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Death is Still Certain, but are Taxes?: An Examination of the Due Process Limitations on Retroactive Tax Legislation After Carlton v. United States

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NOTES

DEATH IS STILL CERTAIN, BUT ARE TAXES?: AN EXAMINATION OF THE DUE PROCESS LIMITATIONS ON RETROACTIVE TAX LEGISLATION AFTER *CARLTON v. UNITED STATES*

Although retroactive civil statutes are not expressly prohibited by the Constitution,[1] the validity of such statutes has frequently

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[1] *See* U.S. CONST. art. I, § 9, cl. 3 ("No . . . ex post facto Law shall be passed."); U.S. CONST. art. I, § 10, cl. 1 ("No State shall . . . pass any . . . ex post facto Law."). In 1798, the Supreme Court first noted that the ex post facto clauses only prohibit retroactive laws of a criminal nature. *See* Calder v. Bull, 3 U.S. (3 Dall.) 386, 390, 397 (1798); RONALD D. ROTUNDA & JOHN E. NOWAK, TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE AND PROCEDURE § 15.9, at 470-71 (2d ed. 1992). Although the reach of the ex post facto clauses has not always been certain, the Supreme Court has confined their application to criminal statutes. *See* Harisiades v. Shaughnessy, 342 U.S. 580, 594-95 (1952) (distinguishing earlier cases interpreting ex post facto clauses broadly); Johannessen v. United States, 225 U.S. 227, 242 (1912). *See generally* LAURENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW §§ 10-2 to -3 (2d ed. 1988) (tracing history of ex post facto clauses from constitutional origins to modern judicial interpretation).

Judicial hostility towards retroactive laws can be traced to early Greek and Roman law. *See* Elmer E. Smead, *The Rule Against Retroactive Legislation: A Basic Principle of Jurisprudence*, 20 MINN. L. REV. 775, 775 (1936). This bias against retroactivity was adopted by the English common-law courts, and later by American courts, as a maxim of statutory construction. *Id.* at 780. "Perhaps the most fundamental reason why retroactive legislation is suspect stems from the principle that a person should be able to plan his conduct with reasonable certainty of the legal consequences." Charles B. Hochman, *The Supreme Court and the Constitutionality of Retroactive Legislation*, 73 HARV. L. REV. 692, 692 (1960). In addition, courts have traditionally opposed retroactive laws because they create instability and can be used either to benefit or to harm selected classes of citizens. *See id.* at 692-93; ROTUNDA & NOWAK, *supra*, § 15.9, at 470-71. Notwithstanding this long tradition of judicial aversion for retroactive legislation, laws having retrospective effect are regularly enacted, and upheld by the courts. *See, e.g.*, *infra* note 10 (demonstrating judicial acceptance of various retroactive taxing statutes); *see also* W. David Slawson, *Constitutional and Legislative Considerations in Retroactive Lawmaking*, 48 CAL. L. REV. 216, 221-25 (1960) (analyzing policies behind due process limitations on retroactive laws); Bryant Smith, *Retroactive*

been assessed under the Due Process Clause of the Fifth Amendment.[2] Operating within this broad framework, courts have developed seemingly nebulous standards.[3] In particular, the standard governing retroactively applied tax laws simply looks to whether the tax is "harsh and oppressive."[4] Not surprisingly, retroactive

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Laws and Vested Rights, 5 TEX. L. REV. 229 (1927) (examining grounds for distinction between valid and invalid retroactive legislation).

[2] *See* U.S. CONST. amend. V. The Due Process Clause of the Fifth Amendment provides that "[n]o person shall be . . . deprived of life, liberty, or property, without due process of law." *Id.* Commentators have suggested that the framers of the Constitution did not intend the Due Process Clause to apply to retroactive civil legislation. *See* ROTUNDA & NOWAK, *supra* note 1, § 15.9, at 457. Nevertheless, the Supreme Court has interpreted the Due Process Clause as a limitation on four major areas of retroactive civil legislation: (1) emergency retroactive legislation; (2) curative statutes; (3) retroactive taxing statutes; and (4) retroactive general legislation. *See id.* (identifying leading cases and standards applicable to each group of retroactive legislation).

The Supreme Court has interpreted other provisions of the Constitution as imposing restrictions, or even prohibitions, on retroactive civil laws. *See* Hochman, *supra* note 1, at 694. In particular, the Supreme Court has relied on the Contract Clause, *id.*, which provides that "[n]o State shall . . . pass any . . . Law impairing the Obligations of Contracts." U.S. CONST. art. I, § 10, cl. 1. The Contract Clause was included in the Constitution in order to prohibit the states' enactment of debtor relief laws. *See* ROTUNDA & NOWAK, *supra* note 1, § 15.8, at 437-38. However, the Marshall Court gave the clause an expansive reading and used it to protect property owners from state regulation. *Id.* at 438-39. The Contract Clause had, until the last fifteen years, remained dormant as a means of voiding retroactive legislation. *See* Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 244-51 (1978) (holding that retroactive statute affecting pension plan obligations violated Contract Clause); United States Trust Co. v. New Jersey, 431 U.S. 1, 14-32 (1977) (finding that Contract Clause prohibited retroactive repeal of statute limiting transportation subsidies); TRIBE, *supra* note 1, §§ 9-11. *But see* Hochman, *supra* note 1, at 694 n.15 (noting occasional use of Fifth Amendment Takings Clause to invalidate retroactive legislation). *See generally* Richard A. Epstein, *Toward a Revitalization of the Contract Clause*, 51 U. CHI. L. REV. 703 (1984) (emphasizing importance of Contract Clause as limitation on legislative power).

[3] *See* Bryant Smith, *Retroactive Laws and Vested Rights II*, 6 TEX. L. REV. 409, 409 (1928). Courts have historically contributed to the uncertainty in the retroactive law area by using nebulous language, such as "against natural right" and "a violation of fundamental principles." *Id.* One scholar has noted that this evasive language constitutes "but blinds to cover up the mental indisposition or inability to see the problem through," which are "expressions of vague feeling that the law is very bad without being able to say just why." *Id.*

[4] United States v. Hemme, 476 U.S. 558, 568-69 (1986) (quoting Welch v. Henry, 305 U.S. 134, 147 (1938)). With slight variation, virtually all circuit courts of appeals have adopted the "harsh and oppressive" standard. *See, e.g.*, Wiggins v. Commissioner, 904 F.2d 311, 314 (5th Cir. 1990); Temple Univ. v. United States, 769 F.2d 126, 135 (3d Cir. 1985), *cert. denied*, 476 U.S. 1182 (1986); Ward v. United States, 695 F.2d 1351, 1353 (10th Cir. 1982). *See generally* BORIS I. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 1.2.6, at 1-30 to -31 (2d ed. 1989) (discussing due process limitations on retroactive taxation). When analyzing the constitutionality of retroactive civil legislation outside the tax field, the Supreme Court determines whether the statute is "arbitrary and irrational." *See* Usery v. Turner Elkhorn Mining Co., 428 U.S. 1, 15 (1976). The "arbitrary and irrational" standard articulated in *Turner Elkhorn* does not differ from the "harsh and

tax legislation has been the subject of considerable litigation and debate.[5]

Courts have interpreted the harsh and oppressive standard flexibly,[6] relying on a variety of factors.[7] Although courts have not

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oppressive" standard applicable to tax legislation. *See* Pension Benefit Guar. Corp. v. R.A. Gray & Co., 467 U.S. 717, 733 (1984).

[5] *See, e.g., Hemme*, 476 U.S. at 568-69 (retroactive change to gift tax provision); United States v. Darusmont, 449 U.S. 292, 301 (1981) (per curiam) (retroactive amendments to minimum tax provisions); *Welch*, 305 U.S. at 146-51 (retroactive state tax provision); Untermyer v. Anderson, 276 U.S. 440, 445-46 (1928) (retroactive gift tax); Brushaber v. Union Pac. R.R., 240 U.S. 1, 8 (1916) (retroactive income tax); *see also* James S. Bryant, *Retroactive Taxation: A Constitutional Analysis of the Minimum Tax on IDCs*, 36 OKLA. L. REV. 107, 114-17 (1983) (arguing that retroactive minimum tax should be unconstitutional); Note, *Setting Effective Dates for Tax Legislation: A Rule of Prospectivity*, 84 HARV. L. REV. 436, 436-37 n.8 (1970) [hereinafter *Rule of Prospectivity*] (noting issues raised by retroactive taxation). *But see* Frederick A. Ballard, *Retroactive Federal Taxation*, 48 HARV. L. REV. 592, 592 (1935) (" 'Arbitrary retroactivity' may continue hopefully to rear its head in tax briefs, but for practical purposes, in this field, it is as dead as wager of law."); Slawson, *supra* note 1, at 232 n.85 (observing that Supreme Court's interpretation of estate tax implies retroactive rate change may be made without notice).

[6] *See, e.g., Hemme*, 476 U.S. at 567-69; Purvis v. United States, 501 F.2d 311, 313 (9th Cir. 1974), *cert. denied*, 420 U.S. 947 (1975); First Nat'l Bank v. United States, 420 F.2d 725, 730 (Ct. Cl.), *cert. denied*, 398 U.S. 950 (1970); *see also* JACOB MERTENS, JR., LAW OF FEDERAL INCOME TAX § 4.15, at 32-33 (1991) (listing factors used to interpret "harsh and oppressive" standard).

[7] *See, e.g., Temple Univ.*, 769 F.2d at 135 (asserting that length of retroactive period can be controlling factor). In *Welch*, the Supreme Court recognized Congress's ability to retroactively tax income derived in the year of statutory enactment, and in some instances, even income derived in the preceding year. 305 U.S. at 148-49; *see also Darusmont*, 449 U.S. at 297 (reaffirming *Welch*'s statement on length of retroactive period). The Supreme Court's ambiguity in *Welch*, with respect to taxation of pre-enactment years, has led some state courts to hold that revenue statutes applied to the year immediately preceding enactment are unconstitutional. *See, e.g.*, Commonwealth v. Budd Co., 108 A.2d 563 (Pa. 1954), *appeal dismissed*, 349 U.S. 935 (1955); Gulf & Western Corp. v. Commonwealth, 459 A.2d 1369 (Pa. Commw. Ct. 1983). The Federal Circuit has not "adopted an absolute temporal limitation on retroactivity." *See Temple Univ.*, 769 F.2d at 135. Curative legislation, enacted to reflect the intent of Congress, has been permitted to reach as far back as four years. *See* New England Baptist Hosp. v. United States, 807 F.2d 280, 284-85 (1st Cir. 1986). *But see* Wheeler v. Commissioner, 143 F.2d 162, 166 (9th Cir. 1944) (holding tax statute with two year retroactive effect unconstitutional), *rev'd on other grounds*, 324 U.S. 542 (1945).

Additionally, courts have considered the type and nature of the tax, scrutinizing "wholly new" taxes more strictly. *See, e.g.*, Estate of Ekins v. Commissioner, 797 F.2d 481, 484-85 (7th Cir. 1986); Fein v. United States, 730 F.2d 1211, 1213-14 (8th Cir.), *cert. denied*, 469 U.S. 858 (1984); Estate of Ceppi v. Commissioner, 698 F.2d 17, 21-22 (1st Cir.), *cert. denied*, 462 U.S. 1120 (1983); Westwick v. Commissioner, 636 F.2d 291, 292 (10th Cir. 1980); *see also infra* notes 19-33 and accompanying text (discussing estate and gift tax cases).

Traditionally, retroactive income tax legislation has been accorded greater legislative deference than retroactive estate and gift tax legislation. *See Darusmont*, 449 U.S. at 296-98 (observing that virtually all past income tax acts that were applied retroactively did not violate Fifth Amendment due process); *Welch*, 305 U.S. at 149 (noting that retroactive application of income tax laws has been unequivocally held constitutional); Cohan v. Commis-

adopted a uniform analysis,[8] one factor many courts consider is the foreseeability of the tax change.[9] Despite the sometimes inconsistent legal doctrine, the results have been consistent: most forms of retroactive taxation have been upheld.[10] Nevertheless, in *Carlton*

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sioner, 39 F.2d 540, 545 (2d Cir. 1930); (concluding that Congress has great freedom to retroactively enact income tax legislation); *see also* Ballard, *supra* note 5, at 597-601 (describing overwhelming trend by courts to affirm retroactive income tax legislation); Lawrence Zelenak, *Are Rifle Shot Transition Rules & Other Ad Hoc Legislation Constitutional?*, 44 TAX L. REV. 563, 608 (1989) (noting that Supreme Court has never sustained due process challenge to retroactive income tax provision). By contrast, the Supreme Court has been more willing to strike down the retroactive application of estate or gift taxes on due process grounds. *See, e.g., Untermyer*, 276 U.S. at 440; Blodgett v. Holden, 275 U.S. 142 (1927), *modified on other grounds*, 276 U.S. 594 (1928); Nichols v. Coolidge, 274 U.S. 531 (1927); *cf.* Coolidge v. Long, 282 U.S. 582 (1931) (holding retroactive state tax violative of Fourteenth Amendment due process).

Finally, some courts have identified whether the taxpayer had a vested right under the pre-amended tax law. *See, e.g.*, Canisius College v. United States, 799 F.2d 18, 25-26 (2d Cir. 1986), *cert. denied*, 481 U.S. 1014 (1987); *New England Baptist Hosp.*, 807 F.2d at 285.

[8] *See supra* note 7 (citing cases implementing different analyses of retroactive taxation).

[9] *See Hemme*, 476 U.S. at 569 (discussing relevance of notice to due process analysis of retroactive taxation); *Welch*, 305 U.S. at 147 (distinguishing cases in which taxpayer could not reasonably anticipate change in tax statute); Milliken v. United States, 283 U.S. 15, 21 (1931) (holding gift tax constitutional because taxpayer could reasonably foresee change); *Untermyer*, 276 U.S. at 445-46 (holding gift tax legislation unconstitutional since taxpayer could not reasonably foresee tax change); *Blodgett*, 275 U.S. at 147 (same); *Nichols*, 274 U.S. at 542 (holding retroactive estate tax unconstitutional due to taxpayer's lack of notice); *Canisius College*, 799 F.2d at 26 (finding retroactive employment tax foreseeable); *see also* Bryant, *supra* note 5, at 108-11 (discussing foreseeability rule). *But cf.* Pension Benefit Guar. Corp. v. R.A. Gray & Co., 467 U.S. 717, 731-32 (1983) (questioning relevance of notice in analyzing due process concerns regarding retroactive change to pension plan regulation).

Additionally, if the court finds that the taxpayer was unable to foresee the tax law change, then it must consider whether the taxpayer relied on the pre-amended tax statute. *See* Hochman, *supra* note 1, at 706-07; *see also Hemme*, 476 U.S. at 571 (holding retroactive estate tax constitutional because taxpayer had "no expectation" of existing tax laws); *Welch*, 305 U.S. at 147 (finding retroactive income tax inoffensive based on taxpayer's failure to voluntarily invoke tax laws); *Blodgett*, 275 U.S. at 147 (implying that taxpayer relied on tax laws as applicable before retroactive change in taxation); *Canisius College*, 799 F.2d at 26 (considering relevance of taxpayer reliance). *See generally* MERTENS, *supra* note 6, at 32-33 (noting requirement of reliance in conjunction with foreseeability).

[10] *See, e.g., Hemme*, 476 U.S. at 572 (estate and gift tax); *Darusmont*, 449 U.S. at 297 (minimum tax); Licari v. Commissioner, 946 F.2d 690, 695 (9th Cir. 1991) (increase in understatement penalty); Wiggins v. Commissioner, 904 F.2d 311, 316-17 (5th Cir. 1990) (minimum tax); *New England Baptist Hosp.*, 807 F.2d at 284-85 (employment tax); *Temple Univ.*, 796 F.2d at 134-36 (employment tax); Sidney v. Commissioner, 273 F.2d 928, 932 (2d Cir. 1960) (tax imposed on gains realized by collapsible corporations); *First Nat'l Bank*, 420 F.2d at 731-32 (interest equalization tax); Ferman v. United States, 790 F. Supp. 656, 662-63 (E.D. La. 1992) (estate tax), *aff'd*, No. 92-3482, 1993 WL 185667 (5th Cir. June 18, 1993). *See generally* David B. Sweet, Annotation, *Retroactive Application of Federal Legislation as Violating Due Process Clause of Federal Constitution's Fifth Amendment—Supreme Court Cases*, 107 L. Ed. 2d 1105, 1115-25 (1991) (summarizing relevant Supreme Court

v. United States,[11] the United States Court of Appeals for the Ninth Circuit recently upset this trend by striking down a federal estate tax amendment on due process grounds.[12]

In *Carlton*, the Ninth Circuit applied a novel two-factor test in interpreting the harsh and oppressive standard.[13] First, the court considered whether the taxpayer had prior actual or constructive notice of the tax change.[14] Second, the court focused on whether the taxpayer reasonably relied to his detriment on the pre-amended tax law.[15] The Ninth Circuit's emphasis on taxpayer notice and foreseeability as controlling due process considerations is perhaps the most striking aspect of its opinion.[16] More significantly, the Ninth Circuit's approach to the due process problem[17] gives rise to a conflict with the circuit courts that often treat taxpayer foreseeability as a presumption.[18]

It is submitted that despite an apparent irreverence for the majority rule, the Ninth Circuit has formulated a test that more accurately reflects Supreme Court authority than that of any other federal court. This Note will explore the relevant case history and policies that support this position. Part One provides an overview

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authority).

[11] 972 F.2d 1051 (9th Cir. 1992) *petition for cert. filed*, 61 U.S.L.W. 3854 (U.S. June 7, 1993) (No. 92-1941).

[12] *Id.* at 1059. *But see Ferman*, 790 F. Supp. at 662-63 (holding against taxpayer on facts similar to *Carlton*).

[13] *Carlton*, 972 F.2d at 1059.

[14] *Id.*

[15] *Id.*

[16] *Id.* at 1064 (Norris, J., dissenting). Judge Norris criticized the majority's finding that the taxpayer had no constructive notice since the precedents indicated that constructive notice is implied in situations in which the retroactive legislation merely effects a change in the tax rate. *Id.* Furthermore, the court's holding created a split among the circuits. *See infra* notes 65-94 and accompanying text (analyzing conflict among circuit courts).

[17] *Carlton*, 972 F.2d at 1055-59. The court first noted that the "harsh and oppressive" standard, articulated in *Welch v. Henry*, 305 U.S. 134, 147 (1938), was controlling. *Id.* at 1055; *see also supra* notes 6-7 and accompanying text (explaining "harsh and oppressive" standard). Next, the court summarized the holdings of the Supreme Court cases in which the Court found retroactive estate and gift taxes unconstitutional. *Carlton*, 972 F.2d at 1056-57; *see infra* notes 20-33 (discussing earlier estate and gift tax cases). Finally, the court considered the holdings and rationale of several recent Supreme Court cases. *Carlton*, 972 F.2d at 1058; *see* United States v. Hemme, 476 U.S 558 (1986) (holding retroactive estate tax provision constitutional); United States v. Darusmont, 449 U.S. 292 (1981) (holding retroactive minimum tax provision constitutional).

[18] *Carlton*, 972 F.2d at 1057. The majority noted that "it cannot be gainsaid that the modern trend has been against successful challenges to retroactive applications of the tax statutes." *Id.* In dissent, Judge Norris argued that the majority, in holding the tax statute unconstitutional, "create[d] a split among the circuits." *Id.* at 1064 (Norris, J., dissenting).

of relevant Supreme Court authority. Part Two explains how circuit courts of appeals, other than the Ninth Circuit, have interpreted the Supreme Court cases. Part Three contrasts the *Carlton* analysis with that of other circuit courts and asserts that *Carlton* represents a superior interpretation of Supreme Court doctrine. Finally, Part Four argues that the Ninth Circuit's analysis in *Carlton* incorporates important policy justifications which compel its adoption by other federal courts.

I. OVERVIEW OF SUPREME COURT AUTHORITY

A. *Estate and Gift Tax Cases*

By the early twentieth century, the Supreme Court had clearly established the constitutional validity of retroactive income tax legislation.[19] The issue again surfaced, with the enactment of a 1919 estate tax amendment, in the landmark case, *Nichols v. Coolidge*.[20] In *Nichols*, the Supreme Court for the first time struck down a retroactively applied federal tax provision as violative of the Due Process Clause of the Fifth Amendment.[21] Unfortunately, the reasoning for the decision was not clearly articulated.[22]

The following term the Supreme Court heard two challenges

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[19] *See* Cooper v. United States, 280 U.S. 409 (1930); Brushaber v. Union Pac. R.R., 240 U.S. 1 (1916); Billings v. United States, 232 U.S. 261 (1914); United States v. Heinszen, 206 U.S. 370 (1907); Stockdale v. Atlantic Ins. Co., 87 U.S. (20 Wall.) 323 (1873). *See generally* Alan S. Novick & Ralph I. Petersberger, *Retroactivity in Federal Taxation*, 1959 TAXES 407, 413-15 [hereinafter Novick & Petersberger, *Retroactivity I*] (synthesizing early Supreme Court cases involving retroactive income tax legislation).

[20] 274 U.S. 531 (1927).

[21] *Id.* at 532. In *Nichols*, the decedent and her spouse organized a trust to hold real estate for the benefit of their children. *Id.* at 533. The trust, which was created in 1907, provided that its income was to go to the settlors until their death, at which time the remainder would pass to their children. *Id.* The settlors transferred all their rights in the trust, including the income stream, to their children in 1917. *Id.* In 1919, a revenue act was passed which required that the inter vivos transfer of 1917 be included in the estate of the decedent, who died in 1921. *Id.*

[22] *See id.* at 542-43. Referring to the estate tax's retroactive application, Justice McReynolds reasoned:

> [S]o far as it requires that there shall be included in the gross estate the value of property transferred by a decedent prior to its passage merely because the conveyance was intended to take effect in possession or enjoyment at or after his death, [it] is arbitrary, capricious and amounts to confiscation.

Id.; *see also* Novick & Petersberger, *Retroactivity I*, *supra* note 19, at 426 (asserting that *Nichols* provides little guidance for future cases).

to the constitutionality of a newly-enacted gift tax provision.[23] In the first case, *Blodgett v. Holden*,[24] a plurality of the Court held the gift tax unconstitutional.[25] The Court refused to apply the tax to an inter vivos transfer completed during the same calendar year but before the gift tax legislation was enacted or even considered by Congress.[26] The taxpayer's actions, the Court found, were taken "in entire good faith and without the slightest premonition of such consequence."[27] In the second case, *Untermyer v. Anderson*,[28] the Court also held application of the gift tax to a completed transfer unconstitutional,[29] adopting an analysis of taxpayer notice similar to that of *Blodgett*.[30] Uniquely, though, the taxpayer in *Untermyer* executed the gift when Congress was on the verge of approving the gift tax provision.[31] Despite this finding, the Court concluded that the taxpayer could not have foreseen the gift tax,[32] therefore rendering its retroactive effect unconstitutional.[33]

B. Modern Trend: Toward a General Rule of Constitutionality

The Supreme Court has since retreated from these early estate and gift tax decisions,[34] often by distinguishing them factually.[35]

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[23] *See* Untermyer v. Anderson, 276 U.S. 440 (1928); Blodgett v. Holden, 275 U.S. 142 (1927), *modified on other grounds*, 276 U.S. 594 (1928).

[24] 275 U.S. at 142.

[25] *Id.* at 147.

[26] *Id.* at 146-47. The taxpayer in *Blodgett* had executed several inter vivos gifts in January 1924. *Id.* at 146. In February 1924, a tax on inter vivos gifts was proposed in Congress; the measure subsequently passed on June 2, 1924. *Id.* As enacted, the gift tax applied to all transfers effected during the calendar year 1924. *Id.*

[27] *Id.* at 147. Only eight justices participated in the decision; four of the eight based their decision on the grounds that the taxpayer lacked adequate notice. *See id.* The other four justices argued that Congress had never intended the tax provision to apply to gifts executed before the statute's enactment. *Id.* at 148-49. Despite the split, all eight Justices ruled in favor of the taxpayer so the tax was struck down. *See* Blodgett v. Holden, 276 U.S. 594 (1928).

[28] 276 U.S. 440 (1928).

[29] *Id.* at 445-46. In *Untermyer*, the petitioner's estate sought to recover taxes paid arising from a gift that was made prior to the retroactive enactment of a new gift tax. *Id.* at 444.

[30] *Compare Blodgett*, 275 U.S. at 147 *with Untermyer*, 276 U.S. at 444-45.

[31] *Untermyer*, 276 U.S. at 445-46.

[32] *Id.* The court observed that "[t]he taxpayer . . . ought not to be required to guess the outcome of pending measures. The future of every bill while before Congress is necessarily uncertain." *Id.*

[33] *Id.*

[34] *See infra* notes 36-45 and accompanying text. In addition to *Nichols*, *Blodgett*, and *Untermyer*, the Supreme Court decided a fourth case, Coolidge v. Long, 282 U.S. 582 (1931), in which a retroactive tax statute was also held unconstitutional. *Id.* at 605-06. In *Long*, the specific issue presented involved the same trust as in *Nichols*. *See id.* at 596.

Indeed, only three years after *Untermyer* was decided, the Court in *Milliken v. United States*[36] refused to find that a retroactive change to an estate tax rate was violative of due process.[37] Unlike *Untermyer*, the *Milliken* Court found that the taxpayer was adequately forewarned of the change in tax rate.[38] More recently, the Supreme Court, in *United States v. Darusmont*,[39] noted that the authority of the earlier estate and gift tax cases was not "controlling" in the context of retroactive income tax legislation.[40] In its latest opinion involving retroactive taxation, *United States v.*

However, the Court was requested to decide whether a retroactive *state inheritance* tax violated the Due Process Clause of the Fourteenth Amendment. *Id.* at 593. The Court found the tax unconstitutional because the interests of the remaindermen were fully vested and indefeasible prior to the enactment of the state tax. *Id.* at 596, 599, 605. Although *Long* often is considered part of the same line of cases involving unconstitutional estate and gift taxes, some commentators distinguish it because it concerned taxation of the beneficiary rather than the taxation of the decedent or donor. *See* Novick & Petersberger, *Retroactivity I*, *supra* note 19, at 428-29.

[35] *See* Hemme v. Unites States, 476 U.S. 558, 567-68 (1986) (distinguishing *Untermyer*); Welch v. Henry, 305 U.S. 134, 147 (1938) (distinguishing earlier estate and gift tax cases); Milliken v. United States, 283 U.S. 15, 21 (1931) (finding earlier estate and gift tax cases not controlling); Tyler v. United States, 281 U.S. 497, 501 (1930) (same).

[36] 283 U.S. 15 (1931).

[37] *Id.* at 24-25. In *Milliken*, a decedent's estate sought to recover taxes it paid on inter vivos transfers considered to have been made by the decedent in contemplation of death. *Id.* at 18-19. The estate objected primarily to the taxes attributable to the increase in tax rate from the level applicable at the time of the actual transfers. *Id.* at 20. Rejecting the estate's due process argument, the Court reasoned that the increase in tax rate merely equalized the tax rates applicable to inter vivos transfers made in contemplation of death and transfers taking effect at death. *Id.* at 23-24.

[38] *Id.*

[39] 449 U.S. 292 (1981). The Court in *Darusmont* held that a retroactive minimum tax amendment was constitutional because the amendment merely increased the rate and decreased an allowable exemption applicable to an existing minimum tax provision. *Id.* at 299-300.

[40] *Id.* at 299. Over a decade after *Nichols*, *Blodgett*, and *Untermyer* were decided, the Supreme Court in Welch v. Henry, 305 U.S. 134, 146-47 (1938), held that these earlier estate and gift tax cases were distinguishable from retroactive income tax cases. *See Darusmont*, 449 U.S. at 299. This distinction was premised on the assumption that a taxpayer, while having little control over the receipt and hence the taxation of income, may forego making a gift or bequest based on tax considerations. *See Welch*, 305 U.S. at 146-48. *But see* Bryant, *supra* note 5, at 107-08 (criticizing courts that determine constitutionality of retroactive tax laws based on "labels"—income, estate, or gift); Hochman, *supra* note 1, at 707 n.76 (questioning distinction made in *Welch* between retroactive income and estate and gift taxation).

In *Darusmont*, the taxpayer proposed a test that included, *inter alia*, an inquiry into whether the taxpayer should have been on notice of the retroactive tax. *Darusmont*, 449 U.S. at 299. The Court failed to decide whether due process required inquiry into taxpayer notice, but went on to find that, even assuming notice was relevant, the taxpayer could not "claim surprise." *Id.*

Hemme,[41] the Court upheld the retroactive application of a transitional rule implementing the unified estate and gift tax credit system.[42] Although the Court observed that *Untermyer* was of "limited value" in cases that did not involve "wholly new" taxes,[43] it nevertheless undertook a detailed analysis of the nature and circumstances of the retroactive tax.[44] As evidenced by *Hemme*, the Court has limited, but not overruled, the authority of the early estate and gift tax cases.[45]

II. Other Circuit Courts' Analyses: Implied Foreseeability

In *Estate of Ceppi v. Commissioner*,[46] the First Circuit held that a federal tax amendment which disallowed an estate tax exemption could be retroactively applied without violating due process.[47] Citing *Milliken*,[48] the circuit court held that the Supreme Court had effectively limited *Untermyer*'s authority to cases in-

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[41] 476 U.S. 558 (1986).

[42] *Id.* at 567-72. The taxpayer in *Hemme* was the trustee of the estate of Charles W. Hirshi. *Id.* at 560. In 1976, Hirshi executed five inter vivos transfers to which he sought to apply certain gift tax exemptions. *Id.* At the time of the transfers, Congress was planning to restructure the gift and estate tax schemes by combining the exemptions available under each into a single unified tax credit. *Id.* at 560-61. The unified credit legislation subsequently enacted included a retroactive transitional rule to account for amounts exempted under the former estate and gift tax systems. *Id.* at 562. Hirschi's death in 1978 caused his estate to fall within the transitional rule. *Id.*

[43] *Id.* at 568.

[44] *See id.* at 567-72. The Court in *Hemme* acknowledged that an important consideration is "whether, without notice, a statute gives a different and more oppressive legal effect to conduct undertaken before enactment of the statute." *Id.* at 569. Upon comparison of the treatment that the taxpayer would have received under the pre-amended law and the actual treatment, the Court concluded that, in some respects, the taxpayer had actually received a benefit under the new law. *Id.* at 570-71.

[45] *See id.* at 567-68; Novick & Petersberger, *Retroactivity I*, *supra* note 19, at 430; *supra* note 35 (citing Supreme Court cases that have distinguished, but not overruled estate and gift tax cases).

[46] 698 F.2d 17 (1st Cir.), *cert. denied*, 462 U.S. 1120 (1983).

[47] *See id.* at 22. In *Ceppi*, the decedent made eight gifts of stock, valued at over $6,000 per gift, to eight different relatives on January 5, 1978. *Id.* at 18. Ten days after the gifts were made, the decedent passed away. *Id.* In preparing the estate tax return, which was filed in October 1978, the executor claimed an exclusion of $3,000 for each gift pursuant to I.R.C. § 2035(b)(2). *Id.* Later that year, § 2035(b)(2) was amended to expressly eliminate the exclusion and was retroactively applied to transactions made after January 1, 1977. *Id.* As a consequence, the IRS assessed a deficiency against the estate; in response, the executor filed a petition in Tax Court. *Id.* The Tax Court held for the IRS, and the executor appealed to the First Circuit. *Id.*

[48] *Milliken*, 283 U.S. at 15; *see also supra* notes 36-38 and accompanying text (discussing *Milliken*).

volving the enactment of wholly new taxes.[49] The *Ceppi* court placed emphasis on the similarity between the retroactive change in *Milliken*, which had increased the tax rate, and the disallowed tax exemption in *Ceppi*.[50]

Relying in part on *Ceppi*, the Eighth Circuit in *Fein v. United States*[51] found the same retroactive estate tax amendment constitutional.[52] However, the *Fein* court interpreted Supreme Court authority as requiring a two-pronged inquiry: (1) "whether the change in the tax law was reasonably foreseeable;"[53] and (2) "whether the change was only a change in tax rate or the imposition of a new tax."[54] The court further explained that the two ostensibly separate inquiries were actually linked "in that a change in the tax rate is considered by its very nature to be reasonably foreseeable."[55] Applying this test, the court concluded that the

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[49] *Ceppi*, 698 F.2d at 20-21. The court noted that the Supreme Court in *Milliken* had distinguished *Untermyer* on the ground that the taxpayer in *Untermyer* could not have reasonably foreseen the tax; whereas, the taxpayer in *Milliken* was " 'left in no uncertainty that the gift he was then making was subject to the provisions of the existing [tax] statute.' " *Id.* at 21 (quoting *Milliken*, 283 U.S. at 23). However, the court found the distinction unconvincing, stating that "*Untermyer* at best remains good law only for the proposition that a wholly new gift tax cannot be applied retroactively." *Id.*; *accord* Westwick v. Commissioner, 636 F.2d 291, 292 (10th Cir. 1980); Buttke v. Commissioner, 625 F.2d 202, 203 (8th Cir. 1980), *cert. denied*, 450 U.S. 982 (1981); Shanahan v. United States, 447 F.2d 1082, 1083 (10th Cir. 1971).

[50] *Ceppi*, 698 F.2d at 21. As additional support, the court cited United States v. Darusmont, 449 U.S. 292, 299 (1981). *Id.* The Court in *Darusmont* observed that taxpayer notice, even if constitutionally mandated, was satisfied because the tax amendment at issue had been a matter of public knowledge at the time the taxable transaction occurred. *Darusmont*, 449 U.S. at 299. Similarly in *Ceppi*, the court implied that a taxpayer could be deemed on notice of new tax legislation that was retroactively applied to the taxpayer's fully consummated act when Congress had been considering the legislation prior to the taxpayer's action. *Ceppi*, 698 F.2d at 22.

[51] 730 F.2d 1211 (8th Cir.), *cert. denied*, 469 U.S. 858 (1984).

[52] *Id.* at 1213-14. "In coming to this conclusion, we [are] greatly aided by Judge Bailey Brown's analysis in *Ceppi* . . . ." *Id.* at 1213. In *Fein*, the decedent, prior to his death on June 13, 1977, transferred a life insurance policy to his wife. *Id.* at 1212. At the time of the transfer, the policy was worth less than $3,000 and therefore qualified for exclusion from his gross estate under I.R.C. § 2035(b)(2). *Id.* Subsequently, the Revenue Act of 1978, Pub. Law No. 95-600, which retroactively disallowed the exclusion of life insurance policies, was enacted. *Id.* This disallowance caused the life insurance policy transferred by the decedent to be included in his gross estate. *Id.*

[53] *Id.* In support of its inquiry into foreseeability, the court cited numerous Supreme Court cases. *See id.* at 1212-13; *see also supra* note 9 (citing Supreme Court cases that note foreseeability is relevant to constitutional analysis of retroactive tax legislation).

[54] *Fein*, 730 F.2d at 1213.

[55] *Id.* The court relied exclusively on the authority of *Milliken* in making this assertion. *Id.*; *see* Milliken v. United States, 283 U.S. 15, 23-24 (1931).

consequences of the retroactive tax amendment were "closer in kind and in effect to a mere increase in the tax rate than to enactment of a wholly new tax."[56] Since the tax change at issue was impliedly foreseeable, and given that it could not be considered a "new tax," the court had no choice but to uphold the retroactive tax change.[57]

On facts substantially similar to *Fein*, the Seventh Circuit in *Estate of Ekins v. Commissioner*[58] upheld the retroactive inclusion of a life insurance policy in a decedent's gross estate.[59] In its rationale, the court adopted the two-pronged test articulated in *Fein* as well as the presumptive link between a change in tax rates and its deemed foreseeability.[60]

Other circuit courts have undertaken varying approaches to retroactive tax legislation.[61] Some federal circuit courts have considered whether the taxpayer had a vested right under the preexisting tax statute.[62] Other circuit courts have based their decisions only in part on taxpayer foreseeability.[63] Although *Carlton* does not necessarily conflict with this latter group of cases, it is asserted that *Carlton*'s identifiable, multifactor test is superior to

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[56] *Fein*, 730 F.2d at 1213.

[57] *Id.* As in *Ceppi*, the Eighth Circuit also considered the authority of *Untermyer* to be limited to cases involving the imposition of a wholly new tax. *Id.* at 1214.

[58] 797 F.2d 481 (7th Cir. 1986).

[59] *Id.* at 485. In *Ekins*, the court ruled on the same estate tax provision which had been challenged in *Ceppi* and *Fein*, I.R.C. § 2035 (b)(2). *Id.* at 482. The decedent similarly had transferred certain life insurance policies to other individuals shortly, one month, before his death. *Id.* As a result of the retroactive application of § 2035(b)(2), the life insurance policies, which had been excluded, were included in the decedent's gross estate. *Id.*

[60] *Id.* at 484.

[61] *See infra* notes 62-63 and accompanying text (describing approaches taken by other circuit courts).

[62] *See, e.g.*, Canisius College v. United States, 799 F.2d 18, 25-26 (2d Cir. 1986) (holding that retroactive employment tax did not abrogate vested right), *cert. denied*, 481 U.S. 1014 (1987); New England Baptist Hosp. v. United States, 807 F.2d 280, 285 (1st Cir. 1986) (same). *But cf.* Hochman, *supra* note 1, at 696 (contending that "vested rights" analysis of retroactivity is conclusory). *See generally* MERTENS, *supra* note 6, § 4.15 (discussing vested rights and retroactivity); Smith, *supra* note 3, at 409 (same).

[63] *See, e.g.*, Wiggins v. Commissioner, 904 F.2d 311, 315-17 (5th Cir. 1990) (analyzing taxpayer notice of retroactive tax change in minimum tax); Estate of Ceppi v. Commissioner, 698 F.2d 17, 21-22 (1st Cir.) (noting that taxpayer had constructive notice of retroactive estate tax provision), *cert. denied*, 462 U.S. 1120 (1983); *see also* Sidney v. Commissioner, 273 F.2d 928, 932 (2d Cir. 1960) (noting that taxpayer had notice of retroactive tax amendment); First Nat'l Bank v. United States, 420 F.2d 725, 729-30 (Ct. Cl.) (holding retroactive interest equalization tax constitutional where taxpayer notice extensive), *cert. denied*, 398 U.S. 950 (1970); Smith, *supra* note 3, at 418-19 (discussing retroactive legislation and foreseeability).

the ad hoc analyses employed by these other circuit courts of appeals.[64] Rather, the true conflict exists between the Ninth Circuit's analysis in *Carlton* and the method applied by the Seventh and Eighth Circuit Courts of Appeals.[65]

III. THE NINTH CIRCUIT'S ANALYSIS: A SUPERIOR INTERPRETATION OF SUPREME COURT AUTHORITY

It is submitted that the Seventh and Eighth Circuits have based their construction of the "harsh and oppressive" standard on either an overly-broad or incorrect interpretation of Supreme Court authority. In particular, the Seventh and Eighth Circuits, by linking foreseeability and tax rate changes, have created a test that effectively ignores the relevance of foreseeability in assessing the constitutionality of retroactive taxation.[66] The Ninth Circuit's analysis, in contrast, stresses foreseeability in accordance with the Supreme Court's consistent interest in that factor when faced with the retroactive application of an estate or gift tax.

In analyzing retroactive tax legislation, the Supreme Court has repeatedly examined whether the taxpayer could reasonably have foreseen the retroactive tax.[67] Although this consideration has clearly not served as a bright-line test,[68] the Court has placed par-

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[64] *See supra* notes 62-63 (citing circuit courts that have not adopted cohesive analysis).

[65] *See infra* notes 66-94 and accompanying text. The analyses of the First Circuit in *Ceppi*, the Seventh Circuit in *Ekins*, and the Eighth Circuit in *Fein* are similar in that each relied significantly on *Milliken*. *See supra* notes 46-60 and accompanying text. However, the First Circuit test does not incorporate a presumption between a change in tax rate and its deemed foreseeability. *See Ceppi*, 698 F.2d at 21-22. Since the First Circuit specifically considered taxpayer foreseeability rather than relying on a legal presumption, its decision in *Ceppi* is not in significant conflict with *Carlton*. *See id.*

[66] *See supra* notes 51-60 and accompanying text (analyzing Seventh and Eighth Circuits' reasoning).

[67] *See supra* notes 20-45 and accompanying text (discussing Supreme Court authority); *supra* note 9 (citing additional case law); *see also* Hochman, *supra* note 1, at 706. "The primary consideration which appears from an analysis of the cases involving retroactive taxation is the ability of the taxpayer, at the time of the transaction in dispute, reasonably to have foreseen that a tax would be imposed . . . ." *Id.*

The Supreme Court in *Darusmont* had cast some doubt on the continued validity of foreseeability analysis in retroactive tax cases. *See Darusmont*, 449 U.S. at 299. The Court refused to expressly adopt the taxpayer's formulation of the foreseeability requirement in terms of taxpayer notice, choosing only to assume, without deciding, its relevance. *Id.* In *Hemme*, however, the Court disregarded its earlier questioning of foreseeability, noting that an important consideration in retroactive tax analysis is whether the taxpayer was subjected to unfair treatment "without notice." *Hemme*, 476 U.S. at 569.

[68] See *Darusmont*, 449 U.S. at 299-300, in which the Supreme Court cited favorably two earlier decisions upholding retroactive income tax provisions even though taxpayer notice

ticular emphasis on it in the estate and gift tax areas.[69] An underlying reason for this emphasis is the discretionary nature of bequests or gifts, which are usually undertaken with full knowledge of, and reliance on, existing tax laws.[70] On the other hand, the taxation of income is less subject to taxpayer control—the taxpayer generally will not or cannot refuse the income.[71] Accordingly, foreseeability in the context of an income tax change may be of little real consequence,[72] but may be relevant when the change pertains to estate or gift taxation.[73]

In *Carlton*, the Ninth Circuit framed the analysis of foreseeability by specifically focusing on whether the taxpayer had actual or constructive notice of the retroactive tax.[74] The court concluded that the taxpayer had detrimentally relied on an estate tax statute at a time when there was no meaningful notice of any proposed change to the statute.[75] The use of notice as a determining factor is

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was not demonstrated. *See also* Welch v. Henry, 305 U.S. 134, 147-51 (1938) (upholding retroactive state income tax despite lack of taxpayer notice); Cooper v. United States, 280 U.S. 409, 412 (1930) (finding change in federal income tax provision constitutional).

[69] *See supra* notes 19-33 and accompanying text.

[70] *Welch*, 305 U.S. at 147-48.

[71] *See id.* The Supreme Court has observed that shareholders would not refuse to accept dividend payments even if they believed that the applicable tax on dividends was going to be increased. *Id.* at 148; *see also* Hochman, *supra* note 1, at 706-11 (discussing disparate justifications for upholding retroactive income tax provisions vis-a-vis estate and gift tax provisions).

[72] *See Welch*, 305 U.S. at 147-48.

[73] *See id.* at 147. The Court in *Welch* stated:

> In the cases in which this Court has held invalid the taxation of gifts made and completely vested before the enactment of the taxing statute, decision was rested on the ground that the nature or amount of the tax could not reasonably have been anticipated by the taxpayer at the time of the particular voluntary act which the statute later made the taxable event.

Id.

[74] *See Carlton*, 972 F.2d at 1059.

[75] *Id.* at 1059-62. The petitioner in *Carlton* was the executor of the estate of Willametta K. Day. *Id.* at 1053. Prior to filing Day's estate tax return on December 29, 1986, the petitioner discovered that the Tax Reform Act of 1986 (effective October 22, 1986) included an amendment to I.R.C. § 2057 which would allow the estate to deduct half of the proceeds received from the sale of securities to an Employee Stock Ownership Plan ("ESOP"). *Id.* at 1053-54. In order to take advantage of this provision, the petitioner arranged to purchase 1,500,000 shares of MCI stock for a total price of $11,206,000. *Id.* at 1054. Petitioner acquired the stock and two days later resold the stock to the MCI ESOP trustee at a loss of $631,000. *Id.* Petitioner filed the Day estate return, deducting half of the proceeds received from the sale of stock, or $5,287,500. *Id.* On February 26, 1987, Congress began discussions on a bill requiring a decedent to directly own any subsequently transferred stock on the date of death in order to take advantage of the deduction. *Id.* The provision was to become effective as of October 22, 1986. *Id.* at 1053-54. The bill's subsequent passage caused the

entirely consonant with the Supreme Court's rulings in *Blodgett* and *Untermyer*.[76] In both decisions, the Court found the absence of taxpayer notice highly significant.[77] Similarly, in *Milliken* the Court ruled that the retroactive application of an estate tax did not violate due process because, *inter alia*, the taxpayer had received notice of the forthcoming change.[78]

The Court's holdings in both *Darusmont* and *Hemme* can be distinguished from *Carlton*. In *Darusmont*, the Court found that the taxpayer had received "ample advance notice."[79] Moreover, reliance was not a controlling factor because the statute provided for an income tax.[80] Factually, *Hemme* can be distinguished because the challenged retroactive change was a transitional reduction of an already existing tax credit,[81] not a case in which the taxpayer specifically and detrimentally relied on a deduction that was subsequently eliminated. Further, the Court in *Hemme* found that the change was not "unreasonably harsh and oppressive" because the change, in its entirety, actually produced a tax benefit for the taxpayer.[82]

The Seventh and Eighth Circuits also ostensibly considered the impact of foreseeability in addressing retroactive taxation.[83] However, upon closer examination, it appears that the foreseeability analysis adopted by both circuit courts is conclusory.[84] As noted

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taxpayer to lose the ESOP stock deduction. *Id.* at 1055.

As a corollary to the taxpayer's actual reliance, the court also pointed out that such reliance was "reasonable" because congressional intent clearly supported the prior tax provision. *Id.* at 1060-61. The court rejected the Government's argument that taxpayer reliance on the statute was unreasonable because the pre-amended provision was " 'too good to be true.' " *Id.* at 1060.

[76] *See supra* notes 23-33 and accompanying text.

[77] *See supra* notes 23-33 and accompanying text. Justice McReynolds, writing for the *Untermyer* Court, asserted that "[t]he taxpayer may justly demand to know when and how he becomes liable for taxes—he cannot foresee and ought not to be required to guess the outcome of pending measures." Untermyer v. Anderson, 276 U.S. 440, 445-46 (1928).

[78] *See supra* notes 36-38 and accompanying text.

[79] United States v. Darusmont, 449 U.S. 292, 299 (1981).

[80] *Id.*

[81] *See supra* notes 41-42 and accompanying text.

[82] United States v. Hemme, 476 U.S. 558, 566-71 (1986). Justice Marshall stated: "Taking into account Congress' equation, then, we cannot but deduce that appellees are no worse off than they would have been without the enactment of the Act." *Id.* at 570.

[83] *See Ekins*, 797 F.2d at 484; *Fein*, 730 F.2d at 1212-13.

[84] *Compare Fein*, 730 F.2d at 1213 *with Ekins*, 797 F.2d at 484. Despite the *Fein* court's oblique discussion of whether the taxpayer had notice of, or relied on, the pre-amended tax law, the plain interpretation of the court's standard—the presumption that a change in tax rate or base is by its nature foreseeable—could theoretically be applied by

earlier, *Fein* and *Ekins* rely exclusively on *Milliken* for the assertion that any change in a tax rate or in tax base is "by its very nature . . . reasonably foreseeable."[85] However, in *Milliken* taxpayer notice was not presumed.[86] The Court actually found the taxpayer "well warned" of the retroactive change by the policies underlying prior taxing statutes.[87] Rather than address the factual distinctions of *Milliken*, the Seventh and Eighth Circuits chose to focus on certain language which, in isolation, suggests that a change in tax rate could be presumed foreseeable.[88]

Arguably, under the *Fein/Ekins* analysis virtually any type of retroactive change in taxation is but a change in "tax rate" and thus should be presumed foreseeable.[89] This type of aggressive analysis may be justified in the context of retroactive income tax legislation,[90] which does not necessarily involve taxpayer reliance

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future courts without any consideration or analysis of taxpayer notice or reliance. *See Fein*, 730 F.2d at 1212-13.

[85] *Fein*, 730 F.2d at 1213; *accord Ekins*, 797 F.2d at 484.

[86] *See Milliken*, 283 U.S. at 23-24. The Supreme Court in *Hemme* observed that the retroactive tax change in *Milliken* was constitutional because the taxpayer "should have known" of the possibility of the change. *Hemme*, 476 U.S. at 568; *see also supra* note 49 and accompanying text (interpreting *Milliken*).

[87] *Milliken*, 283 U.S. at 24.

[88] *See Fein*, 730 F.2d at 1213 (citing *Milliken*); *Ekins*, 797 F.2d at 484 (citing *Fein*). The relevant portion of the *Milliken* opinion provides:

> Not only was the decedent left in no uncertainty that the gift he was then making was subject to the provisions of the existing statute, but in view of its well understood purpose he should be regarded as taking his chances of any increase in the tax burden which might result from carrying out the established policy of taxation . . . .
>
> . . . A change in the rate applicable to transfers at death necessitates a corresponding change in the rate applicable to gifts made in contemplation of death . . . .

Milliken, 283 U.S. at 23-24.

[89] *See supra* note 10 (citing examples of retroactive taxation cases). Any retroactive change in taxation in response to which a taxpayer brings suit necessarily implies that the taxpayer was forced to pay more taxes (e.g., because deductions were lost, new types of income were taxed, etc.). *See id.* Because any of these changes in taxation will, technically, constitute a change in the effective tax rate, the general proposition that implies foreseeability for changes in tax rates is obviously too broad. *See Retroactivity of Tax Legislation*, 29 TAX LAW. 21, 22 (1975) (noting distinction between mere tax rate change and substantive rule change).

[90] *See supra* notes 67-73 and accompanying text (explaining that taxpayer foreseeability is not controlling in retroactive income tax cases); *see also* Ward v. United States, 695 F.2d 1351, 1353 (10th Cir. 1982) (distinguishing between liberal treatment traditionally accorded retroactive income tax legislation as opposed to gift tax legislation). In an oft-cited opinion, Judge Learned Hand noted the liberal treatment accorded retroactive changes in income tax rates:

> Nobody has a vested right in the rate of [income] taxation, which may be retroac-

or expectation.[91] However, with respect to retroactive estate and gift taxes, the Supreme Court has indicated that taxpayer notice is an essential consideration.[92] In *Carlton*, the Ninth Circuit effectively integrated this factor,[93] whereas the Seventh and Eighth Circuit Courts disregarded Supreme Court authority that requires consideration of taxpayer foreseeability.[94]

IV. POLICY JUSTIFYING ADOPTION OF *CARLTON*'S ANALYSIS

Although it has long been recognized by the Supreme Court that Congress has the discretion to enact retroactive tax legislation,[95] there are limitations to this authority.[96] In the late 1950's, two commentators observed that "should some Congress of the future be more prone to allow past, untaxed events to pay the way for present and future government expenses, we may expect the due process clause to again be used to tell the legislature it has transgressed its constitutional power."[97] Many modern tax scholars and practitioners believe that Congress has fulfilled this prophecy by repeatedly enacting retroactive tax statute amendments.[98]

> tively changed at the will of Congress at least for periods of less than twelve months; Congress has done so from the outset. . . . [O]ne may indeed complain that, could he have foreseen the increase, he would have kept the transaction unliquidated, but it will not avail him; he must be prepared for such possibilities [i.e., the retroactive increase in tax rates], the system being already in operation. His is a different case from that of one who, when he takes action, has no reason to suppose that any transactions of the sort will be taxed at all.

Cohan v. Commissioner, 39 F.2d 540, 545 (2d Cir. 1930). *See generally* Ballard, *supra* note 5, at 597-98, 602, 618-19 (noting that retroactive income tax laws have been historically immune to constitutional attack whereas estate and gift taxes have presented more complicated issues).

[91] *See supra* notes 71-72 and accompanying text. The Supreme Court has expressly stated that retroactive income tax legislation should not be subject to the same considerations as retroactive estate and gift taxation. *See Darusmont*, 449 U.S. at 299 (stating that prior decisions involving retroactive gift taxation were not "controlling authority" in area of retroactive income tax); Welch v. Henry, 305 U.S. 134, 147-48 (1938) (same).

[92] *See supra* notes 19-33 and accompanying text (estate and gift tax cases).

[93] *See supra* notes 13-18 and accompanying text (discussing *Carlton* opinion).

[94] *See supra* notes 51-60 and accompanying text (analyzing Seventh and Eighth Circuits' opinions).

[95] *See supra* note 10 and accompanying text.

[96] *See supra* notes 2-4 and accompanying text (stating that retroactive tax legislation is restrained by due process).

[97] *See* Novick & Petersberger, *Retroactivity I*, *supra* note 19, at 432.

[98] *See* Frank M. Burke, Jr., *The 1976 Retroactive Amendment of the Minimum Tax: An Exercise of the Taxing Power or a Taking of Property?*, 32 BAYLOR L. REV. 165, 173 (1980) (criticizing retroactive minimum tax provisions); John A. Corry, *Retroactive Penalties Raise Constitutional Issues*, 36 TAX NOTES 723, 723-27 (1987) (asserting that retroac-

These "technical corrections" often do not merely "fine tune" an existing tax statute, but actually change its plain meaning.[99] As a consequence, many taxpayers have had their tax planning objectives frustrated.[100]

While Congressional authority to retroactively amend taxing statutes without violating the Constitution is beyond dispute,[101] Congress must also recognize its obligation to balance certain policy factors in the retroactive tax equation.[102] On the side of the taxpayer, policy would dictate against retroactivity to the extent a taxpayer has reasonably relied on an existing law.[103] This notion of reliance holds special relevance to the tax area because of the "taxpayer's paramount desire for certainty in tax planning combined with the unique degree of specificity found in the tax laws."[104] A related policy consideration is whether the taxpayer may be considered on "notice" of an impending tax change.[105] In contrast to

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tively-imposed tax penalty is unconstitutional); Jerry A. Kasner, *The Amendment of Section 2057 was Unconstitutional*, TAX NOTES TODAY, Oct. 14, 1992, *available in* LEXIS, Fedtax Library, TNT File ("We have seen too many examples, through 'technical corrections' . . . of the plain meaning of a statute being overturned."); Letter from Philip J. Wiesner, Principal, Peat, Marwick, Mitchell & Co., to Rep. Dan Rostenkowski, Chairman of House Ways and Means Committee (Apr. 30, 1984), *available in* LEXIS, Fedtax Library, Txnote File (arguing that "technical corrections" unfairly changed substantive meaning of prior tax provision).

[99] *See* Kasner, *supra* note 98.

[100] *See, e.g.*, New England Baptist Hosp. v. United States, 807 F.2d 280, 281 (1st Cir. 1986) (retroactive employment tax); Westwick v. Commissioner, 636 F.2d 291, 292 (10th Cir. 1980) (minimum tax provision); *see also supra* note 9 (citing cases in which taxpayer who relied on statute had expectations disappointed by retroactive tax statute).

[101] *See* Pension Benefit Guar. Corp. v. R.A. Gray & Co., 467 U.S. 717, 729 (1984). The Supreme Court has confirmed that, in the context of economic regulation, "the strong deference accorded legislation in the field of national economic policy is no less applicable when that legislation is applied retroactively." *Id.*; *see also supra* note 10 (discussing extensive power of Congress to enact retroactive tax legislation).

[102] See Hochman, *supra* note 1, at 726-27; Alan S. Novick & Ralph I. Petersberger, *Retroactivity in Federal Taxation II*, 1959 TAXES 499, 500 [hereinafter Novick & Petersberger, *Retroactivity II*]; *Retroactivity of Tax Legislation*, *supra* note 89, at 23, 28; *Rule of Prospectivity*, *supra* note 5, at 438-42, for general discussions of the "interest balancing" that is required when Congress enacts retroactive tax legislation.

[103] *See* Novick & Petersberger, *Retroactivity II*, *supra* note 102, at 499-502 ("The factor of reliance is part of a general policy consideration in regard to retroactivity."); *Rule of Prospectivity*, *supra* note 5, at 439.

[104] *Rule of Prospectivity*, *supra* note 5, at 439.

[105] *See Rule of Prospectivity*, *supra* note 5, at 439. Notice and reliance are intertwined in that notice may "neutralize" the importance of taxpayer reliance. *See* Novick & Petersberger, *Retroactivity II*, *supra* note 102, at 500. A primary concern underlying these two policies is the taxpayer's ability to conduct his affairs with reasonable certainty and without the "crippling effect of tax uncertainty—the inability to act at all." *Retroactivity of Tax*

these essentially pro-taxpayer concerns is the government's desire to distribute the tax burden while promoting administrative efficiency.[106] The interpretation and balancing of these general policies is not a simple task.[107] However, Congress appears to have overemphasized the interests of government at the unjustified expense of taxpayers.[108] Therefore, it is submitted that the policies which seek to protect taxpayers' interests, such as reliance and notice, should be considered by the courts as constituents of the due process inquiry.

In *Carlton*, the Ninth Circuit has employed a two-pronged test that mirrors the above-considered policy factors and reflects pertinent Supreme Court doctrine.[109] Although terms such as "notice" and "reliance" may initially be imprecise,[110] the uncertainty surrounding their use should diminish once courts begin to consistently apply this unified framework of analysis.[111] Furthermore, courts should also consider applying the *Carlton* test beyond the

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Legislation, *supra* note 89, at 21; *accord* Hochman, *supra* note 1, at 692. *See generally* THE FEDERALIST No. 44, at 282-83 (James Madison) (Arlington House ed., 1967) (noting that one should be able to plan conduct with reasonable certainty of consequences).

[106] *See Rule of Prospectivity*, *supra* note 5, at 441; *cf.* Michael J. Graetz, *Legal Transitions: The Case of Retroactivity in Income Tax Revision*, 126 U. PA. L. REV. 47, 68-70 (1977) (discussing administrative burdens of using transition rules versus grandfather clauses in tax revision).

[107] *See Retroactivity of Tax Legislation*, *supra* note 89, at 22. The difficulty of balancing the interests that underlie retroactive tax legislation is manifest. *Id.* The application of these policies will often vary from one set of circumstances to another. *Id.*

[108] *See supra* notes 95-98 and accompanying text (asserting that Congress unfairly implements retroactive taxation).

[109] *See supra* notes 13-15, 74-78 and accompanying text (discussing *Carlton*'s analysis).

[110] *See* Novick & Petersberger, *Retroactivity II*, *supra* note 102, at 499-530, 562 (discussing thoroughly different interpretations and distinctions made in applying the policies "reliance" and "notice"); *Retroactivity of Tax Legislation*, *supra* note 89, at 22 (noting subtleties manifest in interpreting policy interest of "reliance"); *Rule of Prospectivity*, *supra* note 5, at 439-40 ("reliance" not subject to simple interpretation). The difficulties manifest in objectively defining the concept of notice can be seen in Purvis v. United States, 501 F.2d 311 (9th Cir. 1974), *cert. denied*, 420 U.S. 947 (1975), in which the majority and dissent split on the issue of whether a presidential speech provided sufficient notice to apprise the taxpayer of a retroactive tax. *Compare id.* at 314-15 (holding notice adequate) *with id.* at 316-17 (Wallace, J., dissenting) (declaring tax unconstitutional).

[111] *See* Novick & Petersberger, *Retroactivity II*, *supra* note 102, at 530 (concluding that formulation of general rules for evaluating retroactive tax legislation is possible); *Retroactivity of Tax Legislation*, *supra* note 89, at 23. Tax commentators have suggested that retroactive tax legislation can be mechanically broken down into two, time-reference categories: before the date of announced legislative change and after the date of announced legislative change. *Id.* Courts would disfavor legislation affecting activity in the "before announcement" category, but would support application of "after announcement" rules. *See id.* at 23-26.

estate tax realm to other types of retroactive taxes.[112] In sum, the *Carlton* test represents a superior articulation of due process and relevant policy considerations that should be adopted by other federal courts.

CONCLUSION

In *Carlton*, the Ninth Circuit took a unique approach to the due process concerns raised by retroactive tax legislation. The *Carlton* test focuses on whether the taxpayer had actual or constructive notice of the tax change. In contrast, the Seventh and Eighth Circuits have employed an analysis that finds retroactive tax changes presumptively foreseeable. By employing a test that makes taxpayer notice a dispositive factor, the Ninth Circuit created a concrete framework through which to analyze retroactive tax laws. To this end, however, the Ninth Circuit upset the overwhelming trend in favor of tax retroactivity.

It is suggested that the *Carlton* test not only represents a superior reflection of Supreme Court doctrine, but also incorporates certain policy considerations that call for overall fairness in the tax law making process. It is hoped that when other federal courts are asked to rule on the constitutionality of retroactive tax laws, they will overlook historical trends and choose to focus on the Supreme Court doctrine and policies embodied in the *Carlton* test. In sum, by taking a focused approach to the due process inquiry, the Ninth Circuit has given a clearer, more equitable meaning to an otherwise elusive construction of the Due Process Clause.

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[112] *See* Bryant, *supra* note 5, at 107-08; Hochman, *supra* note 1, at 707 n.76. Tax scholars have questioned the legitimacy and logic of the Supreme Court's distinction between retroactive income tax legislation and estate and gift tax legislation. *See* Bryant, *supra* note 5, at 107-08; Hochman, *supra* note 1, at 707 n.76. Therefore, it may be argued that the identical standards that apply to one type of tax could logically be applied to another.