination could be revised based on new information did not make the determination less final. The Court would not require the plaintiff to await enforcement and risk "serious criminal and civil penalties" from a violation in order to challenge the determination.¹¹⁰

Litigation is also potentially limited by the fact that not everyone can bring suit alleging a violation of the APA's procedures. The litigation must meet the requirements of a "case or controversy" in Article III of the United States Constitution, discussed below. Additionally, suits may only be begun by a "person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute"¹¹¹ "Agency action" is defined to include "the whole or a part of an agency rule, order, license, sanction, relief, or the equivalent or denial thereof, or failure to act"¹¹² Therefore, with respect to guidance, someone must be harmed, "adversely affected or aggrieved" by an agency's rule or, possibly, failure to issue a rule. To this end, a discrete-action limitation precludes broad programmatic attacks, such as the one rejected in *Lujan v. National Wildlife Federation*,¹¹³ in which the Court would not permit a

105. See *Cement Kiln Recycling Coal. v. EPA*, 493 F.3d 207, 226 (D.C. Cir. 2007).

106. See *Oregon v. Ashcroft*, 368 F.3d 1118, 1120 (9th Cir. 2004), *aff'd sub nom. Gonzales v. Oregon*, 546 U.S. 243 (2006); *Barrick Goldstrike Mines Inc. v. Browner*, 215 F.3d 45, 48 (D.C. Cir. 2000); *Nat'l Automatic Laundry & Cleaning Council v. Schultz*, 443 F.2d 689, 698–702 (D.C. Cir. 1971).

107. See *New Jersey v. U.S. Nuclear Regulatory Comm'n*, 526 F.3d 98, 103 (3d Cir. 2008).

108. ___ U.S. ___, 136 S. Ct. 1807 (2016).

109. *Id.* at 1813; see also *Sackett v. EPA*, ___ U.S. ___, 132 S. Ct. 1367 (2012).

110. *U.S. Army Corps of Eng'rs v. Hawkes Co.*, ___ U.S. ___, 136 S. Ct. 1807, 1815 (2016).

111. 5 U.S.C. § 702 (2012).

112. *Id.* § 551(13).

113. 497 U.S. 871 (1990).

wildlife group's challenge to "seek *wholesale* improvement" of a broad-based land use program.¹¹⁴

Courts may also decide that issues may not be litigated if they were not first raised in the notice-and-comment process, if that process was used, and may limit the extent of the challenge.¹¹⁵ This limit applies regardless of the import of a particular issue; an issue generally must be first raised during the rulemaking process or else it is waived. In other words, petitioners must first exhaust their administrative avenues before proceeding to the courts even when the "failure is understandable."¹¹⁶ This encourages participation in the rulemaking process, something beneficial to the creation of all rules, including tax rules.

Unlike the rules regarding who can bring challenges and when those challenges can be brought, enabling statutes generally determine the forum of judicial review of agency rules. Most enabling statutes containing judicial review provisions call for direct, pre-enforcement review in circuit courts as opposed to district courts, with a notable exception of the National Labor Relations Board.¹¹⁷ The Administrative Conference recommended appeals to one of the courts of appeals when (1) the rule is sufficiently significant that a district court decision would likely be appealed or (2) the "public interest requires prompt, authoritative determination of the validity of the rule."¹¹⁸ The federal district and circuit courts are less common avenues in the tax context as most cases are litigated in the Tax Court, which permits tax litigation after enforcement but before the payment of the taxes owed.¹¹⁹

Courts debate the justiciability of an alleged APA violation and not the agency's enabling act. They generally hold that the APA is not an independent basis of jurisdiction.¹²⁰ When there is no specifically applicable judicial review provision under the agency's enabling statute, the petitioner should seek review in a district court through one of the

114. *Id.* at 891 (emphasis in original).

115. *See* *City of Portland v. EPA*, 507 F.3d 706, 710 (D.C. Cir. 2007).

116. *Small Bus. in Telecomms. v. FCC*, 251 F.3d 1015, 1026 (D.C. Cir. 2001).

117. The Administrative Orders Review Act applies to limited agencies, not including the Treasury Department, and provides for review in the courts of appeals. 28 U.S.C. § 2342 (2012); *see also* LUBBERS, *supra* note 34, at 391.

118. ACUS Recommendation 75-3, *The Choice of Forum for Judicial Review of Administrative Action*, 40 Fed. Reg. 27,926, 27,926-27 (July 2, 1975).

119. I.R.S., DATA BOOK 63 tbl.27 (2015); *see also* I.R.C. § 7422 (2012); 28 U.S.C. § 1345(a)(1) (2012); *Flora v. United States*, 357 U.S. 63 (1958).

120. *See* *Califano v. Sanders*, 430 U.S. 99, 104-07 (1977). In tax, jurisdiction for refunds is given to the federal district courts and United States Court of Federal Claims in 28 U.S.C. § 1346 (2012), and jurisdiction is given to the Tax Court in I.R.C. § 7442 (2012).

general jurisdictional statutes. The most frequently cited provision is the federal question provision, which grants district courts “original jurisdiction of all civil actions arising under the Constitution, laws, or treaties of the United States.”¹²¹ Under this claim there is no jurisdictional amount requirement.

The jurisdictional basis can raise questions of when a case may be heard. For example, in *Abbott Laboratories v. Gardner*,¹²² the FDA’s enabling statute did not grant pre-enforcement review, but the Supreme Court permitted the litigation.¹²³ The issue arose over certain drug labeling, and the Court permitted the case to proceed on the basis that there was “no evidence at all that members of Congress meant to preclude traditional avenues of judicial relief,” and the rules would have an immediate and direct impact on manufacturers.¹²⁴ The early challenge prevented the manufacturers from having to violate the rules and wait for enforcement. Since *Abbott Laboratories*, courts generally permit pre-enforcement review of regulations.¹²⁵ Often temporary relief is requested until the issue is heard by a court and will likely be granted if the court finds the rule has immediate and important effects on businesses.¹²⁶

Although *Abbott Laboratories* has reduced agencies’ ability to use ripeness as a defense against pre-enforcement litigation, the argument has not disappeared. In a companion case to *Abbott Laboratories*, *Toilet Goods Ass’n v. Gardner*,¹²⁷ the Court denied pre-enforcement review of an FDA rule because it was not ripe, using the prudential rules to deny hearing despite it being permitted under the APA.¹²⁸ Although the regulation allowing the Commissioner to suspend the certification of additives when their manufacturer refused access to inspectors was final and a legal issue, there was no clear immediate or irreparable impact.¹²⁹ The rule would only apply if access was denied and action was undertaken. At that time, the facts of the situation would be important. Thus, relief is less likely if a court finds there is no immediate impact on the business.

121. 28 U.S.C. § 1331.

122. 387 U.S. 136 (1967).

123. *Id.* at 142, 152.

124. *Id.* at 142.

125. See JAMES T. O’REILLY, ADMINISTRATIVE RULEMAKING § 13.2 (2016); RICHARD J. PIERCE, JR. ET AL., ADMINISTRATIVE LAW AND PROCESS § 5.7.3 (4th ed. 2004).

126. 5 U.S.C. § 705 (2012).

127. 387 U.S. 158 (1967).

128. *Id.* at 162–64. For more on ripeness, see *infra* section II.C.

129. *Id.* at 162–64.

The existence of APA challenges may have greater impact on the agency and on taxpayers depending upon the standard courts use to evaluate the perceived procedural violation. However, the standards for reviewing perceived violations of the APA's procedures are uncertain. The APA provides that the reviewing court will "compel agency action unlawfully withheld or unreasonably delayed" or "hold unlawful and set aside agency action" if certain findings are made.¹³⁰ In particular, if the agency action is "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law" or "without observance of procedure required by law" the rule is in violation of the APA.¹³¹

Extending beyond substantive issues, a catch-all provision requires agencies to not act arbitrarily and capriciously in their rule-making, "picking up administrative misconduct not covered by the other more specific paragraphs."¹³² Thus, the arbitrary and capricious test is the traditional standard applied by courts for reviewing agency actions. Courts tend to focus on the following: whether the record supports the factual conclusion on which the rule is based; the rationality or reasonableness of the policy conclusions underlying the rule; and the extent to which the agency has adequately articulated the basis for its conclusions.

Much of administrative law litigation applying the arbitrary and capricious standard focuses on the substance of agency rules but encompasses the procedures behind formation of the rule. Courts question whether the agency has satisfactorily come to its substantive conclusion through adherence to proper procedure. Reviewing courts' interpretation of this standard has changed over time, sometimes depends on the judge, and often depends upon the subject matter and the perceived seriousness of the issue.¹³³ The standard is both intrusive and deferential. Some have argued that any distinction between arbitrary and capricious, and other standards, at least the substantial evidence standard, is "largely semantic."¹³⁴ David Zaring concludes that courts use basic reasonableness criteria in each of the standards used to evaluate agency actions.¹³⁵

130. 5 U.S.C. § 706 (2012).

131. *Id.* § 706(2)(A), (D).

132. *Ass'n of Data Processing Serv. Orgs., Inc. v. Bd. of Governors*, 745 F.2d 677, 683 (D.C. Cir. 1984).

133. See Paul R. Verkuil et al., Special Feature, *A Blackletter Statement of Federal Administrative Law*, 54 ADMIN L. REV. 1, 42-43 (2002).

134. *Data Processing*, 745 F.2d at 684 (citations omitted).

135. David Zaring, *Reasonable Agencies*, 96 VA. L. REV. 135 (2010); see also Richard Pierce,

For example, in *Baltimore Gas & Electric Co. v. Natural Resources Defense Council, Inc.*,¹³⁶ the Supreme Court held that the Nuclear Regulatory Commission's evaluation of the environmental effects of a nuclear power plant's fuel cycle was a prediction "within its area of special expertise, at the frontiers of science" so that the reviewing court "must generally be at its most deferential" in its review of this type of scientific conclusion.¹³⁷ As long as the agency's assumptions were "within the bounds of reasoned decisionmaking," and the agency "considered the relevant factors and articulated a rational connection between the facts found and the choice made," the Court was not to second-guess the conclusion.¹³⁸

On the other hand, in the same term the Court decided *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Insurance Co.*¹³⁹ In *State Farm*, which involved the rescission of a rule requiring passive restraints in new cars, the Court held that the Court was "not to substitute its judgment for that of the agency":

Normally, an agency rule would be arbitrary and capricious if the agency has relied on factors Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.¹⁴⁰

The reasoned justification demanded in *State Farm* requires courts take a hard look to ensure an agency has adequately considered all comments and that the agency has adequately supported its contested assumptions. Courts undertake this review after-the-fact. Only once the agency successfully proves it has considered all comments is the court to exercise constraint and uphold the agency's action.¹⁴¹

This test for evaluating whether there is a violation of APA procedures in pre-enforcement litigation is significantly tougher on the agency when courts apply the *State Farm* hard look review. Under the hard look review, courts are required to examine the administrative

Jr., *What Do the Studies of Judicial Review of Agency Actions Mean?*, 63 ADMIN. L. REV. 77, 95–96 (2011).

136. 462 U.S. 87 (1983).

137. *Id.* at 103.

138. *Id.* at 104–05.

139. 463 U.S. 29 (1983).

140. *Id.* at 43.

141. See *Greater Bos. Television Corp. v. FCC*, 444 F.2d 841, 850–51 (1970).

record created at the time of the promulgation of the final guidance and any explanatory materials accompanying the guidance. From that data, courts review the methodology, the criteria applied, the relevant factors and options considered, and the explanation of all of these items.¹⁴²

When a court finds that the creation of a rule violates APA procedures, the normal response is to remand the rule to the agency.¹⁴³ Agencies can often retain parts, or even all, of a remanded rule. Of the D.C. Circuit's sixty-one remands of legislative rules between 1985 and 1996, in only twelve did the agency not recover from the remand.¹⁴⁴ Thus, in most instances, through the remand procedure, agencies are able to promulgate similar rules but using correct APA procedure.

During the period of remand, the court can choose whether or not to vacate the remanded rule. With vacatur, the rule that was promulgated through inappropriate procedures is no longer binding.¹⁴⁵ Daniel Rodriguez argues that remand without vacatur is used "to temper the draconian impact of hard look review," but, in the process, "it facilitates the use of more aggressive judicial scrutiny" by offering this means of softening the judgment.¹⁴⁶

Some judges use their discretion as to the choice of approach in any given case, and many judges consider the damage to the public interest from setting aside the rule before doing so.¹⁴⁷ However, other judges do not accept that the statute provides this discretion. They interpret the language of the APA as requiring they vacate the rule because section 706(2)(A) provides that a reviewing court confronted with a procedurally invalid rule shall "hold unlawful and set aside" the rule.¹⁴⁸ This is a minority position, and most rules are not vacated.¹⁴⁹ In twenty-

142. Thomas O. McGarity, *The Courts and the Ossification of Rulemaking*, 75 TEX. L. REV. 525, 527 (1997).

143. See *Fla. Power & Light Co. v. Lorion*, 470 U.S. 729, 744 (1985).

144. William S. Jordan, III, *Ossification Revisited*, 94 NW. U. L. REV. 393, 418 (2000).

145. For evaluation of the vacatur, see Ronald M. Levin, "Vacation" at Sea, 53 DUKE L.J. 291 (2003) (defending remand without vacatur as act of discretion); Boris Bershteyn, Note, *An Article I, Section 7 Perspective on Administrative Law Remedies*, 114 YALE L.J. 359 (2004) (using public choice to support vacatur); Kristina Daugirda, Note, *Evaluating Remand Without Vacatur*, 80 N.Y.U. L. REV. 278 (2005) (arguing that remand without vacatur is justified where costs of vacating are particularly high).

146. Daniel B. Rodriguez, *Gift Horses and Great Expectations*, 36 ARIZ. ST. L.J. 599, 601 (2004).

147. See *Sugar Cane Growers Coop. of Fla. v. Veneman*, 289 F.3d 89, 98 (D.C. Cir. 2002); *Int'l Union, United Mine Workers of Am. v. Fed. Mine Safety & Health Admin.*, 920 F.2d 960, 966-67 (D.C. Cir. 1990).

148. *Checkosky v. SEC*, 23 F.3d 452, 491-93 (D.C. Cir. 1994) (Randolph, J., dissenting).

149. See Jordan, *supra* note 144, at 410.

eight of sixty-one studied cases, William Jordan found the D.C. Circuit did not even explicitly state whether the rule was vacated on the assumption it would not be.¹⁵⁰

Thus, the APA generally permits pre-enforcement litigation of agencies' procedural violations in the creation of rules. However, this permission is not universal, and the likelihood that a court will remand a rule for a violation is uncertain in any given instance. Nevertheless, the APA does provide a tool for those affected by agency action to ensure procedures are applied fairly. That agencies know they may be subject to challenge likely increases their respect of process in their activities. With historically little judicial oversight in the tax context, there is less of an external constraint on the Treasury Department's actions. One study found that over forty percent of tax regulations were developed without following the traditional notice-and-comment procedure, most of those without stating the basis for failing to do so.¹⁵¹ Pre-enforcement litigation would likely mitigate this failure.

B. *Statutory Limitations*

Although the APA applies to the Treasury Department and the IRS, its general preference for pre-enforcement litigation is not the norm in tax because of longstanding specific statutory prohibitions. Neither the assessment of tax nor its collection can be challenged before enforcement actions have been undertaken because of the Tax Anti-Injunction Act¹⁵² and an exception to the Declaratory Judgment Act.¹⁵³ As specific statutory enactments, these statutes trump the APA as a general statute. These acts ensure that the tax system operates with minimal litigation except as the law applies to specific taxpayers.

The Anti-Injunction Act and the Declaratory Judgment Act are often interpreted coextensively, although they target different forms of relief that a court could grant.¹⁵⁴ The Anti-Injunction Act, now in section 7421

150. *Id.* at 410, n.88.

151. Hickman, *Coloring Outside the Lines*, *supra* note 6, at 1749–50.

152. 28 U.S.C. § 2201 (2012).

153. I.R.C. § 7421 (2012). There are narrow statutory exceptions provided in each act. For example, taxpayers can seek Tax Court review of determinations whether they are employees for employment tax purposes. Other provisions grant relief pre-enforcement. For example, I.R.C. section 7476(a) and I.R.C. section 7478 permits taxpayers to have Tax Court review of determinations regarding qualification of retirement plans or applicability of state and local bonds.

154. *See, e.g.*, *Ambort v. United States*, 392 F.3d 1138, 1140 (10th Cir. 2004); *Sigmon Coal Co. v. Apfel*, 226 F.3d. 291, 300–01 (4th Cir. 2000). “[T]he federal tax exception to the Declaratory Judgment Act is at least as broad as the prohibition of the Anti-Injunction Act.” *Alexander v. “Ams. United” Inc.*, 416 U.S. 752, 759 n.10 (1974). The Tax Anti-Injunction Act should not be confused

of the Internal Revenue Code, denies injunctive relief by generally disallowing “suit for the purpose of restraining the assessment or collection of any tax [to] be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed.”¹⁵⁵ The Declaratory Judgment Act contains a broader tax exception that prevents courts from providing declaratory relief for controversies “with respect to Federal taxes.”¹⁵⁶

Courts have normally interpreted these provisions broadly, and the Supreme Court has declared that the Anti-Injunction Act was to result in “a minimum of preenforcement judicial interference” in the realm of taxation.¹⁵⁷ Therefore, injunction and declaratory judgment litigation over tax issues is frequent but rarely successful.¹⁵⁸ Kristin Hickman notes that most cases barred by the Anti-Injunction Act and Declaratory Judgment Act are “unsurprising applications” against tax protesters “raising frivolous legal arguments already rejected by the courts” or those “asserting technicalities to avoid levies or property seizures for taxes clearly owed.”¹⁵⁹ But even when issues are framed as constitutional challenges, “the courts have declined to adopt a general exception from I.R.C. § 7421 [the Anti-Injunction Act] and the DJA [Declaratory Judgment Act], concluding (probably rightly) that such an exception would quickly swallow the rule.”¹⁶⁰

There are two limited common law exceptions to the Anti-Injunction Act and Declaratory Judgment Act that permit pre-enforcement tax litigation. First, in *Enochs v. Williams Packing & Navigation Co.*,¹⁶¹ a unanimous Supreme Court established a rule permitting pre-enforcement

with the Anti-Injunction Act, 28 U.S.C. § 2283 (2012), first enacted in 1793, which limits the ways federal courts can enjoin state court proceedings.

155. I.R.C. § 7421 (2012).

156. 28 U.S.C. § 2201(a) (2012).

157. *Hibbs v. Winn*, 542 U.S. 88, 103 (2004) (citation omitted); see also Hickman, *A Problem of Remedy*, *supra* note 8, at 1169.

158. See Paul H. Asofsky, *Injunctions and Declaratory Judgments in Federal Tax Controversies*, 28 RUTGERS L. REV. 785, 786 (1975).

159. Hickman, *A Problem of Remedy*, *supra* note 8, at 1166–67.

160. The Supreme Court has identified a revenue-raising function as a justification for these limitations, with recourse in a suit for a refund. See *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1, 7 (1962); Hickman, *A Problem of Remedy*, *supra* note 8, at 1166–67. Neither provision’s legislative history provides much evidence of congressional intent, although the common law antecedent similarly precluded courts of equity from interfering with tax collection. Asofsky, *supra* note 158, at 787–88; Hickman, *A Problem of Remedy*, *supra* note 8, at 1166–67; Note, *Enjoining the Assessment and Collection of Federal Taxes Despite Statutory Prohibition*, 49 HARV. L. REV. 109, 109 (1935).

161. 370 U.S. 1 (1962).

litigation if “it is clear that in no circumstances could the Government ultimately prevail” and, in addition, “the taxpayer would suffer irreparable injury if collection were effected.”¹⁶² This may be an impossibly high threshold.

The issue in *Williams Packing* was whether a company was the employer of its boats’ crews and therefore liable for employment taxes. The company furnished boats to captains who hired their own crews but who then sold their fish to the company. The lower courts found an irreparable injury permitting jurisdiction because the company would be forced into bankruptcy if it had to pay the taxes before requesting a refund. Despite establishing the test for when jurisdiction would be available, the Court held jurisdiction was barred in *Williams Packing*. This company could not have pre-enforcement review because the government’s claim was “not without foundation” when using the “most liberal view of the law and the facts.”¹⁶³ If the Court had to go to the merits because there was the possibility of government success, it would contravene the purpose of the Anti-Injunction Act.

Williams Packing added a prong to the earlier, more lenient approach adopted in *Miller v. Standard Nut Margarine Co.*¹⁶⁴ In *Standard Nut*, the Court had permitted “extraordinary and exceptional circumstances” to establish equitable relief to justify pre-enforcement review despite the Anti-Injunction Act.¹⁶⁵ In that case, the IRS told Standard Nut that the company was immune to an excise tax on oleomargarine based on a precedent that established margarine was not subject to the tax.¹⁶⁶ The IRS then reversed its position and tried to collect the tax.¹⁶⁷ The Court held that the discriminatory enforcement of the tax against Standard Nut but not its competitors plus the company’s financial losses during the litigation provided a basis for equity jurisdiction.¹⁶⁸ Going forward, application of this more lenient standard “virtually negated the Anti-Injunction Act” and did “violence to the plain words of the statute.”¹⁶⁹ *Williams Packing* eliminated this lenient policy and shifted focus to the merits of the claim.

162. *Id.* at 7.

163. *Id.* at 7–8.

164. 284 U.S. 498 (1932); *see also* Hill v. Wallace, 259 U.S. 44, 62 (1922).

165. 284 U.S. at 510.

166. *Id.*

167. *Id.*

168. *Id.*

169. Asofsky, *supra* note 158, at 792; Gale Ann Norton, *The Limitless Federal Taxing Power*, 8 HARV. J.L. & PUB. POL’Y 591, 622–23 (1985).

The Supreme Court has since concluded that “*Williams Packing* was the ‘capstone’ of judicial construction” of the Anti-Injunction Act.¹⁷⁰ Relying on the requirement that the government not have any chance of winning, in *United States v. American Friends Service Committee*,¹⁷¹ the Court refused to hear a case regarding a pre-enforcement challenge to withholding.¹⁷² Recognizing that requiring these taxpayers to sue for a refund of withheld taxes would frustrate their chosen method for demonstrating religious opposition to the Vietnam War and that there were other ways the government could collect the tax, the Court still applied the Anti-Injunction Act.¹⁷³ The Court reinforced its desire to “end [the] cyclical departures from the Act’s plain meaning.”¹⁷⁴

To satisfy the first prong of the *Williams Packing* test, the case must egregiously operate against the government. It must be “apparent that, under the most liberal view of the law and the facts, the United States cannot establish its claim”¹⁷⁵ The Court of Appeals held in a later case that the IRS must “flout[] the express terms of the Code, or lack[] any factual basis for the assessment of taxes against an individual taxpayer.”¹⁷⁶ The taxpayer must prove that the government could not win under any circumstances, a high burden indeed.¹⁷⁷ In the case of *Investment Annuity Inc. v. Blumenthal*,¹⁷⁸ the D.C. District Court would not permit review of an IRS revenue ruling that investment annuity contracts were not eligible for favorable treatment, despite this making the matter never reviewable by a court. According to the court, the Anti-Injunction Act would only have to yield “when the denial of judicial review rises to the level of a constitutional infirmity.”¹⁷⁹

To satisfy the second prong, the taxpayer must suffer irreparable harm from being denied relief. Unlike in the earlier *Standard Nut*, this is not a test of the taxpayer’s individual situation but whether relief is ever granted under law. Effectively nullifying this exception, a taxpayer’s opportunity to sue for a refund generally negates the irreparable

170. *United States v. Am. Friends Serv. Comm.* 419 U.S. 7, 9–10 (1974).

171. 419 U.S. 7 (1974).

172. *Id.* at 9–10.

173. *Id.*

174. *Id.*

175. *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1, 7 (1962).

176. *Inv. Annuity, Inc. v. Blumenthal*, 609 F.2d 1, 5–6 (D.C. Cir. 1979).

177. *But see Comm’r v. Shapiro*, 424 U.S. 614, 631–32 (1976).

178. 609 F.2d 1 (D.C. Cir. 1979).

179. *Inv. Annuity*, 609 F.2d at 6.

injury.¹⁸⁰ Unsurprisingly, courts rarely apply *Williams Packing* to find jurisdiction.¹⁸¹

A second exception permitting pre-enforcement litigation despite the Anti-Injunction Act and Declaratory Judgment Act was established in *South Carolina v. Regan*.¹⁸² This exception permits review when there is no other legal remedy available. In *Regan*, the state of South Carolina sought declaratory and injunctive relief when the IRS denied interest on its state bonds and exclusion from holders' gross income.¹⁸³ South Carolina argued it could not seek a refund as it was not the affected taxpayer.¹⁸⁴ The Court concluded there was no other legal remedy available.¹⁸⁵ This exception is often narrowly construed.¹⁸⁶

Similar to *Regan*, cases that involve increasing other people's taxes might not be limited by the Anti-Injunction Act and Declaratory Judgment Act. In *McGlotten v. Connally*,¹⁸⁷ a black man denied membership in a fraternal lodge because of his race was permitted to bring a class action to enjoin the Treasury Department from granting tax benefits to racially discriminatory groups.¹⁸⁸ The lower court held that the action has "nothing to do with the collection or assessment of taxes" and the plaintiff is unable to raise "his objections in a suit of refund."¹⁸⁹

180. *United States v. Am. Friends Serv.* Comm. 419 U.S. 1, 11 (1974); *Alexander v. "Ams. United," Inc.* 416 U.S. 752, 761–62 (1974). *But see* *Cohen v. United States*, 650 F.3d 717 (D.C. Cir. 2011).

181. Hickman, *A Problem of Remedy*, *supra* note 8, at 1171; *see also* *Estate of Michal v. Lullo*, 173 F.3d 503, 506–07, 512 (4th Cir. 1999); *Lampert v. United States*, No. 87-2421, 1989 WL 104459, at *3 (9th Cir. Aug. 31, 1989); *Ponchik v. Comm'r*, 854 F.2d 1127, 1131–32 (8th Cir. 1988).

182. 465 U.S. 367 (1984).

183. I.R.C. § 103 (2012); *Regan*, 465 U.S. at 372.

184. *Regan*, 465 U.S. at 379–80.

185. *Id.*

186. *Ryo Mach., LLC v. Dep't of Treasury*, 696 F.3d 467, 472–73 (6th Cir. 2012); *SEC v. Credit Bancorp, Ltd.*, 297 F.3d 127, 139–40 (2d Cir. 2002); *Nat'l Taxpayers Union, Inc. v. United States*, 68 F.3d 1428, 1436 (D.C. Cir. 1995).

187. 338 F. Supp. 448 (D.D.C. 1972).

188. *Id.* at 453–54; *see also* *Abortion Rights Mobilization, Inc. v. Regan*, 544 F. Supp. 471, 489–90 (S.D.N.Y. 1982), *rev'd on other grounds sub nom.* *U.S. Catholic Conference v. Abortion Rights Mobilization, Inc.*, 487 U.S. 72 (1988); *Tax Analysts & Advocates v. Shultz*, 376 F. Supp. 889, 892–94 (D.D.C. 1974). The Southern District of New York concluded, "[t]hird party suits to compel tax collection as a means to vindicate plaintiffs' rights do not pose the threat of clogging the federal revenue pipeline that taxpayer-sought injunctions would present because third party suits are 'few and far between.'" *Regan*, 544 F. Supp. at 489 (quoting *Wright v. Regan*, 656 F.2d 820, 836 n.52 (D.C. Cir. 1981)).

189. *McGlotten*, 338 F. Supp. at 453–54.

The court looked to the purpose of the Anti-Injunction Act as a tax increasing measure to create this exception.

In addition to these two exceptions, challengers have also avoided the Anti-Injunction Act and Declaratory Judgment Act when courts find that the Acts do not apply. Possibly creating a new exception, the Supreme Court recently circumvented the Anti-Injunction Act and Declaratory Judgment Act's limitation on pre-enforcement litigation with an interesting turn of language of what constitutes a "tax." In *National Federation of Independent Business v. Sebelius*,¹⁹⁰ the Court held the healthcare mandate of the Patient Protection and Affordable Care Act of 2010 was a tax for purposes of the Constitution but not for purposes of the Anti-Injunction Act.¹⁹¹ Two former IRS commissioners, Mortimer Caplin and Sheldon Cohen, filed an amici curiae brief arguing the Anti-Injunction Act and Declaratory Judgment Act prevented pre-enforcement judicial review of the mandate.¹⁹² Nevertheless, the Supreme Court distinguished between a "tax" for statutory and constitutional bases, denying the application of the Anti-Injunction Act and the Declaratory Judgment Act to the penalty that is administered through the tax system.¹⁹³

Consistent with this reasoning, earlier the Supreme Court found the Anti-Injunction Act and Declaratory Judgment Act did not limit certain pre-enforcement challenges because the regulation did not implicate the statutory language of "for the purpose of" or "with respect to" the "assessment or collection" of a tax required by the Anti-Injunction Act or Declaratory Judgment Act.¹⁹⁴ This language has been debated, and the results may come down to fine points of language or what the regulation requires. According to the Supreme Court, the regulation's connection to tax collection does not have to be direct to warrant application of the Anti-Injunction Act and Declaratory Judgment Act.¹⁹⁵

190. 567 U.S. 519 (2012).

191. *Id.* at 546, 574; see also Michael C. Dorf & Neil S. Siegel, "Early-Bird Special" Indeed!: Why the Anti-Injunction Act Permits the Present Challenges to the Minimum Coverage Provision, 121 YALE L.J. F. 389, 397–99 (2012); Steve R. Johnson, *The Anti-Injunction Act and the Individual Mandate*, 133 TAX NOTES 1395, 1399–1400 (2011); Kevin Walsh, *The Anti-Injunction Act, Congressional Inactivity, and Pre-Enforcement Challenges to § 5000A of the Tax Code*, 46 U. RICH. L. REV. 823, 838–43 (2012).

192. Johnson, *supra* note 191, at 1399.

193. *Nat'l Fed'n*, 567 U.S. at 564–67.

194. Declaratory Judgment Act, 28 U.S.C. § 2201 (2012); Tax Anti-Injunction Act, I.R.C. § 7421 (2012).

195. See *Bob Jones Univ. v. Simon*, 416 U.S. 725, 739–40 (1974); *Alexander v. "Ams. United," Inc.*, 416 U.S. 752, 760–61 (1974). However, Congress permits this review for tax-exempt status in I.R.C. § 7428 and 28 U.S.C. § 2201.

For example, in *Bob Jones University v. Simon*,¹⁹⁶ a private university sought injunctive and declaratory relief from an IRS plan to withdraw its tax-exempt status.¹⁹⁷ The university had received a determination of its tax-exempt status in 1942, but in 1970 the IRS changed its position so that private schools with racially discriminatory admissions policies would not be granted tax-exempt status.¹⁹⁸ Although the university claimed the issue was not its tax obligation but its flow of contributions, the Court did not accept this because of the consequence it would have for the institution's tax liability.¹⁹⁹ That there may be non-tax-related motives "ignores the fact that petitioner has not shown that the Service's action is without an independent basis in the requirements of the Code."²⁰⁰ Consequently, the Court applied the Anti-Injunction Act and denied hearing. If there were "no access at all to judicial review . . . our conclusion might well be different," but because there would be an opportunity to litigate when the university has taxable income or pays employment taxes, the litigation was delayed.²⁰¹

Similarly, in *Alexander v. "Americans United," Inc.*,²⁰² another nonprofit organization sought to challenge its loss of tax-exempt status.²⁰³ This organization, with a stated purpose to defend and disseminate information regarding the separation of church and state, received a letter ruling from the IRS in 1950 classifying it as a section 501(c)(3) tax-exempt entity.²⁰⁴ When the IRS found in 1969 that a substantial part of the organization's activities were lobbying for legislation, not permissible for a section 501(c)(3) entity, the IRS revoked the letter.²⁰⁵ The organization sought injunctive relief requiring its reinstatement as a tax-exempt organization. The IRS permitted it to be a 501(c)(4) entity, also exempt from tax, but donations would not be deductible by donors under section 170.²⁰⁶ This latter tax effect was sufficient to prevent pre-enforcement review, especially as the entity could litigate the issue in a refund of unemployment taxes. The Court

196. 416 U.S. 725 (1974).

197. *Id.* at 734.

198. *Id.* at 734–35, 739–40; Rev. Rul. 71-447, 1971-2 C.B. 230.

199. *Bob Jones Univ.*, 416 U.S. at 738–39.

200. *Id.* at 740.

201. *Id.* at 746.

202. 416 U.S. 752 (1974).

203. *Id.* at 755–56.

204. *Id.*

205. *Id.*

206. *Id.*

was not swayed by the fact that the organization raised constitutional matters or that it was not the organization's own taxes that were at issue.²⁰⁷

Continuing the high hurdle for those seeking to challenge Treasury Department rules, in *Debt Buyers' Ass'n v. Snow*,²⁰⁸ decided in 2006, the D.C. District Court disallowed pre-enforcement review of rules requiring the reporting of information about the purchasers of delinquent consumer loans.²⁰⁹ Although the possible tax liability was for those who sold the loans, it was the buyers who had to file reports of the purchases. The court held this reporting requirement helps the IRS determine whether other taxpayers pay their taxes. The issue for the court was that "any action that hinders the IRS in determining the accuracy of [reported gross] income will in fact hinder the assessment and collection of taxes"²¹⁰ Because the purchasers could file a penalty-refund suit, they were not without recourse.

For a moment, the pendulum appeared to swing back in the D.C. District Court in 2014 in *Florida Bankers Ass'n v. Department of Treasury*.²¹¹ The lower court held that the Anti-Injunction Act and Declaratory Judgment Act did not prevent a challenge to regulations requiring banks to report interest income earned by aliens from certain treaty countries.²¹² Although this interest is not taxable in the U.S., according to the Treasury Department, the information is necessary to comply with information-sharing agreements with other countries. The Bankers Association argued the Treasury Department acted arbitrarily and capriciously by failing to consider that some people would withdraw funds from U.S. banks in response to the reporting requirement.²¹³

The lower court permitted review of the regulations but found in favor of the government. The district court concluded that the regulations did not restrain the assessment or collection of taxes but only imposed a reporting requirement.²¹⁴ The district court went on to hold that the Treasury Department did not act arbitrarily and capriciously.²¹⁵ Banks do not owe tax on the reported income even though a penalty,

207. *Id.* at 759–61.

208. 481 F. Supp. 2d 1 (D.D.C. 2006).

209. *Id.* at 3.

210. *Id.* at 9.

211. 19 F. Supp. 3d 111 (D.D.C. 2014).

212. *Id.*

213. *Id.*

214. *Id.*

215. *Id.* at 120–21.

defined in the Code to be a tax, attached, if a bank failed to meet its reporting requirements.²¹⁶ Under the lower court's reading, the Anti-Injunction Act does not apply to reporting requirements. Although the court ultimately sided with the government, it lessened the government's protection from pre-enforcement procedural litigation.

However, this decision was overturned by the D.C. Circuit Court of Appeals on the grounds that the Anti-Injunction Act and Declaratory Judgment Act did, in fact, bar the suit.²¹⁷ The circuit court held it was not permissible to circumvent the Anti-Injunction Act and Declaratory Judgment Act by challenging only the regulatory aspect of a regulatory tax. The issue for the court was that the challenge to the regulation also challenged the tax for failure to comply (although termed a penalty).

According to the circuit court, *Florida Bankers Ass'n* differs from the 1987 case *Foodservice and Lodging Institute, Inc. v. Regan*²¹⁸ because the penalty attached to the reporting requirement reviewed in 2014 was a tax under the Code.²¹⁹ In *Foodservice*, the penalty was not itself listed in the provision governing taxes.²²⁰ Therefore, of four regulations questioned in *Foodservice*, the plaintiffs were allowed to challenge one that required restaurants to report the amount of tips collected in a given year because that regulation was to provide "data useful for assessing tip compliance," but no tax attached for the failure to comply.²²¹ Although the court in *Foodservice* ultimately concluded that the Treasury Department "considered and reasonably rejected the appellant's concerns" in this fourth regulation, the critical issue was that procedural challenges to the reporting requirement were not off limits because of the Anti-Injunction Act or Declaratory Judgment Act in cases where penalties are not designated as taxes.²²²

Belying the support courts give to the tax system in cases involving the Anti-Injunction Act and Declaratory Judgment Act, the government did not raise these challenges in *Loving v. IRS*,²²³ showing that the

216. I.R.C. §§ 6721, 6671 (2012). The penalty is in Chapter 68 Subchapter B per section 6721. Section 6671(a) defines penalties imposed by Title 26, including Chapter 68, Subchapter B, as taxes unless otherwise provided.

217. *Fla. Bankers Ass'n v. Dep't of Treasury*, 799 F.3d 1065, 1069 (D.C. Cir. 2015).

218. 809 F.2d 842 (D.C. Cir. 1987).

219. *Id.* at 846. *But see* *California v. Regan*, 641 F.2d 721, 722 (9th Cir. 1981) (California's reporting requirement pursuant to ERISA is subject to the Declaratory Judgment Act).

220. *Foodservice*, 809 F.2d at 846.

221. *Id.* The other regulations involved the assessment of tax and the employer could "refuse to comply, pay the statutory fine, and sue for a refund of the fine." *Id.* at 843–45.

222. *Id.* at 847.

223. 742 F.3d 1013 (D.C. Cir. 2014), *aff'g* 917 F. Supp. 2d 67 (D.D.C. 2013) (noting that IRS

government recognizes there are limits to these protections. In *Loving*, decided in 2014, the taxpayer won a pre-enforcement challenge to tax regulations that imposed competency testing, continuing education, and ethics requirements on tax return preparers.²²⁴ The link to tax assessment and collection was too tenuous for the government to raise Anti-Injunction Act claims. The Court held the IRS did not have statutory authority for the regulations and permanently enjoined them.

There is scholarly concern over the application of these statutory prohibitions to pre-enforcement challenges. Early discussions of these statutes teased out when tax cases could be heard because, as mentioned above, the provisions do not prevent all pre-enforcement litigation.²²⁵ More recently, these provisions are often recognized, and critiqued, as exceptional, compared to the general preference for pre-enforcement litigation in other areas of law.²²⁶ The focus has turned to the problems with delaying tax litigation over procedural and substantive matters until a refund claim or deficiency litigation.²²⁷ As discussed more fully in the next Part, concerns today generally accept that the law permits the delay of certain issues coming before a court but are frustrated by the results.

C. Prudential Limitations

In addition to statutory limits on pre-enforcement tax litigation, justiciability doctrines, such as standing and ripeness, complicate the prospects for litigation over the procedures used to create tax guidance. Justiciability doctrines derive from the Constitution's cases and controversies requirement.²²⁸ Some of these limitations can be waived, but some may not. Many agencies are increasingly, and successfully, raising these challenges to limit judicial review of their actions.²²⁹

Historically, justiciability was rarely raised in the tax context because of the existence of the statutory limitations on litigation discussed

failed to object in lower court to the remedies and the court found them appropriate).

224. *Id.*

225. Scholars were divided over the appropriate level of judicial review outside of the audit context. See Asofsky, *supra* note 158, at 786; James Lenoir, *Congressional Control Over Suits to Restrain the Assessment or Collection of Federal Taxes*, 3 ARIZ. L. REV. 177 (1961); Norton, *supra* note 169 at 622–23.

226. See *supra* note 8.

227. These limits on pre-enforcement litigation are unlikely to reduce Treasury Department pre-promulgation work because of potential challenges in the event of enforcement activity. See Murphy, *supra* note 2, at 23.

228. U.S. CONST. art. III, § 2, cl. 1.

229. Amy J. Wildermuth & Lincoln L. Davies, *Standing, on Appeal*, 2010 ILL. L. REV. 957, 960.

above.²³⁰ Consequently, few studies focus on justiciability and taxation because of the limited number of tax standing cases. Non-tax specialists tend to lump tax with other cases on standing, often ignoring any interaction with the Anti-Injunction Act or the Declaratory Judgment Act.²³¹ Therefore, only in narrow circumstances is standing likely to be an issue in tax. These prudential concerns most often apply to third parties seeking judicial intervention against the IRS rather than affected taxpayers.²³² The two aspects of justiciability likely to become issues for pre-enforcement tax litigation are standing and ripeness.

First, with respect to standing, over the years the Supreme Court has created a framework for what is required for a case to have standing in the courts. Without standing, a case must be dismissed without consideration of the case's merits. In *Lujan v. Defenders of Wildlife*,²³³ the Court wrote:

Over the years, our cases have established that the irreducible constitutional minimum of standing contains three elements. First, the plaintiff must have suffered an “injury in fact”—an invasion of a legally protected interest which is (a) concrete and particularized and (b) “actual or imminent, not ‘conjectural’ or ‘hypothetical.’” Second, there must be a causal connection between the injury and the conduct complained of—the injury has to be “fairly . . . trace[able] to the challenged action of the defendant, and not . . . th[e] result [of] the independent action of some third party not before the court.” Third, it must be “likely,” as opposed to merely “speculative,” that the injury will be “redressed by a favorable decision.”²³⁴

Thus, standing requires an injury in fact, a causal connection between that injury and the law that is challenged, and that the court's decision could redress the injury.

In order to establish an injury in fact, the plaintiff must prove the injury. How strictly this requirement is to be interpreted has varied over time.²³⁵ Injuries are often defined broadly and recognized as to

230. Hickman, *A Problem of Remedy*, *supra* note 8, at 1174–76.

231. *E.g.*, Karl S. Coplan, *Ideological Plaintiffs, Administrative Lawmaking, Standing, and the Petition Clause*, 61 ME. L. REV. 377, 433–34 (2009); Gene R. Nichol, Jr., *Abusing Standing: A Comment on Allen v. Wright*, 133 U. PA. L. REV. 635, 655–56 (1985); Cass R. Sunstein, *Informational Regulation and Informational Standing: Akins and Beyond*, 147 U. PA. L. REV. 613, 615–17 (1999).

232. Hickman, *A Problem of Remedy*, *supra* note 8, at 1175.

233. 504 U.S. 555 (1992).

234. *Id.* at 560–61 (citations omitted).

235. *See, e.g.*, *Massachusetts v. EPA*, 549 U.S. 497 (2007); *FEC v. Akins*, 524 U.S. 11 (1998);

“‘aesthetic, conservational, and recreational’ as well as economic values.”²³⁶ However, abstract and indefinite injuries are not constitutionally cognizable injuries, so there can be no judicial review. Concrete, though widely shared, injuries might pass the threshold.²³⁷ In 2016, in *Spokeo, Inc. v. Robins*,²³⁸ the Supreme Court reiterated that the injury must be “particularized” and concrete.²³⁹ In that case, procedural violations of the Fair Credit Reporting Act alone were insufficient to establish an injury in fact, despite congressional designation of an intangible harm.²⁴⁰

An agency’s failure to follow proper procedures must fit within this rubric in order to be justiciable. Thus, there is a hurdle despite a Justice Antonin Scalia footnote that “‘procedural rights’ are special.”²⁴¹ Nevertheless, the Court would not recognize that violation of a congressionally-conferred right to everyone of “an abstract, self-contained, noninstrumental ‘right’ to have the Executive observe the procedures required by law” creates an injury in fact.²⁴² The footnote has been interpreted as accepting that a “justiciable claim may be presented by the agency’s failure to comply with statutory mandates” in a more narrowly defined way.²⁴³ For example, a court found that an agency permitting an interested party to have ex parte communications, prohibited as a procedural matter in a formal proceeding, adversely affected “particularized interests in fair decision making” and was therefore be justiciable.²⁴⁴

Nevertheless, in *Town of Castle Rock v. Gonzalez*,²⁴⁵ the Supreme Court suggested that procedural harms alone are unlikely to suffice as an

Lujan v. Defenders of Wildlife, 504 U.S. 555 (1992); Lujan v. Nat’l Wildlife Fed’n, 497 U.S. 871 (1990); Japan Whaling Ass’n v. Am. Cetacean Soc’y, 478 U.S. 221 (1986); United States v. Students Challenging Regulatory Agency Procedures, 412 U.S. 669 (1973).

236. Ass’n of Data Processing Serv. Orgs., Inc. v. Camp, 397 U.S. 150, 154 (1970) (citations omitted).

237. *Akins*, 524 U.S. at 24–25.

238. ___ U.S. ___, 136 S. Ct. 1540 (2016).

239. *Id.* at 1548.

240. *Id.* at 1550.

241. Lujan v. Defenders of Wildlife, 504 U.S. 555, 572 n.7 (1992) (challenging regulation that other agencies must confer with Secretary of the Interior under the Endangered Species Act only in limited circumstances).

242. *Id.* at 573.

243. Cynthia R. Farina, *Standing*, in A GUIDE TO JUDICIAL AND POLITICAL REVIEW OF FEDERAL AGENCIES 17, 35 (John Fitzgerald Duffy & Michael E. Herz eds., 2005).

244. Elec. Power Supply Ass’n v. FERC, 391 F.3d 1255, 1262 (D.C. Cir. 2004).

245. 545 U.S. 748 (2005).

injury in fact unless there is proof that this harm caused an injury to concrete interests.²⁴⁶ The procedural right at issue must protect concrete interests to permit the person to litigate the right, and statutory grants of these rights only avert the need for the litigant to prove redressability and immediacy. In *Summers v. Earth Island Institute*,²⁴⁷ being deprived of the ability to comment on regulations was insufficient to show an injury in fact even though the procedural right was granted by Congress.²⁴⁸

Furthermore, the plaintiff must prove a link between the procedure and substantive agency action.²⁴⁹ This is the case even if it leaves plaintiffs waiting for enforcement. For example, courts may require taxpayers to wait until after penalties are assessed before they are allowed to challenge the procedure regarding the rule. In *Stephenson v. Brady*,²⁵⁰ the plaintiff alleged, in part, that required informational returns referenced in the regulations were invalid because they had not gone through notice-and-comment.²⁵¹ Despite the taxpayer having been threatened with penalties and prior negotiations with the IRS falling apart the court concluded that there was no injury until the penalty was assessed.

This does not mean procedural claims are never heard. In *Massachusetts v. Environmental Protection Agency*,²⁵² the Court permitted “standing if there is some possibility that the requested relief will prompt the injury-causing party to reconsider the decision that allegedly harmed the litigant.”²⁵³ In this case involving the regulation of greenhouse gas emissions from motor vehicles, the EPA’s failure to act gave Massachusetts standing because the EPA’s refusal presented a risk to the state of rising sea levels.²⁵⁴ Although refusals to act are given the

246. *Id.* at 764 (wife did not have protected property interest in police enforcement of restraining order because seeking an arrest warrant is “an entitlement to nothing but procedure”); *see also* *Ctr. for Law & Educ. v. Dep’t. of Educ.*, 396 F.3d 1152, 1159–60 (D.C. Cir. 2005) (advocacy group lacked standing to challenge alleged defect in rulemaking committee due to lack of particularized harm).

247. 555 U.S. 488 (2009).

248. *Id.* at 496–97.

249. *Massachusetts v. EPA*, 549 U.S. 497, 517–18 (2007); *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 573 n.7 (1992); *Sugar Cane Growers Coop. of Fla. v. Veneman*, 289 F.3d 89, 94–95 (D.C. Cir. 2002).

250. No. 90-3042, 1991 WL 22835 (4th Cir. Feb. 26, 1991) (per curiam).

251. *Id.* at *2.

252. 549 U.S. 497 (2007).

253. *Id.* at 518.

254. *Id.*

utmost in deference, the Court nevertheless demanded agency action. Moreover, in *Sugar Cane Growers Cooperative of Florida v. Veneman*,²⁵⁵ the D.C. Circuit also said that a person “who alleges a deprivation of a procedural protection to which he is entitled never has to prove that if he had received the procedure the substantive result would have been altered.”²⁵⁶ In this case, a payment-in-kind program increased the supply of sugar depressing its price, but the program was issued without notice-and-comment. Thus, the key is to prove the failure of procedure affected the resulting guidance and that guidance caused an injury, not that the lack of procedure was harmful.

The requirement that there be an injury in fact cannot be waived. These issues are jurisdictional.²⁵⁷ Therefore, even if they want to, the petitioner and government cannot simply assume an injury or that standing is self-evident. Courts are to raise the issue *sua sponte*.²⁵⁸ When confronted with the issue, the Court held that “the requirement of injury in fact is a hard floor of Article III jurisdiction that cannot be removed by statute.”²⁵⁹ This may mean that the parties invited to comment on guidance and otherwise influence policy choices are prevented from receiving judicial review of the agency’s procedures.²⁶⁰

Thus, courts have not allowed Congress to circumvent the required injury in fact, a prerequisite of standing, even though the doctrine is muddled.²⁶¹ How it will apply in the tax context is unknown. The general position was established in 1923 when the Supreme Court denied a taxpayer suit regarding government expenditures on the grounds that the taxpayer’s interest in government revenue, as one of millions of taxpayers, was too small.²⁶² According to the Court:

If one taxpayer may champion and litigate such a cause, then every other taxpayer may do the same, not only in respect of the statute here under review, but also in respect of every other appropriation act and statute whose administration requires the

255. 289 F.3d 89 (D.C. Cir. 2002).

256. *Id.* at 94–95.

257. Wildermuth & Davies, *supra* note 229, at 963.

258. *Am. Library Ass’n v. FCC*, 401 F.3d 489, 493 (D.C. Cir. 2005).

259. *Summers v. Earth Island Inst.*, 555 U.S. 488, 497 (2009); *see also Spokeo, Inc. v. Robins*, ___ U.S. ___, 136 S. Ct. 1540, 1549 (2016).

260. Wildermuth & Davies, *supra* note 229, at 960.

261. Coplan, *supra* note 231; Elizabeth Magill, *Standing for the Public*, 95 VA. L. REV. 1131 (2009).

262. *Massachusetts v. Mellon*, 262 U.S. 447, 487 (1923) (litigating the Maternity Act of 1921, conditioning federal aid to states on programs to protect maternal health).

outlay of public money, and whose validity may be questioned.²⁶³

The Court worried that judicial review “would operate to disturb the whole revenue system of the government.”²⁶⁴ The IRS’s regulatory behavior may be subject to evaluation and contest but not by an unlimited number of parties.

In addition to proving an injury in fact, those who question the Treasury Department’s procedures may struggle to satisfy the causation prong of the standing test. In general, regulated parties, in the tax context those who owe tax, can more easily demonstrate that the law caused injury than can the beneficiaries of regulation, in the tax context those who receive benefits from federal funding. Also, in the tax context, causation is difficult for taxpayers who are relatively disadvantaged by not receiving a particular tax preference. The Supreme Court accepts the difficulty this creates for some plaintiffs, noting the injury is often less direct but “hinge[s] on the response of the regulated (or regulable) third party to the government action or inaction.”²⁶⁵ Although standing is not precluded in these cases, “it is ordinarily ‘substantially more difficult’ to establish.”²⁶⁶

Through the application of the standing doctrine, courts may deny third-party standing in tax matters.²⁶⁷ In a two-sentence 1976 concurrence, Justice Potter Stewart wrote, “I cannot now imagine a case . . . where a person whose own tax liability was not affected ever could have standing to litigate the federal tax liability of someone else.”²⁶⁸ The D.C. Circuit goes so far to state, “[i]t is well-recognized that the standing inquiry in tax cases is more restrictive than in other cases.”²⁶⁹

These limitations mean that direct beneficiaries of programs may not be able to litigate changes in IRS policy. In *Simon v. Eastern Kentucky Welfare Rights Organization*,²⁷⁰ indigent rights organizations sought to

263. *Id.*

264. *Louisiana v. McAdoo*, 234 U.S. 627, 632 (1914); *see also* Richard B. Stewart, *Standing for Solidarity*, 88 YALE L.J. 1559, 1568 (1979).

265. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 562 (1992).

266. *Id.*

267. *See* Nancy C. Staudt, *Taxpayers in Court: A Systemic Study of a (Misunderstood) Standing Doctrine*, 52 EMORY L.J. 771, 774 (2003).

268. *Simon v. E. Ky. Welfare Rights Org.*, 426 U.S. 26, 46 (1976) (Stewart, J., concurring) (excepting the First Amendment).

269. *Nat’l Taxpayers Union, Inc. v. United States*, 68 F.3d 1428, 1434 (D.C. Cir. 1995); *see also* *DaimlerChrysler Corp. v. Cuno*, 547 U.S. 332, 343–44 (2006).

270. 426 U.S. 26 (1976).

challenge a revenue ruling, a form of IRS guidance that does not complete notice-and-comment, that reduced the requirement for tax-exempt hospitals to offer emergency care to those unable to pay.²⁷¹ The plaintiffs challenged both the substance of the ruling and the lack of procedure in its creation.²⁷² Instead of relying on the Anti-Injunction Act and Declaratory Judgment Act, the Supreme Court dismissed the case for lack of standing.²⁷³ The Court concluded that the connection between the ruling and the denial of medical services was too speculative; even if the rule were changed, there is no reason to know that the plaintiff would get medical care or even that the hospital would pursue tax-exempt status.²⁷⁴ In *Fulani v. Brady*,²⁷⁵ when a presidential candidate sought to invalidate the tax-exempt status of a presidential debate sponsor, the D.C. Circuit Court took issue with the plaintiff seeking to change the agency's rule "*only as a means to alter the conduct of a third party.*"²⁷⁶

The combination of standing and the statutory prohibitions often reduce judicial review through a two-step sieve. If litigation is not stopped by one, it is stopped by the other. For example, in *National Taxpayers Union v. United States*,²⁷⁷ the D.C. Circuit accepted that a taxpayer organization established standing on behalf of the group's members to raise an early constitutional challenge against a retroactive tax rate increase.²⁷⁸ Nevertheless, the court then blocked the litigation with the Anti-Injunction Act and Declaratory Judgment Act.

Examining the standing rules as they apply to the review of tax-exempt charities' qualifications, Lynn Lu has criticized the inability of those with interests in tax regulations, but who are not the direct object of the regulation, to contest them in court.²⁷⁹ Lu provides two examples of failed challenges on standing grounds: people unable to pay for medical care challenging the IRS change of requirements for tax-exempt hospitals and African-American families challenging the tax-exempt status of de facto segregated private schools.²⁸⁰ The goal, at least for Lu,

271. *Id.* at 33.

272. *Id.*

273. *Id.* at 46.

274. *Id.* at 45–46.

275. 935 F.2d 1324 (D.C. Cir. 1991).

276. *Id.* at 1330 (emphasis in original).

277. 68 F.3d 1428 (D.C. Cir. 1995).

278. *Id.* at 1435.

279. Lynn D. Lu, *Standing in the Shadow of Tax Exceptionalism: Expanding Access to Judicial Review of Federal Agency Rules*, 66 ADMIN. L. REV. 73 (2014).

280. *Id.* at 89; E. Ky. Welfare Rights Org. v. Shultz, 370 F. Supp. 325 (D.D.C. 1973), *rev'd sub*

is to use the judicial process to circumvent the agency and Congress; to accomplish what they would not do.

Some cases in which judicial review was denied were politically sensitive and unlikely to elicit a favorable legislative response when the courts refused to act. For example, in *Allen v. Wright*,²⁸¹ the Court denied standing to challenge income tax exemptions for racially segregated schools.²⁸² Although the injury in fact in *Allen* was the same as that in *Bob Jones* and “one of the most serious injuries recognized in our legal system,” the “links in the chain of causation between the challenged Government conduct and the asserted injury are far too weak.”²⁸³ The Court would not go so far as to permit litigation to force the IRS to do what it had voluntarily done in *Bob Jones*.

Because standing is a constitutional jurisdictional requirement, exceptions to the standing requirement are narrowly drawn. In *Flast v. Cohen*,²⁸⁴ the Supreme Court recognized such an exception when it granted standing to taxpayers who sought to enjoin the use of federal funds to buy textbooks for parochial schools.²⁸⁵ However, *Flast* was more of a First Amendment case than a tax case because of its focus on the separation of church and state. Although *Flast* indicated that Article III does not prohibit taxpayer suits, its holding is generally limited to its facts and may not extend to administrative actions. For example, in *Hein v. Freedom from Religion Foundation*,²⁸⁶ the Court declined to grant standing to challenge the White House’s use of federal money to fund conferences to promote “faith-based initiatives.”²⁸⁷ That it was executive

nom. E. Ky. Welfare Rights Org. v. Simon, 506 F.2d 1278 (D.C. Cir. 1974), *vac’d*, Simon v. E. Ky. Welfare Rights Org., 426 U.S. 26 (1976); Wright v. Miller, 480 F. Supp. 790 (D.D.C. 1979), *rev’d sub nom.* Wright v. Regan, 656 F.2d 820 (D.C. Cir. 1981), *rev’d sub nom.* Allen v. Wright 468 U.S. 737 (1984). Ignoring that potential claimants to pre-enforcement litigation could be limitless, Lu’s proposal would pressure the definition of particularized, concrete injuries. Nichol, *supra* note 231, at 655–56; Sunstein, *supra* note 231, at 615–17.

281. 468 U.S. 737 (1984).

282. *Id.*

283. *Id.* at 756, 759; *Bob Jones Univ. v. Simon*, 416 U.S. 725 (1974).

284. 392 U.S. 83 (1968).

285. *Id.* *Flast* held that the *Massachusetts v. Mellon*, 262 U.S. 447 (1923) limit on taxpayer standing was only prudential in nature, thus suggesting that there might be standing if authorized by Congress. See also Michael E. Solimine, *Congress, Separation of Powers, and Standing*, 59 CASE W. RES. L. REV. 1023, 1042–43 (2009).

286. 551 U.S. 587 (2007).

287. *Id.* at 602–03 (drawing a distinction between congressional action and executive discretion); see also *Bowen v. Kendrick*, 487 U.S. 589, 618–20 (1988); *Valley Forge Christian Coll. v. Ams. United for Separation of Church and State, Inc.*, 454 U.S. 464, 479 (1982); *United States v. Richardson*, 418 U.S. 166, 173 (1974). In *Arizona Christian School Tuition Organization v. Winn*, 563 U.S. 125, 141–43 (2011), the Court held that Arizona state tax credits did not count as

action made it beyond the reach of *Flast* standing. *Flast* has been the only Supreme Court case allowing a taxpayer to challenge spending as a violation of the Establishment Clause.

Thus, standing for the public in tax matters is limited so that in most cases pre-enforcement litigation is not permitted.²⁸⁸ Similar to the Anti-Injunction Act, the “inconvenience and relatively minor expense” of complying with regulations before filing suit in response to a tax audit is insufficient to justify earlier judicial review.²⁸⁹ The tools that the Treasury Department or IRS use to prevent pre-enforcement litigation in a particular case, whether statute or common law, may differ, but the result is often the same.

Additional prudential principles of standing may be waived by Congress but to date are rarely waived in the tax context.²⁹⁰ Waivable prudential principles include the prohibition on a litigant raising another person’s legal rights and the rule barring adjudication of generalized grievances more appropriately addressed in the representative branches. The latter arises frequently in the tax context but is infrequently waived. Without congressional waiver, courts may refrain from deciding “abstract questions of wide public significance,” which amount to “generalized grievances” that would be better addressed by Congress.²⁹¹ When the public as a group shares concerns about unfair administration, courts routinely dismiss the generalized grievance to prevent overuse of the court system.²⁹² The issue is more properly congressional than judicial.

government spending and so could not be challenged under *Flast*. This argument contravenes most academic interpretation that urges tax expenditures be equated with direct spending because they both cost government revenue and accomplish the same objectives, despite the court’s claim this is the spending of the taxpayers’ money and not the states’. Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705 (1970); Eric Toder, *Tax Cuts or Spending—Does It Make a Difference?*, 53 NAT’L TAX J. 361 (2000); David A. Weisbach & Jacob Nussim, *The Integration of Tax and Spending Programs*, 113 YALE L.J. 955 (2004). *But see* J. Clifton Fleming, Jr. & Robert J. Peroni, *Can Tax Expenditure Analysis Be Divorced from a Normative Base?: A Critique of the “New Paradigm” and Its Denouement*, 30 VA. TAX REV. 135, 142 (2010).

288. Magill, *supra* note 261.

289. *Stephenson v. Brady*, No. 90-3042, 1991 WL 22835, at *4 (4th Cir. Feb. 26, 1991) (per curiam).

290. *See Allen v. Wright*, 468 U.S. 737, 751 (1984); *Ctr. for Auto Safety v. Nat’l Highway Traffic Safety Admin.*, 793 F.2d 1322, 1335 (D.C. Cir. 1986).

291. *Warth v. Seldin*, 422 U.S. 490, 499–500 (1975); *see also United States v. Students Challenging Regulatory Agency Procedures*, 412 U.S. 669, 687 (1973).

292. *See id.*

A final justiciability consideration is the ripeness of the issue. The issue of ripeness is not whether jurisdiction exists but whether the case is currently ready for adjudication. Ripeness requires the issue be fit for judicial decision and the parties must experience hardship, namely a legal wrong, without judicial consideration of the case. Ripeness issues frequently arise when plaintiffs seek anticipatory relief. In *Abbott Laboratories v. Gardner*,²⁹³ the Supreme Court held that ripeness's "basic rationale is to prevent the courts, through avoidance of premature adjudication, from entangling themselves in abstract disagreements over administrative policies, and also to protect agencies from judicial interference until an administrative decision has been formalized and its effects felt in a concrete way by the challenging parties."²⁹⁴ Despite the rhetoric, *Abbott Laboratories* upheld pre-enforcement review of an administrative regulation.

Abbott Laboratories established an expansive presumption in favor of early judicial review of agency action that has since been narrowed.²⁹⁵ Nevertheless, ripeness is rarely a high hurdle for procedural challenges to agency rules unless the court determines that the practical application of the rule would assist in the judicial evaluation.²⁹⁶ The issue is likely to turn on whether the challenge is to the rule on its face or whether the challenge "depends as well on the way in which the [rule] will be applied."²⁹⁷ This may be a higher standard if the rule confers a benefit than if the rule imposes a burden.²⁹⁸

Much of the difficulty created by the standing and ripeness doctrines to the ability to make procedural claims against tax guidance would occur whether or not the claim is raised before or after enforcement. It is difficult for third parties to prove the required injury occurred. Pre-enforcement litigation of tax guidance has the additional difficulty of proving the issue is ripe because it is unknown whether the rule will be enforced at all. Ripeness will be a particular concern for forms of tax guidance that are not generally applicable or that purport to forecast future regulations.

293. 387 U.S. 136 (1967).

294. *Id.* at 148–49.

295. Hickman, *A Problem of Remedy*, *supra* note 8, at 1180.

296. *Cement Kiln Recycling Coal. v. EPA*, 493 F.3d 207, 216 (D.C. Cir. 2007). *But see* Nat'l Park Hosp. Ass'n v. Dep't of the Interior, 538 U.S. 803, 810–11 (2003); *Reno v. Catholic Soc. Servs.*, 509 U.S. 43, 57–59 (1993).

297. *Cement Kiln*, 493 F.3d at 216.

298. *Reno*, 509 U.S. at 58–59.

Consequently, despite the APA's preference for pre-enforcement, it is surprising that any litigation over the procedures used to promulgate tax guidance is successfully litigated before enforcement. Part of the difficulty is the complexity of the issues even when divorced from taxation. Hickman summarizes these doctrinal issues succinctly: "the law in this area is a mess."²⁹⁹ These messy prudential requirements would not be eliminated even if statutory limits were repealed.

III. JUSTIFICATIONS FOR ENFORCEMENT LITIGATION

Although the creation of tax guidance must comply with the APA, interested parties often find it difficult to challenge the Treasury Department's compliance in courts.³⁰⁰ When they can undertake such a challenge, the challenge is often after the law has been applied to them so that they are challenging operative guidance. Under this system, some types of procedural claims can never be made, and people not directly impacted by tax guidance cannot challenge it, either substantively or procedurally. There is a cost of these timing and scope limitations. When courts hear the challenge after the guidance has affected many taxpayers, there are costs to taxpayers and the tax system. Taxpayer rights and the consistency of the tax law are jeopardized through the delayed or limited litigation of procedural complaints.

A. *Courts Belatedly Confront Procedural Claims*

Taxpayers are increasingly bringing cases asking courts to invalidate regulations and other forms of tax guidance because of the Treasury Department's or IRS's lack of appropriate procedure, but these cases are generally heard only late in the life of the guidance.³⁰¹ These late challenges appear from blog reports and academic articles to be increasing in frequency but rarely earlier in their timing.³⁰² Courts generally hear these cases only late in the process of a taxpayer

299. Hickman, *A Problem of Remedy*, *supra* note 8, at 1200.

300. *Hosp. Corp. of Am. v. Comm'r*, 348 F.3d 136, 145 n.3 (6th Cir. 2003) (the Sixth Circuit pointed out the failure to make procedural claims).

301. The Court has not always focused on procedural issues. For example, in 2003, ignoring the issue of the APA, in *Boeing Co. v. United States*, the Supreme Court accepted that even if the regulations governing cost allocations were interpretive, they would be entitled to deference and, moreover, they were not arbitrary. 537 U.S. 437 (2003). The Court, instead, jumped into the substance of the regulation and whether it conformed to the statute.

302. Hickman concluded in 2008, "taxpayers rarely contest Treasury regulations on procedural grounds." *A Problem of Remedy*, *supra* note 8, at 1154.

challenging that taxpayer's personal tax liability. Thus, the guidance is challenged in response to a taxpayer's audit and failed negotiation with the agency and long after the guidance has operated on taxpayers. A few cases have successfully made it before courts earlier in the process, but early litigation is hard to secure under current law and heavily depends on the facts of the case to show the tax itself is not being challenged.³⁰³ For example, regulations imposing information reporting obligations are susceptible to procedural challenge whereas a deduction or loss thereof would not be. This distinction puts pressure on courts that may seek to grant procedural review but generally can only do so belatedly.

In 2015, the D.C. Circuit summarized the imperfect mesh of case law, holding that the Anti-Injunction Act: (1) prevents litigation over an organization's tax status (*Bob Jones* and "*Americans United*"), except for statutorily authorized actions; (2) permits litigation when the plaintiff has no other means to challenge the result (*South Carolina*) or the challenge does not affect tax assessment and collection (*Cohen*); and (3) permits litigation if the IRS engages in viewpoint discrimination (*Regan*).³⁰⁴ Through this relative maze of law, taxpayers seek to overturn unfavorable regulations before they apply to prevent potential penalties or the cost of compliance.

Temporary regulations issued by the Treasury Department regarding inversions illustrate the complexity of the case law challengers face when bringing early procedural claims. For example, the Chamber of Commerce filed a lawsuit in Texas seeking to block the temporary inversion regulations promulgated by the Treasury Department in April 2016.³⁰⁵ Inversions are when a U.S. corporation relocates its legal domicile outside the U.S. to avoid U.S. taxation on its worldwide income. Section 7874, the statutory basis of the regulations, disqualifies inversions for U.S. tax purposes in certain limited circumstances to force the parent corporation to remain subject to U.S. taxation.³⁰⁶ Congress enacted the statute in 2004 to target inversions using a merger of a U.S.

303. The issue of the procedure used for the promulgation of tax guidance is often wrapped up in issues of the proper amount of deference that courts should give to that guidance. The Supreme Court unanimously extended *Chevron* deference to tax regulations in 2011 in *Mayo Foundation for Medical Education & Research v. United States*. 562 U.S. 44 (2011). Although claiming a changed regulatory interpretation originated in the Department's general authority to issue needful rules and regulations, the Department used notice and comment procedures to do so, a fact noted by the Court. Thereafter, the Court ruled that the Treasury Department "certainly did not act irrationally" in its regulations as it upheld their application. *Id.* at 60.

304. *Z Street v. Koskinen*, 791 F.3d 24, 31 (D.C. Cir. 2015).

305. *Chamber of Commerce v. IRS*, No. 1:16-cv-944 (W.D. Tex. Aug. 4, 2016).

306. I.R.C. § 7874 (2012).

corporation into a foreign corporation if the foreign acquirer's shareholders do not retain a meaningful stake in the new foreign parent corporation.³⁰⁷ In other words, the U.S. government ignores the inversion if U.S. shareholders retain a sufficiently large stake in the new foreign parent corporation.

The regulations extend the definition of disqualified mergers to deny a tax effect if a U.S. corporation merges into a foreign corporation, but U.S. shareholders retain a smaller stake in the corporation than defined in the statute if other facts that make the inversion appear abusive.³⁰⁸ This agency action is not surprising given the political reaction to American corporations moving offshore; the issue is the means by which the IRS tries to deter the activity. In the face of congressional opposition to former President Barack Obama's desire to thwart these inversions, the regulations create a three-year lookback rule to ensure the foreign company did not increase in its size to avoid the prior inversion threshold.³⁰⁹

It is commonly accepted that these new regulations were issued on April 5, 2016 to block the \$152 billion merger of Ireland-based Allergan, Plc and New York-based Pfizer, Inc. and to dissuade other companies from attempting similar inversions.³¹⁰ In the short-term the strategy was successful. The Pfizer deal was called off, stating that the decision "was driven by the actions announced by the U.S. Department of Treasury . . ."³¹¹

As part of its litigation strategy, the Chamber of Commerce argued that the temporary regulations, issued in conjunction with proposed regulations, exceed the Treasury Department's statutory authority, are arbitrary and capricious, and failed to follow notice-and-comment procedures. In particular, the Chamber complained that the temporary regulation was issued without prior notice-and-comment and without

307. The statute defines a meaningful stake as sixty percent of the voting and eighty percent of the value of the new corporation. *Id.*

308. 26 C.F.R. § 1.7874-8T(g)(6) (2016).

309. *Id.*

310. Laurel Brubaker Calkins, *IRS Tax Inversion Rule Change Draws Chamber of Commerce Suit*, BLOOMBERG (Aug. 4, 2016), <https://www.bloomberg.com/news/articles/2016-08-04/irs-tax-inve> [<https://perma.cc/J39K-XCXM>]; 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), https://www.nytimes.com/2016/04/06/business/dealbook/tax-inver?_r=0 [<https://perma.cc/H9GC-LC26>].

311. *Pfizer Announces Termination of Proposed Combination with Allergan* (Apr. 6, 2016), http://www.pfizer.com/news/press-release/press-release-detail/pfizer_announces_termination_of_proposed_combination_with_allergan [<https://perma.cc/V9HG-KDJ5>].

sufficient explanation for doing so; the Treasury Department's statement claimed that it had "determined that sections 553(b) and (d) of the Administrative Procedure Act" did not apply.³¹²

A difficulty for the Chamber to achieve early review, however, is proving standing. In particular, as required by *Lujan*, the Chamber must prove someone was injured by the regulations. If Pfizer had consummated its transaction and then been subject to tax, it would have had the requisite injury in fact.³¹³ But the regulations operate in practice to prevent challenges by dissuading the activity because the potential cost is too high. This standing issue increases the difficulty of the case and is, perhaps, one reason the case was initiated in Texas, a more taxpayer-friendly jurisdiction than Pfizer's home state of New York.

Moreover, even if standing is satisfied, Daniel Hemel notes this case is likely to be dismissed because of the Anti-Injunction Act; the parties must wait until after it has been applied to taxpayers.³¹⁴ The Chamber seeks the court to set aside a rule that it does not like because the rule makes it harder for corporations to avoid the inversion limits. The effect of overturning the rule would be to restrain the IRS from assessing and collecting tax because more inversions could occur, placing more revenue outside the reach of the IRS. The purpose of the Anti-Injunction Act is to prevent litigation such as this that would frustrate the collection of revenue.³¹⁵ However, the likely result is that even if the regulation is ultimately declared invalid, no one will risk the penalties from undertaking a big stakes transaction so the regulation accomplishes its objective.

Additionally, the proposed regulations attempt to limit earnings stripping by which American subsidiaries borrow from foreign parent or affiliated corporations. Challengers to this part of the regulations face similar difficulties as do those opposing the inversion rules, although it is more likely businesses will risk penalties to challenge the earnings stripping rule after their application because the stakes are not as high.

312. T.D. 9761, 81 Fed. Reg. 68, 20882 (Apr. 8, 2016); Fed. Reg. 135734-14 (May 2, 2016).

313. Despite Pfizer's claim, it is unlikely the transaction was sufficiently developed to permit a claim that Pfizer had an imminent business transaction that fell through as a direct result of the new tax regulation, which would be a difficult claim with the best facts.

314. Daniel Hemel, *The Chamber of Commerce Has an Anti-Injunction Act Problem*, MEDIUM (Aug. 8, 2016), <https://medium.com/whatever-source-derived/the-chamber-of-commerce-has-an-anti-injunction-act-problem-9cc28f6947c#ch14uwtxe> [<https://perma.cc/67XR-V6UU>]; see also *Challenging the IRS Anti-Inversion Notice: A Hollow Threat*, SKADDEN, ARPS, SLATE, MEAGHER & FLOM LLP (Jan. 2015), <https://www.skadden.com/insights/challenging-irs-anti-inversion-notice-hollow-threat> [<https://perma.cc/7REJ-LP5H>].

315. See *supra* note 156.

The issue is that on the payment of interest, an American corporation may claim a tax deduction, reducing its income in the U.S. even as it increases income reportable in another country. Traditionally these types of loans have received favorable U.S. tax treatment but are not reported on financial statements because they occur within one larger conglomerate. The regulations seek to target this earnings stripping by treating related-party debt as stock. The payment of dividends, unlike interest, is not tax deductible, thereby eliminating the current tax benefit enjoyed by these loans.³¹⁶

These proposed regulations on earnings stripping have since been finalized after a significant number of comments were received, and it remains to be seen if they will be challenged.³¹⁷ The final regulations contain a number of changes in response to “detailed and thoughtful comments.”³¹⁸ For example, exceptions were added for several ordinary business transactions. Additionally, the effective date for a documentation requirement for interests to be treated as indebtedness was only for debt instruments issued on or after January 1, 2018, whereas the other rules are generally effective on or after January 19, 2017. Showing its response to potential procedural litigation, the Department issued a 380-page preamble to its final regulations to prove its response to the public’s comments.

The earnings stripping issue is controversial and likely to face its own litigation, in part based on procedure. Although taxpayers may seek pre-enforcement review, they are unlikely to receive it. For example, the Business Round Table complained that, when proposed, the regulations did not comply with the APA’s effective date and had an “insufficient [comment period] given the complexity of the regulations.”³¹⁹ The *Daily Tax Report* noted that “[r]eams of paper filled with detailed technical responses to comments won’t stop court challenges” to the new rules.³²⁰ However, problems with the Anti-Injunction Act remain, and the result is likely to be delayed litigation, less on the procedure than on the

316. I.R.C. § 163 (2012).

317. T.D. 9790, 81 Fed. Reg. 204.

318. *Id.* at 72859.

319. Doug Oberhelman et al., *Letter to U.S. Treasury Secretary*, BUS. ROUND TABLE (July 7, 2016), <http://businessroundtable.org/resources/brt-comment-letter-treasury-department-proposed-385-regulations> [https://perma.cc/T7R6-L6JE].

320. Erin McManus, *Voluminous Preamble Won’t Stop Court Challenge to Debt Rules*, BLOOMBERG BNA, DAILY TAX REPORT (Oct. 17, 2016), http://news.bna.com/dtln/display_batch_print_display.adp?searchid=28625713 [https://perma.cc/C9EF-DL3J].

substance of the regulations.³²¹ Not mentioning timing, the IRS's associate chief counsel expects the rules to withstand legal challenge.³²²

These potential cases are procedurally harder to hear early than other recent tax challenges, which have drawn lines around activities for the “assessment and collection of tax,” and therefore sought to evade the limitations of the Anti-Injunction Act and Declaratory Judgment Act on pre-enforcement litigation.³²³ Particularly with the expansion of reporting obligations, the litigating public seeks a narrow reading of this clause in the Anti-Injunction Act and Declaratory Judgment Act to permit early challenges to reporting regulations. For example, in 2015, in *Direct Marketing Ass'n v. Brohl*,³²⁴ the Supreme Court narrowly read the Tax Injunction Act, a law similar to the Anti-Injunction Act, but one that prohibits federal district courts from hearing challenges to state taxes in order to permit challenges to reporting requirements.³²⁵ In that case, Colorado law required retailers to notify Colorado customers of potential use tax liability and required retailers to report tax-related information to state tax authorities. Thus, the law imposed notice and reporting obligations but no additional tax.

The Tax Injunction Act is not exactly like the Anti-Injunction Act, with the Tax Injunction Act adding “restrain” with “enjoin, [and] suspend,” but the Court “assume[d] that words used in both Acts are generally used in the same way . . .”³²⁶ The “assessment, levy, or collection” processes referred to in the statute were, according to the Court, discrete phases of the taxation process that “do not include informational notices or private reports of information relevant to tax liability.”³²⁷ The Court read “restrain” as having a “narrow[] meaning . . . captur[ing] only those orders that stop . . . ’assessment, levy and collection”” rather than “merely inhibit[] those activities.”³²⁸

Direct Marketing, if applied to the Anti-Injunction Act, would greatly expand the number of cases that could be heard pre-enforcement because

321. Hickman suggests the use of temporary regulations coinciding with the proposed regulations might be a means of challenging the final rules. *Id.*

322. Kat Lucero, *IRS Official: Controversial Treasury Rules Should Survive Legal Challenge*, HILL (Oct. 28, 2016), [http://origin-ny1.thehill.com/policy/finance/303325-irs-official-controversial-treasury-rules-should-survive-legal-challenge?amp \[https://perma.cc/CBV8-YY2K\]](http://origin-ny1.thehill.com/policy/finance/303325-irs-official-controversial-treasury-rules-should-survive-legal-challenge?amp [https://perma.cc/CBV8-YY2K]).

323. *See supra* notes 151–52.

324. ___ U.S. ___, 135 S. Ct. 1124 (2015).

325. *Id.* at 1132.

326. *Id.* at 1129.

327. *Id.* at 1126.

328. *Id.* at 1132–33.

information gathering, “includ[ing] private reporting of information used to determine tax liability,” was excluded from the Tax Injunction Act.³²⁹ Although assessment “might also be understood more broadly to encompass the process by which [the] amount [of tax liability] is calculated,” the Court chose to interpret it as the official action taken based on information already reported.³³⁰ In the Court’s reading in *Direct Marketing*, collection occurs only “after a formal assessment” and is part of the enforcement process. In this reading, guidance regarding anything that occurs prior to a tax return being filed is open to pre-enforcement litigation.

Direct Marketing is seemingly at odds with another case, discussed in the prior Part, *Florida Bankers Ass’n v. Department of Treasury*.³³¹ *Florida Bankers* is a lower court decision, but it was squarely on the Anti-Injunction Act. The D.C. Circuit Court held, also in 2015, that a pre-enforcement suit was barred by the Anti-Injunction Act despite its involving banks’ reporting obligations of the interest earned by non-resident aliens. In *Florida Bankers*, the penalty imposed for failing to comply with the reporting requirements, although not yet imposed, was sufficient to trigger the statutory bar.³³² Some scholars take exception to this as inconsistent with the new, narrower reading of these statutes.³³³

Only four years before in *Cohen v. United States*,³³⁴ the D.C. Circuit had appeared to embrace a more narrow reading of the Anti-Injunction Act and Declaratory Judgment Act that would permit courts to hear cases earlier.³³⁵ In *Cohen*, the taxpayers did not request a refund but challenged the Notice announcing refund procedures on the basis the Notice violated the APA.³³⁶ The court denied tax an exception from procedural APA challenges in refund procedures laid out in Notice 2006-50,³³⁷ and, on remand, the district court determined the notice was binding and therefore invalid because it had not been submitted for

329. *Id.* at 1129.

330. *Id.* at 1130.

331. 799 F.3d 1065 (D.C. Cir. 2015).

332. *Id.* at 1081.

333. Patrick J. Smith, *D.C. Circuit Majority Opinion in Florida Bankers Not Consistent with Supreme Court’s Direct Marketing Decisions*, PROCEDURALLY TAXING (Aug. 17, 2015), <http://procedurallytaxing.com/d-c-circuit-majority-opinion-in-florida-bankers-not-consistent-with-supreme-courts-direct-marketing-decision-part-1/> [<https://perma.cc/QY3E-J6MQ>].

334. 650 F.3d 717 (D.C. Cir. 2011), *cert. denied*, 135 S. Ct. 946 (2015).

335. *Id.* at 728.

336. *Id.*

337. Notice 2006-50, 2006-1 C.B. 1141.

notice-and-comment.³³⁸ Arguing for administrative law uniformity, the D.C. Circuit's majority concluded "[t]he IRS is not special in this regard; no exception exists shielding it—unlike the rest of the Federal Government—from suit under the APA."³³⁹

While *Cohen* opens up the door to pre-enforcement litigation in the D.C. Circuit, *Florida Bankers* seems to close it unless the D.C. Circuit is deterred by the *Direct Market* decision. But *Cohen* had limiting facts because the court highlighted that its early litigation involved the refund of taxes already collected as opposed to the assessment and collection of taxes. Thus, *Cohen* may signal a tightening of the court's interpretation of what constitutes tax collection and assessment in the Anti-Injunction Act and Declaratory Judgment Act. The vacatur was prospective because more than 100 million taxpayers had obtained refunds.³⁴⁰ The IRS continued to entertain claims filed under the contested procedures until 2012, and the D.C. Circuit held that the IRS did not need to replace the procedure but that taxpayers should use general refund procedures.³⁴¹

Artful description of the assessment and collection of taxes have also served organizations that previously lacked standing or were unable to sue on issues not yet ripe, although not yet with respect to the issuance of tax guidance. In a 2015 case, *Z Street v. Koskinen*,³⁴² a non-profit organization dedicated to Israeli issues sued the IRS on the grounds that the IRS undertook more rigorous review of its internal policies than other non-profits as a result of then President Barack Obama's Middle East policies.³⁴³ The District Court concluded this litigation was not to restrain "the 'assessment or collection' of a tax, but rather to prevent the IRS from delaying consideration of its application [for tax-exempt status]."³⁴⁴ The D.C. Circuit Court agreed that *Z Street* had no other remedy, consistent with the *South Carolina v. Regan* exception to the Anti-Injunction Act.³⁴⁵ Although *Z Street* could wait and pursue administrative remedies, those remedies only apply to the organization's qualification for tax-exempt status. Here the issue was the timing of

338. *Cohen*, 650 F.3d at 721.

339. *Id.* at 723.

340. *In re Long-Distance Tel. Serv. Fed. Excise Tax Refund Lit.*, 853 F. Supp. 2d 138, 144–45 (D.D.C. 2012).

341. *In re Long-Distance Tel. Serv. Fed. Excise Tax Refund Lit.*, 751 F.3d 629, 634 (D.C. Cir. 2014); Announcement 2012-16, 2012-18 I.R.B. 876.

342. *Z Street v. Koskinen*, 791 F.3d 24, 31 (D.C. Cir. 2015).

343. *Id.*

344. *Id.* at 26.

345. *Id.* at 31.

consideration, not the result, because of the organization's views on Israel.

Regardless of the timing of litigation, this newer, narrower approach to the assessment and collection of taxes language risks opening up guidance to wide-ranging attacks of courts that strictly impose the APA on guidance not previously held to this standard. In 2012 in *Dominion Resources Inc. v. United States*,³⁴⁶ a taxpayer filed suit seeking a refund of its corporate income taxes.³⁴⁷ At issue was a long-standing regulation. A notice of upcoming regulations was published in 1988, a notice of proposed rulemaking was issued in 1991, and the final regulations were published in 1994.³⁴⁸ Ignoring the length of time the regulations were effective, the Federal Circuit invalidated the final regulation, which governed the capitalization of interest (as opposed to its current deductibility) on the grounds that the regulation was not a reasonable interpretation of the statute.³⁴⁹ Applying hard look review, the court concluded that the regulation was arbitrary and capricious because its promulgation did not have a judicially mandated reasoned explanation of the Treasury Department's decision-making.³⁵⁰

The lower court in *Dominion Resources*³⁵¹ had noted the procedural need for a reasoned explanation but dismissed the concern. The Court of Federal Claims had found that, while "it is a stretch to conclude" that the Treasury Department cogently explained its processes, the "'path' that Treasury was taking in the rulemaking proceedings could be 'discerned,' albeit somewhat murkily."³⁵² Examining the evolution of the regulations, the lower court had concluded that the public had been made aware of the issue and the Treasury Department had addressed commentators' suggestions. Therefore, the lower court, until overturned, accepted the "lack of exactitude and the ensuing confusion" did not "signify that

346. 681 F.3d 1313 (Fed. Cir. 2012).

347. *Id.*; see also Ellen P. Aprill, *The Impact of Agency Procedures and Judicial Review on Tax Reforms*, 65 NAT'L TAX J. 917, 923 (2012).

348. Notice 88-99, 1988-2 C.B. 422; Capitalization of Interest, 56 Fed. Reg. 40,815-01 (proposed Aug. 16, 1991); Capitalization of Interest, 59 Fed. Reg. 67,187 (Dec. 29, 1994).

349. Treas. Reg. § 1.263A-11(e)(1)(ii)(B) (1995).

350. *Dominion Resources*, 681 F.3d at 1319. From the tone of the opinion, it is unlikely any explanation would have satisfied the majority who disliked a legal fiction on which the regulations were based, even though the concurrence pointed out some fiction was likely inevitable. Similar problems existed before, but not often. See *Am. Standard, Inc. v. United States*, 602 F.2d 256, 267 (Ct. Cl. 1979).

351. 97 Fed. Cl. 239 (2011).

352. *Id.* at 239, 259.

Treasury acted to establish the final rule in an arbitrary and capricious manner.”³⁵³

The Court of Claims in *Balestra v. United States*³⁵⁴ may have signaled it has backtracked from hard look review, although the case did not focus on the procedure used to promulgate a regulation.³⁵⁵ In *Balestra*, a husband and a wife who filed a joint tax return brought a refund suit for Federal Insurance Contribution Act (FICA) contributions on deferred retirement compensation that the husband would never receive because his employer went bankrupt.³⁵⁶ The taxpayers argued that the regulation defining the “present value” of an “amount deferred” should have considered the employer’s financial condition.³⁵⁷ The court refused to substitute its own construction of the statute for what it deemed a reasonable interpretation by the agency.³⁵⁸ Although purporting to apply *State Farm* review, the court cursorily repeated the notice of proposed and final rulemaking. In doing so, the court found the Treasury Department did not act “arbitrarily or capriciously,” but that, instead, it sought “workable, simple, and flexible” rules.³⁵⁹ The “path” used to create the regulations was “reasonably discernable.”³⁶⁰

These issues of the application of review and the timing of when the review is to occur will be particularly important in the Tax Court, which hears ninety percent of tax cases but traditionally did not focus as much on administrative law matters as other federal courts.³⁶¹ The Tax Court has recently gone directly to the heart of APA procedure and its application to tax regulations. The Tax Court has set aside regulations that had undergone notice-and-comment but did not have an adequate statement responding to comments after their application to a particular taxpayer.³⁶² In *Altera Corp. v. Commissioner*,³⁶³ decided in 2015, a

353. *Id.* at 259.

354. 803 F.3d 1363 (Fed. Cir. 2015).

355. *Id.*

356. *Id.* at 1367–68.

357. *Id.* at 1369.

358. *Id.* at 1374.

359. *Id.* at 1363, 1371.

360. *Id.* at 1374.

361. I.R.S., DATA BOOK 63 tbl.27 (2015). For an example of the Tax Court’s traditional response to notice and comment, see *Intermountain Ins. Serv. of Vail LLC v. Comm’r*, 174 T.C. 211, 245–46 (2010), *rev’d on other grounds*, 650 F.3d 691 (D.C. Cir. 2011). Judges Halpern and Holmes of the Tax Court rejected the traditional interpretation. *Id.* (Halpern and Holmes, J.J., concurring).

362. See, e.g., *Altera Corp. v. Comm’r*, 145 T.C. 3 (2015), *appeal docketed*, No. 16-70497 (9th Cir. Feb. 23, 2016).

unanimous Tax Court invalidated certain transfer pricing regulations issued in 2003.³⁶⁴ Multi-national corporations use transfer pricing to allocate expenses among their subsidiaries in different countries. In *Altera*, the regulations involved the use of stock-based compensation in cost-sharing arrangements.³⁶⁵ The affiliated group of corporations sought a redetermination of the deficiencies of the taxes they were found to owe.³⁶⁶ The court ruled on the grounds that the Treasury Department failed to comply with the APA and granted the taxpayer a partial summary judgment.³⁶⁷

The taxpayer contested the rule of stock-based compensation in cost-sharing arrangements, a well-known and hotly debated issue long before the *Altera* case. The issue was raised in prior litigation and also in the notice of proposed rulemaking and public hearings.³⁶⁸ There were thirteen submitted comments and four participants in the hearings, but these regulations could only be litigated after application.³⁶⁹ Nevertheless, at the time the final rule was issued, the Treasury Department's files did not contain expert opinions, empirical data, or papers that supported its position, which was opposed by the comments.³⁷⁰ The Treasury Department attempted to address comments by stating they "do not agree" with them despite acknowledging contrary "data may not be available."³⁷¹ The Department asserted that the evidence provided by the commentators "do[es] not share enough characteristics" with the issues raised by the regulations to be conclusive.³⁷² The court found these were mere assertions by the agency.³⁷³

Applying hard look review, the court found that the Treasury Department failed to undertake a necessary fact-finding in order to support its position.³⁷⁴ Moreover, the regulation's preamble, while

363. 145 T.C. 3 (2015), *appeal docketed*, No. 16-70497 (9th Cir. Feb. 23, 2016).

364. *Id.* at 133.

365. *Id.* at 93.

366. *Id.* at 91.

367. *Id.* at 134.

368. *Xilinx Inc. v. Comm'r*, 125 T.C. 37 (2005); *Compensatory Stock Options Under Section 482*, 67 Fed. Reg. 48,997 (July 29, 2002).

369. *Altera*, 145 T.C. at 104.

370. *Id.* at 107.

371. *Id.* at 108.

372. T.D. 9088, 2003-2 C.B. at 842-43.

373. *Altera*, 145 T.C. at 130.

374. *Id.* at 122-23.

responding to some comments, was held not to justify the final rule.³⁷⁵ The court appeared frustrated that the Treasury Department did not consider sufficient variables, and while “improving administrability can be a reasonable basis for agency action,” the Treasury Department did not make this claim in its preamble (although even if it did, it does not appear the court would accept this claim without more significant fact-finding).³⁷⁶ Invalidating the regulations, the Tax Court disagreed with the Treasury Department that the APA did not apply and found the Treasury Department failed to engage in reasoned decision-making by not producing this evidence and not responding to several comments. As a result, the Treasury Department was found to have engaged in arbitrary and capricious decision-making.³⁷⁷

This is a change in tenor but not in timing from earlier Tax Court decisions. For example, in 1998, in *Schwalbach v. Commissioner*,³⁷⁸ when challenging taxes determined to be owed, the taxpayer argued that the passive activity loss regulations did not comply with the APA and so the amount of taxes the IRS claimed were owed should be reduced, and the Tax Court held the regulations did.³⁷⁹ In its discussion, the court focused on the interaction between the agency and the public in two rounds of comments rather than evaluating the wording of notices and comments.³⁸⁰ In *Schwalbach*, the proposed regulations had not reached shareholders of C corporations, but this relationship was governed by the final regulations.³⁸¹ The court concluded that, even though this provision was not in the proposed regulation, the absence did not invalidate the notice-and-comment process, a position inconsistent with modern hard look review.³⁸²

With the evolution to greater receptiveness to APA procedural challenges, taxpayers recognize this change as a means of changing tax outcomes once they have been subject to audit. In other words, savvy taxpayers understand that challenging procedures is now a tool when a taxpayer is confronted with an audit and tax deficiency. To this end, a

375. *Id.* at 118.

376. *Id.* at 126.

377. *Id.* at 134.

378. 111 T.C. 215 (1998).

379. *Id.*; *see also* *Am. Med. Ass’n v. United States*, 887 F.2d 760 (7th Cir. 1989); *Griffin Indus., Inc. v. United States*, 27 Fed. Cl. 183 (1992); *Dow Corning Corp. v. United States*, 22 Cl. Ct. 184 (1990); *Wing v. Comm’r*, 81 T.C. 17 (1983).

380. *Schwalbach*, 111 T.C. at 230.

381. *Id.* at 220.

382. *Id.* at 216.

partner at McDermott Will & Emery LLP wrote that “the impact of [Altera] and its limits on the IRS’s rulemaking authority could also be felt more broadly”³⁸³ He notes, perhaps with glee, that regulations are binding on the IRS even as taxpayers are free to challenge them.³⁸⁴ In its own “Tax Controversy Alert,” a partner at Steptoe & Johnson LLP noted that the arbitrary and capricious requirement “is not a toothless throwaway requirement but rather a real and potentially potent method of challenging Treasury regulations.”³⁸⁵ And a Florida State law professor told the Florida Bar that a “warrior who does not use all weapons risks unnecessary defeat” when “encourag[ing] taxpayers’ counsel” to make APA challenges.³⁸⁶ In 2016, NYU Law School hosted a program on using the APA to challenge IRS guidance and, in 2014, Duke Law School held a symposium on applying administrative law in tax.³⁸⁷ These issues are not going away. If anything, the need to resolve procedural issues will grow.

B. *Sometimes Courts Never Review Procedural Violations*

Despite the likelihood that courts will hear more procedural cases, existing statutory and prudential limitations mean that some procedural claims can never successfully be presented. As a result, some claims that a piece of tax guidance was not created using proper procedures are never heard by a court, whether before or after enforcement. This Article focuses on two types of guidance that are unlikely to be litigated to illustrate these concerns: first, guidance that favors a select group of taxpayers, due to issues involving standing; and, second, tax notices that

383. Roger Jones et al., McDermott Will & Emery LLP, *How to Challenge Tax Regs on Administrative Law Grounds*, NAT’L L. REV. (Oct. 3, 2015), <http://www.natlawreview.com/article/altera-how-to-challenge-tax-regulations-administrative-law-grounds> [https://perma.cc/H4TR-SDMR].

384. *Id.*

385. J. Walker Johnson et al., STEPTOE & JOHNSON LLP, *Tax Controversy Alert, Using the Administrative Procedure Act to Challenge Claims that IRS Regulations Are Entitled to Chevron Deference* (2012), <http://www.steptoel.com/assets/attachments/4472.pdf> [https://perma.cc/FWU3-WG3N].

386. Steve Johnson, *Using Administrative Law to Challenge IRS Determinations*, 88 FLA. B.J. 81 (2014).

387. *Using the Administrative Procedure Act to Challenge IRS Guidance*, N.Y.U. LAW TAX BLOG (Feb. 1, 2016), <http://blogs.law.nyu.edu/taxblog/2016/02/using-the-administrative-procedure-act-to-challenge-irs-guidance> [https://perma.cc/CWY3-LHPT]; Mila Sohoni, *On Dollars and Deference: Agencies, Spending, and Economic Rights*, DUKE L.J., <http://dlj.law.duke.edu/current-issue/> [https://perma.cc/H82M-V28W].

promise future regulations, due to lack of finality. In both instances, procedural claims are not reviewable.

Looking at the first instance, guidance that favors isolated groups of taxpayers is one example of how some procedural issues are unlikely to be addressed even if the agency used an undemocratic process in creating the guidance. When the government narrowly tailors tax reduction for political or administrative reasons, those benefited are unlikely to object to the resulting benefit. Even if they wanted to, they may be unable to make procedural objections to the way the reduction was formulated. For rules that create favorable tax treatment, such as an exclusion from tax, there is no enforcement per se, and there is generally no injury from the favorable rule. Thus, those that benefit from the rule but oppose the procedure are unable to challenge it in court.

Third party suits to tailored tax benefits are also unlikely. Although the Anti-Injunction Act and Declaratory Judgment Act are unlikely to apply as tax preferences are not to raise revenue, as discussed in the prior Part,³⁸⁸ *Flast* has set a high bar for establishing standing in tax cases.³⁸⁹ Issues of favoritism are generally deemed political matters. Except in extreme circumstances such as in *Flast* involving First Amendment rights, these issues are subject only to congressional review. Treasury Department and IRS favoritism in the enforcement of a congressional statute might warrant an exception, but one not yet created.

These issues of tax favoritism arise more often than one might think. For example, the IRS makes numerous preferential interpretations of the Internal Revenue Code, often as a result of concern for the administrability of a particular issue, that benefit select groups of taxpayers. Lawrence Zelenak refers to these as customary deviations from what is required by the Code.³⁹⁰ According to Zelenak, these deviations are different from dubious readings of the statutory language or from positions contrary to the literal language of the Code but that are almost certainly required by courts, such as not taxing imputed income.³⁹¹ Additionally, they are different from simple under-enforcement without any public indication of that approach, such as the IRS not seeking actual tip amounts in excess of eight percent of restaurant sales.³⁹²

388. See section II.B.

389. See *supra* notes 275–68.

390. Zelenak, *supra* note 23.

391. *Id.* at 833–34.

392. *Id.* at 834–35.

Consider, for example, the issue of frequent flyer miles. The IRS announced that, although technically within the meaning of gross income in section 61 of the Code, it would not seek to tax frequent flyer miles received for business travel.³⁹³ Because a tax is not being applied so that no one is taxed as a result of the rule, there is no enforcement to trigger a lawsuit. There is no injury in fact for standing. Without the lawsuit, the policy of not taxing this fringe benefit cannot be judicially challenged. Although this exclusion remains the law, at least one exception has been carved out when frequent flyer miles are received for opening a bank account, although the rule was instigated more by Citibank's issuance of a Form 1099-MISC than the IRS. The inclusion of income was quickly challenged.³⁹⁴

As another example, the IRS narrowed statutory limits on the deductibility of corporate net operating losses and unrealized built-in losses following a corporate acquisition.³⁹⁵ The rules are complicated but aim to prevent taxpayers from deducting losses after mergers planned to traffic in tax deductions. Notice 2008-83 declared that the limits of this section would not apply to banks.³⁹⁶ The new rule single-handedly permitted mergers between banks to maintain certain loss deductions and did so at odds with express statutory prohibitions. The notice was issued at the beginning of the Great Recession and immediately prior to the bailout of the financial industry.³⁹⁷ This notice facilitated the acquisition of Wachovia, a failing bank, by Wells Fargo, one that survived the Recession.³⁹⁸

The favorable impact of Notice 2008-83 on the targeted taxpayers was not challengeable in courts. No one had standing to challenge the liberalization of the rules that allowed Wells Fargo to buy Wachovia's tax deductions. Political fallout nevertheless occurred. Numerous people

393. Announcement 2002-18, 2002-10 I.R.B. 621, *discussed in* Zelenak, *supra* note 23, at 831–32.

394. *Shankar v. Comm'r*, 143 T.C. 140 (2014); *see also* Kelly Phillips Erb, *Tax Court Sides with IRS in Tax Treatment of Frequent Flyer Miles Issued by Citibank*, FORBES (Aug. 28, 2014, 8:35 AM), <https://www.forbes.com/sites/kellyphillipserb/2014/08/28/tax-court-sides-with-irs-in-tax-treatment-of-frequent-flyer-miles-issued-by-citibank/> [<https://perma.cc/529D-7F3N>].

395. Notice 2008-83, 2008-2 C.B. 905, *discussed in* Alice G. Abreu & Richard K. Greenstein, *The Rule of Law as a Law of Standards: Interpreting the Internal Revenue Code*, 64 *Duke L.J. ONLINE* 53, 88–92 (2015); Zelenak, *supra* note 23, at 847.

396. Notice 2008-83, 2008-2 C.B. 905.

397. *Id.*

398. Memorandum from Rich Delmar, Counsel to the Inspector Gen., to Eric Thorson, Inspector Gen., on Inquiry Regarding IRS Notice 2008-83 (Sept. 3, 2009), <https://www.treasury.gov/about/organizational-structure/ig/Documents/Inquiry%20Regarding%20IRS%20Notice%202008-83.pdf> [<https://perma.cc/8EKQ-S5N2>].

critiqued the notice.³⁹⁹ It was a significant enough issue that Congress responded by enacting legislation that disapproved of Notice 2008-83 as “inconsistent with the congressional intent” of section 382 and describing the IRS’s authority for the notice as “doubtful.”⁴⁰⁰ Congress focused on concerns of the separation of powers rather than narrow procedural matters. Also, undermining this strong rhetorical position explicitly stating that the agency had no authority to issue the guidance, Congress acknowledged that taxpayers need to be able to rely on IRS guidance. Congress permitted taxpayers to rely on the notice for ownership changes that occurred before January 17, 2009, the date the legislation was enacted.⁴⁰¹ Not to be deterred, in 2010, the IRS issued Notice 2010-2, declaring that section 382 would not apply if the Treasury Department were to sell its shares, presumably of General Motors, to the public.⁴⁰² It has not been overturned.⁴⁰³

Favorable agency action, such as with respect to frequent flyer miles or net operating losses, published through the issuance of notices that do not receive public feedback in a notice-and-comment process are particularly troubling. The agency is creating law, which may be a valid use of its delegated authority under section 7805. However, in doing so the agency should take the requisite steps to write that law in the process designed for such activity by Congress. In other words, to maintain our democratic system, when the public does not participate through Congress in the making of exceptions to the tax law, the public should be able to participate through notice-and-comment in order to maintain agency accountability to the people.

It is difficult to fix this problem of lack of accountability for tax favoritism. Arguably litigation over favorable rules is not prohibited by the Anti-Injunction Act or the Declaratory Judgment Act because these exceptions reduce, rather than increase, tax revenue. However, because

399. Nathaniel Cushman, Comment, *The Impact of Illegal Tax Guidance: Notice 2008-83*, 62 TAX LAW. 867 (2009); 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.html> [https://perma.cc/Q6JE-ZTAS] (citing interviews with a dozen tax lawyers); *Tax Policy: Treasury Should Have Consulted Congress Before Giving Banks Breaks, Grassley Says*, BLOOMBERG BNA: DAILY TAX REP., Oct. 14, 2008, at G-1.

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

401. *Id.*

402. Notice 2010-2, 2010-1 C.B. 251.

403. Senate Bill 2916 would have nullified Notice 2010-2; however, it died in committee. S.B. 2916 111th Cong., Reg. Sess. (2009).

these notices favor the taxpayer at whom they are aimed, no one is in a position to challenge them in court other than as a third-party claim.⁴⁰⁴ Moreover, because they are favorable to the taxpayer, they must be challenged before enforcement, or the challenge has little effect. Challenges occurring after their effective date would likely be after those benefited submitted tax returns, so that remedies would likely only be prospective.⁴⁰⁵ Although this would be better than the current system, even better solutions should be found.

A second group of tax guidance for which procedural claims are unlikely to be heard is guidance that operates against taxpayers, but the guidance is not, strictly speaking, a final rule forcing taxpayer action. For example, some IRS Notices, which are arguably not final rules so not subject to challenge, alert taxpayers to potential enforcement activity and are intended to influence taxpayer behavior.⁴⁰⁶ If determined to be final, the guidance would increase a taxpayer's tax obligation and thus raise Anti-Injunction Act and Declaratory Judgment Act limits to pre-enforcement litigation. However, if found to be a final rule, the prohibition on litigation becomes a timing issue. Procedural claims could be raised after enforcement. If the IRS uses the notice as part of its justification for the tax assessment, courts could hear procedural claims against the specific guidance because the guidance is used to cause the harm of the tax assessment. An issue remains whether the notice is final because its application appears final, even if a notice does not purport to be.

For example, the IRS not infrequently issues notices warning of potential action, such as "to relate what regulations will say in situations where the regulations may not be published in the immediate future."⁴⁰⁷ Returning to the issue of the inversion regulations, before the final regulations were issued in 2016, the IRS issued Notice 2014-52 on September 22, 2014, and amended the notice with Notice 2015-79 on November 19, 2015.⁴⁰⁸ The notices contained rules in the form of regulations but only announced that the Treasury Department "intends to

404. Taxpayer advocates or tax clinics are natural advocates over these issues.

405. There are good reasons that taxpayers filing tax returns should be able to rely on government guidance outstanding at the date of filing and, practically, these taxpayers' statute of limitations is likely to have lapsed before litigation over procedure is complete.

406. This attempt to influence may be particularly troubling because of the tax system's stated reliance on voluntary compliance.

407. *Understanding IRS Guidance - A Brief Primer*, IRS, <https://www.irs.gov/newsroom/understanding-irs-guidance-a-brief-primer> [<https://perma.cc/R2ZE-E45S>].

408. Notice 2014-52, 2014-42 I.R.B. 712, *modified by* Notice 2015-79, 2015-49 I.R.B. 775; *see also* T.D. 9761, 81 Fed. Reg. 20858 (Apr. 8, 2016).

issue” regulations to reduce the benefit of inversion transactions and requested public comments. Thus, the language was a basis for regulations but failed to be published to initiate formal notice-and-comment.

These notices were expressly intended to provide awareness of the issue and potential future actions of the IRS; however, it is hard to believe they were not also intended to stop these types of transactions. The notices also limited companies’ ability to claim certain tax benefits if they undertake inversions after the notice was released. This raises companies’ risk of challenging the rules at the same time that it minimizes chances of procedural challenges. With this method of announcing proposed regulations without following the prescribed publication, the agency failed to meet the requirements for beginning notice-and-comment. Nevertheless, the notices’ Fact Sheet announced the proposal as having full force of law and the regulations were expected to apply to transactions completed on or after the publication of the notices.⁴⁰⁹

As another example, the IRS issues notices putting transactions on a list of transactions that impose reporting and penalty burdens. Although classification as a listed transaction does not impose a tax itself, its burdens are intended to affect taxpayer behavior. As a listed transaction, taxpayers who have entered into these types of transactions are required to disclose those transactions and their advisors may be subject to registration and required to maintain lists.⁴¹⁰

One of the many listed transactions was designated as such in 2015 when the IRS issued notices on certain contracts it viewed as abusive.⁴¹¹ The IRS designated certain “basket option contracts” as listed transactions and other “basket contracts” as transactions of interest. The IRS was concerned that these contracts have the potential for tax avoidance because they may result in the improper deferral of income or improper categorization of income as long-term capital gain. In particular, the IRS focused on contracts that do not hold static assets, so that the referenced property changes over time, and in which the taxpayer or designee has some amount of control over the components of the underlying contract. Although the IRS admitted not having

409. *Fact Sheet: Treasury Actions to Rein in Corporate Tax Inversions*, U.S. DEP’T OF TREASURY (Sept. 22, 2014), <https://www.treasury.gov/press-center/press-releases/Pages/jl2645.aspx> [<https://perma.cc/H6JM-2J8Z>].

410. I.R.C. §§ 1.6011-4, 6111, 6112 (2012).

411. Notice 2015-73, 2015-46 I.R.B. 660, Notice 2015-74, 2015-46 I.R.B. 663, *revoking* Notice 2015-47, 2015-30 I.R.B. 76, Notice 2015-48, 2015-30 I.R.B. 77.

sufficient information about basket contracts to determine whether they should be identified as tax avoidance transactions, the IRS required they be disclosed and the IRS retained discretion to remove these transactions from the list after more information is gathered.

These notices were not unexpected. The IRS issued a legal advice memorandum in 2010 challenging the contracts' characterization as options for tax purposes and the Senate has critiqued their use.⁴¹² However, within months of issuing the notices the IRS had issued new notices, revoking the old ones. The new notices provided greater detail and discussion of the types of transactions to be covered but created a trail of law that is harder to follow than would have been necessary if all of the information had been in the first issuance. And that trail was created without formal public input.

Following a contract's designation as a listed transaction, if the IRS chooses to enforce failure to comply with the listed transaction rules, then the punishment would open the door to a procedural challenge.⁴¹³ However, penalties are not the only goal of designating activities as listed transactions. As the law firm Mayer Brown notes,

Historically, the IRS has used the reportable transaction disclosure regime not only as a warning to taxpayers . . . who are considering engaging in the transactions, but also as a means to collect preliminary information to aid in the future examination of taxpayers that have already implemented the structures.⁴¹⁴

To the extent the IRS accomplishes its objective without imposing the penalty, the notice is not reviewable.

Despite the existence of this information-gathering objective, taxpayers are unlikely to be able to challenge the procedure behind the creation of these rules until the IRS enforces them against a taxpayer.⁴¹⁵ The Anti-Injunction Act and Declaratory Judgment Act almost certainly will be held to prohibit review because the rules are closely tied to the

412. Office of Chief Counsel, IRM, to Area Counsel, Hedge Fund Basket Option Contracts, A.M. 2010-005, Oct. 15, 2010; Senate, Permanent Subcomm. on Invest., *Abuse of Structured Financial Products*, at 6–8 (July 22, 2014).

413. I.R.C. § 6707A (2012).

414. *Out-of-the-Money: The IRS Designates Basket Options as Listed Transactions and Transactions of Interest*, MAYER BROWN (July 24, 2015), <https://m.mayerbrown.com/files/Publication/4f8936ef-7748-4fdd-9ce4-1160ee83be65/Presentation/PublicationAttachment/20ea76ae-2f3d-442c-afcc-2351b96b8687/150716-UPDATE-CHI-Tax.pdf> [<https://perma.cc/35AL-97T2>].

415. This concern was also noticed by Skadden, Arps, Slate, Meagher & Flom LLP. *Challenging the IRS Anti-Inversion Notice: A Hollow Threat* (Jan. 2015), <https://www.skadden.com/insights/challenging-irs-anti-inversion-notice-hollow-threat> [<https://perma.cc/ZB74-84LK>].

“assessment and collection” of federal revenue. Moreover, even with a claim that the notices violate the APA, it is unlikely a court would find this type of notice “a final agency action” under section 704 as is necessary to give rise to APA review.

What is more troubling is the extent to which guidance may alert taxpayers of future changes in regulations and, therefore, change behavior but may not be used for enforcement. For example, the IRS sometimes issues notices warning of future regulations that may or may not ever be issued. To the extent taxpayers voluntarily comply with the notice, if only because of the threat that future regulations will be retroactive back to the notice, it has changed behavior in the same way as would an enforceable rule. However, the notice is arguably not subject to review. With a significant exercise of government power, a practical but not justiciable injury is caused.

Similar problems of changing taxpayer behavior without the public’s input in the formation of the rule exist with the issuance of temporary regulations. Temporary regulations often have effective dates as of their issuance although proposed regulations are simultaneously proceeding through notice-and-comment. These temporary regulations are only somewhat more likely to be reviewed by courts than are notices. Kristin Hickman notes how temporary regulations are unlikely to face successful challenge because they will be turned into permanent regulations before litigation is complete.⁴¹⁶ Litigation is often slow, but the process of taking regulations from temporary to final “usually takes about a year.”⁴¹⁷

The procedural problem could render the succeeding regulations invalid, but that is not always the case.⁴¹⁸ For many courts, whether to overturn the final regulations depends upon whether the agency kept an “open mind” when considering comments or demonstrated its responsiveness to the public.⁴¹⁹ Michael Asimow, for one, criticizes the invalidation of a rule that completes notice-and-comment just because a prior one failed to do so.⁴²⁰ Nevertheless, without some consequence to

416. Hickman, *A Problem of Remedy*, *supra* note 8, at 1190–91.

417. *Id.*

418. *Fed. Express Corp. v. Mineta*, 373 F.3d 112, 120 (D.C. Cir. 2004); *Mortg. Inv’rs Corp. of Ohio v. Gober*, 220 F.3d 1375, 1378–79 (Fed. Cir. 2000); *Nat. Res. Def. Council, Inc. v. EPA*, 683 F.2d 752, 767–68 (3d Cir. 1982).

419. *Gober*, 220 F.3d at 1379; *Advocates for Highway & Auto Safety v. Fed. Highway Admin.*, 28 F.3d 1288, 1292–93 (D.C. Cir. 1994); *Levesque v. Block*, 723 F.2d 175, 188 (1st Cir. 1983).

420. Asimow, *supra* note 74, at 725–27. Although forms of guidance other than regulations are often issued by the IRS, they do not go through notice and comment on the grounds they are interpretive, and it is questionable whether they would survive a challenge under the APA. Rulings

using temporary regulations, the agency is likely to continue changing public behavior before the public has the opportunity to comment.

The issue of using notices to affect taxpaying behavior may better be left to Congress than the courts. In particular when the notices extend tax preferences rather than threaten penalties, the ability may be the heart of agency discretion, especially when the alternative is difficult to administer. Alice Abreu and Richard Greenstein argue that the Treasury Department has a long-standing policy of not enforcing the gross income provision of the Code to its fullest as a matter of agency discretion.⁴²¹ Arguing that this approach is the response of conscientious administrators to practical problems, these authors would likely (although it is unknown for certain) not want to turn this administrative power over to courts who may be less concerned with issues of valuation, liquidity, enforceability, and public understanding. Through its exercise of discretion in the form of notices, the agency can address concerns quickly and efficiently.

The underlying problem, at least for this Article, is not the subject matter of these rules but that the IRS's method of extending these benefits and these burdens does not provide the public an opportunity to comment. Because these rules do not originate in Congress, there is no democratic oversight in the traditional sense. Even when Congress becomes engaged in an issue, as it did with net operating losses, the legislative fix is generally to substantive matters rather than procedural concerns. As a result, tax law is being created behind closed doors. To make matters worse, under the current legislative and prudential restrictions on tax litigation, the process is unlikely to be subject to judicial review.

C. Specific Problems with Denying Early Review

The timing for when courts review procedural claims over tax guidance is problematic. This Part explores some of the problems caused by this litigation occurring after enforcement but does not seek to cover them all. The problems range from those imposed on individual taxpayers, who may or may not owe more in tax, to those imposed on society as a whole. The tax system loses consistency as its guidance is

have less weight than regulations but, according to the IRS, "may be used as precedents" by both taxpayers and the IRS. Treas. Reg. § 601.201(a)(6); Rev. Proc. 89-14, 1989-1 C.B. 814; I.R.M. § 32.2.2.10.

421. I.R.C. § 61 (2012); Alice G. Abreu & Richard K. Greenstein, *Defining Income*, 11 FLA. TAX REV. 295 (2011).

challenged and possibly overturned, and faith in the tax system may be compromised. Pre-enforcement litigation of procedure would not fix all of these problems but would mitigate many of their costs.

The problems created by procedural deficiencies in the tax context are not new and have already received significant attention by the academic community. Michael Asimow claimed in 1991 that the Treasury Department's procedures "leave[] in doubt the validity of numerous temporary and final regulations . . ."⁴²² Kristin Hickman has written about ten articles, many of which are quoted herein, on the issue of Treasury Department and IRS compliance with the APA. With respect to the issuance of binding temporary regulations with the simultaneous issuance of proposed regulations for notice-and-comment, Juan Vasquez and Peter Lowy described this as "obliterat[ing] the APA's notice-and-comment procedures."⁴²³ John Coverdale questioned "what justification the Treasury believes it has for not using notice and comment . . ."⁴²⁴ Juan Lavilla called the Department's actions "particularly remarkable" when compared with other agencies.⁴²⁵

Although there is pushback to the wholesale importation of the APA into taxation, the perception of agency abuse alone should be sufficient to demand action.⁴²⁶ However, delaying litigation over procedural matters until after enforcement, as required by the statutory prohibitions and common law, makes it less likely that these claims will be brought, thereby strengthening critics' claims. Even though the agency created neither cause of the deferral—the statutory or prudential limitations—it is often blamed for the lateness of the litigation.⁴²⁷

A chief problem with the timing of litigation is that it necessarily limits who can bring suit. Only those taxpayers found in violation of the tax guidance and who do not settle their tax liability are able to challenge the procedures behind the creation of the guidance. To reach a stage that permits this litigation first requires exhausting administrative

422. Asimow, *supra* note 73, at 369–70.

423. Juan F. Vasquez, Jr. & Peter A. Lowy, *Challenging Temporary Treasury Regulations: An Analysis of the Administrative Procedure Act, Legislative Reenactment Doctrine, Deference, and Invalidity*, 3 HOUS. BUS. & TAX L.J. 248, 253 (2003); *see also* Hickman, *A Problem of Remedy*, *supra* note 8, at 1160.

424. John F. Coverdale, *Chevron's Reduced Domain: Judicial Review of Treasury Regulations and Revenue Rulings After Mead*, 55 ADMIN. L. REV. 39, 69 (2003).

425. Juan J. Lavilla, *The Good Cause Exemption to Notice and Comment Rulemaking Requirements Under the Administrative Procedure Act*, 3 ADMIN. L.J. 317, 341 (1989).

426. *See supra* note 8.

427. *Id.*

avenues to redress the substantive tax issues.⁴²⁸ Following audit and a determination of deficiency, the taxpayer must challenge the result in the IRS's Appeals Office before being able to proceed to court.⁴²⁹ To choose litigation to permit a court to hear procedural claims, the taxpayer would forego the option of settlement in either audit or on administrative appeal. If the taxpayer raised and won the issue in settlement, settlements are confidential, as are tax returns.⁴³⁰ Thus, with both administrative resolution and settlement, the matter is closed without establishing precedent.

The structure of litigation also means that those who do not owe tax have very few options for challenging guidance's procedures, and not owing tax may result from the IRS's failure to audit for particular issues.⁴³¹ Instead, taxpayers who may be willing to challenge the procedures behind the creation of rules must wait until they are, if ever, assessed penalties. If the IRS does not audit the issue, the procedural claim may never be litigated. With the audit rate currently less than one percent, although higher for certain categories of taxpayers, it is likely many issues that could provoke challenge are not given an opportunity for review.⁴³² Consequently, assuming compliance imposes some cost on complying taxpayers, those who comply will be at a disadvantage compared to those who do not.

In addition, the delay in litigation reduces the value of successful claims. What most taxpayers may gain in litigation is unlikely to offset the expense of the litigation itself. For example, because of the limited benefit of potential remedies the court could impose, Kristin Hickman points out that taxpayers might feel that challenging temporary regulations "is a futile act not worth the effort."⁴³³ Because taxpayers cannot use class actions in tax litigation over tax liability because of the

428. *Quarty v. United States*, 170 F.3d 961, 972 (9th Cir. 1999); *Brennan v. Sw. Airlines Co.*, 134 F.3d 1405, 1412 (9th Cir. 1998); *Bartley v. United States*, 123 F.3d 466, 468 (7th Cir. 1997).

429. First, if the taxpayer does not pay the liability determined to be owed the taxpayer can pursue deficiency litigation in the Tax Court. I.R.C. §§ 6211(a), 6212(a), 6213(a) (2012). Alternatively, a taxpayer can pay the tax the IRS determines is owed and seek a refund. This subjects the taxpayer "to an equivalent to an audit" as the case proceeds in the appropriate District Court or the Court of Claims. I.R.C. § 7422(a); Hickman, *A Problem of Remedy*, *supra* note 8, at 1184–85.

430. I.R.C. § 6103(a). For more on the play of confidentiality, see Hickman, *A Problem of Remedy*, *supra* note 8, at 1185–87.

431. *Debt Buyers' Ass'n v. Snow*, 481 F. Supp. 2d 1, 10, 15 (D.D.C. 2006).

432. *SOI Stats—Examination Coverage—Individual Income Tax Returns Examined*, I.R.S. (2014), <https://www.irs.gov/uac/soi-tax-stats-examination-coverage-individual-income-tax-returns-examined-irs-data-book-table-9b> [<https://perma.cc/VP25-7EAX>].

433. Hickman, *A Problem of Remedy*, *supra* note 8, at 1193, 1206.

individualized results post-assessment, even if the issue has a small impact on many taxpayers, spreading the cost of tax suits is difficult.⁴³⁴ Thus, there might be little incentive to fight how guidance is made.

Disincentives are increased because, unlike in other areas of law that permit pre-enforcement litigation, people are not suing in post-enforcement tax litigation simply to perfect the agency's procedures. Instead, they are suing over their own tax obligations. The personal nature of the result and that the costs are already imposed likely changes the way people perceive the litigation. With pre-enforcement litigation, a judge remanding a case to the agency to correct the procedures would be a victory. In a tax refund or deficiency case, remand is insufficient to accomplish the goal of reducing the taxes owed. If courts are likely to remand procedural matters without vacating the rule, the taxpayer has little incentive to challenge the rules because the personal outcome remains the same.

These limits on litigation reduce the voices that are heard in matters of tax procedure and the substance of the rules themselves. Eliminating a check to ensure compliance with notice-and-comment potentially loses the voices of lower-income and less well-connected individuals because these groups are unlikely to have other routes to influence the Treasury Department.⁴³⁵ There is no guarantee these groups would claim the opportunity to engage in procedural litigation or to participate in notice-and-comment; however, any future absence is no reason to foreclose the possibility. It may speak to a need to permit organizations to litigate and advocate on these groups' behalf. Organizations exist to help taxpayers with the tax filing and audit processes, and they may bring procedural claims in the process of enforcement. Although currently foreclosed from doing so, these organizations should be empowered to engage in pre-enforcement litigation and the submission of comments that would aid their constituents prospectively.⁴³⁶

434. Norton, *supra* note 169 at 624. Taxpayers may seek representative suits, but even if the IRS loses, the IRS may not acquiesce to the judgment. Unless the Supreme Court decides an issue, the IRS is free to continue fighting. *Id.* It is possible to have class action lawsuits over other regulatory matters; for example, there is a class action suit regarding preparer tax identification numbers. See Alistair M. Nevius, *PTIN Class Action Lawsuit Affects All Tax Return Preparers*, J. ACCOUNTANCY (Oct. 13, 2016), <http://www.journalofaccountancy.com/news/2016/oct/ptin-class-action-lawsuit-201615343.html> [https://perma.cc/7Q8Q-VJKP].

435. Mariano-Florentino Cuellar, *Rethinking Regulatory Democracy*, 57 ADMIN. L. REV. 411, 414, 460–61 (2005); Hickman, *A Problem of Remedy*, *supra* note 8, at 1205–06.

436. Leslie Book, *A New Paradigm for IRS Guidance: Ensuring Input and Enhancing Participation*, 12 FLA. TAX REV. 517, 554 (2012).

Until someone is willing and able to litigate procedural issues, people are forced to operate under rules that might have procedural imperfections that would nullify the rule. This means that during the life of the guidance, taxpayers must evaluate the law's substance plus its procedural history as they plan their tax lives. This is an undue burden on taxpayers and, as Richard Pierce warns, the lack of pre-enforcement review may "induce regulatees to comply with a rule, even if they believe the rule to be invalid, rather than to take the risks attendant to noncompliance and a subsequent challenge to the validity of the rule in an enforcement case."⁴³⁷ Taxpayers must evaluate procedure despite courts not applying consistent standards in their evaluation, making it more difficult for non-experts to do so, especially without the judiciary acting as referee.

The evaluation process is complicated by the possibility that a court will apply *Chevron* deference if the court gets past procedural concerns. With *Chevron* deference, courts defer to reasonable agency interpretations of ambiguous statutes.⁴³⁸ Therefore, if a taxpayer misjudges a procedural issue, the taxpayer faces the prospect of the court deferring to the rule even if it is not the best interpretation of the statute. However, notwithstanding its broad language, *Chevron* is not consistently applied.⁴³⁹ Courts do not clearly or consistently apply any of the deference standards, and scholars debate the effect deference has on the outcome of cases.⁴⁴⁰

In particular with respect to tax cases, *Chevron* deference has not always resulted in victory for the government. Although courts defer to the Treasury Department regarding tax matters more than most other agencies receive deference for other issues, courts do not defer nearly as

437. Richard J. Pierce, Jr., *Seven Ways to Deossify Agency Rulemaking*, 47 ADMIN. L. REV. 59, 90 (1995); see also Mark Seidenfeld, *Playing Games with the Timing of Judicial Review: An Evaluation of Proposals to Restrict Pre-Enforcement Review of Agency Rules*, 58 OHIO ST. L.J. 85, 100-01 (1997).

438. *Chevron U.S.A., Inc. v. Nat. Res. Def. Council, Inc.*, 467 U.S. 837, 844 (1984).

439. Ellen P. Aprill, *The Interpretive Voice*, 38 LOY. L.A. L. REV. 2081 (2005); Lisa Schultz Bressman, *How Mead Has Muddled Judicial Review of Agency Action*, 58 VAND. L. REV. 1443 (2005); Evan J. Criddle, *Chevron's Consensus*, 88 B.U. L. REV. 1271 (2008); Mark Seidenfeld, *Chevron's Foundation*, 86 NOTRE DAME L. REV. 273 (2011).

440. Hickman, *Coloring Outside the Lines*, *supra* note 6; Kristin E. Hickman & Matthew D. Krueger, *In Search of the Modern Skidmore Standard*, 107 COLUM. L. REV. 1235 (2007); Richard J. Pierce, Jr., *Democratizing the Administrative State*, 48 WM. & MARY L. REV. 559, 568-69 (2006); Amy J. Wildermuth, *Solving the Puzzle of Mead and Christensen: What Would Justice Stevens Do?*, 74 FORDHAM L. REV. 1877, 1898-99 (2006); Eric R. Womack, *Into the Third Era of Administrative Law: An Empirical Study of the Supreme Court's Retreat from Chevron Principles in United States v. Mead*, 107 DICK. L. REV. 289, 325-28 (2002); Zaring, *supra* note 135 at 170-76.

often to the IRS.⁴⁴¹ Even for the Treasury Department, deference is far from guaranteed. For example, in 2012, in *United States v. Home Concrete & Supply, LLC*,⁴⁴² the Supreme Court reviewed final regulations extending the statute of limitations in a way that applied to a well-known abusive tax shelter.⁴⁴³ Based on judicial precedent, the Court found there was no statutory ambiguity and therefore no need to defer to the Treasury Department.⁴⁴⁴ Congress has since changed the statute to overturn *Home Concrete*.⁴⁴⁵

Similarly, in 2014, in *King v. Burwell*,⁴⁴⁶ the Supreme Court refused to defer to Treasury Department regulations interpreting provisions of the Patient Protection and Affordable Care Act.⁴⁴⁷ Despite finding the language ambiguous, the first step of *Chevron*, the Court then interpreted the provision in a manner “that is compatible with the rest of the law.”⁴⁴⁸ Sidestepping *Chevron*, the Court created its own operational rules on the grounds that, if Congress wanted to assign such power over the new healthcare system to the agency, Congress “surely would have done so expressly.”⁴⁴⁹

Therefore, taxpayers face uncertain outcomes and a level of judicial deference for challenging what they believe are inadequate procedures. They risk financial penalties to do so; however, to receive statutory penalties, taxpayers’ arguments would need to be very weak. The IRS may impose penalties if a taxpayer fails to follow guidance, even for guidance that the Treasury Department claims is interpretive and not subject to notice-and-comment.⁴⁵⁰ However, the application of penalties depends upon the type of guidance and the taxpayer’s reasons for failing to follow them. In other words, a reasonable argument for failing to follow the regulation will not incur penalties. In addition to potential penalties, interest accrues during periods of dispute over the procedures

441. Kent Barnett & Christopher J. Walker, *Chevron in the Circuit Courts*, 115 MICH. L. REV. (forthcoming 2017) (manuscript at 48–49, 51).

442. ___ U.S. ___, 132 S. Ct. 1836 (2012), *superseded by statute*, Surface Transportation and Veterans Healthcare Choice Improvement Act of 2015, Pub. L. No. 114–41, § 2005, 129 Stat. 443, 456–57 (2015).

443. *Id.* at 1839.

444. *Id.* at 1844.

445. § 2005, 129 Stat. 443, 456–57.

446. ___ U.S. ___, 135 S. Ct. 2480 (2015).

447. *Id.* at 2489.

448. *Id.* at 2492 (quoting *United Sav. Ass’n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988)).

449. *Id.* at 2489.

450. I.R.C. § 6662 (2012).

(as well as substantive disagreements), payable only if the taxpayer loses the challenge. Although interest and penalties may toll at various times in the assessment process and during collection proceedings, they generally accrue during administrative challenge.⁴⁵¹

If taxpayers are willing to face these ambiguities and costs, under current law there is a time limit on how long they can make procedural challenges, if only the government remembers to raise the statute of limitations. In general, procedural challenges are limited by the six-year general federal statute of limitations unless a statutory grant prescribes a different time frame.⁴⁵² Underlying this limitation is “a concern for the agency’s interest in prompt review and the public’s settled expectations regarding agency action.”⁴⁵³ Courts have also held that failure to engage in notice-and-comment does not represent a continuing violation of the APA.⁴⁵⁴ This statute of limitations is often held not to be jurisdictional, and some courts have pointed out that the government often fails to make the claim.⁴⁵⁵

Despite the statute of limitations, there remain loopholes within the statute of limitations that would permit the invalidation of regulations on procedural grounds at any time. For example, the general federal statute of limitations is extended for three years after a potential litigant is no longer “beyond the seas” or under “legal disability.”⁴⁵⁶ There is also the issue of when the period starts. For procedural matters, the statute of limitations begins when the rule becomes final; for substantive matters, timing is based on when the agency applies the rule to the challenger.⁴⁵⁷ However, in addition, for many rules, the statute of limitations applies after applying the doctrines of finality, ripeness, and exhaustion, which may be long after publication.⁴⁵⁸ In *Hudson v. Federal Aviation Administration*,⁴⁵⁹ the court held that a statutory sixty-day statute of limitations did not limit challenges to a notice because the notice was not ripe until it was applied in order to allow courts a better opportunity to

451. *Id.* § 6601(a), (b)(5).

452. 28 U.S.C. § 2401(a) (2012).

453. *Schiller v. Tower Semiconductor Ltd.*, 449 F.3d 286, 293 (2d Cir. 2006).

454. *Preminger v. Sec’y of Veterans Affairs*, 517 F.3d 1299, 1307 (Fed. Cir. 2008).

455. *Schiller*, 449 F.3d at 294; *Rocky Mountain Wild v. Walsh*, 216 F. Supp. 3d 1234, 1246 (D. Colo. 2016); *see also* *Wong v. Doar*, 571 F.3d 247 (2d Cir. 2009).

456. 28 U.S.C. § 2401(a) (2012).

457. *Harris v. FAA*, 353 F.3d 1006, 1010 (D.C. Cir. 2004)

458. RICHARD J. PIERCE, JR., *ADMINISTRATIVE LAW TREATISE* § 11.7 (5th ed. 2010).

459. 192 F.3d 1031 (D.C. Cir. 1999).

understand its meaning.⁴⁶⁰ Moreover, late claims are sometimes permitted. For example, it is possible to petition an agency for amendment or rescission of the rule and then appeal, although this is less likely to be successful for purely procedural claims.⁴⁶¹ Thus, the window under the general statute of limitations is not as limiting as one might suppose.

Although it is uncertain what remedies courts will devise for successful procedural claims, one option is to vacate the guidance. This would nullify the guidance for all taxpayers retroactively. Because the agency retains discretion to create a new rule using appropriate procedure, courts cannot simply substitute a rule for the litigating taxpayers so that the taxpayer and others in a similar position are in a tax limbo, potentially hoping for the lapse of the permissible collection period. To the extent vacatur occurs, tax law loses valuable consistency because rules may change long after their issuance. This may also exacerbate differences between those who voluntarily complied with the law and those who either ignored it or planned for the challenge.

An alternative approach is to remand the guidance so that it is changed only prospectively. However, remanding guidance works poorly when the litigation occurs after enforcement action has commenced because the court is dealing with a real taxpayer who needs to know an actual tax result. Nevertheless, the Supreme Court stated in a non-tax case that it did not impose its own interpretation because “Congress is well aware that the ambiguities it chooses to produce in a statute will be resolved by the implementing agency.”⁴⁶²

A reviewing court can order an agency to provide the relief it denied only in the unusual case where the court concludes that the underlying law and facts are such that the agency has no discretion to act in any other manner, and then only when the court concludes that a remand to the agency would produce substantial injustice in the form of further delay of action to which the petition is clearly entitled.⁴⁶³

460. *Id.* at 1034–35.

461. O'REILLY, *supra* note 125, § 15.14. “[C]hallenges to the procedural lineage of agency regulations, whether raised by direct appeal, by petition for amendment or rescission of the regulation or as a defense to an agency enforcement proceeding, will not be entertained outside the 60-day period provided by statute.” *JEM Broad. Co. v. FCC*, 22 F.3d 320, 325 (D.C. Cir. 1994).

462. *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 397 (1999), *quoted in Hickman, A Problem of Remedy*, *supra* note 8, at 1195 n.191.

463. *PIERCE, JR.*, *supra* note 458, § 18.1.

Therefore, generally courts cannot direct the agency's actions because under our separated powers system the agency must create the law. Consequently, when enforcement has begun, remand for the agency to create a new rule poorly addresses the problem for the complaining taxpayer.

Between the difficulty of bringing procedural claims and the lack of value to a litigant who is successful, there is a narrow funnel through which procedural claims must flow. The result is that these cases may be more of a distraction than a true means of remedying procedural inadequacies. The better result may either be to eliminate such challenges by carving tax out of the APA or to permit litigation over procedural matters before the guidance is enforced. In addition, the tax context may necessitate more immediate judicial relief than remand when cases are brought post-enforcement. To gain greater judicial direction, Congress would need to extend to courts the express power to do so.⁴⁶⁴

The current regime also poses the risk that, as taxpayers learn of procedural ambiguities and their own inability to challenge the agency's procedures, taxpayers may lose faith in the tax system and that, in turn, may hurt compliance.⁴⁶⁵ This is not to suggest that permitting the public to comment on tax guidance will increase taxpayers' affection for the tax system. However, foreclosing their voice may have the opposite effect. Additionally, asking the public not to comply with rules issued by the IRS or the Treasury Department in order to create a legal basis for a challenge may threaten the voluntary, compliant tax system. The system must encourage compliance when possible, so courts telling people to deliberately fail to comply hoping to be assessed to permit a challenge to the assessment is antithetical to the system.

464. A similar circumstance could be cases involving the denial of Social Security benefits in which courts occasionally order the agency to take specific action rather than reconsider its decision. In Social Security cases, however, the statute provides courts explicit authority to "affirm[], modify[], or revers[e] the decision . . . with or without remanding the cause for a rehearing." 42 U.S.C. § 405(g) (2012) (cited in Hickman, *A Problem of Remedy*, *supra* note 8, at 1195 n.193).

465. I.R.S. OVERSIGHT BOARD, 2009 ANNUAL REPORT TO CONGRESS 19 (2010) (finding it is important to taxpayers that the I.R.S. fairly enforce tax laws); Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO ST. L.J. 1453, 1497-99 (2003) (stating that punishing free-riders in the context of public goods may help maintain voluntary contributions); Steven M. Sheffrin & Robert K. Triest, *Can Brute Deterrence Backfire? Perceptions and Attitudes in Taxpayer Compliance*, in WHY PEOPLE PAY TAXES: TAX COMPLIANCE AND ENFORCEMENT 193, 194-95 (Joel Slemrod ed., 1992) (noting that perception of general tax compliance is important to individual compliance decisions).

IV. PROPOSALS THAT BALANCE POLICY CONCERNS

If courts permit procedural challenges to tax guidance, this litigation should occur before the guidance is enforced against taxpayers. Although this would likely increase the cost of tax administration, it would improve the law's consistency and better manage the use of the agency's limited resources. Under current rules, pre-enforcement litigation is rare because of the Anti-Injunction Act, the Declaratory Judgment Act, and prudential justiciability constraints. This Part proposes that Congress enact narrow statutory changes to the Anti-Injunction Act and the Declaratory Judgment Act to funnel procedural litigation before the application of tax guidance. Although this proposal does not perfectly address all concerns about the Treasury Department's and the IRS's failure to follow APA procedures, it balances concerns regarding good procedure and good administration of the tax system.

The two changes proposed in this Article are premised on the assumption that procedural litigation will occur. Proper procedure provides the agency and the public the opportunity for voices to be heard but does not guarantee a change in the agency's position. Those voices may, however, change the shape of rules by influencing the way the agency understands the issues. Because the voices only have the power to persuade and to create a record for litigation, the timing of those voices is critical to maximize their value. If a court or Congress carves tax out of the APA, thus denying procedural constraints on agency action, these proposals would be moot.

Together these two proposals remove the statutory block to pre-enforcement litigation and strengthen the case for finality and injuries in fact. The first is a narrow amendment to the Anti-Injunction Act and the Declaratory Judgment Act to permit procedural litigation before the guidance's enforcement. The second proposal legislates the finality of notices and recognizes the harm to non-recipient taxpayers from narrowly tailored and exclusive favorable tax provisions. The first proposal may operate to limit procedural litigation even as the second operates to expand it. They seek to balance the best use of government resources for all taxpayers. To do so, these proposals require congressional action, something that is far from assured in today's political environment. Nevertheless, they are an important step in recognizing that courts cannot make consistent progress in this area without greater assistance from the legislature.

A. *Narrow Exemption to Keep the Default*

Congress intended the Anti-Injunction Act and the Declaratory Judgment Act to support the government's need to "raise revenue for public purposes in the face of citizen recalcitrance;" therefore, any exception to their prohibitions must be evaluated, at least in part, for the extent to which the exception risks revenue.⁴⁶⁶ Procedural litigation before tax enforcement minimally slows the IRS's collection processes, reducing revenue. To minimize revenue loss, exceptions permitting this early litigation must be narrowly drawn and, ideally, facilitate enforcement after the litigation. To accomplish both objectives, this section proposes Congress narrowly amend the Anti-Injunction Act and the Declaratory Judgment Act to permit procedural litigation within a finite number of days, for example ninety days, after tax guidance's publication.⁴⁶⁷ Thereafter, procedural challenges would be foreclosed.

To resolve the issues discussed in this Article without opening floodgates to litigation with unknown consequences, this exception to current statutory prohibitions on pre-enforcement litigation for the "assessment and collection of taxes" is limited to the Treasury Department's and the IRS's compliance with the APA in the creation of tax guidance. In other words, this proposal would permit pre-enforcement litigation of procedural requirements and a judicial evaluation of whether the process used, including the clarity of the statement and the comment period, suffices for APA purposes. For example, commentators who felt the Treasury Department did not properly respond to their comments could begin litigation of that matter before the guidance is enforced.

In its limited form, this proposal purposefully does not repeal the Tax Anti-Injunction Act or the tax exception in the Declaratory Judgment Act. Instead of a wholesale change with unknowable effects, this proposal limits the change to manage the risk of new litigation. The agency has faced significant charges within the last decade, and as it faces the demand to incorporate the APA more fully into its creation of tax guidance, new burdens need to be circumspectly added. Thus, this proposal urges moderation even as it advocates for important changes.

466. Asofsky, *supra* note 158, at 787.

467. Making wholesale changes to the standard would require crafting a line that other courts would need to respect. Alternatively, courts would throw open the doors to tax litigation, something they are unlikely to want to do based on their historic views of tax litigation, and something that is dangerous at a time of an underfunded agency to fight that litigation. Paul L. Caron, *Tax Myopia, or Mamas Don't Let Your Babies Grow Up to Be Tax Lawyers*, 13 VA. TAX REV. 517, 518, 525–26 (1994); Temkin, *supra* note 19.

While addressing pressing concerns, the proposal also forces congressional discussion of its expectations of administrative agencies. Through debates over this statutory change, Congress would have to define the extent to which it wants the Treasury Department and the IRS to comply with the APA and, possibly, determine if there are acceptable differences between the many types of tax guidance. Considering that an open-ended statement permitting pre-enforcement litigation over APA compliance may expand notice-and-comment to every facet of agency life, it may not be unreasonable to expect Congress to take seriously the need to weigh when procedure is most valuable. This line drawing is difficult but not impossible.⁴⁶⁸

There is precedent for narrow exceptions permitting pre-enforcement review similar to those proposed in this Article. To date, however, these exceptions have focused on substantive law issues. For example, the Revenue Act of 1978 made available declaratory judgments to prospective issuers of certain government obligations.⁴⁶⁹ Positing an “actual controversy” to determine whether state or local debt obligations that are not yet issued are taxable rather than tax-exempt, the Tax Court is granted the power to declare whether they are, or are not, tax-exempt.⁴⁷⁰ Not only is the subject matter limited, only the prospective issuer can bring the suit and must first exhaust administrative remedies.⁴⁷¹ Finally, there is a ninety-one-day deadline for filing suit after the IRS mails the determination letter to the state.⁴⁷² This grants the Tax Court jurisdiction, but not without limits, to hear *South Carolina v. Regan*-type cases.

Similarly, the Employee Retirement Income Security Act of 1974⁴⁷³ granted the Tax Court the limited power to grant declaratory judgments for certain issues relating to the qualification of select retirement plans.⁴⁷⁴ Although requiring a case or controversy, this narrow exception

468. For example, with respect to the Tax Injunction Act, which applies to lower federal courts’ review of state tax law, courts persist in drawing distinctions between revenue raising and revenue losing issues, the latter being subject to pre-enforcement review. *See Hibbs v. Winn*, 542 U.S. 88, 108–09 (2004); *Dunn v. Carey*, 808 F.2d 555, 558 (7th Cir. 1986); *Wells v. Malloy*, 510 F.2d 74, 77 (2d Cir. 1975). State level claims permit only constitutional challenges, as there is no equivalent to the APA to require certain procedure.

469. Internal Revenue Amendments, Pub. L. No. 95-600, § 336, 92 Stat. 2841, 2841–42 (1978) (codified at I.R.C. § 7478 (2012)).

470. *Id.*

471. I.R.C. § 7478(b).

472. *Id.*

473. Pub. L. No. 93-406, 88 Stat. 949 (1974).

474. *Id.* § 1041(a), 88 Stat. at 950, (codified at I.R.C. § 7476 (2012)).

permits the court to evaluate the merits of an issue to aid in the creation of retirement plans but only after exhaustion of administrative remedies. In some ways broader than the exception for tax-exempt bonds, any interested party under the regulations can pursue this claim. By creating this type of review, Congress permits those who are interested to seek resolution of matters before enforcement occurs.

In the form of a narrow exception, the language proposed in this Article would reduce the importance of defining the assessment and collection of taxes.⁴⁷⁵ Today, as shown in *Direct Marketing Ass'n v. Brohl*,⁴⁷⁶ judges who want to hear procedural claims must fit the substance of the guidance outside of the assessment and collection of taxes in order to gain jurisdiction.⁴⁷⁷ This alternate path of redefining terms risks broadening the exceptions to the Anti-Injunction and Declaratory Judgment Acts, not only for procedural claims but for all claims. In the process, courts might open Pandora's box to litigation in a way that thwarts the revenue-raising objectives of these acts. A narrow statutorily defined exception acknowledges Congress's goals without the risk of unleashing havoc on tax administration.

By expanding review from current law, the proposal risks reducing the issuance of rules; however, the alternative of delaying litigation encourages the creation of rules that may be overturned by courts.⁴⁷⁸ The only real advantage of delaying litigation is if the litigation never occurs. To prefer that result, one must accept that the existence of guidance is more important than that it be formed consistent with APA procedures, in which case Congress should except tax from the APA. If APA procedures matter in tax, there must be a method to ensure that the procedure is followed.

475. Limiting the language to the narrow processes of assessment and collection as suggested by the court in *Altera Corp. v. Comm'r*, 145 T.C. 3 (2015) would put tremendous pressure on these terms as used in the processes of the Internal Revenue Code as it now operates, because those terms were not so narrowly confided in 1867 when the Anti-Injunction Act was first enacted. Hickman suggests that courts interpret the "purpose of restraining the assessment or collection of any tax" as more specifically and temporally proximate "assessment" and "collection" of taxes. Hickman, *A Problem of Remedy*, *supra* note 8, at 1210. Hickman recognizes this might "push[] the pendulum again back too far in favor of judicial review." *Id.* at 1213.

476. ___ U.S. ___, 135 S. Ct. 1124 (2015).

477. *Id.* at 1133.

478. *See supra* note 60. Not everyone agrees that ossification occurs. Even if ossification produces less guidance, reducing the amount of guidance may be necessary to ensure judicial scrutiny of agency action. *See* Robert A. Anthony & David A. Codevilla, *Pro-Ossification: A Harder Look at Agency Policy Statements*, 31 WAKE FOREST L. REV. 667 (1996); Thomas O. Sargentich, *The Critique of Active Judicial Review of Administrative Agencies: A Reevaluation*, 49 ADMIN. L. REV. 599 (1997); Seidenfeld, *supra* note 437.

Because this proposed exception, although narrow, would open up the government to new litigation claims, limits on the litigation need to be imposed to ensure these claims do not become overly burdensome to the tax system. Moreover, these claims need to be constrained in order to ensure the consistency of the law. Permitting unlimited procedural challenges keeps the law in a state of flux until the end of the window for such challenges, and potentially longer if such challenges are permitted.

To limit the negative impact litigation over tax guidance would have on the agency's revenue-raising function, the proposal suggests a window of time when litigation over procedural issues may proceed. Time limits are often jurisdictional, forcing the dismissal of claims if the time has lapsed, although courts often interpret these limits narrowly.⁴⁷⁹ Thus, after the lapsed period, however narrowly interpreted, procedural claims are foreclosed. This rule precluding future review at the enforcement stage results from a compelling need to achieve consistent application of the tax code on a national basis. For consistency in application, the law needs to be settled; therefore, claims that do not go to the substance of whether the guidance has a statutory basis must be resolved and then put aside.

This limited time frame is consistent with the Administrative Conference of the United States's recommendation. The Conference recommends limiting review for complex areas of law because of the need for regulatory certainty and the presence of unrecoverable costs if the rule is overturned.⁴⁸⁰ "The uncertainty caused by the potential for conflicting court decisions and by the possibility that a rule may be overturned several years after its promulgation can be extremely disruptive of the regulatory scheme."⁴⁸¹ Moreover, limiting the period of review should increase participation in the rulemaking process, bring finality to the administrative process, and conserve administrative resources.⁴⁸²

For example, the statute at issue in *Eagle-Picher Industries v. Environmental Protection Agency*,⁴⁸³ the Comprehensive Environmental

479. See *Adamo Wrecking Co. v. United States*, 434 U.S. 275, 288–89 (1978); *Eagle-Picher Indus. v. EPA*, 759 F.2d 905, 911 (D.C. Cir. 1985); *Nat. Res. Def. Council v. Nuclear Regulatory Comm'n*, 666 F.2d 595, 602 (D.C. Cir. 1981).

480. ADMIN. CONFERENCE OF THE U.S., RECOMMENDATION 82-7: JUDICIAL REVIEW OF RULES IN ENFORCEMENT PROCEEDINGS 3 (1982).

481. *Id.* at 2.

482. *Id.* at 3.

483. 759 F.2d 905 (D.C. Cir. 1985).

Response, Compensation Act and Liability Act of 1980 (CERCLA), provided that:

Review of any regulation promulgated under [CERCLA] may be . . . made within ninety days from the date of promulgation of such regulations. Any matter with respect to which review could have been obtained under this subsection shall not be subject to judicial review in any civil or criminal proceeding for enforcement or to obtain damages or recovery of response costs.⁴⁸⁴

This provision successfully limited the court and the timing in which cases could be heard.⁴⁸⁵ Even though the court grappled with issues of ripeness in its interpretation of its jurisdiction, the court accepted the limit as it applied.

Despite much successful litigation on the topic of time limits, some courts may refuse to accept this type of limitation. For example, courts have ignored these types of limitations when they find petitioners lacked a meaningful opportunity to challenge the action during the review period because of a lack of notice, a lack of ripeness, or confusion in the law as to the proper forum of review.⁴⁸⁶ Similarly, courts may wait to hear challenges until after guidance is applied in order to prove sufficient hardship to warrant review.⁴⁸⁷ But these arguments are carefully scrutinized because of Congress's stated desire to limit the review. Additionally, ripeness is less likely to be a concern within the narrow confines of procedural litigation.

Nevertheless, despite this proposal's focus on procedural issues, some substantive issues would be litigated before enforcement, such as whether the Treasury Department's reading was consistent with the statute. However, the proposal does not close the door on future litigation of those substantive matters as well. Although litigants would lose the ability to litigate over specific APA procedural rights after the window closes, they would retain their right to litigate whether the guidance comports with the language of the statute. In doing so, the proposal seeks to encourage a focused look at procedure at the time guidance is issued and shortly thereafter, and then put the procedure to bed so that attention turns to the guidance's substance.

484. 42 U.S.C. § 9613(a) (1982).

485. *Eagle-Picher*, 759 F.2d at 909.

486. *Recreation Vehicle Indus. Ass'n v. EPA*, 653 F.2d 562, 569 (D.C. Cir. 1981); *Geller v. FCC*, 610 F.2d 973, 977-78 (D.C. Cir. 1979); *Inv. Co. Inst. v. Bd. of Governors*, 551 F.2d 1270, 1282-83 (D.C. Cir. 1977).

487. *E.g.*, *Diamond Shamrock Corp. v. Costle*, 580 F.2d 670 (D.C. Cir. 1978).

One result of the proposal would be that some people initially indifferent or unaware of the guidance will not have the opportunity to litigate procedural matters when later affected by the guidance.⁴⁸⁸ However, this curtailment of claims currently exists, although with longer windows, from the application of the general six-year statute of limitations.⁴⁸⁹ Moreover, shorter windows better balance the competing priorities these issues raise: holding agencies to the standards of the APA but also managing agency and judicial resources and creating reliable tax guidance. Shorter windows also encourage people to participate in the creation of guidance, the purpose for which the procedures were enacted, rather than waiting until after the fact to bemoan the result. This would ultimately strengthen the APA's goal of fostering public involvement in rule-making.

A final question is which courts should hear these claims. Generalist courts are likely preferable for this pre-enforcement litigation because substantive tax knowledge is not required. One could question the appropriateness of delegating federal procedural matters under the APA to a court specializing in substantive tax matters. Furthermore, retaining these cases in general federal courts would likely facilitate uniformity in administrative law as well as remove more of the silo around tax's procedures.

On the other hand, Congress could justifiably give the Tax Court the authority to hear these cases, despite the Tax Court having no particular specialty in administrative law. Although it has not been proven, the Tax Court might be more sympathetic to the difficulty of creating, and the need for, tax guidance. If Congress chose for these matters to be reviewed by the Tax Court, it would need to extend its jurisdiction. Under current law, Tax Court cases must involve refund procedures or other matters specifically granted jurisdiction by Congress.⁴⁹⁰ Therefore, although most tax cases originate in the Tax Court, its jurisdiction does not currently extend to purely procedural claims.

There are risks to this proposal, even for those solely focused on taxpayers' rights. To the extent pre-enforcement litigation grows as a share of the Treasury Department's budget, it reduces the ability to engage in other activities. Those other activities, such as taxpayer education and responding to questions, may provide a larger benefit to

488. See *Graceba Total Commc'ns, Inc. v. FCC*, 115 F.3d 1038, 1040 (D.C. Cir. 1997); *Functional Music Inc. v. FCC*, 274 F.2d 543, 546 (D.C. Cir. 1958).

489. See *Debt Buyers' Ass'n v. Snow*, 481 F. Supp. 2d 1 (D.D.C. 2006).

490. I.R.C. §§ 6213–6214, 7442; I.R.M. § 35.1.1 (Aug. 11, 2004), https://www.irs.gov/irm/part35/irm_35-001-001.html [<https://perma.cc/T7VR-T74R>].

taxpayers than litigation over guidance. The cost in terms of these other activities is greater because of the relative difficulty of cutting funding from, or ignoring, taxpayer litigation. Once litigation is allowed, the agency must devote resources to it if the agency is to retain the guidance. It is the proverbial squeaky wheel that demands resources to oil.

Recognizing that it is difficult to create good guidance and that not everyone has the best of intentions with procedural litigation, this proposal seeks a balance. The proposal seeks to balance the need for guidance created with procedures that are respected by the agency and the public with the need for some limits on tax litigation. To do so, this proposed change would permit procedural litigation that meets the justiciability rules but does not permit this long after guidance has been operational.

B. Recognizing the Injury

Although the first proposal permits pre-enforcement litigation for those who could litigate the issues after the fact, it does not expand the issues to be litigated or the group who may engage in this litigation. To accomplish that feat is difficult, if not impossible. Some of the justiciability limitations that prevent third-party suits and early litigation are constitutional. They cannot be waived even with congressional action. This second proposal accepts that limitation but has Congress legislate recognition of the finality of, and possible injury from, guidance that works to change taxpayer behavior even though not in the form of final regulations. Additionally, Congress's enactment would explain to the courts its understanding of how injuries exist with certain agency action and that third parties may be harmed when other taxpayers are given tax benefits.

First, Congress should statutorily designate the forms of guidance that are subject to review. This list should include regulations and all tax guidance intended to change taxpayer behavior. Others have tied this issue to the deference given to tax guidance or the potential for triggering tax penalties; however, the more critical issue is the ability the agency has to influence behavior with guidance that was not given democratic review.⁴⁹¹

By limiting this proposal to guidance intended to change taxpayer behavior, every agency action will not be subject to notice-and-comment. Only prospective rules are intended to change, as opposed to define, prior action. Additionally, the focus on changing behavior limits

491. Hickman, *A Problem of Remedy*, *supra* note 8.

the guidance subject to review to that altering baseline behavior rather than merely clarifying the application of the law. If Congress does not want a piece of forward-looking guidance to go through notice-and-comment, for example if it wants to facilitate the listing of listed transactions, Congress can exempt the guidance from the APA in its statute.

Consider the following example to clarify the distinction. The IRS issued Revenue Ruling 2001-4 to define the extent an airline can refurbish an airplane and claim a current deduction for the cost rather than booking it as a capital expenditure.⁴⁹² The rule clarifies the application of the law to mitigate taxpayers' need to find an answer. Under the proposal, this clarifying ruling would not be reviewable for testing whether it completed notice-and-comment. On the other hand, the notice warning of impending inversion regulations or the notice classifying transactions as listed transactions are forward looking and changes the law that previously existed. These notices are intended to change behavior and, therefore, the proposal requires they go through notice-and-comment unless an exemption is statutorily provided.

This proposal would have produced different outcomes in some historical cases. It would likely have changed the result in *Cohen*, the case involving refund procedures, because refunds involve past taxpaying behavior.⁴⁹³ Guidance that imposes information reporting obligations would be reviewable depending on what the guidance does. If the guidance imposes new obligations rather than clarifying old ones, the guidance would require notice-and-comment and be subject to pre-enforcement litigation. Thus, the proposal is not a bright-line rule but, nonetheless, imposes greater clarity and order than the existing, evolving common law.

Although subjecting many forms of tax guidance to procedural review, this proposal does not suggest that Congress eliminate the varied forms of guidance. Congress should, however, require that all guidance intended to change behavior be held to the same level of review. In tax-speak, substance should triumph over form. Even if a rule is not in a regulation, it should have the same opportunity for public comment if it has the same impact on the public.

Listing guidance that is subject to the APA's notice-and-comment procedures reduces the likelihood of successful agency defenses on the ground the guidance is not yet ripe. However, the law is not clear in this

492. Rev. Rul. 2001-3, 2001-1 C.B. 295.

493. *Cohen v. United States*, 650 F.3d 717 (D.C. Cir. 2011), *cert. denied*, 135 S. Ct. 946 (2015).

area, therefore congressional opinion may not sway a court. Under current law, non-legislative rules may not be ripe for judicial review, although some non-legislative rules have been determined to be ripe even though the direct injury or harm will not arise until (and unless) enforcement action occurs.⁴⁹⁴ Congressional action cannot undo the uncertainty in this area of jurisprudence but does mitigate it as much as possible.

Second, Congress should legislate that, because of federal budget constraints, all taxpayers are injured by the application of tax reducing guidance.⁴⁹⁵ This is not arguing the government is entitled to all of a taxpayer's income. It is arguing that tax preferences for some are inherently discriminatory against others, although possibly for good reasons. Although it might be politically popular to frame taxes as the taxpayer versus the government, in reality the better view is the taxpayer versus other taxpayers. As one taxpayer pays less in tax, to raise the same amount of revenue tax rates on others must increase. Even without the tax increase, the person who pays less tax has benefited relative to those who do not.

Preferential treatment for some taxpayers receive narrow support from policymakers, while other preferences are created through democratic means. If the benefit is justified, as defined by society, the tax discrimination is fair and appropriate. The issue for this Article is not whether a particular form of favoritism is justified, but who gets to decide if the benefit is justified. When Congress enacts tax preferences, they are democratic even if sometimes unwise. When an agency creates a preference, it is less likely the preference is recognized as of democratic, rather than bureaucratic, origin. Only through the imposition of procedures, such as notice-and-comment, can the public be certain of its voice in the creation of the benefit.

Moreover, this Article argues the procedure for creating the benefit should be subject to the same review as a tax burden would be. The irony of today's system is that people can fight over the creation of tax burdens but not tax relief even though economists conclude they are the same.⁴⁹⁶ To impose a tax on one half of the country is economically equivalent to giving a tax break to the other half. Perhaps it derives from people's fear of loss, but the taxpaying public is more passive to benefits given to others. This proposal ignores that sentiment and recognizes the

494. Compare *Nat'l Park Hosp. Ass'n v. Dep't of Interior*, 538 U.S. 803, 808–11 (2003), with *Sabre, Inc. v. Dep't of Transp.*, 429 F.3d 1113, 1120–21 (D.C. Cir. 2005).

495. For the recognition of the likely prudential challenges, see Part IV.

496. See discussion *supra* note 277.

economic equivalence—not preventing either taxes or preferences but holding both to the same procedural standard.

Through these two additions to existing statutory language, Congress strengthens the claim for the public to litigate procedural matters in tax guidance. This would open the door to court for rules that might otherwise never face judicial challenge. In the process, it furthers one purpose of the APA, to ensure the public's involvement in the creation of the rules affecting the public by pushing them into a more democratic process. Not only would the litigation be more democratic because of more participants, it encourages the agency to adopt more democratic procedures.

Thus, one point of this second proposed change is to increase the amount of litigation the IRS faces. In doing so, it would impose a cost on the tax system. That cost should be weighed in the decision to accept this proposal; however, it is a necessary cost if the government is to hear relevant procedural claims. It is an example of the necessary balancing of individual equity and administrability that must be undertaken if the tax system is to function fairly. To the extent that guidance has a negative effect on others, those others should be given the opportunity to voice their complaints in a meaningful way about the undemocratic nature of the guidance's creation. Although these complainants can go to Congress, access to courts offers the possibility of more meaningful review, as recognized by the creation of the APA itself.

Broadening the litigation pool is not without risk, however. Not only is it costly, permitting the voice of those not directly affected by guidance might have the unintended consequence of making it a tool for entrenchment. Regulatory capture theories suggest that businesses and the wealthy might influence policies not directly of interest to themselves in order to further their own interests in other ways. In tax, it is possible well established groups might litigate in order to free up revenue to fund their own projects or because of a dislike of those with less power. In other words, in a world of unintended consequences, opening the door to speakers does not guarantee the voices one would want or what those voices will say. Litigants may usurp courts to engage in a “kind of private conscription of public resources . . . that undermines a fully democratic effort . . . to allocate . . . limited [agency] resources to the most serious problems.”⁴⁹⁷

This risk of usurpation is not specific to litigation over procedural matters and is of less concern in this context because the stakes are

497. Sunstein, *supra* note 231, at 631.

relatively low. In other words, there is less risk of people engaging in pre-enforcement procedural litigation for reasons other than a concern with process because it is a narrowly defined exception to the prohibition on pre-enforcement litigation and should only change how rules are made rather than necessarily their substance. Making this incremental change to the Anti-Injunction Act and Declaratory Judgment Act provides an experiment to see exactly how the public will respond without a risk to the system overall.

Even if Congress is persuaded to enact these changes, the future of the litigation would likely have an uphill judicial battle. As discussed in Part II, courts do not always recognize a connection between tax expenditures and spending much less between those who benefit from tax expenditures and those who do not. “Bare procedural violations” without a direct harm do not satisfy the injury in fact requirement; however, the proposal goes further and argues that an actual particularized injury occurs, although one that exists for all recipients of government programs.⁴⁹⁸ The constitutional requirement of injury in fact makes it harder to gain access for third-party suits in the tax context other than in the particular factual situation of *Flast*, and this proposal attempts to supply that injury. But courts may dismiss the harm.

Although some courts may be reluctant, others may accept this as an opportunity to hear cases they are already moving to hear. Courts at times have been open to future harms or probabilistic harms as creating the requisite injury in fact. For example, in 2010 in *Monsanto Co. v. Geertson Seed Farms*,⁴⁹⁹ an agency approved unconditional deregulation of a particular genetically modified alfalfa plant without a study required by law.⁵⁰⁰ Growers of conventional alfalfa sued on the grounds the deregulation violated the enabling statute. The lower courts sided with the conventional alfalfa growers and enjoined the planting of the modified alfalfa. Although reversing the injunction, the Supreme Court upheld the farmers’ standing even though their injuries were characterized by marketers as alleged risks of future contamination. On the other hand, in 2009, in *Summers v. Earth Island Institute*,⁵⁰¹ the Court held there was no standing for plaintiffs after the Forest Service approved a salvage sale of tracts of national forest land because there were no particularized affidavits to prove the injury in fact.⁵⁰² The

498. See *Spokeo, Inc. v. Robins*, __ U.S. __, 136 S. Ct. 1540, 1549 (2016).

499. 561 U.S. 139 (2010).

500. *Id.* at 152–55.

501. 555 U.S. 488 (2009).

502. *Id.* at 494–96.

determination of standing in these cases is very much facts- and circumstances-specific so it is impossible to predict with certainty how courts will respond to this proposal. Nevertheless, with the current trend toward permitting procedural tax litigation, Congress should use the opportunity to make the litigation as comprehensive as possible.

Courts generally permit Congress to limit prudential limitations and have respected congressional grants for citizen suits. For example, in *Bennett v. Spear*,⁵⁰³ the Supreme Court addressed the citizen suit provision of the Endangered Species Act (ESA) that authorizes “any person” to sue to challenge certain violations of the act.⁵⁰⁴ The Fish and Wildlife Service had issued an opinion on a reservoir; ranch operators and irrigation districts sued arguing the Fish and Wildlife Service did not use best scientific and commercial data available to create the rule as required by the ESA. The Court recognized that the ESA’s broad authorization of people to bring suits overturns the prudential requirement that the person’s interests be within the zone of interest protected by the statute.

Therefore, to succeed, this proposal needs Congress to expressly state that it intends to waive the agency’s common law defenses to pre-enforcement litigation in order to permit procedural claims by any person. Additionally, Congress must acknowledge that guidance intended to shape taxpayer behavior, even if designated by the agency as interpretive, is final for review. Finally, courts must recognize the statement as explaining that harms are, in fact, created when the Treasury Department or the IRS creates targeted preferences or anticipatory guidance to permit review.

To be clear, this proposal does not vest judicial power over the policy choices contained within the guidance. Instead, the proposal provides that agencies cannot extend the law without using the same proper procedure necessary for all rules. In doing so, the proposal creates a more reasonable and fair tax system for everyone involved. The same tools that the APA extends to the public in other contexts would be employed in tax, and the judiciary would be recognized as the best means of following through with procedural challenges.

CONCLUSION

The Treasury Department and the IRS are given substantial discretion in creating the rules that implement the tax system. However, that

503. 520 U.S. 154 (1997).

504. *Id.* at 162–64.

discretion is circumscribed by the APA, which demands procedures for the exercise of agency discretion. Unless Congress limits the application of the APA, the issuance of rules must be according to the arduous procedure laid out in statute. This is not an endorsement of forcing everything agencies do to go through notice-and-comment. However, until Congress legislates otherwise, courts must decipher what the APA requires for every piece of tax guidance, and taxpayers and the agency are left in limbo not knowing when notice-and-comment applies.

Tax's special statutory limitations and limited standing rules that prohibit pre-enforcement litigation highlight the historical exceptionalism of the tax system. If the tax system is now to operate like every other administrative system, the procedural rules protecting it need to be carefully evaluated to ensure they work in the new world order. The worst of all worlds is to create procedural challenges that can only be used by those seeking last-ditch efforts to eliminate their personal tax liabilities rather than trying to create a just and democratic tax system. If the old system is to be dismantled, the dismantling should be thoughtfully done.

With the more frequent application of the APA to tax matters and the impact this has on the legitimacy of tax guidance, it has become clear that the litigation over procedures needs to occur before widespread reliance on the guidance. To permit this pre-enforcement litigation will require statutory change. That change needs to be circumspect because litigation imposes risks on the existence of the guidance itself and, perhaps more importantly, the tax agency's budget. In a world of shrinking budgets, the Treasury Department currently spends three and one-half percent of its budget creating guidance.⁵⁰⁵ Although the Department of Justice handles most tax litigation, a portion of the Treasury Department's tax enforcement budget is spent on litigation support. Broadening exceptions to permit ever more litigation may prevent the IRS and the administration from engaging in other, equally valuable efforts for taxpayers because litigation is not the end sought but the more democratic creation of guidance.

That the proposals contained herein would increase the amount of litigation might bankrupt the tax system in much the same way as simply repealing the Tax Injunction Act. However, these narrow proposals are a necessary protection for taxpayer rights when accepting that procedural attacks will be permitted. And they do so in the narrowest way possible. If drug manufacturers deserved pre-enforcement understanding of the

505. U.S. DEP'T OF THE TREASURY, THE BUDGET IN BRIEF 13–14 (2015).

law that was to apply in *Abbott Laboratories*, so too should taxpayers be entitled to that same information. Encouraging taxpayers to break the law in order to test its procedural integrity is a poor way to encourage faith in the federal tax system.