NEWS ANALYSIS

Further Studies in Federal Tax and the Supreme Court

by Marie Sapirie — marie.sapirie@taxanalysts.org

The prospect of a new justice joining the Supreme Court offers a good reason for reviewing its contributions to tax law, and a newly revised book on its tax jurisprudence from Jasper L. Cummings, Jr., fits that bill.

In The Supreme Court’s Federal Tax Jurisprudence, Cummings focuses on the fact-finding methods and statutory interpretation in the Court’s tax opinions. In the first edition, Cummings analyzed the over 900 federal tax cases the Court weighed in on through 2010, while in the revised version he reflects on the handful of opinions the Court has issued since, while also featuring additions that make it even more useful to tax lawyers. (Prior coverage: Tax Notes, Jan. 17, 2011, p. 343.)

The premise of Cummings’s book is that the “most authoritative and substantial body of principles for the application of the Code is the tax opinions of the Supreme Court of the United States.” He traces the logic of the Court’s opinions, from core concepts such as the definition of income to the development of positive rules of law such as the economic substance doctrine. By organizing the Supreme Court’s case law in that way, Cummings builds both a historical account and a roadmap for lawyers to distinguish cases and develop arguments. His observations range from the predictive (in the suggestion that the continued creation of anti-taxpayer rules could pave the way for a new, or partially new, system) to the practical (in a helpful list — and accompanying footnotes — of common statutory words the Court has defined).

In the preface, Cummings explains that his intent is both to create a treatise of black-letter law and to explode the idea that the federal tax laws are different from the rest of the law. He does both admirably.

Fact-Finding

The basic framework through which Cummings examines the Court’s tax cases is that tax cases in the federal district and circuit courts are too often analyzed on bases other than standard law and fact-finding, resulting in the creation and perpetuation of tax-specific doctrines by the lower courts. Cummings explains that these doctrines, with the exception of the economic substance doctrine, are nothing more than the applications of standard methods of fact-finding or legal interpretation that the lower courts have transposed into antiavoidance tools, sometimes in contrast to the Supreme Court’s opinions. He traces the evolution of interpretive presumptions in an effort to explain the tax-specific doctrines.

History in Context

The framework for Cummings’s discussion of the arc of the Court’s jurisprudence draws from scholarly work from the late 1930s and 1940s, which provides historical context that modern lawyers might not have studied. Looking back on the 1937 work of Randolph Paul, the founder of Paul, Weiss, Rifkind, Wharton & Garrison LLP, in developing a Restatement of the Law of Tax Avoidance, Cummings develops a schema of doctrines, and “cluster rules” of more limited scope, to draw connections between cases. The concept of cluster rules comes from a 1953 case law survey by Ralph S. Rice in the Michigan Law Review, which suggested tracking the evolving conclusions reached by courts in specific problem areas.

Cummings groups fact patterns or transactions that frequently recur in cases. He identifies the assignment of income doctrine as tax law’s primary cluster rule. “It had to be developed to prevent evasion of a progressive income tax, the utilization of one person’s favorable tax attributes by another, and the avoidance of one person’s unfavorable tax attributes,” he writes.

The references to scholarship that predates the 1986 tax code by at least four decades are not a nostalgic choice, but one driven by the timeline of Supreme Court tax jurisprudence. As Cummings explains, the heyday of Supreme Court tax cases was 1935, and the bulk of Supreme Court opinions on the code were issued before 1950.

The problem with rules that develop around fact clusters is that federal courts other than the Supreme Court tend to convert them into universal doctrines instead of keeping them limited in application, Cummings says. Contemporary cluster rules are creations of the lower federal courts because of the limited tax docket at the Supreme Court. Cummings convincingly argues that the utility of identifying cluster rules is that they can thereby be limited in their application to the facts for which they were developed.
Even though federal tax laws are the federal statutes most litigated in the Supreme Court, there has been a sharp decline in the number of tax opinions issued by the Court in recent years. Cummings acknowledges that his efforts in cataloging and synthesizing the Supreme Court tax jurisprudence might go underappreciated as the Court’s federal tax case load drops to near zero. “The role of the Supreme Court in generally fashioning the federal tax law over time has not been adequately appreciated and studied recently, although what it does in specific cases and areas and specific terms or periods has been well studied,” he writes.

As he ties together the Supreme Court’s cases, Cummings considers whether the Court’s interpretation of the code should be expansive, noting the inclusive income tax Congress instituted in 1913. “This assumes an overarching interpretational rule, which this book shows (perhaps unfortunately) does not exist,” he writes.

Although Cummings finds plenty of common threads in the Court’s tax jurisprudence, one area eludes synthesis. “The most debated issue in federal taxation is the location of the line between permitted intentional tax reduction and the tax reduction efforts that can lead to denial of desired tax benefits,” he writes. Still, Cummings identifies cluster areas around which legal rules, reporting, and disclosure requirements have coalesced, particularly deductions and losses, transactions with tax-indifferent persons, related-party transactions, partnership issues, and income shifting.

**Supreme Court Tax Doctrines**

Perhaps the most practical component of the book is Chapter VI, which functions as a restatement of the Supreme Court’s application of federal tax law. Cummings’s intent is that it “be a serviceable guide to all Code users,” and he achieves that. Attorneys can benefit from the concise statements of Supreme Court opinions and footnotes when drafting briefs, but the section should also be required reading for federal court law clerks who are assisting on their first tax case.


**Economic Substance Doctrine**

Cummings gives the economic substance doctrine an in-depth examination in the second edition. He criticizes the view that both the substance-over-form and business purpose doctrines originated in the Court’s 1935 *Gregory v. Helvering* decision. “In reality, *Gregory* was a case of statutory construction in which the Supreme Court construed a normal course of business requirement into the statutory words ‘in pursuance of a plan of reorganization,’” he writes. Moreover, Cummings finds that legal commentators at the time didn’t see *Gregory* as changing the entire universe of tax law interpretation.

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Noting that the code is designed to be a template to which events in their “natural state” can be fitted, Cummings calls the economic substance doctrine “the most dramatic response to the failure of [that] assumption.” He asserts that although the New Deal Court represented a pivotal turning point in tax law, it did not create the economic substance doctrine.

**Possible Solutions**

To fill the void left by the Court’s diminished role in supervising tax laws, Cummings suggests that Treasury increase its output of published guidance. However, in light of recent developments, particularly the 2-for-1 executive order on regulations, that may be difficult for the IRS and Treasury to accomplish.

Cummings concludes the second edition with the same observation he made seven years ago, namely that “the application of the federal tax laws both suffers and benefits from the absence of a cohesive view of the relationship of taxpayers to tax paying.” After analyzing how that void has been filled by tax-specific doctrines, and the economic substance doctrine in particular, Cummings suggests that taxpayer electivity and flexibility may in the future be further constrained, and then perhaps challenged, by reform efforts. That points to one more potential, but possibly less obvious, audience for the second edition: legislators.