The IRS Can't Use a Notice to Change Statutory Meaning in an Anti-Taxpayer Way: *Feigh v. Commissioner*

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Feigh v. Commissioner*, decided in May 2019, has interesting things to say about whether the Internal Revenue Service can take away otherwise available tax benefits by issuing a notice and whether any deference should be accorded statutory interpretation contained in a notice.*

Introduction

At first glance, *Feigh v. Commissioner*,[1] decided by the Tax Court in May, seems to deal with a pedestrian issue, the tax equivalent of jaywalking: the availability of the earned income tax credit (EITC) and the refundable portion of the child tax credit to parents who, pursuant to a state Medicaid waiver program, receive payments to compensate them for caring, in their own home, for their disabled adult children. That's obviously an important issue for taxpayers in those circumstances, but it's unlikely to directly affect many readers of the *Journal of Taxation of Investments*.

First glances can be deceiving, however (and jaywalking can be dangerous, for that matter). *Feigh* contains a fascinating discussion of whether, by issuing a notice (in this case one that was intended to be taxpayer-friendly, Notice 2014-7[2]), the Internal Revenue Service can limit a benefit that is made available to taxpayers under the Internal Revenue Code. (Judge Goeke's answer was No, at least in situations in which the statutory requirements for the benefit are clearly satisfied.) And the court also discussed the level of deference, if any, that should be accorded a statutory interpretation of the

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[1] 152 TC No. 15 (2019).

[2] 2014-4 IRB 445.

Service when that interpretation is in a notice, not a regulation or revenue ruling. (The answer: Not much, especially if the position doesn't reflect a long-time, well-considered position of the Service.)

Feigh and the Relevant Legal Structure

The Feighs care for their disabled adult children at home and, for 2015, Mrs. Feigh received a W-2 showing $7,353 in "wages, tips, and other compensation" attributable to Medicaid waiver payments for that care.[3] The Feighs didn't report the $7,353 as gross income, however, and with good reason—because of a 2014 notice issued by the Internal Revenue Service. But they also claimed credits that required they have "earned" income, and their only income that was arguably earned was that nontaxable $7,353. The ultimate issue in the case was whether the untaxed payments could constitute "earned income" for purposes of the credit provisions.

The Section 131 Exclusion. The potentially relevant exclusion from gross income in these circumstances should have been Code Section 131, but by its terms that exclusion didn't seem to be available to the Feighs. Section 131 provides that "[g]ross income shall not include amounts received by a foster care provider during the taxable year as qualified foster care payments."[4] A "qualified foster care payment" is generally "any payment made pursuant to a foster care program of a State or political subdivision thereof[,] which is paid by . . . a State or political subdivision thereof," and which is "paid to the foster care provider for caring for a qualified foster individual in the foster care provider's home, or . . . a difficulty of care payment."[5] A "qualified foster individual" is someone "who is living in a foster family home in which such individual was placed by . . . an agency of a State or political subdivision thereof, or . . . a qualified foster care placement agency."[6] Finally—this is several mouthfuls, isn't it?—"difficulty of care payments" are "payments to

[3] A Medicaid waiver payment is a payment received by an individual care provider as part of a state's Medicaid Home and Community-Based Services Waiver Program under Social Security Act Section 1915(c). See 42 U.S.C. § 1396n(c). Under that section, a state may obtain a waiver that allows the state to include in its Medicaid program the cost of most home or community-based services (including personal care services, habilitation services, and other services that are "cost effective and necessary to avoid institutionalization") provided to individuals who otherwise would require institutional care. See 42 CFR § 440.180. Medicaid waiver programs generally don't compensate a family member for providing personal care services to an eligible individual if the family member is legally responsible for the individual (for example, a minor child). See 42 CFR § 440.167(a)(2), (h).

[4] IRC § 131(a).

[5] IRC § 131(b)(1).

[6] IRC § 131(b)(2).

individuals which . . . are compensation for providing the additional care of a qualified foster individual which is . . . required by reason of a physical, mental, or emotional handicap of such individual with respect to which the State has determined that there is a need for additional compensation, and provided in the home of the foster care provider."[7]

The Service had historically, and generally successfully, challenged the excludability under Section 131 of payments such as those received by the Feighs.[8] Caring for one's own kids isn't "foster care" as that term is generally understood, and the kids don't seem to have been "placed" in their own home by any state agency. The Feighs' disabled adult children therefore didn't seem to be "qualified foster individuals." Nor had the Service in the past considered the nonstatutory exclusion for general welfare benefits to be applicable to such payments, and courts had agreed.[9]

Notice 2014-7 and Section 131. As a matter of first principle, however, it seemed harsh to distinguish between payments for exactly the same services—taxable to some, but not others, based on whether the beneficiaries are related to the services provider. Congress unquestionably could have amended Section 131 to cover situations like the Feighs',[10] but it hadn't done so. The Service then acted on its own. In Notice 2014-7, it announced that it would treat payments like those received by Mrs. Feigh as "difficulty of care payments" for purposes of Section 131,[11] thus excludable from gross income:

> To achieve consistent federal tax treatment of Medicaid waiver payments among the states and individual care providers, this notice provides that as of January 3, 2014, the Service will treat qualified Medicaid waiver

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[7] IRC § 131(c)(1)(A). The payments must also be designated by the payor as compensation for the relevant services. IRC § 131(c)(1)(B).

[8] See, e.g., Alexander v. Comm'r, TC Summ. Op. 2011-48 (holding that Medicaid waiver payments to taxpayers caring for one spouse's parents residing in the taxpayers' home weren't excludable under IRC § 131 because the taxpayers didn't show they operated a "foster family home" under state law and the parents weren't "placed" in the taxpayers' home by the state). Similarly, a 2010 Program Manager Technical Advice had concluded that a biological parent of a disabled child couldn't exclude payments under IRC § 131 because the ordinary meaning of foster care doesn't include care by a biological parent. See PMTA 2010-007 (Mar. 29, 2010), available at https://www.irs.gov/pub/lanoa/pmta_2010-07.pdf.

[9] See, e.g., Bannon v. Comm'r, 99 TC 59 (1992) (payments received by the taxpayer, under a state program for in-home supportive services, for caring for her adult disabled daughter, weren't protected from taxation by the general welfare exclusion); Harper v. Comm'r, TC Summ. Op. 2011-56 (following *Bannon*).

[10] As Judge Goeke noted, "Congress, of course, may exercise its prerogative to definitively provide that these payments are earned income but not subject to taxation as it did with combat service pay under [S]ection 32(c)(2)(B)(vi)." *Feigh*, slip op. at 16–17.

[11] See supra text accompanying note 7.

> payments as difficulty of care payments under [Section] 131(c) that are excludable under [Section] 131, and this treatment will apply whether the care provider is related or unrelated to the eligible individual.[12]

The Service also announced that, as of the same date, it would no longer assert the position it had previously taken in announcements and in litigation "to conclude that a caregiver of a biological relative receiving qualified Medicaid waiver payments may not qualify as a foster care provider under [Section] 131."[13] The Section 131 exclusion could be available when payments are received for care provided to "an eligible individual (whether related or unrelated) living in the individual care provider's home."[14] Furthermore, the notice concluded that the term "placed," not defined in the statute, can encompass approval by an appropriate state agency of the home and the payment rates for family arrangements like the Feighs'—as evidenced by a contract entered into with the "foster care providers."[15] That interpretation stretched the statutory language a lot, but obviously taxpayers aren't going to challenge a generous, albeit suspect, interpretation of a statute.[16]

Relying on the notice, the Feighs didn't include the $7,353 in gross income, and the Commissioner didn't object.[17] That brings us to the real issue in the case.

Availability of the EITC and Refundable Child Tax Credits in Light of Notice 2014-7. The dispute in *Feigh* arose because the Feighs, for 2015, claimed an earned income tax credit under Section 32 and the refundable portion of the child tax credit under Section 24. To be eligible for those credits, the Feighs had to have had "earned income," as defined in Section

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[12] Notice 2014-7, 2014-4 IRB at 446.

[13] Id.

[14] Id.

[15] The notice cited Micoresco v. Comm'r, TC Memo. 1998-398, in support of that conclusion. See Notice 2014-7, 2014-4 IRB at 446. But, as Judge Goeke noted in *Feigh*, the placement activity engaged in by the state agency in *Micoresco* was much more substantial—such as assisting in locating foster homes, providing transportation to look at the homes, and negotiating prices—than what occurred in *Feigh*: "[N]one of these things can reasonably be said to have been done in [*Feigh*], where the individuals receiving care remained in their own home." *Feigh*, slip op. at 10.

[16] Indeed, a taxpayer may not do so. A taxpayer obviously doesn't have standing to complain that he is being treated more favorably than the Code requires, and the rest of us don't have standing, as taxpayers, to complain in court that someone else is getting more tax breaks than he should. (We can complain, just not in a judicial proceeding.)

[17] See infra note 23.

32(c)(2)(A), for that year.[18] That section defines "earned income" generally as "wages, salaries, tips, and other compensation, *but only if such amounts are includible in gross income for the taxable year*."[19] As noted earlier, the $7,353 in Medicaid waiver payments constituted the Feighs' only arguably earned income for 2015. (The Feighs received no other W-2s and reported no other wages, tips, or similar compensation.) The Feighs treated the Medicaid waiver payments as earned income for these purposes, even though, because of the interpretation of Section 131 set out in Notice 2014-7, the payments were arguably not treated as includible in gross income. Not surprisingly, the Commissioner challenged that characterization, basically arguing that the category of "earned income" doesn't include amounts that are excluded from a taxpayer's gross income.

This, according to Judge Goeke, was a "novel question."[20] And, given the complex statutory language involved, the novel might well have been *The Sound and the Fury*.[21]

As noted, Section 131 provides an exclusion only if the otherwise qualifying earned income is "includible" in gross income.[22] Relying on Notice 2014-7, the Feighs hadn't included the $7,353 in their reported gross income. But if the notice misinterpreted the language of Section 131, the waiver payments were "includible" in their gross income—and should have been "included," even though—with good reason—they weren't.[23]

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[18] See IRC §§ 32(a)(1) (calculating EITC as percentage of taxpayer's "earned income," as defined in IRC § 32(c)(2)(A)); 24(d) (providing, when no tax liability is imposed, for refundable portion of child tax credit based on taxpayer's "earned income," as defined in IRC § 32(c)(2)(A)).

[19] IRC § 32(c)(2)(A)(i) (emphasis added). "Earned income" also includes self-employment income. See IRC § 32(c)(2)(A)(ii).

[20] *Feigh*, slip op. at 4.

[21] I hope before I die to get beyond page 40 of that novel. I've tried—unsuccessfully—several times.

[22] You write "includible," others write "includable," with the same ible-able difference applicable on the exclusion side. Nothing other than linguistic purity turns on the difference in spelling.

[23] In his opinion, Judge Goeke did suggest that, despite the position taken in the notice, the Commissioner could have challenged the applicability of IRC § 131 to the Feighs. *Feigh*, slip op. at 16–17. If IRC § 131 didn't apply (and he concluded that by its terms it didn't), the issue in the case would have gone away. The income would have been earned and taxable. But the judge refused to make the Commissioner's arguments for him. In any event, it would have been awkward for the Commissioner to have taken a position inconsistent with a published notice—even if the notice doesn't have the status of law. Indeed, the Commissioner argued that, because of the notice, the Feighs were *required* to exclude the payments from gross income; the notice did not, that is, provide for taxpayers to elect whether to exclude the income. See *Feigh*, slip op. at 16–17 & n.8.

Judge Goeke discussed the difference between the meanings of "included" and "includible" at some length:

> This Court has previously opined on the meaning of "includible" versus "included," and we have held that these words are not functionally the same.[24] While "included" refers to the actual treatment of income, "includible" refers to a required treatment of income, whether or not the income was actually so treated.[25] Thus, an item of income is "includible" in gross income if it is required to be included as income irrespective of whether the item was actually included in the taxpayer's gross income. Because [the Feighs'] Medicaid waiver payment is "includible" in their gross income but for Notice 2014-7, . . . the question for us becomes whether a notice can effectively usurp Congress' authority in granting tax credits by denying petitioners a credit they would have been entitled to in the absence of this notice."[26]

The answer was No. The notice had concluded that the "treatment of qualified Medicaid waiver payments as 'difficulty of care payments' is consistent with the definition under [Section] 131(c)."[27] However, wrote Judge Goeke, "these payments clearly do not meet the plain statutory definition found in the Code."[28] The payments therefore were held to be includible in gross income in 2015, and they therefore did constitute earned income for that year within the meaning of Section 32(c)(2)(A).

Presumably the Service wasn't thinking of the credit issue when it promulgated Notice 2014-7; the notice focused on the gross income results of the Medicaid waiver payments, not on any spillover consequences of the Section 131 analysis. But regardless of the Service's intent, the court concluded that the Service can't take away a tax benefit provided in the Code by issuing what the court (following terminology used by the Feighs in their court papers) referred to as a "subregulatory notice."[29] The Service can use a notice to advise the world that it won't challenge the treatment of positions

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[24] Citing Venture Funding, Ltd. v. Comm'r, 110 TC 236, 240-242 (1998), *aff'd without published opinion*, 198 F3d 248 (6th Cir. 1999); Tesco Driveaway Co. v. Comm'r, TC Memo. 2001-294, slip op. at 16 (noting that "includible" refers to "the date that the income should have been reported" while "included" means "the date that the recipient reported the income").

[25] Citing *Venture Funding Ltd.*, supra note 24, 110 TC at 240–41, 250 (Colvin, J., concurring) ("The 'ed' ending refers to something done in fact * * *. The 'ible' (or 'able') ending refers to something legally required[.]"); Eichenberger v. ESPN, Inc., 876 F3d 979, 984 (9th Cir. 2017) ("[T]he suffix 'able' means 'capable of.'").

[26] *Feigh*, slip op. at 11–12.

[27] Notice 2014-7, supra note 2, at 446.

[28] *Feigh*, slip op. at 8.

[29] Id. at 6; see also id. at 12 ("IRS notices—as mere statements of the Commissioner's position—lack the force of law.").

that are taxpayer-friendly—the Service can say, that is, that it won't enforce the rules as stringently as it would have the authority to do.[30] In that case, no one will be in a position to complain, at least not in a court of law. But, Judge Goeke concluded, "[t]he IRS cannot remove a statutory benefit provided by Congress"—at least not by issuance of a "subregulatory notice."[31]

Judge Goeke also noted that if Notice 2014-7 would have resulted in the characterization of the Medicaid waiver payments as something other than earned income, the Feighs would have been in a *worse* position than if the supposedly beneficial notice hadn't been issued. As he put it,

> We assume [the Commissioner's] motive for issuing Notice 2014-7 was well intended; but we note that, at least as applied to [the Feighs], it may actually cause more harm than good. Applying the notice as they did, to exclude their Medicaid waiver payment from gross income, but include it in calculating earned income, petitioners had no tax liability and received over $4,000 in refundable tax credits. Even in the absence of respondent's notice, petitioners would have no tax liability and over $2,500 in refundable tax credits. However, if petitioners had applied the notice as respondent argues they should have—to exclude their Medicaid waiver payment from gross income and from their earned income calculation—they would still have no tax liability, but would miss out on over $2,500 in refundable tax credits.[32]

That would have been a crazy result.[33] To be sure, Congress could have required such a counterintuitive result—congressional benefits can have unexpected, negative consequences—but the Service lacks the authority to impose such negative results on its own. In short, if there's incongruity in the statutory structure, it's something Congress, not the Internal Revenue Service, should address.

Deference Due Notice 2014-7 (and Notices Generally)

Even if the Service in Notice 2014-7 got the law wrong, as Judge Goeke concluded, shouldn't the Service's interpretation of the statutory structure still

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[30] For example, it might decide that it doesn't have the resources to police a particular area in a cost-effective way, and it will therefore not challenge particular return positions taken by taxpayers in that area.

[31] *Feigh*, slip op. at 14. Judge Goeke didn't rule on whether the Service could have achieved that result by regulation—going through the full notice and comment process: "Our holding addresses the power of the IRS, through a notice, to deem income otherwise includible as not includible for purposes of calculating a benefit bestowed by Congress. We do not reach the related issue of whether the IRS may properly classify income as not includible through a regulation." Id. at 14 n.6.

[32] Id., slip op. at 16 n.7.

[33] The law is sometimes crazy, of course, but craziness isn't a virtue.

carry substantial weight? After all, courts are inclined to defer to administrative agencies' interpretations of the statutes the agencies administer; doing so makes life easier for judges.

But there are limits to any required deference,[34] and notices are pretty low in the pecking order of authorities—"mere statements of the Commissioner's position," as Judge Goeke put it.[35] "Thus, they can only provide insight into the Commissioner's interpretation of the law; they cannot effect substantive changes in the law."[36]

Despite the low status of notices, Judge Goeke considered whether Notice 2014-7 was due some minimal deference under *Skidmore* standards.[37] Judicial deference has been given to revenue rulings, so long as they reflect "a 'body of experience and informed judgment' that the IRS has developed" over the years.[38] But even with revenue rulings, which are much higher in the hierarchy of authorities than are notices, "under *Skidmore*, the weight we afford them depends upon their persuasiveness and the consistency of the Commissioner's position over time."[39]

With the notice, Judge Goeke considered (quoting *Skidmore*) "the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking power to control."[40] Because he had already concluded that, in construing Section 131, the notice got it wrong, the case for deference was weak to begin with. If that weren't enough to doom the argument for deference, the fact that the notice overturned what had been the Service's longstanding administrative practice put the nail in the coffin.[41] It's impossible to say that a body of "informed judgment" has developed over the years or that the Commissioner's position has been consistent over time when a notice takes a brand new position. Judge Goeke therefore concluded that, "[i]n the light of these factors, we determine that the notice is entitled little, if any, deference."[42] In this context, "little, if any" seems to mean "none." Statutes don't always mean what administrative agencies say they mean.

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[34] And there are hints that, with the new members of the Supreme Court, the principles to determine when deference must be shown to administrative pronouncements, even regulations, may be changed—to lessen the power of administrative agencies.

[35] *Feigh*, slip op. at 12.

[36] Id.

[37] See Skidmore v. Swift & Co., 323 U.S. 134 (1944).

[38] *Feigh*, slip op. at 12 (citing Webber v. Comm'r, 144 TC 324, 358 (2015) (quoting *Skidmore*, 323 U.S. at 140)).

[39] Id. (quoting *Webber,* 144 TC at 352–53).

[40] Id. at 13 (quoting *Skidmore*, 323 U.S. at 140).

[41] See supra notes 8–9 and accompanying text.

[42] *Feigh*, slip op. at 13.

Conclusion

Feigh is an unusual case, to be sure, but its lessons are worth heeding: the Service's power to take away congressionally provided tax benefits is limited. A "subregulatory notice" cannot be used to overturn the plain language of a statute, if that plain language is beneficial to a taxpayer:[43] "[T]he IRS is not free to circumscribe the credits that the legislature has chosen to authorize through statute; that is a power only Congress has. Therefore, to the extent [the Commissioner] seeks to use Notice 2014-7 . . . to deprive petitioners of a benefit bestowed by Congress, we hold he may not do so."[44] And a court has no duty to give the Commissioner's statutory interpretation in a notice any deference, when the statutory language is relatively clear and when the interpretation hasn't been maintained over a significant period of time.

[43] Id. at 14. For that matter, a revenue ruling or even a regulation presumably couldn't do that either—at least when there are negative consequences for taxpayers.

[44] Id. at 15. The Commissioner had also argued that there was no "statutory provision demonstrating congressional intent to allow petitioners a double tax benefit. [He] suggests that if Congress intended to provide a double benefit here, it would have done so explicitly as it did in [S]ection 32(c)(2)(B) where it allowed taxpayers to treat as earned income combat service pay excluded from gross income under [S]ection 112." *Feigh*, slip op. at 15. Judge Goeke's short answer to that argument was that the double tax benefit arose because of the effects of Notice 2014-7. If the Service had gotten the IRC § 131 analysis right, the Medicaid waiver payments would have been taxable; the only tax benefit would have come from the credits. Judge Goeke wrote that the Commissioner, "however, has decided to disturb this equilibrium by telling taxpayers like petitioners that they need not pay tax on their Medicaid waiver payments." *Feigh*, slip op. at 15. The apparent incongruity was the Commissioner's fault, not Congress's.

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