ARTICLE

EVERYTHING IS TAX: EVALUATING THE STRUCTURAL TRANSFORMATION OF U.S. POLICYMAKING

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In contrast to major legislative reform packages in the 20th century, the Affordable Care Act of 2010 took the form of a tax bill. Although this legislation is the first massive social and regulatory overhaul completed through the tax code, in the past twenty-five years the U.S. Congress and presidential administrations have substantially increased their use of tax law for non-revenue-raising purposes. Growing reliance on the tax code represents a structural transformation of how Congress and presidential administrations have come to approach lawmaking goals. This transformation defies the near-consensus of previous tax scholarship, which, following Stanley Surrey, disapproves of embedding social and regulatory programs in the tax code. However, that dominant view rests on assumptions that have become outdated. This Article analyzes the ongoing structural transformation by observing and explaining the advantages that accrue from pursuing social and regulatory objectives through the tax code. In particular, this Article identifies a number of legislative and normative advantages that tax-embedded policies offer.

I. INTRODUCTION

For the past twenty-five years, Congress has been relying increasingly on the tax code[1] to accomplish goals beyond raising revenue. Taxpayers have quietly become accustomed to finding social and regulatory programs buried in the tax code. Perhaps as a result, no one has seemed to notice as Congress and presidential administrations have, more and more frequently, employed the tax code to accomplish goals that have nothing to do with raising revenue. In a 2011 speech, the Treasury Department's former Assistant Secretary for Tax Policy Pamela F. Olson explained that the tax code has recently come to incorporate "policies aimed at the environment, conservation, green energy, manufacturing, innovation, education, saving, retirement, health care, child care, welfare, corporate governance, export promotion, charitable giving, governance of tax exempt organizations, and economic development,

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[1] The phrase "tax code" refers to the Internal Revenue Code of 1986, as amended, found in Title 26 of the U.S. Code.

to name a few."[2] The Affordable Care Act is the latest and most significant example of this larger trend.

The day the Patient Protection and Affordable Care Act ("the Affordable Care Act")[3] passed marked a dramatic recent phase in this structural transformation of law and policymaking. Most observers know the Affordable Care Act as a major piece of social and regulatory legislation. However, they have failed to focus on the fact that the bill was in large part a tax bill. Many of the bill's major elements took the form of tax code provisions.[4] The bill's regulations were tax code penalties. The bill's subsidies were tax credits. The bill raised revenue through tax increases. The bill came out of the Congressional tax-writing committees. The Supreme Court upheld several of the bill's key provisions under Congress's taxing power.[5] The IRS will administer the bill. Tax lawyers will tell their clients how to comply with the bill. Tax commentators will write about the bill. Tax scholars will study the bill.

Tax scholarship has, until this point, generally criticized using the tax code to do anything except raise revenue. This critique has prevailed because every serious student of tax policy has had one great teacher from the last generation: Stanley Surrey. His agenda was to rid the tax code of non-revenue-raising provisions.[6] However, the world has changed radically since Surrey wrote. Today, embedding policy in the tax code looks very different from the way embedding policy in the tax code looked thirty years ago. As a result, it is past time for scholarship to rethink its instinctive objection to what has become a major structural transformation.

This Article is the first to take a comprehensive look at the potential advantages of embedding social and regulatory policy in the tax code. In particular, this Article identifies two types of advantages. The first are legislative advantages, which suggest why presidential administrations and members of Congress have pursued this structural transformation. The second are normative advantages of two types. One, placing social policy and regulation in the tax code advances distributive justice goals. Two, enacting major

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[2] Pamela F. Olson, Laurence Neal Woodworth Memorial Lecture: And Then Cnut Told Reagan . . . Lessons from the Tax Reform Act of 1986 (May 6, 2010) (transcript available at http://law.onu.edu/sites/default/files/Olson.pdf). The provisions to which Olson refers are I.R.C. §§ 21, 24, 25A, 25B, 32, 41 45, 45D, 45Q, 106(a), 114 (repealed in 2004), 162(m), 170(b)(1)(E), 174, 198, 199 174, 280G, 401(k), 403(b), 501, 864(b), 921–927 (repealed in 2000), 2031(c), 4064, 6707A(e), and 9507. *Id.*

[3] Patient Protection and Affordable Care Act ("Affordable Care Act"), Pub. L. No. 11-148, 124 Stat. 119 (2010) (to be codified as amended in scattered sections of I.R.C. and 42 U.S.C.).

[4] §§ 1402, 1411–1412, 1414–1415, 1421, 1502, 1514–1515, 3308(b), 6301, 9001–9015, 9017, 9021–9023, 10108, 10908.

[5] Nat'l Fed'n of Indep. Bus. v. Sebelius, 132 S. Ct. 2566 (2012).

[6] *See generally* Stanley S. Surrey, Pathways to Tax Reform (1973); Stanley S. Surrey & Paul R. McDaniel, Tax Expenditures (1985).

policy changes through the tax code has what I will call major "institutional" advantages, or effects created for, or by, political institutions.[7]

This Article will proceed in four sections. Section II will describe the current tax-oriented structural transformation and then will discuss why this transformation is not entirely consistent with the existing academic literature. Section III will consider the legislative advantages of this transformation. Section IV will turn to its normative advantages, both in terms of distributive justice and institutional effects. Section V will offer concluding thoughts.

II. The Structural Transformation

A. *Nature of Tax-Oriented Structural Transformation*

Throughout the last quarter century, the federal government has been increasing its use of the tax code to accomplish key objectives. Earlier in the 20th century, Congress and presidential administrations relied heavily on direct non-tax subsidies and regulations to achieve policy goals.[8] However, as former Assistant Secretary Olson so accurately observed,[9] more recently lawmakers have started embedding substantial amounts of policy in the tax code. These tax-embedded policies, which I define as policies enacted as provisions of the tax code and given to the IRS to administer, are rapidly sprouting up across many areas of the law.

To take one example, for most of the 20th century, in the social welfare area, the federal government's major initiatives were Aid to Families with Dependent Children, food stamps, Social Security, Medicare, and Medicaid. All of these were direct expenditure programs that distributed funds either immediately to recipients or through state governments. However, in recent years, the federal government has started turning the tax code into the primary vehicle to provide for new social welfare programs in the form of

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[7] By focusing on these advantages, this Article does not mean to suggest that embedding policies in the tax code is a good idea in all circumstances. However, in the years since Surrey wrote, the tax literature has exhaustively catalogued the many disadvantages of using the tax code for non-revenue raising purposes and largely ignored the advantages that this practice can offer. *See, e.g.*, Michael Graetz, The U.S. Income Tax 3–25 (1999); Anne Alstott, *The Earned Income Tax Credit and the Limitations of Tax-Based Welfare Reform*, 108 Harv. L. Rev. 533 (1995); William D. Andrews, *Personal Deductions in an Ideal Income Tax*, 86 Harv. L. Rev. 309 (1972); Mark G. Kelman, *Personal Deductions Revisited: Why They Fit Poorly in an "Ideal" Income Tax and Why They Fit Worse in a Far from Ideal World*, 31 Stan. L. Rev. 831 (1979); Edward Yorio, *The Future of Tax Reform: A Rejoinder to Professor Zelinsky*, 55 Fordham L. Rev. 899 (1987).

[8] In earlier years, architects of major legislative reforms would often enact tax provisions to pay for these reforms. As a result, major reform packages often included revenue-raising tax provisions and complex funding schemes enacted through the tax code. One key example of this was the Social Security Act. However, the shift described here focuses on using the tax code to accomplish goals besides raising revenue.

[9] Olson, *supra* note 2.

discounts off of tax bills. These discounts can be exclusions from income, deductions from income, nonrefundable credits against tax liability, or, as is increasingly common in recent years, refundable credits against tax liability—an option only used once before 1986.[10] The Earned Income Tax Credit ("EITC") has become the federal government's largest anti-poverty endeavor.[11] In addition, the federal government's latest new social initiatives almost all assume the shape of tax discounts: the empowerment zone credits,[12] the child credit,[13] the first-time homebuyer credit,[14] and expansions of the child care credit[15] and the personal and dependency exemptions.[16]

To take another example, this trend toward tax embedding has also emerged in the energy area. While the federal government used to subsidize energy primarily through direct grants by creating new agencies and spending programs,[17] the government has more recently turned to tax incentives to promote energy policy goals. In the past twenty-five years, Congress and presidential administrations have passed, among others, the energy-efficient homes credit,[18] the credits for residential and nonbusiness energy property,[19] the credit for electricity production from renewable resources,[20] the credit for use of new coal technologies,[21] the alternative motor vehicle credits,[22] the immediate deduction for mine safety equipment,[23] gain deferral on dispositions of energy transmission equipment,[24] and the credit for production from advanced nuclear power facilities.[25] In addition, according to scholarship on energy policy, "tax incentives dominated" 2005's energy policy legislation[26] which was "the most significant energy policy legislation" of the past fif-

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[10] As this Article will discuss in greater detail, a refundable credit is one where the taxpayer gets a refund from the IRS to the extent that the credit amount exceeds tax liability. For example, if a taxpayer has $100 in tax liability and is entitled to a $200 refundable credit, the credit will reduce the taxpayer's tax bill to 0, and the taxpayer will get $100 from the IRS.

[11] *See generally* Hilary Hoynes, *The Earned Income Tax Credit, Welfare Reform, and the Employment of Low-Skilled Single Mothers*, *in* Strategies for Improving Economic Mobility of Workers: Bridging Research and Practice 65 (Maude Toussaint-Comeau & Bruce D. Meyer, eds. 2009).

[12] I.R.C. § 1396 (2006).

[13] I.R.C. § 24 (2006 & Supp. IV 2010).

[14] I.R.C. § 36 (Supp. IV 2010).

[15] I.R.C. § 21 (2006 & Supp. I 2007).

[16] I.R.C. § 151(b)–(c) (2006).

[17] *See* Energy Information Agency, U.S. Dep't of Energy, Federal Financial Interventions and Subsidies in Energy Markets 1999: Energy Transformation and End Use 7–10 (2000), *available at* ftp://ftp.eia.doe.gov/service/oiaf0002.pdf.

[18] I.R.C. § 45L (2006 & Supp. IV 2010).

[19] I.R.C. § 25C (2006 & Supp. IV. 2010); I.R.C. § 25D (2006 & Supp. III 2009).

[20] I.R.C. § 48 (2006 & Supp. III 2009).

[21] I.R.C. § 48A (2006 & Supp. III 2009).

[22] I.R.C. § 30B (2006 & Supp. IV 2010).

[23] I.R.C. § 179E (2006 & Supp. IV 2010).

[24] I.R.C. § 451(i) (2006 & Supp. IV 2010).

[25] I.R.C. § 45J (2006 & Supp. IV 2010).

[26] Mona Hymel, *The United States' Experience With Energy-Based Tax Incentives: The Evidence Supporting Tax Incentives for Renewable Energy*, 38 Loy. U. Chi. L.J. 43, 43 (2007).

teen years.[27] As this energy scholarship suggests, when the federal government now wants to work on energy, it does so through tax law. Likewise, other areas of federal law, such as housing,[28] education,[29] community development[30] and scientific research[31] have witnessed similar patterns.

Stepping back from specific policy areas to view the landscape more broadly, since 1986, both the number of tax-embedded policies and the share of GDP that they represent have swelled. In 1981, the tax code contained 81 non-revenue-raising provisions.[32] By 2010, the number had climbed to 151, an increase of 86%.[33] While tax deductions have stayed relatively constant, credits, which have been the primary tool of this structural transformation, have gone from 0.3% of GDP in 1988 to 1.6% of GDP in 2010.[34] These increases suggest how often Congress is now using the tax code for non-revenue-raising purposes.

The Affordable Care Act marks the latest and most significant step in this structural transformation.[35] Four tax provisions—the premium assistance credit, the small business credit, the individual mandate, and the employer mandate—are the primary planks of the health care reform package. All of these take the form of tax code sections, and the IRS is responsible for administering all of them.

Looking at each in turn, first, the refundable "premium assistance credit" subsidizes the purchase of certain health insurance plans.[36] Individuals receive a premium assistance credit based on income, which the IRS pays directly to the insurance plan in which the individual is enrolled.[37] The individual then pays to the plan the difference between the premium tax credit

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[27] *Id.* at 51.

[28] *See, e.g.*, I.R.C. § 25C (2006 & Supp. IV 2010); I.R.C. § 25D (2006 & Supp. III 2009); I.R.C. § 36(a) (Supp. IV 2010); I.R.C. § 121 (2006 & Supp. IV 2010); I.R.C. § 179(d)(2) (2006 & Supp. IV 2010); I.R.C. § 460(e)(6)(B)(i) (2006 & Supp. IV 2010); I.R.C. § 702 (2006); I.R.C. § 1400I (2006).

[29] *See, e.g.*, I.R.C. § 25A (2006 & Supp. IV 2010); I.R.C. § 41(b)(3) (2006 & Supp. IV 2010); I.R.C. § 54E (Supp. IV 2010); I.R.C. § 108(f) (2006 & Supp. IV 2010); I.R.C. § 222 (2006 & Supp. IV 2010); I.R.C. § 529 (2006 & Supp. III 2009).

[30] *See, e.g.*, I.R.C. § 179(d)(2) (2006 & Supp. IV 2010); I.R.C. § 1396 (2006); I.R.C. § 1400E (2006); I.R.C. § 1400H (2006); I.R.C. § 1400I (2006), I.R.C. § 1400N (2006 & Supp. IV 2010); I.R.C. § 1400T (2006); Katrina Emergency Tax Relief Act of 2005, P.L. 109-73 § 201, 119 Stat. 2016, 2020–21.

[31] *See, e.g.*, I.R.C. § 41 (2006 & Supp. IV 2010); I.R.C. § 45C (2006 & Supp. IV 2010); I.R.C. § 45O (Supp. II 2008); I.R.C. § 48A (2006 & Supp. III 2009); I.R.C. § 48B (2006 & Supp. III 2009); I.R.C. § 48D (Supp. IV 2010).

[32] Suzanne Mettler, The Submerged State: How Invisible Government Policies Undermine American Democracy 20 (2011).

[33] *Id.*

[34] *Id.*

[35] Of course, the Affordable Care Act's thousand pages include several non-tax provisions. While the bill's major subsidies and regulations take the form of tax laws, a few of the bill's other innovations are not provisions that could fit easily into the tax code. Most notably, the rules for the state-based health care exchanges are not tax provisions.

[36] I.R.C. § 36B (Supp. V 2010).

[37] I.R.C. § 36B(b).

amount and the total plan premium.[38] Individuals and families with household incomes between 100% and 400% of the federal poverty level receive premium assistance credits on a sliding scale.[39] The scale ensures that those at 100% of the federal poverty level spend no more than 2% of income on health insurance premiums.[40] That percentage rises with income.[41] Individuals cannot receive the premium assistance credit along with employer-provided insurance.[42] The credit is refundable, so if individuals are entitled to credit amounts in excess of tax liability, the IRS will issue a refund equal to the difference.[43]

Second, the Affordable Care Act provides a tax credit for small businesses that offer their employees health insurance.[44] Under the provision, qualified small business employers can get nonrefundable tax credits for purchasing employee health insurance.[45] After 2013, the credit will only be available to employers that purchase health insurance coverage for employees through one of the new health insurance exchanges that the bill envisions states will establish.[46] The credit equals a set percentage of the small business employer's health insurance contribution per employee.[47]

The third major tax provision in the Affordable Care Act is what the popular press calls the "individual mandate." Under the individual mandate, starting in January of 2014, U.S. citizens must maintain what the bill calls "minimum essential" health insurance coverage.[48] Individuals who fail to maintain minimum essential coverage in 2016 are subject to a penalty, determined monthly, equal to the greater of: (1) 2.5% of household income in excess of the taxpayer's household income for the taxable year over a set threshold, or (2) $695 per uninsured adult in the household.[49] The fee for an uninsured individual under age eighteen is one-half of the adult fee.[50] The IRS cannot use liens or property seizures to collect the penalty, and individuals can apply for a hardship exemption to the mandate.[51]

In its fourth major tax provision, the Affordable Care Act also imposes a tax penalty on large employers that do not offer their full-time employees affordable health insurance.[52] If the employer does not offer sufficient coverage in a month, the penalty equals the number of full-time employees over a

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[38] *Id.*
[39] *Id.*
[40] *Id.*
[41] *Id.*
[42] I.R.C. § 36B(c).
[43] *Id.*
[44] I.R.C. § 45R (Supp. IV 2010).
[45] *Id.*
[46] *Id.*
[47] *Id.*
[48] I.R.C. § 5000A (Supp. IV 2010).
[49] I.R.C. § 5000A(c).
[50] *Id.*
[51] I.R.C. § 5000A(g).
[52] I.R.C. § 4980H (Supp. V 2011).

thirty-employee threshold during the applicable month multiplied by one-twelfth of $2,000.[53] If any of the employer's employees receives one of the Affordable Care Act's tax subsidies, the penalty for any month in which that is the case equals one-twelfth of $3,000 for every employee eligible to receive the subsidy.[54]

The Affordable Care Act also contains a long series of other tax provisions, each of which is an important piece of health care reform's architecture.[55] Taken together, these provisions amount to major tax legislation. The Supreme Court's 2012 decision upholding the legislation's penalties for failure to purchase health insurance under Congress's taxing power only highlights further the law's fundamental character as a tax law. The structural transformation in U.S. policymaking that has been underway for the past quarter century has culminated here.

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[53] I.R.C. § 4980H(c).

[54] I.R.C. § 4980H(b).

[55] These provisions are as follows: §§ 1402, 1411–1412 (tax credits that limit the extent to which recipients of the premium assistance credit have to share in their health insurance plan's costs); § 1414 (rules about disclosing health insurance information on tax returns); § 1415 (limits on the extent to which tax subsidies received under the Affordable Care Act can affect eligibility for other federal programs); § 9005 (changes to the tax rules for "cafeteria plans"); and § 6301 (a new "patient-centered outcomes research trust fund" funded through new taxes on health insurance policies). Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010) (to be codified as amended in scattered sections of I.R.C. and 42 U.S.C.). In addition to these, the bill contains various "revenue provisions," which also take the form of new tax laws. These include § 9001 (an excise tax on what the popular press calls "Cadillac plans"); § 9002 (the requirement that employers include the cost of employer-provided health care on employees' tax Forms W-2); § 9003–9004 (limits on tax-free distributions from health plans and certain savings accounts for health care); § 9005 (restrictions on other types of savings account for health care; § 9007 (additional rules for tax-exempt hospitals); § 9008 (a tax on pharmaceutical companies that create or import brand-name drugs); § 9009 (a tax on medical device manufacturers and importers); § 9010 (a tax on health insurance providers); § 9012 (repeal of the business deduction for certain retiree prescription drug plans); § 9013 (limits on the itemized deduction for medical expenses); § 9014 (restrictions on the extent to which health insurance providers can deduct executive salaries); § 9015 (a hospital insurance tax on high-income taxpayers); § 9016 (limits on deductions for property and casualty insurance companies); § 9017 (a tax on indoor tanning services known in the popular media as the "Snooki tax," after the well-known character on the reality television program "Jersey Shore"); § 9021 (an exclusion for health benefits from Indian tribes); § 9007 (now repealed, consisted of information reporting requirements on payments to corporations for goods and services); § 9022 (new "cafeteria plan" rules for small businesses); § 10908 (an exclusion for health care student loan forgiveness); § 9023 (an investment credit for therapeutic research); § 10108 (health care vouchers); § 10909 (an exclusion for employer-provided adoption assistance and an expansion of the adoption credit). *Id.* In the follow-up to the Affordable Care Act, Congress added still more tax provisions through the Health Care and Education Reconciliation Act of 2010, including § 1004(d) (changes to the rules for adult dependents and contributions to Medicare) and §§ 1408–1410 (limits on the cellulosic biofuel producer credit, new rules about the "economic substance" that transactions need to be respected for tax law purposes, changes to the timing for corporate estimated tax payments). Health Care and Education Reconciliation Act, Pub. L. No. 111-152, 124 Stat. 1029 (2010) (to be codified in scattered sections of I.R.C. and 42 U.S.C.).

B. A Transformation Defying Consensus in the Tax Community

Using the tax code for non-revenue-raising purposes has been under attack from the academic tax literature since the late 1960s, long before the current transformation was on the horizon. Non-revenue-raising tax provisions first received major criticism in the late 1960s and early 1970s. At this point, most of these non-revenue-raising tax provisions took the form of exclusions and deductions, often targeted toward businesses.[56] During this period, Assistant Secretary of the Treasury for Tax Policy, Stanley S. Surrey, whom many would call the most influential figure ever to hold the executive branch's highest tax policymaking position,[57] became famous for his campaign against what he called "tax expenditures."[58] For Surrey, who was also a professor at Harvard Law School, tax expenditures were "provisions of the Internal Revenue Code that are deliberate departures from generally accepted concepts of net income (usually by way of special exemptions, deductions, credits or exclusions) and that affect the private economy in ways that usually are accomplished by direct government spending."[59] In the view of the "tax expenditure literature" that Surrey launched, Congress was stuffing the tax code with expensive tax expenditure programs that imposed huge hidden burdens on the federal budget.[60]

At the heart of Surrey's critique was the argument that policymakers at the time did not recognize that a tax break subsidizing a certain activity was as expensive as a direct-spending program subsidizing the same thing.[61] In addition, programs implemented through the tax code had common shortcomings not found in their direct-spending counterparts. For these reasons, Surrey called for increased tax expenditure scrutiny that, in his opinion, would bring these facts to light and reduce the practice of embedding programs in the tax code.[62] In particular, he pushed Congress's Joint Committee

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[56] SURREY, *supra* note 6, at 60–65, 72–81.

[57] *See, e.g.*, Erwin N. Griswold, *In Memoriam: Stanley S. Surrey—A True Public Servant*, 98 HARV. L. REV. 329, 331 (1984) ("By common consent [Surrey] was the greatest tax scholar of his generation.").

[58] SURREY, *supra* note 6, at 3. This Article is more generally focused on cases in which Congress enacts any social and regulatory policies through the tax code. This includes implementing tax expenditures but also includes enacting a variety of other tax-embedded programs that would not qualify as tax expenditures. For example, one of the health care reform bill's major tax provisions is the penalty for individuals who do not carry insurance. This is an example of a regulatory policy carried out through the tax code that would not fall within Surrey's definition. There are many other such tax-embedded regulatory policies including a number of federal excise taxes on various purportedly harmful activities. All of these are part of the current structural transformation that is the subject of this Article. Therefore, while Surrey's critique would apply to certain key pieces of the structural transformation, it would not be relevant to all of it.

[59] JOINT COMM. ON TAXATION, A RECONSIDERATION OF TAX EXPENDITURE ANALYSIS, JCX-37-08, at 2 (2008).

[60] *Id.*

[61] SURREY, *supra* note 6, at 33–34.

[62] JOINT COMM. ON TAXATION, *supra* note 59, at 2.

on Taxation ("JCT") to publish what he called an annual "tax expenditure budget" that would expose tax expenditures and their costs and flaws.[63] He hoped that, "once tax expenditures were identified and clearly displayed as government spending substitutes, subsequent dissection would reveal them to be poorly targeted or inefficient, when compared either to an actual government spending program, or (in most cases) when compared to not expending government resources at all."[64] Further, in Surrey's words, "policymakers would recognize that many such proposals were inconsistent with the goal of a fair, efficient and simple income tax system."[65]

The tax policy community responded enthusiastically to Surrey's critique. For example, since 1974, federal legislation has required both the JCT, in conjunction with the Congressional Budget Office, and the Treasury Department to publish lists of tax expenditures and their costs.[66] What is more, politicians took up Surrey's call to arms. In 1969, following Surrey, Congress passed, and President Nixon signed, the Tax Reform Act of 1969.[67] This was the first major piece of legislation aimed at pruning tax provisions that had nothing to do with raising revenue.[68] However, while this law successfully excised a number of tax expenditures, it still left Surrey, the tax policy community, and powerful tax policymakers unsatisfied.[69] The years 1972[70] and 1976[71] saw further substantial efforts at "tax reform," although political obstacles at the time prevented these bills from cutting provisions very drastically.[72]

Even so, widespread opposition to using the tax code for non-revenue-raising purposes continued to grow, reaching a new height in the early 1980s. Two of the most prominent financial journalists writing about the problem in that period complained that "the code became like a giant Swiss cheese with too many holes. It was on the verge of collapse."[73] Some of the most powerful tax policymakers from both sides of the aisle shared this view that using the tax code for social and regulatory purposes was making the tax system "collapse."[74] Among the individuals who shared this perspective

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[63] Joint Comm. on Taxation, *supra* note 59, at 2.

[64] Joint Comm. on Taxation, *supra* note 59, at 2.

[65] Joint Comm. on Taxation, *supra* note 59, at 3.

[66] Joint Comm. on Taxation, Estimates of Fed. Tax Expenditures for Fiscal Years 2010–2014, JCS-3-10, at 3 (2010).

[67] Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487 (codified as amended in scattered sections of I.R.C.).

[68] *See generally* John Witte, The Politics and Development of the Federal Income Tax (1985).

[69] Surrey, *supra* note 6, at 5.

[70] *See* Michael J., Graetz, *Reflections on the Tax Legislative Process: Prelude to Reform*, 58 Va. L. Rev. 1389 (1972).

[71] Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520 (codified as amended in scattered sections I.R.C.).

[72] Surrey & McDaniel, *supra* note 6, at 34–37.

[73] Jeffrey H. Birnbaum & Alan Murray, Showdown at Gucci Gulch: Lawmakers, Lobbyists, and the Tax Reform Act of 1986 7 (1988).

[74] *Id.*

were Republican Treasury Secretaries Donald Regan and James Baker, Republican Senate Finance Committee Chair Robert Packwood (Or.), and Democratic House Ways & Means Committee Chair Dan Rostenkowski (Ill.).[75] These executive and legislative leaders, powerful tax figures of their generation, adopted Surrey's views in full and exerted Herculean effort—in the face of interest-group resistance—to rid the tax code of non-revenue-raising provisions through the Tax Reform Act of 1986.[76] Tax scholars debate the extent to which any part of this reform has lasted, but most agree that this was, at least at the time it passed, a landmark legislative accomplishment.[77]

Since Surrey's views first took hold in the 1960s, several tax scholars have begun to notice the positive features of tax expenditures that Surrey's wholesale critique neglected.[78] Even so, Surrey's critique maintains much of its original force among scholars. Indeed, many present-day scholars accept Surrey's critique as fundamentally correct. Tax scholar Edward Zelinsky has explained that "academics, government officials, journalists, and public interest advocates have concluded that the federal income tax ought to be purged of provisions identified as 'tax incentives' or 'tax expenditures.'"[79] Similarly, in more recent testimony about general tax reform before the Senate Finance Committee, Yale and Columbia tax professor Michael Graetz observed that

> [O]ur current individual income tax is a mess largely because our presidents and the Congress ask it to do too much. The result is a level of complexity that baffles experts, let alone ordinary Americans at tax time. Presidents and members of Congress from both political parties have come to believe that an income tax credit or deduction is the best prescription for virtually every economic and social problem our nation faces. In the process, we have turned the Internal Revenue Service from a tax collector into the administrator of many of the nation's most important spending programs.[80]

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[75] *Id.* at 19–22.

[76] *Id.* at 3–6.

[77] *See* Eric M. Patashnik, Reforms at Risk: What Happens After Major Policy Changes Are Enacted 35–55 (2008).

[78] *See*, *e.g.*, Nancy Staudt, *Redundant Tax and Spending Programs*, 100 Nw. U. L. Rev. 1197 (2006); Victor Thuronyi, *Tax Expenditures: A Reassessment*, 1988 Duke L.J. 1155 (1988); David A. Weisbach & Jacob Nussim, *The Integration of Tax and Spending Programs*, 113 Yale L.J. 955 (2004); David A. Weisbach, *Tax Expenditures, Principal-Agent Problems, and Redundancy*, 84 Wash. U. L. Rev. 1823 (2006); Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions*, 102 Yale L.J. 1165 (1993); Edward A. Zelinsky, *Efficiency and Income Taxes: The Rehabilitation of Tax Incentives*, 64 Tex. L. Rev. 973 (1986).

[79] Zelinsky, *Efficiency and Income Taxes*, *supra* note 78, at 973.

[80] *Does the Tax System Support Economic Efficiency, Job Creation and Broad-Based Economic Growth? Hearing on Tax Reform Before the S. Fin. Comm.*, 111th Cong. 10 (2011) (statement of Michael J. Graetz, Isidor and Seville Sulzbacher Professor of Law, Columbia Law School).

In related work, political scientist Suzanne Mettler also recently considered tax embedding.[81] In her view, the practice "threatens to undermine the basic principles encapsulated in the idea of 'government of the people, by the people, for the people.'"[82] Yet, despite the widespread acceptance of the views of Surrey and scholars working along similar lines, in the years since the Tax Reform Act of 1986, Congress has transformed its approach to social and regulatory policymaking into one that is overwhelmingly tax-oriented.

Significantly, however, the ongoing structural transformation involves none of the primary features of tax expenditures that motivated Surrey's critique. As a result, much of the literature based on Surrey's work does not apply to the current structural transformation.[83]

1. *Surrey's Distributional Critiques No Longer Apply*

When Surrey was writing, the tax code accomplished its non-revenue raising goals through exclusions and deductions. For this reason, Surrey's critique of the early tax expenditures rested, in the first instance, on *distributional* problems that he believed arise from embedding social and regulatory policy in the tax code. Surrey's distributional critique consisted of two primary arguments. Surrey's first distributional critique held that tax-embedded policies are "upside-down" subsidies.[84] He demonstrated that deductions and exclusions are worth more to taxpayers in higher tax brackets.[85] As a result, higher-income taxpayers walk away with the bulk of benefits distributed through the tax code. For this reason, Surrey concluded that putting subsidies in the tax code "is the primary source of unfairness in our tax

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[81] Mettler, *supra* note 32, at 26.

[82] *Id.*

[83] Some scholars have considered one or two positive features of the transformation. *See, e.g.*, Ruth Mason, *Federalism and the Taxing Power*, 99 CAL. L. REV. 975 (2011); Staudt, *supra* note 78; Weisbach, *Tax Expenditures, Principal-Agent Problems, and Redundancy*, *supra* note 78; Edward A. Zelinsky, *Do Tax Expenditures Create Framing Effects? Volunteer Firefighters, Property Tax Exemptions, and the Paradox of Tax Expenditure Analysis*, 24 VA. TAX REV. 797 (2005); Zelinsky, *James Madison and Public Choice at Gucci Gulch, supra* note 78; Zelinsky, *Efficiency and Income Taxes, supra* note 78. Others have considered how well a single tax-embedded program works. *See, e.g.*, Alstott, *supra* note 7; Dennis J. Ventry, Jr., *Welfare By Any Other Name: Tax Transfers and the EITC*, 56 AM. U. L. REV. 1261 (2007); Weisbach & Nussim, *supra* note 78.

[84] SURREY, *supra* note 6, at 37.

[85] Surrey accurately observes that this is the case because the value of a deduction or an exclusion to a taxpayer equals the dollar amount of the deduction or exclusion multiplied by the taxpayer's marginal rate. For example, imagine two single taxpayers, one making $10,000 in gross income and in the 15% bracket and the other making $50,000 in gross income and in the 25% bracket. Each receives a $2,000 deduction. Taxpayer A's taxable income falls by $2,000. As a result, her tax liability falls by $2,000 multiplied by her 15% marginal rate, or by $300. Taxpayer B's taxable income also falls by $2,000. As a result, her tax liability falls by $2,000 multiplied by her 25% marginal rate, or by $500. Due to her lower marginal rate, Taxpayer A's deduction was worth $200 less to her than to Taxpayer B. This is the "upside-down" effect that Surrey noted. *Id.*

system."[86] Looking at tax-embedded programs in 1973, he complained that, "[o]n the average, [through the tax system], the individual with $3,000 is given an annual grant of a dollar. The millionaire is given an annual grant of $725,865. Whatever may be the defects of direct subsidies, they scarcely have this bizarre distributional effect."[87]

However, Surrey's upside-down subsidies distributional critique no longer applies. When Surrey published his updated tax expenditure critique in 1985, the tax code included only one refundable credit.[88] Given this, his work never accounted for the fact that refundable credits are a way to accomplish goals through the tax code without creating upside-down subsidies. Perhaps because the tax policy community listened so closely to Surrey, almost all of the most recently enacted tax-embedded social programs have taken the form of refundable credits.[89] For example, the Affordable Care Act's primary program for low- to middle-income families, the premium assistance credit, is a refundable credit. The EITC—currently the federal government's largest anti-poverty program as mentioned above—also takes the form of a refundable credit. The child tax credit is a partially refundable credit.[90]

Refundable credits completely solve the upside-down subsidy problem that Surrey identified. The value of a refundable credit is not higher for higher-bracket taxpayers, and the value does not depend on tax liability. If a taxpayer is entitled to a refundable credit of a certain amount, say, $2,000, the taxpayer will get $2,000 regardless of bracket or tax liability. A refundable credit is thus worth the same dollar amount to every eligible taxpayer.[91]

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[86] *Id.* at 69.

[87] *Id.* at 72 tbl.3.8.

[88] This sole refundable credit was the earned income tax credit. *See* SURREY & MCDANIEL, *supra* note 6, at 39. *See also* Brian Jenn, *The Case for Tax Credits*, 61 TAX LAW. 549 (2008).

[89] *See, e.g.*, I.R.C. § 23 (2006 & Supp. IV 2010) (adoption expense credit); I.R.C. § 24 (2006 & Supp. IV 2010) (child tax credit); I.R.C. § 25A (2006 & Supp. IV 2010) (modified Hope credit/American Opportunity tax credit); I.R.C. § 35(a) (2006 & Supp. V 2011) (health coverage tax credit); I.R.C. § 36(a) (2006 & Supp. IV 2010) (first-time homebuyer credit); I.R.C. § 36A (2006 & Supp. III 2009) (Making Work Pay credit); I.R.C. § 36B (2006 & Supp. V 2011) (health insurance premium credit); I.R.C. § 6426(a)(2) (2006 & Supp. IV 2010) (alternative fuel credit, *see* I.R.S. Notice 2006-92, 2006-2 C.B. 774); I.R.C. § 6428 (2006 & Supp. II 2008) (recovery rebate credit); I.R.C. § 6431 (2006 & Supp. IV 2010) (five refundable credits for issuers of certain bonds); JOINT COMM. ON TAXATION, TECHNICAL EXPLANATION OF THE REVENUE PROVISIONS OF H.R. 5140, THE "ECON. STIMULUS ACT of 2008" AS PASSED BY THE HOUSE OF REPRESENTATIVES AND THE SENATE ON FEBRUARY 7, 2008, JCX-16-08, at 2–7 (2008). American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, § 2202 123 Stat. 115, 454–55 (government retiree credit); Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, Pub. L. No. 111-312 §§ 701(c), 704(c), 124 Stat. 3296, 3310–11 (2010) (cellulosic biofuel credit).

[90] Of course, many major non-revenue-raising tax policies enacted before the current ongoing structural transformation still take the form of exclusions and deductions and raise the upside-down subsidy problem. For this reason, while Surrey's critique does not apply to this transformation, Congress still may want to address the upside-down subsidy issue by converting existing exclusions and deductions into credits. *See* Jenn, *supra* note 88.

[91] Congress has also used progressive phaseouts to solve the distributional problem that Surrey identified. See *infra* Part IV for further discussion of this approach.

For this reason, enacting social or regulatory policy through a refundable credit entirely fixes the upside-down subsidy problem that Surrey identified.

Further, Congress has regularly structured and restructured even those tax-embedded programs that do not take the form of refundable credits to tilt them toward lower-income taxpayers. For example, the child care credit allows taxpayers to take nonrefundable credits for amounts paid for child care. The amount of the credit varies inversely with income. If adjusted gross income is $15,000 or less, the credit equals 35% of eligible child care expenses. This percentage falls by 1% for each $2,000 of adjusted gross income (or fraction thereof) in excess of $10,000 down to a minimum of 20% for taxpayers with AGI over $43,000.[92] Congress has enacted a number of similar progressive phaseouts for tax-embedded subsidies such as the child tax credit,[93] the education credits,[94] the first-time homebuyer credit,[95] the exclusion of interest on savings bonds redeemed for higher education expenses,[96] the student loan interest deduction[97] and the personal exemption.[98] These phaseouts are another way in which Congress has directly addressed Surrey's upside-down subsidy distribution-based critique.

Surrey's second distributional critique charged that the tax code was a home only for policies aimed at wealthy individuals and businesses. Surrey accurately observed that, at the time he was writing, Congress purposefully directed almost all tax expenditures toward higher-income individuals and corporations.[99] Surrey maintained that almost all of the subsidies embedded in the tax code helped these groups, while "no assistance is given by these tax expenditures to individuals too poor to pay an income tax"[100] and any benefit that tax expenditures gave to lower-income groups was "almost entirely limited to the elderly."[101] However, this charge is another piece of Surrey's analysis that does not apply to the current transformation. Since Surrey's time, Congress has enacted many major programs for low- and middle-income families through the tax code, including the EITC,[102] the child tax credit,[103] the child care credit,[104] the deduction for dependent care assistance,[105] the education credits,[106] the adoption credit,[107] renewal community

[92] I.R.C. § 21(a)(2) (2006 & Supp. I 2007); 26 C.F.R. § 1.21-1(a)(2) (2007).
[93] I.R.C. § 24(b) (2006 & Supp. IV 2010).
[94] I.R.C. § 25A(h)(2) (2006 & Supp. IV 2010).
[95] I.R.C. § 36(b)(2)(A) (2006 & Supp. V. 2011).
[96] I.R.C. § 135(b)(2) (2006).
[97] I.R.C. § 221(b)(2) (2006).
[98] I.R.C. § 151(d)(3) (2006).
[99] Surrey, *supra* note 6, at 60–67, 78–80.
[100] Surrey, *supra* note 6, at 68.
[101] Surrey, *supra* note 6, at 68.
[102] I.R.C. § 32 (2006 & Supp. IV 2010).
[103] I.R.C. § 24 (2006 & Supp. IV 2010).
[104] I.R.C. § 21 (2006 & Supp. I 2007).
[105] I.R.C. § 129 (2006).
[106] I.R.C. § 25A (2006 & Supp. IV 2010).
[107] I.R.C. § 23 (2006 & Supp. IV 2010).

credits[108] and the first-time homebuyer credit.[109] The tax provisions of the Affordable Care Act are part of a major legislative scheme to help low- and middle-income families purchase health care. As the transformation proceeds, Congress is likely to do even more of its social policy geared toward low- and middle-income families through the tax code. This may be particularly true given the fact that the Supreme Court upheld key sections of the Affordable Care Act under Congress's taxing power. For this reason, this distributional critique does not apply with the same force.

2. *Surrey's Transparency Critique No Longer Applies*

In addition to highlighting distributional problems, Surrey objected to putting non-revenue-raising policies in the tax code on the grounds that these policies lack transparency. According to Surrey, neither members of Congress nor the general public understood that discounts off of tax bills are government subsidies. In view of this defective understanding, a member of Congress could seek to enact a social or regulatory program through the tax code without sufficient public accountability.

This lack of transparency problem, however, is another that has long since passed, thanks, in fact, to Surrey's own efforts. At Surrey's urging, the Congressional Budget Office, the Joint Committee on Taxation, and the Treasury now publish highly visible annual lists of tax expenditures that show both how much money these cost the government and how those costs fall among different income groups.[110] These lists have become particularly salient as Congress has, in the past twenty years, passed a number of new rules requiring new tax subsidies to be offset with cuts in existing ones.[111] Tax scholar Elizabeth Garrett has described the attention that the tax expenditure estimates now garner:

> Interest groups comb these lists, paying special attention to upward revisions in revenue estimates. . . . Public interest organizations and think tanks also produce documents that can be scoured for offsets, and boutique Washington firms specialize in identifying and drafting suitable offsets for those seeking new tax subsidies. Groups may publicize negative aspects of tax subsidies that benefit their competitors either to level the playing field or to gain a competitive advantage.[112]

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[108] I.R.C. § 1400H (2006).

[109] I.R.C. § 36(a) (Supp. IV 2010) (now defunct).

[110] JOINT COMM. ON TAXATION, *supra* note 59, at 3.

[111] *See, e.g.*, 2 U.S.C. § 902 (2006) (requiring legislation that increase the deficit to trigger offsetting budget cuts); *see also* Elizabeth Garrett, *Harnessing Politics: The Dynamics of Offset Requirements in the Tax Legislative Process*, 65 U. CHI. L. REV. 501, 512–13 (1998) (describing parliamentary procedures in the Senate used to enforce its pay-as-you-go provision).

[112] Garrett, *supra* note 111, at 517–18.

As a consequence of dynamics such as these, non-revenue-raising tax code provisions are substantially more visible than they were when Surrey conducted his analysis. Further, the particular tax provisions that Surrey singled out for criticism because of their invisibility were provisions that entered the tax code as small pieces of lengthy and often unrelated bills.[113] However, at the current point in time, the policymaking transformation has so advanced that lawmakers enact not just minor subsidies but major legislative reform packages through the tax code. These packages are so visible to relevant constituencies that lawmakers cannot try to hide the legislation through the tax code or otherwise. Although the general public could certainly still stand to learn more about tax-embedded policies and how they work, Surrey's picture of covert efforts to sneak programs into law unnoticed through the tax code fails to make sense when extended to bills as prominent as the 2005 energy bill or, particularly, the Affordable Care Act. What is more, as the following sections will observe, there are now various ways in which relevant stakeholders can become aware of and involved in forming tax-embedded policy.

III. Legislative Advantages

Programs embedded in the tax code have certain features that make them easier to enact and maintain than equivalent programs enacted outside of the tax code. I call these features the legislative advantages of tax-embedded programs. A social program or a regulation enacted through the tax code generally has a very different trajectory than a program or regulation that is otherwise the same but enacted through some other area of the law.

The fact that implementing a program through the tax code influences how the program will develop is not surprising in light of political science research on the politics of social policy. Recent scholarship in that area has demonstrated how early policy-design decisions can powerfully shape the ways in which a particular social policy will develop over time. Political scientists, accordingly, often describe social policies in terms of "path dependence"—the tendency of a policy to bear the heavy impress of its origins for years afterwards—and research shows that some policies are more likely to exhibit path-dependent properties than others. In his pioneering 2002 study of this topic, Jacob Hacker finds that tax policy is particularly susceptible to the mechanisms of path dependence.[114] For this reason, the choice to

[113] Surrey, *supra* note 6, at 5–6.

[114] This literature diverges from earlier political-science scholarship that emphasized the ways in which macro-level political shifts, rather than aspects of a policy itself, shape a policy's future. *See generally* Jacob S. Hacker, The Divided Welfare State: The Battle Over Public and Private Social Benefits in the United States (2002); Paul Pierson, *Increasing Returns, Path Dependence, and the Study of Politics*, 94 Am. Pol. Sci. Rev. 251 (2000); Paul Pierson, *Not Just What, But When: Timing and Sequence in Political Processes*, 14 Stud. in Am. Pol. Dev. 72 (2000); Theda Skocpol, Protecting Soldiers and Mothers: The Political Origins of Social Policy in the United States (1995).

embed a policy in the tax code will be particularly important to what happens to that policy over time.

This research on path dependence also suggests that the decision to implement a policy through the tax code affects not just how that policy will develop in the long term, but how easy that policy will be to enact in the first place. Congress's procedures and rules treat tax laws differently than other laws. For this reason, tax laws can gain initial advantages over non-tax counterparts and those advantages may only grow, in the manner that path dependence scholars would suggest, over time. Further, some of these advantages may help to explain why Congress now so frequently uses the tax code for non-revenue-raising purposes. Members of Congress who select the tax code as the vehicle for a program of choice may be aware of these advantages and seek to use them to advance that program.[115]

A. Proposed Tax-Embedded Programs Have Smoother Routes Through Congress Than Corresponding Direct-Spending Programs.

The legislative advantages of tax-embedded programs start with these programs' relatively smooth routes through Congress. A tax-embedded social program or regulation may have a much easier time winding its way through the procedural hurdles of the legislative process than a similar law proposed in a non-tax area. This is the case for four main reasons.

First, the particular committees that handle tax-embedded programs smooth their legislative paths through Congress. New tax laws are the province of Congress's tax-writing committees, called the House Ways & Means Committee and the Senate Finance Committee.[116] The House Ways & Means Committee, where all tax bills originate, is relatively effective at getting legislation through Congress.[117] This is in part because Ways & Means has traditionally had very powerful leadership.[118] Ways & Means is one of the most coveted committee assignments in the House, and the members have gener-

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[115] This section describes relatively entrenched features of the legislative process. Congressional reformers might reasonably hope to redesign some of these features at some future point. How reformers might do this in ways that would improve tax policymaking is an interesting topic for future research.

[116] *See* STANDING RULES OF THE SENATE, Rule XXV, Cl. 1(i), 111th Cong. (2009); RULES OF THE HOUSE OF REPRESENTATIVES, Rule X, Cl. 1(t), 111th Cong. (2009).

[117] The word "relatively" here points to the fact that the tax-writing committees, like all political institutions, have substantial flaws. Given the numbers of people affected and the complexity of the issues involved, no political institution can handle tax issues perfectly. However, the particular advantages and flaws of the tax-writing committees make them the best of the highly imperfect alternative possible venues for making tax policy. For more on why and how lawmakers must select among less-than-ideal institutions and about the type of comparative institutional analysis I am using here, *see* NEIL K. KOMESAR, IMPERFECT ALTERNATIVES—CHOOSING INSTITUTIONS IN LAW, ECONOMICS, AND PUBLIC POLICY (1994).

[118] RICHARD F. FENNO, CONGRESSMEN IN COMMITTEES 114–18 (1973). *See also* RICHARD F. FENNO, LEARNING TO GOVERN: AN INSTITUTIONAL VIEW OF THE U.S. CONGRESS (1997).

ally spent decades accumulating power within the chamber.[119] In addition, the Ways & Means Committee has a particularly good reputation in the House because the committee has historically cultivated credibility. Research on Congressional committees has shown that the primary goal of Ways & Means is to craft bills that will pass the parent chamber[120] and to maintain a relationship with the parent chamber that is "influential" and "responsive" to members' preferences.[121] Data suggest that the tax-writing committees reflect fairly well the distribution of preferences within their party caucuses and, as a result, within their chambers,[122] making Ways & Means a committee on which the House majority can rely for "good" legislation that the chamber could pass.[123] All of these features that grease the policymaking wheels at Ways & Means similarly characterize the Senate Finance Committee.[124]

Second, many tax bills enjoy certain formal procedural protections, and three of these protections are discussed in subpoints A, B and C. (A) Bills from Ways & Means go to the floor of the House under a closed rule, which means that other members of Congress cannot slow the bills down by trying to amend them on the floor.[125] (B) The 1974 Budget Act gives programs enacted through the tax code and emerging from Ways & Means higher priority on the floor than direct-spending counterparts.[126] (C) Many tax bills only have to make it through a single committee to get to the parent chamber. In contrast, non-tax, non-entitlement spending programs must go through more than one committee,[127] and these programs often must win Congressional approval twice: once on authorization and once when receiving appropriations. Some of Congress's subject-matter committees are also so notoriously contentious that they have trouble getting any bills out of committee.[128] Other subject-matter committees have low credibility with the parent chamber.[129] Even though not every tax bill enjoys all of these three formal procedural protections, the fact that many tax bills do enhances Ways & Means' reputation for churning out legislation that requires few changes at the chamber level.

Third, as recent studies on tax policy perceptions suggest, tax-embedded programs may be more likely than their direct-spending counterparts to

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[119] Christopher J. Deering & Steven S. Smith, Committees in Congress 60–73 (1997).

[120] *Id.* at 68.

[121] Fenno, Congressmen in Committees, *supra* note 118, at 202.

[122] Deering & Smith, *supra* note 119, at 111.

[123] Fenno, Congressmen in Committees, *supra* note 118, at 203–04.

[124] Fenno, Congressmen in Committees, *supra* note 118, at 82–83. Research does reveal some differences between the two committees, such as responsiveness to constituencies, but that none of the differences undermine these three similarities.

[125] Deering & Smith, *supra* note 119, at 68.

[126] *See* Garrett, *supra* note 111, at 507–08.

[127] Garrett, *supra* note 111, at 510.

[128] *See* Fenno, Congressmen in Committees, *supra* note 118, at 226–40.

[129] Fenno, Congressmen in Committees, *supra* note 118, at 240.

command the support of bipartisan coalitions that will help get the programs through parent chambers. Even to the casual observer, tax-embedded policies often confound the traditional view that Democrats alone support social-welfare subsidies. Republicans have traditionally opposed direct-spending programs. However, with respect to the recent 112th Congress, of the 238 members of the House and the 41 senators who signed conservative activist Grover Norquist's "Taxpayer Protection Pledge," all but three were Republicans.[130] All of these signatories promised to "oppose and vote against any effort to raise the federal income tax on individuals or corporations."[131] As part of this promise, the signers have pledged "to oppose changes in tax deductions or credits that increase the net tax burden on Americans."[132] Significantly, this pledge to preserve existing tax deductions and credits extended across the board, *applying to all kinds of tax-embedded policies including refundable tax credits*—even where the latter, apart from their place in the tax code, otherwise resemble the very types of social-welfare programs that are traditionally unpopular with Republicans. That a Norquist-type activist would extract from nearly three hundred members of Congress a pledge to preserve some social-welfare program not embedded in the tax code, however, is difficult even to imagine.

Scholarship employing experimental data may partially explain this paradox. As previously discussed, tax-embedded programs often take the shape of discounts off of tax liability. Even tax-embedded programs that provide their subsidies as refundable credits accurately frame benefits as partial reductions of tax liability. Subsidies that reduce tax liability are more popular across both sides of the aisle than subsidies that take the form of direct payments and are independent of tax liability.[133] Edward Zelinsky's research in particular has revealed that:

> [s]ome otherwise rational persons view $100 granted through the tax system as different from $100 awarded through an equivalent direct outlay because, for them, the label attached to public largesse matters. For these individuals, policies unacceptable when framed as direct expenditures become supportable when labeled as tax subsidies, even though the economic substance of the policies is the same . . . For a critical segment of the public, public subsidy

[130] *The Taxpayer Protection Pledge Signers 112th Congressional List*, AMERICANS FOR TAX REFORM, http://s3.amazonaws.com/atrfiles/files/files/081012-federalpledgesigners.pdf (last visited Nov. 5, 2012).

[131] *Federal Taxpayer Protection Pledge Questions and Answers*, AMERICANS FOR TAX REFORM, http://www.atr.org/federal-taxpayer-protection-questions-answers-a6204 (last visited Nov. 5, 2012).

[132] *Id.*

[133] *See* Zelinsky, *Do Tax Expenditures Create Framing Effects?*, *supra* note 83, at 799. This effect only applies to the tax-embedded programs that are subsidies as opposed to tax penalties.

framed as tax relief is different from, and less objectionable than, equivalent cash payments.[134]

This may be particularly true among members of Congress who believe that taxes are generally too high. Elizabeth Garrett's research has shown that "some lawmakers," again, perhaps accurately, "see the enactment of tax expenditures as tax cuts, rather than as new federal spending programs."[135] For these reasons, the same member of Congress who does not personally support, for example, sending out government checks to low- or middle-income Americans for the purchase of health care may support cutting Americans' tax bills by some amount spent on health care.

In addition, putting aside the individual preferences of members of Congress, constituents may be more likely to support programs framed as tax relief than programs framed as cash subsidies. Legislators who sponsor or vote for tax-embedded subsidy programs will be able to claim legitimate credit for lowering taxes. Conventional wisdom holds that tax cuts are very popular with the American public and that tax increases are extraordinarily unpopular. Enacting a new direct-spending program or expanding an existing one may in fact require tax increases. However, a subsidy designed as a discount off of a tax bill amounts to a possibly voter-pleasing tax cut. Also in contrast to tax-embedded programs, direct-spending programs risk association with deeply unpopular policies such as welfare. For these reasons, a refundable credit for the purchase of health care is likely to get more constituent approval than a direct check to families who buy health care.[136] Members of Congress from both parties who examine poll data would likely know these facts. As a consequence, a subsidy taking the form of a tax credit will generally have more bipartisan support than a direct-spending counterpart, further easing the tax subsidy's path through Congress.

Fourth, the tax committees interact particularly frequently with the Executive Branch, earning them the political-science label of "executive-led."[137] As a result, the tax committees are particularly likely to deal with policies that have support of the current administration, a circumstance that helps tax bills actually to become law. If a sitting presidential administration hopes to get a policy through Congress, that administration will have an easier time working with Ways & Means and Senate Finance, with which the

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[134] *Id.* at 799–823. *See also* David S. Gamage & Darien Shanske, *Three Essays on Tax Salience: Market Salience & Political Salience*, 65 TAX L. REV. 19–38 (2012).

[135] Elizabeth Garrett, *Rethinking the Structures of Decisionmaking in the Federal Budget Process*, 35 HARV. J. ON LEGIS. 387, 434 (1998).

[136] *See* Edward J. McCaffery, *Cognitive Theory and Tax*, 41 UCLA L. REV. 1861, 1905 (1994); *see also* Garrett, *supra* note 135; Zelinsky, *Do Tax Expenditures Create Framing Effects?*, *supra* note 83.

[137] FENNO, CONGRESSMEN IN COMMITTEES, *supra* note 118, at 22–23 (characterizing Ways & Means as an executive-led committee because the Executive Branch drives the committee's agenda given that clientele groups take their demands to the Executive Branch, which packages those proposals into a legislative program, which in turn structures the work of Ways & Means).

administration already has close relationships. Similarly, if a member of either of those committees wants to get a bill through, that member will be more likely to be able to build on those relationships to get the bill past the executive.

B. Tax-Embedded Programs Face Particularly Robust and Balanced Political Debate

The committee origins of tax bills also ensure that these bills will undergo a more politically robust and balanced debate in Congress, as compared to direct subsidies.[138] Committees are where the details of legislation emerge. Notably, more, as well as more diverse, interest groups can get a more receptive audience before Ways & Means than before other committees. Historically, the Ways & Means Committee, as compared to other House committees, has operated relatively free from the control of a small handful of powerful interest groups.[139] While multiple interest groups are generally able to give input to Ways & Means, no particular subset has tended to dominate. Interest groups certainly have power before the tax-writing committees, but no *particular* interest group holds disproportionate sway. As a result, the tax-writing committees tend to be the congressional committees least susceptible to interest group capture.[140] Indeed, writing about Ways & Means in the *Yale Law Journal*, Zelinsky notes the features of the tax-writing committees that resemble James Madison's ideal of unbiased pluralist debate:

> [T]he institutions formulating and administering tax policy are more competitive and visible than their direct outlay counterparts because tax institutions are subject to more numerous and diverse constituencies than the specialized, limited-clientele organizations that design and implement direct government spending. . . .[141]
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> . . . The specialized orientation of the nontax committees and departments makes each of these institutions highly susceptible to capture by the limited constituencies affected by its comparatively narrow jurisdiction. In pluralist terms, the outcomes emanating from direct expenditure committees and departments possess less

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[138] *See* Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1175–82.

[139] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1175–82.

[140] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1187 n.68.

[141] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1166.

> legitimacy than if more numerous and more diverse groups were to participate in the deliberations of these institutions. . . .[142]
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> . . . In contrast, the Treasury and Congress' tax-writers supply more fungible services—tax subsidies—in a more competitive environment, distinguished by many more possible purchasers and consequent collective action problems. While the various buyers of tax subsidies may attempt to cartelize themselves, and may often succeed, in general the more competitive tax process is less conducive to such cartelization than the procedures which supply direct expenditure programs.[143]

This is the case in large part because members of Ways & Means do not depend on concentrated constituencies for campaign funds.[144] This situation renders Ways & Means, and to a lesser degree Senate Finance,[145] more likely than other committees to weigh a wide variety of interest groups and to debate legislation without undue influence from any one in particular. In contrast, non-tax committees often fall under the disproportionate sway of a handful of constituencies. For example, the House Appropriations Committee, which often receives negative publicity for the way it deals with interest groups when distributing earmarks, has very powerful subcommittees, each of which cultivates a strong relationship with a few such groups.[146] The tax-writing committees, which rely much less heavily on subcommittees, instead entertain a wide variety of would-be influence peddlers, none of which is able to dominate.[147]

To be sure, as the tax-writing committees' jurisdictions expand to include more substantive areas, interest-group representatives associated with those areas may attempt to develop the close relationships with members of the tax-writing committees that these interest-group representatives may have previously had with members of other committees. As this happens, the tax-writing committees may face increased potential for interest-group capture.[148] The quality of the debate at these committees may suffer correspondingly.

However, two factors specific to the tax-writing committees will likely prevent interest-group capture from posing as great a threat to them as it does to other committees. First, both tax-writing committees (but particu-

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[142] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1176–77.

[143] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1178.

[144] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1183.

[145] FENNO, CONGRESSMEN IN COMMITTEES, *supra* note 118, at 156–60.

[146] *See* Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1188.

[147] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1188.

[148] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1188. I mean this term more loosely than the strict definition of regulatory capture.

larly Ways & Means) have, as previously discussed, prioritized their reputations, which depend in part on independence from interest groups. Therefore, the Ways & Means Committee is less likely to be captured than other committees operating within committee subcultures with stronger capture traditions. Second, the tax-writing committees already play host to many would-be wielders of influence.[149] Even if new interest groups join the fray, they will have to compete with the existing diversity of interest-group representatives plying their trade before the tax-writing committees. Some of these new interest groups may successfully cultivate relationships with certain tax-writing subcommittees, but when the bill is before the full committee, that debate will have to balance existing interests with the new ones, reducing the risk that any particular group will dominate.

C. Tax-Embedded Programs, Once Enacted, are More Stable Than Their Direct-Spending Counterparts

The next legislative advantage that a tax-embedded program may achieve emerges once the program has become law. Tax-embedded programs are more stable than their non-tax counterparts. This is so for three principal reasons. First, tax-embedded programs do not require yearly appropriations. As a result, these programs escape the annual threat of cuts from appropriations committees. For this reason, tax-embedded programs tend to cement themselves in the tax code[150] and amass active supportive constituencies. Garrett has observed this phenomenon: "Currently, spending through the tax code . . . is often more valuable to interest groups than the appropriated benefits. The former are more durable than discretionary programs because they usually need not be reviewed once they are established and the funding is automatic as long as the law remains unchanged."[151]

Second, tax-embedded programs are situated in a web of tax law that makes them hard to excise cleanly. Removing provisions from the tax code requires extricating them from a dense nest of interrelated provisions. Doing so calls for detailed new legislation rather than a mere end date. Surrey and McDaniel accurately noted this:

> Terminating a tax expenditure . . . [is] more complicated than terminating a direct program. Because of the technical interrelationships between code provisions, termination of one provision frequently requires changes in others; therefore, extensive study would be required to determine the full economic effects of a given change. . . . [In addition,] because business and economic

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[149] Zelinsky, *James Madison and Public Choice at Gucci Gulch*, *supra* note 78, at 1178.
[150] Edward A. Zelinsky, *Are Tax "Benefits" Constitutionally Equivalent to Direct Expenditures?*, 112 Harv. L. Rev. 379, 396–97 (1998).
[151] Garrett, *supra* note 135, at 421.

> decisions are based on tax considerations, total termination without transition rules might prove unfair.[152]

These complications arise because tax code provisions cross-reference each other frequently. For example, slicing out any particular itemized deduction requires altering a long list of other seemingly unrelated provisions that involve that particular itemized deduction. Then, cutting an itemized deduction might require changes to the standard deduction to account for the influx of new takers of the standard deduction. Any re-writes of the standard deduction statute would in turn call for revising another list of provisions that refer to *that* statute. The process can become quite cumbersome.

Third, pruning a tax-embedded policy may trigger a particularly negative public response because doing so amounts to a tax hike. As discussed above, raising taxes has large political costs.[153] For instance, if a future Congress were to reduce the premium assistance credit of the Affordable Care Act, political opponents could point out that any member who voted "yes" had voted to raise taxes on low-to-middle-income Americans. Those yes-voters would likely have violated the Taxpayer Protection Pledge and any other campaign promises they may have made not to raise taxes.[154] As a result of these sorts of potential political problems, members of Congress may be particularly unwilling to vote for cutting tax-embedded programs.

Taken together, these stabilizing devices have a significant implication. Insofar as Congress increasingly opts to insert additional social and regulatory policies in the tax code, then programs benefiting weaker groups in American society will likely acquire more of the stability that various laws for more powerful interest groups have already attained. Powerful interest groups have long known how to navigate the political processes described here and to lobby for tax-embedded programs.[155] This know-how has enabled these groups to maintain their steady diet of tax-embedded programs even as Congress's general appropriation pie has been shrinking and to accomplish this outcome at the expense of weaker social groups that have not known how to request an audience before the tax-writing committees.[156] To the extent that Congress continues to place new programs in the tax code,

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[152] SURREY & MCDANIEL, *supra* note 6, at 62. Tax law has a strong tradition of transition rules. When Congress changes a tax law, everyone expects transition relief. *See* DANIEL SHAVIRO, WHEN RULES CHANGE: AN ECONOMIC AND POLITICAL ANALYSIS OF TRANSITION RELIEF AND RETROACTIVITY 2–3, 12 (2000).

[153] *See* discussion *supra* Part III.A.

[154] *See Federal Taxpayer Protection Pledge Questions and Answers*, *supra* note 131. Many observers have noted the substantial political downside of failing to sign or breaking the Taxpayer Protection Pledge. *See* Trip Gabriel, *Election Cycle Emerges as the Year of the Pledge, But Some Candidates Resist*, N.Y. TIMES, July 17, 2011, at A14; Jason Horowitz, *Taxes Hold 'em*, WASH. POST, July 13, 2011, at C3; Alex Leary, *GOP Owes Antitax Brand to Him*, ST. PETERSBURG TIMES, Sept. 18, 2011, at 1A; Shira Schoenberg, *For Candidates, Position Pledges Can Pose Unexpected Perils; Romney Not Alone in Tripping Over Special Interests*, BOSTON GLOBE, June 29, 2011, at 9.

[155] Garrett, *supra* note 135, at 421.

[156] Garrett, *supra* note 135, at 421.

however, these weaker groups achieve more equal procedural footing in the competition for funds, as well as liberation from the albatross of the annual appropriations process that has long hung around the neck of non-tax-embedded programs.[157] This change provides much-needed program stability even to those groups that have traditionally been unable to get it.

To be sure, placing social programs within the tangled web of the tax code might raise concerns about unnecessary statutory complexity. However, while this descriptor might apply to any isolated social policy inserted into the tax code, using the tax code to accomplish multiple social or regulatory purposes in fact reduces aggregate complexity across statutes. This is so because, although a legislative mandate that includes tax provisions and thus cross-references previous tax provisions might be more complicated than a mandate with no cross-referenced tax provisions, the cross-referencing of existing tax provisions is simpler than the alternative situation, in which legislators are forced to craft new terminology every time a new bill includes terms not found in earlier legislation.

Further, the staffs of the tax-writing committees and the Treasury Department can easily identify and harmonize competing definitions of similar terms if the terms are all located within the tax code. Congress and Treasury Department officials can pursue this goal with an eye to simplifying the tax code. For example, before 2004, different tax code sections had different definitions of "dependent." In 2004, Congress adopted a uniform definition that incorporated successful elements of the preexisting definitions.[158] Now, the same definition of "dependent" applies across all income tax provisions using that word, including the dependency exemption, the EITC, the child credit, the dependent care credit, and head of household filing status.[159] A leading tax treatise explains that Congress adopted the uniform definition "to reduce complexity for taxpayers and thereby improve compliance."[160] If the competing definitions had been in non-tax statutes, no Congressional committee would have been positioned to notice and to fix the discrepancies. With terminological discrepancies in the tax code, however, not only did a Congressional committee attend to the issue, but the interconnected nature of tax provisions made the problem relatively simple to solve.

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[157] One other reason that tax-embedded programs are more stable is that they are less vulnerable to Constitutional challenge. While many tax scholars have convincingly argued that courts should treat subsidies provided through the tax code the same way as direct subsidies for Constitutional purposes, that is not currently the case. *See, e.g.*, Donna D. Adler, *The Internal Revenue Code, the Constitution, and the Courts: The Use of Tax Expenditure Analysis in Judicial Decision Making*, 28 Wake Forest L. Rev. 855 (1993); Zelinsky, *supra* note 150. However, because so much compelling work has recently argued for the similar treatment of tax benefits and direct subsidies, this difference may not remain for long.

[158] Working Families Tax Relief Act of 2004, Pub. L. No. 108-311, §§ 201– 208, 118 Stat. 1166, 1169–78 (2004).

[159] *Id.*

[160] Boris Bittker & Lawrence Lokken, Federal Taxation of Income, Estates and Gifts ¶ 30.3 (3d ed. Supp. 2012).

D. Tax-Embedded Programs, Once Enacted, Grow More Easily Than Their Direct-Spending Counterparts.

A final major legislative advantage of embedding a social program or regulation in the tax code also stems from tax-embedded programs' long-range trajectories. Not only are tax-embedded programs once enacted more deeply entrenched than their direct-spending counterparts, but the tax-embedded programs can more easily spread to cover more taxpayers.

This is a major advantage for any program, particularly one that, like most non-tax subsidies, would otherwise require regular Congressional funding. A home in the tax code means that a program can easily grow over time and become a major feature of the social-policy or regulatory landscape. For example, the refundable tax credit for low- and middle-income families' health care purchases, with no further Congressional attention, can quickly expand to cover everyone who meets the income and health care purchase tests.[161] This expansion is exactly what happened to the EITC. Several years ago, the IRS determined that more people were becoming eligible for the EITC. The large and growing number of people who were claiming the EITC conveyed to lawmakers that even more eligible individuals were probably out there with no idea they could apply for the EITC. As a result, the IRS tried to reach out to potential recipients to show them how to apply. To this end, the IRS now conducts annual EITC Awareness Days to educate the public about the EITC.[162] IRS staff members also try to get interviews with prominent newspapers with nationwide audience bases to talk about the EITC.[163] In 2010, for instance, the IRS held 68 EITC news conferences around the country, and worked with "[c]ommunity coalitions and IRS partners nationwide" to "issu[e] . . . 128 news releases, writ[e] . . . letters to the editor and us[e] . . . social media tools to spread the word about EITC."[164] Finally, the IRS maintains what it hopes is a user-friendly website about the EITC.[165] These publicity efforts raised the number of EITC recipients substantially without forcing the program through the Appropriations Committee.

To the outside observer, this development may initially appear to pose a problem for tax-embedded programs. Many taxpayers have concerns about wasteful government spending. From this perspective, a policy device that offers a chance for social programs to grow unattended seems like a potential disaster. However, the particular opportunities for tax-embedded pro-

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[161] I.R.C. § 36B (Supp. V 2011).

[162] *EITC Awareness Day*, INTERNAL REVENUE SERV., http://www.eitc.irs.gov/ptoolkit/awarenessday (last updated Feb. 23, 2012).

[163] *IRS Marks EITC Awareness Day; Highlights Expanded Tax Credit*, INTERNAL REVENUE SERV. (Jan. 29, 2010), http://www.irs.gov/uac/IRS-Marks-EITC-Awareness-Day;-Highlights-Expanded-Tax-Credit.

[164] *Id.*

[165] *See EITC*, INTERNAL REVENUE SERV., http://www.eitc.irs.gov (last updated Oct. 9, 2012).

grams to grow would not result from a member of Congress's game of golf with a representative of a prominent local interest group. Instead, a tax-embedded program would grow if the IRS, an administrative agency with notably limited discretion, found that more potential recipients met the strictly defined requirements that Congress has put into place for the program. As a consequence, tax-embedded programs do not lose the legitimacy they derive from the legislative process, while still possessing the needed flexibility to respond immediately to changing societal conditions.

Nor does enacting a program through the tax code impede Congress's ability to finesse the program over time. Congress need simply fine-tune the relevant law to effect change through the tax code. For example, if a program becomes too expensive, Congress can always intervene and change the eligibility criteria. However, Congress will not be able to trim the program without reviewing those criteria and how they might be failing. Rather than just look at a numerical budget figure and impose a quick cut, members of Congress will need to examine the statute and to select which features to alter for cost control. This process will also lead to greater accountability than merely slashing a number on a budget. As a result, while tax-embedded programs can grow more easily than their non-tax counterparts, that growth will be responsive and transparent.

IV. Normative Advantages

The preceding section discussed legislative advantages that accrue to social and regulatory programs enacted through the tax code. However, the question remains: even if the legislative process does give tax-embedded programs these advantages, is this privilege a good thing? The Surrey-inspired tax expenditure literature would say no. However, as discussed above, that literature rests on assumptions about the tax policy environment that no longer have much force. At the same time, the influence of this literature continues to prevent scholars from comprehensively evaluating the normative advantages that embedding social and regulatory policy in the tax code can provide.[166] A number of these advantages have become particularly pronounced in the current environment and may help explain why the current tax-oriented structural transformation is taking place. The previous section analyzed many of the legislative reasons why this transformation is happening, but lawmakers may also prefer enacting policies through the tax code because some legislators are (tacitly) aware of the possible normative advan-

[166] In the wake of the tax expenditure literature, only a few articles from outside of that school have been at all critical of placing non-revenue-raising laws in the tax code. *See generally* Alstott, *supra* note 7. However, that literature has focused almost exclusively on efficiency problems with the earned income tax credit and has been controversial. For a prominent critique, see generally Weisbach & Nussim, *supra* note 78. For the opposite view on the efficiency issue, see generally Zelinsky, *Efficiency and Income Taxes*, *supra* note 78.

tages of doing so. This section will discuss two particular types of normative advantages: distributive justice advantages and institutional advantages.

A. Distributive Justice Advantages

Inscribing a law in the tax code allows that law to assist low- and middle-income individuals and families particularly well, and, in this way, to further distributive justice goals. This assertion challenges a longtime tenet of tax expenditure analysis. As described previously, Surrey emphasized the ways in which tax-embedded policies, by virtue of their design as exclusions and deductions and, in a few cases, as nonrefundable credits, undermined the tax system's progressivity. However, also as discussed above, many of Surrey's distributional objections do not apply to the current tax-oriented structural transformation.[167] What is more, lingering concern over these now-largely-obsolete distributional problems has obscured the real distributive justice advantages of enacting laws through the tax code. The following subsections consider three of these advantages.[168]

1. People Who Need Benefits are More Likely to Apply for Them Through the Tax Code

Traditionally, one major hurdle facing programs aimed at low- and middle-income families is that eligible individuals and families are unaware of available benefits.[169] However, putting a new program into the tax code can help to overcome this problem. People who do not initially realize they are eligible for social programs are more likely to find out about them through the tax code.

This is the case because of what I call "automatic notification." Automatic notification occurs because employed persons generally file tax returns. When taxpayers file, the return has specific blanks for programs with which the individuals might not be familiar. Tax filing software and income tax preparation services magnify this effect. When, for example, a middle-income filer enters income and family size data into the well-known tax software TurboTax, TurboTax will automatically suggest tax benefits gener-

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[167] *See supra* Part II.B.

[168] This section moves beyond the criteria that tax policy scholars have traditionally used to evaluate the equity of different tax policies. Specifically, tax policy scholars have generally asked how tax laws further what tax scholars call "vertical" and "horizontal" equity. While these are important, tax scholars designed these criteria to evaluate a tax code whose major purpose was only to raise revenue. When evaluating tax policy in the face of the current structural transformation, tax scholarship needs to look beyond these traditional measures of how the tax system distributes its revenue-raising obligations. Tax scholarship should also examine how the tax system furthers broader redistributive goals, which is the issue that this section will address.

[169] *See* Allison Barrett & Anni Poikolainen, U.S. Dep't of Agric., Food Stamp Program Participation Rates: 2004 (2006); *see also* Frank J. Thompson & Thomas L. Gais, *Federalism and the Safety Net: Delinkage and Participation Rates*, 30 Publius 119 (2000).

ally available to individuals with that income and family size profile.[170] The TurboTax company has an incentive to identify these automatic benefits so that the company can advertise that it helps its clients obtain maximum possible refunds. For example, if TurboTax thinks that a taxpayer might be eligible for the premium assistance credit, TurboTax will ask the taxpayer directly whether he or she paid any premiums that year. Most income tax preparers, who serve low-income individuals and families and who also have an incentive to maximize clients' refunds, do the same.[171] Moreover, the IRS's recent initiative to train preparers on tax law changes enables the automatic notification process to incorporate almost immediately any changes in a tax-embedded program that might expand the group of potential beneficiaries.[172]

In this way, the return filing process helps taxpayers learn about programs they might never otherwise discover. For even if workers had a vague sense they may be eligible for non-tax federal assistance, concern about stigma or wasting time may prevent a visit to a social service agency. For instance, imagine a new public-school teacher making $30,000 per year with three children, a woman who considers herself middle-class. This teacher may even have heard of the earned income tax credit or the child tax credit, but would not be sure enough that she was eligible to spend an afternoon attempting to figure it out.[173] She may be embarrassed to try—partly because of distaste for what she sees as the welfare office or partly because she does not want an intimidating bureaucrat to explain to her that she is in fact not

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[170] *See Why Choose TurboTax*, TurboTax, http://turbotax.intuit.com/best-tax-software/why-choose-turbotax (last visited Nov. 5, 2012).

[171] The incentive for tax preparers to maximize refunds, to be sure, poses a problem that the IRS is currently trying to address with its preparer initiative. But putting aside the incentives for fraud and inaccuracy that refund maximization may create, it certainly gives tax preparers incentives to tell their clients about programs for which they are actually eligible.

[172] The IRS's recent preparer initiative also addresses a distributive justice concern that David Super has raised about placing anti-poverty programs in the tax code. Super noted that claimants apply for—and then get into disputes over—tax-embedded programs with the help of private-industry preparers. In contrast, claimants interact with direct-spending programs with the help of government employees. Super worries that "the least sophisticated claimants are likely to need the most assistance negotiating the application process. These unsophisticated individuals are likely to be disproportionately the poorest and hence, those on whom denial of a meritorious claim is likely to create the greatest hardship. Moreover, these claimants may be the least effective at selecting competent representatives . . . ." *See* David A. Super, *Privatization, Policy Paralysis, and the Poor*, 96 Calif. L. Rev. 393, 438 (2008) (footnotes omitted). However, as the IRS exerts substantial new oversight over commercial preparers and works on developing a federal certification process for would-be preparers, this clear line between private-sector preparers and public-sector workers will vanish. Perhaps the IRS's new attention to this area stems in part from the structural transformation that this Article discusses. The more that benefits flow through the tax code, the greater the need for the IRS to ensure that the citizens who need these benefits are getting them, while at the same time guarding against increased opportunities for fraud.

[173] Even major direct-spending programs often require phone or in-person contact with a federal agency. Individuals cannot figure out if they are eligible solely using the Internet. *See, e.g.*, *FoodShare Wisconsin Eligibility*, Wis. Dep't of Health Servs., http://www.dhs.wisconsin.gov/foodshare/fseligibility.htm (last updated Sept. 11, 2012).

entitled to benefits. However, under automatic notification, she risks neither wasted time nor humiliation when her return or tax software tells her, based on information she has already entered, that she may be entitled to a child tax credit or a refundable credit for purchasing health care for her family.

The "automatic notification" that comes with placing social policy and regulation in the tax code echoes a recent trend in social service provision toward so-called "no wrong door" centers.[174] At these centers, individuals can apply for multiple public programs at the same location.[175] To take an example, one of Virginia's recent "no wrong door" initiatives has as its mission to "connect . . . public and private agencies and providers through the development of single, coordinated systems of information, referral, and access to . . . support services."[176] This "no wrong door" approach saves time and resources and also allows low- and middle-income people to learn about potentially unfamiliar services. Embedding programs in the tax code serves the same function. When a low- or middle-income person files a tax return, that tax return becomes, in essence, a much cheaper version of a "no wrong door" center. If someone applies for just one benefit using a tax return, he or she will automatically get every other relevant benefit. The current structural transformation in federal policymaking will substantially amplify this salutary "no wrong door" effect. As more and more social-welfare programs join the tax code, recipients will be able to get basically every subsidy to which they are entitled by filling out one form at home.

Automatic notification confers a major distributive justice advantage on programs enacted through the tax code. Proponents of policies that help low- and middle-income individuals can use the tax code to increase the likelihood that targeted beneficiaries will actually find out about and receive those benefits. A program aimed at low- and middle-income families that actually reaches its intended beneficiaries will serve the goal of distributing resources to those families particularly well. For this reason, tax-embedded programs provide a relatively effective means of accomplishing distributive justice ends.

2. *Tax-Embedded Programs Provide More Resources to Intended Beneficiaries*

Distributing resources through the tax code is also an effective approach because those benefits are not taxable. As discussed above, most social programs that Congress enacts through the tax code in the current era take the form of tax credits, particularly refundable ones. While Congress and the IRS have not addressed this issue directly in most cases, a number of authorities support the conclusion that tax credits, refundable or not, are not

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[174] *See* Super, *supra* note 172, at 451.

[175] Super, *supra* note 172, at 451.

[176] *No Wrong Door*, VA. DEP'T FOR THE AGING, http://www.vda.virginia.gov/nowrongdoor.asp (last visited Nov. 5, 2012).

taxable income to recipients. For that reason, recipients of a benefit administered through the tax code will receive the full amount of the intended benefit. While Surrey noted that full-benefits availability held for the wealthy, he ignored the way in which this feature enhances the ability of tax-embedded programs to distribute money to low- and middle-income people.

Under current law, government benefits *not* provided through the tax code are included in gross income unless a statutory exception specifies otherwise.[177] Current tax law does exclude some social-welfare benefits from gross income via what tax legislation calls the "general welfare exception," which excludes certain government transfers from gross income.[178] However, the general welfare exception is not part of the tax code, and IRS authority has limited the exception substantially. In particular, the IRS has hesitated to extend the general welfare exception to payments conditioned on certain behavior, holding that these payments actually represent compensation for services.[179] Most notably, the IRS has expressed this view with regard to payments made to individuals under the Temporary Assistance to Needy Families ("TANF") program.[180] The IRS will only allow TANF recipients to exclude their payments from income if strict stipulations hold:

> 1. The payments must be received directly from a state or local welfare agency or from an entity with which the agency contracts to administer its TANF program;
> 2. Eligibility for the payments is based solely on need, and the payments for work are funded solely by the TANF program; and
> 3. The payments are in amounts determined by welfare laws, and the hours of work are restricted to the amounts paid, divided by the minimum wage.[181]

These stipulations restrict Congress's ability to deliver tax-free payments directly. If legislators want, as they commonly do, to make a public benefit conditional on some behavior, and particularly if they want the amount of the benefit to vary with levels of behavior, members of Congress have to hope that the IRS issues a ruling allowing benefits to be excluded from taxpayers' income. Otherwise, legislators face the prospect of substantially undercutting the effect of the program when the IRS decides to force program recipients to pay tax on received benefits.

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[177] Bittker & Lokken, *supra* note 160, at ¶ 16.4, (citing Deason v. Commissioner, 590 F.2d 1377 (5th Cir. 1979)).

[178] Bittker & Lokken, *supra* note 160, at ¶ 16.4.

[179] I.R.S. Notice 99-3, 1999-1 C.B. 271 (1999).

[180] *Id.* (citing Rev. Rul. 75-246, 1975-1 C.B. 24 (1975); Rev. Rul. 71-425, 1971-2 C.B. 76 (1971)); *see also* Rev. Rul. 2009-19, 2009-2 C.B. 111 (2009).

[181] *See* 1999-1 C.B. 271. The text that corresponds with this footnote paraphrases the language from the I.R.S. notice.

Further, the IRS has declined to extend the general-welfare exception to government transfers to businesses.[182] However, Congress often may want to use payments to businesses to further distributive justice objectives. For example, the Affordable Care Act includes the aforementioned credit for small employers to help them purchase health care for their employees.[183] This credit is limited to health care for employees who have annual full-time equivalent wages that average no more than $50,000.[184] This limit suggests that Congress specifically designed this credit to help low- and middle-income workers. However, were this credit to take the form of a direct payment, small businesses would be required to include that payment in income. These required income taxes would reduce the magnitude of the program's distributive justice effect.

In contrast, the IRS's treatment of tax credits demonstrates that they are *not* income to recipients. The existing scholarship also essentially assumes they are not income.[185] The IRS has never made any general attempt to include tax credits in income. The IRS's few rulings requiring taxpayers to include *specific* credits in income suggest that the IRS takes the opposite view: credits are not gross income unless specifically enumerated in administrative guidance or statute.[186] For example, in administrative guidance, the IRS disavowed misleadingly broad language in an earlier ruling and explained that credits are included in gross income only in very limited circumstances.[187] In other published guidance, the IRS lists "refundable credits" as an example of an item that a taxpayer would not need to include in income.[188]

Congress has also passed several statutes specifically including certain refundable credits in income, further suggesting that treating a credit as income requires specific legislative authorization.[189] For instance, in section

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[182] *See, e.g.*, I.R.S. Notice 2003-18, 2003-1 C.B. 699 (2003). The Treasury Department and the IRS do not want to exclude government payments to businesses from gross income because, in the Treasury and the IRS's view, businesses use these payments to make deductible expenses. According to this perspective, excluding a payment from income and then using it to make deductible expenses is a double benefit that taxpayers should not be able to take.

[183] *See supra* Part II.A.

[184] I.R.C. § 45R (Supp. V 2011). The legislative history to the bill makes clear that the premium assistance credit is excluded from gross income. *See* Joint Comm. on Taxation, Technical Explanation of the Revenue Provisions of the "Reconciliation Act of 2010," as Amended, in Combination with the "Patient Protection and Affordable Care Act" JCX-18-10, at 25 (2010).

[185] *See* Jenn, *supra* note 88, at 12–13.

[186] *See, e.g.*, I.R.S. Notice 2005-31, 2005-14 C.B. 830 (2005); I.R.S. Gen. Couns. Mem. 34,936 (July 3, 1972); *see also* Rev. Rul. 79-315, 1979-2 C.B. 27 (1979).

[187] I.R.S. Gen. Couns. Mem. 34,936 (July 3, 1972).

[188] This Notice specifically discusses whether to include the refundable portions of refundable credits in adjusted gross income. However, if the refundable portion is not included in adjusted gross income the entire credit would not be included in adjusted gross income either and, as a result, would not be gross income.

[189] While some might think that the current policy represents too large a grant of discretion to the IRS, this is in fact a Congressional issue. Congress decides when to include the amount of a credit in income and has not often done so.

1397E, Congress included in income the nonrefundable federal income tax credit associated with Qualified Zone Academy Bonds.[190] In section 87, Congress provided that gross income encompasses the tax credits for alcohol fuel and for biodiesel fuel.[191] Nowhere in the statute, nor the legislative history of these specific inclusion rules, does Congress even imply that tax credits are generally included in gross income. As a consequence, tax credits generally are not treated as gross income, and taxpayers do not have to pay tax on their value. For this reason, tax-embedded benefits serve as more powerful distributive justice tools than their direct-spending counterparts.[192]

3. *Enacting Benefits Through the Tax Code Fosters Inclusion of Potentially Marginalized Groups*

As an integrated system of near-universal contribution and distribution, taxation becomes an arena in which all citizens participate, including those citizens who are from low-income communities or who historically have been marginalized. The more the tax code encompasses social programs and regulations, the more inclusive it becomes. Increased use of tax law for non-revenue-raising purposes can provide a way to promote shared identity among citizens.[193] In fact, social-welfare scholar Neil Gilbert has celebrated how what I have called the structural transformation has turned "programs that offered 'passive' income supports [into] an array of sanctions and incentives designed to promote . . . contributions to the community."[194]

This conclusion rests on the fact that almost every citizen at some point in his or her life has to pay taxes or file returns. Members of a nation join the citizenry by contributing and paying—or at least filing returns to pay—federal taxes. The tax code then adjusts the required pay-in to reflect the needs and nonfinancial donations of contributors. The state makes this adjustment by offering active participants various discounts off of that mandated amount. Those discounts take the form of various tax-embedded programs. This citizen-contribution effect becomes all the more powerful as more policies join the tax code and as a citizen's tax return and bill reflect his or her social participation.

Further, as discussed above, placing more programs in the tax code encourages more people to file tax returns each year. Filing a return creates an opportunity for the filer to assume the identity of a taxpayer. A recipient

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[190] I.R.C. § 1397E(j) (2006 & Supp. V 2011).

[191] I.R.C. § 87 (2006).

[192] Congress could of course always raise the levels of taxable benefits to compensate for the fact that recipients have to pay income tax on them. However, to make sure that the income tax did not affect the amount of any recipient's benefits, Congress would have to fine-tune the tax adjustment to account for the fact that different recipients will have different real marginal rates. This would be difficult to do outside of the tax code.

[193] NEIL GILBERT, TRANSFORMATION OF THE WELFARE STATE: THE SILENT SURRENDER OF PUBLIC RESPONSIBILITY 45, 65, 101–04, 126–27, 171, 181–82, 191–92 (2004).

[194] *Id.* at 39.

of benefits through the tax code assumes this identity the minute he or she walks into a tax preparer's office to file the year's return. Come tax season, the low-income taxpayer who primarily uses the tax system to get benefits shares the experience of a wealthier taxpayer who primarily uses the tax system to make his annual revenue contribution. Both recognize that they have the same return-filing obligation, both approach their return preparer hoping to do a bit better than last year, and both will likely walk away with some sort of refund.[195] This shared experience is not stigmatizing for either party and is in fact remarkably similar for both.

Assuming the mantle of a taxpayer arguably confers on the recipient the sense that he or she is a stakeholder in the government that collects the taxes. Tax scholar Lawrence Zelenak calls tax return filing "a valuable civic ceremony."[196] He comments that filing can

> serve the important civic purpose of recognizing and formalizing the fulfillment of the financial responsibilities of citizenship . . . Such an important civic activity demands a ceremony, and the filing of one's tax return is that ceremony. The filing ceremony may prompt taxpayers to ponder how much civilization they want to buy and whether they are getting good civilization value for their tax dollars, but the linkage between citizen and government through the tax return process has the potential to go deeper than that.[197]

Zelenak goes on to detail many of the ways in which return filing enhances the filer's civic self-image.[198]

Further, tax filing, as a unified system of contribution and distribution, does not clearly distinguish between the contributors and the distributees, perhaps because almost every filer is a bit of both. Most taxpayers receive refunds.[199] As a result, many people may not even know if, in a given year, they actually got more out of the tax system than they contributed. The answer to this question may be different in different years, but no matter what the answer, the low- and middle-income filer still considers herself a taxpayer, with all the benefits and burdens that accompany that status. In some cases, being a taxpayer gives an individual legal standing to sue over whether the government may have violated the Constitution.[200] By filing returns to receive their benefits, individuals may come to think of themselves

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[195] In 2009, the most recent year for which data is available, 83.4% of individual income tax returns resulted in refunds. *See SOI Tax Stats—IRS Data Book*, INTERNAL REVENUE SERVICE, http://www.irs.gov/uac/SOI-Tax-Stats---IRS-Data-Book, tbls.2 & 12 (last visited Nov. 5, 2012).

[196] Lawrence Zelenak, *Justice Holmes, Ralph Kramden, and the Civic Virtues of a Tax Return Filing Requirement*, 61 TAX L. REV. 53, 61 (2007).

[197] *Id.* at 59–60.

[198] *Id.* at 60–88.

[199] *See* INTERNAL REVENUE SERV., *supra* note 195.

[200] *See, e.g.*, Flast v. Cohen, 392 U.S. 83 (1968).

as being able to engage publicly and to challenge the government through legal and other means.

Although researchers like Suzanne Mettler have argued that individuals who receive direct subsidies are more likely to engage civically than individuals who receive subsidies through the tax code,[201] my analysis challenges this view. Mettler's research understates the extent to which enacting policy through the tax code actually fosters civic inclusion. She errs in this regard for three reasons. First, she misinterprets certain survey data to conclude incorrectly that whether a program is placed in the tax code affects program participants' views on tax fairness.[202] Second, she admits that the citizen-participation dynamic she describes does not apply to refundable credits and she consequently excludes them from her analysis.[203]

Third, Mettler ignores all the ways in which placing social and regulatory programs in the tax code builds recipients' notions of citizenship and encourages program beneficiaries to regard themselves as important contributors to the system from which they benefit. To understand properly the effect of tax embedding on civic participation, she should have assessed whether and how recipients of different programs view themselves as participating in the public sphere. One piece of Mettler's data suggests that, in fact, recipients of tax-embedded benefits are *likely* to have embraced taxpayer status. She notes that when she surveyed beneficiaries of tax-embedded programs about whether these individuals pay their fair share of federal income taxes, only one percent of respondents said that they do not pay federal income taxes.[204] In the year preceding her survey (2009), 32.6% of Americans had no federal income tax liability.[205] Even so, the surveyed individuals still perceived themselves as sufficiently full participants in the tax system to assess the fairness of their personal tax burden. This perception may be in

[201] Mettler, *supra* note 32, at 44–46, 113.

[202] Although Mettler claims that her regressions show that use of direct-spending programs affect perception of tax fairness more than tax-embedded programs, the regressions themselves do not support this claim. According to her own regression results, each tax-embedded program is estimated to increase the probability of perceiving the tax system as fair by 1.8 percentage points, exactly the same amount as the estimated increase from a direct-spending program. Mettler interprets the statistical insignificance of the coefficient on tax-embedded programs as showing that tax-embedded programs do not affect perception of tax fairness. Mettler, *supra* note 32, at 43–44. However, statistical insignificance cannot be used to establish this conclusion. *See* Andrew Gelman & Hal Stern, *The Difference Between "Significant" and "Not Significant" is Not Itself Statistically Significant*, 60 Am. Statistician 328 (2006). However, given that the coefficient estimates are precisely the same, her results are consistent with the hypothesis that receiving a tax-embedded benefit has the same effect on perceptions of tax fairness as receiving a direct-spending benefit. Results are even consistent with the hypothesis that receiving a tax-embedded benefit has a larger effect on perceptions of tax fairness. Thanks to Alexander Tahk for this point.

[203] Suzanne Mettler, *Reconstituting the Submerged State: The Challenges of Social Policy Reform in the Obama Era*, 8 Persp. on Pol. 803, 820 n.34 (2010).

[204] *Id.* at 820 n.33.

[205] *Federal Individual Income Tax Returns with Zero or Negative Tax Liability, 1916–2009*, Tax Foundation (Oct. 18, 2011), http://www.taxfoundation.org/taxdata/show/25587.html. This data concerns income tax liability and does not factor in payroll taxes.

part because the surveyed beneficiaries received tax-embedded social benefits that required them to file tax returns and participate in the tax system, just as their higher-income counterparts do.

While accomplishing policy through the tax code offers greater potential for fostering inclusivity, tax embedding does raise one particular exclusivity danger. As more social benefits take the form of discounts off of citizens' tax bills, the number of citizens who may not have positive income tax liability in any given year continues to rise.[206] Even citizens who do not owe may file anyway, but the amount of subsidies they receive through the tax code exceeds the amount of tax owed. The number of citizens in this category is growing in large part because Americans now receive their social benefits as exclusions, deductions, and credits that reduce their tax bills. This increase has started to generate outcry about the number of Americans who "pay no income tax." That complaint may create an "us-v.-them" mentality among citizens who have positive tax liability. While using the tax code to bring marginalized citizens into the tax system's fold, lawmakers must make sure that the shift toward tax embedding does not spur resentment among less marginalized or higher-income taxpayers. Accomplishing this goal may just be a matter of simply re-framing efforts at the legislative or administrative levels.

B. Institutional Advantages

Above and beyond distributive justice advantages, pursuing social and regulatory policy through the tax code has what I call "institutional advantages." These institutional effects accrue, on the one hand, because embedding laws in the tax code can positively influence the governmental agencies involved in enacting and implementing tax policy, and, on the other hand, because use of the tax code for social-policy and regulatory goals can influence the substance of the policies enacted.[207] The following discussion will analyze several relevant governmental institutions to detail these advantages by considering the IRS in comparison with other federal agencies and then considering the federal government in relation to state governments.

1. Introducing the IRS Into a Substantive Area Helps Laws in That Area Achieve Their Goals

When Congress embeds policy in the tax code, that policy then falls to the IRS to implement. In the typical case, that newly tax-embedded policy was one that was previously the domain of some other federal agency. How-

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[206] *See* Scott A. Hodge, *Record Numbers of People Paying No Income Tax; Over 50 Million "Nonpayers" Include Families Making over $50,000*, TAX FOUNDATION (Mar. 10, 2010), http://www.taxfoundation.org/news/show/25962.html.

[207] *See* discussion *supra* Part III.

ever, bringing new policy arenas under the IRS's umbrella offers three specific advantages.[208]

First, incorporating substantive areas such as poverty elimination, energy, housing, education, international trade, community development and so on into the tax code usually introduces the IRS into a field that some other federal agency has traditionally dominated. This helpfully diversifies policy administration.[209] When the IRS enters, the other agencies rarely leave.[210] The resulting multi-agency co-presence may produce better programs and create backstops for when programs fail. When multiple agencies take responsibility for a substantive area, one will likely always be there if pathologies develop in another or if another's programs are just not working. At the same time, the IRS brings particular abilities to jurisdictions that it shares with other agencies. The IRS's focus on accurate revenue collection distinguishes it from agencies geared toward substantive policy goals. According to tax scholar David Weisbach, the IRS's "mission and expertise are so different than a typical line agency. . . . The tax agency is unlikely to have strong views about other programs, such as environmental, energy, housing or education programs."[211] He adds that the IRS's "expertise in processing paper and measuring income may be significantly different than that of other agencies,"[212] so that "adding the tax agency may add an element of diversification not otherwise available."[213]

Second, expanding the IRS's jurisdiction to include substantive areas of law traditionally governed by other agencies may also help the IRS to develop additional strengths and be an even better co-administrator in a given policy field. A common stereotype holds that what bureaucracies can do remains static over time. However, the modern American state itself evolved in part based on the ability of federal agencies to develop new capacities in response to increased programmatic responsibilities.[214] The more this process occurs, the more duties Congress has been willing to give to the agencies. Then, insofar as Congress continues to assign new tasks to the IRS, Congress will reinforce long-term developments that have already started to alter the agency's character. While the IRS will likely retain a strong revenue-collecting identity, IRS staff understanding of the agency's overall mission and capacity may shift. In line with this shift, the IRS would need to hire

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[208] Again, this section focuses on the relative advantages of the IRS. Administering major federal policies is sufficiently difficult that no agency can do it perfectly. The IRS's singular combination of capacities and flaws, however, makes it relatively well-suited to take on the new responsibilities discussed here. As discussed above, for more on this type of comparative institutional analysis, see generally KOMESAR, *supra* note 117.

[209] *See* Staudt, *supra* note 78, at 1223.

[210] Weisbach, *supra* note 78, at 1830–36.

[211] Weisbach, *supra* note 78, at 1841.

[212] Weisbach, *supra* note 78, at 1841.

[213] Weisbach, *supra* note 78, at 1842.

[214] *See* Daniel P. Carpenter, *State Building Through Reputation Building: Policy Innovation and Coalitions of Esteem at the Post Office, 1883–1912*, 14 STUD. IN AM. POL. DEV. 121, 122 (2000).

new personnel.[215] Hiring specialists outside of the traditional tax lineup would further reorient the agency. New hiring would be particularly consequential because embedding more programs in the tax code expands the responsibilities of tax law as a field. Dealing with the tax code generally involves professional intermediaries such as accountants, investors, and tax lawyers, and the field in which these experts operate enlarges as policymakers embed more initiatives in the tax code. To the extent that the tax code expands to cover more and more substantive arenas of lawmaking, tax lawyers and accountants will become responsible for knowing a bit about almost every substantive area. As this happens, the IRS will recruit from new pools of expertise. These pools may be larger than the ones from which the IRS usually selects, because aspiring professionals with a wider array of substantive interests will select tax law as a profession. The new recruits will be positioned to combine their subspecialties with the particular skills that tax lawyers have traditionally offered.

Third, the IRS's experience thus far in administering social policy suggests that the agency is particularly capable of enforcing program rules. Drawing on evidence from the EITC, research has shown that the IRS has especially strong but flexible enforcement capacity, which could serve new programs falling under the agency's jurisdiction.[216]

The IRS's enforcement efforts take several approaches. For example, the IRS sometimes employs "precertification programs."[217] These are programs tailored to specific situations believed to produce noncompliance. For instance, in 1999, the IRS determined that the EITC "qualifying child errors" were common among EITC recipients.[218] A "qualifying child error" occurred when a taxpayer tried to claim the EITC for a child who did not live with him or her.[219] Analyzing return data, the IRS found that qualifying child errors happened most frequently among fathers not filing jointly and among non-parent claimants.[220] Given this, the IRS selected 25,000 taxpayers from that group and required them to "precertify," that is, to demonstrate that any claimed child actually lived with them.[221] If the selected taxpayers could not show this was the case, they could not receive benefits.[222] Now, the IRS imposes severe penalties on people who commit EITC fraud. If the IRS determines that a taxpayer fraudulently claims the EITC, that taxpayer cannot get any more EITCs for ten years even if the taxpayer is otherwise eligi-

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[215] New hiring in this area would of course require Congress to allocate money to the IRS to support this goal. Congress has traditionally increased the resources of federal agencies to which it delegates major new tasks.

[216] *See* Lawrence Zelenak, *Tax or Welfare? The Administration of the Earned Income Tax Credit*, 52 UCLA L. Rev. 1867, 1869 (2005).

[217] *Id.* at 1869–70.

[218] *Id.* at 1869.

[219] *Id.*

[220] *See id.* at 1870.

[221] *Id.* at 1871.

[222] *Id.* at 1870.

ble for them.[223] If the IRS determines that a taxpayer has recklessly or intentionally disregarded the rules in claiming the EITC, an otherwise eligible taxpayer cannot get any more EITCs for two years.[224] Significantly, the IRS has used this enforcement power judiciously. Research has shown that the IRS is less likely than other agencies to make eligibility and measurement mistakes, and, when it does, it is more likely than those other agencies to make taxpayer-friendly mistakes. In fact, research has demonstrated that "[EITC] errors in favor of taxpayers exceeded errors in favor of the government by a ratio of more than 5:1."[225]

As a result, the IRS, using both its traditional and newfound capacities, has the potential to become an important force with regard to areas of law that other agencies have historically covered. As lawmaking continues its tax-oriented transformation and the IRS acquires more substantive areas, the benefits of expanding IRS jurisdiction are likely to snowball. Thus, the Affordable Care Act substantially expands the IRS's reach into the health care area, where the Department of Health and Human Services already works, as well as into the low-income subsidy area, previously dominated by the Department of Agriculture and the Department of Labor. Under the Affordable Care Act, the IRS can support and protect these departments' health care-related goals. For example, by giving the IRS responsibility for the individual mandate, the employer mandate, the small employer credit, and the premium assistance credit, the Affordable Care Act allows the IRS to use its information gathering and "measurement" capacity to determine how much health care people have, how much it costs, and how to make sure the right people wind up with the right subsidies.

2. *Tax-Embedded Policies Distribute Power More Equitably Between Federal and State Governments*

One of the key challenges for American political institutions is to achieve an appropriate balance of power between the federal and state governments. From the Founding era onwards, policymakers at both levels have grappled with federalism issues when making new laws, particularly when those laws constitute major social reforms. Unsurprisingly, enacting social programs and regulations through the tax code has substantial consequences for federalism. However, while the ongoing structural transformation may initially seem like improper federal encroachment onto areas of state concern, recent scholarship has shown that using the tax code for non-revenue-raising purposes may actually harness the strengths of both federal and state governments in ways that allocate power between the two appropriately.

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[223] *Id.* at 1893.
[224] *Id.*
[225] *Id.* at 1890.

Enacting law through the federal tax code might initially raise federalism concerns because tax-embedded programs often pertain to policy areas like housing and education that have historically fallen to the states. As Ruth Mason recently put it, federal incentives may "displace the expression of local values and local political preferences."[226] Further, federal taxing and spending may "enlarge the scope of [the federal government's] regulatory influence . . . [and] reduce[ ] the areas in which the states can compete with the federal government and with each other."[227] Scholars who oppose the Affordable Care Act on constitutional grounds make similar points, focusing on the (mis-)use of the tax code for regulatory purposes. For instance, Randy Barnett has argued that using the tax code to enact the individual mandate, insofar as that choice implicates the taxing and spending power, as the Supreme Court ruled that it does,[228] allows Congress "to penalize or mandate any activity by anyone in the country, provided it limit[s] the sanction to a fine enforced by the Internal Revenue Service. This is a congressional power unknown and unheard of before 2010. It would effectively [and unconstitutionally] grant Congress a general police power."[229]

These charges notwithstanding, enacting policy through the tax code appears actually to distribute power between federal and state governments so as to take advantage of the ways that each can enhance the policy. This is the case for multiple reasons. First, the federal government's traditional practice of implementing direct-spending programs through grants to states forces states to accept wholly the terms of these grants.[230] In contrast, states have greater freedom to select among tax-embedded programs so as to find the ones that reflect their citizens' needs and preferences. For example, Mason highlights the fact that "states are not contractually bound to implement federal tax incentives."[231] Instead, states can respond to their residents' views and "enact policies different from or even conflicting with federal tax policies."[232] Data show that more and more states are exercising the option to decouple their tax policies from those of the federal government.[233]

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[226] Mason, *supra* note 83, at 994.

[227] Mason, *supra* note 83, at 994.

[228] Nat'l Fed'n of Indep. Bus. v. Sebelius, 132 S. Ct. 2566 (2012).

[229] Randy E. Barnett, *Commandeering the People: Why the Individual Health Insurance Mandate Is Unconstitutional*, 5 N.Y.U. J. L. & Liberty 581, 613 (2010).

[230] *See* Mason, *supra* note 83, at 1028.

[231] Mason, *supra* note 83, at 1010.

[232] Mason, *supra* note 83, at 1028. How important these state policies are in terms of revenue of course depends on the state income tax rate. States with high individual income tax rates may use the tax to provide more powerful policy incentives than states whose rates are low or zero.

[233] *See, e.g.*, Nicholas Johnson, Ctr. On Budget And Policy Priorities, Many States Are Decoupling from Federal "Bonus Depreciation" Tax Cut (2002), *available at* http://www.cbpp.org/cms/?fa=view&id=356; Elizabeth McNichol, Ctr. On Budget And Policy Priorities, Many States are Decoupling from the Federal Estate Tax Cut (2006), *available at* http://www.cbpp.org/cms/?fa=view&id=308; Mason, *supra* note 83, at 1011 n.189.

Second, Congress is likely to use the tax code to enact policies that harness the states' responsiveness to the needs of their own citizens. When the federal government uses tax law to accomplish a certain goal, Congress generally leaves room for states to finesse the ways in which they will accomplish that goal.[234] For example, Mason contrasts the federal efforts to maintain highways (a direct-spending initiative) with federal efforts to subsidize charitable giving (a tax-embedded policy).[235] She points out that the federal government has enacted an enormous compendium of law to run the highway system. As a result, states do not have much room to innovate with regard to the federal highway laws. However, although Congress and the Treasury do regulate charitable giving, states also have substantial room to do that in accordance with state-level values and aims. State attorneys general have substantial room to set up their own rules for charitable organizations with regard to charitable solicitations, registration, and intra-charity compliance with fiduciary duties.[236] This power-sharing arrangement is typical of programs enacted through the federal tax code. To take another example, when Congress enacted the EITC, it set up a federal template that states could follow, and it established financial incentives for states to do so.[237] As a result, in tax year 2006, nineteen states and the District of Columbia had a state-level EITC in place.[238] These EITCs all use the federal model, but they also reflect the particular conditions and objectives of these states.[239] This is an outcome that will likely replicate itself across new tax-embedded programs.

V. Conclusion

By using tax law to accomplish so many social and regulatory objectives, the federal government has embarked on a quietly revolutionary structural transformation. While presidential administrations and Congress have been embedding non-revenue-raising programs in the tax code for several decades, recent major legislation, particularly the Affordable Care Act, reveals just how substantially the government has shifted from doing some things through the tax code to doing nearly everything through the tax code.

Previous tax scholarship on this topic, following Stanley Surrey's seminal work, has rested for too long on outdated assumptions, and, as a result, has not recognized the substantial advantages that accompany embedding

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[234] *See* Mason, *supra* note 83, at 1014.

[235] Mason, *supra* note 83, at 1014.

[236] For general information about the ways in which state attorneys general regulate charities, see *About Nasco*, Nat'l Assoc. of State Charity Officials, http://www.nasconet.org/about (last visited Nov. 5, 2012).

[237] Ifie Okwuje & Nicholas Johnson, Ctr. On Budget And Policy Priorities, A Rising Number of State Earned Income Tax Credits are Helping Working Families Escape Poverty (2006), *available at* http://www.cbpp.org/cms/?fa=view&id=733.

[238] *Id.*

[239] *Id.*

social and regulatory policy in the tax code. This Article has taken the first comprehensive step toward evaluating some of the advantages that this ongoing structural transformation offers. These advantages, legislative and normative, demonstrate the far-reaching consequences that this development will likely have for the future of U.S. policymaking. This Article initiates what should become a growing effort on the part of tax academics, economists, policy scholars, political scientists, and other social scientists to observe, analyze, and assess the current structural transformation as it unfolds.