

CHAPTER

1

Legislative Sources of Authority

Learning Objectives

1. Distinguish between primary and secondary tax authority.
2. Understand the historical development of the tax law.
3. Describe the legislative process for a tax bill.
4. Detail the organization of the Internal Revenue Code.
5. Differentiate substantial authority and reasonable basis in tax practice.

¶1001

Introduction

Traditionally, tax practice is divided into three distinct components: research, planning, and compliance. But these are not mutually exclusive categories, and one of the purposes of this text is to demonstrate the relationships of all three activities.

The first half of this course is devoted to tax research, the process of examining various primary and secondary sources to determine the answer to a tax question. The last half of the course is devoted to tax planning, the orderly process of arranging one's affairs to minimize tax liabilities. But successful tax planning strategies often depend on solid research so that the strategy chosen will withstand judicial scrutiny.

Tax research and planning are also a significant part of the compliance work in contemporary tax practice. For example, changing accounting methods may require extensive research to develop a justification to the IRS for the change, and may require a substantial tax planning effort to determine which change is most tax-benefit efficient. Only after these questions are answered can the complex compliance task of completing Form 3115

(Application for Change in Accounting Method) and accompanying schedules describing the change be completed.

This text is devoted primarily to tax research and tax planning. The first three chapters introduce the major sources of legislative, administrative, and judicial authorities, collectively known as **primary authority**. The first type of tax authority, legislative authority, is discussed in the remainder of this chapter. Chapter 4 introduces the various print and electronic tax services that aid practicing tax professionals in locating the answer to a tax research, planning or compliance question. Chapters 5 through 8 expand the discussion of tax authority, and review quite a bit of tax law as well, by examining the landmark judicial decisions involving income; deductions; property transactions; and accounting records, methods, and income allocations.

The last half of the text is devoted to procedural issues and tax planning strategies. Chapter 9 reviews the maze of administrative and procedural constraints dominating contemporary tax practice, including taxpayer and preparer penalties. Chapter 10 provides an anatomy of a tax engagement, from beginning to end, with a special emphasis on tax communications. Chapters 11 through 16 introduce common and not-so-common tax planning strategies related to individuals, retirement, basic and advanced transfer tax issues, choice of business entity, and small closely-held businesses.

Finally, the last two chapters of the text introduce two broader aspects of contemporary tax practice. First, Chapter 17 introduces the role of taxes in financial accounting issues by reviewing the tax accrual and the impact of FASB 109 and FIN 48. And lastly, Chapter 18 examines the debate over tax reform by examining the pros and cons of various tax reform ideas proposed in recent years.

¶1003 An Introduction to Tax Authority

.01 PRIMARY VS. SECONDARY TAX AUTHORITY

In researching a tax question, it is extremely important to understand the difference between primary tax authority and secondary tax authority. Although both sources may be consulted in attempting to find the answer to a tax question, the actual answer must always relate to a primary authority.

Primary tax authority, the “official” body of tax law, consists of the Internal Revenue Code as drafted by Congress, Regulations and other pronouncements of the Department of the Treasury, and judicial decisions devoted to tax issues. The answer to a tax question must necessarily be traced back to a primary tax authority.

Secondary tax authority refers to various “unofficial” sources of tax information, such as textbooks, journal articles, commentaries, tax service editorial comments, and even this text. Secondary services are primarily devoted to finding, interpreting and explaining primary authority. These sources, while possibly being very informative and technically accurate, do not represent the tax law and should not be used to justify a position taken on a tax return.

.03 LEGISLATIVE, ADMINISTRATIVE AND JUDICIAL AUTHORITIES

Primary tax authority may be broken into three categories: legislative, administrative, and judicial. **Legislative authority** refers to tax authority enacted by the legislative body, the United States Congress. Tax bills passed by Congress are added to *Title 26* of the U.S. Code and have the force and effect of law, unless they are found to be unconstitutional. As explained later in this chapter, legislative authority also includes the various committee reports issued by the tax-writing committees in Congress, as well as tax treaties involving the United States.

Administrative authority includes all pronouncements of the administration currently controlling the Presidency. Most tax administrative authority is drafted by the Department of Treasury and one of its major divisions, the Internal Revenue Service (IRS). The

primary administrative authority is the tax Regulations, the official interpretations of the tax law by the Treasury and the IRS. Other sources of administrative authority, discussed in Chapter 2, are revenue rulings, revenue procedures, letter rulings, and various other notices and announcements.

Judicial authority refers to decisions of the federal courts on tax matters. As discussed in Chapter 3, a number of courts are asked to decide tax controversies, and these interpretations of the tax law are important components of tax authority. One court, the U.S. Tax Court, is devoted solely to tax cases, while other courts, such as the U.S. District Court and the Court of Claims, hear all kinds of civil and criminal cases, including some tax cases. U.S. Circuit Courts of Appeal, and to a lesser extent the U.S. Supreme Court, may hear tax cases as well.

¶1005 Legislative Authority: A Historical Perspective

The power to tax is specifically defined in the Constitution. Article 1, Section 4, Clause 1 states that “*The Congress shall have the power to lay and collect taxes, duties, imports and excises, to pay the debts and provide for the common defense and general welfare of the United States.*” But this power has not always been exercised by Congress. The following discussion provides a chronological record of taxation in the United States and highlights several concepts that remain important in contemporary tax practice.

- **1643.** The first attempt to tax incomes in the United States was in 1643, when several colonies instituted what was called a *faculties and abilities tax*. This was a modest tax, with tax collectors literally going door to door and asking if the individual had income during the year. If so, the tax was computed on the spot. Needless to say, there were substantial compliance problems with this system.
- **1700s–1800s.** In the early 1700s and well into the 1800s, a number of the southern colonies and states adopted an income tax modeled on the tax instituted in England. This was basically a tax on income, and not on property. The British theory was that you tax the income from property, and not the property itself (i.e., “tax the fruit, but not the tree.”) Thus, gains or losses on sales of property were not subject to taxation.
- **1861–1873.** In 1861, the Union enacted the first federal income tax, designed to help finance the civil war. Tax rates were three percent on income exceeding \$600 and less than \$10,000, and five percent on income exceeding \$10,000. The tax, though modest, did provide substantial funds for the war effort. After the war when the need for federal revenues decreased, Congress let the tax law expire in 1873.
- **1880.** During the 1870s, a number of individuals had challenged the validity of the federal income tax. In 1880, one of these cases had worked its way to the U.S. Supreme Court. In *Springer vs. U.S.*,¹ the taxpayer contended that the income tax on his professional earnings and personal property income violated the “direct tax” requirement of the Constitution. At this time, it was hard for the Supreme Court to be interested in a case involving a tax that expired seven years earlier, and perhaps to avoid the chaos that a decision for the taxpayer would generate, the Court unanimously sided with the government. In effect, the Supreme Court concluded that the income tax was an excise tax, and not a capitation tax (based on population) or a property tax.
- **1894.** By 1894, Congress’s appetite for more revenues had increased, so a new tax law was passed that year. This was a controversial provision, and the law passed with the signature of President Grover Cleveland. The tax, though modest, received much more attention during times of peace.
- **1895.** Once again, a taxpayer challenged the legality of the income tax. In *Pollock v. Farmers’ Loan and Trust Co.*,² a taxpayer sued the corporation in which he owned stock,

¹ *Springer vs. U.S.*, 102 US 586.

² *Pollock v. Farmers’ Loan and Trust Co.*, 158 US 601.

contended that they should never have paid the income tax because it was unconstitutional. In this case, the tax was paid on income from land, and Pollock argued that since a tax on real estate is a direct tax, a tax on the income from such property must be a direct tax as well. And since the Constitution prohibits a direct tax unless certain conditions are met, the income tax should be declared unconstitutional. The direct tax argument was also used by *Springer* in 1880, but now the Court focused more closely on the possible conflict with the Constitution. The provision in question was Article 1, Section 9, Clause 4 of the Constitution. This clause stated the following:

1. “But all duties, imposts, and excises shall be uniform throughout the United States.”
2. “No capitation, or other direct tax shall be laid, unless in proportion to a census or enumeration herein before to be taken.”

In effect, this clause required any direct tax to be based on a census. For example, if the government desired to raise \$10 million, and New York had 20 percent of the total U.S. population at that time, then New York would be required to raise \$2 million. And if New York had 1 million residents, each resident would owe \$1 in taxes. Obviously, a tax based on income could not achieve such proportionality, since incomes differed across individuals. This time, in a 5-4 decision, the Supreme Court ruled that the income tax was unconstitutional. A few days after the initial vote, the Court revoted and reached the same result. Thus, the tax law was ruled unconstitutional, and was effectively repealed.

- **1909.** Congress took two actions in 1909 to deal with their increasing revenue needs. First, they passed a corporate income tax, but labeled it an excise tax on the privilege of doing business. The tax was set at one percent on all incomes exceeding \$5,000. Secondly, Congress passed the 16th Amendment, which would eliminate the apportionment requirement. This amendment reads as follows:

“The Congress shall have the power to lay and collect taxes on incomes from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration.”

- **1911.** The U.S. Supreme Court upheld the corporate “excise tax” as constitutional in *Flint v. Stone Tracey*.³ The court ruled that the tax was a “special excise tax on the privilege of doing business.”
- **1913.** The required three-fourths of the states ratified the 16th Amendment, thus adding the amendment to the constitution. Congress then immediately enacted the first “constitutional” tax law, the *Revenue Act of 1913*. The tax ranged from one percent on income exceeding \$3,000 to seven percent on incomes exceeding \$500,000. For the first time, this statute introduced the notion of a **progressive tax rate** structure (i.e., the tax rate increases as the base, income in this case, increases).
- **1916.** The U.S. Supreme Court upheld the progressive income tax as constitutional in *Brushaber v. Union Pacific Railroad Co.*⁴
- **1916–1939.** During this period, Congress passed a total of 17 different revenue acts devoted to taxation. These were all independent pieces of legislation, as Congress did not bother to eliminate inconsistencies, deadwood provisions, or modifications contained in prior acts. Thus, a person trying to find the answer to a tax question would need to search all 17 Acts. Congress solved this problem in 1939 by merging all of the acts into one cohesive body of tax law titled the *Internal Revenue Code of 1939*. The term “Code” was used to signify that all prior acts had been “codified” into a single location, with inconsistencies and deadwood provisions eliminated.
- **1954.** Following numerous amendments to the Code after 1939, Congress decided to once again reorganize the Code. Amendments were merged into the Code, the

³ *Flint v. Stone Tracey*, 220 US 107.

⁴ *Brushhaber v. Union Pacific Railroad Co.*, S Ct, 1 USTC ¶4, 240 US 1, 36 S Ct 236.

organization was changed to flow more logically, and the title was changed to the *Internal Revenue Code of 1954*.

- **1986.** Following major changes in the Code as part of the Tax Reform Act of 1986, Congress decided to change the name of the Code to the *Internal Revenue Code of 1986*. However, the organizational pattern of the 1954 re-codification was retained, so in essence the 1986 change was in name only.
- **1993, 1996, 2001, 2004.** Major tax legislation was enacted in each of these years, amending the Internal Revenue Code

This brief historical review provides insight into a number of current Code provisions encountered in tax practice. For example, when determining “earnings and profits” of a corporation for purposes of classifying dividends, no amounts prior to March 1, 1913, are included (this is the date of enactment for the *Revenue Act of 1913*). Similarly, if a taxpayer is forced by the IRS to make an accounting methods change, the cumulative adjustment to income required for such a change will not include any amounts generated prior to 1954 (the date of the second codification of the Code).

OBSERVATION

The 1954 re-codification involved an extensive reordering and renumbering of the Code. For example, Sec. 17(j) of the 1939 Code is now Code Sec. 1231 under the 1954 reorganization. Practitioners researching questions involving statutes enacted prior to 1954 need to cross-check Code reference numbers between the two codes. Most major tax services furnish tables providing these cross references.

¶1007 The Legislative Process

.01 INTRODUCTION

Benjamin Disraeli, a famous British politician of the 19th century, once commented that “*There are two things one should never watch: sausage-making and tax legislation.*” The process is indeed complicated, and the path to final passage is often torturous and filled with back-room deals and hidden agendas. Nonetheless, taxes are an important part of everyday life today, and, as Justice Oliver Wendell Holmes once said, “*Taxes are the price we pay for a civilized society.*”

It is important to understand how the legislative process operates, not only from a historical perspective but also from the need to understand how several important by-products of the process are important sources of legislative authority. But before examining the process in detail, perhaps one question should be asked: Exactly what *is* a tax? How is a tax defined?

.03 DEFINITION OF A “TAX”

There have been many definitions of a tax over the years, but perhaps the most succinct and accurate definition was coined by Ray Sommerfeld years ago: *A tax is a nonpenal yet compulsory transfer remitted for the public good.*⁵

Each phrase in this definition is important. First of all, a tax is not a penalty; in theory, taxpayers receive something of value in return, such as those elements of a civilized society referred to by Justice Holmes. Secondly, even though we describe our tax system as a “voluntary self-assessment system,” in reality the system becomes rather involuntary (fines, jail sentences, etc.) if one does not pay his or her share of taxes. So taxes are indeed compulsory transfers. Finally, the exact use of taxes collected by the government is not specified in advance; rather, such collections are used for the public good. The determination of the public good is made by Congress as part of the separate budget process.

⁵ Sommerfeld, Ray, M, Hershel M. Anderson, and Horace Brock, *An Introduction to Taxation* (Harcourt Brace Jovanovich, Inc., 1967), 2.

.05 THE LEGISLATIVE PROCESS—ORIGINS OF A TAX BILL

Although individual members of Congress sometimes author important pieces of a comprehensive tax bill, as a practical matter the process is usually driven by the Administration currently in power. Generally, the staffs of the Department of Treasury are heavily involved in crafting the wishes of the Administration into tax policy, and the initial draft of the bill is presented by the Secretary of the Treasury to Congress. This large bureaucracy includes a number of highly-skilled economists, attorneys, accountants, statisticians, and other professionals.

There are other important players at the beginning of the legislative process. Perhaps more than any other group, the staffs of the two tax writing committees described below (House Ways and Means and Senate Finance Committees) have a major influence on tax legislation. These are bright, highly-skilled individuals with extensive tax knowledge, though generally not much practical experience. Each of these staffs number in excess of 100. In addition, various think tanks, nonprofit organizations and lobby groups manage to leave their imprints on tax legislation as well.

Another key player in the legislative process is the Joint Committee on Taxation (JCT). This committee has 10 members composed of the 5 ranking members of the House Ways and Means and Senate Finance Committees. But it is really the large and experienced staff of this committee that does the heavy lifting in the tax process. JCT staffers work with the two committees in drafting bills and committee reports. They also draft a final report on the new laws after enactment, generally referred to as the “Blue Book,” which is discussed below.

OBSERVATION

All of these players in the tax process are sometimes referred to as the “kitchen bureau,” in that all are trying to serve as cooks in the same kitchen.

.07 THE LEGISLATIVE PROCESS—THE HOUSE OF REPRESENTATIVES

Article 1, Section 7 of the Constitution requires that all tax bills originate in the House of Representatives. The first stop is the House Ways and Means Committee, the primary group devoted to revenue measures. This committee has had a varying number of members over the years, and (1) the membership is apportioned based on the relative numbers of the two parties in the house, and (2) the chair is from the majority party. **Figure 1** lists the members of the committee for the 110th Session of Congress, which began its two-year session in January, 2007.

OBSERVATION

Although the Constitution states that all revenue bills must originate in the House, this did not occur in 1982. In that year House Democrats insisted that if the Reagan Administration wanted to raise taxes that year, then they should start the bill in the Senate, which was controlled by the Republicans. Democrats were still smarting from the publicity given the Republicans for cutting taxes in 1981, and when a desperate need for raising revenues occurred in 1982 due to ballooning deficits, they wanted to make sure that the Republicans received “credit” for raising taxes.

The first order of business for the House Ways and Means Committee upon receiving a tax proposal is to call public hearings. Anyone can submit written testimony, but the Committee decides who will provide oral testimony. By tradition, the Secretary of the Treasury is the first person to testify on the proposed legislation.

Following the public hearings, the Ways and Means Committee “marks up” the bill and begins debate on the merits of the bill. These hearings are open to the public (including the cameras of *C-SPAN* and other organizations), although closed sessions are sometimes

called for the real horse-trading phase of the process. Eventually, the Committee will vote on the bill, which at this stage may look very different than the “marker” that was laid down at the start of the process. If a simple majority passes the bill, it is sent on to the floor of the full House of Representatives. If the bill is defeated, it is essentially dead for this session of Congress.

Figure 1

110th Congress - House Ways and Means Committee (by Seniority)	
Democrats	Republicans
Charles B. Rangel, New York (Chair) *	Jim McCrey, Louisiana *
Fortney Pete Stark, California *	Wally Herger, California *
Sander M. Levin, Michigan *	Dave Camp, Michigan
Jim McDermott, Washington	Jim Ramstad, Minnesota
John Lewis, Georgia	Jim Nussle, Iowa
Richard E. Neal, Massachusetts	Sam Johnson, Texas
Michael R. McNulty, New York	Philip S. English, Pennsylvania
John S. Tanner, Tennessee	J.D. Hayworth, Arizona
Xavier Becerra, California	Jerry Weller, Illinois
Lloyd Doggett, Texas	Kenny Hulshof, Missouri
Earl Pomeroy, North Dakota	Ron Lewis, Kentucky
Stephanie Tubbs Jones, Ohio	Kevin Brady, Texas
Mike Thompson, California	Thomas M. Reynolds, New York
John B. Larson, Connecticut	Paul Ryan, Wisconsin
Rahm Emanuel, Illinois	Eric Cantor, Virginia
Earl Blumenauer, Oregon	John Linder, Georgia
Ron Kind, Wisconsin	Devin Nunes, California
Bill Pascrell, Jr., New Jersey	Pat Tiberi, Ohio
Shelley Berkley, Nevada	Jon Porter, Nevada
Joseph Crowley, New York	
Chris Van Hollen, Maryland	
Kendrick Meek, Florida	
Allyson Y. Schwartz, Pennsylvania	
Artur Davis, Alabama	

* Member of the Joint Committee on Taxation

One important byproduct of the process in the Ways and Means Committee is the *Ways and Means Committee Report*. This detailed report, required of both tax-writing committees in Congress, contains four sections: (1) a draft of the legislation, (2) reasons for the changes, (3) an explanation of the changes, and (4) an estimate of the revenue effects of the change. This report is an important document for purposes of attempting to determine Congressional intent, as it may be years before the IRS gets around to drafting regulations that interpret a particular Code provision.

The full House of Representatives generally debates a bill under a **closed rule**, whereby the only person who may amend the bill is a member of the Ways and Means Committee. If the bill is eventually passed, it is sent on to the Senate; if the bill fails, it is effectively killed for that legislative session.

It is important to recall that the House Ways and Means Committee Report summarizes the activities of the committee up to the point that the bill is sent to the House floor. If a tax researcher wants additional details concerning the debate in the House, reference must be made to the **Congressional Record**. This document has a record of all exchanges on the floor of the House.

.09 THE LEGISLATIVE PROCESS—THE SENATE

The first step for legislation in the Senate is the Senate Finance Committee, the major revenue committee in the Senate. Once again, representation of the committee is proportionate to the full Senate membership, and the chair is always from the majority party. The current membership of this committee is disclosed in **Figure 2**.

The Senate Finance Committee more or less follows the same procedures used by the House Ways and Means Committee. However, there is no requirement that the Finance Committee start with the same bill that the House passed; in fact, it is a rare occurrence when they do. Public hearings are followed by a debate about the merits of the bill, and eventually a vote is taken. If the bill is passed by the Committee, it is sent to the floor of the full Senate.

Figure 2

110 th Congress - Senate Finance Committee (in order of seniority)	
Democrats	Republicans
<i>Mac Baucus, Montana (Chair)*</i>	Charles E. Grassley, Iowa *
John D. Rockefeller IV, West Virginia *	Orrin G. Hatch, Utah *
Kent Conrad, North Dakota *	Trent Lott, Mississippi
Jeff Bingaman, New Mexico	Olympia J. Snowe, Maine
John F. Kerry, Massachusetts	Jon Kyl, Arizona
Blanche Lincoln, Arkansas	Craig Thomas, Wyoming
Ron Wyden, Oregon	Gordon Smith, Oregon
Charles E. Schumer, New York	Jim Bunning, Kentucky
Debbie Stabenow, Michigan	Mike Crappo, Indiana
Maria Cantwell, Washington	Pat Roberts, Kansas
Ken Salazar, Colorado	

* Member of the Joint Committee on Taxation

The Senate Finance Committee also issues a comprehensive report of its activities, the *Senate Finance Committee Report*. This report includes the same four sections as the *House Ways and Means Committee Report*: (1) a draft of the legislation, (2) reasons for the changes, (3) an explanation of the changes, and (4) an estimate of the revenue effects of the change. Just like the *Ways and Means Committee Report*, the *Senate Finance Committee Report* is an important document for attempting to determine Congressional intent, as it may be several years before regulations are issued.

The Senate debates the bill under an **open rule**, whereby any Senator may propose amendments to the bill. Eventually, the Senate will vote on a bill, and this piece of legislation may have little in common with the bill passed by the House. If the bill is defeated, as a practical matter it is a dead issue for the session. If the bill passes, the next series of events depends on how different the two tax bills are. If there are only minor differences in the two bills, the Senate version of the bill may be sent back to the House for a concurring vote, and if approved, this bill is sent to the President for a signature.

As was true with the House, any details regarding amendments made on the floor of the Senate will not be described in the Senate Finance Committee Report. Once again, the *Congressional Record* must be consulted for details.

OBSERVATION

It has sometimes been said the “Representatives represent the people, and Senators represent property.” This view is given additional credence when one closely follows the legislative process. Because the Senate operates under an open rule, this may be the first chance for outsiders to influence the bill. Lobbyists are always waiting outside the Senate chamber for a chance to pitch their view of the bill. In fact, this area is sometimes called *Gucci Gulch*, a reference to the favored footwear of the lobbyists.

.11 THE LEGISLATIVE PROCESS—THE CONFERENCE COMMITTEE

In the vast majority of cases, the House and Senate bills are quite a bit different, necessitating a Conference Committee. The chairs of the House Ways and Means and the Senate Finance Committees each appoint representatives to this committee, which has the simple purpose of trying to draft compromise legislation. The Conference Committee has a varying number of members each year.

OBSERVATION

Until the 1986 Act, the chairs of the two tax-writing committees would generally make appointments to the Conference Committee based on seniority on the respective committees. However, when the 1986 Conference Committee was established, both chairs decided to appoint members that they believed would best represent their committee’s interests in Conference. For that reason, two prominent names associated with tax policy, Bill Bradley, a senator from New Jersey, and Jack Kemp, a representative from New York, were appointed to the committee even though both were relatively fresh faces in Congress.

If the Conference Committee eventually crafts and passes a compromise tax bill, it is sent back to the House and Senate for a vote; after all, neither chamber of Congress had actually approved the compromise bill. If both houses pass the compromise, it is then sent to the President for a signature.

The Conference Committee also produces a final report of its work, simply called the *Conference Committee Report*. However, this report is not as comprehensive as the reports issued by the House Ways and Means and Senate Finance Committees. In many cases, the Committee adopts either the House or Senate version of a particular provision, and in such a case the *Conference Committee Report* merely refers the reader to the original committee report for details. If a compromise provision is drafted by the committee, the *Conference Committee Report* will include more detailed explanations.

.13 THE LEGISLATIVE PROCESS—THE PRESIDENTIAL SIGNATURE

Generally, there is a 10-day interval between the time that a bill is delivered to the President’s desk and when he or she actually signs the bill. During this interim period, staffers on the Joint Committee of Taxation comb the bill carefully for any errors or inconsistencies, and Congress then votes on a Concurrent Resolution to ratify any needed corrections in the bill. The objective of this process is to make sure the President signs a tax bill that is as clean and error-free as possible.

OBSERVATION

The *Tax Reform Act of 1986* made major changes in the tax laws, in some cases upsetting members of Congress who saw provisions that they championed for their consistencies go away. When the Concurrent Resolution came up for a vote, a number of these unhappy members of Congress started proposing amendments to put their pet provisions back in the bill. As a result, the Concurrent Resolution started hemorrhaging revenue, which violated the “revenue neutrality” pledge that was part of the process in 1986. Revenue neutrality essentially required that final tax bill raise the same amount of total revenue as the tax law before the changes. So in the end, the Concurrent Resolution was not passed, President Reagan signed a bill with over 100 errors, and it was not until two years later that most of these errors were corrected.

Once the tax bill reaches the President’s desk, he or she can take one of three actions: (1) sign the bill, at which point it becomes part of *Title 26* of the U.S. Code, (2) veto the bill, or (3) choose not to sign the bill, in which case the bill becomes law after ten days. If Congress adjourns within the ten-day period and the President does not sign the bill, the effect is the same as a veto; this occurrence is known as a **pocket veto**. In most cases, the effective date of the new legislation is the date that the President signs the bill, although in some cases retroactive dates are established for certain provisions; this is discussed later in this chapter.

.15 THE LEGISLATIVE PROCESS—THE JOINT COMMITTEE REPORT AND TECHNICAL CORRECTIONS

As mentioned earlier, The Joint Committee on Taxation issues a final report on the tax legislative process commonly called the “Blue Book” due to the color of the cover on the paperback edition. The Joint Committee on Taxation Report includes the same four elements that the Ways and Means Committee and Senate Finance Committee reports: (1) a draft of the legislation, (2) reasons for the changes, (3) an explanation of the changes, and (4) an estimate of the revenue effects of the change. All of these elements have changed as the bill moved through the process, so in many respects the Blue Book is the most accurate and comprehensive explanation of the new law. Nonetheless, many courts do not give it much weight as a source for determining Congressional intent, as explained later.

In some cases, major tax legislation is followed in the next year or two with a “Technical Corrections Act.” No matter how many times staffers read and review a tax bill, errors will frequently slip through the net. And sometimes legislation has unintended consequences that no one could have foreseen. A technical corrections act is drafted to remedy these deficiencies. For example, the *Technical Corrections Act of 1988* was devoted to cleaning up more than 100 errors in the *Tax Reform Act of 1986* caused primarily by the failure of Congress to pass a Concurring Resolution that year.

¶1009 The Internal Revenue Code: A Closer Look

.01 TRACKING THE STAGES OF A TAX BILL

A tax bill is referred to in various manners as it winds its way through the legislative process. When a bill is first introduced in the House or the Senate, it is assigned a bill number. For example, a 2005 tax proposal when first introduced was referenced as follows in the two houses of Congress:

- *H.R. 4297, 109th Cong., 1st Sess. (2005)*
- *S. 2020, 109th Cong., 1st Sess. (2005)*

Once the bill passes either house, it can be called an Act and is given an official name. In recent years, the art of naming an Act has become somewhat political, with certain

emotionally charged words as Jobs and Opportunity and Workers featured in the title. This was the case in this 2005 legislation:

Tax Increase Prevention and Reconciliation Act of 2005

OBSERVATION

Two recent examples of emotionally-charged names of tax acts:

Jumpstart our Business Strength Act (JOBS), 2004

P. L. 110-141, Legislation to Exclude from Gross Income Payments from the Hokie Spirit Memorial Fund to the Victims of the Tragic Event at Virginia Polytechnic Institute & State University, 2007

When an act becomes law, it is first published as a “slip law,” given a Public Law number, and is then bound into the appropriate volume of the *United States Statutes at Large*. This 2005 legislation is titled as follows:

P. L. 109-222

OBSERVATION

The first two digits in a Public Law number represent the session of Congress. These Congressional session numbers may be converted to the second calendar year of the session (each session lasts two years) by multiplying the session number by 2 and subtracting 212. For example, the 109th Session of Congress ended in 2006 $[(109 \times 2) - 212 = 06]$. For sessions of Congress before 2000, the subtraction is only 112, and not 212. Thus, the 99th session ended in 1986 $[(99 \times 2) - 112 = 86]$.

Once the tax act is finally codified into the U.S. Code, the “official” full citation of the act can be quite cumbersome. For example, a complete citation of the 2005 Act is:

Tax Increase Prevention and Reconciliation Act of 2005, Pub. L. No. 109-222, 120 Stat. 346-372

.03 ORGANIZATION OF THE CODE

Just as the official title of a tax act can be somewhat cumbersome to remember, so can the Code location of a particular provision. As mentioned earlier, completed tax bills are added to Title 26 of the U.S. Code. But the Code has many titles, subtitles, chapters, subchapters, parts, subparts, etc. to remember. For example, the complete citation for the tax law devoted to computing tax liability for a married couple is disclosed in Figure 3.

Fortunately for tax researchers, there is one unique Code section for each provision of the federal income tax law. So as a practical matter, tax publications generally just refer to a Code section for reference purposes. For example, the provision illustrated in **Figure 3** would simply be Code Section 1.

Figure 3 also provides two examples of short-hand references for a particular Code section. One is simply an abbreviation (*Sec.*), and the other a symbol (§). And as discussed in Chapter 2, tax Regulations, the official interpretations of Code sections, use the Code section number as part of the referencing procedure for this tax authority.

OBSERVATION

Although the unique section numbers in the Code provide for ease of reference, it is important to understand the various divisions within the Code. For example, a particular Code section may use the expression “for purposes of this subtitle” or “for purposes of this subpart”. In such a case, it is important to know exactly where you are in the Code to know for sure if the provision is applicable to your tax question. It is a good idea to always refer to the Code index to see exactly what Code sections are included in the “subtitle” or “subpart” you are examining.

.05 GUIDES FOR READING AND INTERPRETING THE CODE

Two cardinal rules should always be followed in attempting to determine the answer to a federal tax question: (1) get the facts (GTF) and (2) read the code (RTC). A tax professional must have a firm grip on the facts of a particular case before beginning the research effort; otherwise, subtle differences or nuances may escape detection and lead to the wrong conclusion.

Figure 3

Organization of the Internal Revenue Code Referencing the Internal Revenue Code and Regulations

Internal Revenue Code:

The Internal Revenue Code is Title 26 of the United States Code. This portion of the Code contains the internal revenue laws as enacted by Congress. An example of a complete reference is the following, related to the tax computation of a married couple:

- 26. Title (Internal Revenue Title)
 - A. Subtitle (Income Taxes)
 - 1. Chapter (Normal Taxes and Surtaxes)
 - A. Subchapter A (Determination of Tax Liability)
 - I. Subpart (Tax on Individuals)
 - 1. Section (Tax Imposed)
 - (a) Subsection (Married individuals . . .)
 - (1) Paragraph
 - (A) Subparagraph
 - (1) Clause

Example of a common reference for citation purposes:

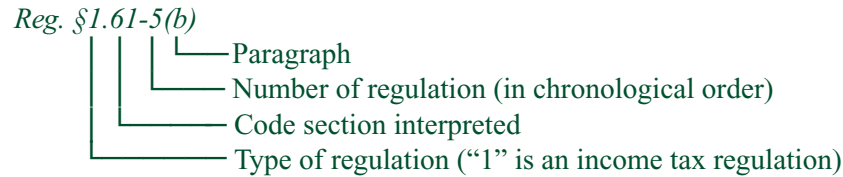
Sec. 1

 Section number
 Shorthand reference for “Section” (also the symbol “§”)

Treasury Regulations:

Treasury regulations are the Department of the Treasury’s official interpretation of the Internal Revenue Code. Regulations are numbered to correspond to the section of the Code being interpreted. These regulations are found in Title 26 of the Code of Federal Regulations.

Example of a common reference for citation purposes:



The importance of reading the Code cannot be emphasized enough; every answer to a tax question must somehow relate directly to the ultimate primary authority, the Internal Revenue Code. In tax practice there is a temptation to examine the “easy to read” secondary authorities first when trying to find the answer to a question. But these are only interpretations, and if the answer is in the Code itself, the interpretations are irrelevant. Courts have consistently emphasized that their purpose is to interpret the law, and not legislate. This view is illustrated in the following case quotes:

- *Huntsberry v. Commissioner*.⁶ “Unequivocal evidence of legislative purpose is required before the court will override the plain meaning of the statutory language.”
- *Strogoff v. United States*.⁷ “The context from which the meaning of a word is taken must be the words of the statute itself.”
- *Woods v. Commissioner*.⁸ “To glean the meaning of the words used by Congress, we must first look to the ordinary or settled meaning of the words used to convey its intent.”
- *American Automobile Association*.⁹ “The validity of the long established policy of the Court in deferring, where possible, to Congressional procedures in the tax field is clearly indicated in this case.”
- *Eisner v. MaComber*.¹⁰ “And, as this court has so often said, the high prerogative of declaring an Act of Congress invalid, should never be exercised except in a clear case.”

When reading and interpreting the Code, it is important to read the language closely, constantly being on the lookout for definitions, cross references, and connectors. For example, *Code Sec. 280A(c)* addresses the office in the home deduction, and one of the key words in that provision is in subsection (c)(1)(B), the word “or”. Thus, a home office will qualify if any one of the three conditions is met. This connector was also used as a justification for modifying *Code Sec. 280A* in 1997; this will be discussed in Chapter 6.

OBSERVATION

Definitions can be extremely important in interpreting the Code. In some cases, the definitions of key terms are contained in the statute; in other cases the researcher may need to check a key word index for the Code to find the definition (e.g., *Code Sec. 152* defines a “dependent” for tax purposes). Additionally, *Code Sec. 7701* is titled “Definitions” and contains over 50 definitions of common terms used in the Code, such as “person” and “corporation.”

In summary, the words used in the Code must be interpreted in their everyday meaning. Furthermore, if the Code is clear on an issue, there is no need to go any further.

.07 TAX ACT PROVISIONS THAT ARE NOT CODIFIED

A common misperception about the Internal Revenue Code is the notion that every part of a tax act is added to the Internal Revenue Code. In reality, a number of provisions do not make it into the Code; these include transition rules, effective dates, and sunset provisions.

⁶ *Huntsberry*, 83 TC 742 (1984).

⁷ *Strogoff*, 86-2 USTC ¶9616, 10 ClsCt 584.

⁸ *Woods*, 91 TC 11.

⁹ *American Automobile Association*, S Ct 61-2 USTC ¶9517, 367 US 687.

¹⁰ *Eisner v. Macomber*, 252 US 159.

Most of the transition rules affect only a few taxpayers and are of short duration. For example, in order to obtain support from certain members of Congress, special rules may be enacted to “soften” the landing of certain constituents who are losing existing tax benefits because of either new provisions or a repeal of old provisions. This has led to such legislation as the “Gallo Amendment,” designed to help the famous vineyard family adjust to a change in the estate tax law.

Also, the transition rules are also the favorite vehicle for Congress to dole out special political favors to constituents. This is an action that members of Congress would prefer to be shielded from public scrutiny.

In some cases, new provisions are effective for only a limited period of time, or an old provision is being phased out over a limited period of time. In these cases, Congress may keep these effective dates out of the Code in order to avoid confusion and to keep the Code relatively clean. In such a case, the researcher must refer to the Act, and not the Code, for the details on these effective dates. These transition rules are often difficult to locate.

Effective Dates

Generally, most provisions contained in a new tax act become effective on the date that the President signs the Act into law. For example, President Bush signed the *Working Families Tax Relief Act of 2004* on October 4, 2004, and this is the effective date unless stated differently in the Act.

In some cases, the effective date may be prospective; for example, a new provision may not take effect until the following tax year. In other cases, a provision may be retroactive to a date specified by Congress. In many cases, a retroactive date is the first day the provision was discussed in Congress; that way, taxpayers are prevented from “planning around” the new law before it takes effect.

¶1011 Evaluating and Locating Legislative Authority

.01 CONSTITUTION

The Constitution is the ultimate tax authority; if a statute is found to violate the Constitution, it will be declared invalid. Recall the *Pollock* case mentioned earlier in the tax history; this was the only successful challenge to the constitutionality of our tax laws, and this occurred in 1895.

OBSERVATION

There are a number of authors and speakers who make a living by selling products and information that “proves” that the tax law is unconstitutional, and if you will just follow their advice, you will not have to pay taxes. Obviously, none of these schemes have ever worked. Interestingly, the IRS recently did a study on these authors and commentators and found that over 95 percent of them actually do file and pay their own taxes; they know better than to follow their own advice.

The 1895 challenge in the *Pollock* case was the *last* successful challenge on the constitutionality of the federal income tax. And yet, there are always gullible individuals who believe various authors and speakers when they assert that the income tax is unconstitutional and does not have to be paid. A recent case in point was the actor Wesley Snipes, who bought into the notorious “861 argument” of a leading tax protestor. *Code Sec. 861* states that foreign-source wages of U.S. citizens are taxable, and the protest movement argues that since this section does not mention U.S. wages, they must not be taxable! At trial, Mr. Snipes changed his defense to argue that he was “duped” by the tax protestors. Although Mr. Snipes was not found guilty of tax fraud, he was convicted on three counts of failure to file a tax return on income exceeding \$10 million (payment for two sequel films in the *Blade* series). The interest and penalties alone on this \$10 million deficiency may very well exceed \$10 million.

A copy of the Constitution is included in Volume 1 of the U.S. Code. Most tax services, both print and online, also offer copies of the Constitution.

ON THE WEB

The Constitution is available free of charge online at the following locations:

<http://www.nara.gov/exhall/charters/constitution/conmain.html>

<http://www.lcweb2.loc.gov/const/const.html>

.03 THE INTERNAL REVENUE CODE

As a practical matter, the Internal Revenue Code is the final tax authority for most matters, as long as the Constitution is not violated. As a result, the answer to any tax question must first be tied to a provision of the Code, as statutory authority is always controlling. Interpretations such as Regulations and court cases may help understand how a Code provision is applied, but the ultimate authority is still the Code.

The Internal Revenue Code is available as Title 26 of the United States Code, and is also reprinted in most tax services, both print and online editions. The major publishers also sell hard copy editions as separate volumes, either as one volume by the Research Institute of America (RIA) and two volumes by Commerce Clearing House (CCH).

ON THE WEB

The Code is available free of charge online at the following locations:

<http://www.gpo.ucop.edu/catalog/uscode26usc.html>

<http://www.law.cornell.edu/uscode/26>

.05 TAX ACTS

As mentioned earlier, not all provisions of a Tax Act are eventually codified. For that reason, it is frequently necessary to examine the full Act, especially for effective dates, transition rules, and sunset provisions. The full text of a tax act is published by the Government Printing Office, and is usually offered as a paperback supplement for most paper tax services.

ON THE WEB

Most tax acts are offered free of charge at the following sites on the worldwide web:

<http://www.loc.gov>

<http://www.gpo.ucop.edu>

<http://thomas.loc.gov>

.07 TAX TREATIES

Tax treaties are another source of legislative authority that has not been discussed thus far in this chapter. In general, the President of the United States may enter into a treaty with any other country, and such treaty is considered having the force and effect of law once it is approved with the advice and consent of the Senate (a two-thirds vote is required). Most treaties are designed to eliminate the double taxation of income, either for a U.S. citizen working abroad or for a citizen of another country working in the United States.

The courts generally tend to give equal weight to both the Code and treaties. When the two are in conflict, courts usually assumed that the one adopted later controls. In addition, other agreements between the United States and other countries, such as the North American Free Trade Act (NAFTA), though technically not treaties, may have the effect of a treaty for tax purposes.

The full texts of treaties are sometimes difficult to find. Commerce Clearing House and Warren Gorham Lamont offer Tax Treaty Services, and treaties may be found in the United States Code Annotated published by West Publishing Company. Currently, treaties are available only in print publications; there are no websites devoted to full-text delivery of treaties.

.09 COMMITTEE REPORTS

As discussed earlier, the various committee reports of the various tax committees (House Ways and Means, Senate Finance, and Conference) are useful indicators of Congressional intent. These reports may be the only interpretation until regulations are enacted.

However, at all times, it must be remembered that legislative history may be used to solve Congressional ambiguity, and not create it. Committee reports may not be used to overturn the plain meaning of the words in the statute itself. Of the three documents, the Conference Committee Report is usually accorded greater weight since it summarizes the final product of Congress. But in many cases this document merely refers the reader to one of the other two committee reports if the final provision is close (or the same) in wording to the original proposal in one of the houses.

Earlier it was mentioned that the **Joint Committee on Taxation Report (the Blue Book)** is often regarded as the most comprehensive and lucid explanation of a new tax law. Nonetheless, over the years courts have traditionally accorded this document less weight than other sources, since it is not written “contemporaneously” with the legislative process. Recall that the Joint Committee does not have a legislative function; it serves as an interpretive body only. More importantly, there is no opportunity for Congress or anyone else involved in the legislative process to rebut the Blue Book’s conclusions.

However, two recent events have tended to provide more authority to the Blue Book. First, the Blue Book is now listed as “substantial authority” for purposes of avoiding the Code Sec. 6662 Penalty discussed later in the chapter. Second, the U.S. Supreme Court stated the following in *FPC v. Memphis Light*,¹¹ concerning the Blue Book: “It provides a compelling contemporary indication of the legislation’s effect.”

Full-text copies of the various committee reports are printed in the weekly Internal Revenue Bulletin after the tax legislation is passed, and are printed again in the Cumulative Bulletin that is compiled at the end of the year. (There is one exception—the IRS chose not to reprint the 888 pages of the committee reports accompanying the 1954 recodification.) Committee reports for years prior to 1939 are reprinted in the 1939 cumulative bulletin. In addition, most tax services provide all committee reports in paperback form with print services and on their websites.

ON THE WEB

Committee reports may be found on the following websites on the Worldwide Web:

<http://www.house.gov/jct>

http://www.house.gov/ways_means

<http://www.senate.gov/~finance>

<http://thomas.loc.gov>

There are two other valuable print services that offer access to selected portions of committee reports for legislation enacted prior to 1954. One is J.S. Seidman, *Legislative History of Federal Income Tax Laws, 1861-1938, 1939-1953* (6 volumes).¹² This service organizes pre-1954 legislation by Code section and/or topic, and provides cross-reference tables for converting 1954 code section numbers to 1939 code section numbers and vice versa. A second source is Walter E. Barton and Carroll W. Browning, *Federal Tax Laws Correlated*.¹³

.11 THE CONGRESSIONAL RECORD

The *Congressional Record* is the only source for determining legislative intent on amendments made on the floor of the House or Senate. The relevant discussion must be located by the day of the debate, no easy task. However, there is no other alternative to locating this information.

¹¹ *Federal Power Commission v. Memphis Light*, SCt 73-1 USTC ¶9412, 411 US 458, 93 SCt 1723.

¹² J.S. Seidman, *Legislative History of Federal Income Tax Laws, 1861-1938, 1939-1953*. Prentice-Hall, Inc. (Englewood Cliffs, N.J.: 1954).

¹³ Walter E. Barton and Carroll W. Browning, *Federal Tax Laws Correlated*. Warren Gorham & Lamont (Boston: 1969).

An important part of this document in regard to a discussion of tax law changes is the presence of *colloquies* and *floor statements*. These represent discussions between members of Congress and the managers (from the Joint Committee) of a tax bill that are intended to clarify specific provisions. These discussions are inserted into the *Congressional Record*. As a general rule, colloquies and floor statements may be relied on only in the event the statute or Committee reports fail to yield any insight into Congressional intent or actions.

There is some question as to how much weight should be accorded to colloquies and floor statements. As a general rule, the following guidelines apply:

- Similar colloquies in both houses is strong affirmation of Congressional intent.
- A colloquy given affirmation by the tax-writing committee chair (or the author of the bill) is given the greatest weight.
- Colloquies and floor statements made *before* a vote are given much greater weight than those given *after* a vote.

Most libraries provide access to the *Congressional Record*, either through print services, microfiche, or online services such as the LEXIS and WESTLAW electronic libraries.

ON THE WEB

The Historical Congressional Record Index may be accessed through the Government Printing Office (GPO) site at the following location:

<http://www.gpo.ucop.edu>

.13 CONGRESSIONAL HEARINGS

Public hearings of the House Ways and Means Committee and the Senate Finance Committee yield very little in terms of tax authority. Hearings records typically provide insight into the problems, but not necessarily the legislative solutions. For that reason, hearings records tend to be given little if any weight by the Courts.

Most libraries provide access to Congressional hearings, either with print volumes from the Government Printing Office or online with a LEXIS or WESTLAW subscription.

ON THE WEB

The Historical Congressional Record Index may be accessed through the Government Printing Office (GPO) site:

<http://www.gpo.ucop.edu>

.15 PENDING LEGISLATION AND UNENACTED LEGISLATION

Questions inevitably arise concerning the weight given to pending legislation, particularly technical corrections that appear certain to be enacted by Congress. The IRS official position is that no reliance can be made on pending legislation until the provisions have actually been signed into law. However, the IRS has sometimes considered pending legislation when issuing private letter rulings.¹⁴

OBSERVATION

Sometimes the old axiom “No good deed goes unpunished” also applies to tax professionals who try to do the right thing. For example, in 1986 Congress revised the alternative minimum tax (AMT) rules for individuals, and in doing so forgot to continue the required adjustment for personal exemption deductions, since such amounts are not allowed for the AMT. Everyone knew that Congress would eventually correct this oversight and apply the change retroactively, so some firms went ahead and made the adjustment anyway on 1987 returns. Much to their dismay, the returns were bounced by the IRS, who said that the law does not read that way. So the returns were filed a second time, this time without the adjustment, and, oh yes, then refiled a third time in 1988 after Congress made the technical correction!

¹⁴ For example, see Ltr. Rul. 88020045.

Unenacted Legislation

At first blush, it is difficult to understand how legislation that was *not* enacted could have any relevance whatsoever to a tax researcher. The answer is that, if nothing else, unenacted legislation tells one what Congress did not intend to enact. There is some value in knowing that Congress considered such an interpretation and consciously decided not to enact that interpretation.

The concept of unenacted legislation is also relevant in explaining an argument sometimes used by taxpayers and occasionally by the IRS. This defense is termed “legislative reenactment,” and describes a situation where the IRS or the courts have issued an interpretation of a particular law and Congress has a chance to change the interpretation (in subsequent legislation) but chooses not to. Thus, the IRS or court interpretation is “legislatively reenacted.” Generally, taxpayers have had little success in sustaining such arguments, since silence is not necessarily agreement.

¶1013 “Substantial Authority” and “Reasonable Basis” in Tax Controversies

The Internal Revenue Code contains a number of penalties that may be applied to tax professionals for certain actions. However, in some cases these penalties will not apply if the tax professional has “substantial authority” for the position taken on the tax return. In addition, certain positions may be taken on a return only if a “reasonable basis” exists for that position. A “reasonable basis” is defined as the likelihood of success should the item be questioned by the IRS. Various publications of the IRS and the accounting profession set minimum standards for such reasonable positions. These are discussed in detail in Chapter 9.

.01 SUBSTANTIAL AUTHORITY

One of the more common penalties potentially applicable to tax professionals is the “substantial understatement” penalty of *Code Sec. 6662*. This penalty is equal to 20 percent of the understatement; however, it may be reduced if there is “substantial authority” for the treatment of the item.

For purposes of reducing the amount of understatement of income tax subject to the “substantial understatement penalty,” *Reg. §§1.6661-3(b)* and *1.6662-4(d)* define **substantial authority** to include the following:

1. The Internal Revenue Code and other statutes
2. Regulations (final, temporary, and proposed)
3. Court cases
4. Tax treaties
5. Statements of Congressional intent, including:
 - a. House Ways and Means Committee Reports
 - b. Senate Finance Committee Reports
 - c. Joint Conference Committee Reports
 - d. Congressional Record
 - e. Joint Committee on Taxation Report (the “Blue Book”)
6. Administrative pronouncements, including:
 - a. Revenue Rulings
 - b. Revenue Procedures
 - c. Private Letter Rulings (PLRs)
 - d. Technical Advice Memoranda (TAMs)
 - e. Actions on Decisions (AODs)
 - f. General Counsel Memoranda (GCMs)
 - g. Notices, Press Releases, and similar documents

The Internal Revenue Service does have the power to except certain authorities from this list. At least once a year, the IRS must publish in the Federal Register a list of positions it believes lack substantial authority and that affect a significant number of taxpayers. However, this does not mean that substantial authority exists for positions not included on the list.

Reasonable Basis for a Position: Standards of Certainty

The professional literature and guidance from the IRS (primarily through *Circular 230*) provide for different levels of certainty regarding the likelihood that a taxpayer's position on a particular item would be sustained if challenged by the IRS. Certain levels are required to avoid the imposition of a penalty, and other levels are required for taking a position on a return, with a higher level generally required for not disclosing that position on the return. These are discussed in detail in Chapter 9.

¶1015

Summary

- A tax bill must work its way through the House Ways and Means Committee, the Senate Finance Committee, the Joint Conference Committee, and passage by both the House and Senate before being sent to the President for his signature.
- The Constitution, Internal Revenue Code, and tax treaties are the three main sources of legislative authority.
- The Internal Revenue Code contains the tax laws passed by Congress and is the highest level of authority in most tax research issues.

Review Questions for Chapter 1

True or False

Indicate which of the following statements are true or false by circling the correct answer.

- | | | | |
|-----|---|---|---|
| 1. | An article in the <i>Journal of Taxation</i> is an example of secondary authority. | T | F |
| 2. | All answers to a tax question must necessarily be traced back to secondary tax authority. | T | F |
| 3. | A decision of the U.S. Supreme Court is an example of administrative tax authority. | T | F |
| 4. | The Senate Finance Committee Report is an example of legislative authority. | T | F |
| 5. | Under the early British income tax laws that were duplicated in the United States in the 1800s, gains and losses on property were includible in the tax base. | T | F |
| 6. | In <i>Springer vs. U.S.</i> , the federal income tax was found to be unconstitutional by the Supreme Court. | T | F |
| 7. | The corporate income tax enacted in 1909, labeled as an “excise tax on the privilege of doing business,” was later ruled unconstitutional. | T | F |
| 8. | The U.S. House of Representatives generally debates a tax bill under a “closed rule,” allowing amendments only by Ways and Means Committee members. | T | F |
| 9. | A Conference Committee bill must generally be voted on once again by both houses of Congress. | T | F |
| 10. | <i>Reg. §1.263-4</i> refers to the fourth section of the first regulation issued on <i>Code Sec. 263</i> of the Internal Revenue Code. | T | F |

Fill in the Blanks

Fill in each blank with the appropriate word or phrase that completes each sentence.

11. A decision of the 5th Circuit Court of Appeals is an example of _____ (primary, secondary) tax authority.
12. _____ authority refers to authority as enacted by the U.S. Congress.
13. The first truly national income tax in the U.S. was used to fund the _____.
14. The U.S. income tax was ruled unconstitutional in 1895 because the Supreme Court ruled that it was a _____ tax, requiring apportionment by a census.
15. The _____ Amendment to the Constitution eliminated the apportionment requirement for the federal income tax.
16. The second codification of the U.S. tax laws occurred in _____.
17. The Constitution requires that all revenue bills originate in the _____.
18. For an explanation of changes to a tax bill that occurred on the floor of the Senate, reference must be made to the _____.
19. A(n) _____ occurs if Congress adjourns within the 10-day period that the President is considering a tax bill, and the President does not sign the bill.
20. In the broadest sense, the ultimate tax authority is the _____.

Multiple Choice

Circle the best answer for each of the following questions.

21. Which of the following is not a category of primary tax authority?
 - a. judicial authority
 - b. administrative authority
 - c. procedural authority
 - d. legislative authority

22. Which of the following is not a traditional component of tax practice?
 - a. tax planning
 - b. tax research
 - c. tax compliance
 - d. tax accounting

23. A Revenue Procedure issued by the IRS is an example of:
 - a. legislative authority
 - b. administrative authority
 - c. judicial authority
 - d. none of the above

24. The first “codification” of the U.S. income tax laws occurred in:
 - a. 1913
 - b. 1921
 - c. 1939
 - d. 1954

25. Which of the following is not a part of the final reports of the Ways and Means Committee or the Senate Finance Committee?
 - a. explanation of the changes
 - b. transcripts of oral testimony to the committee on proposed law changes
 - c. estimate of the revenue effects of the changes
 - d. reasons for the changes

26. A Presidential veto may be overridden only by an affirmative vote of:
 - a. a simple majority of both houses of Congress
 - b. a two-thirds majority of both houses of Congress
 - c. a three-fourths majority of both houses of Congress
 - d. none of the above

27. The final comprehensive report issued that explains recently-enacted tax legislation is the:
 - a. Conference Committee Report
 - b. Congressional Record
 - c. Senate Finance Committee Report
 - d. Joint Committee on Taxation Report

28. P. L. 106-43 would have been enacted in the session of Congress that ended in the year:
 - a. 1996
 - b. 1998
 - c. 2000
 - d. 2006

29. The short-hand method of referencing a particular part of the Internal Revenue Code is to cite the:
 - a. subtitle number
 - b. chapter number
 - c. subchapter number
 - d. section number
30. Tax Act provisions that may not be added to the Internal Revenue Code itself can include:
 - a. effective dates
 - b. sunset provisions
 - c. transition rules
 - d. any of the above

Review Problems

31. Give two examples of each of the following: (a) primary tax authority and (b) secondary authority.
32. List the three basic types of tax authority, and provide an example of each one.
33. What is the importance of each of the following dates in U.S. tax history: 1861, 1895, 1913, 1939, and 1954?
34. What was the U.S. Supreme Court's rationale for declaring the federal income tax unconstitutional in the *Pollock v. Farmers' Loan and Trust Co.* case of 1895?
35. Explain how Congress "fixed" the apportionment problem with regards to the federal income tax in 1909.
36. Define the term "codification," and list the major codifications of the Internal Revenue Code. Why are these dates sometimes important in researching a federal tax question?
37. Explain the basic steps that a tax bill follows in both the House Ways and Means Committee and the Senate Finance Committee. Do both houses of Congress also follow the same procedures when debating a bill on the floor of the entire legislative body? Explain.
38. Why is the Conference Committee Report typically much smaller in size than either the House Ways and Means Committee Report or the Senate Finance Committee Report. Explain.
39. What are the President's options when a tax bill reaches his or her desk?
40. Why are the courts sometimes hesitant to cite the "Blue Book" (Joint Committee on Taxation Report) as authority? Explain.
41. Explain how to convert the following public law numbers to the last year of the legislative session generating the law: P. L. 98-200 and P. L. 107-420.
42. Since each "section" of the Code has a unique Section number, is it necessary to be concerned about broader subdivisions, such as Subchapter, Chapter, and Part?
43. Do all provisions of a tax act eventually end up in the Internal Revenue Code? Explain.
44. "The role of the courts is to interpret the law, and not make the law." Do you agree? Explain.
45. How much weight should be given to colloquies and floor statements? Explain.

Research Questions

46. Which subchapter of the Code contains *Code Sec. 303*?
47. How is a "dependent" defined for purposes of *Code Sec. 119(a)*?
48. *Code Sec. 411(a)(11)(A)* was amended several years ago to increase the involuntary maximum pension "cash-out" amount from \$3,500 to \$5,000. This represents the present value of the maximum amount that the employer may cash out of the pension plan for an employee who terminates his or her participation in the qualified plan without the employee's approval. Which Act of Congress made this change, and when was the change effective?

49. Refer to *Code Sec. 411(a)(11)(A)*. Is the new \$5,000 figure adjusted for inflation each year? Which house of Congress originally proposed such an inflation adjustment?
50. *Code Sec. 317* defines the term “property.” Is this definition of property to be used for other sections of the Code, such as *Code Sec. 1001*? Explain.
51. During deliberations of the *American Jobs Creation Act of 2004*, there was a proposal to modify the corporate rate schedule gradually over the next few years (this particular proposal was not related to the domestic activities deduction computation). What was (1) the House proposal, (2) the Senate proposal, and (3) the final decision of the Conference Committee? (Hint: Open the Federal Tab of the CCH Tax Network, scroll to the Tax Legislation section, and choose an appropriate link.)
52. What is the title of Section 5 of *P. L. 110-42*? (Hint: Open the Federal Tab of the CCH Tax Network, scroll to the Tax Legislation section, and click on Tax Bills and Reports – 110th Congress).
53. What was the purpose of *P. L. 110-176*?
54. When was *Code Sec. 441(i)* last amended, and what was the Act that amended this provision?
55. How did the Technical Corrections Act of 1982 modify *Code Sec. 1092(c)* of the Internal Revenue Code?

