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# The Almost-Restatement of Income Tax of 1954

WHEN TAX GIANTS ROAMED THE EARTH\*

*Lawrence Zelenak*<sup>†</sup>

## INTRODUCTION

The American Law Institute (ALI) has published Restatements of about two dozen areas of the law, ranging alphabetically from Agency to Unfair Competition. Even an unbiased observer (that is, anyone other than a tax lawyer) would probably concede that federal income taxation is at least as important a field as a number of the areas of the law that have been blessed with Restatements.

Why, then, has the ALI never produced—or even attempted—a *Restatement of the Law of Federal Income Taxation*? One might suppose it is because the goal of restating federal income tax law has been too ambitious for even the redoubtable ALI, but the truth is closer to the opposite—that a mere Restatement was not ambitious enough. According to the ALI, Restatements “reflect the law as it presently stands or might plausibly be stated by a court. Restatement black-letter formulations assume the stance of describing the law as it is.”<sup>1</sup> When the ALI embarked on its Income Tax Project in 1948, it was not interested in the relatively modest goal of describing existing tax law. Rather, its ambition was “to prepare . . . an improved and modernized income tax statute with explanatory comments, which will be presented . . . for such consideration as Congress may wish to give it.”<sup>2</sup> In the ALI’s project classification system, this meant that the goal of the Project was the

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<sup>1</sup> *ALI Overview*, A.L.I., <http://www.ali.org/index.cfm?fuseaction+projects> (last visited Oct. 29, 2013).

<sup>2</sup> Herbert F. Goodrich, *Annual Report of the Director*, 1948 A.L.I. PROC. 1, 16 (quoting a statement of an anonymous participant in the Income Tax Project).

production not of a Restatement, but of a model code. Again according to the ALI, “Model codes . . . are addressed mainly to legislatures, with a view toward legislative enactment. Statutory formulations assume the stance of prescribing the law as it shall be.”<sup>3</sup>

From the vantage point of 2013, the goal of creating a complete model federal income tax statute seems absurdly ambitious. Yet by February 1954—just in time for consideration by Congress in the drafting of what became the Internal Revenue Code of 1954<sup>4</sup>—the ALI had produced a nearly-complete draft of an income tax statute.<sup>5</sup> By design, the Draft did not include procedural provisions, provisions applicable to a few special classes of taxpayers (“such as insurance companies”), or provisions in a few other highly specialized areas (such as “pension[s,] trusts[,], and employee benefits”).<sup>6</sup> Subject to those few exceptions, the 1954 Draft was a complete income tax statute.<sup>7</sup> Published in two volumes, the 1954 Draft featured 374 pages of proposed statutory language, accompanied by 587 pages of explanatory comments.

Although Congress left large chunks of the ALI’s Draft on the cutting room floor, it also followed (to varying degrees) the ALI’s lead on many topics—including, perhaps most significantly, a complete revision of the partnership tax rules.<sup>8</sup> Both commentators who applauded the Internal Revenue Code of 1954 and those who lamented it agreed that the ALI’s fingerprints were all over the Code. Writing in 1955, prominent New York tax attorney Norris Darrell, who viewed the 1954 Code as “a most commendable accomplishment,”<sup>9</sup> opined that “without the Institute’s groundwork we would not now have the new Code.”<sup>10</sup> Writing in 1960, Columbia Law School Professor William L. Cary, who viewed the 1954 Code as “both erroneously conceived and poorly executed,” described the Code as

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<sup>3</sup> *ALI Overview*, *supra* note 1.

<sup>4</sup> Internal Revenue Code of 1954, Pub. L. No. 83-591, 68A Stat. 3 (1954).

<sup>5</sup> See A.L.I., FEDERAL INCOME TAX STATUTE (Draft, Feb. 1954) [hereinafter 1954 DRAFT or DRAFT].

<sup>6</sup> *Id.* at xxxi-xxxii.

<sup>7</sup> See *id.*

<sup>8</sup> Compare II ALI, FEDERAL INCOME TAX STATUTE (Draft, Feb. 1954) [hereinafter ALI VOLUME II], with Internal Revenue Code of 1954, §§ 701-71, 68A Stat. at 239-54.

<sup>9</sup> Norris Darrell, *Internal Revenue Code of 1954—A Striking Example of the Legislative Process in Action*, 1955 S. CAL. TAX INST. 1, 25 (1955).

<sup>10</sup> *Id.* at 21.

“follow[ing] in the Institute’s footsteps—though carelessly and inconsistently.”<sup>11</sup>

If the ALI were to propose today the drafting of a nearly complete model federal income tax statute for the twenty-first century, in the hopes that the model would guide Congress in its revisions of the Internal Revenue Code, informed observers would view the ALI as taking on a doubly hopeless task—hopeless in terms of both the drafting challenge and the political challenge. Circumstances have changed drastically since 1954. The non-procedural aspects of the current federal income tax occupy nearly 2,350 pages of the current (2012) United States Code—more than six times the number of pages in the ALI’s draft.<sup>12</sup> If a 2013 model code were to approximate the level of detail of the current Internal Revenue Code, the drafting challenge would be several times more daunting than the challenge faced by the midcentury ALI. And today’s political barriers to the enactment of tax reform legislation dwarf those of 1954. As of 2012, virtually all Republican members of Congress had taken the no-tax-increase pledge of Grover Norquist’s Americans for Tax Reform,<sup>13</sup> and even a revenue-neutral Code revision focused on technical improvements would inevitably include many provisions that Norquist would describe as tax increases.<sup>14</sup>

Even granting these differences in circumstances, it is difficult for a tax lawyer in 2013, viewing the handiwork of the midcentury ALI’s tax experts, to resist the conclusion that tax giants once roamed the earth. Neither those giants nor their descendants have been spotted in recent decades. Although the ALI has remained active in the federal tax arena, producing a number of focused projects on particular aspects of the income tax (including the income taxation of corporations, partnerships,

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<sup>11</sup> William L. Cary, *Reflections Upon the American Law Institute Tax Project and the Internal Revenue Code: A Plea for a Moratorium and Reappraisal*, 60 COLUM. L. REV. 259, 261 (1960).

<sup>12</sup> The pages of the ALI Draft and those of the current Code are not strictly comparable. On the one hand, the Code fits more words on a page than does the ALI Draft. On the other hand, the Code contains copious information on effective dates and amendments, in addition to the Code itself. The differences work in opposite directions. It appears that the differences may approximately offset each other, in which case the page counts may, after all, give a good sense of the relative lengths of the two productions.

<sup>13</sup> Jonathan Weisman, *At Fiscal Cliff, Anti-Tax Vow Gets New Look*, N.Y. TIMES, July 18, 2012, at A1.

<sup>14</sup> To take an example more-or-less at random, the elimination of the charitable deduction for unrealized appreciation in donated property is something the ALI might propose as improving the structural coherence of the income tax, but it would undeniably result in tax increases for donors.

trusts, and estates),<sup>15</sup> it has never again attempted the drafting of a comprehensive model income tax statute.

This essay describes the ALI's Income Tax Project of 1948–1954—its origins, goals, drafting process, final product, and influence on Congress. The essay concludes with some thoughts on what role the ALI can and should play today in the tax legislative process. Whether the fault is in the stars or in ourselves (probably both, but with the stars deserving most of the blame), the drafting of a new ALI model income tax statute for the twenty-first century would be an almost insurmountable challenge in technical terms, and probably pointless in political terms. Nevertheless, there remains room for targeted ALI tax interventions, with a Restatement-type approach to the interpretation of the recently-codified economic substance doctrine<sup>16</sup> seeming especially promising.

#### I. THE MIDCENTURY INCOME TAX PROJECT: GENESIS, GOALS, AND PROCESS

The ALI's Income Tax Project began in 1948.<sup>17</sup> According to ALI Director Herbert Goodrich, in 1946 Colin Stam, the long-time Chief of Staff of the Joint Committee on Taxation,<sup>18</sup> informally suggested to Norris Darrell that an ALI-produced model income tax statute could be helpful to the Joint Committee and to Congress.<sup>19</sup> Leading members of the Senate Finance Committee and the House Ways and Means Committee added their unofficial encouragement, as did high-level Treasury officials.<sup>20</sup> ALI President Harrison Tweed told a slightly different version of the story. According to Tweed, the Project grew out of

some discussions which one of the members of our Council had . . . with representatives of the Treasury, the Joint Committee, and the

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<sup>15</sup> The ALI's post-1954 income tax projects are described *infra* notes 111-120 and accompanying text.

<sup>16</sup> 26 U.S.C. § 7701(o) (2011). The statute defines the doctrine as “the common law doctrine under which tax benefits under subtitle A with respect to a transaction are not allowable if the transaction does not have economic substance or lacks a business purpose.” *Id.*

<sup>17</sup> Darrell, *supra* note 9, at 17-18.

<sup>18</sup> “The Joint Committee on Taxation is a nonpartisan [congressional committee] . . . chaired on a rotating basis by the Chairman of the Senate Finance Committee and the Chairman of House Ways and Means Committee.” *Overview, JOINT COMMITTEE ON TAXATION*, <https://www.jct.gov/about-us/overview.html> (last visited Oct. 30, 2013) (providing a fuller description of the Committee).

<sup>19</sup> *General Revenue Provision: Hearing Before the H. Comm. on Ways and Means*, 83d Cong. 1812-13 (1953) [hereinafter *General Revenue Provision Hearings*] (statement of Herbert F. Goodrich, judge, U.S. Ct. of Appeals for the 3d Cir.).

<sup>20</sup> *Id.* at 1813; *see also* Darrell, *supra* note 9, at 17.

committees of the two Houses of Congress. They expressed the hope and the expectation that something might be done by the Institute to help in the situation which then existed and has existed for a long while, that the Income Tax Law needed overhauling and some fairly major changes and alterations in the judgment of a disinterested body.<sup>21</sup>

The ALI sought funding for the project from the Maurice and Laura Falk Foundation of Pittsburgh, and received an initial grant of \$225,000, later supplemented by additional grants, bringing the total to \$620,000<sup>22</sup> (over \$6 million in 2013 dollars).<sup>23</sup> Harvard Law School Professor Stanley S. Surrey was appointed Chief Reporter for the Project, and Columbia Law School Professor (later Dean) William C. Warren was appointed Associate Chief Reporter.<sup>24</sup> A small but elite army aided the reporters' efforts. The reporters were advised by a 10-member Tax Policy Committee consisting of eight leading tax attorneys, along with the President and the Director of the ALI.<sup>25</sup> The reporters were assisted by nine special consultants whose duties focused on various aspects of the Project.<sup>26</sup> The reporters also regularly sought the input of a Tax Advisory Group composed of the members of the Policy Committee, the special consultants, and more than 50 tax law luminaries from around the country.<sup>27</sup>

For several years the Policy Committee convened "about once a month for [a] one [or] two-day meeting[]" to determine the policies to be embodied in the model statute and to review proposed provisions drafted by the Reporters with the aid of their research assistants.<sup>28</sup> Following approval by the Policy Committee, proposed provisions were presented as discussion drafts to the Tax Advisory Committee at the annual meeting of the ALI.<sup>29</sup> After further revision in response to the comments of

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<sup>21</sup> A.L.I., *Remarks of Harrison Tweed*, 2 26TH ANN. MEETING OF THE ALI IN JOINT SESSION WITH THE NAT'L CONF. OF COMM'RS ON UNIF. STATE LAWS 618, 618-19 (1949) [hereinafter *Remarks of Harrison Tweed*].

<sup>22</sup> HERBERT F. GOODRICH & PAUL A. WOLKIN, *THE STORY OF THE AMERICAN LAW INSTITUTE, 1923-1961* 29 (1961).

<sup>23</sup> CPI Inflation Calculator, Bureau of Labor Statistics, [http://www.bls.gov/data/inflation\\_calculator.htm](http://www.bls.gov/data/inflation_calculator.htm) (input "620,000" in "\$" field, select "1948" in "in" dropdown menu, then click "calculate").

<sup>24</sup> GOODRICH & WOLKIN, *supra* note 22, at 30.

<sup>25</sup> 1954 DRAFT, *supra* note 5, at v. Norris Darrell, Erwin Griswold, and Randolph Paul were among the members of the Policy Committee.

<sup>26</sup> *Id.*

<sup>27</sup> *Id.* at vi. There was nary a woman among the seventy-two members of the Tax Advisory Group, although there were two women among the two-dozen research assistants to the reporters. *Id.* at vii.

<sup>28</sup> Stanley S. Surrey & William C. Warren, *The Income Tax Project of the American Law Institute: Gross Income, Deductions, Accounting, Gains and Losses, Cancellation of Indebtedness*, 66 HARV. L. REV. 761, 766 (1953).

<sup>29</sup> *Id.* at 767.

the Advisory Committee, the discussion drafts were presented to the 40-member governing Council of the ALI.<sup>30</sup> The reporters then prepared tentative drafts for presentation to the full membership of the ALI at its annual meetings.<sup>31</sup> All told, the reporters produced 11 tentative drafts.<sup>32</sup> In February 1954, with Congress at work on what was to become the Internal Revenue Code of 1954, the ALI published a compilation of the drafts and accompanying commentary as its “Federal Income Tax Statute, February 1954 Draft.”<sup>33</sup>

In the foreword to the Draft, ALI Director Goodrich explained that, unlike Restatements, the model statute and commentary had never been officially promulgated by the ALI.<sup>34</sup> He described the statute and commentary as “represent[ing] a composite of the views of [the] Tax Policy Committee and the Reporters assisted by the Special Consultants and guided by . . . the Tax Advisory Group, the Council of the Institute[,] and the Institute membership and by informal discussion with other organizations in the tax field.”<sup>35</sup> Noting the ongoing tax revision efforts in Congress, Goodrich observed, “If there ever was a time when an objective study would be helpful to a legislative group, . . . this seems to be the time.”<sup>36</sup> Four years earlier, near the inception of the Project, ALI President Tweed—who was obviously unable to imagine what the Internal Revenue Code would look like in 2013—had set a low bar for judging the Project’s real-world success: “Anything that is accomplished will be worthwhile, because the current situation . . . cannot be much worse.”<sup>37</sup>

In describing the goals of the Income Tax Project, the ALI explained that it intended to steer clear of political big-picture tax policy issues. Questions such as the design of the tax rate schedules, whether and how to tax capital gains, and the double taxation (or not) of corporate income, were all—emphasized Tweed—“fiscal and political questions into which it would serve no useful purpose for the Institute to plunge.”<sup>38</sup> The

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<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

<sup>32</sup> GOODRICH & WOLKIN, *supra* note 22, at 29.

<sup>33</sup> 1954 DRAFT, *supra* note 5.

<sup>34</sup> *Id.* at iv.

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Remarks of Harrison Tweed, supra* note 21, at 628.

<sup>38</sup> *Id.* at 624; *see also* Surrey & Warren, *supra* note 28, at 764 (making the same point and giving additional examples of political questions beyond the scope of the Project, including the tax treatment of municipal bond interest and the percentage depletion allowance).

Project's ambitions were, nevertheless, considerable. Tweed insisted that the goal was not "a mere statement of the law as it now stands,"<sup>39</sup> and Surrey and Warren concurred: "It is not a mere tinkering here and there, a tidying up of one provision or a smoothing out of another."<sup>40</sup> Rather, explained Surrey and Warren, the focus of the Project was on the "broad middle ground . . . which we have come to refer to as the 'technical' provisions of the income tax."<sup>41</sup> They elaborated: "The term 'technical' is used to contrast the provisions which are largely shaped by tax technicians . . . with the provisions whose content is determined by . . . political compromises."<sup>42</sup> Within that broad middle ground, Goodrich explained, the goal was not the ALI's usual goal of restatement: "Here in this field of legislative drafting we are frankly going to state the law as we think it should be."<sup>43</sup>

In an impressive display of self-confidence—if not hubris—Surrey and Warren described the Project as "a major frontal attack on the technical shortcomings of our federal income tax."<sup>44</sup> Because technical shortcomings permeated the entire Code, "All of the major segments of the income tax—gross income, deductions, gains and losses, accounting provisions, partnerships, trusts, corporations, income from sources abroad—are within [the Project's] scope."<sup>45</sup> Viewing such technical issues as essentially apolitical, Tweed claimed that the ALI's proposal would be drafted "by men who know their business but who have no political axes to grind and have no self-interest to serve."<sup>46</sup> Surrey and Warren acknowledged that the distinction between big-picture policy questions and technical issues could be indistinct at the margin, but they confidently asserted that "an awareness of the difference between the two and a desire to stay within the confines of technical policy afford proper guidance."<sup>47</sup>

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<sup>39</sup> *Remarks of Harrison Tweed, supra* note 21, at 624.

<sup>40</sup> Surrey & Warren, *supra* note 28, at 765.

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> Goodrich, *supra* note 2, at 18.

<sup>44</sup> Surrey & Warren, *supra* note 28, at 765.

<sup>45</sup> *Id.*

<sup>46</sup> *Remarks of Harrison Tweed, supra* note 21, at 629.

<sup>47</sup> Surrey & Warren, *supra* note 28, at 765. At least as of 1948, Judge Learned Hand was less sanguine about the possibility of separating the technical from the political. According to Goodrich, Hand remarked that "the subject will develop such a degree of heat among the members of the Institute that the Director should take the precaution to have a platoon of police officers on hand to assist the Chairman in preserving order." Goodrich, *supra* note 2, at 23.



In addition to the major goal of substantive technical improvement, the Project had a secondary goal of proposing a more user-friendly Internal Revenue Code. The drafters aimed to incorporate important judicial glosses into the statute itself, and to improve the clarity and readability of the statute.<sup>48</sup>

Writing in 1953, when most of the work of the Project had been accomplished but Congress had not yet legislated, Surrey and Warren pronounced the Project an unqualified success on the merits: “In no other tax forum has there been so fair, so objective, or so intelligent a consideration of technical tax issues . . . [F]or the first time in the history of the federal income tax we are becoming really aware of its anatomical structure, so to speak.”<sup>49</sup>

Although the influence of the Project on the 1954 Code can be gauged by comparing the ALI’s February 1954 Draft with the 1954 legislation (as discussed in the following section of this essay), there is little direct evidence of the extent to which the tax-writing committees of Congress and their staffs consulted with Surrey and Warren or worked from the ALI’s various tentative drafts. As Goodrich pointed out in his foreword to the February 1954 Draft, the ALI “does not lobby for this Code or any other piece of legislation.”<sup>50</sup> But as Tax Policy Committee member Robert Miller remarked, “There is no question, however, that the men who are engaged in these [ALI] efforts are favorably known to the congressional committees and their staffs, and that serious consideration will be given to the Institute’s recommendations.”<sup>51</sup>

ALI President Tweed reported in 1949 that Surrey and Warren had “been in close contact with representatives of the Joint Committee, and representatives of the Joint Committee ha[d] attended meetings of the Policy Committee’s hostings.”<sup>52</sup> According to Darrell, the Policy Committee, along with Surrey and Warren and their staff, had two meetings—one in 1953 and one in 1954—with the Joint Committee and Treasury staffs for wide-ranging discussions of the ALI’s drafts and the pending legislation.<sup>53</sup> Darrell also reported that in 1954 several of the people most closely connected with the Project “were

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<sup>48</sup> Goodrich, *supra* note 2, at 12-13; *see also* 1954 DRAFT, *supra* note 5, at xvii.

<sup>49</sup> Surrey & Warren, *supra* note 28, at 768.

<sup>50</sup> 1954 DRAFT, *supra* note 5, at iv.

<sup>51</sup> Robert N. Miller, *The Law Institute’s Income Tax Project: An Answer to a Challenge*, 37 A.B.A. J. 191, 194 (1951).

<sup>52</sup> *Remarks of Harrison Tweed*, *supra* note 21, at 621.

<sup>53</sup> Darrell, *supra* note 9, at 19.

repeatedly called upon for counsel and advice in connection with the revision of [the House bill].”<sup>54</sup>

The most prominent acknowledgment of the legislative influence of the ALI’s Income Tax Project occurred in August 1953, when ALI Director Goodrich appeared at a tax revision hearing of the Ways and Means Committee. Emphasizing that he was not “advocating this or any other publication,” Goodrich offered the Committee the material the Project had produced to that point.<sup>55</sup> In thanking Goodrich, Committee Chairman Daniel Reed commented, “You have undertaken what I consider a monumental and very important piece of work for the whole country, and you are making a very helpful contribution.”<sup>56</sup>

## II. A BRIEF DESCRIPTION OF THE ALI’S FEBRUARY 1954 DRAFT AND ITS INFLUENCE ON THE 1954 CODE

Judged on its merits, the February 1954 Draft largely fulfilled the ALI’s goals for the Income Tax Project. The model statute was clearly—at times even elegantly—drafted. Even William L. Cary, perhaps the harshest critic of the ALI’s decision to draft a highly detailed statute (by midcentury standards), who viewed the ALI’s alleged goal of “SPECIFICITY AT ALL COST” to have been “erroneously conceived,”<sup>57</sup> conceded that the ALI’s Draft was “well executed” by “superior craftsmen.”<sup>58</sup>

The successful effort to incorporate established judicial interpretations of the statute into the statute itself—so as to make finding the law much easier for non-specialist readers—is evident throughout the Draft, from the addition of a nonexclusive list of 20 items includible in gross income,<sup>59</sup> to a codification of the exclusion from gross income of working condition fringes,<sup>60</sup> to a comprehensive compilation of the

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<sup>54</sup> *Id.* at 20.

<sup>55</sup> *General Revenue Provision Hearings*, *supra* note 19, at 1814 (statement of Herbert F. Goodrich).

<sup>56</sup> *Id.* (remarks of Rep. Daniel Reed, Chairman, H. Comm. on Ways and Means).

<sup>57</sup> Cary, *supra* note 11, at 259, 261 (capitalization in original).

<sup>58</sup> *Id.* at 260, 261.

<sup>59</sup> 1954 DRAFT, *supra* note 5, at 25-27. This approach was followed by Congress. Internal Revenue Code of 1954, Pub. L. No. 83-591, § 61, 68A Stat. 3, 17 (codified at 26 U.S.C. § 61(a) (2011)).

<sup>60</sup> 1954 DRAFT, *supra* note 5, at 30. This approach was followed by Congress three decades later. Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 531(a), 98 Stat. 494, 877 (codified at 26 U.S.C. § 132(f) (2011)). Working condition fringes are in-kind benefits received by an employee from an employer, the cost of which would be deductible by the employee as a business expense if the employee had paid for the benefits herself.

various ways of obtaining a “cost” basis in an asset,<sup>61</sup> to a proposed codification of the doctrine of constructive receipt.<sup>62</sup> Surprisingly, however, in a few instances the Draft moved in the opposite direction, by eliminating existing statutory detail with the explanation that the detail would be better relegated to the regulations (but without offering a guiding principle as to when a detail belonged in the statute and when it belonged in the regulations).<sup>63</sup>

As the ALI drafters had promised, they did not limit themselves to a user-friendly restatement of existing tax law. They offered ambitious rewrites of substantial portions of the Internal Revenue Code, sometimes merely to incorporate judicial glosses into the statute, but often to resolve unsettled issues or to make significant substantive changes to settled law. For example, the Draft proposed a much more elaborate statutory treatment of cancellation-of-indebtedness income, which in some respects merely added to the statute well-established judicial (and administrative) interpretations, but in other cases resolved unsettled issues.<sup>64</sup>

Significant changes in the Code proposed by the Draft are far too numerous to describe them all here, but a few representative examples provide a sense of the Draft’s ambitions. Among many other changes, the Draft proposed:

- Nonrecognition of gain and loss, and a transferred basis regime, for property transferred in connection with a divorce;<sup>65</sup> Congress did not adopt this

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<sup>61</sup> 1954 DRAFT, *supra* note 5, at 118-20. Congress has never enacted a similar provision.

<sup>62</sup> *Id.* at 138-39. Again, Congress has never enacted a similar provision. Under the doctrine of constructive receipt, “A taxpayer may not deliberately turn his back upon income and thus select the year for which he will report it.” *Hamilton Nat’l Bank of Chattanooga v. Comm’r*, 29 B.T.A. 63, 67 (1933).

<sup>63</sup> 1954 DRAFT, *supra* note 5, at 107, 357 (moving from the statute to the regulations much of the detail concerning the nonrecognition of gain on the sale of a personal residence); *id.* at 148-49, 424 (moving details of the discount bond rules from the statute to the regulations).

<sup>64</sup> *See id.* at 34-43. One innovation of the ALI’s treatment of cancellation-of-indebtedness income was its choice of mistake-correction over balance-sheet as the exclusive theory of debt-cancellation income. *Id.* at 35. Despite the ALI’s efforts, this issue remains unresolved even today. Lawrence Zelenak, *Cancellation-of-Indebtedness Income and Transactional Accounting*, 29 VA. TAX REV. 277, 280-85 (2009) (describing the unsettled state of the law). Another ALI innovation was the explicit statutory adoption of a bifurcation approach to the disposition of property subject to a nonrecourse mortgage in excess of the value of the property. 1954 DRAFT, *supra* note 5, at 38. Decades later, the Supreme Court settled on a different approach. *Comm’r v. Tufts*, 461 U.S. 300, 307-08 (1983).

<sup>65</sup> 1954 DRAFT, *supra* note 5, at 28, 114.

approach in 1954, but finally did so three decades later.<sup>66</sup>

- A major revision of the rules for calculating the portion of an annuity payment excludable from gross income;<sup>67</sup> Congress adopted the ALI approach in the 1954 Code.<sup>68</sup>
- Elective relief provisions for taxpayers subject to either the tax benefit rule<sup>69</sup> or the claim of right doctrine<sup>70</sup> and adversely affected by differences in marginal tax rates in different years;<sup>71</sup> oddly, the 1954 Code followed the ALI approach in the case of the claim of right doctrine, but not in the case of the tax benefit rule.<sup>72</sup>
- Elimination of the rule generally permitting capital losses to be deducted only against capital gains;<sup>73</sup> Congress has never been persuaded to follow the ALI's lead on this issue.
- Extension of the nonrecognition treatment for exchanges of like-kind property to sales of like-kind property followed by purchases of like-kind replacement property;<sup>74</sup> neither the 1954 legislation nor later legislation adopted this proposal.
- Introducing the concept of “tainted” stock as a means of preventing the use of dividends of preferred stock as a device for distributing corporate earnings at capital

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<sup>66</sup> Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 421, 98 Stat. 494, 793-95.

<sup>67</sup> 1954 DRAFT, *supra* note 5, at 47.

<sup>68</sup> Internal Revenue Code of 1954, Pub. L. No. 83-591, § 72(b), 68A Stat. 3, 20 (codified at 26 U.S.C. § 72(b) (2011)).

<sup>69</sup> Under the tax benefit rule, if an event occurs in a later year which is fundamentally inconsistent with the taxpayer's claiming of a deduction in an earlier year, the taxpayer must offset the earlier deduction with a gross income inclusion in the later year. *Hillsboro Nat'l Bank v. Comm'r*, 460 U.S. 370, 383-85 (1983).

<sup>70</sup> Under the claim of right doctrine, if a taxpayer receives an amount in an earlier year under a “claim of right” and includes that amount in gross income, but the taxpayer is required to repay that amount because of developments in a later year, the taxpayer is entitled to a deduction for the repayment in the later year. *United States v. Lewis*, 340 U.S. 590, 591-92 (1951).

<sup>71</sup> 1954 DRAFT, *supra* note 5, at 157-60.

<sup>72</sup> Internal Revenue Code of 1954, § 1341, 68A Stat. at 348 (codified at 26 U.S.C. § 1341 (2011)).

<sup>73</sup> 1954 DRAFT, *supra* note 5, at 101-02.

<sup>74</sup> *Id.* at 106.

gains rates;<sup>75</sup> the 1954 Code took the same basic approach as the ALI's Draft.<sup>76</sup>

- Introduction of ownership attribution rules of mechanical application, for use in determining whether stock redemptions are to be taxed as dividends or as sales;<sup>77</sup> the 1954 Code followed the ALI's approach, with modifications.<sup>78</sup>
- Extension of the so-called *General Utilities* rule (under which a corporation did not recognize gain on the in-kind distribution to its shareholders of appreciated assets)<sup>79</sup> to sales of assets by a closely-held corporation in connection with a plan of complete liquidation;<sup>80</sup> the 1954 Code went even further, applying the ALI approach to all liquidating corporations, whether closely-held or public.<sup>81</sup>
- A major change in the continuity-of-interest rules for tax-free acquisitive reorganizations, under which satisfaction of the continuity requirement depended on the percentage of the stock of the acquiring corporation owned by the shareholders of the target corporation following the acquisition;<sup>82</sup> Congress has never enacted the ALI approach.<sup>83</sup>
- The elimination of rules against “thin incorporation”; under the ALI approach corporate debt owned proportionately to stock would never be reclassified merely because of the combination of the proportional

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<sup>75</sup> ALI VOLUME II, *supra* note 8, at 16-20.

<sup>76</sup> Internal Revenue Code of 1954, § 306, 68A Stat. at 90-93 (codified at 26 U.S.C. § 306).

<sup>77</sup> ALI VOLUME II, *supra* note 8, at 31-33.

<sup>78</sup> Internal Revenue Code of 1954, § 318, 68A Stat. at 99-101 (codified at 26 U.S.C. § 318).

<sup>79</sup> The doctrine's name is derived from the Supreme Court case acknowledging the existence of the doctrine. *Gen. Utils. & Operating Co. v. Comm'r*, 296 U.S. 200, 206 (1935).

<sup>80</sup> ALI VOLUME II, *supra* note 8, at 37-39.

<sup>81</sup> Internal Revenue Code of 1954, § 337, 68A Stat. at 106-07 (codified at 26 U.S.C. § 337).

<sup>82</sup> ALI VOLUME II, *supra* note 8, at 54-57.

<sup>83</sup> Norris Darrell, despite his overall enthusiasm for the ALI's February 1954 Draft, commented, “This particular provision in the Institute's draft may not have been a wise one; insufficient consideration may have been given to the theoretical or practical factors involved, or both.” Darrell, *supra* note 9, at 22.

ownership and a high ratio of insider debt to equity;<sup>84</sup> Congress also has never enacted this approach.

The February 1954 Draft also proposed comprehensive revisions of the provisions governing the income taxation of trusts and of partnerships,<sup>85</sup> and the influence of the draft on the 1954 legislation in these areas was immense.

As the legislative fates of the ALI provisions mentioned above suggest, the ALI was moderately successful in leaving its imprint on the Internal Revenue Code of 1954. Despite their deep disagreement on the merits of the Income Tax Project, William L. Cary and Norris Darrell agreed that the Draft played a major role in shaping the new Code.<sup>86</sup> The ALI Draft influenced both the style and the substance of the 1954 Code. In a number of areas, the Code followed the ALI's drafting preference for a more fully elaborated set of rules than had been featured in the 1939 version of the Code. Cary noted with disapproval, "In both instances [the 1954 Draft and the 1954 Code] the policy of the draftsmen seems to have been that tax statutes should be as specific, detailed, and inclusive as possible."<sup>87</sup> As for the ALI's substantive influence on the 1954 Code, the results were mixed.

The ALI cared enough about the extent of its influence to publish, early in 1955, a 30-page "Comparison of the American Law Institute February, 1954 Income Tax Draft and 1954 Internal Revenue Code."<sup>88</sup> There were major successes. As the ALI's Comparison observed, the partnership tax provisions of the 1954 Code were "almost entirely in accord with" the sweeping revisions of the ALI Draft.<sup>89</sup> The ALI enjoyed another major victory with respect to its proposed revisions of the income taxation of trusts, as to which the 1954 Code was, again, "almost entirely in accord with" the ALI Draft's "complete revision."<sup>90</sup> The 1954 Code also followed the ALI's lead on a number of narrower issues, including the formula for determining the nontaxable portion of an annuity payment, an attack on so-called preferred stock bailouts, the introduction of detailed ownership attribution

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<sup>84</sup> ALI VOLUME II, *supra* note 8, at 2-3, 231-32.

<sup>85</sup> *Id.* at 121-46 (trusts) and 86-119 (partnerships).

<sup>86</sup> *See supra* text accompanying notes 9-11.

<sup>87</sup> Cary, *supra* note 11, at 259.

<sup>88</sup> A.L.I., FEDERAL INCOME, ESTATE AND GIFT TAX PROJECT: COMPARISON OF THE AMERICAN LAW INSTITUTE FEBRUARY, 1954 INCOME TAX DRAFT AND 1954 INTERNAL REVENUE CODE (1955) [hereinafter ALI COMPARISON].

<sup>89</sup> *Id.* at 29.

<sup>90</sup> *Id.* at 28.

rules applicable to stock redemptions, and the extension of the *General Utilities* doctrine to asset sales in connection with a plan of complete liquidation.<sup>91</sup>

On the other hand, the new Code did not reflect the Draft's complete overhaul of the cancellation-of-indebtedness provisions, because (according to the ALI) Congress had decided that "more study [was] required."<sup>92</sup> Also left on the cutting room floor by Congress were (among many other items) the Draft's elimination of the limitations on the deductibility of capital losses, the extension of like-kind exchange gain nonrecognition to sales followed by reinvestments, and the elimination of the recharacterization of proportional debt as equity because of a high debt to equity ratio.<sup>93</sup>

In a few areas, the Draft's approach had no impact on the 1954 Code, but was adopted by Congress decades later. Examples include the enactment of an express gross income inclusion for working condition fringe benefits in 1984, and the adoption—also in 1984—of nonrecognition and transferred basis rules for property transferred in connection with a divorce.<sup>94</sup>

There may have been some veiled disappointment in ALI Director Goodrich's 1955 Annual Report that Congress was not more strongly influenced by the Draft:

We feel highly pleased with the contribution which our work made to the revision of the income tax law. No one ever expected the Congress to take it over bodily. Congress has its own responsibility on such things and also its own ideas. The most we hoped to do was to make a contribution on the technical side. That we did and that we shall continue to do.<sup>95</sup>

One suspects that Goodrich did not think it altogether a good thing that Congress had "its own ideas." Darrell's evaluation of the success of the Income Tax Project was similar to Goodrich's:

[N]o one, not even the Institute, could or did within reason expect this private work to be officially taken over intact. The most that could be or was hoped for was that a useful contribution could be made—that at least parts of the work would find favor. That, it would appear, has happened . . . I believe that the time spent by the

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<sup>91</sup> See *supra* text accompanying notes 67-68 (annuities), 75-76 (bailouts), 77-78 (attribution rules), and 80-81 (General Utilities).

<sup>92</sup> ALI COMPARISON, *supra* note 88, at 2.

<sup>93</sup> See *supra* text accompanying notes 73 (capital losses), 74 (like-kind nonrecognition), and 84 (debt-equity ratio).

<sup>94</sup> See *supra* text accompanying notes 60 (working condition fringes), and 65-66 (divorce-related property transfers).

<sup>95</sup> Herbert F. Goodrich, *Report of the Director*, 1955 A.L.I. ANN. REP. 5, 12.

Institute was well spent and that, viewed in retrospect, the project from the Institute's standpoint can be considered successful.<sup>96</sup>

Despite the hints of disappointment in the post-mortems of Goodrich and Darrell, the February 1954 Draft stands as a major accomplishment—not only on its merits, but also for the extent of its legislative influence. Given the immense difficulties of persuading Congress to enact tax reform legislation, for the Income Tax Project to have emerged from the 1954 legislative process with half a loaf of influence was no trifling achievement. That a group of private individuals could—without lobbying and solely on the merits of their proposals—have a significant impact on a major revision of the federal income tax is remarkable.

### III. EVALUATING THE PROJECT: THE ALI DRAFT, AVOIDING THE IMPORTANT ISSUES, AND THE DREAM OF A SIMPLE CODE

In the early 1960s two prominent tax professionals offered two criticisms of the ALI's 1954 Draft. Although the two criticisms were completely different in substance, they were alike in raising fundamental questions about the value of the ALI's efforts.

Writing in 1961, prominent tax practitioner Louis Eisenstein complained that the ALI's Project was insufficiently ambitious.<sup>97</sup> Although the ALI claimed to avoid broad policy questions and to concern itself only with technical matters, Eisenstein argued that the ALI's actual practice was to avoid controversial issues while attending only to questions that were noncontroversial (and therefore not very important):

Actually, the Institute handles many questions that are well within the realm of "broad" policy. It only avoids those which fail to evoke an "objective" spirit of togetherness . . . . On critical issues, then, the Institute is "nonpartisan" only in the sense that it is discreetly silent. If the Institute tried to speak, too many excited voices would be heard. It is not difficult to be nonpartisan if one studiously avoids partisan issues.<sup>98</sup>

There would have been little point, however, in the ALI's tackling any of the great tax policy controversies. The great policy issues—the extent of progression in the rate structure, for example—are intensely political. As an organization with members from across the political spectrum,

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<sup>96</sup> Darrell, *supra* note 9, at 25.

<sup>97</sup> LOUIS EISENSTEIN, *THE IDEOLOGIES OF TAXATION* 168-69 (2010).

<sup>98</sup> *Id.* at 168.



the ALI could not have reached a consensus on any of those issues. And even if by some miracle it had managed to do so, Congress would have had no interest in deferring to the ALI's judgment on (for example) the optimal tax rate schedule. Eisenstein was correct in his implication that the ALI was doing little more, metaphorically speaking, than rearranging the deck chairs on the ocean liner that was the Internal Revenue Code. In that sense, it was a modest project. But there is value to putting the deck chairs in order—as long as the ship is not sinking, and in 1954 few thought that it was.

The other criticism was William Cary's 1960 attack on the ALI's preferred style of statutory draftsmanship, which was considerably more detailed than that of the 1939 Code.<sup>99</sup> Although this critique found its fullest expression in Cary's post-Draft commentary, the ALI's preference for elaboration was controversial from the outset. At the 1949 ALI annual meeting, ALI President Tweed recounted that one of the original members of the Tax Policy Committee, Roscoe McGill, was so disappointed that the Committee had rejected the goal of a "short, concise tax statute" that he resigned from the Committee.<sup>100</sup>

From the perspective of 2013, it is difficult to evaluate the criticism of the February 1954 Draft as inordinately complex, because the Draft is immensely simpler than today's Internal Revenue Code. Cary does not claim that the Draft was the apotheosis of complexity; indeed he notes that the Draft's "emphasis on specificity is as nothing by comparison with the 1954 Code."<sup>101</sup> And although Cary could not have known it in 1960, the complexity of the 1954 Code is itself as nothing by comparison with that of today's Code.<sup>102</sup>

It is fair to say, however, that most of the post-1954 increase in statutory complexity is due to substantive policy choices of Congress, rather than to an ever-increasing preference for statutory specification of detail. Some of those post-1954 policy choices are widely applauded by tax technicians and policy analysts.<sup>103</sup> From today's perspective, the 1954 Code was

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<sup>99</sup> Cary, *supra* note 11.

<sup>100</sup> *Remarks of Harrison Tweed*, *supra* note 21, at 627.

<sup>101</sup> Cary, *supra* note 11, at 265.

<sup>102</sup> Cary did, however, fear that the worst was yet to come, writing, "Undoubtedly some committee will still be worrying about these problems [of thin incorporation and collapsible corporations] decades hence—when each of them may well occupy at least twenty pages of the code." *Id.* at 268.

<sup>103</sup> For example, despite the complexity of section 1272 (requiring current inclusion in gross income of original issue discount), few if any policy analysts would favor a return to the economically inaccurate approach of prior law.

shockingly defenseless against tax shelters.<sup>104</sup> The additional complexity attributable to various post-1954 anti-shelter provisions is a price worth paying to safeguard the integrity of the income tax.<sup>105</sup>

Much of the post-1954 increase in the length of the Code, however, is attributable to the proliferation in recent decades of tax expenditures of dubious merit. And much of the increase in tax return computational complexity is due to the alternative minimum tax (AMT) and various phaseout provisions—with both the AMT and the majority of the phaseouts being difficult or impossible to defend on the merits.<sup>106</sup>

Setting aside these post-1954 increases in the length of the Code attributable to substantive policy choices of Congress (some good, some bad), and focusing on Cary's question of the appropriate level of statutory detail to implement any given legislative policy, what are the merits of his critique of the ALI's drafting philosophy? As between Cary and the ALI, the ALI has by far the better of the argument. Consider what Cary offers as "[o]ne of the best illustrations of the ALI philosophy"<sup>107</sup>—its inclusion in the "keystone section" defining gross income of not only a general definition of gross income, but also a non-exclusive list of 20 items included in gross income. According to Cary, "no satisfactory function was served by meticulously cataloguing the various kinds of receipts that the courts have thus far held to be income."<sup>108</sup>

Cary's verdict has a whiff of unconscious elitism. Perhaps a list of 20 items included in gross income would have served no purpose for Cary, because he was already aware of all the judicial decisions distilled in the list. For a less expert reader of the Code, however, it would be immensely easier to determine the tax status of a particular type of receipt by finding it in a list of gross income inclusions, than by tracking down the authoritative judicial interpretation. Cary's focus is

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<sup>104</sup> Tax shelters were then in their infancy. The first modern tax shelter case to reach the Supreme Court, *Knetsch v. United States*, 364 U.S. 361, 362 (1960) (involving a shelter based on a tax-motivated combination of tax-preferred income and interest expense deductions), concerned tax years 1953 and 1954.

<sup>105</sup> Although there are a number of more-or-less complex post-1954 anti-shelter provisions, probably the most significant are the passive loss rules of § 469, enacted in 1986. Tax Reform Act of 1986, Pub. L. No. 99-514, § 501, 100 Stat. 2085, 2233 (codified at 26 U.S.C. § 469 (2011)).

<sup>106</sup> For a detailed discussion of the objections to the AMT and the various phaseouts, see Lawrence Zelenak, *Complex Tax Legislation in the TurboTax Era*, 1 COLUM. J. TAX L. 91, 98-115 (2010).

<sup>107</sup> Cary, *supra* note 11, at 265.

<sup>108</sup> *Id.* at 266.

on the Code's word count, rather than on the lived complexity of the tax laws. Even if the Code is considered in isolation—apart from its judicial and regulatory interpretations—Cary's view is mistaken. A list is not complex; exceptions to exceptions to exceptions generate complexity, but a mere list does not.

Cary makes a second, more important error—conflating the Code with the tax laws (which include judicial and administrative pronouncements, as well as the statute itself). Omitting the list from the gross income provision would make the *Code* shorter, but would actually make the *tax laws* more complex for the average reader. By incorporating into the statute important judicial glosses and administrative interpretations, the ALI's drafting strategy makes the tax laws simpler—more transparent, more accessible, more comprehensible—for the typical user. Cary never offers a satisfactory defense of his fetishization of a low statutory word count, even at the price of greater complexity of the tax laws in their entirety.

Cary does suggest an expertise-based reason for preferring a short and simple tax statute: "Congress . . . is performing the role formerly left to the Internal Revenue Service, the Treasury, and the courts, and at the same time has no thorough understanding of what it is enacting."<sup>109</sup> This aspect of Cary's critique does not depend on a fetishized concern with complexity in the *statute*, without regard to the overall complexity of the *laws*. One could conclude (correctly) that putting most of the details in the regulations rather than in the statute does not make the laws any simpler, and yet prefer putting the details in the regulations because the Treasury Department is likely to draft higher quality details than would Congress. Nevertheless, this aspect of Cary's critique is also unconvincing for two reasons. First, the question of the relative detail-drafting skills of the staffs of the Treasury and of the tax-writing committees in Congress is a highly contingent one, with different answers at different times (and perhaps even at any given time, for different issues). Second, this aspect of Cary's critique fails utterly as a criticism of the ALI Draft, because—as Cary himself conceded—the authors of the ALI Draft were "superior craftsmen."<sup>110</sup> There is no reason to suppose that the midcentury Treasury Department could have produced detailed regulations superior to the ALI's detailed statutory provisions.

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<sup>109</sup> *Id.* at 260.

<sup>110</sup> *Id.*

#### IV. POST-1954 ALI TAX PROJECTS, ACTUAL AND POTENTIAL

The ALI remained active in federal taxation after 1954. Its first major post-1954 tax production was a 1958 “Report of Working Views” (never submitted to the ALI membership for approval) on the “Income Tax Problems of Corporations and Shareholders.”<sup>111</sup> Writing in 1961, Director Goodrich and Associate Director Wolkin predicted that the ALI’s involvement in tax policy would continue “[a]s long as there is worthwhile work to do in the tax field.”<sup>112</sup>

The ensuing decades have borne out their prediction. Highlights have included estate and gift tax recommendations adopted by the ALI in 1968,<sup>113</sup> proposals for the reform of the tax treatment of corporate acquisitions and dispositions (1980),<sup>114</sup> proposals for the reform of the partnership tax provisions of the Code (1982),<sup>115</sup> proposals for the revision of the income taxation of trusts and estates (1984),<sup>116</sup> proposals for reform of the taxation of foreign persons and of foreign-source income (1986),<sup>117</sup> proposals regarding United States income tax treaties (1991),<sup>118</sup> a 1993 Reporter’s Study of corporate tax integration,<sup>119</sup> and a 1999 Reporter’s Study of the taxation of closely-held business enterprises.<sup>120</sup>

These proposals enjoyed a few legislative successes. For example, a 1958 proposal for a detailed statutory definition of corporate debt (as contrasted with equity)<sup>121</sup> foreshadowed the

<sup>111</sup> A.L.I., FEDERAL INCOME, ESTATE AND GIFT TAX PROJECT: INCOME TAX PROBLEMS OF CORPORATIONS AND SHAREHOLDERS (1958) [hereinafter ALI TAX PROBLEMS OF CORPORATIONS AND SHAREHOLDERS].

<sup>112</sup> GOODRICH & WOLKIN, *supra* note 22, at 31.

<sup>113</sup> A.L.I., WILLIAM D. ANDREWS, & A. JAMES CASNER, FEDERAL ESTATE AND GIFT TAXATION: RECOMMENDATIONS AND REPORTERS’ STUDIES (1969).

<sup>114</sup> A.L.I., FEDERAL INCOME TAX PROJECT SUBCHAPTER C: PROPOSALS ON CORPORATE ACQUISITIONS AND DISPOSITIONS (1982) [hereinafter ALI SUBCHAPTER C].

<sup>115</sup> A.L.I., FEDERAL INCOME TAX PROJECT SUBCHAPTER K: PROPOSALS ON THE TAXATION OF PARTNERS (1984).

<sup>116</sup> A.L.I., FEDERAL INCOME TAX PROJECT, SUBCHAPTER J: PROPOSALS ON THE TAXATION OF TRUST AND ESTATE INCOME AND INCOME IN RESPECT OF DECEDENTS (1985).

<sup>117</sup> A.L.I., FEDERAL INCOME TAX PROJECT: INTERNATIONAL ASPECTS OF UNITED STATES INCOME TAXATION: PROPOSALS ON UNITED STATES TAXATION OF FOREIGN PERSONS AND OF THE FOREIGN INCOME OF UNITED STATES PERSONS (1987).

<sup>118</sup> A.L.I., FEDERAL INCOME TAX PROJECT: INTERNATIONAL ASPECTS OF UNITED STATES INCOME TAXATION II: PROPOSALS ON UNITED STATES INCOME TAX TREATIES (1992).

<sup>119</sup> A.L.I. & ALVIN C. WARREN, JR., FEDERAL INCOME TAX PROJECT: INTEGRATION OF THE INDIVIDUAL AND CORPORATE INCOME TAXES AND REPORTER’S STUDY OF CORPORATE TAX INTEGRATION (1993).

<sup>120</sup> A.L.I., GEORGE K. YIN & DAVID J. SHAKOW, FEDERAL INCOME TAX PROJECT: TAXATION OF PRIVATE BUSINESS ENTERPRISES AND REPORTERS’ STUDY (1999).

<sup>121</sup> ALI TAX PROBLEMS OF CORPORATIONS AND SHAREHOLDERS, *supra* note 111, at 62-63.

1969 enactment of section 385 of the Code, which authorized the Treasury to promulgate detailed regulations distinguishing debt from equity.<sup>122</sup> Perhaps the most significant post-1954 ALI success in the tax legislative arena was the 1986 rejection of the *General Utilities* doctrine,<sup>123</sup> under which corporations had not recognized gain on the in-kind distribution of appreciated assets to their shareholders. The ALI's 1980 *Proposals on Corporate Acquisitions and Dispositions* had advocated the doctrine's demise,<sup>124</sup> and Congress complied six years later.

On the whole, however, the ALI's post-1954 tax efforts have found less favor with Congress than the 1954 Draft did. In part this may have been because the post-1954 proposals were often more legislatively ambitious than the 1954 Draft in calling for fundamental overhauls of some long-settled areas of the law—for example, the 1993 proposal for the integration of the corporate and individual income taxes, and the 1999 proposal of a new tax regime for private business enterprises.

Beyond the lesser influence on Congress of the later ALI proposals, the striking difference between the post-1954 ALI efforts and the 1954 Draft is the much narrower focus of the later projects. The 1954 Draft encompassed almost the entirety of the federal income tax; even viewed in the aggregate, the more recent efforts have grappled with only a few subchapters. Only once in the decades since 1954 has anyone even proposed an ALI tax project of comparable scope to the 1954 Draft. Writing in 1997, Harvard Law Professor Daniel Halperin argued that the income tax could be saved only if “we” could develop “a more accurate measure of income, one that would be simpler, more efficient, and most importantly, fair.”<sup>125</sup> For the project he envisioned, comparable in scope to the 1954 Draft, Halperin proposed the ALI's process:

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<sup>122</sup> Tax Reform Act of 1969, Pub. L. No. 91-172, § 415, 83 Stat. 487, 613-14 (codified at 26 U.S.C. § 385 (2011)). Although the enactment of § 385 counts as a legislative success for the ALI, § 385 itself was ultimately a failure. In 1983 the Treasury abandoned its efforts to promulgate regulations under its § 385 authority. Treatment of Certain Interests in Corporations as Stock or Indebtedness, 48 Fed. Reg. 31054 (July 6, 1983). Section 385 remains in the Code, but the Treasury has never resurrected the § 385 regulations project.

<sup>123</sup> Tax Reform Act of 1986, Pub. L. No. 99-514, § 631, 100 Stat. 2085, 2269-75 (codified at 26 U.S.C. §§ 311(b), 336).

<sup>124</sup> ALI SUBCHAPTER C, *supra* note 114, at 105-19. The ALI's was not the only voice calling for the demise of the doctrine. See George K. Yin, *General Utilities Repeal: Is Tax Reform Really Going to Pass It By?*, 31 TAX NOTES 1111, 1112 n.6 (1986) (citing a number of calls for the rejection of the doctrine, including that of the ALI; Yin also advocated the doctrine's demise).

<sup>125</sup> Daniel Halperin, *Saving the Income Tax: An Agenda for Research*, 77 TAX NOTES 967, 967-68 (1997).

What is essential is the ALI approach. Reporters to develop detailed proposals that can easily be translated into a statutory draft, or even a draft itself. Exposure of that draft to a diverse group of consultants who will take the time to examine it closely and debate it among themselves. Only in that way can we truly appreciate what is possible.<sup>126</sup>

Halperin's proposal was extremely ambitious, but no more so than the proposal leading to the 1954 Draft. Yet whereas the midcentury ALI eagerly accepted the challenge of drafting a nearly-complete income tax statute and brought the project to fruition, at the century's end neither the ALI nor any other organization showed any interest in responding to Halperin's call.<sup>127</sup>

Part of the explanation for the differing responses in the two eras may be that the Code has become too massive for anyone to contemplate a comprehensive revision in the spirit of the 1954 Draft. This would be especially true if a comprehensive twenty-first century income tax project were to follow the 1954 Draft's lead in proposing "technical" policy changes while taking as a given Congress's big-picture policy choices. The problem is that in 2013, much more than in 1954, Congress's big-picture policy choices mandate very high levels of statutory detail. Consider the original issue discount (OID) rules<sup>128</sup>—first enacted in 1969,<sup>129</sup> thoroughly revised in 1982,<sup>130</sup> and thoroughly revised again in 1984<sup>131</sup>—as one example drawn

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<sup>126</sup> *Id.* at 968.

<sup>127</sup> The closest thing to a response to Halperin's call is probably the "Shelf Project." Conceived and directed by Calvin H. Johnson, since 2007 the Project has published in *Tax Notes* dozens of proposals to raise revenue by broadening in principled ways the base of the income tax. Calvin H. Johnson, *The Shelf Project: Revenue-Raising Projects that Defend the Tax Base*, 117 TAX NOTES 1077 (2007) (announcing the Project); Calvin H. Johnson, *Two Years of the Shelf Project*, 126 TAX NOTES 513, (2010) (describing the early publications of the Project). However, the Project bears only a faint resemblance to the ALI's 1954 Draft, for two reasons. First, the Project picks its shots, by offering a number of narrowly targeted reform proposals rather than a complete model tax statute. Second, rather than representing a consensus of dozens of experts following several rounds of drafts and comments, the Project is largely the work of one man. See Calvin H. Johnson, *The Evolution of the Shelf Project*, 137 TAX NOTES 216, (2012) (noting that, as of September 2012, Johnson had authored 46 of the 67 published Shelf Project proposals).

<sup>128</sup> Original issue discount is the excess of a debt instrument's stated redemption price at maturity over its issue price. It serves as an economic substitute for explicitly-stated interest. Very generally, the OID rules provide for the identification of OID and for its taxation as interest income to the holder of the debt instrument.

<sup>129</sup> Tax Reform Act of 1969, Pub. L. No. 91-172, § 413(a), 83 Stat. 487, 609-11 (repealed 1984).

<sup>130</sup> Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, § 231, 96 Stat. 324, 496-99 (repealed 1984).

<sup>131</sup> Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 41, 98 Stat. 494, 531-43 (codified at 26 U.S.C. §§ 1271-75 (2011)).

from a large universe of potential examples. A twenty-first century income tax project might try to reduce somewhat the daunting complexity of the OID rules of the Code and regulations, but the project would have to take the existence of the OID rules as a given, because the decision to have such rules is a big-picture policy decision. There is no way to implement that policy decision with anything other than complex rules. The authors of the 1954 Draft were not faced with this source of complexity, because rules requiring bondholders to report OID prior to the receipt of cash did not exist at that time.

The same basic point could be made by reference to the anti-tax shelter passive loss rules enacted in 1986,<sup>132</sup> or any number of other inherently complex post-1954 provisions. Since 1954 Congress has made numerous big-picture policy choices that have, in the aggregate, hugely increased the Code's complexity. A comprehensive twenty-first century project in the spirit of the 1954 Draft would have to accept those choices. In accepting those choices, the drafters would be taking on a challenge many times more formidable than the challenge facing the midcentury drafters.

Perhaps the midcentury ALI had at its disposal the services of tax policy giants imbued with a postwar spirit of limitless optimism, and perhaps no such giants walk the earth today. But even the authors of the 1954 Draft would probably throw up their hands at the prospect of doing for today's Internal Revenue Code what they did for the Code of almost six decades ago. A bit of fudging was required to call the 1954 Draft a complete model income tax statute. With its omission of procedural provisions and some highly specialized substantive provisions,<sup>133</sup> the 1954 Draft was not quite a complete model statute. Today, however, no remotely plausible amount of fudging could make manageable a repeat of the midcentury project. The late 1940s and early 1950s presented a unique set of circumstances under which the 1954 Draft was possible: a Code still simple enough that a not-quite-complete draft of its revision could fit on a few hundred printed pages; an elite tax bar that had, perhaps, only recently become large enough and sophisticated enough to meet the challenge; and a pervasive postwar can-do spirit.

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<sup>132</sup> Tax Reform Act of 1986, Pub. L. No. 99-514, § 501, 100 Stat. 2085, 2233 (codified at 26 U.S.C. § 469).

<sup>133</sup> See *supra* note 6 and accompanying text.

A complete draft of a model income tax statute might be doable even today, if the drafters were willing to jettison the 1954 Draft's philosophy of accepting Congress's big-picture policy choices, and if the drafters consistently opted for simpler approaches than those of the current Code. But a model statute that paid no deference to existing legislative decisions on major policy questions would probably be of little or no interest to Congress. Thus, a major motivation for the authors of the 1954 Draft—the prospect that much of their work would find its way into the Internal Revenue Code—would be missing under this approach.

In sum, the drafting of a model statute accepting the major policy choices embodied in the current Internal Revenue Code is too daunting a task for the ALI (or anyone else), and the alternative of drafting a model statute without deference to existing legislative policy choices may be a quixotic endeavor if the goal is to influence legislation. As a result, we may never again see an income tax project—from the ALI or any other source—comparable to the 1954 Draft.

#### CONCLUSION

Despite the virtual impossibility today of a repeat of the ALI's 1954 performance, two promising avenues remain for ALI tax projects. The first is simply the continuation of the ALI's post-1954 approach of focusing on narrow aspects of the income tax—typically on one or another subchapter of the Code. In particular, one area comes to mind where an ALI project could perform a very valuable service. Congress recently codified the anti-tax-shelter economic substance doctrine,<sup>134</sup> but in such a way that most of the pre-codification judicial development of the doctrine retains its vitality. As it happens, however, the case law in this crucial area is a complete muddle.<sup>135</sup> An ALI Restatement of the economic substance doctrine—and it would be a Restatement, because the point of the project would be to bring order and clarity to existing law, rather than to change the law—could be tremendously useful to the courts, to taxpayers, and to the Internal Revenue Service.

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<sup>134</sup> Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, § 1409(a), 124 Stat. 1029, 1067-70 (codified at 26 U.S.C. § 7701(o) (2011)).

<sup>135</sup> On the existence of the muddle, see, e.g., David P. Hariton, *Sorting Out the Tangle of Economic Substance*, 52 TAX LAW. 235, 236 (1999). The doctrine has not become much less tangled in the years since Hariton's article appeared.



The second possibility is to reject the requirement that any project must have a high probability of being reflected in legislation in the near term. Having thrown off that constraint, the ALI's tax experts would be free to dream. Unfettered by a rule that only "technical" policy choices are up for grabs, the ALI's drafters might pursue Halperin's quest for a deep rethinking of the ways an income tax code measures income, or some other goal of equal audacity. The legislative prospects of such a project would surely be poorer than those of a project in the spirit of the 1954 Draft, but if enough legislators come to view the current income tax as fundamentally broken the odds against the legislative success of the project might not be impossibly long.