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## Omnibus Taxpayers' Bill of Rights Act: Taxpayers' Remedy or Political Placebo?

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## Omnibus Taxpayers' Bill of Rights Act: Taxpayers' Remedy or Political Placebo?

Thomas Treadway lived with his girlfriend, Shirley Lojeski, on her Pennsylvania farm. The Internal Revenue Service (IRS) audited Treadway for tax-years 1977 through 1980 and determined that he owed \$247,000 in back taxes, penalties, and interest.<sup>1</sup> Fearing that collection of this sum was uncertain, the IRS brought a jeopardy<sup>2</sup> and termination<sup>3</sup> assessment against Treadway,<sup>4</sup> allowing an immediate seizure of his property. Believing further that Treadway had transferred assets to Lojeski, a Revenue Officer also filed a lien on Lojeski's farm and levied on her bank account.<sup>5</sup>

On administrative appeal, Treadway recovered the \$247,000, but his battle with the IRS exacted a heavy toll: Treadway incurred \$75,000 in legal and accounting fees and lost both his job and virtually all his assets in the process.<sup>6</sup> Lojeski paid over \$30,000 in such fees<sup>7</sup> and claimed damages (which were not recovered) arising from the threatened foreclosure on her farm, the lost opportunity to sell the farm, the suspension of her horse breeding business, and other wrongful IRS actions.<sup>8</sup>

Treadway and Lojeski's horror stories, along with many others, prompted Senator David Pryor (D.-Ark) to introduce the Omnibus Taxpayers' Bill of Rights Act in 1987.<sup>9</sup> This legislation purports to increase taxpayers' awareness of their rights during an IRS audit<sup>10</sup> and to enhance the procedural safeguards available to taxpayers during an audit. Specifically,<sup>11</sup> the bill would stem the allegedly commonplace

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1. *Lojeski v. Boandl*, 788 F.2d 196, 197 (3d Cir. 1986).

2. *See* I.R.C. § 6861(a) (1982); *see also* note 91 *infra*; I.R.C. § 6331(a) (1982). Section 6331(a) authorizes the Secretary of the Treasury [hereinafter "the Secretary"] to immediately levy against the taxpayer's property when the Code's jeopardy provision applies.

3. *See* I.R.C. § 6851 (1982) (requiring immediate determination and collection of tax liability where taxpayer designs to depart the United States quickly, remove property from the United States, or do anything prejudicial to the IRS' collection of taxes). *See also* note 91 *infra*.

4. 788 F.2d at 197.

5. 788 F.2d at 197.

6. *The Burlington Free Press*, May 20, 1987, at 10A, col. 1.

7. *Id.*

8. 788 F.2d at 197.

9. S. 1774, 100th Cong., 1st Sess., 133 CONG. REC. S13,891-99 (daily ed. Oct. 8, 1987) [hereinafter S. 1774]. Twin legislation has been proposed in the House of Representatives. *See* H.R. 3470, 100th Cong., 1st Sess. (1987). *See generally* Pryor, *The Near-Totalitarian I.R.S.*, N.Y. Times, Apr. 15, 1988, at 27, col. 2; Cramer, *Putting a Leash on the IRS*, TIME, Apr. 11, 1988, at 49 (describing motives for the proposed legislation).

10. S. 1774, *supra* note 9, § 2(a).

11. This Note does not analyze all aspects of the bill, but rather concentrates on reforms aimed at audit and investigation rights, collections, and damages.

IRS practice of disregarding a taxpayer's validly executed power of attorney and communicating directly with the taxpayer to his detriment.<sup>12</sup> The IRS would also be required to conduct audits at a time and place reasonable to both the taxpayer and the IRS.<sup>13</sup> The bill would further protect taxpayers' privacy by preventing the IRS from gathering or retaining information not relevant to the determination or collection of taxes.<sup>14</sup> Second, the bill seeks to eliminate the unfair surprise and inadequate notice inherent in present Internal Revenue Code (the "Code") provisions governing tax collections.<sup>15</sup> Thus, the bill would provide more equitable procedures for installment payment of taxes<sup>16</sup> and require that IRS tax-related property seizures make economic sense.<sup>17</sup> Finally, the bill would permit the taxpayer to recover damages from the IRS for certain Code violations.<sup>18</sup>

This Note examines whether the bill, as drafted, addresses the problems which spawned it. It anticipates the bill's effects on existing law and identifies areas where the bill would likely create new problems in the administration of the federal tax laws. It further identifies areas where the bill would solve problems. This Note concludes that (1) the bill's audit provisions will not significantly expand taxpayer rights, and may in fact disrupt the audit process; (2) except for safeguards for installment agreements, the bill's attempts to reform IRS collections procedures will not achieve its intended objectives; and (3) the bill's damages provision, if properly construed by the courts, will serve to reform IRS abuses.

This Note has five parts. Part I, "Legislative Background," describes the bill's origins and provides reasons for its introduction. Part II, "IRS Audits and Investigations," analyzes the audit process from the viewpoint of both taxpayer rights and IRS administration. Specifically, Part II discusses four aspects of the audit and taxpayer investigations process: (1) audit time and place; (2) the statutory right to record interviews; (3) the power of attorney and (4) taxpayer surveillance. Part II also discusses the legal effect of the Internal Revenue Manual in light of the Administrative Procedure Act. Part III, "IRS Collections Procedures," critiques three aspects of the bill, including (1) the mechanics of the lien and levy proposals, (2) installment payment provisions, and (3) uneconomical levy provisions. Part IV, "Damages Provision," examines the relative merits of the bill's provision that permits taxpayers to obtain damages against the IRS for cer-

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12. S. 1774, *supra* note 9, § 3.

13. S. 1774, *supra* note 9, § 3; *see also* notes 36-38 *infra* and accompanying text.

14. S. 1774, *supra* note 9, § 24; *see also* notes 70-77 *infra* and accompanying text.

15. S. 1774, *supra* note 9, §§ 12-16, 18; *see also* notes 89-140 *infra* and accompanying text.

16. S. 1774, *supra* note 9, § 12; *see also* notes 116-27 *infra* and accompanying text.

17. S. 1774, *supra* note 9, § 13; *see also* notes 129-40 *infra* and accompanying text.

18. S. 1774, *supra* note 9, §§ 22-23; *see also* notes 141-74 *infra* and accompanying text.

tain Code violations. This Part first identifies defects in the existing Code by examining Code safeguards against IRS overreaching in the lien and levy area. In addition, Part IV discusses whether the bill adequately addresses those defects. Finally, Part V summarizes the benefits and drawbacks of the bill and suggests amendments or deletions which would expand taxpayer rights while simultaneously improving IRS administration.

## I. LEGISLATIVE BACKGROUND

Congressional attempts to reform IRS audit and collection practices are hardly novel. In 1980, the Subcommittee on Oversight of Government Management of the Senate Committee on Governmental Affairs compiled an extensive history of IRS violations of its own formal policies.<sup>19</sup> These violations included excesses similar to those faced by Lojeski and Treadway.<sup>20</sup>

IRS abuses are, to an extent, products of the federal budget deficit and resulting budget constraints.<sup>21</sup> Loathe to increase taxes, Congress has sought to enhance revenues through increased appropriations to IRS collection activities.<sup>22</sup> To the extent that IRS seizure and levy activity is an indication, Congress' efforts to stress tax collections in lieu of tax increases have borne fruit: From fiscal year 1981 to 1986, IRS property seizures increased 154 percent and levies grew by more than 119 percent.<sup>23</sup> Yet during the same period, tax delinquencies rose by only 35 percent.<sup>24</sup>

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19. See generally SUBCOMM. ON OVERSIGHT OF GOVERNMENT MANAGEMENT OF THE COMMITTEE ON GOVERNMENTAL AFFAIRS, 96TH CONG., 2D SESS., INTERNAL REVENUE SERVICE COLLECTION PRACTICES — IMPACT ON SMALL BUSINESSES (Comm. Print 1980) [hereinafter SMALL BUSINESS REPORT].

20. See notes 1-8 *supra* and accompanying text. In Lojeski's case, the IRS violated its own internal policies, but the court denied recovery because she could not demonstrate detrimental reliance on those policies. *Lojeski v. Boardl*, 788 F.2d 196, 199 (3d Cir. 1986).

21. See Steuerle, *Who Should Pay for Collecting Taxes?*, TAX NOTES, Oct. 6, 1986, at 99 (excerpted from C. STEUERLE, WHO SHOULD PAY FOR COLLECTING TAXES? — FINANCING THE IRS (1986)).

22. See Gutfeld, *Overtaxed Agency: IRS Faces Pressure To Raise Collections — But Not Get Tough*, Wall St. J., Dec. 24, 1987, at 1, col. 6.

23. See *Omnibus Taxpayers' Bill of Rights: Hearings on S. 604 Before the Subcomm. on Private Retirement Plans and Oversight of the Internal Revenue Service of the Senate Comm. on Finance*, 100th Cong., 1st Sess., pt. 2, at 13 (1987) (statement of Sen. Levin) [hereinafter *Hearings on S. 604*].

24. *Id.* A deficiency is the amount of tax due, determined by the IRS, less the excess of (1) the sum of (a) the amount of tax shown on the taxpayer's return and (b) the amounts previously assessed (or collected without assessment) as a deficiency over (2) the amount of certain statutory rebates. See I.R.C. § 6211(a) (1982). The amount of statutory rebates includes certain abatements, credits, refunds, or other repayments based on a determination that taxes were less than the previously defined excess computation. See I.R.C. § 6211(a)(2) (1982). If a taxpayer incurs an unsatisfied deficiency, it becomes a delinquency, and is subject to collection action. However, the taxpayer may stay collection under certain Code provisions. See note 95 *infra* and accompanying text.

Additional congressional collections appropriations hinge on the IRS' ability to collect incremental revenues that exceed those appropriations. Despite IRS National Office policy to the contrary, some believe the IRS imposes de facto collections quotas on its collections employees.<sup>25</sup> As one would expect, the IRS justifies congressional collections appropriations by favorably expressing tax collections revenues as a multiple of collections costs.<sup>26</sup>

Senator Pryor's response to the perceived collections quotas was to codify the IRS National Office's prohibition on such quotas. The bill thus forbids both tax enforcement production quotas and the use of enforcement results to evaluate IRS employee performance.<sup>27</sup> Ironically, Congress has ineffectively addressed taxpayer service problems, despite mounting congressional sympathy for improving the quality of taxpayer service, in order to enhance the IRS' public image.<sup>28</sup> According to this view, the public's sense of justice, and ultimately its confidence in the voluntary compliance system, would be improved if the IRS was more impartial, more responsive, and more competent.<sup>29</sup> But assessing the economic benefit of public confidence in the voluntary compliance system is difficult, as there are few dollar-based measures. Accordingly, Congress has been less enthusiastic about taxpayer service than it has been about collections. Thus, taxpayer service problems persist.<sup>30</sup> However, while chiefly designed to curb perceived IRS abuses, the bill nevertheless reflects this congressional sensitivity to taxpayer service. For example, the bill requires that the IRS give the taxpayer reasons for deficiencies and penalties.<sup>31</sup>

While Congress' chief concern has been collections, the IRS believes that the problems targeted by the bill are better addressed by modifying the agency's internal procedures.<sup>32</sup> The National Treasury

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25. See *Hearings on S. 604*, *supra* note 23, at 76-79 (statement of Robert Tobias, National President of the National Treasury Employees Union).

26. *Hearings Before the Subcomm. on Treasury, Postal Service and General Government Appropriations of the Senate Comm. on Appropriations*, 100th Cong., 1st Sess. 511 (1987), reprinted in TAX NOTES, microfiche database doc. 87-1264 (1987) (statement of Lawrence B. Gibbs, Commissioner of Internal Revenue) ("Included in our FY 1988 budget, is an investment of \$400 million which will result in an additional \$2.4 billion being brought into the Treasury.").

27. S. 1774, *supra* note 9, § 7.

28. See *Revenue Agents Say Collections Are Top Priority*, TAX NOTES, June 29, 1987, at 1265 ("Congress has become increasingly concerned about taxpayer services, the public's perception of the IRS, and the subsequent effect on voluntary compliance.").

29. See Simon, *Tax Simplification and Justice*, TAX NOTES, July 6, 1987, at 98-99 ("Reducing perceptions of arbitrariness and unfairness can increase greatly overall compliance. . . . Justice is enhanced . . . by having adequate mechanisms for dispute resolution that . . . encourage prompt decisionmaking.").

30. Gutfeld, *supra* note 22, at 4, col. 3 ("people calling the IRS received incorrect answers to their questions 21% of the time"). See also Gutfeld, *IRS Staffers Are Ready to Assist Taxpayers, but Not Always Able*, Wall St. J., Feb. 18, 1988, at 25, col. 4.

31. S. 1774, *supra* note 9, §§ 10-11.

32. See Gibbs *Criticizes Bill of Rights Proposals*, 67 J. TAXN. 266 (1987) (IRS Commissioner

Employees Union agrees, but believes that IRS management practices must change. The Union cites pressure to meet levy and seizure goals as a major reason for the seemingly unreasonable actions undertaken by IRS revenue officers.<sup>33</sup> If Lojeski and Treadway's case is indicative, revenue officers are under such excessive pressure that they neither follow IRS internal procedures<sup>34</sup> nor are they disciplined for those violations. Indeed, the offending agent in that case was later promoted!<sup>35</sup> Having described this legislative background, this Note now turns to an evaluation of the bill's provisions involving audits and investigations.

## II. IRS AUDITS AND INVESTIGATIONS

### A. *New Provisions*

This Part examines four provisions of the bill respecting IRS audits and investigations: (1) audit time and place; (2) the statutory right to record interviews; (3) the power of attorney; and (4) taxpayer surveillance. It draws the following conclusions concerning these provisions: The audit time and place provisions either merely duplicate the existing Code, or needlessly disrupt audits. The right to record and power of attorney provisions expand taxpayer rights, but lack effective remedies for their violation. The taxpayer surveillance provision adds no meaningful taxpayer right, while potentially harming legitimate IRS enforcement efforts.

#### 1. *Audit Time and Place*

The bill states that any IRS interview with a taxpayer in connection with a deficiency must be conducted "at a reasonable time and place convenient to the taxpayer and [the IRS] officer or employee. . . ."<sup>36</sup> This Note argues that this provision adds nothing to the existing Code. The Code already stipulates that the time and place of the examination shall be reasonable under the circumstances.<sup>37</sup> Moreover, the Code requires that examinations be scheduled at least

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indicating that "the Service is implementing an analytical process inside the agency to deal with taxpayer rights problems").

33. See SMALL BUSINESS REPORT, *supra* note 19, at 22 (outlining severe sanctions against revenue officers who fail to meet collections quotas). The IRS practice of measuring revenue officer collections performance based on the number of seizures and levies, rather than on the dollar value of taxes collected, aggravates this problem. *Id.* at 22-25. Confidence in the voluntary compliance system could suffer accordingly. Ironically, it is often the most cooperative taxpayer who is targeted for collection action. *Id.* at 25.

34. See *Lojeski v. Boardl*, 788 F.2d 196, 197 (3d Cir. 1986) (revenue officer failed to obtain approval of IRS Regional Counsel as required by 2 Internal Revenue Manual (CCH) 5424.33).

35. The Burlington Free Press, May 20, 1987, at 10A, col. 2.

36. S. 1774, *supra* note 9, § 3.

37. I.R.C. § 7605(a) (1982).

ten days after the date of summons.<sup>38</sup> Therefore, this provision simply duplicates the existing Code.

The IRS generally conducts its audits in the IRS District where the taxpayer lives.<sup>39</sup> The Service will, however, consider taxpayer requests for a transfer of the audit to a more convenient district, but there is no standard for reviewing such requests, and such determinations seem to be left to IRS discretion.<sup>40</sup> To reviewing courts, the time and place of audit is a matter of administrative detail, and they consider only whether responsiveness to taxpayer needs interferes with the IRS' ability to conduct audits.<sup>41</sup>

Any effort to reform audit logistics in the name of taxpayer convenience must consider the potential for interference with the audit process. The bill permits a taxpayer to discontinue an interview (audit) to consult with an attorney, C.P.A., enrolled agent, or enrolled actuary.<sup>42</sup> Under present law, taxpayers may not enjoin audits, even if they are designed to harass.<sup>43</sup> While taxpayers may have too little control of audits under current law, giving them unchecked powers to discontinue audits has real potential to disrupt bona fide tax-related inquiries. Like the bill's power of attorney provision,<sup>44</sup> there should be an exception to audit discontinuation powers when the discontinuation unreasonably delays or hinders the audit.

In light of the present safeguards, the need for the audit-convenience provision is baffling. For example, the reasonableness of time and place of the audit, as required by I.R.C. section 7605(a), would likely be held by a reviewing court not to be met in a case where the IRS requires the taxpayer to travel to a distant IRS office. Thus, the audit convenience provision does little or nothing to expand taxpayer rights.

## 2. Statutory Right To Record Interviews

The following section discusses the protections afforded by the bill's provision allowing taxpayers to record audits. The analysis first contrasts this provision to existing law, and identifies proof problems

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38. I.R.C. § 7605(a) (1982).

39. INTERNAL REVENUE SERVICE, U.S. DEPARTMENT OF THE TREASURY, PUB. NO. 556, EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND 1 (Rev. Nov. 1986) [hereinafter IRS PUB. 556].

40. *Id.*

41. *See, e.g.,* United States v. United Distillers Prods., 156 F.2d 872 (2d Cir. 1946).

42. S. 1774, *supra* note 9, § 3. As employed by the IRS, the terms "audit" and "examination" are synonymous. *See* IRS PUB. 556, *supra* note 39, at 1. The governing Code sections use the term "examination." *See* I.R.C. §§ 7602, 7605 (1982). Webster defines "interview" as a "meeting at which information is obtained . . . from a person." WEBSTER'S NEW COLLEGIATE DICTIONARY 600 (1979). One may infer that this provision of the bill governs IRS examinations involving personal contact between the IRS and the taxpayer.

43. *See* Keese v. United States, 632 F. Supp. 85, 89 (S.D. Tex. 1985).

44. S. 1774, *supra* note 9, § 3.

inherent in the bill's remedies available to taxpayers for IRS breach of the right-to-record. Second, the discussion illustrates these proof problems through a hypothetical fact situation.

*a. Bill provisions and analysis.* A taxpayer may, under the bill's provisions, record IRS interviews ("audits").<sup>45</sup> There is no existing Code provision granting taxpayers the right to record IRS interviews, but the Internal Revenue Manual permits the taxpayer to record an IRS interview when (1) it is approved by an IRS group manager; (2) the taxpayer or his representative furnishes the recording equipment; (3) the IRS is also permitted to make its own recording; and (4) the recording occurs at a suitable location, normally an IRS office.<sup>46</sup>

This Internal Revenue Manual provision was enacted in response to a 1963 district court decision, *Mott v. MacMahon*,<sup>47</sup> which announced a judicially created right to have a certified shorthand reporter record the audit at the taxpayer's expense. The *Mott* court reasoned that a certified shorthand reporter presented no obstacle to the orderly discharge of IRS objectives and considered other settings where a right to a reporter promoted the interest of "orderly procedure in the administration of justice."<sup>48</sup> This judicially created right to record an audit has been extended no further than the provisions of the Internal Revenue Manual. Both the Eighth and Ninth Circuits, for example, have adhered to the letter of the Manual in denying taxpayers the right to videotape audits.<sup>49</sup>

With the exception of expanding permissible recording media beyond a shorthand reporter, the bill's provision does little more than codify the Internal Revenue Manual and the result obtained in *Mott*. However, this codification does change the legal effect of the present Internal Revenue Manual provisions.<sup>50</sup> Although the bill creates a new right, it proposes an insufficient remedy.

The bill's remedy for IRS failure to observe the statutory right to record audits is inadequate. The bill's right-to-record provision itself provides no relief, limiting the taxpayer to an action for damages under a separate provision prohibiting unreasonable actions by the IRS.<sup>51</sup> Under that provision, the taxpayer may recover the damages resulting from the IRS' failure to adhere to the statute.

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45. S. 1774, *supra* note 9, § 3.

46. 2 Internal Revenue Manual (CCH) 4245.1, at 7309-223 to -24 (Sept. 4, 1985).

47. 214 F. Supp. 20 (N.D. Cal. 1963).

48. 214 F. Supp. at 23-24 (citing *Gonzi v. Superior Court*, 51 Cal. 2d 586, 335 P.2d 97 (1959)).

49. *United States v. Black*, 804 F.2d 1416, 1417 (8th Cir. 1986); *United States v. Huene*, 745 F.2d 1216, 1217 (9th Cir. 1984), *cert. denied*, 472 U.S. 1027 (1985).

50. See discussion at Part II.B *infra*.

51. S. 1774, *supra* note 9, § 23.



In the case of a denial of recording, there will be an obvious problem of proof concerning damages. After all, the taxpayer would presumably need to demonstrate prejudice; namely that, but for the IRS violation, there would have been no deficiency or a smaller-than-assessed deficiency. Once prejudice is shown, the taxpayer must demonstrate that the IRS violation was careless, reckless, or intentional<sup>52</sup> to recover. In cases where the IRS poses a bona fide challenge to the type of permissible recording media, even if its opposition is later determined to be incorrect and a violation of the statute, no recovery could be obtained because the IRS did not act carelessly. Finally, courts will still need to determine the measure of damages. For example, in the case of a prejudicial denial of the right to record, will the court abate the entire deficiency flowing from the audit or employ some other measure of damages, such as increased taxpayer costs?

*b. Proof problems: an illustration.* One can better understand the shortcomings of the bill's right-to-record provision by applying the provision to a hypothetical set of facts.<sup>53</sup> Consider the following:

A young farmer worked part-time to earn additional income. An IRS agent called him to arrange an audit. The farmer requested that the audit be tape-recorded. The agent denied the request. At the audit, the agent determined that because the farmer was not in the full-time business of farming for profit, the losses on his farm were to be denied. The agent told the farmer that he owed the Government \$100,000, but would settle the case for \$10,000. The agent added the threat that if the farmer refused to pay, the agent would promptly make a jeopardy assessment<sup>54</sup> against the farmer, and would immediately begin seizing his assets for the full \$100,000 liability. Fearing injury to his business and reputation, the farmer reluctantly assented to the agent's demands. The agent knew that the IRS position with respect to the farmer's taxes was legally incorrect, and knew that the farmer would rely on his statement. The agent also knew that the jeopardy assessment could not be made, because no deficiency notice and demand for payment had yet been made.<sup>55</sup> Moreover, the agent knew that the farmer had no intention of transferring the assets to avoid payment of any tax.

Assume that the agent's threat would constitute not only willful

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52. S. 1774, *supra* note 9, § 23. This is a problem whenever the bill's damages provision applies.

53. This hypothetical is based on an actual factual situation presented in the *Congressional Record*. See 133 CONG. REC. S2563 (daily ed. Feb. 26, 1987). Because this scenario constitutes mere fiction, it serves only to illustrate the application of the bill's right-to-record provision.

54. I.R.C. § 6861 (1982).

55. See note 93 *infra*.

oppression under color of law<sup>56</sup> but also duress,<sup>57</sup> a ground for setting aside the settlement agreement.<sup>58</sup> In the hypothetical, the farmer sued to set aside the agreement on grounds of duress and violations of the Code. At trial, the agent denied ever threatening the jeopardy assessment. The farmer testified to the contrary. The farmer introduced no evidence to impeach the agent's testimony. The district court concluded that there was insufficient evidence to establish the farmer's claim and upheld the agreement.

To be sure, the preceding scenario constitutes an injustice. But the ability to obtain damages for the IRS' careless, reckless, or intentional failure to permit recording of the audit will not translate into a recovery of damages by the farmer. The farmer incurred at least \$10,000 in damages. Having found that there was insufficient evidence of duress, the district court presents the farmer with a "catch-22": Because the recording was illegally denied, the farmer lost his case; and because the recording was illegally denied, the farmer cannot prove damages for the denial. This illustrates the need for injunctive relief or, in the alternative, an ability to set aside, with prejudice to the IRS, judgments obtained pursuant to illegal audit procedures. Thus, a remedy in damages inadequately compensates the denial of the taxpayer's right to record an audit.

In the actual case cited in the *Congressional Record*,<sup>59</sup> an IRS agent visited several farmers and attempted to exact settlements for sums far below amounts demanded through demands bordering on duress. Fortunately, the farmer in that case did not make the mistake of agreeing to the settlement. If Congress wishes to discourage abusive IRS conduct, it should create an *enforceable* right to record through injunctive remedies. This will provide incentives for IRS agents to conduct themselves politely at audits and, more importantly, will curb sharp tactics.

### 3. Power of Attorney

This section shows that the bill's power of attorney provision remedies the problem that its drafters intended to address: overreaching by the IRS through unwarranted contact with taxpayers, in violation of validly executed powers of attorney. In this area, the bill safeguards

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56. I.R.C. § 7214(a)(1) (1982).

57. See, e.g., *Aircraft Assoc. & Mfg. Co. v. United States*, 357 F.2d 373 (Ct. Cl. 1966); *Haltan Tractor Co. v. United States*, 141 F. Supp. 411 (N.D. Cal. 1956), *modified*, 258 F.2d 612 (9th Cir. 1958).

58. See, e.g., *Schatten v. United States*, 746 F.2d 319, 322 (6th Cir. 1984) (stating in dicta that a settlement agreement is unenforceable when procured through mistake, undue influence, fraud or duress); *Commissioner v. Danielson*, 378 F.2d 771, 775 (3d Cir. 1967) (same); *Duncan v. United States*, 39 F. Supp. 962, 964 (W.D. Ky. 1941). See also cases cited at note 57 *supra*.

59. See note 53 *supra*.

taxpayer rights without jeopardizing the IRS' ability to make bona fide tax-related investigations.

Section three of the bill provides that any person authorized to practice before the IRS may represent the taxpayer at an audit.<sup>60</sup> The bill compels the IRS to treat the representative as the taxpayer unless that representative causes "unreasonable delay or hindrance" to the audit effort.<sup>61</sup> While the Code is silent concerning taxpayer powers of attorney, treasury regulations allow the taxpayer to be represented at an IRS examination (audit) by an attorney, certified public accountant, enrolled actuary, or other certified representative.<sup>62</sup> Thus, although the new provision creates a new right, in reality the provision only strengthens a right taxpayers already have.

Though treasury regulations permit the use of powers of attorney, they do not explicitly prohibit the IRS from contacting the taxpayer directly even though the taxpayer has given a power of attorney to a qualified advisor. However, treasury regulations do permit the IRS to contact the taxpayer directly when the taxpayer's advisor has been unreasonable about furnishing nonprivileged information.<sup>63</sup> From this, one could infer that the taxpayer could not normally be contacted in contravention of the power of attorney. But the IRS declares that it may directly contact taxpayers whenever the taxpayer maintains information needed by the agency.<sup>64</sup> Indeed, the IRS believes that direct contact with taxpayers is critical to the effectiveness of their audit efforts.<sup>65</sup> In addition, taxpayers may not assert that contact by the IRS is protected by the constitutional right to counsel, because civil tax investigations are of a factfinding, nonadjudicative nature.<sup>66</sup>

The codification of a valid power of attorney, coupled with the bill's damages provision, will assuredly enhance the taxpayer's position because no present remedy exists for an IRS violation of a taxpayer's power of attorney. Without injunctive remedies for these violations, however, the taxpayer again faces problems of proof in an action for damages. When the IRS violates a power of attorney, the taxpayer may lose an otherwise meritorious case because the IRS obtained evidence or admissions from the unwitting taxpayer. This evi-

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60. S. 1774, *supra* note 9, § 3.

61. S. 1774, *supra* note 9, § 3.

62. Treas. Reg. § 601.502(b) (as amended in 1984).

63. Treas. Reg. § 601.505(b) (as amended in 1980).

64. See note 68 *infra* and accompanying text.

65. See *id.*

66. See *In re Groban*, 352 U.S. 330, 332 (1957); *Smith v. United States*, 250 F. Supp. 803 (D.N.J. 1966), *dismissing appeal from* 377 F.2d 739 (3d Cir. 1967). See generally *Sixteenth Annual Review of Criminal Procedure: United States Supreme Court and Courts of Appeals 1985-1986*, 75 GEO. L.J. 713, 1029 (1987) (the sixth amendment right to counsel extends to criminal prosecutions resulting in imprisonment and "attaches at the formal initiation of adversary judicial proceedings").

dence would not have been available had the IRS dealt solely with the more knowledgeable authorized representative. Barriers to taxpayer recovery will be compounded by the easily invoked defense that the authorized representative caused unreasonable delay or hindrance to the investigation.

While the provision fails to provide a more explicit definition of unreasonable delay, it will ensure that taxpayers do not delay or disrupt audits via the power of attorney, a critical consideration in a system that conducts approximately 1.27 million examinations each year.<sup>67</sup> Audit quality is a second consideration. Unless the power of attorney unreasonably delays or hinders the audit, the authorized representative steps into the taxpayer's shoes. Even when the taxpayer is represented, the IRS believes that the taxpayer's presence at the audit and willingness to respond to questions are important to audit effectiveness.<sup>68</sup> Thus, the bill may limit the IRS' ability to gather essential information within the taxpayer's peculiar knowledge.<sup>69</sup> But in many instances, particularly when the authorized representative closely advises the taxpayer, that representative may be in the best position to respond to IRS inquiries. Conceding that taxpayers possess vital, peculiar knowledge, there is little to suggest that when this knowledge is needed it could not be obtained via communication between the authorized representative and the taxpayer. Any logistical problems created by the additional communication step between the taxpayer and the authorized representative (as opposed to direct taxpayer communication with the IRS) would be limited, because the bill proscribes unreasonable delay or hindrance of audits. Overall, the bill strikes a reasonable balance between respect for powers of attorney and hindrance of the IRS' ability to conduct audits.

#### 4. *Taxpayer Surveillance*

This section will demonstrate that the provision of the bill prohibiting unrelated taxpayer surveillance is unnecessary. The bill duplicates the rights already granted the taxpayer by the Privacy Act. This provision may also have a harmful effect not associated with the Privacy Act. Principally, the bill's criminal sanctions for these surveillance actions will inhibit the gathering of information relevant to the collection of taxes.

The bill prohibits officers or employees of the United States from authorizing, requiring, or conducting any investigation into or surveillance of a taxpayer that is not relevant to the collection or determina-

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67. See C. STEUERLE, WHO SHOULD PAY FOR COLLECTING TAXES? FINANCING THE IRS 11 (1986) (figures exclude employment, excise, and windfall profit taxes).

68. Letter from Commissioner Lawrence Gibbs to Rep. J.J. Pickle (Nov. 4, 1986), reprinted in TAX NOTES, Nov. 24, 1986, at 714.

69. See *id.*

tion of the taxpayer's tax liability.<sup>70</sup> This section of the bill supplements I.R.C. section 7214, which provides for criminal penalties against the offending agent. The bill would amend that section to include a fine of up to \$10,000 and/or five years imprisonment, as well as discharge of the offending government employee. Moreover, the offending employee must pay the taxpayer's damages stemming from the violation.<sup>71</sup>

This proposed amendment to section 7214 is unnecessary and duplicative. The Privacy Act,<sup>72</sup> which governs surveillance activities by federal agencies, already requires that an agency that maintains a system of records maintain only those records necessary to accomplish its administrative purpose. The Privacy Act also forbids federal agencies from maintaining records describing an individual's exercise of first amendment rights unless those records relate to an authorized law enforcement activity.<sup>73</sup> The intent of both the bill's provision and the Privacy Act are the same: to prohibit unnecessary surveillance of citizens by federal agencies. Moreover, neither the bill's provisions nor the Privacy Act apply when the surveillance or investigation is germane to the collection or determination of the tax liability.<sup>74</sup> Under the Privacy Act, there must be a direct nexus between the information gathered and a criminal, civil, or administrative law enforcement activity.<sup>75</sup> Similarly, surveillance pertinent to the collection or determination of tax liability would be permitted under the bill.

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70. S. 1774, *supra* note 9, § 24. There is also an exception for certain organized crime activities.

71. S. 1774, *supra* note 9, § 24; *see also* I.R.C. § 7214 (1982). I.R.C. § 7423 (1982) permits the Secretary to indemnify certain damages and costs recovered against an offending employee in the due performance of his official duties. Even if unauthorized surveillance was construed to fall within the scope of due performance of official duties, it would not protect the employee against criminal sanctions because § 7423 indemnifies only damages and costs. *See* S. 1774, *supra* note 9, § 24.

*Compare* I.R.C. § 7214 (1982) with I.R.C. § 7431 (1982). Section 7431(a)(1) permits suits against the government for its unauthorized disclosure of taxpayer and return information. It does not permit suit against the government employee who makes the unauthorized disclosure. Similarly, the Federal Tort Claims Act extends jurisdiction to sue the government, but not to sue the offending government employee. *See* 28 U.S.C. § 1346(a) (1982).

On its face, the bill's taxpayer surveillance provisions are designed to protect taxpayer privacy. Thus, if these provisions should be adopted at all, they should appear as amendments to I.R.C. § 7431. The bill's taxpayer surveillance provisions and § 7431 advance similar interests: the former circumscribes information that can be collected, the latter circumscribes the disclosure of lawfully collected information. Thus, the damages framework of § 7431 would best fit the bill's surveillance provision.

72. 5 U.S.C. § 552a(e)(1) (1982) ("Each agency that maintains a system of records shall . . . maintain in its records only such information about an individual as is relevant and necessary to accomplish a purpose of the agency required . . . by statute or by executive order. . . .").

73. 5 U.S.C. § 552a(e)(7) (1982).

74. *See* S. 1774, *supra* note 9, § 24; 5 U.S.C. § 552a(e)(1) (1982). *See also* England v. Commissioner, 798 F.2d 350, 352 (9th Cir. 1986) (no Privacy Act liability exists where the records related solely to the determination of tax liability and were unrelated to the exercise of first amendment rights).

75. *Jabara v. Webster*, 691 F.2d 272 (6th Cir. 1982), *cert. denied*, 464 U.S. 863 (1983).

Duplication of Privacy Act provisions is of comparatively little harm. At worst, there will be a new body of law filling up unnecessary space in an already voluminous Code. However, the real danger of this provision is its potential to chill pertinent IRS information-gathering because of the bill's criminal sanctions for collection or retention of such information. The opposing argument posits that I.R.C. section 7214(a)<sup>76</sup> already provides similar criminal sanctions. Despite the force of this argument, it fails to recognize that the bill's proposed amendment to section 7214(a) does not fit with the purposes of that section. Section 7214(a) deals with, among other things, corrupt practices by IRS employees. Many of these practices, such as bribery and extortion, are already state and federal crimes. The prevention of these corrupt practices goes to the very core of the public's confidence in the voluntary taxpayer compliance system. In contrast, the investigation/surveillance sanctions of the bill criminalize behavior that may only slightly deviate from legitimate and good faith prosecution of tax violators. To attach criminal sanctions to such activities raises the very real potential for impairment of vigorous, good faith enforcement of the tax laws.

In this respect, the Privacy Act provides a more intelligent approach to the problem of unwarranted government investigation and surveillance. Damages for such violations are assessed against the government, not the offending employee.<sup>77</sup> This lessens the possibility of impairment of good faith enforcement efforts. Therefore, the bill's taxpayer surveillance provisions have the dual effect of adding no meaningful protection to taxpayers, while severely hampering necessary IRS investigations.

### B. *Application of the Administrative Procedure Act*

As previously noted, the bill codifies certain provisions of both the

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76. I.R.C. § 7214(a) (1982) provides that

Any officer or employee of the United States acting in connection with any revenue law of the United States — (1) who is guilty of any extortion or willful oppression under color of law; or (2) who knowingly demands other or greater sums than are authorized by law, or receives any fee, compensation, or reward, except as by law prescribed, for the performance of any duty; or (3) who with intent to defeat the application of any provision of this title fails to perform any of the duties of his office of employment; or (4) who conspires or colludes with any other person to defraud the United States; or . . . (7) who makes or signs any fraudulent entry in any book, or makes or signs any fraudulent certificate, return or statement; or (8) who, having knowledge or information of the violation of any revenue law by any person, or of fraud committed by any person against the United States under any revenue law, fails to report, in writing, such knowledge or information to the Secretary; or (9) who demands, or accepts, or attempts to collect, directly or indirectly as payment or gift, or otherwise, any sum of money or other thing of value for the compromise, adjustment, or settlement of any charge or complaint for any violation or alleged violation of law, except as expressly authorized by law so to do; shall be dismissed from office or discharged from employment and, upon conviction thereof, shall be fined not more than \$10,000, or imprisoned not more than 5 years, or both.

77. See 5 U.S.C. § 552a(g)(4) (1982).

Internal Revenue Manual and the treasury regulations. This section proves that the codifications of the Internal Revenue Manual afford greater legal protection to taxpayers, even without significant changes to the terms of the safeguards already provided in the Manual. The right to record taxpayer interviews, for example, and many other taxpayer rights are governed by the Internal Revenue Manual. No statute, however, addresses whether the Internal Revenue Manual has the force of law.<sup>78</sup>

It is, of course, settled law that regulations validly promulgated pursuant to notice and comment or on-the-record requirements of the Administrative Procedure Act have the force of law.<sup>79</sup> It follows that an agency action which violates agency rules cannot stand.<sup>80</sup> However, internal agency rules such as the Internal Revenue Manual are treated differently from regulations and statutes. And because section 23 of the bill provides a damages remedy for an IRS violation of a pertinent statute or regulation, the bill's protection will not extend to violations of the Internal Revenue Manual.<sup>81</sup>

An agency is not required to follow an internal rule if it concerns the internal administration of the agency.<sup>82</sup> However, where individual rights are affected by agency deviation from established rule, the agency must follow that rule, even if it concerns only internal agency procedure.<sup>83</sup> In addition to affecting an individual's rights, detrimental reliance by the taxpayer upon the Internal Revenue Manual is a condition to recovery for violation of a Manual provision.<sup>84</sup>

In addition to protection against agency caprice,<sup>85</sup> codification of an internal rule in a statute eliminates the need for a taxpayer to demonstrate an adverse effect upon him and to demonstrate detrimental reliance upon the internal rule. The first problem, demonstration of an effect upon the taxpayer of the internal rule, is not particularly problematic. Typically, the deviation from the rule affects taxpayer rights, or the claim would never have been brought.<sup>86</sup> More difficult is the need to demonstrate detrimental reliance. Such a requirement

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78. Cf. I.R.C. § 7805(b) (1982) (permitting the Secretary to give rule changes retroactive effect).

79. See, e.g., *Service v. Dulles*, 354 U.S. 363 (1957); *Hammond v. Lenfest*, 398 F.2d 705 (2d Cir. 1968); *Raven-Hansen, Regulatory Estoppel: When Agencies Break Their Own "Laws,"* 64 TEXAS L. REV. 1, 12 (1985).

80. See *Sangamon Valley Television Corp. v. United States*, 269 F.2d 221, 224 (D.C. Cir. 1959).

81. See S. 1774, *supra* note 9, § 23.

82. See, e.g., *United States v. Lockyer*, 448 F.2d 417, 420-21 (10th Cir. 1971).

83. *Morton v. Ruiz*, 415 U.S. 199, 235 (1974).

84. See *Lojeski v. Boandl*, 788 F.2d 196, 199 (3d Cir. 1986).

85. The IRS may change its rules and give them retroactive effect. See note 78 *supra* and accompanying text.

86. Cf. *Raven-Hansen, supra* note 79, at 18.

does not exist with a statute — its provisions apply regardless of whether or not the taxpayer shaped his affairs in reliance on them. In cases of unsophisticated or unrepresented taxpayers, the likelihood of detrimental reliance upon, for example, the Internal Revenue Manual seems slim. Thus, the bill's codification of Internal Revenue Manual provisions will give legal effect to the safeguards presently embodied by the Manual. Similarly, because the Administrative Procedure Act does not give the force of law to the Manual, the codifications of the Manual will provide greater substantive protection to taxpayers.

### III. IRS COLLECTIONS PROCEDURES

#### A. *Liens and Levies*

This section analyzes two problems the bill attempts to address. First, it analyzes the effectiveness of the bill's review provisions for premature levies, and concludes that the bill does not go far enough in providing the timely administrative or judicial review so critical to any workable premature levy safeguard. Indeed, present injunctive remedies extend more protection against premature levies. Second, this section considers the protections afforded by the bill to innocent third parties who are wrongfully subjected to IRS liens or levies. It concludes that these provisions will genuinely aid taxpayers, but that certain aspects of them will also hinder bona fide IRS collection efforts.

##### 1. *Premature Levies*

One may infer that the bill's drafters believe that the present statutory period between the time of notice and demand for payment of taxes and levy against the taxpayer's property is too short.<sup>87</sup> Accordingly, the bill extends I.R.C. section 6331(a)'s<sup>88</sup> ten-day period for notice and demand prior to levy to thirty days.<sup>89</sup> With more advance warning, the taxpayer would be better able to respond in a timely fashion to a request for payment. The bill also provides for a taxpayer review action when the IRS prematurely levies against the taxpayer. Under this provision, if the IRS levies against a taxpayer for the collection of a deficiency less than thirty days after notice and demand for payment, the taxpayer may obtain administrative, and ultimately judicial, review of the premature action under jeopardy assessment procedures.<sup>90</sup>

Premature levies are different from jeopardy assessments. Jeop-

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87. This inference can be drawn because the bill extends I.R.C. § 6331(a)'s ten-day period for notice and demand for payment prior to levy to thirty days. See note 89 *infra* and accompanying text.

88. I.R.C. § 6331(a) (1982) provides that a taxpayer who fails to pay taxes within ten days of notice and demand for payment by the IRS may be subjected to collection action by levy.

89. S. 1774, *supra* note 9, § 14.

90. See I.R.C. § 7429(b) (1982).



ardy assessments give the IRS special collection powers when there is reason to believe that the collection of tax is in jeopardy.<sup>91</sup> Thus, I.R.C. section 7429(a) allows the taxpayer to argue the merits<sup>92</sup> or challenge procedural defects<sup>93</sup> of the jeopardy assessment.<sup>94</sup> In the case of premature levy, however, there are few merits to examine — the IRS has clearly deviated from a statutory timing standard and should be enjoined from collection, with no opportunity to show cause why its premature levy should go forward unless, of course, the IRS makes a jeopardy assessment. The ability to review a levy is useless to the taxpayer whose bank account or other assets are subjected to levy. In such a case, the taxpayer will want to stop the wrongful levy before the IRS takes his assets, rather than review the IRS action after such taking.

Existing law provides taxpayers better safeguards against premature levies than the bill's provisions. The most obvious remedy under

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91. "If the Secretary believes that the assessment or collection of a deficiency, . . . will be jeopardized by delay, he shall, . . . immediately assess such deficiency. . . ." I.R.C. § 6861(a) (1982). See also I.R.C. § 6851(a)(1) (1982), which provides:

If the Secretary finds that a taxpayer designs quickly to depart from the United States or to remove his property therefrom, or to conceal himself or his property therein, or to do any other act . . . tending to prejudice or to render wholly or partially ineffectual proceedings to collect the income tax for the current or the immediately preceding taxable year . . . the Secretary shall immediately make a determination of tax . . . and notwithstanding any other provision of law, such tax shall become immediately due and payable.

92. I.R.C. § 7429(g) (1982) requires that the Secretary prove the reasonableness of the assessment under the circumstances, while the taxpayer has the burden to prove the appropriateness of that assessment. Irreparable injury to the taxpayer will not, standing alone, sustain an injunction over an assessment. See, e.g., *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1, 6 (1962). In addition to irreparable hardship, the IRS action must plainly exceed the agency's statutory authority. An example of such an excess would be the use of a jeopardy assessment to exert pressure on the taxpayer for reasons unrelated to the collection of tax. See *Sherman v. Nash*, 488 F.2d 1081, 1084 (3d Cir. 1973); see also *Pizzarello v. United States*, 408 F.2d 579, 582 (2d Cir. 1969), cert. denied, 396 U.S. 986 (1969) (Notwithstanding I.R.C. § 7421(a)'s prohibition on taxpayer actions to enjoin the collection of any tax, an attempted jeopardy assessment over unpaid wagering taxes may be enjoined if (1) it is clear that under no circumstances could the Government prevail, and (2) equity jurisdiction otherwise exists.); *Shapiro v. Secretary of State*, 499 F.2d 527, 532 (D.C. Cir. 1974), aff'd., 424 U.S. 614 (1976) (same); *Lucia v. United States*, 474 F.2d 565, 575 (5th Cir. 1973) (same); *Williams v. Wiseman*, 333 F.2d 810, 811 (10th Cir. 1964) (same).

93. A jeopardy or termination assessment made without prior notice of deficiency to the taxpayer is illegal, and the taxpayer is entitled to release of any assets obtained by the IRS pursuant to the procedurally defective IRS action. See *Causey v. United States*, 79-1 U.S. Tax Cas. (CCH) ¶ 9,161 (D. Minn. 1978) (citing *Laing v. United States*, 423 U.S. 161 (1976); *Campbell v. United States*, 532 F.2d 1057 (6th Cir. 1976); *L.O.C. Indus. v. United States*, 423 F. Supp. 265 (M.D. Tenn. 1976)). Courts may also set aside a levy pursuant to a jeopardy assessment if the IRS denies the taxpayer notice and opportunity to pay the assessment prior to the levy. *L.O.C. Indus.*, 423 F. Supp. at 273.

94. Administrative and judicial review of jeopardy assessments also extends to termination assessments. I.R.C. § 7429(a) (1982). "[L]egislative history . . . shows that Congress intended 'a taxpayer who has been subjected to a termination assessment to [be able to] contest the ultimate issue of his liability in the Tax Court in the same manner as is provided with respect to a taxpayer who has been subjected to a jeopardy assessment.'" *Perlowin v. Sassi*, 711 F.2d 910, 912 (9th Cir. 1983) (quoting S. REP. NO. 94-938, 94th Cong., 2d Sess. 367, reprinted in 1976 U.S. CODE CONG. & ADMIN. NEWS 2897, 3796).

existing law is for the taxpayer to petition the Tax Court for redetermination of the deficiency, which will automatically enjoin collection action by the IRS.<sup>95</sup> Beyond that, courts will void levies in circumstances where the IRS deviated from statutorily prescribed procedures.<sup>96</sup> Thus, if the IRS fails to provide notice and an opportunity to pay the amount assessed, the statute requires that any levy be enjoined.<sup>97</sup> Given this, why would a taxpayer faced with a premature levy ever want to use the jeopardy review provisions of I.R.C. section 7429, which permit the levy when the Secretary can prove mere reasonableness?<sup>98</sup> The taxpayer is better served here by existing law.

## 2. *Lien and Levy Against an Innocent Third Party*

What will the bill do to cure the injustice worked upon Ms. Lojeski?<sup>99</sup> Recall that her property was levied upon or tied up by liens, and she claimed (but was not awarded) damages based upon those IRS actions. Lojeski was a third party who fell victim to the IRS' suspicion that the allegedly deficient taxpayer, Treadway, had been transferring assets to her. The following discussion concludes that the bill will provide a meaningful remedy to Lojeski (and to taxpayers in general) for the liens that were wrongfully placed on her property.

Under the Code, no suit may be maintained to restrain assessment or collection against an actual transferee of a taxpayer subject to a deficiency.<sup>100</sup> Additionally, no protection exists for the transferee under the Code's wrongful levy provisions.<sup>101</sup> But in the case of an *innocent* third party, the Code provides for a wrongful levy action,<sup>102</sup> and in such actions the IRS carries the burden of proving that the levy was appropriate under the circumstances.<sup>103</sup>

In Lojeski's case, the Code's wrongful levy provision had two shortcomings. First, the provision applies to levies, so Lojeski could

95. See I.R.C. § 6213(a) (1982) (unless a jeopardy or termination assessment has been made, no deficiency assessment or levy can be made until Tax Court decisions become final). Treadway's "horror story," recounted in the text accompanying notes 1-8 *supra*, is probably atypical because he was subjected to a jeopardy assessment, which is used only under special circumstances where collection is in doubt. In the typical case, the well-advised taxpayer need only petition the Tax Court to enjoin any collection action.

96. See, e.g., *Rodriguez v. United States*, 629 F. Supp. 333 (N.D. Ill. 1986). See also note 93 *supra*.

97. I.R.C. § 6213(a) (1982) provides that "the making of [a premature] assessment or . . . levy . . . may be enjoined by a proceeding in the proper court."

98. See I.R.C. § 7429(g) (1982). See also note 93 *supra*.

99. See text accompanying notes 5-8 *supra*.

100. I.R.C. § 7421(b)(1) (1982).

101. See, e.g., *Shannon v. United States*, 521 F.2d 56, 59 (9th Cir. 1975), *cert. denied*, 424 U.S. 965 (1976).

102. I.R.C. § 7426 (1982).

103. See *Flores v. United States*, 551 F.2d 1169, 1175 (9th Cir. 1977).

not obtain relief under the section for her farm, which was subject to a lien. Second, even if the wrongful levy provision applied, the Code makes no allowance for consequential damages, which were a component of the damages claimed. Conceivably, the first problem could be solved by bringing an action to quiet title against the government.<sup>104</sup> This action allows the aggrieved party to sue to remove government liens despite the Code's proscription on taxpayer suits to enjoin tax collections.<sup>105</sup> However, an action to quiet title would still not provide for consequential damages.<sup>106</sup>

Through its provision for recovery of actual damages for careless, reckless, or intentional violations of the Code, the bill should remedy the present unavailability of consequential damages to the taxpayer.<sup>107</sup> In Lojeski's case, there is a strong likelihood that the IRS action would be characterized as careless, if not reckless, because there were no reasonable grounds to support the suspicion that Treadway was transferring assets to her. Thus, the bill addresses the IRS abuse illustrated in Lojeski's case with an adequate remedy in damages.

From an IRS enforcement perspective, the damages provision also makes sense. If the IRS levies against a taxpayer whom the IRS reasonably believes to be a transferee, no damages will be recoverable even if the IRS is wrong when viewed with hindsight. Because IRS tax liens would be challenged under a federal action to quiet title,<sup>108</sup> the bill's damages provisions (which are limited to IRS violations of the Code) would not apply. However, negligent or knowing failure to release an IRS tax lien also triggers recovery of damages under a separate provision of the bill.<sup>109</sup> The recovery of damages for negligent or knowing failure to release a lien is limited to circumstances where the liability has been satisfied, where the liability is unenforceable, (as where the statute of limitations has run) or where a bond has been accepted.<sup>110</sup> A court determination that an IRS lien is wrongful is a

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104. 28 U.S.C. § 2410 (1982) provides, in pertinent part, that "the United States may be named a party in any civil action or suit in any district court, or in any State court having jurisdiction of the subject matter . . . to quiet title to . . . real or personal property on which the United States has or claims a mortgage or other lien."

105. See *United States v. Coson*, 286 F.2d 453, 458-59 (9th Cir. 1961). Innocent third parties like Lojeski use actions to quiet title to remove clouds on title without arguing the merits of the deficiency.

106. See *Ringer v. Basile*, 645 F. Supp. 1517, 1526 (D. Colo. 1986) (court dismissed damages claim coupled with quiet title action because there was no waiver of sovereign immunity for money damages claims). Cf. *Enochs v. Williams Packing & Navigation Co.*, 370 U.S. 1 (1962) (a suit to enjoin the collection or assessment of tax may not be brought merely because collection would cause the taxpayer irreparable injury). See also *Lloyd v. Patterson*, 242 F.2d 742, 744 (5th Cir. 1957).

107. S. 1774, *supra* note 9, § 23.

108. See 28 U.S.C. § 2410 (1982) and note 104 *supra*.

109. S. 1774, *supra* note 9, § 22.

110. See S. 1774, *supra* note 9, § 22. The bill applies only to actions to release a lien under I.R.C. § 6325 (1982). This Code section governs the release of IRS liens only when the liability

further determination that there is no tax liability. If there is no tax liability, the liability should be "satisfied." Thus the bill also extends relief to Lojeski for the liens wrongfully placed on her property.

The bill also creates administrative review for liens. Under the bill, *any person* may administratively appeal when the IRS imposes a lien on their property.<sup>111</sup> In contrast, actions to quiet title typically protect only innocent third parties.<sup>112</sup> As applied to allegedly delinquent taxpayers, the most likely interpretation of the provision will be to enable the taxpayer to challenge the basis for the deficiency.<sup>113</sup> This is true because the Code automatically imposes a lien on all of the taxpayer's property once the IRS demands payment of taxes.<sup>114</sup> Because the taxpayer may not normally challenge a tax lien, any challenge a taxpayer makes to a lien must be on the merits. In other words, the taxpayer must assert that he does not owe the tax.

Administrative review of liens by taxpayers curiously extends a system that already provides for judicial and administrative review on the merits. This will enable any taxpayer to delay the imposition of a lien pending outcome on the merits. This delay will permit taxpayers fraudulently to transfer assets otherwise restrained by liens. In addition, administrative challenges to tax liens extend no needed additional rights to honest taxpayers.<sup>115</sup> Thus, the adoption of an administrative review provision for liens would be contrary to the intent of the bill's drafters: to remedy genuine abuses of taxpayers without hindering IRS enforcement efforts.

### B. *Installment Payment of Income Tax Liabilities*

This section argues that the bill's income tax installment payment provisions substantially enhance taxpayer protection in an area presently susceptible to IRS abuse. Moreover, these provisions require few concessions by the IRS of its collection powers. Finally, the provisions also comport with general notions of notice, fairness and due process. The analysis commences with a factual example of the prob-

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is satisfied, the lien is unenforceable, or a bond is accepted for the liability. The Secretary may, at his discretion, also issue a certificate of discharge in selected circumstances.

111. See S. 1774, *supra* note 9, § 15.

112. The exception to this axiom is "when a taxpayer refrains from contesting the merits of the underlying tax assessment. . . ." *Aqua Bar & Lounge v. United States*, 539 F.2d 935, 940 (3d Cir. 1976).

113. Section 15 of the bill provides that "Any person shall be allowed to appeal to the Secretary, in such form and at such time as the Secretary shall prescribe by regulations, the imposition of a lien under this subchapter on the property or rights to property of such person." S. 1774, *supra* note 9, § 15.

114. I.R.C. § 6321 (1982).

115. See *Hearings on S. 604*, *supra* note 23, at 86 (prepared statement of Robert M. Tobias, National President of the National Treasury Employees Union) (Delays are unwarranted because in 99% of the cases it is the taxpayer's *admitted* liability that is subject to collection. Thus, the bill will halt collection and cause the loss of billions in revenue.).

lem sought to be addressed, followed by a description of the bill's provisions, and concludes with a discussion of the provisions' effect on taxpayer rights.

The problem to be addressed by the bill's income tax installment payment provisions is well illustrated by the following factual situation:

A small businessman entered into an installment agreement with the IRS for back taxes. The taxpayer made every payment on time. . . . One day his creditors began calling him to say that his business checks were bouncing. He then called his bank to find that the IRS had decided to cancel their agreement and had levied on his business account without contacting him. When he finally was able to get through to the IRS, they informed him that they had decided to collect because of the substantial change in the financial condition of his business. Result of the IRS action: creditors called in their notes, many suppliers would only deal in cash after his checks bounced, and some suppliers refused to do business with him.<sup>116</sup>

This "horror story" dramatizes the void the bill intends to fill: the absence of a statutory requirement that the IRS honor income tax installment agreements. Treasury regulations do not aid the taxpayer in this respect, as they all contain permissive language that allows the IRS to release a levy when the taxpayer makes satisfactory arrangements with the IRS district director to pay in installments.<sup>117</sup> But any release from levy by the IRS does not preclude a later levy, as the above example dramatizes.<sup>118</sup> The bill would enable the IRS to enter installment agreements for the payment of income taxes when it "determines that such agreement will facilitate collection" of an income tax liability.<sup>119</sup> If the IRS enters such an agreement, it is to be binding.<sup>120</sup> However, if the financial condition of the taxpayer changes, the IRS may "alter, modify or annul" the installment agreement.<sup>121</sup> To the extent that the IRS does not find a significant change in taxpayer financial condition, the bill considerably enhances the certainty

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116. 133 CONG. REC. S2563 (daily ed. Feb. 26, 1987); see also SMALL BUSINESS REPORT, *supra* note 19, at 10 ("Levies on checking accounts require no notice to the taxpayer, so that a taxpayer's first word of such a levy comes when its checks to creditors are returned as a result of the levy.").

117. Treas. Reg. § 301.6343-1(a)(2)(v) (1972). The IRS has six options in handling cases requiring collection action: (1) require payment from available assets; (2) secure a short-term extension of time to pay or an installment agreement; (3) report the account currently uncollectible; (4) recommend or initiate enforcement action; (5) file notice of federal tax lien; or (6) explain the Code's offer in compromise provisions to the taxpayer. 2 Internal Revenue Manual (CCH) ¶ 5323, at 6538-39 (May 15, 1986).

118. See note 116 *supra* and accompanying text. See also Treas. Reg. § 301.6343-1(a)(1) (1972). Indeed, in some IRS districts, levies are not released at all, even when the taxpayer enters an installment agreement. See *Hearings on S. 604, supra* note 23, at 89 (statement of Robert M. Tobias, National President of the National Treasury Employees Union).

119. S. 1774, *supra* note 9, § 12.

120. S. 1774, *supra* note 9, § 12.

121. S. 1774, *supra* note 9, § 12.

that the IRS will honor installment agreements entered into with taxpayers.

This provision will also compel the IRS to enter installment agreements only in cases where there is a strong likelihood that a greater percentage of the deficiency will be recovered if the taxpayer is allowed to pay by installments. There will no longer be cases in which the IRS has nothing to lose by entering an installment agreement and later levying at their whim. The provision is also fairer to taxpayers, given their perfectly valid expectation that parties honor agreements (or incur liability when they breach such agreements and cause damages). More importantly, the new provision does much to prevent the IRS from unexpectedly levying at an inopportune moment with injurious or even catastrophic effects on the taxpayer.

Allowing the IRS to disregard the installment agreement when there is a significant change in the taxpayer's financial condition first requires a definition of change in financial condition.<sup>122</sup> When financial conditions change for the worse, there will often be no assets against which a levy can be made. When financial conditions change for the better, the "IRS horror story" is bound to recur. One feature of the bill that will remove the harshness of the IRS' power to accelerate collection of its installment debts is a requirement for a hearing on the record<sup>123</sup> pursuant to procedures set out by the Administrative Procedure Act.<sup>124</sup> The hardship incurred in the "IRS horror story" was not so much the inability to pay the remaining obligation in a lump-sum, but rather the lack of notice<sup>125</sup> that the IRS planned to exercise its levy powers. Under the bill, IRS violations of the install-

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122. This change could probably be determined using present IRS procedures governing the payment options discussed at note 117 *supra*. The taxpayer could set out pertinent financial information in a form similar to I.R.S. Form 433-A (Rev. Dec. 1986) (Collection Information Statement). See 2 Internal Revenue Manual (CCH) ¶ 5321(2), at 6537 (Aug. 20, 1986). Under the criteria set out in these forms, if the taxpayer's available cash equals or exceeds the tax liability, the IRS will demand immediate payment and will not enter an installment agreement. *Id.* ¶ 5323(3), at 6539. If the IRS enters an installment agreement, the taxpayer's monthly installments must usually equal or exceed the difference between the taxpayer's net income and IRS allowable expenses. *Id.* ¶ 5323(4)(e), at 6540.

123. S. 1774, *supra* note 9, § 12.

124. See 5 U.S.C. §§ 551-706 (1982).

125. Presently, the IRS installment agreement notifies the taxpayer that the entire tax liability may be collected by levy and seizure if the taxpayer fails to meet the conditions of the agreement or if collection of the taxes is endangered. See I.R.S. Forms 433-D (Rev. Dec. 1985) (Installment Agreement), 433-G (Rev. Aug. 1986) (Direct Debit Installment Agreement). Cf. I.R.S. Form 433-M (Rev. June 1980) (Installment Agreement) ("I understand that this agreement will be withdrawn if . . . the IRS determines that the entire amount of my tax should be collected."). Though the agreements notify the taxpayer that the IRS may either conditionally (as provided in I.R.S. Forms 433-D and 433-G *supra*) or unconditionally (as provided in I.R.S. Form 433-M *supra*) levy against property notwithstanding the installment agreement, these actions may surprise the taxpayer. There is no statutory requirement of notice and opportunity to be heard in these circumstances. It is also commonplace IRS practice to refuse ever to release levies, even when the taxpayer enters an installment agreement. See note 118 *supra*. Accordingly, surprise levies are performed, often with injurious consequences to the taxpayer.

ment payment provision would trigger the bill's damages remedy, so long as the IRS had carelessly, recklessly, or intentionally failed to observe the provision.<sup>126</sup> Damages would chiefly arise in two circumstances: (1) failure to provide notice and a hearing, or (2) levying after determination that there has not been a significant change in financial condition of the taxpayer.

The bill's installment payment provision also allows the IRS to protect its interest when there is a significant change in the taxpayer's financial condition. There are two basic reasons for this. First, thirty days is a relatively short time to await the adjudication of the IRS' claim, and in most cases, barring fraudulent asset transfers, the taxpayer's financial condition will not change dramatically during that period. Second, the IRS would still have available its arsenal of emergency collection powers such as jeopardy assessments. In jeopardy assessments, for example, the IRS may make immediate notice and demand for payment when it believes that the collection of a deficiency will be jeopardized by delay.<sup>127</sup> Therefore, the bill's installment payment provision does much to remedy needless IRS abuses, while reserving IRS powers to collect assets quickly when that type of action is truly needed.

### C. *Uneconomical Levies*

This section evaluates a somewhat novel concept — uneconomical levies.<sup>128</sup> It starts by describing uneconomical levies and then provides a set of facts to which the uneconomical levy provision was intended to apply. It concludes that the uneconomical levy provision does not, in many instances, address the problem to which it was directed. Finally, this section critiques the uneconomical levy provision and posits a more effective way to address the problem.

When expenses incurred by the IRS in conducting a levy and sale of property exceeds the fair market value of the property sold or exceeds the underlying tax liability, the bill prohibits IRS levy.<sup>129</sup> The following scenario illustrates the reasons for this provision: Rose Mary Guzman, a single mother of six, dutifully made mortgage payments on a house titled in her brother's name. She believed all along that the house belonged to her, pursuant to a handwritten and unrecorded agreement in Spanish. Her brother owed \$4,794.96 to the U.S. government, and the house, valued at \$45,000, was sold by the IRS for

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126. S. 1774, *supra* note 9, § 23.

127. See I.R.C. § 6861(a) (1982); see also notes 2, 91 & 95 *supra*.

128. The Uniform Commercial Code (U.C.C.) requires that a secured creditor sell collateral by commercially reasonable methods. See note 133 *infra*. However, the U.C.C. has no analogous provision to the bill's uneconomical levy requirements, described in note 129 *infra* and accompanying text.

129. S. 1774, *supra* note 9, § 13.

\$6,200 to satisfy the delinquency.<sup>130</sup>

By supplementing existing remedies for wrongful levy,<sup>131</sup> the bill adds to the array of taxpayer rights in this area by prohibiting these uneconomical levies. Ironically, however, neither Ms. Guzman nor her brother would obtain relief under the bill's uneconomical levy provisions. Assuming the IRS sold the property for the amount of the deficiency plus costs to the IRS, those costs would total no more than \$1,405.04.<sup>132</sup> Because those costs neither exceed the tax liability nor the fair market value of the property, the bill would not preclude the sale, even though it seems wasteful to sell a \$45,000 property for \$6,200.

Thus, a provision for sale of property subject to tax lien foreclosure at fair market value or under commercially reasonable methods, with recovery of surplus proceeds by the judgment debtor, would better address this problem.<sup>133</sup> Under such a provision, when liens of relatively small value in relation to the property value are attached to the property, the potential for the loss of the taxpayer's equity is eliminated. Unfortunately, the bill lacks these requirements. While the present Code furnishes time, place, and manner guidelines for sales of seized property,<sup>134</sup> it is far from settled whether those sales must be commercially reasonable.<sup>135</sup> Even conceding that there is a commercial reasonableness requirement, remedies for its breach are unclear.

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130. Curry, *IRS Seizes, Sells Home of Mother of 6*, San Antonio Sunday Express News, May 24, 1987, at 2-C, col. 1.

131. I.R.C. § 7426 (1982) provides relief from an IRS levy for parties other than the taxpayer by (1) ensuring recovery of sale proceeds to which the party claiming an interest in the property is entitled, by (2) allowing an injunction of levy, and by (3) providing for recovery of property. Ms. Guzman could have asserted that she held title to the property pursuant to the agreement with her brother, or asserted adverse possession under Texas law. See TEX. CIV. PRAC. & REM. CODE ANN. § 16.026(a) (Vernon 1986).

132. The \$6,200 sale price less the \$4,794.96 deficiency equals \$1,405.04. This figure of \$1,405.04 represents an inference from the given facts. Actual costs may have deviated from this figure.

133. Ms. Guzman's "horror story" illustrates that IRS tax sales are often conducted to promote only the interests of the government and not those of the taxpayer. As between private parties, a sale of property to satisfy a security interest on a defaulted debt requires that the interests of the judgment debtor be considered. See U.C.C. § 9-504(3) (1977) (requiring sale of collateral by commercially reasonable methods). Of course, the best relief available to Ms. Guzman would be an action for wrongful levy under I.R.C. § 7426. See note 131 *supra*.

134. I.R.C. § 6335 (1982).

135. See M. SALTZMAN, IRS PRACTICE AND PROCEDURE ¶ 14.17[2] (Supp. 1986) (indicating that issue of whether IRS must sell property in commercially reasonable fashion is unsettled). See also *Ringer v. Basile*, 645 F. Supp. 1517, 1521 (D. Colo. 1986) (holding that the IRS does not have unfettered discretion to sell property at any value where the property's fair market value greatly exceeds its sale price). Where property is sold pursuant to judicial order, few price objections may be interposed. In this context, a judicial sale will not be set aside for inadequacy of price unless the disparity between price and fair market value is so gross as to shock the conscience of the court and the selling circumstances indicate unfairness, such as chilled bidding. See, e.g., *Breeding Motor Freight Lines v. Reconstruction Fin. Corp.*, 172 F.2d 416, 424 (10th Cir.), *cert. denied*, 338 U.S. 814 (1949).



If Ms. Guzman's case is typical, the IRS does not sell seized property in a commercially reasonable manner. The agency's own internal procedures support the view that property sales should promote IRS interests, with only consequential benefit to the taxpayer.<sup>136</sup> Sales pursuant to I.R.C. section 6335 require the use of property valuation floors<sup>137</sup> and minimum bid prices.<sup>138</sup> While ostensibly protecting taxpayers, the IRS' chief concern is to collect money owed: the minimum bid price for properties sold may not exceed the tax liability plus expenses of sale.<sup>139</sup> This explains why Ms. Guzman's \$45,000 house could be sold for \$6,200.

A different problem with the bill's uneconomical levy provision concerns its prohibition of levies that make economic sense. For example, if the expenses of a sale of property subject to levy exceed the liability for which such levy is made,<sup>140</sup> the bill prohibits such levy. A levy under such circumstances is not necessarily uneconomical, however. Rather, an uneconomical levy is one in which the expense of levy exceeds the amount collected. Any incremental collections above the cost of levy would be an economical levy and therefore the bill's uneconomical levy provisions do not promote the most economically efficient (nor necessarily the fairest) collection policy. Having identified the problems with the bill's uneconomical levy provision, this Note now turns to an evaluation of the bill's damages provision.

#### IV. DAMAGES PROVISION

Does a taxpayer's right to obtain damages for the IRS' careless, reckless or intentional disregard for Code provisions<sup>141</sup> create more problems than it solves? This Part shows that the right to obtain damages takes an important step toward genuine reform, without significant disadvantages. This answer suggests an analysis of the considerations surrounding existing Code safeguards for taxpayers and the availability and scope of damages to aggrieved taxpayers under the bill. Because they pose the most serious potential for taxpayer injury

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136. Cf. Treas. Reg. § 301.7506-1(b)(4) (as amended in 1974) (taxpayer property administered by the United States pursuant to I.R.C. § 7506 permits the revenue officer to withdraw property from sale when to adjourn the sale would best serve the interests of the United States). See also 2 Internal Revenue Manual (CCH) ¶ 56(17)5.22, at 6905 (Nov. 15, 1985).

137. The forced sale value must equal at least 75% of the property's value. See 2 Internal Revenue Manual (CCH) ¶ 56(13)5.1, at 6866 (Jan. 15, 1987).

138. The minimum bid price normally equals at least 80% of the property's forced sale value less encumbrances. *Id.* ¶ 56(13)5.1, at 6866 (Jan. 15, 1987). But see text accompanying note 139 *infra*.

139. *Id.* ¶ 56(13)5.1, at 6866 (Jan. 15, 1987).

140. S. 1774, *supra* note 9, § 13.

141. See S. 1774, *supra* note 9, §§ 22-23 (providing such recovery). A condition to recovery under this provision is an administrative determination in favor of the taxpayer. *Id.*

and are arguably of greatest concern to congressional reformers,<sup>142</sup> the following analysis confines itself to IRS collections.

### A. Existing Remedies

In the majority of cases, the taxpayer can enjoin collection action pending final determination of tax liability by petitioning the Tax Court.<sup>143</sup> It follows that most abuses of the collections process should occur only with jeopardy and termination assessments and wrongful liens and levies.<sup>144</sup> This is because the taxpayer cannot unilaterally control the imposition of jeopardy or termination assessments.<sup>145</sup> Wrongful liens and levies require the taxpayer to show that the IRS has no interest in his property. In contrast, a Tax Court petition enjoins collection, pending adjudication of the tax assessment, regardless of the strength of the taxpayer's substantive position.

In Treadway's case,<sup>146</sup> the administrative appeals process failed, even though Treadway ultimately won.<sup>147</sup> It failed because delays inherent in the process, coupled with the gravity of the IRS action, posed an insurmountable financial burden to Treadway. Thus, under current law, when the IRS wrongfully makes a jeopardy or termination assessment, injuries associated with the delays from administrative and judicial review (such as destruction of a business interest) are uncompensated.

#### 1. Jeopardy and Termination Assessments

One avenue to relief from jeopardy and termination assessments is for the taxpayer to post a bond in the amount of the alleged liability.<sup>148</sup> This bond will stay the assessment.<sup>149</sup> In this context, however, a bond may usually be obtained only when the taxpayer has assets of value that substantially exceed the assessment amount. Moreover, bonding companies usually require cash collateral or its equivalent of value equal to the bond.<sup>150</sup> Bonds are no panacea, as they seriously

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142. Senator Pryor claims that most cases of severe taxpayer abuse occur in the collections process. See *Hearings on S. 604*, *supra* note 23, at 2 (statement of Sen. Pryor).

143. See I.R.C. § 6213(a) (1982).

144. See notes 1-8 *supra* and accompanying text.

145. See notes 2-5 *supra* and accompanying text.

146. See notes 1-8 *supra* and accompanying text.

147. See note 6 *supra* and accompanying text.

148. I.R.C. § 6863 (1982) allows for a stay of all or part of the collection of a jeopardy or termination assessment when the taxpayer obtains a bond in the amount of the stay desired.

149. See *id.*

150. M. SALTZMAN, *supra* note 135, ¶ 10.05[5][a]. Telephone conversations with national surety brokers and underwriters reveal a hesitancy to take even cash collateral. Many underwriters insist on irrevocable letters of credit. Irrevocable letters of credit are preferred because, unlike cash or money market instruments, they are easy to safekeep, are negotiable sight drafts, and are not subject to avoidance as preferential distributions in bankruptcy. Telephone conversations with Detroit and Ann Arbor, Michigan banks reveal that if they agreed to issue irrevocable

impair a taxpayer's working capital. Because of their cash collateral requirements, bonds are no better than payment of the assessment and suit for refund.

Concerning pre-levy rights, the fourth amendment forbids warrantless, nonpermissive entry by the IRS onto the taxpayer's property to take assets in satisfaction of tax liabilities.<sup>151</sup> But nothing suggests that the IRS has difficulty obtaining writs of entry (warrants). In addition, once property has been taken by the IRS, there are few realistic remedies available to taxpayers subject to these actions. Post-seizure rights do include staying the sale of seized property in many circumstances.<sup>152</sup> Sale may be stayed for the period during which the IRS would normally be precluded from levy or seizure if no jeopardy/termination assessment applied.<sup>153</sup> For business, or even investment properties, however, a stay of sale is of little solace where the taxpayer needs the property and cannot easily find substitutes or replacements.

## 2. *Wrongful Liens and Levies*

Currently, the Code affords greater protection against IRS wrongful liens and levies to innocent third parties than to taxpayers. For example, where irreparable injury looms from wrongful levy, the Code extends a rare injunctive remedy to third parties.<sup>154</sup> Further, the Code protects against irreparable harm in this context because it allows the third party who has been subjected to wrongful levy to recover his property.<sup>155</sup> Unique and irreplaceable property thus seem well protected. Remedies for improper liens, however, are more problematic, even for innocent third parties. The IRS must remove a wrongful lien within 30 days of judicial determination of no liability,<sup>156</sup> but the taxpayer may not recover damages if the IRS takes longer.

## 3. *Injury to Reputation and Credit*

Judicial hostility to consequential damages in wrongful lien and

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letters of credit in these circumstances, the banks would require the taxpayer to post cash collateral or its equivalent. (Cash equivalents are money market instruments such as Treasury Bills or bank certificates of deposit.) When a taxpayer is subject to a jeopardy assessment, however, it will be difficult to obtain a bond. When a bond is available, the taxpayer will ultimately be required to pledge cash collateral or its equivalent. Sources of the above information obtained by telephone are on file with the *Michigan Law Review*.

151. See *G.M. Leasing Corp. v. United States*, 429 U.S. 338 (1977).

152. In this context, a seizure is the taking of property by the IRS from the taxpayer. A levy is the taking of taxpayer's property held by a third party. See *M. SALTZMAN*, *supra* note 135, ¶ 14.15. These terms do not necessarily have the same meaning they would have in civil litigation between private parties.

153. See I.R.C. § 6863(b)(3) (1982).

154. I.R.C. § 7426 (1982).

155. I.R.C. § 7426(b)(2) (1982).

156. See I.R.C. § 6325(a) (1982).

levy actions,<sup>157</sup> as well as the belief that such damages are too speculative, have fostered disregard for an important interest: reputation and credit. Many small businesses with a few large customers fear that they will be perceived as incompetent, insolvent, or even dishonest when a wrongful IRS action mars their credit record.<sup>158</sup> Indeed, Treadway's greatest complaint about his nightmare concerned the injury to his credit.<sup>159</sup> Unfortunately, the Code provides no remedy for this wrong. In addition, courts will deny recovery to taxpayers subjected to the common law torts of harassment, defamation, interference with business relationships, trespass, and mental suffering when the IRS agent acted within the scope of his authority.<sup>160</sup> These courts hesitate to find that even the most egregious IRS wrongs were done outside the IRS agent's scope of authority.<sup>161</sup> Occasionally, the judiciary will strain to provide recovery to injured taxpayers under the Code's limited damages provisions.<sup>162</sup> But more often, the taxpayer is

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157. See, e.g., *Young v. United States*, 75-2 U.S. Tax Cas. (CCH) ¶ 9574 (S.D.N.Y. 1975) (citing W. PLUMB, *FEDERAL TAX LIENS* 262-3 (3d ed. 1972)) (I.R.C. § 7426 provides no remedy for consequential or special damages stemming from the IRS' retention of property, or even for its diminution in value resulting from IRS negligence while in their custody).

158. SMALL BUSINESS REPORT, *supra* note 19, at 10; see also note 116 *supra* and accompanying text.

159. 700 Club: *Taxpayer Rights and IRS Internal Affairs* (WDCA television broadcast, Oct. 16, 1987) (transcript of interview of Thomas Treadway by Cynthia Glaser, Christian Broadcasting Network on file with the *Michigan Law Review*) ("I've been stripped of my reputation, but most of all, I've been stripped of my credit, because without credit . . . you can't function.").

160. See, e.g., *Keese v. United States*, 632 F. Supp. 85, 93 (S.D. Tex. 1985).

161. See *Keese*, 632 F. Supp. at 93 ("a federal official is immune from suits under state tort law for acts within the scope of his discretionary duties authorized by law, even if the official acted out of malice or was deliberately misusing his authority"). See also *United States v. Mitchell*, 445 U.S. 535, 538 (1980) (unless it consents to be sued, the United States is immune from suit); *Williamson v. United States Dept. of Agric.*, 815 F.2d 368, 376 (5th Cir. 1987) (claim for actions made in an official government capacity barred by sovereign immunity); *American Assn. of Commodity Traders v. United States Dept. of Treasury*, 598 F.2d 1233, 1235 (1st Cir. 1979) (sovereign immunity not waived merely because IRS agents may be personally liable in *Bivens* action).

162. See *Rorex v. Traynor*, 771 F.2d 383, 386-87 (8th Cir. 1985) (holding IRS liable under § 6103 for actual damages caused by a wrongful bank account levy where the IRS action constituted a violation of disclosure limitations on taxpayer information). The *Rorex* court awarded damages for the violation of I.R.C. § 6103 (1982) under I.R.C. § 7217 (1982). Section 7217 has since been repealed and superseded by I.R.C. § 7431 (1982), which provides like remedies against the Government, rather than the offending IRS employee. Compare *Rorex* with *Timmerman v. Swenson*, 44 A.F.T.R.2d (P-H) 79-5727 to -5731 (D. Minn. 1979), where the court held that a levy against assets not belonging to a delinquent taxpayer resulting in disclosure of the taxpayer's delinquency to third parties violated no duty to the taxpayer. The *Rorex* court distinguished *Timmerman* on the basis that the taxpayers in *Rorex* had made timely installment payments of taxes, while the *Timmerman* taxpayers were delinquent. *Rorex*, 771 F.2d at 386. *Timmerman* did not rest on this distinction, however. Rather, *Timmerman* properly held that even when the IRS violates an Internal Revenue Manual provision that would clearly obviate its challenged action, the violation confers no right of recovery on the taxpayer. *Timmerman*, 44 A.F.T.R.2d (P-H) ¶ 79-5731. See also notes 82-84 *supra* and accompanying text. Similarly, the IRS has no duty to honor the type of installment agreement it entered into in *Rorex*. See note 125 *supra*. No remedies exist for the breach of a nonexistent duty.

Even if there was a duty not to levy against a taxpayer who is current in his installment payments, *Rorex* was wrongly decided. I.R.C. § 6103(k)(6) (1982) authorizes the disclosure of

without a remedy.<sup>163</sup> This compensatory void leads one to wonder whether the bill will do better.

### B. *The Bill's Remedies*

The bill's language providing damages for failure to release liens<sup>164</sup> and providing damages for unreasonable IRS actions<sup>165</sup> bears considerable similarity to the language contained in I.R.C. section 7431(c)<sup>166</sup> (the section containing sanctions for wrongful disclosures of taxpayer information), and the Privacy Act.<sup>167</sup> All those provisions refer to "actual damages."<sup>168</sup> The phrase "actual damages" is employed in many federal statutes,<sup>169</sup> but there is no plain meaning of "actual damages" at common law or elsewhere.<sup>170</sup> Thus, the meaning and prob-

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taxpayer information relating to the type of collection activity undertaken in *Rorex*, according to regulations promulgated by the Secretary of the Treasury. Those regulations expansively define the circumstances in which return information of the type disclosed in *Rorex* may be publicized. Treasury Regulation § 301.6103(k)(6)-1(b)(6) authorizes the disclosure of return information "to locate assets in which the taxpayer has an interest [or] to ascertain the amount of any liability. . . ." Treas. Reg. § 301.6103(k)(6)-1(b)(6) (1980). In this setting, the Code defines return information to include, among other things, the nature, source, or amount of the taxpayer's tax liabilities and deficiencies "or any other data received by, recorded by, prepared by, furnished to, or collected by the Secretary with respect to . . . the determination of the existence, or possible existence, of liability (or the amount thereof) of any person. . . ." I.R.C. § 6103(b)(2)(A) (1982). The treasury regulations require only that no other means to accomplish the collection function exist. See Treas. Reg. § 301.6103(k)(6)-1(b)(7) (1980). Thus, the *Rorex* holding not only lacks legal authority, but it places an unwarranted judicial gloss on the regulations: namely, that return information may be disclosed pursuant to a levy only when it comports with internal IRS policy. This gloss is especially unwarranted on a legislative regulation like the one involved, since I.R.C. § 6103(k)(6) (1982) explicitly grants the Secretary authority to make regulations.

163. See, e.g., *Flippo v. United States*, 670 F. Supp. 638, 641-42 (W.D.N.C. 1987) (a violation of I.R.C. § 7431 did not occur where the IRS agent made a good faith, reasonable effort to inform the taxpayer of a deficiency and contemplated collection action, even though taxpayer had paid the tax prior to the collection action).

Another problem with recovery for wrongful disclosure involves the theory's narrow scope. The IRS can wrongfully collect many assets without disclosure to anyone, leaving the taxpayer without any conceivable remedy.

164. "[U]pon a finding of liability on the part of the defendant, the defendant shall be liable . . . [for] actual damages sustained by the plaintiff as a result of actions of the defendant, or \$100 per day for each day the failure occurred, whichever is greater. . . ." S. 1774, *supra* note 9, § 22.

165. "[A]ctual damages sustained by the plaintiff as a result of actions of the defendant. . . ." S. 1774, *supra* note 9, § 23.

166. "[T]he defendant shall be liable to the plaintiff in an amount equal to the sum of — (1) the greater of — (A) \$1,000 for each act of unauthorized disclosure . . . or (B) the sum of — (i) the actual damages sustained by the plaintiff as a result of such unauthorized disclosure, plus (ii) in the case of a willful disclosure or a disclosure which is the result of gross negligence, punitive damages, plus (2) the costs of the action." I.R.C. § 7431(c) (1982).

167. "[T]he United States shall be liable to the individual in an amount equal to the sum of . . . actual damages sustained by the individual as a result of the refusal or failure, but in no case shall a person entitled to recovery receive less than the sum of \$1,000." 5 U.S.C. § 552a(g)(4)(A) (1982).

168. See notes 164-67 *supra*.

169. See, e.g., 15 U.S.C. § 15 (1982) (the Clayton Act); 7 U.S.C. § 25(a), (b) (1982) (the Commodity Exchange Act); 15 U.S.C. § 1681(n) (1982) (the Fair Credit Reporting Act); 15 U.S.C. § 78bb(a) (1982) (the Securities Exchange Act of 1934).

170. *Johnson v. I.R.S.*, 700 F.2d 971, 974 (5th Cir. 1983) (upon review of authorities cited by

able application of "actual damages" must be derived from the bill's purposes and its relationship with other Code provisions. In addition, it is appropriate to analyze this ambiguous language in light of its usage in other, analogous federal statutes.<sup>171</sup> In large part, the bill's effectiveness will be determined by judicial construction of this language.

As noted, the bill's chief purpose is to stop the perceived abuse of taxpayers.<sup>172</sup> An interpretation of "actual damages" providing for recovery of consequential damages,<sup>173</sup> including injury to reputation and credit, lost profits, and incidental expenses, best serves that purpose. If the Code's present remedies, which protect restitutionary interests,<sup>174</sup> abate wrongful IRS actions,<sup>175</sup> and provide limited recoveries of costs,<sup>176</sup> adequately protected taxpayer interests such as reputation and credit and business profits, there would be far less need for a bill protecting taxpayers' rights.

An expansive construction of "actual damages" can also be supported by the congressional desire to reform IRS practices. Ultimately, the IRS must internalize its costs.<sup>177</sup> By imposing additional

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parties, court concluded that there is no plain meaning or consistent judicial interpretation of "actual damages").

171. See Note, *Damages Under the Privacy Act of 1974: Compensation and Deterrence*, 52 *FORDHAM L. REV.* 611, 629 (1984).

172. See text accompanying notes 10-11 *supra*. See also *Hearings on S. 604, supra* note 23, at 3 ("The Taxpayers' Bill of Rights is intended to put a stop to taxpayer abuse. . .").

173. Many of the wrongs sanctioned by the bill would be deemed tortious. For example, serious interference with a taxpayer's control over a chattel, such as where the IRS dispossesses the taxpayer of personal property, would constitute conversion. See *RESTATEMENT (SECOND) OF TORTS* §§ 222A(1), 223 (1965). Similarly, these actions would constitute trespass to chattels. See *id.* §§ 217, 218. Further, liability for intentional infliction of emotional distress can be found through outrageous conduct intentionally or recklessly directed at the victim. See *id.* § 46. The abuse of a position of authority can represent this sort of outrageous behavior. See *id.* § 46 comment e. Communications, such as those that would injure a taxpayer's credit record, are defamatory. See *id.* § 559. Additionally, a corporation may recover for defamation if the defamatory communication prejudices the company in the conduct of its business or deters others from dealing with it. See *id.* § 561(a).

Tort awards include consequential damages. See *id.* § 917 comment d (1977), which provides:

although a contracting party who breaks his contract in failing to supply a machine would not be liable for the damages occasioned by the shutting down of a plant in which the machine was a necessary unit unless at the time of making the contract he knew or should have known the facts . . . , one who negligently destroys the machine may be responsible for the ensuing loss although he had no reason to know in advance of the machine's importance.

174. See, e.g., I.R.C. § 7426(b)(2)(C)(ii) (1982).

175. See, e.g., I.R.C. § 7429 (1982).

176. I.R.C. § 7430 (1982).

177. See Cooter, *Unity in Tort, Contract, and Property: The Model of Precaution*, 73 *CALIF. L. REV.* 1, 3 (1985) (When an individual bears the full benefits and costs of his precaution, that cost is internalized. Internalization means that the individual sweeps all of the values affected by his actions into his self-interest. Social efficiency is achieved by balancing these costs and benefits.). Of course, internalization rests on the assumption that the Government behaves rationally: that is, it will not invade a protected interest if the cost of doing so exceeds the benefits derived from the invasion. See Note, *supra* note 171, at 631 n.122. However, some evidence indicates

costs for Code violations, the agency has an incentive to curb abuses. For instance, these added costs may cause the Collection Division to jettison the practice of evaluating employee performance based on levy and seizure activity,<sup>178</sup> and to start emphasizing large dollar, low risk collections. Similarly, expansive construction of "actual damages" will encourage taxpayer enforcement of the Code.<sup>179</sup> Finally, "actual damages" should be broadly construed to meet the statute's remedial purpose,<sup>180</sup> because the most legitimate interpretation of a statute is the one that best furthers the legislative purpose.<sup>181</sup>

Existing federal statutes also illuminate the possible meaning of "actual damages," and further clarify the scope of damages provided by this language. Courts interpreting the Privacy Act are split on whether or not "actual damages" go beyond out-of-pocket losses.<sup>182</sup> The decisions that embrace a narrow construction do so out of fear of excessive government liability and the concomitant flurry of litigation.<sup>183</sup> This concern, however, is unwarranted in this instance. To limit any litigation explosion against the government, the bill's drafters added a provision for government recovery of damages for groundless taxpayer claims.<sup>184</sup> This provision, along with the other considerations mentioned above, strongly suggests that the damages provision be adopted and broadly construed.

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that the IRS Collection Division does not act rationally. Because of organizational pressures or other factors, the Division exalts those activities that prove most injurious to taxpayers and least effective in terms of revenues collected. See note 33 *supra*. Nevertheless, the imposition of costs may be the incentive the IRS needs to change its policies.

178. See note 33 *supra*.

179. See Note, *supra* note 171, at 622 (inadequate recoveries resulting from restrictive interpretation of "actual damages" will diminish incentives for citizen enforcement of the Privacy Act).

180. *But see* Posner, *Statutory Interpretation — in the Classroom and in the Courtroom*, 50 U. CHI. L. REV. 800, 808-09 (1983) (to construe remedial statutes broadly is to ignore legislative compromise). Because legislative compromise was probably not the motive for the use of this language, Posner's criticism of the canon that remedial statutes are to be broadly construed should not apply here. The bill's damages provision applies to every conceivable Code violation by the IRS. Thus, a more plausible reason for the ambiguous language is that neither Congress nor anybody else can envision all the potential applications of an omnibus remedial provision that governs all careless, reckless, or intentional Code violations.

181. See, e.g., *Vazquez v. Eastern Air Lines*, 579 F.2d 107, 112 (1st Cir. 1978); *United States v. New York, N. H. & H. R.R.*, 276 F.2d 525, 532 (2d Cir. 1960), *cert. denied*, 362 U.S. 961 (1960). See also Sinclair, *Law and Language: The Role of Pragmatics in Statutory Interpretation*, 46 U. PITT. L. REV. 373, 398-99 (1985).

182. Compare *Johnson v. I.R.S.*, 700 F.2d 971, 972 (5th Cir. 1983) ("actual damages" include emotional injuries), with *Albright v. United States*, 558 F. Supp. 260, 264 (D.D.C. 1982), *aff'd.*, 732 F.2d 181 (D.C. Cir. 1984) ("actual damages" require a showing of out-of-pocket loss).

183. See, e.g., *Pope v. Bond*, 641 F. Supp. 489, 501 (D.D.C. 1986).

184. S. 1774, *supra* note 9, § 23. See also 133 CONG. REC. S13,899 (daily ed. Oct. 8, 1987) ("Damages suits would be subject to frivolous claims penalties."). The federal judiciary is further empowered to sanction frivolous claims using FED. R. CIV. P. 11. See *Brownie v. United States*, 83-1 U.S. Tax Cas. (CCH) ¶ 9334 (E.D.N.Y. 1983); see also *Alyeska Pipeline Serv. Co. v.*

## V. CONCLUSION

The bill's proposed reforms concerning taxpayer audits range from benign, duplicative modifications of the existing Code, to provisions that could disrupt the audit process, to codifications of the Internal Revenue Manual. The codifications, by eliminating the taxpayer's need to demonstrate detrimental reliance on the Internal Revenue Manual, will expand the safeguards already included in the Manual. Moreover, the permanence of these safeguards would be assured to a greater extent than before because the Manual's purpose is to govern IRS internal procedure, and it is subject to change at the whim of that agency. Finally, concerning taxpayer surveillance, the Privacy Act provides safeguards equivalent to those proposed by the bill without chilling enforcement.

The bill attempts to curb abuse of the IRS collections process and — to the extent that greater time is afforded a taxpayer to respond to the threat of levy — the bill serves that end. However, remedies against premature, abusive, and uneconomical levies are impractical or simply ineffective, and will not extend greater protection to taxpayers than existing law.

It seems fair to require the IRS to honor income tax installment payment agreements. This requirement also makes economic sense because it discourages destructive surprise levy tactics. Moreover, the bill reserves sufficient collection flexibility for the IRS while eliminating the unfairness that has characterized the installment payment process.

The most potent safeguard against taxpayer abuse is the provision for recovery of damages for careless, reckless, or intentional Code violations by the IRS. This provision, however, may not aid taxpayers injured by mistakes of fact, or mistakes of fact and law. Whether the bill expands existing compensation to make injured taxpayers completely whole depends largely upon judicial interpretation of "actual damages."

With improved drafting and heightened cognizance of existing law, Congress could go further in providing the safeguards envisioned by the bill without substantially interfering with the tax collection machinery. However, like most other legislation, the bill is a product of

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*Wilderness Socy.*, 421 U.S. 240, 258-59 (1975) (a court may award attorney's fees when a litigant acts "in bad faith, vexatiously, wantonly, or for oppressive reasons") (quoting *Vaughan v. Atkinson*, 369 U.S. 527 (1962)). Another of the bill's barriers to taxpayer recovery is denial of damages when the taxpayer is contributorily negligent. S. 1774, *supra* note 9, § 23. The usage of this provision, however, is beyond the scope of this Note.



compromise<sup>185</sup> and the political aims of its drafters.<sup>186</sup> As such, four suggestions are posited. First, taxpayers should not be permitted to discontinue audits whenever they wish to seek counsel, and the provision permitting this should be deleted. Second, IRS agents should not be held criminally liable for surveillance of taxpayers, and the provision establishing this liability should be deleted. Third, the bill's prohibitions on uneconomical levies should be modified to contemplate the sale of seized property in a commercially reasonable manner. Finally, if possible, Congress should define what it means by "actual damages" in order to ensure full effect to the bill's compensatory mechanism for IRS Code violations. Additionally, the courts should liberally construe any damages provision so as to advance the bill's remedial purpose. By adopting these revisions, Congress could preserve or even improve effective tax law administration, while continuing the legislative trend toward taxpayer compensation.<sup>187</sup>

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185. See S. 604 §§ 2, 16, 100th Cong., 1st Sess. (1987). Among other things, S. 604 required the IRS to provide *Miranda* warnings to taxpayers in civil audits and shifted the burden of proof in litigation with the IRS to that agency. These controversial provisions, in the face of criticism by interested groups, have been deleted from the present version of the bill. See, e.g., TAX DIVISION OF THE AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, COMMENTS ON S. 579 TAXPAYER'S [SIC] BILL OF RIGHTS ACT AND S. 604 OMNIBUS TAXPAYER'S [SIC] BILL OF RIGHTS ACT 1, 4-5 (July 22, 1987) (submitted to the Senate Finance Subcommittee on Private Retirement Plans and Oversight of the IRS) (*Miranda* warnings would create "a 'criminal' atmosphere [and] would only frighten taxpayers and cause ill feelings toward the Service." Placing the burden of proof on the IRS would be an "extreme burden on the [tax collection] system. . ."). Even ardent supporters of S. 604, such as the United States Chamber of Commerce, wondered aloud about the political viability of the proposal to shift the burden of proof in tax litigation to the IRS. See A. YOSHIURA, TAX POLICY: CAPITOL HILL FIGHT TO CURB IRS ABUSES 8 (U.S. Chamber of Commerce Services Watch, July 1987) (recognizing that burden of proof provision was "hotly debated").

186. How can any other conclusion be reached concerning the bill's surveillance provisions, which blatantly overlap the provisions of the Privacy Act? Two former IRS Commissioners might agree with this observation. In their view, the entire bill is "nothing but a political exercise, with the Service playing the role of whipping post." "Taxpayer's [sic] Bill of Rights" Prompts Former Commissioners to Ask: "What's New?," TAX NOTES, Mar. 2, 1987, at 853.

187. See, e.g., I.R.C. § 7430 (1982) (adopted in 1982, the section permits awards of attorney's fees and other costs to taxpayers when the IRS takes an unreasonable litigation position).

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