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EVADING OVERSIGHT:
The Origins and Implications of the IRS Claim That Its Rules Do Not Have an Economic Impact

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The Origins and Implications of the IRS Claim That Its Rules Do Not Have an Economic Impact

James Valvo

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Mission:

Cause of Action Institute ("CoA Institute") is a government oversight group committed to ensuring that the federal regulatory process is open, honest, and fair. As part of its charitable mission, CoA Institute seeks judicial and legislative oversight of the federal regulatory state to protect against law enforcement abuses and arbitrary discretion, as well as to defend robust public access to government information.

Investigative Function:

CoA Institute uses investigative tools to research federal government waste, fraud, and mismanagement, as well as overreach in the form of arbitrary and burdensome regulations. It employs "sunshine advocacy" tools, including document and information requests, lawsuits, ethics complaints, and requests for investigation to promote transparency, integrity, and accountability in government. Its investigations help to expose and prevent government mismanagement of federal funds and to educate the public on how government can be made more accountable.

About the Author:

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Executive Summary

A tension exists in federal administrative law. Agencies are tasked by statute with executing delegated functions, and the president is assigned by the Constitution to head the Executive Branch and take care that laws are faithfully executed. This creates tension because agencies can make controversial, burdensome, unwise, or unaccountable decisions that may conflict with statutory mandates or the president's chosen governing course. This tension has heightened over the past one hundred years as the size and scope of the administrative state has dramatically increased. Disputes over how to control administrative agencies and the validity of their actions have also sharpened during the same period.

In an attempt to alleviate these tensions, Congress and the president have installed various regulatory-oversight mechanisms. The mechanisms, embodied in statutes and executive orders, seek to mitigate the worst agency abuses, while also reinjecting constitutional actors into the agency decision-making process. When agencies act to subvert these oversight mechanisms, they undermine legitimate checks on their power and raise concerns about the propriety of their decisions, thereby exacerbating concerns about lack of control over the administrative state.

The Internal Revenue Service ("IRS") is one such agency. It has systematically constructed a series of exemptions from certain aspects of three important oversight mechanisms: the Regulatory Flexibility Act, White House review pursuant to Executive Order 12,866, and the Congressional Review Act. The IRS purports to base these self-made exemptions on the claim that any economic impact of the rules that it issues flows from the underlying statute and is not attributable to its regulatory actions, for the purpose of triggering economic-impact analyses and information sharing under these three oversight mechanisms. The IRS, however, has not provided any detailed, public explanation to justify its position. Further, the IRS position, if correct, would apply to any regulation promulgated by any agency, as hopefully all regulations are based on a statute.

All three oversight mechanisms are designed to: (1) increase information sharing between agencies and the constitutional actors that oversee their actions, and (2) disclose to the public the economic significance of agency decisions. By claiming an exemption from these mechanisms, the IRS is denying Congress, the president, and the public important information about how IRS rules impact the economy and how different administrative choices could alleviate that impact.

Findings

Finding #1: *In the three sections of the Internal Revenue Manual that govern the IRS approach to compliance with three important regulatory oversight mechanisms, the agency claims that its regulations have no economic impact because any such impact is attributable only to the underlying statute.*

Finding #2: *The IRS asserts that its regulations have no economic impact to claim self-bestowed exemptions that allow it to avoid economic impact analyses and the sharing of information with the White House, Congress, and the public. The IRS has provided no detailed, public explanation to justify its position.*

Finding #3: *The IRS first claimed that its regulations have no economic impact to evade a congressional amendment to the Regulatory Flexibility Act that was explicitly designed to cover IRS regulations.*

Finding #4: *Over time, the IRS has expanded its self-bestowed exemption to avoid a greater number of regulatory-oversight mechanisms. The exemption first applied only to the "revenue impacts" of IRS regulations but is now claimed for all "effects." In addition to avoiding the requirement of the Regulatory Flexibility Act, the IRS also applies its exemption in the context of White House Office of Information and Regulatory Affairs review and the Congressional Review Act. The IRS has provided no detailed, public explanation to justify these expansions.*

Finding #5: *The combination of the IRS assertion that its rules do not create an economic impact and a 1983 memorandum of understanding between the White House and the Department of the Treasury has created a moral hazard that allows the IRS to determine which rules it sends to the White House for pre-publication review, as required under Executive Order 12,866 and its progeny.*

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Introduction

In 1996, Congress updated the Regulatory Flexibility Act ("RFA") to ensure that the IRS analyzes the economic impact of the rules it issues. In 1998, however, the IRS Office of Chief Counsel circulated a memo announcing there was no need to conduct that analysis because IRS rules have no economic impact after all. The IRS advanced this position without statutory justification or detailed public explanation. To compound the problem, the claim that IRS rules have no economic impact has metastasized throughout the Internal Revenue Manual ("IRM") such that the IRS now uses it to exempt itself from three important oversight mechanisms. The origin and basis of this self-bestowed exemption appears to have gone unchallenged for decades and its full extent has only recently come to light as a result of the investigative work that underlies this report.

The basis of the IRS claim that its rules do not have an economic impact is that any impact that may occur is merely a result of the underlying statute and not the rules interpreting or implementing that statute. The IRS has expanded the types of impacts covered by this claim over time. It first proposed that any "revenue impact" (*i.e.*, money collected by the Treasury) is caused by statute and not regulation. This position may be appealing in the context of basic IRS regimes, for example, marginal income tax rates. But the IRS has since expanded its claim by asserting that any and all "effects" of its rules also are caused by the authorizing statute. The effects of IRS rules reach beyond just the money taxpayers remit to the Treasury and extend to macroeconomic impacts, behavioral changes in response to the rule, compliance costs, and recordkeeping and reporting burdens.

The IRS self-exempts itself from other oversight mechanisms as well. As noted, the assertion that IRS rules do not have an economic effect was originally employed to avoid conducting regulatory flexibility analyses under the RFA. But the IRS now uses the same justification to sidestep review of many of its rules by the White House Office of Information and Regulatory Affairs and to shirk responsibilities under the Congressional Review Act.

The IRS claim that its rules do not have an economic impact for purposes of these three oversight and review mechanisms is flawed for a number of reasons. First, if the IRS position were correct, it would seemingly exempt all agencies from these regulatory-oversight regimes. The effects of all regulatory decisions ultimately flow back to an authorizing statute that empowers the agency to act in the first place. But Congress and the president have put these oversight mechanisms in place to police agency regulatory decisions under those organic statutes; a wholesale exemption runs counter to their very purpose and creates an absurd result. Second, even if the IRS were compelled to issue an initial regulation by the passage of a new statute—for example, if the IRS outlined how it would administer a new tax—subsequent decisions to revise a previous regulatory interpretation would be an action the IRS is taking on its own account. The impact of that subsequent decision must be attributable to the agency, not the statute. Given the vast discretion the IRS claims under its authorizing statutes, the argument that the exercise of that discretion to choose one approach to a rule from other competing approaches has no impact is unsupportable.

It appears that, so far, the IRS claim that its rules have no economic impact has escaped judicial review. Both the Small Business Administration Office of Advocacy and the Government Accountability Office have raised questions about the propriety of the agency's self-bestowed exemptions, but the IRS has never been required by a court (or anyone else) to spell out exactly why it believes the exemptions are proper.

This report details the origins and implications of the IRS claim. It explains the three relevant oversight regimes and the way the IRS amended the IRM over time to exempt itself from oversight. Section I discusses the RFA and the IRS Office of Chief Counsel memo that appears to have made the claim for the first time. Section II outlines White House review of agency rules and a 1983 memorandum of agreement between the White House and IRS that laid the groundwork for the IRS to later self-exempt many of its rules. Finally, Section III discusses the Congressional Review Act and explains how the IRS avoids having its rules analyzed as "major rules" under that statute.

I. Regulatory Flexibility Act

Under the RFA, if a proposed regulation "is likely to have a significant economic impact on a substantial number of small entities,"[1] the agency is required to consider alternatives to the proposed regulation that would accomplish the same objectives without unduly burdening small entities. In considering alternatives, the RFA requires agencies to conduct economic impact analyses[2] and describe alternatives that consider tiered application of rules, simplification, performance rather than design standards, and exemptions.[3] The RFA's purpose is to mitigate the "high costs of compliance with regulations by small businesses bound to conform their conduct to those regulations."[4]

The Act has procedural rather than substantive effects. It has been compared to the National Environmental Policy Act ("NEPA") because both are informational statutes requiring the federal government to collect, analyze, and publish information about a pending decision, but neither requires the outcome of the decision to be influenced or supported by that information.[5]

1 5 U.S.C. § 602(a)(1).

2 These analyses are known as an initial regulatory flexibility analysis and a final regulatory flexibility analysis. *See id.* §§ 603–04.

3 *Id.* § 603(c).

4 *Mid-Tex. Elec. Coop., Inc. v. Fed. Energy Regulatory Comm'n*, 773 F.2d 327, 342 (D.C. Cir. 1985).

5 *See, e.g.*, Office of Advocacy, U.S. Small Bus. Admin., A Guide for Government Agencies: How to Comply with the Regulatory Flexibility Act at 7 (2012) [hereinafter SBA RFA Guide], *available at* http://bit.ly/2rsIUOD.

The meaning of "significant economic impact" is a major factor when agencies are considering whether to conduct an RFA analysis. Although there is no statutory definition of the phrase, the Small Business Administration's ("SBA") guidance summarizes the legislative history to provide helpful context:

> "The term 'significant economic impact' is, of necessity, not an exact standard. Because of the diversity of both the community of small entities and of rules themselves, any more precise definition is virtually impossible and may be counterproductive. . . . Agencies should not give a narrow reading to what constitutes a "significant economic impact" . . . [and] a determination of significant economic effect is not limited to easily quantifiable costs."
>
> Congress has identified several examples of "significant impact": a rule that provides a strong disincentive to seek capital; 175 staff hours per year for recordkeeping; impacts greater than the $500 fine (in 1980 dollars) imposed for noncompliance; new capital requirements beyond the reach of the entity; and any impact less cost-efficient than another reasonable regulatory alternative.[6]

Numerous courts also have interpreted the phrase. In *Colorado State Banking Board v. Resolution Trust Corp.*, the U.S. Court of Appeals for the Tenth Circuit found an RFA analysis was not required because the rule "impose[d] no performance standards, no fees, no reporting or recordkeeping criteria, nor any other type of restriction or requirement with which [regulated entities] must comply. Thus, it does not have the type of economic impact addressed by the RFA."[7] But a U.S. district court in Florida found an agency wanting in its refusal to conduct an RFA analysis for a rule dramatically reducing the quota for shark fishermen because it failed to account for evidence in the record relating to the economic impacts of the proposed measure.[8]

A. The Current IRS RFA Procedures

The IRS details its RFA rules and procedures in the IRM.[9] In its definition section, the IRM outlines the steps IRS rule writers should follow when issuing

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6 *Id.* at 20 (citing the Congressional Record).

7 926 F.2d 931, 948 (10th Cir. 1991) (citation omitted); *accord Sw. Pa. Growth All. v. Browner*, 121 F.3d 106, 123 (3d Cir. 1997) (relying on Tenth Circuit's reasoning).

8 *S. Offshore Fishing Ass'n v. Daley*, 995 F. Supp. 1411, 1436 (M.D. Fla. 1998) ("I conclude that the Secretary's 'no significant impact' certification and the FRFA fail to satisfy APA standards and RFA requirements. The record strongly indicates that the 1997 quotas, and most prominently the LCS quota, will significantly injure the prospects of shark fishermen pursuant to Commerce Department thresholds. The record also severely discredits NMFS's argument that no fishermen are dependent on shark fishing and that the plaintiffs can effortlessly transfer their fishing efforts to other stocks.").

9 *See* Internal Revenue Serv., Internal Revenue Manual § 32.1.5 [hereinafter I.R.M.].

interpretative regulations with an information collection requirement. That definition section does not claim that the impact of IRS rules flows from the statute and not the rule.[10] The definition section also does not contain an interpretation as it relates to legislative rules. However, elsewhere in its RFA procedural rules, the IRS carves out RFA exceptions for both interpretative and legislative rules.

1. Interpretative Rules

Under the IRM, an RFA analysis is unnecessary for interpretative rules when the significant economic impact "flows directly from the underlying statute or other legal authority."[11] The decision to forgo the RFA analysis must be justified: "[t]his explanation should not be summary boilerplate but should be appropriately detailed . . . For example, if a regulatory impact analysis is not required because the effect on small entities flows directly from the underlying statute, the certification should explain why the effect or impact flows from the statute or other legal authority being implemented."[12]

32.1.5.4.7.5.4.3 (09-30-2011)
Applicability of RFA: Interpretative Regulations

5. If the regulation contains a collection of information requirement and if the regulation implements a statute or other legal authority that imposes a significant economic impact on a substantial number of small entities, to the extent the significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or other legal authority, a regulatory flexibility analysis is not required. Include the following certification in the Special Analyses section:

   "It is hereby certified that this regulation will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required."

6. Any certification that the RFA analysis is not required should include an explanation. This explanation should not be summary boilerplate but should be appropriately detailed to show that the applicability of the RFA was considered. The reasoning for the certification should be explained. For example, if a regulatory impact analysis is not required because the effect on small entities flows directly from the underlying statute, the certification should explain why the effect or impact flows from the statute or other legal authority being implemented.

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10 *See id.* § 32.1.5.4.7.5.4.1.4 ("For interpretative regulations, the drafting team should estimate the economic impact of the collection of information requirement in a manner similar to determining the burden estimates under the [Paperwork Reduction Act]. The drafting team should calculate the annual economic impact based on all relevant facts and circumstances, including the hours necessary to comply with the collection of information and the costs of purchasing equipment that is necessary to comply with the collection of information. One common method of estimating the economic impact of a collection of information is to multiply the [Paperwork Reduction Act] burden estimate (stated in terms of total hours) by an appropriate hourly rate. Consider the purpose and complexity of the rule to determine whether its economic impact is 'significant.'").

11 *Id.* § 32.1.5.4.7.5.4.3.5 ("[T]o the extent the significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or other legal authority, a regulatory flexibility analysis is not required.").

12 *Id.* § 32.1.5.4.7.5.4.3.6.

Although, by rule, the IRS is not supposed to use boilerplate language when asserting that the effect of a rule change flows from the statute, in practice the agency provides little detail for its claims. For example, in 2016 the IRS proposed changes to the way it valued interests in closely held businesses for the purposes of estate, gift, and generation-skipping transfer taxes.[13] The IRS claimed this was an interpretative rule and, in its *Federal Register* filing, provided no more than the boilerplate claim that "any economic impact on entities affected by section 2704, large or small, is derived from the operation of the statute, or its intended application, and not from the proposed regulations in this notice of proposed rulemaking. Accordingly, a regulatory flexibility analysis is not required."[14] A review of the Regulatory Flexibility Checklist for the rule, obtained through the Freedom of Information Act ("FOIA"), reveals that the rule writers did not provide any justification for this claim or indeed reference it at all.[15]

"The IRS believes "that any regulatory implementation of a statute should not be subject to an RFA analysis. [The Office of] Advocacy does not agree with this analysis."

– Small Business Administration Office of Advocacy

The IRS did submit the rule to the SBA's Office of Advocacy for comment on its impact on small businesses.[16] In response, the Office of Advocacy rejected the IRS claim, which it said "suggests [the IRS believes] that any regulatory implementation of a statute should not be subject to an RFA analysis. [The Office of] Advocacy does not agree with this analysis. The proposed regulations are a legislative rulemaking that should be subject to an RFA analysis."[17]

13 *See* Estate, Gift, and Generation-Skipping Transfer Taxes; Restrictions on Liquidation of an Interest, 81 Fed. Reg. 51,413 (Aug. 4, 2016) (to be codified at 26 C.F.R. pt. 25).

14 *Id*. at 51,418.

15 *See* Internal Revenue Serv., Regulatory Flexibility Checklist, Regulations Project REG-163113-02, Estate, Gift, and Generation-skipping Transfer Taxes; Restrictions on Liquidation of an Interest, *available at* http://coainst.org/2vXF9Cf.

16 *Id*. at 2.

17 Letter from Darryl L. DePriest, Chief Counsel, Office of Advocacy, Small Bus. Admin., *et al*., to William J. Wilkins, Chief Counsel, Internal Revenue Serv. (Nov. 1, 2016), *available at* http://coainst.org/2wuQ31Q.

2. Legislative Rules

For legislative rules, the IRS makes the similar claim that an RFA analysis is not required if "all significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or authority."[18] And, as with the exemption claimed for interpretative rules, IRS rule writers must justify their decision: "[i]f the effect on small entities flows directly from the statute or other legal authority being implemented, the statement should explain why that is the case." [19]

32.1.5.4.7.5.4.4 (09-30-2011)
Applicability of RFA: Legislative Regulations

1. Legislative regulations are subject to the RFA. A regulatory flexibility analysis, however, may not be required for all legislative regulations.
2. A regulatory flexibility analysis is not required if the regulation either
    1. Will not have a significant economic impact on a substantial number of small entities; or
    2. Implements a statute or other legal authority that imposes a significant economic impact on a substantial number of small entities and all significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or authority.
3. If either of the conditions described in CCDM 32.1.5.4.7.5.4.4(2) above apply, include the following certification in the Special Analyses section:

    "It is hereby certified that this regulation will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required."
4. The certification statement should be followed by a factual explanation of the basis for the certification. If the regulation does not affect small entities, explain who is affected by the regulation. If the number of small entities affected is not substantial, explain why and include, to the extent practicable, a quantification of the number of small entities affected. If the economic impact on affected small entities is not significant, include a discussion of the economic impact/burden. If the effect on small entities flows directly from the statute or other legal authority being implemented, the statement should explain why that is the case. If in doubt about the accuracy of the certification, the drafting team should request comment on the accuracy of the certification.

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18 I.R.M. § 32.1.5.4.7.5.4.4.2.2.

19 *Id.* § 32.1.5.4.7.5.4.4.4.

B. Origins of the IRS Claim that the Impact of its Rules Flows from the Statute

The IRS has not always maintained its current practice with respect to the RFA. In the August 1994 revision to the IRM's RFA section, the IRS had not yet claimed that the effects of its rules flow from statute.[20] It also did not appear to have any trouble understanding what the term "significant economic impact" meant, as it did not raise any concerns in the IRM.

Chief Counsel Regulations Handbook **page (30)(15)20–67** (1–18–95)

531.4 *(8–1–94)* (30)(15)20

Regulatory Flexibility Act

Under the Regulatory Flexibility Act (5 U.S.C. chapter 6), if regulations will have a significant economic impact on a substantial number of small entities, a Regulatory Flexibility Analysis must be prepared. The requirements of the Act do not apply if—

- A notice of proposed rulemaking is not required by law to be published, even if one was in fact published;
- The regulations are temporary regulations as opposed to final regulations; or
- The Commissioner certifies that the regulations will not have a significant economic impact on a substantial number of small entities.

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"The IRS appears to have created this self-bestowed exemption in response to Congress expressly amending the RFA to cover IRS interpretative regulations.

20 In 1994, the IRS codified this section using the designation (30)(15)20 and Section 531.4. The entire IRM was re-codified in the early 2000s.

The earliest reference uncovered of the IRS claim that its rules do not have an economic impact is a March 1998 notice from the IRS Office of Chief Counsel. The office sent that notice, superseding the above-referenced Section 531.4, following the 1996 passage of the Small Business Regulatory Enforcement Fairness Act ("SBREFA").

Department of the Treasury | Internal Revenue Service | Office of Chief Counsel

Notice

N(30)(15)531-1

March 3, 1998

Subject: Regulatory Flexibility Act Cancellation Date: August 30, 1998

The following material replaces existing section 531 of the Regulations Handbook regarding background and procedures to be followed in ensuring compliance with the Regulatory Flexibility Act. The updated material incorporates changes to the Regulatory Flexibility Act made by the Small Business Regulatory Enforcement Fairness Act.

SBREFA amended the RFA explicitly to cover IRS interpretative rules that impose a collection-of-information requirement on small entities and to provide for judicial review of agency actions under the RFA.[21]

The 1998 IRS Notice claims that the RFA

> and [its] legislative history also do not define the term 'significant economic impact.' With respect to interpretative regulations, any possible revenue impact of the regulations is inherently part of the revenue impact of the underlying statute, and thus is not considered in measuring any economic impact attributable to the regulations. Also, because the RFA applies only to the portion of interpretative regulations that imposes a collection of information, the relevant economic impact of such regulations is only the economic impact of the collection of information.

21 *See* Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. 104-121, §§ 241–42, 110 Stat. 847 (codified at 5 U.S.C. § 603(a), 611) (ensuring that "proposed rulemaking[s] for an interpretative rule involving the internal revenue laws of the United States" are covered) [hereinafter SBREFA].

This appears to be the first time the IRS claimed the statutory term "significant economic impact" lacks sufficient definition, despite its presence in the RFA since 1980.[22]

B. Significant Economic Impact. The applicable statute and legislative history also do not define the term "significant economic impact." With respect to interpretative regulations, any possible revenue impact of the regulations is inherently part of the revenue impact of the underlying statute, and thus is not considered in measuring any economic impact attributable to the regulations. Also, because the RFA applies only to the portion of interpretative regulations that imposes a collection of information, the relevant economic impact of such regulations is only the economic impact of the collection of information. See 5 U.S.C. 603(a). The economic impact of a collection of information should be estimated in a manner consistent with similar estimates that are required for purposes of the PRA. The estimate generally should be determined on an annual basis and should be based on all relevant facts and circumstances, including the hours necessary to comply with the collection of information, the costs of purchasing equipment that is necessary to comply with the collection of information, etc. Cf. 44 U.S.C. 3502(2) (definition of "burden" for purposes of the PRA). Burden estimates under the PRA generally are stated in terms of a number of hours. One possible method of estimating the economic impact of a collection of information is to multiply the PRA estimate of burden hours times an hourly rate.

Pages IRS00849–53; Ex. 1

22 *See* Regulatory Flexibility Act, Pub. L. 96-354, § 3, 94 Stat. 1164 (1980).

IRS reliance on the 1998 Notice raises at least three significant problems. First, the Notice claims the RFA and its legislative history do not define "significant economic impact." This is misleading. Although the statute does not contain a definition, the RFA's legislative history does provide guidance and examples. The SBA has collected this history in its guide for agency compliance with the Act. The SBA catalogues that covered impacts include: a strong disincentive to seek capital, staff hours for recordkeeping, large fines for noncompliance, new capital requirements beyond an entity's reach, and inefficient regulatory alternatives.[23] In addition, although the assertion about the lack of a definition appears to be the basis for the central IRS claim in the next sentence—"any possible revenue impact of the regulations is inherently part of the revenue impact of the underlying statute"—it is unclear how a purported lack of a definition relates to whether an impact flows from the statute or the regulation. The type of impacts measured is a different question than the source of those impacts. It also bears noting that other agencies around the same time period did not try to use the lack of statutory definition for the term as an excuse to avoid their responsibilities.[24]

> *"The original IRS claim was limited to an exemption for interpretative regulations and revenue impacts; both limitations fell away over time.*

Second, the Notice limits its claim about impacts in two ways: by only discussing (1) interpretative regulations, and (2) the revenue impact of a rule (*i.e.*, the dollar amount transferred to the U.S. Treasury). Both of these limitations fall away without explanation or justification in later iterations of the claim as it relates to the RFA and as it proliferates throughout other sections of the IRM. For example, see below the August 2004 codification of the 1998 Notice as it applies to the RFA.

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23 *See* SBA RFA Guide, *supra* note 5, at 20.

24 *See, e.g.*, Groundfish Fishery of the Gulf of Alaska Proposed 1999 Harvest Specifications, 63 Fed. Reg. 71,876, 71,883 (proposed Dec. 30, 1998) (to be codified at 50 C.F.R. pt. 679) (Department of Commerce considering the extent of recordkeeping and reporting burdens); Changes to the Board of Directors of the National Exchange Carrier Association, Inc., 63 Fed. Reg. 70,564, 70,571 (Dec. 21, 1998) (to be codified at 47 C.F.R. pts. 54 & 69) (Federal Communications Commission comparing filing requirements under new standard to existing rules); Multi-Purpose Lighters, 63 Fed. Reg. 52,397, 53,413 (proposed Sept. 30, 1998) (to be codified at 16 C.F.R. pt. 1212) (Consumer Product Safety Commission considering effects on competition).

Third, the Notice only addresses impacts in the context of interpretative rules' information-collection burdens under the RFA.[25] When the original RFA was enacted, the IRS evaded the statute's requirements by characterizing almost all IRS rules as "interpretive rules" that, it claimed, fall outside the scope of the Act.[26] The IRS, in other words, purposefully categorized its rules to avoid the statutory safeguards imposed by the RFA. This gambit did not please Congress and led Senator Dale Bumpers to call IRS rules "*so-called* interpretative rulemakings."[27] It also led Congress to enact SBREFA in an attempt to force the IRS to perform RFA analyses on interpretative rules that impose a collection-of-information requirement on small entities.[28]

The 1998 Notice correctly acknowledged the requirements of SBREFA and charged the IRS with conducting an initial regulatory flexibility analysis for such rules in a manner similar to ones conducted pursuant to the Paperwork Reduction Act. The Notice comported with the requirements of the newly amended RFA and aligned with congressional intent as reflected in the legislative history.[29] Despite this, however, IRS noncompliance has persisted. At a 2003 congressional hearing discussing IRS compliance, Congressman Donald Manzullo remarked that "[r]ather than embrace the changes in SBREFA, the IRS and the Department [of the Treasury] adopted new interpretations to avoid compliance with the RFA."[30]

25 The RFA distinction between IRS legislative and interpretative rules underscores the ongoing dispute surrounding the IRS position that nearly all of its rules are interpretative. *See generally* 5 U.S.C. § 553; I.R.M. § 32.1.2.3.3 ("most IRS/Treasury regulations are interpretative"); Kristin E. Hickman, *IRB Guidance: The No Man's Land of Tax Code*, 2009 Mich. St. L. Rev. 239 (2009); Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 Notre Dame L. Rev. 1727, 1740–59 (2007).

26 U.S. Gov't Accountability Office, GAO/GGD-94-105, Regulatory Flexibility Act: Status of Agencies' Compliance 4 (1994), *available at* http://www.gao.gov/assets/220/219465.pdf.

27 142 Cong. Rec. S2156 (daily ed. Mar. 15, 1996) (emphasis added).

28 *Id.*; SBREFA, *supra* note 21 (amending 5 U.S.C. 603(a)).

29 "The Committee interprets" the term "'collection of information' as used in the Paperwork Reduction Act . . . to include all tax recordkeeping, filing and similar compliance activities." 142 Cong. Rec. S2159 (emphasis added).

30 *See* IRS Compliance with The Regulatory Flexibility Act: Hearing Before the H. Comm. on Small Bus., 108th Cong. 1 (2003) (statement of Rep. Donald Manzullo, Chairman, H. Comm. on Small Bus.).

In August 2004, the IRS moved the language from the Chief Counsel's 1998 Notice into the IRM and re-codified the section.[31] Unfortunately, the IRS dropped the language concerning Section 603(a) (requiring RFA analyses on interpretative rules that impose a collection-of-information requirement) and instead focused on its self-made "underlying statute" rationale. This rationale, and the current wording of the IRM, likely has led to ongoing noncompliance.

32.1.5.4.7.5.4.3
(08-11-2004)
Applicability of RFA: Interpretative Regulations

(1) If the regulation is interpretative, but does not involve the internal revenue laws of the United States, it is not subject to the RFA. Include a statement in the Special Analyses section explaining that the RFA does not apply because it does not involve any internal revenue laws.

(2) If the final regulation is an interpretative final regulation for which an NPRM was issued prior to March 29, 1996, it is not subject to the RFA. Include the following statement in the Special Analyses section:

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(5) If the regulation contains a collection of information requirement and if the regulation implements a statute or other legal authority that imposes a significant economic impact on a substantial number of small entities, to the extent the significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or other legal authority, a regulatory flexibility analysis is not required. Include the following certification in the Special Analyses section:

> "It is hereby certified that this regulation will not have a significant economic impact on a substantial number of small entities. Accordingly, a regulatory flexibility analysis is not required."

Note: Follow this statement with an explanation of why the effect on small entities flows directly from the statute or other legal authority being implemented. If in doubt about the accuracy of the certification, the drafting team should request comment on the accuracy of the certification.

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32.1.5.4.7.5.4.4
(08-11-2004)
Applicability of RFA: Legislative Regulations

(1) Legislative regulations are subject to the RFA. A regulatory flexibility analysis, however, may not be required for all legislative regulations.

(2) A regulatory flexibility analysis is not required if the regulation either

a. Will not have a significant economic impact on a substantial number of small entities; or
b. Implements a statute or other legal authority that imposes a significant economic impact on a substantial number of small entities and all significant economic impact on a substantial number of small entities contained in the regulation flows directly from the underlying statute or authority.

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The above language outlining procedures for both interpretative and legislative regulations looks much the same as it does today.[32] The IRS continues to use this exemption of its own making to evade RFA analysis on these rules.

31 The 1998 Notice was included as an exhibit in the 2004 IRM. *See* IRM Ex. 32.1.5-2, Chief Counsel Notice N(30)(15)531-1 (Bates IRS00459).

32 The Note following 32.1.5.4.7.5.4.3.5 has since become .6.

II. White House Review of IRS Rules

A. A Brief History of White House Review of Agency Rulemaking

In 1981, President Ronald Reagan made a major shift in the way agency regulations are created, reviewed, and promulgated. As part of his Cabinet-level Task Force on Regulatory Relief, President Reagan issued Executive Order ("EO") 12,291, which required agencies to conduct cost-benefit analyses of proposed regulations.[33] The order only applied to "major rules," a new conceptualization of regulatory actions that would have a long-lasting impact. "Major rules" included those with an annual economic impact of $100 million or more, a major increase in costs or prices, or an adverse impact on key areas of American businesses, such as employment, investment, and productivity.[34] EO 12,291 also placed the White House Office and Management and Budget's ("OMB") Office of Information and Regulatory Affairs ("OIRA") at the center of the regulatory process, a position OIRA has not relinquished in the thirty-five years since.[35] Four years after EO 12,291 was introduced, President Reagan bolstered this agency's oversight authority with another executive order that required agency heads to submit to OMB "a statement of its regulatory policies, goals, and objectives for the coming year and information concerning all significant regulatory actions underway or planned[.]"[36]

33 Exec. Order No. 12,291, 46 Fed. Reg. 13,193 (Feb. 17, 1981); *see also* Jim Tozzi, *OIRA's Formative Years: The Historical Record*, 63 Admin. L. Rev. (Special Edition) 37 (2011) [hereinafter Tozzi, *OIRA's Formation Years*] (detailing the early years of White House review of agency rulemaking).

34 Exec. Order No. 12,291 § 1(b).

35 Tozzi, *OIRA's Formation Years* at 39 ("[T]he signing of Executive Order 12,291 did not mark the initiation of centralized regulatory review but . . . rather the culmination of a fifteen-year effort spanning the four previous presidential administrations.").

36 Exec. Order No. 12,498, 50 Fed. Reg. 1,036 (Jan. 4, 1985).

In 1993, President Bill Clinton issued EO 12,866,[37] which again expanded the scope of White House review of agency rulemaking and required agencies to submit "significant regulatory actions"[38] to OIRA before publishing them in the *Federal Register*.[39] This order covered "major rules," as previously defined in EO 12,291, and extended review to rules that overlap with another agency's authority and those that raise novel legal or policy issues.[40] This reformulation, however, actually decreased the total number of rules OIRA reviewed because it "no longer reviewed . . . 'routine and frequent' or 'informational/ administrative' rules[.]"[41] Presidents Obama and Trump have reaffirmed EO 12,866's role in the regulatory process.[42]

B. Treasury – OMB Memorandum of Agreement Exempts IRS from OIRA Review

In 1983, as the Reagan Administration was implementing EO 12,291, OMB and the Department of the Treasury entered into a memorandum of agreement exempting all IRS rules from OMB review "except legislative regulations that are 'major' as defined in the Executive Order."[43] This memorandum had long been kept secret and was only recently made public following a FOIA request by Cause of Action Institute.[44]

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37 Exec. Order No. 12,866, 58 Fed. Reg. 51,735 (Sept. 30, 1993).

38 *Id.* § 3(f).

39 *Id.* § 8.

40 *Id.* § 3(f)(2), (4).

41 Curtis W. Copeland, *The Role of the Office of Information and Regulatory Affairs in Federal Rulemaking*, 33 Fordham Urb. L.J. 1257, 1272 (2006).

42 *See* Exec. Order No. 13,563 § 1(b), 76 Fed. Reg. 3821 (Jan. 18, 2011) ("reaffirm[ing] the principles, structures, and definitions governing contemporary regulatory review that were established in Executive Order 12866"); Mem. from Cass R. Sunstein, Adm'r, Office of Info. & Regulatory Affairs, Office of Mgmt. & Budget, The White House, to Heads of Exec. Dep'ts & Agencies, & Independent Regulatory Agencies, M-11-10 (Feb. 2, 2011) ("Executive Order 13563 specifically reiterates five principles from Executive Order 12866[, including the] consideration of benefits, costs, and burdens[.]"), *available at* http://bit.ly/2tWRCck; *see also* Exec. Order No. 13,771, 82 Fed. Reg. 9339 (Jan. 30, 2017); Mem. from Dominic J. Mancini, Acting Adm'r, Office of Info. & Regulatory Affairs, Office of Mgmt. & Budget, The White House, to Regulatory Policy Officers at Exec. Dep'ts & Agencies, & Managing & Exec. Dirs. of Certain Agencies & Comm'ns at § 2, M-17-21 (Apr. 5, 2017) ("EO 12866 remains the primary governing EO regarding regulatory planning and review. Accordingly, . . . agencies must continue to assess and consider both the benefits and costs of regulatory actions, including deregulatory actions, when making regulatory decisions, and issue regulations only upon a reasoned determination that benefits justify costs."), *available at* http://bit.ly/2vbfvwS.

43 Mem. of Agreement between Dep't of the Treasury and Office of Mgmt. & Budget, Implementation of Executive Order 12291, at § II(a)(1) (Apr. 29, 1983) [hereinafter Treasury – OMB 1983 Memorandum of Agreement], *available at* http://coainst.org/2gycPlw; Ex. 2; *see also id.* § III (exemption IRS revenue rulings and similar ruling documents); *id.* § IV (identifying an as-of-yet unreleased April 1982 memorandum that was in effect at the time of the 1983 memorandum).

44 *See* Press Release, Cause of Action Inst., Cause of Action Institute Secures Access to Secret IRS Memos with the White House (Sept. 22, 2016), http://coainst.org/2gsr2xp.

II. Regulations

Internal Revenue Service
Bureau of Alcohol, Tobacco and Firearms
U.S. Customs Service

(a)(1) The review procedures of the Executive order are waived with respect to all regulations except legislative regulations that are "major" as defined in the Executive order.

(2) The procedures specified in section II(c) of this agreement do not apply to major legislative regulations, regulations defined in section 1(a)(1)-(3) or subject to section 8 of the Executive order, advance notices of proposed rulemaking, regulations which are not reviewed or subject to approval by an Assistant Secretary prior to issuance, regulations concerning the establishment or designation of geographical viticultural areas, and technical corrections to previously published regulations. OMB may exempt additional regulations or classes of regulations from these procedures.

(b) Treasury will be responsible for alerting OMB to:

(1) any major regulation for which Executive order review has been waived.

(2) any non-major regulation that reasonably could be expected to have a significant economic impact.

Read the full memos; Ex. 2

The memorandum laid out special OMB review procedures for IRS rules that had been exempted from EO 12,291. These procedures required IRS to send OMB a statement describing the regulation, any significant policy changes, and a justification for why IRS believed the rule to be either not major or not legislative.[45] The agreement also exempted still more IRS rulemakings from the memorandum's review procedures.[46] The most significant of these additional exemptions was for any "regulations which are not reviewed or subject to approval by an Assistant

45 Treasury – OMB 1983 Memorandum of Agreement § II(c). Although the IRM has detailed procedures for how to comply with OIRA review of IRS rules, it does not explain that the agency is required to provide a statement to OMB when the IRS believes it rule is exempt from EO 12866 review. *See* I.R.M. § 32.1.5.4.7.5.3.6 ("If the regulation is not significant, the drafting team should document in the file the reasons why the regulation is not significant, including, for most projects, how any economic impact flows from the statute and not the regulation."). This instruction does not reveal that, according to the Treasury – OMB 1983 Memorandum of Agreement, the IRS is required to provide these details to OIRA for review.

46 Treasury – OMB 1983 Memorandum of Agreement § II(a)(2).

Secretary prior to issuance[.]"[47] This distinction between rules that were and were not subject to review was later reflected in a 1992 revision to the IRM procedures for sending regulations to OMB for review.[48]

The agreement created a three-tiered system for OIRA review of IRS rules. At the highest level were major legislative rules, which were subject to EO 12,291, the same as other agencies. At the middle level were non-major or non-legislative rules that were reviewed by or subject to approval by an Assistant Secretary. At the lowest level were rules that were exempted from both review regimes and thus receive no substantive OIRA review at all.

In 1993, after President Clinton issued EO 12,866, OIRA Administrator Sally Katzen issued guidance on its implementation and "decided that the previously granted exemptions [*i.e.*, those just described] should be kept in effect[.]"[49] Department of the Treasury General Counsel Jean Hanson responded to the guidance with a letter to OIRA stating that it was her understanding that IRS "regulations that are not subject to the approval of an Assistant Secretary prior to issuance," for example, "regulations amending the statement of Procedural Rules," will "continue to be exempt from review under E.O. 12866[.]"[50] Katzen replied that OIRA is "continuing the Treasury Department's current exemptions from regulatory review,"[51] specifically IRS "regulations that are not subject to the approval of an Assistant Secretary prior to issuance [and] [r]ulings documents[.]"[52] Katzen concluded that "[a]ll other rules should be included on the lists of rules under development that is to be submitted periodically to OMB so that [it] can determine which are 'significant' and hence warrant centralized review."[53]

Thus the 1993 issuance of EO 12,866 and the corresponding agreement between Treasury and OIRA left the three-tiered structure of OIRA review of IRS rules unchanged.[54] When OMB issued similar review procedures for economically

47 *Id*. Other notable exemptions from the memorandum's notification procedures include rules exempt from EO 12,291, advanced notices of proposed rulemakings, and technical corrections rules.

48 *See infra* II.D.

49 Memorandum from Hon. Sally Katzen, Adm'r, Office of Info. & Regulatory Affairs, to Heads of Executive Departments and Agencies, and Independent Regulatory Agencies, Guidance for Implementing E.O. 12866, at 7 (Oct. 12, 1993), *available at* http://bit.ly/2AZsAJk.

50 Letter from Hon. Jean E. Hanson, Gen. Counsel, Dep't of the Treasury to Hon. Sally Katzen, Adm'r, Office of Info. & Regulatory Affairs, at 2 (Nov. 4, 1993), *available at* http://coainst.org/2gycPlw; Ex. 2.

51 Letter from Hon. Sally Katzen, Adm'r, Office of Info. & Regulatory Affairs, to Hon. Jean E. Hanson, Gen. Counsel, Dep't of the Treasury (Dec. 22, 1993), *available at* http://coainst.org/2gycPlw; Ex. 2.

52 *Id*. at Enclosure.

53 *Id*. at 1.

54 The only exception is that EO 12,866 added advanced notices of proposed rulemakings to OIRA review. *See id*. at 1. ("[T]he new Executive Order does apply to advance notices of proposed rules (ANPRM's) unless an ANPRM falls within one of the substantive areas that we have agreed to exempt.").

significant guidance documents in 2007, Treasury and OMB reached a similar exemption for IRS guidance materials.[55] The Government Accountability Office ("GAO") reports that when President Obama "reaffirmed E.O. 12866 with E.O. 13563, OMB and Treasury officials did not revisit the agreement."[56] There is no evidence that the Trump Administration has revisited the agreement either.

C. Problems with the IRS Exemption from OIRA Review

The above-described three-tiered approach creates myriad opportunities for IRS to game the system and avoid OIRA review. The most obvious of these is the well-known and as-of-yet unrestrained IRS practice of claiming that nearly all of its rulemakings are non-legislative.[57] Such claims not only allow the IRS to evade the Administrative Procedure Act's notice-and-comment regime, but also allow it to claim an exemption from EO 12,866 review. There is ample persuasive criticism of the IRS claim on this point, which need not be recanvassed here.[58] Suffice it to say that allowing the IRS to determine whether its own rules are exempt from EO 12,866 review creates an obvious moral hazard.

Another opportunity for the IRS to avoid EO 12,866 review is when a rule does not meet the order's definition of a "significant regulatory action." The IRS almost always claims to be exempt because it claims that its rules do not meet this definition.[59] The IRS supports this position with two arguments. First, it claims that "the economic effect of a regulation under E.O. 12866 is not determined by the amount of taxes imposed or collected under the regulation. Federal taxes raise revenue to fund government operations and are not considered in determining economic effect."[60] One problem with this argument is that many IRS rules and regulations have nothing to do with raising revenue to fund government operations. Two examples are rules governing the tax-exempt nonprofit sector and the swath of rules implementing tax credits and deductions. Any exemption from EO 12,866 review for those types of rules cannot be justified by a claim that the IRS is merely collecting funds for government operations. Second—and of the most relevance here—the IRS claims that its "regulations merely implement a statute" and thus merely "provide a mechanism" for the tax to be paid or the payment issued to

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55 Gov't Accountability Office, GAO-16-720, Regulatory Guidance Processes: Treasury and OMB Need to Reevaluate Long-Standing Exemptions of Tax Regulations and Guidance, at 28 (2016) [hereinafter GAO Report on IRS Regulatory Processes].

56 *Id.* at 26.

57 *See, e.g.*, *id.* at 22 ("Between 2013 and 2015, [GAO] found that nearly 90 percent of the proposed, temporary, and final regulations issued [by the IRS] during this period" were claimed to be exempt from APA notice-and-comment procedures.).

58 *See supra* note 25.

59 *See* I.R.M. § 32.1.2.3.4; *see also* Jennifer Nou, *Agency Self-Insulation Under Presidential Review,* 126 Harv. L. Rev. 1755, 1786-87 (2013) (discussing ways agencies avoid OIRA review, including by claiming rules are not significant).

60 I.R.M. § 32.1.5.5.7.5.3.4

the taxpayer.[61] The IRS argues, "the effect from a rule in most IRS/Treasury regulations is almost always a result of the underlying statute, rather than the regulation itself."[62] This argument appears to have originated in the above-discussed 1998 Notice regarding the RFA and then spread to the IRS procedures for OIRA review.

> *"Allowing the IRS to determine whether its own rules are exempt from Executive Order 12,866 review creates an obvious moral hazard.*

D. History of IRS Procedures for OIRA Review

In 1988, the IRS added a provision to the IRM calling on attorneys drafting new regulations to prepare a "4-point" memorandum for OMB to facilitate OIRA review of the rule.

page (39)–142
(10–7–88)

(39)300 Regulations and Legislation

should refer the matter to the Assistant Chief Counsel.

(5) The Technical reviewer is responsible for furnishing to the Assistant Chief Counsel and the Deputy Assistant Chief Counsel copies of any draft regulations or policy memorandum to be circulated outside of Technical for comment or approval so that the Assistant Chief Counsel and the Deputy Assistant Chief Counsel can follow the progress of the project and monitor the quality of the drafting.

(39)314 *(10–7–88)*
Procedures for Development of Regulations Projects

(39)314.1 *(10–7–88)*
Initial Work on the Project Before Drafting

(39)314.2 *(10–7–88)*
Preparation of Draft

(1) Drafting will not begin until the staff attorneys and their reviewers are satisfied that they have made sufficient progress in identifying and resolving issues to warrant preparation of a draft.

(2) Except as otherwise agreed, the Technical drafting attorney will be responsible for preparing the preliminary draft of regulations, any policy memorandum, and the 4-point memorandum for OMB.

(3) The Technical reviewer is responsible for ensuring that any other necessary documents (for example, Form SF–83 relating to reporting or recordkeeping requirements) are prepared at the earliest time practicable to permit orderly review of those documents.

Page IRS01783

61 *Id.*

62 *Id.*

In 1992, the IRM was expanded to include the IRS-OMB exemption agreed to in the 1983 IRS-Treasury memorandum. The new IRM provision also explained the "4-points" that the memo must include.

the drafting is seriously deficient should discuss the matter with the Domestic reviewer. If the commenter and the Domestic reviewer are unable to resolve the matter satisfactorily, they should refer the matter to the Assistant Chief Counsel.

(5) The Domestic reviewer is responsible for furnishing to the Assistant Chief Counsel and the Deputy Assistant Chief Counsel copies of any draft regulations or policy memorandum to be circulated outside of Domestic for comment or approval so that the Assistant Chief Counsel and the Deputy Assistant Chief Counsel can follow the progress of the project and monitor the quality of the drafting.

(39)314 *(10–7–88)*
Procedures for Development of Regulations Projects

(39)314.1 *(12–2–92)*
Initial Work on the Project Before Drafting

(1) The Domestic drafting attorney and the Treasury attorney working on a regulations project are responsible for keeping their reviewers and representatives of other offices (such as the offices of the Commissioner, the Chief Counsel, the Associate Chief Counsel (Domestic) and the Associate Chief Counsel (International), who express an interest in the project, informed of developments. These attorneys should inform the reviewers and representatives from other offices of the progress being made on the project and difficulties that have

randum and present the issue at a joint briefing (see (39)316 below).

(39)314.2 *(12–2–92)*
Preparation of Draft

(1) Drafting should not begin until the drafting attorneys and the Treasury attorneys, and their reviewers, are satisfied that they have made sufficient progress in identifying and resolving issues to warrant preparation of a draft.

(2) Except as otherwise agreed, the Domestic drafting attorney will be responsible for preparing the preliminary draft of regulations, any policy memorandum, and the 4-point memorandum for the Office of Management and Budget (OMB). Any regulations document that must be approved by the Assistant Secretary (Tax Policy) and is not a major legislative regulation must have a 4-point memorandum. The 4-point memorandum must also be approved by OMB. The 4-point memorandum must include the following points: (1) the identifying number and title of the project; (2) whether the document is a Treasury decision or a notice of proposed rule making; (3) what the document does, stated briefly; and (4) whether the regulations are major legislative regulations.

(3) The Domestic drafting attorney is responsible for ensuring that any other necessary documents (for example, Form SF–83 relating to reporting or recordkeeping requirements) are prepared at the earliest time practicable to permit orderly review of those documents.

Page IRS02013

In 1994, the IRM provision was again amended to reflect a newly expanded "7-point" memo to OMB.[63] This version of the provision incorporates a discussion of when a regulatory action is either "economically significant" or "significant" under EO 12,866.

531.2 *(8–1–94)* (30)(15)20

Executive Order 12866

The Order requires agencies to notify OMB of all planned regulatory actions. The 7-point memo is used by IRS to notify OMB. Only regulations that are characterized as economically significant or significant are subject to the analysis requirements of the Order. After reviewing a 7-point memo, OMB may recharacterize the regulations, thus subjecting them to analysis under the Order.

Under the Order, an **economically significant** regulatory action is any regulatory action that may—

- Have an annual effect on the economy of $100,000,000 or more; or
- Adversely effect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local, or tribal governments or communities.

Under the Order, a **significant** regulatory action is any regulation action may—

- Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;
- Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or
- Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles of the Order.

Pages IRS00050–51

63 The version of the IRM provision pictured was created in 1994, but was retransmitted in 2005 to reflect a recodification of the IRM.

The 1994 revision also included an exhibit providing further detailed instructions for completing the "7-point" memo and identifying economically significant rules.

Chief Counsel Regulations Handbook **page (30)(15)20–86**

(8–1–94)

Exhibit 4

7 Point Memorandum

Notice of Planned Regulatory Action
Pursuant To Executive Order 12866
DEPARTMENT OF THE TREASURY

Office/Bureau: Internal Revenue Service
Title:[1]
Significance:[2]
Upcoming Action:[3]
Planned Publication:[4]
RIN: 1545–
Statutory/Judicial Deadline:[5]
Description:[6]
Agency Contact:[7]

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1. Enter the project number and title.
2. Enter *one* of the following terms:

   "Economically Significant" if the regulation may (1) have an annual effect on the economy of $100 million or more; or (2) adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or state, local, or tribal governments or communities.

   "Significant" if the regulations may (1) create a serious inconsistency or otherwise interfere with an action taken or planned by another agency; (2) materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or (3) raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles of Executive Order 12866.

   "Not Significant" if the regulations are neither "Economically Significant" or "Significant."
3. Enter the stage of regulatory action (NPRM, Temporary and XREF, Final Regulations after NPRM, Final Regulations without prior NPRM).
4. For regulations that are "Not Significant," indicate the expected date of publication in the Federal Register, taking into account Treasury review time.

   For regulations that are "Economically Significant" or "Significant," indicate the expected date of submission to OMB for review under Executive Order 12866.
5. Enter date of any statutory or judicial deadline, or "Not Applicable."
6. Briefly describe in *plain language* (1) the provisions of the regulations (including significant changes from existing regulations) and why it is being issued; (2) associated issues, as appropriate (such as, benefits and costs, interagency and intergovernmental effects, budgetary effects, time pressures, and why the regulations are important, sensitive, controversial, or precedential; and (3) for final regulations with a prior NPRM, the nature and extent of changes made in response to the public comments.
7. Enter the name and telephone number of the person who can respond to detailed questions concerning the regulations.

Page IRS00069

Importantly, none of the IRM provisions created before the Office of Chief Counsel's 1998 memo on the RFA make any claim that the economic impact of IRS rules flows from the statute or that they are exempt from OIRA review on that basis. The first time that position makes an appearance in the IRM's OMB review provisions is 2004.

In an August 2004 revision, the IRS added a note to the IRM section on preparing the "7-point" memo, which claimed that "IRS/Treasury regulations are rarely significant regulatory actions because the effect of the rule is usually due to the underlying statute, rather than to the regulation." This note does not contain the same qualifying language found in Office of Chief Counsel's 1998 Notice. In that Notice, the claim was that the "any possible *revenue impact*" of a regulation is due to the statute. The claim now being asserted is that any "*effect* of the rule" is due to the statute. The IRS provides no explanation for this expanded claim and the shift in language is more than just semantic. The "revenue impact" of an IRS rule only accounts for money transferred from the private sector to the U.S. Treasury. The full range of "effects" of IRS rules should account for macroeconomic impacts, behavioral changes in response to the rule, compliance costs, and recordkeeping and reporting burdens.[64]

32.1.2.4
(08-11-2004)
OMB Notice of Planned Regulatory Action (7-Point Memo)

(1) Pursuant to E.O. 12866, OMB reviews all regulatory actions prior to publication. Regulatory actions are any substantive action normally published in the FR that are expected to lead to a final regulation (for example, ANPRMs and NPRMs). The Notice of Planned Regulatory Action (7-point memo) is the Service's notification to OMB of its intent to publish a regulation.

(2) The 7-point memo (that actually contains 8 points) provides the following information:

a. Title and CASE-MIS ID number of the regulation,
b. Whether the regulatory action is significant, as defined in E.O. 12866. State the significance of the regulation (i.e., economically significant; significant; not significant). A significant regulatory action is a regulatory action that is likely to result in a rule that may:

64 Other agencies that conduct RFA impact analyses consider these types of impacts. *See, e.g.*, U.S. Fish & Wildlife Serv., Dep't of Interior, Final Regulatory Flexibility Analysis for Listing Constrictor Snake Species as Injurious Under The Lacey Act (Jan. 2012) (considering impacts to economic output, decrease in employment, and imports), *available at* http://bit.ly/2AsRFiD; Office Of Standards, Regulations, and Variances, Mine Safety & Health Admin., Dep't of Labor, Final Regulatory Flexibility Analysis, Diesel Particulate Matter Exposure of Underground Coal Miners (Dec. 2000) (considering compliance costs, increased turnover of existing equipment, and employee training expenses), *available at* http://bit.ly/2nhBuzo; Food and Drug Admin., Dep't of Health & Human Servs., Final Regulatory Flexibility Analysis, Deeming Tobacco Products to be Subject to the Food, Drug, and Cosmetic Act (May 2016) (considering compliance costs, labeling costs, market adjustments, product registration costs, and administrative and recordkeeping costs), *available at* http://bit.ly/2AjMilz.

- Have an annual effect on the economy of $100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities,
- Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency,
- Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof, or
- Raise novel legal or policy issues arising out of legal mandates, the President's priorities, or the principles set forth in E.O. 12866. In the rare case that an IRS/Treasury regulatory action is determined to be significant, submit to OMB a cost-benefit analysis and a regulatory assessment. OMB has issued guidance on what is required for an effective cost-benefit analysis. See www.whitehouse.gov/omb/inforeg/riaguide.html .

Note: IRS/Treasury regulations are rarely significant regulatory actions because the effect of the rule is usually due to the underlying statute, rather than to the regulation.

Pages IRS00313–14

The note below the IRM provision does not change in a 2009 revision to the section. But in 2011 the note is moved into the text of subsection (2) without substantive change. The claimed exemption is currently listed at 32.1.2.4.3.2 without any change in the wording.

32.1.2.4 (09-23-2011)
OMB Notice of Planned Regulatory Action (7-Point Memo)

2. IRS/Treasury regulations are rarely significant regulatory actions because the effect of the rule is usually due to the underlying statute, rather than to the regulation. In the rare case that an IRS/Treasury regulatory action is determined to be significant, submit to OMB a cost-benefit analysis and a regulatory assessment. OMB has issued guidance on what is required for an effective cost-benefit analysis. See http://www.whitehouse.gov/omb/ and CCDM 32.1.5.4.7.5.3 for further discussion on E.O. 12866 and determining whether a regulation may be significant.

2017 IRM

32.1.5.4.7.5.3 (10-15-2015)
Executive Order 12866, as supplemented by Executive Order 13563

4. Most IRS/Treasury regulations are not significant regulatory actions for two key reasons. First, the economic effect of a regulation under E.O. 12866 is not determined by the amount of taxes imposed or collected under the regulation. Federal taxes raise revenue to fund government operations and are not considered in determining economic effect. Second, most IRS/Treasury regulations merely implement a statute. The underlying statute provides adequate legal authority to impose or collect a tax, or issue a payment to a taxpayer. IRS/Treasury regulations provide a mechanism for the tax to be satisfied or collected, or payment to be issued to the taxpayer. The effect from a rule in most IRS/Treasury regulations is almost always a result of the underlying statute, rather than the regulation itself. If the regulation is not a significant regulatory action, the Special Analysis section should use the following language:

   > "Certain IRS regulations, including this one, are exempt from the requirements of Executive Order 12866, as supplemented and reaffirmed by Executive Order 13563. Therefore, a regulatory impact assessment is not required."

5. Notwithstanding paragraph (4), IRS/Treasury regulations that do not relate to the imposition of tax may have an economic effect that does not flow from the relevant statute. In these circumstances, the drafting team must determine whether the rule has an economic effect on the economy of $100 million or adversely affects the economy in a material way.

   Note:
   OMB currently interprets E.O. 12866 so that the $100 million annual effect threshold is met if the rule results in a $100 million effect on the economy in any particular year.

2017 IRM

GAO recommended that the Director of OMB and the Secretary of the Treasury (1) reexamine "the relevance of the long-standing agreement that exempts certain IRS regulations from executive order requirements and OIRA oversight; and if relevant, make publicly available any reaffirmation of the agreement and the reasons for it," and (2) "develop a process to ensure that OIRA has the information necessary to determine whether IRS rules are major under CRA and significant under E.O.12866."[65] Senate Finance Committee Chairman Orrin Hatch also has voiced concern that the IRS exemption from the "transparency and accountability requirements [of this series of executive orders] appear to have been thwarted for decades due to the Treasury Department's long-secret MOA with . . . OIRA."[66]

The exemption for IRS rules from OMB oversight has gone unexamined for too long. OMB review of agency rules ensures that the president is able to exercise his proper constitutional role to direct the Executive Branch. The exclusion of the IRS from that regime is troubling and should be reviewed.

III. Congressional Review Act

As discussed above, the IRS generally treats all rulemakings as exempt from significant rulemaking analysis under the RFA and regulatory executive orders. In addition, the IRS also treats rulemakings as exempt from major rule analysis under the Congressional Review Act ("CRA"). The IRS makes these determinations without providing any analysis as to why its rules are rarely major rules.

A. A Brief History of the Congressional Review Act

In 1996, Congress passed the CRA to reclaim some of its policymaking authority.[67] The CRA allows Congress to use a (lawful) legislative veto to overturn rules promulgated by executive and independent agencies.[68] In general, before any covered rule can go into effect, an agency must submit a report to each House of Congress and the Comptroller General of GAO.[69] The CRA contains an intentionally broad definition of "rule" and covers more rules than either the RFA or EO 12,866. Covered rules include "any agency statement of general . . . applicability designed to implement, interpret, or prescribe law or policy[.]"[70] In other words, the whole or part of any agency rule, regulation, guidance, procedure,

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65 GAO Report on IRS Regulatory Processes, *supra* note 55, at 35.

66 Letter from Sen. Orrin Hatch, to Hon. Jacob Lew, Sec., Dep't of the Treasury (Oct. 11, 2016), *available at* http://bit.ly/2BpLAkx.

67 142 Cong. Rec. S3,684 (daily ed. April 18, 1996) [hereinafter CRA History] (statements of Senators Nickles, Reid, and Stevens).

68 *See generally* 5 U.S.C. §§ 801–08.

69 *Id.* § 801(a).

70 CRA History at S3,687 ("[T]he APA's broad definition of 'rule' was adopted by the authors of this legislation to discourage circumvention of the requirements of chapter 8."); *see* 5 U.S.C. § 804(3).

or interpretation of law is subject to disapproval under the CRA.[71] The CRA reporting requirement applies to major and non-major rules, and to economically significant and non-significant rules. The CRA defines the term "major rule" to include any rule that has or is likely to have:

> an annual effect on the economy of $100,000,000 or more; a major increase in costs or prices for consumers, individual industries, Federal, State, or local government agencies, or geographic regions; or significant adverse effects on competition, employment, investment, productivity, innovation, or on the ability of United States-based enterprises to compete with foreign-based enterprises in domestic and export markets.[72]

The CRA delays the effective date of major rules by an additional sixty days and requires the Comptroller General to issue a report to Congress within fifteen calendar days of the rule's submission.[73] The report must analyze the agency's compliance with certain other procedural statutes, including the RFA.[74]

B. Overview of IRS Instructions for CRA Compliance

The IRM instructs IRS rule writers how to comply with the CRA's requirements. The IRM explicitly states that IRS rules are subject to the CRA and will not take effect unless the CRA forms are accurately completed and submitted.[75] The CRA forms contain instructions for complying with Section 801 of the CRA by sending rule reports to each House of Congress and the Comptroller General. These instructions lay out exactly how to follow the report format mandated by the CRA, including indicating whether the rule is a major rule. The CRA form and attachments must be properly submitted for the regulation to be effective and it is the drafting attorney's responsibility to ensure they are submitted to the Publications and Regulations Branch for forwarding to the Senate, House of Representatives, and GAO.

However, the IRM discourages a finding that a regulation qualifies as a major rule under the CRA by echoing the language from other sections of the IRM. It instructs rule writers that "IRS rules are rarely major rules because the effect of most IRS rules is due to the underlying statute, rather than to the regulation" and that they should "[c]onsult the Chief, Regulations Unit, before responding that the document is a major rule."[76]

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71 CRA History at S3,687.

72 5 U.S.C. § 804(2).

73 *Id*. § 801(a)(2)(A).

74 *Id*. § 801(a)(1)(B).

75 I.R.M. § 32.1.6.10.2.1.

76 *Id*., Exhibit 32.1.6-6.

Exhibit 32.1.6-6 (08-11-2004)
Instructions for Completing Congressional Review Act Form

INSTRUCTIONS FOR COMPLETING CONGRESSIONAL REVIEW ACT FORM

Rev. 6-3-2003

IRS rules are rarely major rules because the effect of most IRS rules is due to the underlying statute, rather than to the regulation. Consult the Chief, Regulations Unit, before responding that the document is a major rule.

Page IRS00751

Given the strict IRS compliance procedures for the CRA, it follows that the IRS does not consider its regulations categorically exempt from the CRA's provisions or definitions. Yet it effectively ignores the CRA's major rule definition and its associated benefits for government accountability. This has the effect of shielding a key Article I power of Congress (*i.e.*, the power to tax) from view.

C. Problems with the IRS Claim that Its Rules Rarely Qualify as Major Rules Under the CRA

The IRS claim that its rules usually do not qualify as major rules under the CRA misapplies the CRA's provisions for three reasons. First, by categorizing its rules the way that it does, the IRS may be trying to avoid the sixty-day delay of the regulation's effective date that allows Congress time to review the regulation and introduce a disapproval resolution under Section 802. The IRS also avoids a GAO report that analyzes their compliance with other procedural statutes and that might find noncompliance, such as with the RFA.[77] The GAO report would also indicate whether the regulation is the least burdensome alternative. It would seem that the IRS is taking the position that its regulations are already the least burdensome alternative because it believes that they do not have an impact on the economy and only generate revenue for the government pursuant to the underlying statutes. However, many tax regulations generate enormous compliance costs for the public and do not relate to generating government revenue. Americans could greatly benefit from an analysis of less burdensome alternatives to IRS regulations.

The second problem, and perhaps the most striking, is the lack of IRS analysis regarding the major rule requirements of the CRA. The IRS does not address any of the three types of rules that qualify as major rules under the Section 804 definition. Instead, the agency appears to have created its rationale *ex nihlo*, as it provides no supporting sources or justification for the broad exemption from major rule analysis. It claims that just because a statute provides legal authority to issue

77 *See* 5 U.S.C. § 801(a)(2) (detailing report GAO prepares for Congress on major rules).

a regulation, that regulation does not have to conform to the economic analysis requirements. That position ignores the reality that agencies only derive their legal authority to promulgate any regulation from an authorizing statute. In other words, under IRS logic, all IRS regulations would be exempt from the whole CRA statutory scheme if those regulations are exempt from the major rule determination. Tax regulations certainly result in "a major increase in costs or prices for consumers, [or] individual industries[.]"[78] The IRS appears to equate the definition of economically significant rules from EO 12,866 with the definition of major rules from the CRA. To do so is a misapplication of the law and misunderstands the specific statutory framework crafted by Congress after EO 12,866 was issued. Taxes have an enormous economic effect, even purely revenue raising taxes, because they remove money from the economy, drive up consumer prices, and have significant compliance costs.

Finally, the CRA contains no exemption for rules that are "due to the underlying statute." In fact, the CRA only exempts rules of "particular applicability" or rules that do not "substantially affect the rights or obligations of non-agency parties."[79] The IRS makes the untenable claim that a rule that would otherwise qualify as a major rule loses that status just because its effects are "due to the underlying statute." And the IRS gives rule drafters *carte blanche* to certify rules as non-major rules without any analysis whatsoever. Assuming, *arguendo*, that the IRS is correct that most of its rules are not major rules, it should still provide some kind of analysis for each rule detailing why that rule does not qualify as a major rule. It is not enough for the IRS simply to assert that its rules are almost never major rules.

IV. Conclusion

Congressional and presidential oversight of agency decision-making is critical to ensure legitimacy and good governance. The IRS has systematically acted to undermine that oversight by claiming that the economic impact of its rules is solely attributable to the underlying statute and that its regulatory actions do not trigger the economic-impact analyses and information sharing that these oversight mechanisms demand. The IRS claim has been criticized by the GAO and the SBA but so far there has been no judicial review or public airing of the IRS position. This report serves to begin that discussion and hopefully increase the oversight of both IRS rules and the agency's attempt to evade oversight.

78 *Id.* § 804(2).

79 *See id.* § 804(3).

Exhibits

Exhibit 1: Office of Chief Counsel, Internal Revenue Service, Notice, Regulatory Flexibility Act, Mar. 3, 1998

Exhibit 2: Department of the Treasury and White House Office of Management and Budget, Memorandum of Agreement regarding Implementation of Executive Order 12,291, Apr. 29, 1983

Letters between General Counsel, Department of the Treasury and White House Office of Information and Regulatory Affairs, Nov. 4, & Dec. 22, 1993

Exhibit
1

Department of the Treasury | Internal Revenue Service | Office of Chief Counsel

Notice

N(30)(15)531-1

March 3, 1998

Subject: Regulatory Flexibility Act Cancellation Date: August 30, 1998

The following material replaces existing section 531 of the Regulations Handbook regarding background and procedures to be followed in ensuring compliance with the Regulatory Flexibility Act. The updated material incorporates changes to the Regulatory Flexibility Act made by the Small Business Regulatory Enforcement Fairness Act.

531.4 Regulatory Flexibility Act

531.41 Background and Discussion

1. The purpose of the Regulatory Flexibility Act (RFA) is to establish as a principle of regulatory issuance that agencies shall endeavor, consistent with the objectives of the rule and of applicable statutes, to fit regulatory and informational requirements to the scale of the businesses, organizations, and governmental jurisdictions subject to regulation. See Pub. L. 96-354, § 2(b). Consistent with this purpose, in drafting and formulating regulations, consideration should be given to alternative approaches that satisfy the statutory requirements while reducing burdens, if any, imposed on small entities.

2. Regulations to which the RFA applies. The RFA generally applies to two types of regulations issued by the Service:

   A. legislative regulations, i.e., regulations for which notice of proposed rulemaking is required to be published in the Federal Register pursuant to 5 U.S.C. 553(b); and

   B. interpretative regulations to the extent the regulations impose a collection of information on small entities.

Filing Instructions: Binder art (30)(15) Regulations Handbook
Master Sets: NO X RO X
NO: Circulate__ Distribute X to: All Personnel__ Attorneys X In: all divisions
RO: Circulate__ Distribute X to: All Personnel__ Attorneys X In: all divisions
Other National and Regional FOIA Reading Rooms
Electronic Filename: RegFlex.wpd Original signed copy in: CC:F&M:PF:PA

5 U.S.C. 601(2), 603. Because interpretative regulations are covered only "to the extent" of the collection of information, only the portion of the interpretative regulations that imposes a collection of information on small entities is subject to the RFA. See 5 U.S.C. 603(a). Prior to the Small Business Regulatory Enforcement Fairness Act (SBREFA), the RFA did not apply to interpretative regulations. The SBREFA amendments generally are effective June 27, 1996, but under a transition rule interpretative regulations that were proposed prior to March 29, 1996 and are finalized on or after June 27, 1996 are not required to contain a final regulatory flexibility analysis.

3. Collection of Information. "Collection of information" has the same definition in all meaningful respects under the RFA as under the Paperwork Reduction Act (PRA), and thus generally should be given the same meaning under both statutory provisions. Compare 5 U.S.C. 601(7) and 44 U.S.C. 3502(3). The definition of a "small entity" includes small businesses, small organizations, and small governmental jurisdictions. 5 U.S.C. 601(3)-(6). The term "small business" includes businesses that satisfy the Small Business Administration’s (SBA’s) size standards. See 15 U.S.C. 632; 13 C.F.R. Part 121. These size standards vary for different industries, but most businesses likely will be classified as "small" under the standards. (A 1994 report prepared by SBA estimated that, of the 21.5 million business tax returns filed in the U.S., only about 14,000 of the businesses were "large.") The businesses may be in the legal form of an individual proprietorship, partnership, limited liability company, corporation, joint venture, association, trust or cooperative. 13 C.F.R. 121.105.

4. Content and Preparation of Analysis. If regulations are subject to the RFA, a regulatory flexibility analysis must be prepared for the regulations both when the regulations are proposed and when they are issued as final regulations. 5 U.S.C. 603, 604. The analysis must be published in the Federal Register, and must include the information set forth in 5 U.S.C. 603(b) and (c) (for proposed regulations) or in 5 U.S.C. 604(a) (for final regulations). An example of the type of information required to be included in the analysis is a description and estimate, where feasible, of the number of small entities to which the regulations will apply. See 5 U.S.C. 603(b)(3).

5. Exception for cases in which IRS can certify. A regulatory flexibility analysis is not required if the head of the agency certifies that a regulation will not have a significant economic impact on a substantial number of small entities. 5 U.S.C. 605(b). Any such certification must be

published in the Federal Register, along with a statement providing the factual basis for the certification. Id.

A. Substantial Number of Small Entities. Although in 1996 the SBA estimated that there are 22 million small businesses, neither the statute nor the legislative history defines the term "substantial number" of small entities. Until issuance of guidance by OMB, whether a number of affected small entities is substantial will be based on all relevant facts and circumstances. The higher the number of affected small entities, the more likely that such number may be "substantial." In addition, regulations are more likely to be considered to affect a substantial number of small entities if the regulations are targeted at a specific industry and the regulations affect a high percentage of small entities in that industry.

B. Significant Economic Impact. The applicable statute and legislative history also do not define the term "significant economic impact." With respect to interpretative regulations, any possible revenue impact of the regulations is inherently part of the revenue impact of the underlying statute, and thus is not considered in measuring any economic impact attributable to the regulations. Also, because the RFA applies only to the portion of interpretative regulations that imposes a collection of information, the relevant economic impact of such regulations is only the economic impact of the collection of information. See 5 U.S.C. 603(a). The economic impact of a collection of information should be estimated in a manner consistent with similar estimates that are required for purposes of the PRA. The estimate generally should be determined on an annual basis and should be based on all relevant facts and circumstances, including the hours necessary to comply with the collection of information, the costs of purchasing equipment that is necessary to comply with the collection of information, etc. Cf. 44 U.S.C. 3502(2) (definition of "burden" for purposes of the PRA). Burden estimates under the PRA generally are stated in terms of a number of hours. One possible method of estimating the economic impact of a collection of information is to multiply the PRA estimate of burden hours times an hourly rate.

6. Judicial Review. Most agency actions pursuant to the RFA are subject to judicial review. See 5 U.S.C. 611. The RFA provides broad discretion to courts to fashion appropriate remedies (e.g., remanding the rule to the agency, deferring

enforcement of the rule, etc.) in the event of noncompliance with the requirements of the RFA. Id.

531.42 Procedures for Ensuring Compliance with the RFA

1. The principal author of regulations should assess whether the RFA applies to the regulations, and, if so, should take steps to ensure that the regulations fully comply with the RFA. The steps should include:

    A. The author should determine whether the regulations are one of the two types of regulations described above to which the RFA applies: legislative regulations, and interpretative regulations that impose a collection of information on small entities.

    B. If the RFA applies to the regulations, the author should prepare a regulatory flexibility analysis unless it is determined that the regulations will not have a significant economic impact on a substantial number of small entities (see (C) below). Statistical and other data concerning the number of affected small entities may be obtained through a number of resources, including the IRS Statistics of Income Division, the IRS Forms and Publications Division, the IRS Office of Small Business Affairs, tax practitioners, small businesses, Treasury's Office of Tax Analysis, revenue estimates and other legislative history of the underlying statute, and other resources available in the Chief Counsel library.

    C. If it is determined that the regulations will not have a significant economic impact on a substantial number of small entities, the factual basis for such determination should be documented. See (B) above for potential sources to consult in determining the number of affected small entities.

    D. The regulatory flexibility analysis or other language, as appropriate, should be inserted into the preamble of the regulations. See Appendix A for model language.

    E. The principal author should prepare a RFA Checklist as described below.

531.43 RFA Checklist

1. A RFA Checklist should be prepared for all regulations, regardless of whether the regulations are subject to the

RFA. The form to be used for the checklist is set forth as Appendix B.

2. The original Checklist should be placed in the regulations file. A copy of the Checklist should be attached to and circulated with the regulations signature package for review by all reviewers of the regulations. A copy of the Checklist (along with a copy of the regulations and the plain language summary) should be sent to the IRS Office of Small Business Affairs (Attn: Director, Small Business Affairs) on or prior to the date the signature package is circulated for review. Prior to sending the regulations to the Federal Register, the regulations unit will detach the Checklist and file it in a central file in the regulations unit that will contain the Checklist for all regulations. A copy of the Checklist also should be attached to the report that is sent to GAO pursuant to 5 U.S.C. 801.

/s/
STUART L. BROWN
CHIEF COUNSEL

Exhibit
2

MEMORANDUM OF AGREEMENT

TREASURY AND OMB IMPLEMENTATION OF
EXECUTIVE ORDER 12291

I. General

Treasury economists will be responsible for:

(a) Identifying economic issues in Treasury regulations.
(b) Preparing Regulatory Impact Analyses, when required.

II. Regulations

Internal Revenue Service
Bureau of Alcohol, Tobacco and Firearms
U.S. Customs Service

(a)(1) The review procedures of the Executive order are waived with respect to all regulations except legislative regulations that are "major" as defined in the Executive order.

(2) The procedures specified in section II(c) of this agreement do not apply to major legislative regulations, regulations defined in section 1(a)(1)-(3) or subject to section 8 of the Executive order, advance notices of proposed rulemaking, regulations which are not reviewed or subject to approval by an Assistant Secretary prior to issuance, regulations concerning the establishment or designation of geographical viticultural areas, and technical corrections to previously published regulations. OMB may exempt additional regulations or classes of regulations from these procedures.

(b) Treasury will be responsible for alerting OMB to:

(1) any major regulation for which Executive order review has been waived.

(2) any non-major regulation that reasonably could be expected to have a significant economic impact.

(c) Prior to publication of a regulation in the Federal Register, and at such times as Treasury may determine, Treasury will provide to the appropriate OMB desk officer three (3) copies of a statement that:

(1) Identifies the title of the regulation;

(2) Indicates the stage of rulemaking;

(3) Briefly describes what the regulation will require and identifies any significant policy changes proposed or resulting from the regulation; and

(4) Indicates the basis for determining that the regulation is not a major regulation or, in the case of an interpretative regulation, explains why the regulation is considered interpretative.

Treasury will not publish any regulation subject to this subsection until OMB review has been completed. OMB review will be deemed to be completed in 10 calendar days (or, if required with respect to a specific regulation, within such lesser time as may be agreed by OMB and Treasury) unless, prior to such time, OMB advises Treasury that either review has been completed or requests, pursuant to subsection II(d), to review the regulation under the terms of the Executive Order.

(d) OMB reserves the right to review the economic impact of any regulation under the terms of the Executive order. Requests for such review may be made orally, and shall be confirmed in writing by the Administrator or Deputy Administrator for Information and Regulatory Affairs. Any review under the terms of the Executive order will be deemed to be completed 10 calendar days from the date OMB received the materials required for review, unless prior to such time:

(1) OMB orally notifies Treasury that review has been completed; or

(2) OMB orally notifies Treasury that it is extending review pursuant to section 3(f) of the Executive order. Any such notice shall be confirmed in writing by the Administrator or Deputy Administrator for Information and Regulatory Affairs.

Treasury will not publish any such regulation until OMB review has been completed under the terms of the Executive order.

Bureau of Public Debt

The review procedures of the Executive order are waived with respect to all circulars and regulations issued by the Bureau of Public Debt which implement, through the exercise of the general borrowing power, the fiscal policies of the United States.

. Rulings

Internal Revenue Service
Bureau of Alcohol, Tobacco and Firearms
U.S. Customs Service

(a) The review procedures of the Executive order are waived with respect to revenue rulings, revenue procedures, Customs decisions, legal determinations, and other similar ruling documents.

(b) Treasury will be responsible for alerting OMB to any ruling document that reasonably could be expected to have a significant economic impact, particularly rulings in which there is a wide range of options with varying degrees of economic impact.

(c) In accordance with the procedures of section II(d), OMB reserves the right to review the economic impact of a particular ruling under the terms of the Executive order. Treasury will not publish any such ruling until OMB review has been completed under the terms of the Executive order.

IV. Effective Date

These procedures will become effective 30 days after the date of this agreement, and will continue for one year or until 90 days after either OMB or Treasury notifies the other that the agreement is terminated, which ever date is later. The Memorandum of Agreement between OMB and Treasury, dated April 28, 1982, shall continue in effect until the effective date of this agreement.

Peter J. Wallison
Peter J. Wallison
General Counsel
Department of the Treasury

Christopher DeMuth
Christopher DeMuth
Administrator for Information
and Regulatory Affairs

DATED: APR 29 1983

DEPARTMENT OF THE TREASURY
WASHINGTON

GENERAL COUNSEL

November 4, 1993

The Honorable Sally Katzen
Administrator, Office of Information
and Regulatory Affairs
Executive Office of the President
Office of Management and Budget
Washington, D.C. 20503

Dear Sally:

The purpose of this letter is to restate my understanding, based on our previous conversations and your October 12 guidance memorandum, that E.O. 12866 does not apply to regulatory actions of the Department of the Treasury that were not subject to review under the terms of E.O. 12291 or the Treasury-OMB memorandum of agreement (MOA) implementing that Order.

E.O. 12291 did not apply to agency regulations "issued with respect to a military or foreign affairs function of the United States." E.O. 12866 contains a parallel exemption, but specifically includes such regulations that involve the "import or export of non-defense articles and services." It is my understanding that this limitation on the exemption is not intended to apply to Treasury regulations that were not subject to E.O. 12291. Examples of such regulations include:

- Regulations issued by the Office of Foreign Assets Control (OFAC) that implement the President's foreign policy by blocking assets and imposing economic sanctions on foreign countries. Current sanctions programs include Haiti, Iraq, Vietnam, Cuba, Iran, Libya, and Yugoslavia (Serbia and Montenegro).
- Regulations issued by the Secretary of the Treasury in his capacity as Chairman of the Committee on Foreign Investment in the United States pursuant to the Defense Production Act of 1950 (as amended by the Omnibus Trade and Competitiveness Act of 1988), providing for the national security review of mergers, acquisitions and takeovers of U.S. firms by foreign entities.
- Regulations issued by the Assistant Secretary (Economic Policy) concerning the periodic reporting of portfolio capital positions and transactions pursuant to the International Investment and Trade in Services Survey Act and the Bretton Woods Agreements Act, and the reporting of foreign currency positions of large U.S. business enterprises and their foreign affiliates pursuant to section 5315 of title 31, United States Code.

- Customs regulations restricting the importation of particular articles. For example, Customs issues regulations to restrict the importation of articles based on determinations made by the U.S. Information Agency (USIA) under the authority of the Convention on Cultural Property Implementation Act. Recently, such regulations have restricted the importation of archaeological artifacts from Mali, El Salvador and Guatemala.

The MOA exempted from E.O. 12291 review (1) all rulings documents issued by the Internal Revenue Service (IRS), the Bureau of Alcohol, Tobacco and Firearms (BATF), and the U.S. Customs Service and (2) and specified regulations issued by those bureaus and the Bureau of the Public Debt (BPD). Appendix C of your October 12 guidance memorandum, which lists regulations that are not subject to E.O. 12866 review, includes the ruling documents but omits the regulations included in the MOA. We believe this was an oversight and it is my understanding that the following continue to be exempt from review under E.O. 12866 on the basis of the statement in your memorandum that previously granted exemptions remain in effect:

- BPD regulations that implement, through the exercise of the general borrowing power, the fiscal policies of the United States.

- BATF regulations concerning the establishment or designation of geographical viticultural areas.

- IRS, Customs and BATF regulations that are not subject to the approval of an Assistant Secretary prior to issuance. For example, Customs issues regulations pursuant to certifications made by the State Department that grant vessels or aircraft of a foreign country reciprocal treatment in the United States when the foreign country provides the same treatment to U.S. vessels or aircraft; the IRS issues regulations amending the Statement of Procedural Rules, 26 CFR Part 601.

- Advance notices of proposed rulemaking (ANPRMs) issued by IRS, Customs and BATF. In the past three years, BATF issued three ANPRMs and Customs issued one, none of which contained proposed regulatory text; the IRS did not issue any ANPRMs during this period.

We would be pleased to discuss any of the above referenced regulations with you or your staff.

Sincerely,

Jean E. Hanson
General Counsel

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

ADMINISTRATOR
OFFICE OF
INFORMATION AND
REGULATORY AFFAIRS

DEC 22 1993

Honorable Jean E. Hanson
General Counsel
Department of the Treasury
Room 300
Washington, D.C. 20220

Dear Jean:

This is in response to your letter of November 4, 1993, which discussed the application of Executive Order No. 12866 to Treasury regulations.

You are correct in stating our agreement that the new Executive Order does not apply to the substantive categories of regulatory actions of the Department of the Treasury that were not subject to review under Executive Order 12291 or the Treasury/OMB Memorandum of Agreement implementing that Order. Please note, however, that the new Executive Order does apply to advance notices of proposed rules (ANPRM's) unless an ANPRM falls within one of the substantive areas that we have agreed to exempt.

In the enclosed document, we have outlined the substantive areas of regulation that we are prepared to add to the "exempt list" attached to our October 12 guidance memorandum. All other rules should be included on the lists of rules under development that is to be submitted periodically to OMB so that we can determine which are "significant" and hence warrant centralized review. Simply stated, we are continuing the Treasury Department's current exemptions from regulatory review, except for ANPRM's. If the nature of Treasury's regulatory issues should change, we will consult with you to work out any necessary adjustments.

I want to take this occasion to thank you again for the professional and expeditious way your staff has handled regulatory issues. I look forward to working with you as we implement the new Executive Order.

Sincerely,

Sally

Sally Katzen

Enclosure

ENCLOSURE

Treasury Department Regulations Not Subject to Review Under E.O. 12866 as of November 1993

- o Regulations that implement a military and foreign affairs function of the United States, including:
  - Regulations issued by the Office of Foreign Assets Control (OFAC) that implement the President's foreign policy by blocking assets and imposing economic sanctions on foreign countries.
  - Regulations issued by the Secretary of the Treasury in his capacity as Chairman of the Committee on Foreign Investment in the United States pursuant of the Defense Production Act of 1950 (as amended by the Omnibus Trade and Competitiveness Act of 1988), providing for the national security review of mergers, acquisitions and takeovers of U.S. firms by foreign entities.
  - Regulations issued by the Assistant Secretary (Economic Policy) concerning the periodic reporting of portfolio capital positions and transactions pursuant to the International Investment and Trade in Services Survey Act and the Bretton Woods Agreements Act, and the reporting of foreign currency positions of large U.S. business enterprises and their foreign affiliates pursuant to Section 5315 of title 31, United States Code.
  - U. S. Customs Service (Customs) regulations restricting the importation of particular articles.
- o Bureau of Public Debt (BPD) regulations that implement, through the exercise of the general borrowing power, the fiscal policies of the United States.
- o Bureau of Alcohol, Tobacco and Firearms (BATF) regulations concerning the establishment or designation of geographical viticultural areas.
- o Internal Revenue Service (IRS), Customs and BATF regulations that are not subject to the approval of an Assistant Secretary prior to issuance.
- o Rulings documents issued by the IRS, BATF, and Customs.

Appendix

Hyperlinks to full index of documents received from IRS, hosted on Cause of Action Institute's website:

- 1983 Treasury–OMB Memorandum of Agreement and related letters
- IRS0001-200
- IRS0201-374
- IRS00375-848
- IRS00849-1070
- IRS01071-1198
- IRS01199-1420
- IRS01421-1590
- IRS01591-1751
- IRS01752-1881
- IRS01882-2010
- IRS02011-2032