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Commentaries on Professor Sneed's Lecture

Donald C. Lubick

U.S. Department of the Treasury

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IMPACT OF FEDERAL TAXATION

The *Hardenbergh* Case which Mr. Sneed has mentioned is a case differentiating between renunciation of legacies and renunciation of an intestate's succession. It is a case in which it seems to me that a court, the Tax Court originally, fell into a trap, into a difficulty which a sense of judicial responsibility should have avoided. It was faced, perhaps as I read between the lines of its opinion, with a decision of a Court of Appeals with which it disagreed, in the case of *Brown v. Routzahn*. Instead of facing that disagreement, it turned to this quite specious difference between vesting subject to divesting and not vesting at all. Now indeed it is almost inconceivable that any rational person could have felt that this had any function to perform with respect to the federal gift tax statute, whether the legatee or heir should or should not pay a gift tax. But the Tax Court adopted it; it was affirmed by a different Court of Appeals, and the tax differences are now such as to move the states to eliminate at best a meaningless differentiation. Whether this should move the states or whether it just differentiates the states seems to me not particularly significant. All I am saying is that with the difference turning on perhaps a bit of terminology, and not much more than that in state law, it is certainly something that a conscientious court might have turned away from.

When I say courts I should broaden the responsibility, because it is the responsibility of lawyers as well. I take it that it is the first responsibility of the lawyers in the Treasury and Department of Justice to administer the tax law wisely. Their responsibility for winning cases lies within the ambit of that first responsibility. They present such points to the federal courts, and in doing so they certainly seem to me to be departing from that wise overall policy of reconciling uniformity and diversity. I think both of these can be achieved. We may ultimately want to do away with the diversity. But while we have it, tax uniformity with diversity of law can be achieved. They do take restraint and some measure of thought. But I for one don't think that the achievement is likely to be inconsistent with the call to greatness which Professor Sneed has mentioned.

DONALD C. LUBICK*

Dean Hyman, the accident of alphabet makes it rather difficult for me to add anything to the comments which we have been fortunate to receive from three of the best and leading scholars in the tax legal field in the country. However, I perhaps can bring you a message that is even better, since yesterday my boss, the Secretary of the Treasury, emphasized that next year we will have both lower taxes and greatness, and the sooner we have them, the sooner I can get back to Buffalo. We have heard a good deal today about the distortions of state law by federal tax rules. You may not know that

* Tax Legislative Counsel, U.S. Department of the Treasury. A.B. 1945, University of Buffalo; LL.B. 1949, Harvard University Law School; Lecturer in Law (1950-1960) University of Buffalo School of Law.

in the expense account legislation which Dean Hyman has mentioned, we almost had a distortion of federal tax law caused by rules of state substantive law. At one stage the Senate Finance Committee voted to disallow all entertainment expenses except those which a prudent man might incur. After a raft of editorials and speculation, Congress thought better of that idea and retreated to the well established federal tax principles of "directly related" and "associated with," which of course are time honored and clear.

I think Professor Sneed has well illustrated the fact of which many of us practicing in the tax field have been aware that tax pressures do influence results both in litigation and legislation in the development of legal rules, and I think that even if our destiny for this century were not our commitment to leadership of the free world that this would be true anyway. I think taxes play such a significant role in our economy that they are bound to have this effect.

As Professor Blum has pointed out, taxes are not unique in their effect upon development of private substantive law. Changing social views and economic pressures of all kinds have always shaped the development of private law. Anyone, I think, can come up with a number of instances from the law of torts, contracts or property. The first year law student case of *MacPherson v. Buick* dealing with liability of manufacturers in tort, I think, is an illustration of the impact of changing ideas and changing factors on the development of private law. Often times familiar rules are distorted to reach a particular result. Without giving a good bit of thought to it, I recall my first year class in contracts from Professor Brown where we discussed the charitable pledge cases where doctrines of consideration were changed and yielded to pressures to reach a particular desirable result. So I agree largely with Professor Blum that it is neither undesirable nor unexpected that tax factors are going significantly to effect the development of our private law; and I also agree, I think with all of my colleagues here, that the state courts must follow precedents carefully, studying and applying prior decisions in their proper context, but after all this is basically the best technique of the common law process.

And of course where state substantive rights become significant for the first time, as in the illustrations of the marital deduction cases, and the cases involving the obligation of support, it is necessary for the courts to think through and weigh carefully what they are doing. Again this is a phenomenon which we can observe in many other areas. The influence of labor relations, I dare say, has had a lot to do with the development of the law of third party beneficiaries' rights to sue on collective bargaining agreements, and so forth.

Now I am most concerned, of course, at the present time with the legislative role in this process, and I agree that it is important to those engaged in the legislative process not to pivot a significant tax distinction on insignificant features of local law or those features which cannot simply bear the strain, such as making significant tax consequences turn on definition of an obligation

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to support. I do want to say that for those engaged in the legislative process at the federal level, it is, however, frequently difficult to see these issues clearly enough, early enough, and I think I ought to defend for Professor Brown the role of the draftsman in his legislative work. The professional draftsmen on the Congressional committee staffs are unsung heroes, I think, of the tax process. They are among the most capable, expert draftsmen that anyone could ask for to be preparing vital legislation. They operate, however, under very difficult conditions and pressures not only of time. Decisions are frequently made by the Congressional committees in rather vague terms. A decision is made that we ought to disallow entertainment expenses in certain categories, then it is up to the draftsmen to fill in all of the chinks that have been left open, to try, as faithfully as they can, to carry out the legislative intent. These men are dedicated, hard working and excellent craftsmen. I think it is important that you know that most of the ambiguous drafting that we undoubtedly have in the Internal Revenue Code is not the fault of the draftsmen.

I would like to say a little bit about the role of the federal tax law in our economy. I think I would agree wholeheartedly with Professor Brown that our object is uniformity. We want to allocate the tax burden as fairly as possible among all of our citizens. However, we must recognize that, as Professor Brown has said, the tax law can really never be neutral. And so I think it is also desirable that the tax system be used to induce particular desirable social or economic purposes where those purposes are tied to a broad popular consensus of what is a desirable social purpose and that it be so used in situations where the tax law can be used appropriately to deal with the problem and non-tax approaches are not as suitable.

Let me illustrate with a couple of examples. During the consideration of the Trade Expansion Act of 1962, the trade bill, there was a good deal of pressure in order to provide tax benefits for industries and firms that were injured by import competition, and one of the usual tax devices, if you will, that, it was suggested, would be desirable in this situation is the five-year write-off of the cost of equipment, or rapid depreciation. Now it seems to me that this is a situation where there is a desirable social purpose, trying to help import-injured industries and firms to re-adjust because of the governmental action of changing tariffs which had allowed them to achieve a certain degree of prosperity. However, it seems to me that this is a case where the appropriateness of using the tax system is limited. Proper aid to the import-injured industries calls for a discrimination which it is not possible to achieve through the tax system. For example, those businesses which were most hurt would be ones that would be showing losses, and therefore an extra depreciation deduction would not be of use to them. By granting them across the board, you might help some, but much of the deductions would have been granted where not needed. It was not possible to use the tax system in the discriminating way that would be called for in that situation.

On the other hand, perhaps the consensus is that the use of a deduction for contributions to charitable organizations is a useful way to use the tax system to influence decisions. It may be desirable to encourage private philanthropy and to avoid close governmental regulation in these areas, and therefore we may have a situation where the tax law quite properly can be used to induce the particular result. Now this in turn, this tax policy, has certainly encouraged the growth of charitable institutions, among them private foundations. Here is an area where the states ought to respond to a federally tax induced situation to regulate, but the states have abdicated their responsibility. There have been many cases of abuses of charitable foundations, and because the states have not exercised control, it may be necessary again for the federal government to step in through changes in the tax system or otherwise.

I would agree finally with Professor Sneed that the economic interests and pressures generated by the impact of taxation are such that we are always going to have a vying to induce certain results through changes in the tax law. I think I have a more optimistic view than he does. By and large I think that in the end it is all going to work out all right. We have seen a period of a tax structure with very high rates which has led to many inroads in the tax base which have produced and created a lot of these distortions about which Professor Sneed has been talking, but I think the atmosphere is such and the consciousness of people in our country today is such that the pendulum is swinging the other way; and I think that now counterpressures have been set in force which will induce a correction of some of these, the greatest of the distortions and an awareness of the possible effects of the tax law; and I think that not only in the administrative end of government but in the legislative end there is a new awareness of the problems requiring careful use of tax policy to induce or prevent a tax inspired response. I can say again for the Secretary that we are looking forward next year not only to a rate revision which will mean a reduction in personal and corporate income taxes from top to bottom but also a correction of some of the factors which have been productive of some of the distortion; and hence we may expect toward a greater uniformity of taxation than we have had in recent years, with more heed paid to the admonitions of Professor Sneed to weigh carefully the reaction which tax action will induce.