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From the Editor:

IRS Restructuring: Ten Years Later

By Jon Almeras — jalmeras@tax.org

In some ways it's hard to believe, but it's been 10 years since the Internal Revenue Service Restructuring and Reform Act became law.

Remember those Senate Finance hearings in 1997 — the ones where IRS employees testified with their identities hidden? A story in *Tax Notes* from September of that year began: ''IRS employees and aggrieved taxpayers painted a picture last week of an out-of-control tax administration agency so bent on fulfilling its law enforcement mission that it will destroy innocent taxpayers rather than admit to a mistake.'' Makes everything you've read in these pages lately seem downright mundane, doesn't it?

Based on the testimony at the hearings, it wasn't a surprise when Congress acted in the summer of 1998 to rein in the IRS and make it more taxpayer friendly. Things like the Taxpayer Bill of Rights and the 10 Deadly Sins became part of the tax vernacular. But in the last 10 years, there have been complaints that the accusations against the IRS were overblown and that the restructuring gutted the agency's enforcement efforts.

With that in mind, Tax Analysts recently sponsored a conference to mark the anniversary and see how the act changed the IRS over the last decade, and several key players in the restructuring spoke about the experience and what lessons should be learned from the process.

Donna Steele Flynn, who was staff director for the House Ways and Means Oversight Subcommittee in 1998, discussed the process and said work on the legislation was a model that Congress should be following today.

However, Christopher Rizek, who was then associate tax legislative counsel at Treasury, said there was a failure at the time to recognize the restructuring issue as one of tax policy. The Clinton administration treated it like a government efficiency reform effort, he said, and was cowed into acquiescence at the end of the process. Because the administration didn't push back on tax policy issues, that led to things that ''have turned out to be problems,'' Rizek said.

Rizek agreed that the reform act had made the IRS kinder and friendlier, but he thought the degree varied by issue and operating division. Other panelists were more enthusiastic about the change to a more taxpayer-friendly agency. National Taxpayer Advocate Nina Olson said she ''could go on and on about what's positive about the restructuring act,'' beginning with the existence of her job. Villanova Law Prof. Les Book, who directs a low-income taxpayer clinic, cited the more than 150 such clinics now in existence as a positive effect of the restructuring.

But for all its customer service gains, the IRS must still enforce the tax laws. Commissioner Douglas Shulman, who was chief of staff of the restructuring commission that prepared the legislation, said he thinks the IRS has worked hard the last 10 years to strike the right balance between service and enforcement. Restructuring and modernization helped, he said, but there is still more that needs to be done, like upgrading the Service's data system which dates to the 1960s. The IRS needs ''steady support for modernization,'' Shulman said.

Rob Portman, who was a member of the Ways and Means Committee 10 years ago and cochaired the restructuring commission, agreed with Shulman and added that lawmakers and administrators must remain vigilant in keeping the proper balance between service and enforcement. It must be constantly ''watched and tweaked,'' he said. (Full coverage of the conference begins on p. 300.)

Energy

Marty Sullivan continues his recent series of articles about U.S. energy tax policy. Lately, former oilman T. Boone Pickens has been all over the airwaves and even up to Capitol Hill promoting his plan for energy independence. Pickens wants to build wind farms lots of them to meet the country's power needs, and convert our cars to natural gas. That would mean less dependence on foreign oil, the reasoning goes. But is it good policy?

Sullivan doesn't necessarily quibble with Pickens's idea (although he does think Pickens fails to take into consideration things like plug-in hybrids), but he thinks it's better pitched to investors and not to the government. Sullivan thinks the government should be setting overall policy goals (reducing oil dependence or reducing greenhouse gases, for example) but should not be picking technologies to achieve those goals (p. 283).

In another energy-themed article, Sullivan examines ethanol subsidies. Everyone bashes ethanol subsidies, and Sullivan says a lot of that bashing is

justified: The subsidies are blatant protectionism, they aren't environmentally justified, they take farmland away from food production, etc. However, Sullivan thinks there is still "an ironclad case for a permanent subsidy for ethanol." See p. 285 to find out why.

Tax ALJs

In other analysis, Jeremiah Coder looks at the curious case of administrative law judges. Treasury has none of its own, so when the IRS Office of Professional Responsibility needs an ALJ, it has to get one from another agency. Lately those ALJs have been coming from the National Labor Relations Board. But with OPR beefing up its enforcement activities and higher penalty standards, many practitioners are wondering if the ALJ conducting the hearing should be versed in the complexities of tax law to make a fair judgment on a practitioner's ethics. However, those practitioners weren't willing to go on the record. Coder examines the issues on p. 305.

Who's on First?

Ajay Gupta has some fun with this week's special report, in which he gives us a clever play on a famous Abbott and Costello routine. In this first of a two-part report, Gupta claims that the stream of commentary in both professional and academic circles that followed in the wake of the Tax Court's first *Hubert* decision was largely misguided. He says that in seeking to apply the section 752 liability-sharing rules to LLC members' section 465 at-risk claims, the commentators ignored the facts of the case — in particular the desire to exploit the aggregation principles of the at-risk rules (p. 335).

More Commentary

In a practice article, Robert Borteck describes an offense-strategy use of section 2032 — relating to alternate valuation — to convert a controlling interest in a closely held business into multiple minority interests to reduce transfer tax. The IRS finds this approach troubling and has proposed regulations that would prevent it. Borteck questions those regulations (p. 323). In another practice article, Robert Feinschreiber and Margaret Kent warn about unscrupulous promoters intent on selling the 20 percent spread between the regular income tax rate and the dividend rate as a domestic international sales corporation benefit (p. 331).

In Of Corporate Interest, Robert Willens looks at what he calls Digimarc's "two-step." The parties to this dance intend that, for tax purposes, a spinoff and reverse merger will constitute a single integrated transaction in which the spinoff would be treated as a redemption of shares. Willens has a feeling the IRS may not respect the intentions of the dancers on this one (p. 361).

Prof. Calvin Johnson says that adjusted basis needs to describe the investment value of an asset, and he presents another Shelf Project proposal reflecting this belief. Johnson's latest proposal would deny a business or casualty loss deduction for basis to the extent of the fair market value of the property held by the taxpayer after a casualty or loss event. To the extent the property still has value, no basis is lost. His proposal would have no effect on sales, total losses, or property such as cars and machinery, which does not ordinarily appreciate (p. 357).

Letters

Johnson's last Shelf Project on deferred payment sales (*Tax Notes*, July 14, 2008, p. 157) spurred Robert Wood to write in. Wood thinks the proposal, especially as it relates to installment sales, is unwarranted. Those sales aren't a problem, and there are other places Congress can look for revenue, he says (p. 366).

Our other letter this week is from Paul Streckfus. In it, he criticizes Ways and Means Chair Charles Rangel over the congressman's reaction to ethics questions about his fundraising for a school in New York that will bear his name (see p. 298 for the latest coverage). Streckfus takes issue with Rangel's statement that foundations that have contributed grants to the school don't have issues before Ways and Means. That statement's a "whopper," Streckfus says, and he also targets other taxwriters who seek out funding for their pet projects from foundations. There may be nothing wrong, Streckfus says, but politicians' actions raise suspicions that the foundations giving grants will be looked on more favorably by the taxwriting committees. See p. 365 for the letter. ■

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