# The Federal Tax Personality of Disregarded LLCs [*Littriello v. United States*, 484 F.3d 372 (6th Cir. 2007)]

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## I. INTRODUCTION

In 1977, the Wyoming Legislature created the limited liability company (LLC), a business entity structured with corporate characteristics and yet free from corporate taxation.[1] Since then, all fifty states have enacted LLC statutes, and business owners have organized over 1.2 million LLCs.[2] The nucleus of LLC statutes is a provision protecting the owners, members, and managers from personal liability for an LLC's debts and obligations.[3] This liability protection is possible because an LLC and its owner are separate legal entities.[4]

The Department of Treasury (Treasury) challenged the limited liability of certain LLCs when it promulgated the check-the-box regulations in 1996.[5] Pursuant to the regulations, the Treasury disregards some single-member LLCs as entities separate from their owner for federal tax purposes.[6] Although the regulations are silent on the issue, the Internal Revenue Service (IRS) maintains that a disregarded LLC is

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1. WYO. STAT. ANN. § 17-15-103(a) (1977); Susan Pace Hamill, *The Origins Behind the Limited Liability Company*, 59 OHIO ST. L.J. 1459, 1460 (1998).

2. Tim Wheeler & Nina Shumofsky, *Partnership Returns, 2004,* STAT. OF INCOME BULL. 104, 110 (Fall 2006), http://www.irs.gov/pub/irs-soi/04partnr.pdf. Approximately 310,000 limited liability companies (LLCs) are owned by single members as sole proprietorships. Kevin Pierce & Michael Parisi, *Sole Proprietorship Returns, 2004,* STAT. OF INCOME BULL. 7, 13 (Fall 2006), http://www.irs.gov/pub/irs-soi/04solp.pdf. It is unclear, however, whether these are included in the 1.2 million LLCs.

3. Thomas E. Rutledge & Lady E. Booth, *The Limited Liability Company Act: Understanding Kentucky's New Organizational Option*, 83 KY. L.J. 1, 6 (1995).

4. The Internal Revenue Service (IRS) recognizes LLCs as entities for federal tax purposes. *See* Treas. Reg. § 301.7701-2(a) (as amended in 2006).

5. *See* Simplification of Entity Classification Rules, 61 Fed. Reg. 66584, 66589 (Dec. 18, 1996) (codified at Treas. Reg. §§ 301.7701-1 to -3). The regulations are referred to as check-the-box because they allow certain business owners to elect how to have their companies taxed by checking the appropriate box on Form 8832. *Id.* at 66585.

6. Treas. Reg. §§ 301.7701-1(a)(4), -3(b)(1)(ii) (as amended in 2006).

not a "person" as defined by Congress.[7] This is significant because federal employment tax statutes provide that the "employer" of a company's employees, who is directly liable for paying a company's employment taxes, is a "person."[8] Consequently, the IRS maintains that an LLC disregarded for federal tax purposes cannot be the "employer" of its employees.[9] Therefore, the IRS views the owner of a disregarded LLC as the "employer" of the company's employees, and holds him personally liable for the company's federal employment taxes.[10]

In *Littriello v. United States*,[11] the United States Court of Appeals for the Sixth Circuit relied on the *Chevron* test[12] to uphold the validity of the check-the-box regulations.[13] The court also deferred to the IRS's conclusion that a disregarded entity cannot be the "employer" for employment tax purposes.[14] Accordingly, the court concluded that because the owner of a disregarded LLC is the "employer" of the company's employees, he is directly liable for the company's employment taxes.[15] This comment examines the Sixth Circuit's opinion and analyzes what amount of deference courts should extend to the IRS's position that a disregarded LLC cannot be the "employer" of the LLC's employees. The comment considers relevant Supreme Court opinions, analyzes the statutory definition and regulatory interpretation of the term "person," addresses the circuits' conflicting interpretations of this term, and discusses relevant authority regarding the role of state law.

## II. CASE DESCRIPTION

In September 2000, Frank A. Littriello organized a nursing home

7. *See* I.R.S. Notice 99-6, 1999-3 I.R.B. 12 ("In general, employment tax responsibilities rest with an employer. . . . Under these rules, the person for whom services are performed as an employee is generally considered the employer for purposes of the employment tax provisions. . . . [Section] 301.7701-2(c)(2) cause[s] the owner of a disregarded entity to be treated as the employer of the disregarded entity's employees for federal employment tax purposes. Thus, the owner generally is responsible for complying with all the employment tax obligations related to those employees."). Although the Treasury has never expressly stated that a disregarded entity is not a "person," it did so implicitly by stating that a disregarded entity cannot be the "employer" for employment tax purposes. *See* I.R.C. §§ 3121(b), 3306(a), 3401(d) (2000). If the IRS does not base its position on this assumption, then it is an arbitrary and capricious conclusion, because if an entity is a "person," it can be the "employer." *See* 5 U.S.C. § 706(2)(A) (2000). The default definition of "person" is codified at Code § 7701(a)(1) (2000).

8. I.R.C. §§ 3102(a), (b), 3111(a), 3121(b), 3301, 3306(a), 3401(d), 3402(a)(1), 3403 (2000).

9. I.R.S. Notice, *supra* note 7.

10. *Id.*

11. 484 F.3d 372 (6th Cir. 2007).

12. *See* Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984).

13. *Littriello*, 484 F.3d at 378. See *infra* notes 193-198 and accompanying text for a brief explanation of the *Chevron* test.

14. *Id.*; *see* discussion *supra* note 7.

15. *Littriello*, 484 F.3d at 378. The court concluded that the IRS could hold the owner of a single-member LLC, which did not elect to be classified as an association as permitted under the check-the-box regulations, personally liable for the LLC's unpaid employment taxes. *Id.* According to the check-the-box regulations, a single member company that does not elect to be classified as an association is disregarded as an entity separate from its owner for federal tax purposes. *See* Treas. Reg. § 301.7701-2(a) (as amended in 2006).

business, Kentuckiana Healthcare (Kentuckiana), as a single-member LLC.[16] Littriello did not elect to classify his company as an association for federal tax purposes.[17] Consequently, the IRS disregarded the existence of the LLC completely and treated Kentuckiana as a sole proprietorship for federal tax purposes.[18] After reclassifying his company as a sole proprietorship, the IRS held Littriello personally liable for Kentuckiana's federal taxes and withholdings, notwithstanding the existence of Kentucky statutes that expressly prohibit such treatment.[19]

In 2000 and 2001, Kentuckiana's general manager embezzled money from the company and neglected to file the company's federal employment taxes.[20] Although Littriello did not participate in the operation of the company in any way, and was not aware of the general manager's conduct, the IRS held him personally liable for the unpaid taxes because his LLC was a disregarded entity.[21] In January 2003, the IRS informed Littriello it would enforce previously filed tax liens against his personal property.[22] Upon learning that the IRS intended to levy his personal property, Littriello requested a Collection Due Process hearing with the IRS.[23] Approximately one year later, the IRS deter-

16. Final Brief for the Appellees at 5, *Littriello*, 484 F.3d 372 (No. 05-6494). Littriello actually had four similar cases pending before the district court, but the court consolidated them. *Id.* at 1-2. For the purpose of clarity, this comment will only refer to the facts of the lead case.

17. *Littriello*, 484 F.3d at 374. The check-the-box regulations give unincorporated organizations with a single owner the option of electing to be taxed as an association, or to be taxed as a disregarded entity by default. Treas. Reg. § 301.7701-3(a) (as amended in 2006). The statutory definition of "corporation" includes associations. I.R.C. § 7701(a)(3) (2000). Therefore, if Littriello had elected to classify Kentuckiana as an association for tax purposes, it would have been subject to the corporate income tax.

18. Treas. Reg. § 301.7701-3(b)(ii) (as amended in 2006). Kentucky state law establishes that a Kentucky LLC and the owner of the LLC are separate entities, and protects the owner from liability for the debts of the LLC. KY. REV. STAT. ANN. § 275.150 (LexisNexis 2003). The effect of disregarding an entity is that the IRS treats the owner of the disregarded entity and the entity itself as one single taxable entity. In other words, the owner of a disregarded entity is treated as the owner of a sole proprietorship. Philip B. Wright, *Disregarded Entities in Corporate Transactions*, 4 TAX STRATEGIES FOR CORP. ACQUISITIONS, DISPOSITIONS, SPIN-OFFS, JOINT VENTURES, FINANCINGS, REORGANIZATIONS & RESTRUCTURINGS 1025, 1031, 1033-34 (2006).

19. KY. REV. STAT. ANN. § 275.150 (LexisNexis 2003). Although the Kentucky statute states that the owner of an LLC cannot be held personally liable for the company's debts or obligations, the court held that federal tax provisions are not effected by state laws. *Littriello*, 484 F.3d at 379. The court concluded that business owners "are entitled to whatever advantages state law may extend, but state law cannot abrogate . . . federal tax liability." *Id.*

20. Final Brief of Appellant at 6, *Littriello*, 484 F.3d 372 (No. 05-6494); *see infra* note 157 and accompanying text for a brief explanation of federal employment taxes. Kentuckiana failed to pay more than $530,000 of withholding and FICA taxes from 2000 to 2002. William J. Rowe, Note, *Right Without Reason? The Check-the-Box Corporate or Partnership Election Regulations Correctly Held Valid:* Littriello v. United States, 59 TAX LAW. 913, 914 (2006). Littriello, however, correctly reported his earnings and losses from Kentuckiana on his personal tax returns during this period. Final Brief of Appellant at 7, *Littriello*, 484 F.3d 372 (No. 05-6494).

21. *Littriello*, 484 F.3d at 374; Complaint at ¶ 5(f), Littriello v. United States, No. 03:04-CV-143-H (W.D. Ky. May 18, 2005), 2005 WL 1173277.

22. *Littriello*, 484 F.3d at 374. The IRS was required to do this. I.R.C. § 6330(a)(1) (2000).

23. Final Brief of Appellant, *supra* note 20, at 5-6. A taxpayer may request a hearing with the IRS Office of Appeals within thirty days after receiving notice of a pending tax liability. I.R.C. § 6330(a)(3)(B) (2000). An impartial IRS officer not previously involved with the taxpayer's matter conducts the hearing. *Id.* § 6330(b)(3). The taxpayer may dispute liability or the amount in question during the hearing. *Id.* § 6330(c)(2)(B). After the hearing, the IRS prepares a written determination

mined that it would fully enforce the liens against Littriello as originally filed.[24]

### *A. United States District Court*

Shortly after the IRS issued its ruling, Littriello sought judicial review in the United States District Court for the Western District of Kentucky.[25] In its opinion, the district court identified what it believed to be the real issue of the case—the validity of the check-the-box regulations.[26] By granting the government's motion for summary judgment, the district court held that the check-the-box regulations were valid and upheld the assessment against Littriello.[27] The court acknowledged that Littriello's arguments were reasonable but considered them unpersuasive.[28] The majority of the opinion focused on what the court considered to be the "real dispute," while glossing over Littriello's contention that the check-the-box regulations are not applicable to employment taxes.[29]

### *B. United States Court of Appeals for the Sixth Circuit*

After the district court denied his motion to reconsider, Littriello filed a timely Notice of Appeal with the United States Court of Appeals for the Sixth Circuit, where he echoed the same arguments he had raised previously in the district court.[30] Once again, the court focused primarily on the validity of the check-the-box regulations under the *Chevron* test.[31] The court also discussed whether the regulations were applicable

regarding the tax liability. *Id.* § 6330(d)(1). If necessary, the taxpayer is then permitted to file an appeal. *Id.*

24. Final Brief of Appellant, *supra* note 20, at 6.

25. Final Brief for the Appellees, *supra* note 16, at 2.

26. Littriello v. United States, No. Civ.A.3:04CV-143-H, 2005 WL 1173277, at *1 (W.D. Ky. May 18, 2005). Littriello did not expressly question the validity of the check-the-box regulations in his original complaint. Rather, he argued the IRS should not have held him liable for the unpaid taxes, because he was not the responsible person for those taxes under Internal Revenue Code (Code) § 6672. Complaint, *supra* note 21, ¶ 6. Only after the government clarified that the liens filed against Littriello were not related in any way to Code § 6672 did Littriello challenge the reasonableness of holding him personally liable for the unpaid employment taxes pursuant to the check-the-box regulations. Reply ¶ 2, *Littriello*, 2005 WL 1173277 (No. 03:04-CV-143-H).

27. *Littriello*, 484 F.3d at 375.

28. *Littriello*, 2005 WL 1173277, at *3. Littriello argued that the check-the-box regulations (1) are invalid because Congress intended taxation to be based on the realistic nature of a business entity; (2) cannot change the status of a company created by state law; and (3) do not apply to employment withholdings because they are debts, not taxes, owed by the company. *Id.* at *4. He also argued that Congress intended Code § 6672 to be the only recourse available to the IRS to recover unpaid employment taxes. *Id.*

29. *See Littriello*, 2005 WL 1173277, at *4. A subsequent case, Kandi v. United States, No. C05-0840C, 2006 WL 83463 (W.D. Wash. Jan. 11, 2006), currently under appeal in the United States Court of Appeals for the Ninth Circuit, discusses this issue very thoroughly. *Kandi*, 2006 WL 83463, at *4-5.

30. Final Brief of Appellant, *supra* note 20, at 1. Littriello filed a "motion for reconsideration of the order granting summary judgment to the government." Final Brief for the Appellees, *supra* note 16, at 3. The court denied the motion on August 4, 2005. *Id.*

31. *Littriello*, 484 F.3d at 374. See *infra* notes 193-198 and accompanying text for a brief expla-

to federal employment taxes in light of proposed amendments to the regulations.[32] The Sixth Circuit, however, did not address whether the IRS was justified in concluding that Littriello's disregarded LLC could not be the "employer" for employment tax purposes.[33]

Littriello argued that the *Chevron* test was irrelevant because of the United States Supreme Court decision in *Morrissey v. Commissioner*.[34] The court rejected this argument and affirmed district court's decision.[35] The court also rejected Littriello's argument that the IRS cannot abrogate state law through the check-the-box regulations, and that Internal Revenue Code (Code) section 6672 is the only recourse available to collect unpaid employment taxes.[36] Littriello recently filed for a rehearing en banc, although the court has yet to rule on the petition.[37] Since the Sixth Circuit issued its opinion, the United State Court of Appeals for the Second Circuit likewise affirmed the validity of the check-the-box regulations in a case very similar to *Littriello*.[38] Another case is also currently on appeal before the United State Court of Appeals for the Ninth Circuit.[39]

## III. BACKGROUND

### *A. Entity Classification*

The classification of a business entity is significant, because it dictates how the federal government will tax the entity.[40] In general, the IRS classifies business entities as either corporations or partnerships.[41] Corporations are subject to double taxation—their income is taxed first at the corporate level and again at the individual shareholder level.[42] Partnerships, on the other hand, are taxed only once—their income is taxed after it passes through to the individual partners, where it is taxed

nation of the *Chevron* test.

32. *Littriello*, 484 F.3d at 379.

33. *See generally Littriello*, 484 F.3d 372.

34. 296 U.S. 344 (1935); Final Brief of Appellant, *supra* note 20, at 18. For in depth commentary on this argument, see Greg D. Polsky, *Can Treasury Overrule the Supreme Court?*, 84 B.U. L. REV. 185 (2004).

35. *Littriello*, 484 F.3d at 380.

36. *Id.*

37. Petition for Rehearing and Petition for Rehearing En Banc, *Littriello*, 484 F.3d 372, (6th Cir. 2007) (No. 05-6494).

38. *See* McNamee v. Dep't of the Treasury, 488 F.3d 100, 103 (2d Cir. 2007).

39. *See* Kandi v. United States, No. C05-0840C, 2006 WL 83463 (W.D. Wash. Jan. 11, 2006). The court in this case directly addressed whether the check-the-box regulations apply to employment taxes and whether a disregarded entity is the employer for employment tax purposes. *Id.* at *4-5. Although the court ultimately agreed with the IRS's position on the latter issue, this comment will explain the flaws of that conclusion.

40. *See* Polsky, *supra* note 34, at 186.

41. Treas. Reg. § 301.7701-2(a) (as amended in 2006).

42. *Littriello*, 484 F.3d at 375. For further explanation on the difference between the taxation of corporations and partnerships, see Victor E. Fleischer, Note, "*If It Looks Like a Duck": Corporate Resemblance and Check-the-Box Elective Tax Classification*, 96 COLUM. L. REV. 518, 522-23 (1996).

as their personal income.[43]

The first step in classifying a business entity is to look to the definition of "corporation" in Code section 7701(a)(3).[44] Generally, if an entity fits within the definition provided in section 7701(a)(3), the entity is classified as a tax corporation.[45] If not, Code section 7701(a)(2) provides that the business entity is a tax partnership by default.[46] Classifying business entities as corporations or partnerships has proven a costly, time-consuming challenge for business owners and the IRS for several decades.[47]

### 1. State v. Federal

State and federal governments each play a role in the entity classification process.[48] While the authority to create business structures and to define their rights and obligations rests with the states, the authority to classify businesses for federal tax purposes lies with the federal government.[49] Therefore, the IRS can reclassify or even disregard a business entity recognized under state law for federal tax purposes.[50] Courts have tried to determine what effect, if any, an entity's rights and duties provided by state law have on its federal tax classification.[51]

Because of the overlapping of state and federal powers in this area, state and federal laws regarding entity classification have evolved continually over time.[52] The Treasury has consistently promulgated federal regulations to maximize national revenue generation, and state legislatures have repeatedly enacted laws designed to help business owners exploit such regulations and maximize their personal rights and interests.[53]

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43. Consequently, partnership taxation is commonly referred to as "pass-through" taxation. *Littriello*, 484 F.3d at 375.

44. Polsky, *supra* note 34, at 212.

45. Fleischer, *supra* note 42, at 523; I.R.C. § 11(a) (2000). The Treasury changed this in 1996 by finalizing the check-the-box regulations. Treas. Reg. §§ 301.7701-1 to -3, (as amended by T.D. 8697).

46. Bradley T. Borden, *The Federal Definition of Tax Partnership*, 43 HOUS. L. REV. 925, 936 (2006); Polsky, *supra* note 34, at 212.

47. *See Littriello*, 484 F.3d at 376; Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21990 (May 13, 1996). While discussing the amount of time and money expended in applying the *Kintner* regulations, the Treasury stated, "For example, since the issuance of Rev. Rul. 88-76, the IRS has issued seventeen revenue rulings analyzing individual state limited liability company statutes, and has issued several revenue procedures and numerous letter rulings relating to classification of various business organizations." Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21990 (May 13, 1996). The Treasury also noted that it was so costly that many small business organizations lacked the resources necessary to achieve the tax classification they desired. *Id.*

48. Treas. Reg. § 301.7701-1(a)(1) (as amended in 2006); s*ee* Hamill, *supra* note 1, at 1484.

49. Treas. Reg. § 301.7701-1(a)(1) (as amended in 2006); Hamill, *supra* note 1, at 1484.

50. *See* Fleischer, *supra* note 42, at 523.

51. *See Littriello*, 484 F.3d at 378-79 (referring to the Supreme Court cases *United States v. Galletti*, 541 U.S. 114 (2004), and *Hecht v. Malley*, 265 U.S. 144 (1924), while discussing the effect of state law on an entity's tax classification).

52. *See* Patrick E. Hobbs, *Entity Classification: The One Hundred-Year Debate*, 44 CATH. U. L. REV. 437, 481-518 (1995) (explaining how federal tax law evolved in response to state laws that provided for organizations such as professional corporations, limited partnerships, and LLCs).

53. *See id.*

The clash between state legislatures and the Treasury likely commenced when states developed primary control over incorporation and then grew more intense after the creation of the modern day entity-level income tax.[54] Because Congress exempted certain entities from this income tax, some business owners and state legislators developed alternative business structures that would not be subject to the tax, while others specifically sought ways to classify their businesses as associations or corporations.[55] In response to the new business entities, the Treasury modified the existing regulations to maximize the number of taxable entities.[56] In turn, states and taxpayers developed other new forms of business that the Treasury had not previously considered.[57] This cycle has repeated itself several times.[58]

### 2. Corporate Income Tax

The debate concerning entity classification began late in the nineteenth century, when Congress imposed the country's first peacetime tax on individual and corporate income, as provided in the Revenue Act of 1894.[59] Prior to 1894, the federal government relied primarily on tariffs to generate revenue unless the country was at war.[60] Post Civil War economic changes, however, led many people to believe it would be more equitable to impose a tax on the income of large corporations and wealthy individuals.[61] After much debate, Congress finalized the Revenue Act in August 1894, imposing a federal income tax on "corporations, companies, or associations doing business for profit in the United States, no matter how created and organized, but not including partnerships."[62] Shortly thereafter, in *Pollock v. Farmers' Loan & Trust Co.*,[63]

54. *See* Revenue Act of 1913, ch. 16,§ II(G)(a), 38 Stat. 114, 172 (amended 1917) (establishing a federal entity-level income tax); Hamill, *supra* note 1, at 1484-85, 1501-02 (explaining that the evolution of state and federal tax laws, which made it possible to create LLCs, was a result of the states having the primary power of incorporation and the creation of a corporate income tax).

55. *See* Hobbs, *supra* note 52, at 481-518 (explaining how the Treasury responded to the creation of professional corporations, limited partnerships, and LLCs). The Revenue Act of 1913 expressly stated that the tax was not applicable to partnerships. Revenue Act of 1913, ch. 16, § II(G)(a), 38 Stat. 114, 172. Although the Act established the tax for corporations and associations established under state law, it was not until 1918 that Congress made it clear that associations were different from corporations. Hamill, *supra* note 1, at 1503.

56. *See* Hobbs, *supra* note 52, at 481-518 (explaining how the Treasury responded to the creation of professional corporations, limited partnerships, and LLCs). Although this implies that the Treasury would want all companies classified as corporations, this is not always the case. Sometimes, when it believes that certain entities, like professional associations or corporations, should not be able to reap corporate benefits, the Treasury will directly fight against those entities being recognized as associations. *See id.* at 483.

57. *Id.* at 481-518.

58. *Id.*

59. Revenue Act of 1894, ch. 349, § 32, 28 Stat. 509, 556, *invalidated by* Pollock v. Farmers' Loan & Trust Co., 158 U.S. 601 (1895); *see* Hobbs, *supra* note 52, at 441.

60. Hobbs, *supra* note 52, at 442.

61. *Id.* at 442-43.

62. *See* Hobbs, *supra* note 52, at 444, 451 (quoting Revenue Act of 1894, ch. 349, § 32, 28 Stat. 509, 556).

the Supreme Court declared the Act unconstitutional, violating Article I, Section 2 of the United States Constitution.[64]

Approximately fifteen years after *Pollock*, President Taft proposed that Congress prepare a constitutional amendment that would give Congress the authority to enact an income tax.[65] The President also suggested that, until such an income tax was constitutional, Congress enact an excise tax on corporate income.[66] As a result, the Corporate Excise Tax became law on August 4, 1909.[67] Although Congress likely intended the excise tax to apply only to corporations and joint-stock companies, the Treasury interpreted the excise tax statute to apply independently to associations as well.[68] The Supreme Court addressed and corrected this in 1911, when it clarified that Congress did not intend the term "associations" to be an independent concept.[69] The Court also held that Congress only intended the excise tax to extend to corporations and joint-stock companies organized under statute.[70]

Two years later, under the Sixteenth Amendment to the United States Constitution and the Revenue Act of 1913, the federal government finally created a constitutional income tax.[71] The Sixteenth Amendment grants Congress the power "to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration."[72] With its authority to tax established, Congress enacted the Revenue Act

63. 158 U.S. 601 (1895).

64. *Id.* at 637. Because the greatest portion of the income subject to taxation under the Act came from property, and because those taxes were not apportioned among the states based on their respective populations, the Court found the tax unconstitutional. *Id.*

65. Hobbs, *supra* note 52, at 454 (citing 44 CONG. REC. 3344-45 (1909)).

66. *Id.* By calling the tax an excise tax, President Taft prevented the Supreme Court from having to reexamine the income tax issue and possibly overturn its decision in *Pollock*—and also satisfied those Republicans who opposed the income tax. *Id.* An excise tax is a tax imposed on a particular act, event, or transaction. United States v. 4,432 Mastercases of Cigarettes, More or Less, 448 F.3d 1168, 1185 (9th Cir. 2006). Our country's most basic excise tax is the sales tax, which is imposed upon the act of purchasing goods. *Id.* A corporate excise tax can be a tax on the privilege of doing corporate business within a particular state. *See* Cook Export Corp. v. King, 652 S.W.2d 896, 900 (Tenn. 1983).

67. Revenue Act of 1909, ch. 6, § 38, 36 Stat. 11, 112-13 (amended 1913).

68. Treas. Reg. 31, T.D. 1571, 12 Treas. Dec. Int. Rev. 131, 135-36 (1909); Hobbs, *supra* note 52, at 454. (explaining that President Taft specified when he suggested this tax to Congress that it was to apply only to corporations and joint-stock companies, and further that the way the tax was drafted confirms that this was Congress's intent, even though the term "association" is included in the language of the statute). The Revenue Act of 1909 stated that the excise tax was to be paid by "every corporation, joint-stock company or association, organized for profit and having a capital stock represented by shares, and every insurance company." Revenue Act of 1909, ch. 6, § 38, 36 Stat. 11, 112. Regulation 31 changed the substantive meaning of this provision by adding a comma between joint-stock companies and associations, thus treating associations as separate from joint-stock companies. The Regulations provided that the tax applied to "all corporations, joint-stock companies, associations, or insurance companies." Treas. Reg. 31, T.D. 1571, 12 Treas. Dec. Int. Rev. 131, 135 (1909).

69. Flint v. Stone Tracy Co., 220 U.S. 107, 144 (1911), *overruled by* Garcia v. San Antonio Metro. Transit, 469 U.S. 528 (1985).

70. Eliot v. Freeman, 220 U.S. 178, 185 (1911).

71. U.S. CONST. amend. XVI; Revenue Act of 1913, ch. 16, § II(G)(a), 38 Stat. 114, 172 (amended 1917).

72. U.S. CONST. amend. XVI.

of 1913, which imposed a federal income tax on "every corporation, joint-stock company or association, and every insurance company . . . not including partnerships."[73] Once again, the Treasury attempted to interpret the statute more liberally than Congress actually intended, and once again, the Supreme Court had to intervene and address the flaw of the regulations.[74]

From 1894 through 1913, it appeared Congress intended the corporate income tax to apply to corporations and joint-stock companies, but not to associations.[75] During the same period, however, the Treasury attempted to modify the tax, by construing the term "association" more broadly, so it would apply to more business entities.[76] The Revenue Act of 1918 eliminated any discrepancy between the postures of Congress and the Treasury concerning entity classification.[77] In this Act, Congress, for the first time, provided a definitional section that applied to the entire Act.[78] This was significant, particularly because Congress provided a new definition of the term "corporation," which officially separated joint-stock companies and associations.[79] By providing this definition, "[t]he Revenue Act of 1918 marked the end of the first entity-classification debate and the beginning of the next."[80]

### 3. *Morrissey v. Commissioner*

A significant challenge concerning entity classification lies in the definitions of the terms "corporation" and "partnership" provided by Congress.[81] The statutory definition of "corporation," unaltered since

73. Revenue Act of 1913, ch. 16, § II(G)(a), 38 Stat. 114, 172. Congress drafted this Act with joint-stock companies and associations considered together as it did in the Revenue Act of 1909 rather than adopting the modified language of Regulation 31 with the misplaced comma. *Id.* This may imply that Congress did not intend associations to be considered as a classification separate and independent from corporations and joint-stock companies. *See* Hobbs, *supra* note 52, at 467.

74. Crocker v. Malley, 249 U.S. 223, 233-34 (1919); Hobbs, *supra* note 52, at 463-64. The federal government was attempting to tax a trust as a corporation based on the broad interpretation of the term association provided by the Treasury, but the Supreme Court clarified that the trust was not an association because it "would not fall under any familiar conception of a joint-stock association." *Crocker*, 249 U.S. at 233.

75. "The joint-stock company fell midway between the corporation and the partnership on the business entity spectrum, and it existed both at common law and in statutory form. The Senators regarded the terms 'associations' and 'joint-stock companies' as synonymous. [One Senator] even regarded these terms as interchangeable." Hobbs, *supra* note 52, at 450-51.

76. *Id.* at 455-56, 463-64.

77. *See* Revenue Act of 1918, ch. 18, § 1, 40 Stat. 1057, 1058 (amended 1921). It was evident after the Revenue Act of 1916 that Congress was beginning to accept the broad interpretation of the term "association" endorsed by the Treasury. *See* Hobbs, *supra* note 52, at 467. Of the thirty times that the words "joint-stock companies" and "associations" appeared in the Act, three of them included a comma between the two terms, supporting the idea that Congress was beginning to consider treating the two terms as separate concepts. *Id.*

78. Revenue Act of 1918, ch. 18, § 1, 40 Stat. 1057.

79. *Id.* at 1058. The definition section indicated that Congress had officially adopted the broad interpretation of the term "association" by providing that the term "corporation" includes "associations, joint-stock companies, and insurance companies." *Id.*

80. Hobbs, *supra* note 52, at 467.

81. I.R.C. §§ 7701(a)(2) to (3) (2000).

1918, provides that "[t]he term 'corporation' includes associations, joint-stock companies, and insurance companies."[82] Under this framework, state-law corporations are not the only entities subject to the corporate income tax.[83] The federal government classifies any unincorporated organization that qualifies as an "association" as a corporation for tax purposes as well.[84] By failing to define the term "association," Congress caused courts and administrators to struggle for years with defining the term.[85]

Recognizing the insufficiency of the definitions provided by Congress, the Treasury promulgated regulations to clarify and interpret the definitions.[86] These regulations, however, did not solve the entity classification problem.[87] Additionally, these regulations raised another major legal question—whether the Treasury has authority to issue such interpretive regulations at all.[88]

In 1935, the Supreme Court provided some guidance concerning the meaning of the term "association" in *Morrissey*.[89] The Court clarified that because Congress did not define the term "association," the Treasury possessed authority "to supply rules for the enforcement of the Act within the permissible bounds of administrative construction."[90] The Court further explained that the scope of the Treasury's authority encompassed the ability to clarify or enlarge existing regulations "to meet administrative exigencies or conform to judicial decision[s]."[91] The Court noted that "the recurring disputes" concerning the term "association," accentuated the need to examine congressional intent to clarify the scope of the classification rules.[92]

The Court concluded that Congress intended to tax any unincorporated organization that sufficiently resembles a corporation as an "association."[93] The Court also outlined six corporate factors to consider in determining whether an organization resembles a corporation closely enough to classify it as an association.[94] Using the corporate resem-

82. I.R.C. § 7701(a)(3) (2000); Revenue Act of 1918, ch. 18, § 1, 40 Stat. 1057, 1058; Morrissey v. Comm'r, 296 U.S. 344, 349 (1935).

83. *See* I.R.C. § 7701(a)(3) (2000).

84. *See id.*

85. Polsky, *supra* note 34, at 213.

86. *See Morrissey*, 296 U.S. at 353-54 (explaining the evolution of the applicable regulations promulgated under the different Revenue Acts).

87. *See* Hobbs, *supra* note 52, at 478 (stating that the regulations promulgated by the Treasury "muddled" the definition of "association").

88. *See* Caroline Elizabeth Costle, Note, *Judicial Deference to Interpretive Regulations in the Face of Inconclusive Legislative History: The Example of* Nalle v. Commissioner, 47 TAX LAW. 259, 262 (1993).

89. *Morrissey*, 296 U.S. at 356-57; Polsky, *supra* note 34, at 213.

90. *Morrissey*, 296 U.S. at 354-55.

91. *Id.* at 355.

92. *Id.* at 356.

93. *Id.* at 357, 359-60.

94. *Id.* at 359-60. The factors include: (1) the presence of associates; (2) title to property; (3) centralized management; (4) continuity of existence; (5) free transferability of interests; and (6) lim-

blance test, the Court held that a business entity organized as a trust under state law should be an association for tax purposes.[95]

### 4. *Kintner* Regulations

The corporate resemblance test established in *Morrissey* remained the entity classification standard until 1960.[96] Yet, the corporate resemblance test did not cure all of the classification problems that plagued the courts and administrators.[97] Because the Court did not indicate the weight each of the six corporate factors should carry and failed to quantify a number of factors that must be present for a court to classify an entity as an association, implementation of the test was very challenging and unpredictable.[98]

Inspired by the Ninth Circuit decision in *United States v. Kintner*,[99] the Treasury promulgated new regulations in 1960 to address the difficulties of the corporate resemblance test.[100] The *Kintner* regulations specified that an unincorporated organization was only an association, and therefore a tax corporation—if it had more corporate characteristics than non-corporate characteristics.[101] Like the Court in *Morrissey*, the *Kintner* regulations mentioned six characteristics that distinguish corporations from other business organizations.[102] The Treasury recognized, however, that some of the enumerated characteristics were also common to partnerships and trusts.[103] Therefore, the regulations instructed that in determining whether an organization resembled a corporation

ited liability. Littriello v. United States, 484 F.3d 372, 375 (6th Cir. 2007). Before the United States Court of Appeals for the Sixth Circuit, Littriello argued that the precedent set by *Morrissey* dictates that, to be valid, entity classification must be based on "a fact sensitive determination of the business characteristics of a taxpayer entity." Final Brief of Appellant, *supra* note 20, at 16. Other commentators disagree, suggesting that "the Court never intended a mechanical application of its enumerated factors." Fleischer, *supra* note 42, at 525-26.

95. *Morrissey*, 296 U.S. at 360.

96. Polsky, *supra* note 34, at 216.

97. The Court in *Morrissey* did not really provide anything completely new to solve the existing problems. Hobbs, *supra* note 52, at 478. Although the corporate resemblance test received its seal of approval in this decision, the test itself was not much different than what already existed in the form of the Treasury regulations. *Id.*

98. Polsky, *supra* note 34, at 216. S*ee generally Morrissey*, 296 U.S. 344.

99. 216 F.2d 418 (9th Cir. 1954).

100. *See* Treas. Reg. § 301.7701-2(a)(3), T.D. 6503, 1960-2 C.B. 409, 414. In *Kintner*, the Ninth Circuit determined that an unincorporated organization of physicians established by Dr. Arthur Kintner was a tax corporation. 216 F.2d at 428. If professional associations such as the one Dr. Kintner belonged to were classified as corporations, they could adopt tax-favored pension plans and reap other corporate benefits. Hobbs, *supra* note 52, at 481-82. Because the government did not want to allow Kintner's unincorporated organization to receive corporate benefits, it argued that the association of doctors should not be classified as a corporation because state law did not allow physicians to form corporations. *Kintner*, 216 F.2d at 421. The court rejected the government's arguments and concluded that Kintner's association was a tax corporation. *Id.* at 428. In response to the decision in *Kintner*, the Treasury eventually revised its regulations to limit the types of business organizations classifiable as tax corporations. *See* Hobbs, *supra* note 52, at 485-88.

101. Treas. Reg. § 301.7701-2(a)(3) (1960).

102. Treas. Reg. § 301.7701-2(a)(1) (1960).

103. Treas. Reg. § 301.7701-2(a)(3) (1960).

more than a partnership, courts should consider only those characteristics not shared by both types of organizations.[104]

While on the surface these regulations appeared to be nothing more than an attempt by the Treasury to simplify the entity classification process, the Treasury was actually repositioning in response to strategic moves made within the states that concerned a new and popular form of business—professional associations.[105] One of the Treasury's main objectives in promulgating these regulations was to prevent professional associations from qualifying for corporate classification.[106] In response, state legislatures helped taxpayers circumvent the *Kintner* regulations by enacting state statutes incorporating professional associations.[107]

In 1965, the Treasury amended the *Kintner* regulations and abolished the longstanding rule requiring the federal government to recognize any business entity expressly classified as a corporation under state law as a corporation for tax purposes.[108] These amendments implicitly provided "that while the *Kintner* Regulations remained the general standard of review for association status . . . an independent, insurmountable test" was the standard for professional corporations.[109]

Several courts responded to the Treasury's tactics by invalidating the amended regulations.[110] In *O'Neill v. United States*,[111] the Sixth Circuit explained that Congress clearly intended all businesses organized as corporations under state law to be tax corporations without any further requirement concerning corporate resemblance as articulated in *Morrissey*.[112] Conceding defeat on this issue, the Treasury agreed to classify

104. *Id.*

105. Hobbs, *supra* note 52, at 488 (explaining that, by promulgating the *Kintner* regulations, the Treasury was specifically trying to prevent professional associations from being classified as tax corporations).

106. *Id.* When professional associations first started to appear in the 1930s, the Treasury fought to have these new organizations classified as corporations for tax purposes. *Id.* at 481. What the Treasury failed to foresee was that many business owners would find corporate classification enticing due to certain benefits only available to corporate entities, such as tax-favorable pension plans. *Id.* at 481-82. Once these new companies started reaping these corporate benefits, the Treasury did a 180-degree turn and fought to deny the right of professional associations to be treated as a corporation. *Id.* at 483.

107. *Id.* at 489. The validity of the *Kintner* regulations has never been challenged on the grounds that the Treasury Department lacked regulatory authority to issue them in light of *Morrissey*. Polsky, *supra* note 34, at 218.

108. T.D. 6797, 1965-1 C.B. 553, 554 ("[T]he labels applied by local law to organizations, which may now or hereafter be authorized by local law, are in and of themselves of no importance in the classification of such organizations for the purposes of taxation under the Internal Revenue Code. Thus, a professional service [corporation] . . . would not be classified for purposes of taxation as a 'corporation' merely because the organization was so labeled under local law.").

109. Hobbs, *supra* note 52, at 490.

110. *See* O'Neill v. United States, 410 F.2d 888, 899 (6th Cir. 1969); Rev. Rul. 70-101, 1970-1 C.B. 278 (explaining that the Treasury was changing its position because so many courts invalidated the regulations).

111. 410 F.2d 888 (6th Cir. 1969).

112. *Id.* at 899. The Sixth Circuit was, for all practical purposes, performing the first step of the *Chevron* analysis, albeit twenty-five years before the Supreme Court officially adopted the analysis.

those organizations formed under professional corporation statutes as corporations for tax purposes.[113] Although the debate concerning professional corporations had ended, this would not be the last time the Treasury would confront a new type of business designed to allow business owners to avoid tax liabilities while reaping corporate benefits.

### 5. Limited Liability Companies

In 1977, the Wyoming Legislature made it possible to create an LLC, a new type of business that would trouble the Treasury for many years.[114] This new hybrid business entity combined corporate limited liability with partnership pass-through taxation.[115] The Wyoming Legislature accomplished this, in part, because of the *Kintner* regulations, which prohibited classifying unincorporated organizations as associations unless the business possessed at least three key corporate characteristics.[116] Therefore, business owners could structure LLCs with limited liability and one other key corporate characteristic and still manage to avoid corporate taxation.[117] The Wyoming Legislature, for example, drafted its statute so that LLCs would possess limited liability and, potentially, centralized management, but would lack continuity of life or free transferability of interests.[118]

Although the Wyoming legislation made it possible to create LLCs, it was unclear whether the IRS would actually agree to classify these almost-corporate entities as partnerships for federal tax purposes, and the IRS was in no hurry to make a decision on the matter.[119] Finally, in late 1980, the IRS issued a private letter ruling, which stated that it would classify a Wyoming LLC as a partnership.[120] The IRS also ex-

*Id.* at 493; *Chevron*, 467 U.S. at 842-43. The Sixth Circuit viewed this case as "one of statutory construction" in which it found that the plain meaning and Congress's intent was evident. *O'Neill*, 410 F.2d at 890. Therefore, because Congress had already clearly indicated that state-law corporations were to be classified as corporations for federal tax purposes, the regulations were invalid because they included additional requirements. *Id.* at 899.

113. Rev. Rul. 70-101, 1970-1 C.B. 278.

114. WYO. STAT. ANN. § 17-15-103(a) (1977).

115. Laurel Wheeling Farrar & Susan Pace Hamill, *Dissociation from Alabama Limited Liability Companies in the Post Check-the-Box Era*, 49 ALA. L. REV. 909, 909 (1998).

116. *See* Hobbs, *supra* note 52, at 511.

117. The key corporate characteristics in the *Kintner* regulations include: (1) centralized management; (2) continuity of life; (3) free transferability of interests; and (4) limited liability. Treas. Reg. § 301.7701-2(a)(2), T.D. 6503, 1960-2 C.B. 409, 413-14 (1960). According to the regulations, an LLC could possess limited liability and one of the other three characteristics listed and successfully avoid corporate taxation. *Id.* § 301.7701-2(a)(3). LLCs can also possess associates and an objective to carry on business for profit, because the *Kintner* regulations recognized that these two characteristics were common to both corporations and partnerships, and therefore did not consider them to determine entity classification. *Id.*

118. *See* WYO. STAT. ANN. §§ 17-15-113, -116, -122, -123 (1977). The Wyoming statute allowed the business owners to control whether or not to have centralized management. Hobbs, *supra* note 52, at 512-13.

119. Hamill, *supra* note 1, at 1466-67. The IRS took over three years to respond to the initial request for partnership classification. *Id.*

120. I.R.S. Priv. Ltr. Rul. 81-06-082 (Nov. 18, 1980) ("Since [the LLC] will lack continuity of life

plained, however, that it had published proposed amendments to the Treasury regulations the previous day, and that they would require that "an organization in which no member has personal liability for the debts of the organization be classified as an association taxable as a corporation."[121] Eventually, the IRS withdrew the proposed regulations.[122] Nevertheless, the fate of LLCs remained in limbo until 1988, when the IRS issued a pivotal revenue ruling.[123] The IRS concluded that although the Wyoming LLC possessed limited liability, it could still secure partnership classification.[124] After the IRS issued this ruling, several other state legislatures enacted limited liability company statutes.[125] By 1996, only eight years after the revenue ruling, all fifty states had established similar statutes, and business owners had organized over 210,000 LLCs nationwide.[126]

In 1994, Kentucky became the forty-first state to pass an LLC act.[127] The Kentucky Act grants individual business owners flexibility in structuring LLCs.[128] The Act also provides certain default rules that business owners can choose to incorporate into their LLCs.[129] An LLC organized according to the default rules possesses limited liability for its members, but lacks free transferability of interests, continuity of life, and centralized management, and is therefore classified as a partnership for federal tax purposes.[130] The Kentucky LLC statute also permits the

and free transferability of interests, [it] will not have a preponderance of corporate characteristics. Therefore, [it] will be treated as a partnership for Federal income tax purposes and not as an association taxable as a corporation."). Although Private Letter Rulings are helpful because they make known the current IRS position on tax issues, taxpayers may not cite or rely upon them as legal precedent. I.R.C. § 6110(k)(3) (2000).

121. I.R.S. Priv. Ltr. Rul. 81-06-082 (Nov. 18, 1980). Apparently, the IRS did not want to classify LLCs as partnerships, but could not find a way to avoid it under the regulations existing at the time.

122. Hamill, *supra* note 1, at 1469.

123. *See* Rev. Rul. 88-76, 1988-2 C.B. 360. A revenue ruling is "a public interpretation of the law all taxpayers can rely upon." Hamill, *supra* note 1, at 1469. The Treasury has provided that:

> Revenue Rulings . . . do not have the force and effect of Treasury Department Regulations (including Treasury decisions), but are published to provide precedents to be used in the disposition of other cases, and may be cited and relied upon for that purpose . . . .
> Taxpayers generally may rely upon Revenue Rulings published in the Bulletin in determining the tax treatment of their own transactions and need not request specific rulings applying the principles of a published Revenue Ruling to the facts of their particular cases. However, since each Revenue Ruling represents the conclusion of the Service as to the application of the law to the entire state of facts involved, taxpayers, Service personnel, and others concerned are cautioned against reaching the same conclusion in other cases unless the facts and circumstances are substantially the same. They should consider the effect of subsequent legislation, regulations, court decisions, and revenue rulings.

Treas. Reg. § 601.601(d)(2)(v)(d), (e) (as amended in 1987).

124. Rev. Rul. 88-76, 1988-2 C.B. 360, 361.

125. *See, e.g.*, COLO. REV. STAT. § 7-80-101 (1990); Kansas Limited Liability Act, ch. 80, 1990 Kan. Sess. Laws 585.

126. Hamill, *supra* note 1, at 1477-78.

127. Rutledge, *supra* note 3, at 4; *see* KY. REV. STAT. ANN. § 275.001 (LexisNexis 2007).

128. Rutledge, *supra* note 3, at 87. The statute provides default rules that apply in the event that the business owner does not wish to structure the LLC differently. For a more thorough discussion of flexible LLC statutes see Karen C. Burke, *The Uncertain Future of Limited Liability Companies*, 12 AM. J. TAX POL'Y 13, 40-41 (1995).

129. Rutledge, *supra* note 3, at 87-88.

130. *Id.* With regard to limited liability, Kentucky law expressly provides that "[a] member of a

creation of single-member LLCs, which presents the question whether any single-member company can be a tax partnership, a concept that presupposes the existence of at least two members.[131]

### 6. Check-the-Box Regulations

LLCs forced the Treasury to acknowledge the ineffectiveness of the *Kintner* regulations and consider alternative methods to regulate entity classification.[132] After years of considering possible alternatives, the Treasury finally developed a plan to "simplify[] the classification regulations to allow taxpayers to treat domestic unincorporated business organizations as partnerships or as associations on an elective basis."[133] On May 13, 1996, the Treasury published proposed regulations.[134] Seven months later, the Treasury finalized the regulations commonly known as check-the-box.[135]

The Treasury issued the check-the-box regulations pursuant to Code section 7805.[136] According to the Treasury, the new regulations were necessary because the previous regulations and the corporate resemblance test had "become increasingly formalistic."[137] To some extent, by strategically selecting which corporate characteristics to adopt in their company, business owners had already been electing how to have their businesses taxed for years.[138] The Treasury replaced the resemblance test with a much simpler, elective approach to provide business owners increased flexibility in the entity classification exercise.[139]

Although commentators have described the check-the-box regulations as an elective classification regime, that description is not entirely

limited liability company shall not be a proper party to a proceeding by or against a limited liability company . . . ." KY. REV. STAT. ANN. § 275.155 (LexisNexis 2007). Kentucky statutes also state that:

> [N]o member, manager, employee, or agent of a limited liability company . . . shall be personally liable . . . for a debt, obligation, or liability of the limited liability company, whether arising in contract, tort, or otherwise. The status of a person as a member, manager, employee, or agent of a limited liability company . . . shall not subject the person to personal liability for the acts or omissions, including any negligence, wrongful act, or actionable misconduct, of any other member, manager, agent, or employee of the limited liability company.

*Id.* § 275.150(1).

131. KY. REV. STAT. ANN. § 275.015(8) (LexisNexis 2007); *see* Rutledge, *supra* note 3, at 58 n.292 ("Whether an LLC can have only one member and be classified as a partnership remains an unresolved issue."). The check-the-box regulations seem to resolve this issue by stating that only LLCs with at least two members may be federal tax partnerships. Treas. Reg. § 301.7701-2(c)(1) (as amended in 2006).

132. *See* Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21990 (May 13, 1996).

133. I.R.S. Notice 95-14, 1995-1 C.B. 297, 297; *see* Hamill, *supra* note 1, at 1470-73.

134. Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21989 (May 13, 1996).

135. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 66584 (Dec. 18, 1996); *see* Polsky, *supra* note 34, at 221.

136. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 66584, 66588 (Dec. 18, 1996).

137. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 66584, 66584 (Dec. 18, 1996).

138. *See* Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21990 (May 13, 1996).

139. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 66584, 66584 (Dec. 18, 1996).

accurate.[140] The regulations specify eight types of organizations that are tax corporations by default.[141] Organizations not enumerated in that list are eligible to elect their tax classification.[142] The regulations make a distinction between eligible entities with multiple members and those with only a single owner.[143] While the regulations allow business entities with two or more members to elect to be tax corporations or tax partnerships, they deny single-member companies the option of partnership classification.[144] The check-the-box regulations provide these companies the election to be a tax corporation or a disregarded entity for tax purposes.[145]

To simplify the classification process, the regulations provide default classifications for eligible entities.[146] Furthermore, the regulations do not require eligible entities to make an affirmative election unless they wish to change their previous tax classification.[147] The one exception to this rule is that the IRS now disregards the separate existence of single-member eligible entities and treats them as sole proprietorships unless they affirmatively elect to be tax corporations.[148] According to the new regulations, "whether an organization is an entity separate from its owners for federal tax purposes is a matter of federal tax law and does not depend on whether the organization is recognized as an entity under local law."[149] When the Treasury previously attempted to claim that state statutes were irrelevant in determining the separate existence of a business entity, courts rejected the idea repeatedly.[150] Nevertheless, the Treasury relied on this presumption to justify disregarding the exis-

140. *See* Polsky, *supra* note 34, at 222.

141. Treas. Reg. § 301.7701-2(b)(1) to (8) (as amended in 2006). The eight types of organizations that are tax corporations by default according to the check-the-box regulations include: (1) entities recognized as corporations under Federal or State statute; (2) associations; (3) joint-stock companies or associations; (4) insurance companies; (5) State-chartered banking entities; (6) business entities owned by a state or a foreign government; (7) tax corporations; and (8) certain foreign entities. *Id.*

142. Consequently, the Treasury refers to these entities as "eligible entities." Treas. Reg. § 301.7701-3(a) (as amended in 2006).

143. Treas. Reg. § 301.7701-2(a) (as amended in 2006).

144. *Id.* In the proposed regulations, the Treasury explained that some commentators suggested that the Treasury classify unincorporated organizations with a single owner as partnerships. Prop. Treas. Reg. §§ 301.7701-1 to -3, 61 Fed. Reg. 21989, 21991 (May 13, 1996). The Treasury, however, felt that "[b]ecause a fundamental characteristic of a partnership is the presence of associates, an entity with a single owner cannot conduct business as a partnership." *Id.*

145. The actual language of the regulation states that a business entity with only one owner can be classified as a corporation or disregarded, and then explains that if the entity is disregarded, it is treated the same as a sole proprietorship of the owner. Treas. Reg. § 301.7701-2(a) (as amended in 2006). For discussion regarding sole proprietorships, see 9 JASON B. BINIMOW, ET AL., MERTENS THE LAW OF FEDERAL INCOME TAXATION § 35A:05 (Supp. June 2007). The regulations allow an eligible entity to make an election by filing a properly completed Form 8832 and attaching a copy of the same to their federal income tax return for that year. Treas. Reg. §§ 301.7701-3(c)(1)(i), (ii) (as amended in 2006).

146. Treas. Reg. § 301.7701-3(b) (as amended in 2006).

147. Treas. Reg. § 301.7701-3(b)(3) (as amended in 2006).

148. *Id.*

149. Treas. Reg. § 301.7701-1(a)(1) (as amended in 2006).

150. *See* Rev. Rul. 70-101, 1970-1 C.B. 278 (containing a complete list of courts that invalidated the 1965 amendments to the Treasury regulations).

tence of a business entity recognized as an entity separate from its owner under state law.[151]

In general, states and business owners have accepted the check-the-box regulations as a proper solution to the entity classification problem.[152] Although the regulations have been generally well received, commentators maintain that they are invalid for two main reasons.[153] First, commentators suggest that the Treasury may have exceeded its authority by establishing a classification system based on something other than the corporate resemblance test.[154] Second, critics contend that the check-the-box regulations are invalid because they contradict federal statutes concerning employment tax liability.[155]

### *B. Employment Tax Liability*

Congress has enacted legislation making employers responsible for paying federal employment taxes.[156] Federal employment taxes include: (1) wage withholding taxes, (2) the employer's Federal Insurance Contributions Act (FICA) taxes, and (3) the employer's taxes due under the Federal Unemployment Tax Act (FUTA).[157] Congress has specified that liability for the payment of these employment taxes falls on the "employer" of each company's employees.[158]

For purposes of income tax withholdings and FUTA taxes, Congress has defined the "employer" to be "the *person* for whom an individual performs or performed any service . . . as the employee of such *person*,"[159] and "'any *person'* who paid a threshold amount of wages or employed at least one individual for a threshold number of days."[160]

151. Treas. Reg. §§ 301.7701-1(a)(1) to (4) (as amended in 2006).

152. Payson R. Peabody, *States Generally Endorse Check-the-Box but Key Issues Remain*, 87 J. TAX'N 228, 228 (1997).

153. *See infra* notes 154-155 and accompanying text.

154. *See* Susan Pace Hamill, *A Case for Eliminating the Partnership Classification Regulations*, 68 TAX NOTES 335, 337 n.15 (1995); Polsky, *supra* note 34, at 187-88.

155. Brant J. Hellwig & Gregg L. Polsky, *The Employment Tax Challenge to the Check-the-Box Regulations*, 111 TAX NOTES 1039, ¶ 3 (2006).

156. *See, e.g.*, I.R.C. §§ 3102(a), (b), 3111, 3301, 3402(a), 3403 (2000).

157. *See* I.R.C. §§ 3102(a), (b), 3402(a), 3403 (2000) (stating that employers are responsible for withholding from their employees' wages (1) the employees' appropriate income taxes, and (2) the taxes owed by the employees under FICA); I.R.C. §§ 3111, 3301 (2000).

158. I.R.C. § 3102(a) (2000) (FICA taxes "shall be collected by the employer of the taxpayer."); I.R.C. § 3102(b) (2000) ("Every employer required so to deduct the [FICA] tax shall be liable for the payment of such tax . . . ."); I.R.C. § 3111(a) (2000) (Under FICA, there is "imposed on every employer an excise tax, with respect to having individuals in his employ."); I.R.C. § 3301 (2000) (Under FUTA, there is "imposed on every employer . . . an excise tax, with respect to having individuals in his employ."); I.R.C. § 3402(a)(1) (2000) ("[E]very employer making payment of wages" is required to withhold the appropriate amount of income taxes from each of its employees.); I.R.C. § 3403 (2000) ("The employer shall be liable for the payment" of income tax withholdings.).

159. I.R.C. § 3401(d) (2000) (emphasis added).

160. Hellwig, *supra* note 155, ¶ 8 (emphasis added); I.R.C. § 3306(a)(1) (2000). Congress did not provide an express definition of the term "employer" for FICA tax purposes, but the definition of the term "employment" in that section describes the employer as "the person" that employs the employee. I.R.C. § 3121(b) (2000).

According to these statutes, the "employer" for employment tax purposes must be a "person."[161] Consequently, the definition of "person" is significant in the realm of employment tax liability.[162] Because Congress did not provide a specific definition of the term "person" for employment tax purposes, the default definition of the term found in Code section 7701(a)(1) governs.[163] Congress established that "[t]he term 'person' shall be construed to mean and include an individual, a trust, estate, partnership, association, company or corporation."[164]

Courts repeatedly have concluded that the list of entities that constitute a "person" is nonexclusive.[165] For example, the United States Court of Appeals for the Tenth Circuit recently held that the word "person" in section 7701(a)(1) "unambiguously encompasses all legal entities that are the subject of rights and duties."[166] The Tenth Circuit's conclusion is supported by the fact that the Treasury interprets the term "person" to include "an individual, a corporation, a partnership, a trust or estate, a joint-stock company, an association, or a syndicate, group, pool, joint venture, or other unincorporated organization or group."[167] In other words, the term "person" is broader than the tax classification terms such as "corporation" and "partnership," and encompasses anything recognized as a legal entity.[168]

With regard to wage withholding taxes, Congress has specified that the "employer" is to hold any funds collected for federal tax purposes from its employees in a special trust fund for the United States until they become due.[169] To ensure that employers accurately collect, report, and pay federal wage withholding taxes, and to deter misuse of properly withheld funds, Congress established penalties for employers that fail to properly collect or pay withholding taxes.[170] Code section

161. I.R.C. §§ 3306(a), 3401(d) (2000).

162. Hellwig, *supra* note 155, ¶ 9.

163. *See* Chickasaw Nation v. United States, 208 F.3d 871, 878 (10th Cir. 2000) ("Because neither § 4401 nor § 4411 defines the word "person," it is agreed we must rely on the [Code's] general 'Definitions' provision, [Code] § 7701."). This definition applies to all sections of the Code, except for those that expressly provide a different definition of the term. *See* I.R.C. § 7701(a) (2000) (stating that the definitions in this section apply "[w]hen used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof"). The position of this comment is that a disregarded entity is a "person" within the scope of Code § 7701(a)(1). This argument does not necessarily apply to those sections of the Code that expressly provide an alternative definition of the term "person." The author has not explored exactly how many sections of the Code rely on the definition of "person" provided in § 7701(a)(1).

164. I.R.C. § 7701(a)(1) (2000).

165. *See* Hellwig, *supra* note 155, ¶ 13 n.27 (providing a list of four cases that have held that the list is nonexclusive).

166. *Chickasaw Nation*, 208 F.3d at 880.

167. Treas. Reg. § 301.7701-6(a) (as amended in 1996).

168. *Chickasaw Nation*, 208 F.3d at 880.

169. I.R.C. § 7501(a) (2000).

170. I.R.C. § 7501(b) (2000) (stating that the penalties applicable to failure to collect or pay withholding taxes are found in Code §§ 6672 and 7202). When business owners struggle financially, they may be tempted to use the withholding trust funds as a source of short-term financing. Richard Daguanno, *Employee Withholding Taxes: Who is Responsible?*, 68 MICH. B.J. 496, 496 (1989). In

6672 provides that any person responsible for collecting, accounting for, and paying over any tax that willfully fails to do so will be "liable to a penalty equal to the total amount of the tax evaded."[171] Consequently, the IRS is able to assess responsible persons in their individual capacity for unpaid employment taxes if a business entity recognized as the "employer" is unable to pay its employment taxes.[172]

In 2004, the Supreme Court's decision in *United States v. Galletti*[173] further clarified who Congress intended to be the "employer" for employment tax purposes.[174] In *Galletti*, the Court held that where state law recognizes a business and its owners as separate entities, the business entity is the "employer," and therefore the "person" primarily liable for the payment of employment taxes.[175] In contrast to the Supreme Court's position in *Galletti*, the IRS does not look to state law to determine whether a business entity or the business's owner is the "employer" for employment tax purposes.[176] The IRS maintains that an entity disregarded for federal tax purposes cannot be the "employer" for federal employment tax purposes.[177] This position also conflicts with the Tenth Circuit's holding in *Chickasaw Nation v. United States*[178] because it implies that a disregarded entity cannot be a "person" within the scope of Code section 7701(a)(1).[179]

### *C. Administrative Law*

The Constitution vests Congress with "[a]ll legislative powers,"[180] as well as with the "[p]ower [t]o lay and collect [t]axes."[181] Pursuant to

fact, some business owners use the withholding funds to pay creditors or payroll with the hope of repaying the trust funds before they become due to the federal government. *Id.*

171. I.R.C. § 6672(a) (2000).

172. Daguanno, *supra* note 170, at 497. "The range of persons potentially subject to a section 6672 penalty, however, does not include the person who is required to collect, account for, and pay over the tax in the first place . . . ." Hellwig, *supra* note 155, ¶ 2 n.4; *see* Treas. Reg. § 301.6672-1 (as amended in 2001).

173. 541 U.S. 114 (2004).

174. *Id.* at 116. In this case, a general partnership failed to pay over $400,000 in federal employment taxes. *Id.* at 117. As a result, the IRS filed a timely assessment against the partnership, but not against the individual partners. *Id.* Code § 6501(a) requires the IRS to assess any deficiency within three years after the return was filed, and states that failure to do so precludes any action in court regarding the deficiency. The partners argued that the court should recognize them as "employers" liable for the payment of the unpaid taxes, and that the court should not permit the IRS to collect the taxes from them because it did not assess them individually. *Id.* at 117-18, 121-22. The Court rejected this argument, concluding that because California law recognizes a general partnership as an entity separate from the partners, the partnership is "the only relevant 'taxpayer' for purposes of §§ 6501-6502." *Id.* at 116.

175. *Id.* at 121.

176. *See* Kandi v. United States, No. C05-0840C, 2006 WL 83463, at *1 (W.D. Wash. Jan. 11, 2006).

177. Prop. Treas. Reg. § 301.7701-2, 70 Fed. Reg. 60475, 60475 (Oct. 18, 2005); I.R.S. Notice, *supra* note 7.

178. 208 F.3d 871 (10th Cir. 2000).

179. *See infra* notes 274-286 and accompanying text.

180. U.S. CONST. art. I, § 1.

181. U.S. CONST. art. I, § 8.

those powers, Congress has enacted laws to govern the taxation of both business entities and individuals.[182] Although Congress writes the federal tax statutes, the Treasury is primarily responsible for administering and executing such laws.[183] The Secretary of the Treasury has power to prescribe all rules and regulations necessary to enforce Title 26 of the United States Code, otherwise known as the Internal Revenue Code.[184] Regulations promulgated pursuant to this power are interpretive.[185] In contrast, regulations issued under specific statutory authority to define a particular term are legislative.[186] Whereas a legislative regulation is akin to a valid statute, interpretive regulations simply interpret previously enacted statutes, but are not law.[187]

Courts are often responsible for determining whether interpretive regulations are valid.[188] There has been much debate concerning the amount of deference courts should extend to the agency interpretations in federal regulations.[189] Until recently, courts had not applied a consistent standard for reviewing interpretive regulations.[190] Some courts deferred to agency interpretations while others independently interpreted the statutory language.[191] No court, however, had provided a clear explanation for selecting one method over the other.[192]

In 1984, the Supreme Court addressed this issue in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*,[193] establishing a two-step inquiry for reviewing agency regulations.[194] Based on this standard, the first inquiry a court must make is whether Congress has directly addressed the precise question at issue.[195] If Congress's intent is clear, the court need not give deference to the agency's interpretation because unambiguous federal statutes leave no room for agency discretion.[196] If, however, "Congress has not directly addressed the precise question at issue, the court" must defer to the agency's interpretation

182. 26 U.S.C. 22 (2000).

183. *See* U.S. CONST. art. II, § 1 (stating that the executive powers are vested in the President); 3 U.S.C. § 301 (2000) (authorizing the President to delegate executive authority to the head of any executive department or agency); 31 U.S.C. § 301(a)-(b) (2000) (stating that the Department of the Treasury is an executive department of the federal government); Ellen P. Aprill, *The Interpretive Voice*, 38 LOY. L.A. L. REV. 2081, 2081 (2005).

184. I.R.C. § 7805(a) (2000).

185. CWT Farms, Inc. v. Comm'r, 755 F.2d 790, 800 (11th Cir. 1985).

186. *Id.*

187. *Id.* (citing Batterton v. Francis, 432 U.S. 416, 425 (1977)); Costle, *supra* note 88, at 262 (citing Caterpillar Tractor Co. v. United States, 589 F.2d 1040, 1043 (Ct. Cl. 1978)).

188. *See* Littriello v. United States, 484 F.3d 372, 378 (6th Cir. 2007).

189. Costle, *supra* note 88, at 262.

190. Thomas W. Merrill, *Judicial Deference to Executive Precedent*, 101 YALE L.J. 969, 972 (1992).

191. *Id.*

192. *Id.*

193. 467 U.S. 837 (1984).

194. *Id.* at 842-43.

195. *Id.*; Aprill, *supra* note 183, at 2082.

196. *Chevron*, 467 U.S. at 842-43; Aprill, *supra* note 183, at 2082.

unless it is an impermissible construction of the statute.[197] The question the court must consider is not whether the regulations are the best possible solution, but whether the regulations are a reasonable interpretation of the federal statute.[198]

Courts continue to employ the *Chevron* test to determine whether interpretive agency regulations are valid.[199] Courts also use the *Chevron* test to determine how a judicial construction of a federal statute affects an agency's authority to promulgate subsequent regulations interpreting that statute.[200] In 2005, the Supreme Court in *National Cable & Telecommunications Ass'n v. Brand X Internet Services*[201] clarified how a court should evaluate agency regulations that conflict with a prior judicial statutory construction.[202] The Court explained that a judicial construction of a statute precludes subsequent interpretive agency regulations only if the construing court concluded that the statute was unambiguous and thus left "no room for agency discretion."[203] On the other hand, if the original court did not find the federal statute to be unambiguous, the reviewing court is to defer to the agency's interpretation so long as it is a permissible interpretation of the statute.[204]

Many tax cases involve and expose various issues of administrative law particularly well.[205] One administrative law issue raised in tax law is what amount of deference courts should extend to the IRS's interpretation of its own valid regulations.[206] In 1945, the Supreme Court in *Bowles v. Seminole Rock & Sand Co.*[207] explained that when an agency interprets its own ambiguous regulation, courts should defer to the agency's interpretation unless clearly erroneous or inconsistent with the regulation.[208] The Supreme Court in *Auer v. Robbins*[209] used the

197. *Chevron*, 467 U.S. at 842-43; Aprill, *supra* note 183, at 2082.

198. *Chevron*, 467 U.S. at 842-43; Aprill, *supra* note 183, at 2082.

199. *See* Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 982, 986 (2005); Littriello v. United States, 484 F.3d 372, 377 (6th Cir. 2007).

200. *Nat'l Cable*, 545 U.S. at 982.

201. 545 U.S. 967 (2005).

202. *Id.* at 982.

203. *Id.* This is significant because Littriello argued that the Supreme Court's decision in *Morrissey* should have precluded the Treasury from promulgating any additional regulations to interpret Code § 7701. Final Brief of Appellant, *supra* note 20, at 18. As the Sixth Circuit noted, however, the *Morrissey* Court acknowledged that Code § 7701 was ambiguous. *See Littriello*, 484 F.3d at 377-78. Therefore, according to *National Cable*, the Treasury was permitted to promulgate the check-the-box regulations. *See Nat'l Cable*, 545 U.S. at 982. Basically, the Court in *National Cable* reaffirmed that unless a court concludes that interpretive regulations fail the first step of *Chevron*, the court must defer to the regulations. *Id.* at 982-83.

204. *See id.* at 986.

205. Aprill, *supra* note 183, at 2083-84.

206. *See* Auer v. Robbins, 519 U.S. 452, 461 (1997); Bowles v. Seminole Rock & Sand Co., 325 U.S. 410, 413-14 (1945).

207. 325 U.S. 410 (1945).

208. *Id.* at 413-14 ("Since this involves an interpretation of an administrative regulation a court must necessarily look to the administrative construction of the regulation if the meaning of the words used is in doubt. The intention of Congress or the principles of the Constitution in some situations may be relevant in the first instance in choosing between various constructions. But the ultimate criterion is the administrative interpretation, which becomes of controlling weight unless it is plainly

"plainly erroneous or inconsistent" test to determine whether an agency's interpretation of its own ambiguous regulation was acceptable.[210] Consequently, the Supreme Court now refers to this test as "*Auer* deference."[211] In 2000, the Supreme Court in *Christensen v. Harris County*[212] clarified that when an interpretive regulation is unambiguous, an agency's interpretation is not entitled to *Auer* deference.[213] Rather, in such cases courts are to respect agency interpretations only to the extent that they have the "power to persuade."[214]

## IV. COURT'S DECISION

*Littriello v. United States* presented the first opportunity for a court to address whether the check-the-box regulations are valid, whether they apply to employment taxes, and whether a disregarded entity can be the "employer" for employment tax purposes.[215] In *Littriello*, the Sixth Circuit, operating under the assumption that the first issue was determinative of the other two, focused primarily on addressing the validity of the regulations under the *Chevron* analysis.[216] After considering the parties' arguments, the court held that the check-the-box regulations were valid and applicable to employment taxes.[217] The court also held that the owner of a disregarded LLC was the "employer" for employment tax purposes.[218]

Littriello first contended that the check-the-box regulations were invalid because they failed the first step of the *Chevron* test.[219] He argued that the *Morrissey* holding had been incorporated into the definitions provided in Code section 7701 and effectively eliminated any am-

erroneous or inconsistent with the regulation. . . . Our only tools, therefore, are the plain words of the regulation and any relevant interpretations of the Administrator.").

209. 519 U.S. 452 (1997).

210. *Id.* at 461; *see* Robertson v. Methow Valley Citizens Council, 490 U.S. 332, 359 (1989) (applying the clearly erroneous or inconsistent test).

211. *See* Christensen v. Harris County, 529 U.S. 576, 588 (2000) ("*Auer* deference is warranted only when the language of the regulation is ambiguous.").

212. 529 U.S. 576 (2000); *see infra* text accompanying note 290.

213. *Christensen*, 529 U.S. at 588.

214. *Id.* at 587 (quoting Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944)). The IRS seems to agree that it does not have authority to interpret its own regulation in a way that conflicts with the plain language of the regulation. *See* I.R.S. Notice, CC-2003-014 (2003) ("[O]ur litigation positions should be derived from, and consistent with, the Internal Revenue Code and our published guidance.").

215. Littriello v. United States, 484 F.3d 372, 374, 376 (6th Cir. 2007). Judge Daughtrey, writing for the Sixth Circuit, described Littriello's case as one "of first impression regarding the validity of the . . . 'check-the-box' regulations." *Id.* at 374. The court acknowledged, as an afterthought, that "Littriello also contends that the regulations do not apply to employment taxes . . . ." *Id.* at 376.

216. *Id.* at 376-79. The court apparently assumed that if the check-the-box regulations were valid, they unquestionably applied to employment tax liability. *See id.* at 376. The court stated that Littriello's argument that the regulations did not apply to employment taxes depended on proposed amendments to the check-the-box regulations, suggesting that without the proposed amendments the check-the-box regulations indisputably applied to employment taxes. *Id.*

217. *Id.* at 378.

218. *Id.*

219. Final Brief of Appellant, *supra* note 20, at 18.

biguity that may have previously existed within the statute.[220] Therefore, reasoned Littriello, the Supreme Court's ruling in *Morrissey* precluded any subsequent agency interpretation of Code section 7701.[221] In response, the government asserted that the Supreme Court had directly rejected Littriello's argument in *National Cable*.[222] The government also argued that section 7701 was ambiguous because the definitions of "corporation" and "partnership" overlapped.[223] Agreeing with the government, the Sixth Circuit explained that because the *Morrissey* Court found the definitions ambiguous, the holding in *Morrissey* did not preclude the Treasury from promulgating the check-the-box regulations.[224] The Sixth Circuit concluded that section 7701 was ambiguous when applied to business entities such as Littriello's LLC, and therefore, the regulations passed the first step of the *Chevron* analysis.[225]

Littriello also argued that the Treasury regulations represented an unreasonable interpretation of Code section 7701, and therefore failed the second step of the *Chevron* test.[226] He claimed the regulations were unreasonable for three reasons.[227] First, Littriello maintained that the regulations were unreasonable and invalid because they allowed certain business entities, uniquely classifiable under the corporate resemblance test, to elect an alternative classification.[228] Next, he claimed that the check-the-box regulations were unreasonable because they allowed the IRS to disregard the separate existence of a business entity despite state statutes that expressly provide that the organization is an entity separate from its owner.[229] Finally, Littriello argued the check-the-box regulations were invalid because they created a new method of collecting unpaid employment taxes from business owners.[230] This was unreasonable, contended Littriello, because Congress intended Code section

220. *Id.*

221. *Id.* at 19. Littriello relied on *Neal v. United States*, 516 U.S. 284 (1996), *Maslin Industries United States Inc. v. Primary Steel Inc.*, 497 U.S. 116 (1990), and *Lechmere Inc. v. NLRB*, 502 U.S. 527 (1992) as authority for this argument. Final Brief of Appellant, *supra* note 20, at 18 n.1.

222. Final Brief for the Appellees, *supra* note 16, at 22.

223. *Id.* at 27-28.

224. Littriello v. United States, 484 F.3d 372, 377-78 (6th Cir. 2007) ("[A] court's prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference *only if* the prior court decision holds that its construction follows from the *unambiguous* terms of the statute and thus leaves no room for agency discretion." (quoting Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs., 545 U.S. 967, 982 (2005))) (emphasis added in *Littriello*).

225. *Id.* at 378.

226. Final Brief of Appellant, *supra* note 20, at 11, 15, 29.

227. *Id.*

228. *Id.* at 11.

229. *Id.* at 15. Littriello contended that the Treasury did not have authority to hold the owner of a Kentucky, single-member LLC liable for the company's unpaid employment taxes because the Kentucky Limited Liability Company Act "specifically provides that a member of a limited liability company is not liable for its debts." *Id.* at 21. He relied on *Galletti,* Rev. Rul. 2004-41, 2004-1 C.B. 846, and the proposed amendments to the check-the-box regulations to show that the federal government must acknowledge state statutes in classifying business entities for tax purposes. Final Brief of Appellant, *supra* note 20, at 24.

230. *Id.* at 29.

6672 to be the sole recourse available to the IRS for collecting unpaid employment taxes.[231] He asserted that "[Code section] 6672 is Congressional recognition that there is no other procedure available to reach an individual 'responsible person' on the employer's failure to remit collected or uncollected employment taxes when the employer and the 'responsible person' have separate legal identities."[232] The Sixth Circuit rejected Littriello's arguments, found the check-the-box regulations "eminently reasonable," and affirmed the validity of the regulations.[233]

Littriello argued alternatively that even if the Treasury regulations were valid, they did not apply to employment taxes.[234] The government maintained that the regulations expressly applied to "*all* federal tax purposes," a phrase that encompasses federal employment taxes.[235] Littriello argued, however, that wage withholding taxes are not taxes owed by the employer to the federal government.[236] Rather, contended Littriello, they are trust funds owed by the employer to the government under a debtor/creditor relationship.[237] Therefore, Littriello argued that collecting and distributing employment taxes for the federal government is not a "federal tax purpose" governed by the check-the-box regulations.[238] The Sixth Circuit stated that this argument depended on the relevance of proposed amendments to the check-the-box regulations.[239] The court concluded that because they were not final regulations, it could not accept the proposed amendments as the current policy accepted by the Treasury regarding this issue.[240] Additionally, the court emphasized that the purpose of the proposed regulations was simply to improve the administrative procedures for collecting employment taxes.[241] Consequently, the court concluded that the Treasury did not intend to endorse Littriello's litigation position with the proposed regulations.[242] Therefore, the Sixth Circuit held that the check-the-box regulations did apply to employment taxes.[243]

231. *Id.* at 26.
232. *Id.*
233. Littriello v. United States, 484 F.3d 372, 378 (6th Cir. 2007).
234. Final Brief of Appellant, *supra* note 20, at 20.
235. Final Brief for the Appellees, *supra* note 16, at 49.
236. Final Brief of Appellant, *supra* note 20, at 20.
237. *Id.*
238. *Id.*
239. Littriello v. United States, 484 F.3d 372, 376 (6th Cir. 2007).
240. *Id.* at 379.
241. *Id.*
242. *Id.*
243. *Id.* at 380. On August 16, 2007, the Treasury finalized the amendments to the check-the-box regulations. Disregarded Entities; Employment and Excise Taxes, 72 Fed. Reg. 45,891 (Aug. 16, 2007). The Treasury summarizes the new regulations as follows:

> [T]he final regulations provide that a disregarded entity is treated as a separate entity for purposes of employment taxes and related reporting requirements. The final regulations clarify that the separate entity is treated as a corporation for purposes of employment taxes and related reporting requirements. As provided in the proposed regulations, a disregarded entity continues to be disregarded for other Federal tax purposes.

After concluding that the regulations were valid, the Sixth Circuit extended complete deference to the IRS's conclusion that a disregarded entity, such as Littriello's LLC, cannot be an "employer" for employment tax purposes.[244] The court did not discuss whether the regulations were ambiguous or silent regarding this issue.[245] Nor did the court examine the IRS's interpretation of its own regulations under the lens of *Auer* or *Christensen*.[246]

## V. COMMENTARY

When reviewing agency regulations and other interpretations of federal statutes, courts often defer to an agency's interpretation.[247] The amount of deference a court should extend to an agency depends on the subject of judicial review.[248] When reviewing an official agency regulation, a court should generally extend *Chevron* deference to the agency's interpretation of federal statutes.[249] When the subject of judicial review is an agency's interpretation of its own regulation, however, *Chevron* deference is unwarranted.[250] In the latter scenario, courts should review an agency's interpretation of its own regulation according to *Auer* if the regulation is ambiguous, or *Christensen* if it is unambiguous.[251]

*Littriello v. United States* presented two considerable issues to the Sixth Circuit: (1) whether the check-the-box regulations are valid; and (2) whether the IRS's position that a disregarded entity cannot be the "employer" for employment tax purposes is reasonable.[252] The first is-

*Id.* The Treasury reiterated that the regulations are intended to "improve administration of the Federal tax laws and simplify the Federal tax compliance with respect to reporting, payment, and collection of employment taxes." *Id.* at 45,892. Therefore, it is unclear if the Sixth Circuit, or any other court that has issued a ruling on this matter, would rule differently concerning the applicability of the regulations to employment taxes in light of the new regulations. The court could rule that the regulations are still applicable for all "federal tax purposes," and that the amendments simply change how they apply to employment taxes. Treas. Reg. §§ 301.7701-1(a), -3(a) (as amended in 2006). Although under the new regulations Littriello would not be personally liable for paying federal employment taxes, the regulations do not resolve the flaw in *Littriello*. Rather than conclude that a disregarded entity is a "person" and therefore can be the "employer" for employment tax purposes, the new regulations provide that disregarded entities are not disregarded for employment tax purposes. Disregarded Entities; Employment and Excise Taxes, 72 Fed. Reg. at 45,891. Furthermore, for employment taxes the regulations only apply to wages paid after January 1, 2009. *Id.* at 45,892. Therefore, the IRS could arguably continue holding the owners of disregarded LLCs personally liable for employment taxes until after 2009, when it stops treating disregarded entities as such for employment tax purposes. *See id.*

244. By concluding that Littriello was directly liable for the unpaid employment taxes, the court implied that he, and not his disregarded LLC, was the "employer." *Littriello*, 484 F.3d at 378.

245. *See generally id.*

246. *See generally id.*

247. Daniel Riesel & Elizabeth Knauer, *Obtaining Effective Judicial Review of Federal Agency Action in the Environmental Context*, SM092 A.L.I.-A.B.A. 97, 115 (2007).

248. *Id.* at 100-01.

249. Christensen v. Harris County, 529 U.S. 576, 587 (2000) ("[T]he framework of deference set forth in *Chevron* does apply to an agency interpretation contained in a regulation.").

250. *Id.*

251. *Id.* at 588.

252. Littriello v. United States, 484 F.3d 372, 374 (6th Cir. 2007).

sue deals with the validity of the check-the-box regulations and is a question of entity classification.[253] To address this issue, courts should analyze the regulations and the federal statutes that govern entity classification through the lens of *Chevron*.[254] The second issue, on the other hand, deals with the Treasury's interpretation of the check-the-box regulations and is a question of employment tax liability.[255] Therefore, to address this issue adequately, a court should examine the regulations and the Treasury's interpretation of the regulations that relate to employment tax liability according to *Auer* or *Christensen*.[256]

In *Littriello*, rather than recognize and address both issues, the Sixth Circuit framed the case as if the validity of the check-the-box regulations were the only issue worthy of analysis.[257] Accordingly, the court applied the *Chevron* test, and upheld the validity of the check-the-box regulations.[258] Rather than look beyond *Chevron* to consider the persuasiveness of the IRS's stance, the court simply deferred to the IRS's position that, because it was a disregarded entity, Littriello's LLC could not be the "employer" for employment taxes.[259] The *Chevron* test does not apply to this issue, however, because the regulations are silent on whether a disregarded entity can be the "employer" for employment tax purposes.[260] Besides addressing *Chevron*, the court should have analyzed the IRS's position concerning disregarded entities under *Christensen*.[261] An analysis of the plain language of the Treasury regulations

253. The real question concerning the validity of the regulations is whether it is reasonable for the Treasury to allow certain business entities to elect how to be classified, or whether Congress has clearly specified how all business entities should be classified. *Id.* at 378 (stating that Congress had not clearly specified how entities should be classified and that the check-the-box regulations were reasonable).

254. *Christensen*, 529 U.S. at 587 (stating that *Chevron* is the correct standard for reviewing the validity of agency regulations).

255. *Littriello*, 484 F.3d at 374. The real question was whether Littriello's LLC could be liable for its unpaid employment taxes even though it was disregarded for federal tax purposes under the check-the-box regulations. *See id.*

256. *See Christensen*, 529 U.S. at 587-88; Auer v. Robbins, 519 U.S. 452, 461 (1997). *But see* Edelman v. Lynchburg Coll., 535 U.S. 106, 114 (2002) ("Because we so clearly agree with the EEOC, there is no occasion to defer and no point in asking what kind of deference, or how much."). Even prior to considering the Treasury's interpretation of its regulation, the court should determine whether the sections of the regulations that relate to employment tax liability statutes are valid under *Chevron*. *Christensen*, 529 U.S. at 587. In this case, the court should have examined Treas. Reg. § 301.7701-6(a), which includes an interpretation of the term "person." Treas. Reg. § 301.7701-6(a) (as amended in 1996). For purposes of this comment, the author assumes that if the court had done so, it would have concluded that the regulations were valid under *Chevron*.

257. *See Littriello*, 484 F.3d at 374.

258. *Id.* at 378. For purposes of this comment, the author assumes that the court's analysis and conclusion of this issue was correct.

259. *Id.* ("[T]he plaintiff's failure to make an election under the 'check-the-box' provision dictates that his companies be treated as disregarded entities under those regulations . . . he is, therefore, liable individually for the employment taxes due and owing from those businesses because they constitute sole proprietorships under § 7701, and he is the proprietor.").

260. *See Christensen*, 529 U.S. at 587-88 (explaining that because the relevant regulations did not expressly address the issue, and because the regulations were otherwise unambiguous, deference was unwarranted under *Chevron* and *Auer*).

261. *See id.* (stating that *Chevron* was not the correct test because the regulations did not address the issue under review).

and the Tenth Circuit's decision in *Chickasaw Nation* reveals that the IRS's position does not warrant judicial deference under this approach.

### *A. Treasury's Interpretation of "Person"*

Congress has directly stated that employment tax liability rests with the "employer," which is the "person" for whom employees perform services in return for compensation.[262] Therefore, the IRS's position presupposes that a disregarded entity is not a "person" within the scope of Code section 7701(a)(1).[263] If a disregarded LLC is a "person," it is arbitrary and capricious for the IRS to conclude that it cannot be the "employer" and be liable for federal employment taxes.[264] Thus, to determine whether it is reasonable for the IRS to conclude that a disregarded LLC cannot be the "employer" within the scope of employment tax statutes, courts should examine the interpretation of the term "person" included in the Treasury regulations.[265]

The plain language of the regulations provides that the term "person" includes "an individual, a corporation, a partnership, a trust or estate, a joint-stock company, an association, or a syndicate, group, pool, joint venture, or other unincorporated organization or group."[266] An LLC is undeniably an unincorporated organization.[267] This is no less true for an LLC disregarded for federal tax purposes.[268] Therefore, according to the plain language of the regulation, a disregarded LLC falls within the definition of "person."[269]

Additionally, joint-stock companies, associations, syndicates, groups, pools, joint ventures, and unincorporated organizations are not tax classifications, but literal classifications.[270] The statutory definition of a tax partnership includes syndicates, groups, pools, joint ventures, and unincorporated organizations.[271] Likewise, the statutory definition of a tax corporation includes associations and joint-stock companies.[272] The fact that the Treasury specifically enumerated these non-tax entities

262. *See, e.g.*, I.R.C. §§ 3102(a), (b) (2000) (stating that the employer is responsible for collecting employment taxes); I.R.C. § 3306(a)(1) (2000) (defining employer to mean any person that meets certain requirements).

263. *See* I.R.S. Notice, *supra* note 7, at 12.

264. *See* I.R.C. §§ 3102(a), (b) (2000) (stating that the employer is responsible for collecting employment taxes); I.R.C. § 3306(a)(1) (2000) (defining employer as a person); 5 U.S.C. § 706(2)(A) (2000).

265. *See, e.g.*, I.R.C. §§ 3102(a), (b) (2000) (stating that the employer is responsible for collecting employment taxes); I.R.C. § 3306(a)(1) (2000) (defining employer as a person).

266. Treas. Reg. § 301.7701-6(a) (as amended in 1996).

267. LLCs are not state law corporations. If this were not true, all LLCs would have to be classified as tax corporations. *See* Treas. Reg. § 301.7701-2(b)(1) (as amended in 2006).

268. An LLC does not become a corporation when it is disregarded for federal tax purposes. *See* I.R.C. § 7701(a)(3) (2000).

269. Treas. Reg. § 301.7701-6(a) (as amended in 2006).

270. I.R.C. §§ 7701(a)(2), (3) (2000).

271. I.R.C. § 7701(a)(2) (2000).

272. I.R.C. § 7701(a)(3) (2000).

in the regulation suggests that an entity's actual classification, not its tax classification, dictates whether it is a "person" within the meaning of Code section 7701.[273] The Tenth Circuit's decision in *Chickasaw Nation* supports this conclusion.[274]

### *B. Chickasaw Nation v. United States*

Code Section 7701(a)(1) states that the term "person" means "an individual, a trust, estate, partnership, association, company or corporation."[275] Several courts have concluded that Congress intended this list to be nonexclusive.[276] As mentioned above, the Treasury regulations support this position by providing that the term "person" includes unincorporated organizations.[277]

In *Chickasaw Nation*, the Tenth Circuit examined whether an Indian Tribe was a "person" within the meaning of section 7701(a)(1).[278] The court stated that this issue turned on statutory construction and required the court to determine congressional intent.[279] The court explained that because Congress prefaced the definition of the term "person" with the word "include" courts should not construe the list of entities contained in section 7701(a)(1) to be exhaustive.[280] To determine whether Congress intended Indian organizations to fall within the scope of section 7701(a)(1), the court looked to the dictionary, which defines "person" to include "a human being, a body of persons, or a corporation, partnership, or other legal entity that is recognized by law as the subject of rights and duties."[281] Therefore, the Tenth Circuit found that "Congress unambiguously intended for the word 'person' . . . to encompass all legal entities . . . that are the subject of rights and duties," and concluded that an Indian Tribe was a "person" because it was a legal entity recognized by law as the subject of rights and duties.[282]

The Tenth Circuit's holding is not limited to entities recognized by the IRS for federal tax purposes.[283] Rather, it extends to all legal entities, regardless of their federal tax classifications, which are the subject

273. *See supra* notes 165-168 and accompanying text.
274. Chickasaw Nation v. United States, 208 F.3d 871, 879-80 (10th Cir. 2000).
275. I.R.C. § 7701(a)(1) (2000).
276. *See Chickasaw Nation*, 208 F.3d at 879 (concluding that the definition of "person" includes Indian tribes); Estate of Wycoff v. Comm'r, 506 F.2d 1144, 1151 (10th Cir. 1974) (finding the definition of "person" to include individual states and the United States).
277. Treas. Reg. § 301.7701-6(a) (as amended in 2006).
278. *Chickasaw Nation*, 208 F.3d at 879.
279. *Id.* at 878.
280. *Id.* Congress provided that "[t]he terms 'includes' and 'including' when used in a definition contained in this title shall not be deemed to exclude other things otherwise within the meaning of the term defined." I.R.C. § 7701(c) (2000).
281. *Chickasaw Nation*, 208 F.3d at 879 (quoting WEBSTER'S THIRD NEW INT'L DICTIONARY 1686).
282. *Id.*
283. *See id.*

of rights and duties.[284] An LLC is a legal entity that is the subject of rights and duties.[285] Applying the Tenth Circuit's rationale, a disregarded LLC is a "person" within the meaning of section 7701(a)(1).[286] Yet, two circuit courts and a federal district court have each implicitly concluded otherwise by completely deferring to the IRS's position regarding disregarded entities.[287] Unfortunately, none of these courts considered the definition of "person" or addressed whether the IRS's interpretation of its regulations was reasonable or persuasive.[288] Because the regulations are silent on the issue, courts should not extend *Chevron* deference to the IRS's position that a disregarded LLC cannot be the "employer" for employment tax purposes.[289] Rather, courts should examine the term "person" and only defer to the IRS's position according to its "power to persuade" as established in *Christensen*.[290] Using this approach, courts will likely conclude that the Treasury's position is unpersuasive and find that a disregarded LLC is a "person" within in the scope of section 7701(a)(1), and therefore can be the "employer" for employment tax purposes.[291]

### *C. Whether a Disregarded LLC is the "Employer"*

Finding that a disregarded LLC is a "person" does not require a

284. *Id.*

285. *See, e.g.*, COLO. REV. STAT. § 7-80-104 (amended 2006); Kansas Limited Liability Act, ch. 80 §§ 3-4, 1990 Kan. Sess. Laws 585-86.

286. *See Chickasaw Nation*, 208 F.3d at 879.

287. *See* McNamee v. Dep't of the Treasury, 488 F.3d 100, 110 (2d Cir. 2007); Littriello v. United States, 484 F.3d 372, 378 (6th Cir. 2007) (validating the check-the-box regulations and concluding that the owner of a single-member LLC was the "employer" for employment tax purposes); Kandi v. United States, No. C05-0840C, 2006 WL 83463, at *5 (W.D. Wash. Jan. 11, 2006).

288. *See generally McNamee*, 488 F.3d 100; *Littriello*, 484 F.3d 372; *Kandi*, 2006 WL 83463.

289. Christensen v. Harris County, 529 U.S. 576, 587-88 (2000).

290. *Id.* at 587 (quoting Skidmore v. Swift & Co., 323 U.S. 134, 140 (1944)). In *Christensen*, the Court examined whether a policy adopted by Harris County violated the Fair Labor Standards Act (FLSA). *Id.* at 578. The Harris County policy established a maximum number of compensatory hours county employees could accumulate. *Id.* at 581. The Court focused on a provision of the county policy that authorized supervisors to require county employees to use their compensatory time once they approached the maximum number of hours. *Id.* The petitioners argued that this provision of the policy violated the FLSA. *Id.* The primary authority for the petitioners' position was an opinion letter from the Department of Labor addressing the issue for Harris County. *Id.* The United States, as amicus curiae, argued that the Court should extend *Chevron* deference to the position contained in the opinion letter. *Id.* at 582, 586. In response, the Court explained that agency interpretations arrived at without public notice and comment do not warrant *Chevron* deference, but are "entitled to respect" according to their "power to persuade." *Id.* at 587 (quoting *Skidmore*, 323 U.S. at 140). The United States also contended that the Supreme Court's decision in *Auer* required the Court to defer to the opinion letter, because it was the Department of Labor's interpretation of its own regulation. *Id.* at 588. The Court explained, however, that an agency's interpretation of its own regulation is only entitled to *Auer* deference if the regulation is ambiguous. *Id.* Because the agency regulation was unambiguous in general, and silent regarding the specific issue, the Court did not extend deference to the Department of Labor's interpretation of the FLSA. *Id.* After clarifying the doctrines of judicial deference, the Court concluded that the FLSA did not have to expressly authorize policies such as the one adopted by Harris County. *Id.* Unless the FLSA expressly prohibited Harris County from adopting its policy, explained the Court, the policy was not a violation of the FLSA. *Id.*

291. *See Chickasaw Nation*, 208 F.3d at 879.

court to conclude that the disregarded LLC is *the* "employer" liable for employment taxes.[292] Because the definition of "person" also includes an individual, it appears on the surface that Congress intended for either a disregarded LLC or its owner to qualify as the "person" subject to employment tax liability.[293] Courts can resolve this issue by addressing the Supreme Court's decision in *Galletti*.[294] The Supreme Court in *Galletti* explained that where state law recognizes a business organization and its owners as separate entities, the business entity is *the* "employer" and, therefore, is the "person" liable for the company's employment taxes.[295] Similar to the Tenth Circuit's holding in *Chickasaw Nation*, the *Galletti* holding is not limited to entities recognized for federal tax purposes.[296] Therefore, because state laws recognize a disregarded LLC as an entity separate from its owner, the disregarded LLC is *the* "employer" for employment tax purposes.[297]

### *D. Additional Authority*

The Sixth Circuit summarily concluded that several sources of authority were irrelevant and inapplicable to Littriello's case because none of them dealt specifically with a disregarded entity.[298] The court, however, based its conclusion on the presumption that a disregarded entity is not a "person" for employment tax purposes.[299] After a court recognizes a disregarded LLC as a "person," cases and other persuasive authority the court may have previously considered irrelevant become very applicable. For example, the Sixth Circuit concluded that the holding in *Galletti*—that a business entity is the "employer" where state law recognizes the business and its owner as separate legal entities—was inapplicable to *Littriello*.[300] After recognizing that a disregarded LLC is a "person" and can be the "employer" for employment tax purposes, however, *Galletti* clearly dictates that a disregarded LLC is the "employer" for federal employment taxes.[301]

Similarly, Revenue Ruling 2004-41 provides that the IRS must look to state law to determine whether the owners of an LLC are liable for employment taxes.[302] The Sixth Circuit completely disregarded this rul-

292. *See* Hellwig, *supra* note 155, ¶ 15.
293. *Id.*; Treas. Reg. § 301.7701-6(a) (as amended in 1996).
294. United States v. Galletti, 541 U.S. 114, 116 (2004); Treas. Reg. § 301.7701-6(a) (as amended in 1996); Hellwig, *supra* note 155, ¶ 15.
295. *Galletti*, 541 U.S. at 116.
296. *See id.*
297. *See id.*
298. Littriello v. United States, 484 F.3d 372, 378-79 (6th Cir. 2007).
299. *Id.*
300. *Id.* The court also rejected Littriello's reliance on *People Place Auto Hand Carwash, LLC v. Commissioner*, 126 T.C. 359 (2006). *Id.*
301. *See Galletti*, 541 U.S. at 116.
302. Rev. Rul. 2004-41, 2004-1 C.B. 845, 846.

ing, which states:

> If under state law the members of the LLC are not liable for the debts of the LLC, then absent fraudulent transfers or other special circumstances, the IRS may not collect the LLC's employment tax liability from the members, including by levy on the property and rights to property of the members.[303]

The IRS's position indicates that state law governs whether an entity may be directly subject to employment tax liability.[304] Although the ruling specifically addresses whether the owners of a multi-member LLC can be liable for unpaid employment taxes, after determining that a disregarded LLC is a "person," courts should find the ruling equally applicable to a disregarded single-member LLC.[305] It would be unreasonable to conclude that the IRS's holding is irrelevant to certain LLCs solely because the government classifies them as disregarded entities for federal tax purposes.[306]

This revenue ruling also suggests that the IRS does not look to an entity's tax classification to determine employment tax liability.[307] In arriving at its conclusion, the IRS did not rely on the entity classification of the multi-member LLC, but on its rights and duties specified by state law.[308] By default, the IRS classifies multi-member LLCs as partnerships for federal tax purposes.[309] Partnerships, like disregarded LLCs, are not recognized as entities separate from their owners.[310] The IRS concluded, however, that notwithstanding its tax classification as a partnership, a multi-member LLC could not be liable for employment tax purposes because of state law.[311] In addressing this issue, courts should consider this revenue ruling and promote consistent, rather than arbi-

303. *Id.* Although Littriello relied on this revenue ruling in his brief, the Sixth Circuit did not even mention it in its opinion.

304. *Id.* This could help persuade a court to follow *Chickasaw Nation*, and conclude that a "person" is any entity that is subject to rights and duties under state law. *See* Chickasaw Nation v. United States, 208 F.3d 871, 879 (10th Cir. 2000).

305. *See* Rev. Rul. 2004-41, 2004-1 C.B. 845.

306. *See id.* Several courts have explained that although a revenue ruling is not binding on the court, the IRS may not assume a litigation position contrary to a relevant revenue ruling. *See* Estate of McLendon v. Comm'r, 135 F.3d 1017, 1024-25 (5th Cir. 1998) (holding that a revenue ruling governed the case because of Treas. Reg. section 601.601(e), which "provides that taxpayers may generally rely on published revenue rulings in determining the tax treatment of their own transactions, if the facts and circumstances of their transactions are substantially the same as those that prompted the ruling"); Transco Exploration Co. v. Comm'r, 949 F.2d 837, 840 (5th Cir. 1992) (stating that the Commissioner could not take a position that conflicted with a previous private-letter ruling); Rauenhorst v. Comm'r, 119 T.C. 157, 171 (2002) ("We agree . . . that revenue rulings are not binding on this Court, or other Federal courts for that matter. However, we cannot agree that the Commissioner is not bound to follow his revenue rulings in Tax Court proceedings." (internal citations omitted)).

307. *See* Rev. Rul. 2004-41, 2004-1 C.B. 845. This supports the argument that the definition of "person" included in the Treasury regulations looks to an entity's actual classification rather than its tax classification.

308. *See id.*

309. Treas. Reg. § 301.7701-3(b) (as amended in 2006).

310. Jeanne M. Whalen, Note & Comment, *Safekeeping Client Property: Why the ABA is Hands-Off and the States are Hand-Holding*, 38 U. TOL. L. REV. 1279, 1314 (2007).

311. *See* Rev. Rul. 2004-41, 2004-1 C.B. 845.

trary and capricious, rulings by the IRS.[312]

## VI. CONCLUSION

From the country's earliest days, states have had authority to create businesses and define their rights.[313] For nearly as long, the Treasury has attempted to usurp that authority.[314] Most recently, the Treasury challenged the states' authority to grant liability protection to business owners by promulgating the check-the-box regulations.[315] According to the Treasury, the check-the-box regulations provide that owners of certain LLCs may be directly liable for paying federal employment taxes despite state statutes expressly prohibiting such treatment.[316] The Treasury bases its position on the presumption that a disregarded LLC is not a "person," and therefore, cannot be the "employer" for federal employment taxes.[317] Thus far, when given the opportunity to consider the validity of the IRS's interpretation of the check-the-box regulations, courts have elected not to do so.[318] Courts have instead extended *Chevron* deference to the IRS's position.[319] In so doing, courts have failed to recognize the federal tax personality of disregarded LLCs. While *Chevron* is the correct standard for evaluating the validity of the check-the-box regulations, *Christensen* is the appropriate standard for examining the IRS's interpretation of its own unambiguous regulations.[320] Under this approach, deference to the IRS's position that a disregarded LLC is not a "person" is unwarranted because, in light of the authority discussed above, it lacks the "power to persuade."[321]

312. *See* 5 U.S.C. § 706 (2000). *Littriello*, like the other two cases that have addressed the check-the-box regulations, illustrates why courts should be hesitant to consider litigation positions submitted on behalf of an administrative agency that conflict with guidance previously published by that agency. In all three cases that have addressed the issue, the court considered the proposed regulations published by the Treasury in 2005, under which the owner of a disregarded LLC would not be liable for the company's employment taxes, and concluded that they did not represent the Treasury's current position on the issue. McNamee v. Dep't of the Treasury, 488 F.3d 100, 109-10 (2d Cir. 2007); Littriello v. United States, 484 F.3d 372, 379 (6th Cir. 2007); Kandi v. United States, No. C05-0840C, 2006 WL 83463, at *2-3 (W.D. Wash. Jan. 11, 2006). In conflict with the courts' conclusion, the Treasury finalized those regulations on August 16, 2007. Disregarded Entities; Employment and Excise Taxes, 72 Fed. Reg. 45,891 (Aug. 16, 2007).

313. Hamill, *supra* note 1, at 1485.

314. *See supra* Part III.A.

315. *See* Simplification of Entity Classification Rules, 61 Fed. Reg. 66584, 66589 (Dec. 18, 1996) (codified at Treas. Reg. §§ 301.7701-1 to -3).

316. *See* I.R.S. Notice, *supra* note 7, at 12.

317. *See id.*; Prop. Treas. Reg. § 301.7701-1 to -3, 70 Fed. Reg. 60475, 60475 (Oct. 18, 2005).

318. *See generally* McNamee v. Dep't of the Treasury, 488 F.3d 100 (2d Cir. 2007); Littriello v. United States, 484 F.3d 372 (6th Cir. 2007) Kandi v. United States, No. C05-0840C, 2006 WL 83463 (W.D. Wash. Jan. 11, 2006).

319. *Littriello*, 484 F.3d at 378; *McNamee*, 488 F.3d at 109.

320. Christensen v. Harris County, 529 U.S. 576, 587-88 (2000).

321. *Id.*