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Internal Revenue Service Investigations of Unidentified Persons

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INTERNAL REVENUE SERVICE INVESTIGATIONS OF UNIDENTIFIED PERSONS

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I. INTRODUCTION

In 1976, legislation was enacted that substantially restricted the Internal Revenue Service's (IRS) power to issue John Doe summonses to investigate unidentified persons.[1] Congress action reflected its concern about the use of these summonses to conduct "fishing expeditions" through the records of banks and other third parties in the hope of uncovering useful information about someone.[2] The new law seeks to protect the privacy of such records by permitting a John Doe summons to issue only *after* the IRS has satisfied a district court, in an *ex parte* hearing, that there is a reasonable basis for believing that ascertainable persons may have violated the tax laws.

The new legislation and IRS interpretation of the statute have raised a number of questions concerning the scope of the IRS authority to conduct investigations or research projects not focused upon any particular taxpayer or tax liability. One issue involves IRS attempts to circumvent the John Doe summons requirements by requesting information about unidentified persons while auditing an identified taxpayer. An administrative summons is issued for documents relevant to the audited person's tax liability.[3] The IRS does not follow the John Doe summons requirements even though the records concern unidentified persons. The courts have disagreed about whether administrative summonses with a dual purpose of investigating both the audited person and an unidentified person are enforceable. Several courts have ruled administrative summonses with a dual purpose are enforceable[4] while one court has required the IRS to follow the John Doe summons requirements any time information is requested about unascertained persons.[5]

The IRS has also sought to avoid the John Doe summons procedures by

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1. Tax Reform Act of 1976, Pub. L. No. 94-455, § 1205, 90 Stat. 1520, 1701 (codified at I.R.C. § 7609(f) (1976)).

2. H.R. REP. NO. 658, 94th Cong., 1st Sess. 311 (1975) *reprinted in* 1976 U.S. CODE CONG. & AD. NEWS 2897, 3207 [hereinafter cited as H.R. REP. 658]; S. REP. NO. 938, 94th Cong., 2d Sess. 373 *reprinted in* 1976 U.S. CODE CONG. & AD. NEWS 3439, 3802 [hereinafter cited as S. REP. 938].

3. The general administrative summons is issued pursuant to I.R.C. § 7602 (1976). *See infra* note 14 and accompanying text.

4. United States v. First Nat'l Bank, 635 F.2d 391 (5th Cir. 1981); United States v. Flagg, 634 F.2d 1087 (8th Cir.), *cert. denied*, 451 U.S. 909 (1980); United States v. Barter Sys., Inc., 82-2 U.S. Tax Cas. (CCH) ¶ 9698 (8th Cir. 1982); United States v. Constantinides, 80-2 U.S. Tax Cas. (CCH) ¶ 9830 (D.C. Md. 1980). *See infra* notes 64-66 and 73-86 and accompanying text.

5. United States v. Gottlieb, 82-1 U.S. Tax Cas. (CCH) ¶ 9257 (M.D. Fla. 1982). *See infra* notes 67-69 and accompanying text.

relying upon a statutory right to inspect records that taxpayers and other third parties are required to maintain.[6] The IRS has asserted that the inspection authority is implicit in the statutes that mandate recordkeeping.[7] Such warrantless inspections, however, may raise serious constitutional issues in light of Supreme Court decisions involving administrative searches.[8]

Another controversy focuses on the reasonable basis standard for issuing and enforcing a John Doe summons. The courts have disagreed as to what the IRS must show to establish a reasonable basis for its belief that the taxpayer has not complied with the tax laws. Some courts have concluded this belief may be based upon IRS audit experience and statistical analyses,[9] while one court has required evidence about the specific unidentified person or transaction.[10] Courts have also disagreed about whether the *ex parte* judicial determination authorizing issuance of a John Doe summons may be challenged in a subsequent adversarial enforcement proceeding.[11]

A final area of concern is the possible "chilling effect" an IRS summmons may have upon the exercise of first amendment freedoms. It has been asserted that a summons for documents identifying members of controversial groups has an impermissible impact upon the members' freedom of association.[12] Similarly, summonses for records of religious organizations have been challenged as infringing upon the members' right to exercise their religious beliefs.[13] The courts in each of these cases have attempted to create standards that will protect the interests of both the IRS and the taxpayers.

II. BACKGROUND

A. *Administrative Summonses in General*

The basic investigatory tool of the IRS is the administrative summons authorized by I.R.C. Section 7602.[14] The statute grants the IRS broad pow-

6. This claim is based upon I.R.C. § 6001 (Supp. V 1981) and the regulations promulgated thereunder.

7. United States v. Mobil Corp., 543 F. Supp. 507 (N.D. Tex. 1981); United States v. Ohio Bell Tel. Co., 475 F. Supp. 697 (N.D. Ohio 1978). *See infra* notes 87-108 and accompanying text.

8. Marshall v. Barlow's, 436 U.S. 307 (1978); Camara v. Municipal Court, 387 U.S. 523 (1967); See v. Seattle, 387 U.S. 541 (1967). *See also* United States v. Mobil Corp., 543 F. Supp. 507, 517-19 (N.D. Tex. 1981). *See infra* notes 109-19 and accompanying text.

9. United States v. Pittsburgh Trade Exch., Inc., 644 F.2d 302 (3d Cir. 1981); United States v. Island Trade Exch., Inc., 535 F. Supp. 993 (E.D.N.Y. 1982). *See infra* notes 120-28 and accompanying text.

10. United States v. Brigham Young Univ., 679 F.2d 1345 (10th Cir. 1982). *See infra* notes 129-44 and accompanying text.

11. United States v. Brigham Young Univ., 679 F.2d 1345 (10th Cir. 1982), *cert. granted*, 103 S. Ct. 713 (1983); United States v. Pittsburgh Trade Exch., Inc., 644 F.2d 302 (3d Cir. 1981); *In re* John Does, Dairy Cattle Prog., 541 F. Supp. 213 (N.D.N.Y. 1982); United States v. Island Trade Exch., Inc., 535 F. Supp. 993 (E.D.N.Y. 1982). *See infra* notes 146-69 and accompanying text.

12. United States v. Citizens State Bank, 612 F.2d 1091 (8th Cir. 1980). *See infra* notes 170-78.

13. United States v. Grayson County State Bank, 656 F.2d 1070 (5th Cir. 1981), *cert. denied*, 455 U.S. 1920 (1982); United States v. Holmes, 614 F.2d 985 (5th Cir. 1980). *See infra* notes 179-86.

14. I.R.C. § 7602 (1976) provides:
Examination of books and witness

ers to require persons to produce information relevant to the determination or collection of federal taxes. In *United States v. Powell*[15] the Supreme Court analogized the IRS summons to a grand jury subpoena,[16] and held that the government need make no showing of probable cause to obtain enforcement of a summons.[17] A subpoena may be issued, therefore, based on suspicion that the laws have been violated, or merely to ascertain that the law *is* being obeyed.[18]

Although issued by an IRS agent, an administrative summons is enforced only through an order of a federal district court.[19] This enforcement proceeding provides for an impartial judicial officer to determine whether the summons meets all statutory and constitutional requirements. In *Powell*, the Supreme Court held that a summons will be enforced if: 1) the investigation has a legitimate purpose, 2) the information sought is relevant to the purpose, 3) the IRS does not already possess the information, and 4) the summons procedural requirements have been followed.[20]

The *Powell* decision maintained that a taxpayer may challenge a summons on "any appropriate ground."[21] Prior to the Tax Reform Act of 1976,[22] however, taxpayers had little opportunity to challenge a summons served on a third party seeking information about their affairs. In many instances, the third parties (such as banks and credit-card issuers) voluntarily complied with the summons, thereby eliminating the judicial enforcement proceeding.[23] The IRS was not required to notify taxpayers that informa-

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For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary is authorized—

(1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;

(2) To summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary may deem proper, to appear before the Secretary at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry; and

(3) To take such testimony of the person concerned, under oath, as may be relevant or material to such inquiry.

15. 379 U.S. 48 (1964).

16. *Id.* at 57.

17. *Id.*

18. *Id.* at 57-58.

19. I.R.C. § 7402(b) (1976) provides:

To Enforce Summons—

If any person is summoned under the internal revenue laws to appear, to testify, or to produce books, papers, or other data, the district court of the United States for the district in which such person resides or may be found shall have jurisdiction by appropriate process to compel such attendance, testimony, or production of books, papers, or other data.

20. 379 U.S. at 57-58.

21. *Id.* at 58 (citing Reisman v. Caplin, 375 U.S. 440, 449 (1964)).

22. Pub. L. No. 94-455, 90 Stat. 1699 (codified in scattered sections of 26 U.S.C.).

23. *See generally* Kenderdine, *The Internal Revenue Service Summons to Produce Documents: Powers, Procedures, and Taxpayer Defenses*, 64 MINN. L. REV. 73 (1977); Note, *Taxation: IRS Use of John Doe Administrative Summonses*, 30 OKLA. L. REV. 465 (1977); Comment, *Government Access to Bank*

tion concerning their affairs was being requested from a third party. Even if the taxpayer was aware of the summons, he could not be assured that the third party would assert any defenses in his absence. Moreover, if the summoned third party refused to comply, the taxpayer had no absolute right to intervene in the enforcement proceeding to present his case.[24]

Congress provided a partial remedy in 1976 by creating special procedures for the issuance of third-party summonses. Section 7609(a)(1) requires the IRS to notify a taxpayer whenever a summons concerning his affairs is served upon a statutorily defined third-party recordkeeper.[25] If the taxpayer challenges the summons, the IRS must seek an enforcement order in the district court.[26] The taxpayer now has an absolute right to intervene in the enforcement proceeding and he may raise any appropriate defense.[27]

B. *The John Doe Summons*

Obviously, if the taxpayer's identity is not known, the rights to notice of the summons and to intervene in the enforcement proceeding provide no practical protection. In these situations I.R.C. section 7609(f) provides judicial supervision for IRS use of the John Doe summons by requiring a district court proceeding *before* the summons is issued.[28] In that proceeding, the IRS must establish that: 1) the summons relates to an investigation of particular

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Records in the Aftermath of United States v. Miller *and the Tax Reform Act of 1976*, 14 HOUS. L. REV. 636 (1977).

24. Donaldson v. United States, 400 U.S. 517, 527-30 (1971) (taxpayer may not intervene in third-party summons enforcement proceeding merely because his tax liability is the subject of the summons).

25. I.R.C. § 7609(a)(3) (West Supp. 1983).

Third-party recordkeeper defined.

For purposes of this subsection, the term "third-party recordkeeper" means—

(A) any mutual savings bank, cooperative bank, domestic building and loan association, or other savings institution chartered and supervised as a savings and loan or similar association under Federal or State law, any bank (as defined in section 581), or any credit union (within the meaning of section 501(c)(14)(A));

(B) any consumer reporting agency (as defined under section 603(d) of the Fair Credit Reporting Act (15 U.S.C. 1681a(f)));

(C) any person extending credit through the use of credit cards or similar devices;

(D) any broker (as defined in section 3(a)(4) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(4)));

(E) any attorney;

(F) any accountant; and

(G) any barter exchange (as defined in section 6045(c)(3)).

26. The Tax Equity and Fiscal Responsibility Act of 1982 (Act), Pub. L. No. 97-248, 96 Stat. 324 (codified in scattered sections of 26 U.S.C.), made some changes in this area. Prior to this Act, a taxpayer could stay compliance of the summons by notifying the third party. The new statute requires the taxpayer to file a petition to quash the summons in the appropriate district court within 20 days after receiving notice of the summons. Tax Equity and Fiscal Responsibility Act of 1982, § 331(a), (b) (codified at I.R.C. § 7609(b)(2), (d) (West Supp. 1983).

27. I.R.C. § 7609(b)(1) (West Supp. 1983).

28. I.R.C. § 7609(f) (West Supp. 1983).

Additional requirement in the case of a John Doe summons.—

Any summons described in subsection (c) which does not identify the person with respect to whose liability the summons is issued may be served only after a court proceeding in which the Secretary establishes that—

(1) the summons relates to the investigation of a particular person or ascertainable group or class of persons,

(2) there is a reasonable basis for believing that such person or group or

persons; 2) there is a reasonable basis for believing the person being investigated has not complied with the tax laws; and 3) the information sought is not readily available from other sources.[29]

The John Doe summons requirements provide greater taxpayer protection than the general administrative summons requirements. One major difference is the John Doe summons requirement that the IRS must establish a reasonable basis for believing that the unidentified taxpayer has not complied with the tax laws.[30] This limitation on the traditionally broad investigatory power of the IRS questions the validity of the Supreme Court's analogy in *Powell* between an IRS summons and a grand jury subpoena.[31] A second important difference is that the restrictions of section 7609(f) apply to the issuance of *all* John Doe summonses, whereas the notice requirements of section 7609(a) are only applicable when a summons is served on a third-party recordkeeper.[32]

The legislative history of the Tax Reform Act of 1976[33] suggests section 7609(f) was enacted in response to a congressional belief that the IRS might abuse the summons power in the case of unidentified taxpayers.[34] The legislation appears to have been prompted by the Supreme Court's holding in *United States v. Bisceglia*.[35] Several commentators suggested *Bisceglia* allowed the IRS to use a John Doe summons as a "license to fish" through third-party records.[36] Although the committee reports do not indicate an intent to overrule any particular decision, it is clear Congress was not satisfied that the privacy interests of taxpayers were properly safeguarded.[37]

In *Bisceglia*, the IRS was attempting to learn the identity of a person who had deposited $20,000 in "paper thin, severely disintegrated" $100 bills

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class of persons may fail or may have failed to comply with any provision of any internal revenue law, and

(3) the information sought to be obtained from the examination of the records (and the identity of the person or persons with respect to whose liability the summons is issued) is not readily available from other sources.

29. *Id.*

30. I.R.C. § 7609(f)(2).

31. 379 U.S. at 57. *See supra* notes 15-18 and accompanying text.

32. *See supra* note 25 and accompanying text.

33. Pub. L. No. 94-455, 90 Stat. 1699 (1976).

34. The House Ways and Means Committee explained its rationale for changing the law relating to administrative summonses as follows:

> The Service has instituted an administrative policy designed to establish certain safeguards in this area. Under this policy, IRS representatives are instructed to obtain information from taxpayers and third parties on a voluntary basis where possible. Where a third party summons is served, advanced supervisory approval is required. In the case of a John Doe summons, the advance supervisory approval must be obtained on a high level basis. The committee believes, however, that these administrative changes, while commendable, do not fully provide all of the safeguards which might be desirable in terms of protecting the right of privacy.

H.R. REP. 658, *supra* note 2, at 307; S. REP. 938, *supra* note 2, at 368.

35. 420 U.S. 141 (1975).

36. *See* Note, *The IRS Gets Its Fishing License*—United States v. Bisceglia, 11 GONZ. L. REV. 251 (1976) [hereinafter cited as *IRS Gets Fishing License*]; Note, *Federal Tax Procedure—An Extension of the Summons Authority of the Internal Revenue Service*, 21 LOY. L. REV. 1026 (1975) [hereinafter cited as *Extension of Summons*]; Note, *IRS Subpoena Power to Investigate Unknown Taxpayers*, 50 N.Y.U. L. REV. 177 (1976) [hereinafter cited as *IRS Subpoena Power*].

37. H.R. REP. 658, *supra* note 2, at 307; S. REP. 938, *supra* note 2, at 373.

at a bank.[38] An IRS agent, suspecting unpaid taxes, issued a John Doe summons to the bank requesting all its records for the time period during which the deposits were made. The bank refused to comply and the IRS obtained an enforcement order from the district court.[39] The Sixth Circuit reversed, holding that the section 7602 summons power requires the IRS to identify the person it wishes to investigate.[40]

Chief Justice Burger, writing for the majority, disagreed with this conclusion, emphasizing the practical necessities of the tax collection business. "[I]t would be naive," the Chief Justice maintained, "to ignore the reality that some persons attempt to outwit the system, and tax evaders are not readily identifiable."[41] The opinion suggests that the IRS summons power must be viewed against such a realistic background.

The Court stressed that sections 7601 and 7602 authorize the IRS to investigate *all* persons who may be liable for *any* tax and to summon *any* persons with respect to *any* tax liability.[42] To read these statutes in a restrictive fashion would ignore the fact the IRS "has a legitimate interest in large or unusual financial transactions, especially those involving cash."[43] It would be impractical to investigate such transactions if the IRS was required to ascertain the identities of the persons involved. Such a requirement would frustrate the broad power of inquiry authorized by Congress in section 7601.[44]

Chief Justice Burger's opinion rejected the contention that the Court was permitting the IRS to carry on "fishing expeditions into the private affairs of bank depositors."[45] Because the IRS must enforce a summons through the courts,[46] taxpayers will be protected from improper searches. The Court did not, however, address the practical question of who would challenge a John Doe summons, given that the summoned third party has little at stake.

A second decision, *United States v. Humble Oil & Refining Co.*,[47] apparently convinced Congress that the IRS might engage in "fishing expeditions." The issue in *Humble Oil* was the enforceability of a John Doe summons issued in connection with an IRS research project concerning the extent of tax avoidance among mineral property lessors. The summons requested the names of all mineral lessors who held leases that were surrendered by Humble Oil without production.[48] The Fifth Circuit refused to enforce the summons and held the section 7602 summons authority extended only to investigations of specific individuals. The summons power could not be used

38. 420 U.S. at 142-43.
39. United States v. Bisceglia, 72-1 U.S. Tax Cas. (CCH) ¶ 9474 (D.C. Ky. 1972).
40. Bisceglia v. United States, 486 F.2d 706, 710 (6th Cir. 1973).
41. 420 U.S. at 145.
42. *Id.* at 149.
43. *Id.*
44. *Id.* at 150.
45. *Id.*
46. *Id.* at 151.
47. 488 F.2d 953 (5th Cir. 1974), *vacated and remanded*, 421 U.S. 943, *aff'd per curiam*, 518 F.2d 747 (5th Cir. 1975).
48. 488 F.2d at 954.

to conduct general research projects.[49]

The Supreme Court vacated the Fifth Circuit's decision and remanded the case for reconsideration in light of the holding in *Bisceglia*.[50] On remand, the Fifth Circuit again concluded the summons was unenforceable.[51] The court distinguished *Bisceglia* as involving an ongoing particularized investigation which presented facts indicating tax evasion.[52] In contrast, *Humble Oil* involved a research project that might reveal liability for unpaid taxes only as a result of an IRS fishing expedition.[53]

Justices Blackmun and Powell in their concurring opinion in *Bisceglia* observed that a John Doe summons may be used to learn the identity of a particular person whose transactions "strongly suggest liability for unpaid taxes."[54] The Fifth Circuit's holding in *Humble Oil* is in agreement with this interpretation.[55] If this more limited view of the summons power had been generally accepted, it is doubtful Congress would have enacted section 7609(f). The legislative history of section 7609 indicated, however, that Congress feared *Bisceglia* allowed the IRS to roam at will through third-party records in order to discover liability for unpaid taxes.[56]

III. WHEN MUST THE JOHN DOE SUMMONS BE USED

A. *The Dual Purpose Summons*

Many of the questions about John Doe summonses have arisen in connection with the burgeoning phenomenon of barter exchanges. These entities operate as clearinghouses for exchanges of goods and services between exchange members. Each member is credited with units in proportion to the dollar value of the goods and services he provides. These units are then traded for goods and services contributed by other exchange members.[57]

With few exceptions,[58] an exchange of property is a taxable event which is to be reported as income by each party to the exchange. The amount of reportable income equals the difference between the value of the property received and the adjusted basis of the property contributed. In the barter exchange context, the IRS views the taxable event as occurring when the member's account is credited with units having an ascertainable market value.[59] IRS experience indicated exchange members frequently failed to report income from barter exchange transactions.[60]

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49. 488 F.2d at 962-63.
50. 421 U.S. 943 (1975).
51. 518 F.2d at 748-49.
52. *Id.*
53. *Id.*
54. 420 U.S. at 151 (Blackmun, J., concurring).
55. 518 F.2d at 748-49.
56. H.R. REP. 658, *supra* note 2, at 307; S. REP. 938, *supra* note 2, at 373. *See generally IRS Gets Fishing License*, *supra* note 36; *Extension of Summons*, *supra* note 36; *IRS Subpoena Power*, *supra* note 36.
57. United States v. Barter Sys., Inc., 82-1 U.S. Tax Cas. (CCH) ¶ 9127 (D. Neb. 1981).
58. Nonrecognition or deferral of gain realized from a property exchange is provided for certain exchanges of "like-kind" property by I.R.C. § 1031 (1976).
59. Rev. Rul. 80-52, 1980-1 C.B. 100.
60. Congress responded to the increasing use of barter exchanges as tax avoidance devices in the Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324

The IRS sought to discourage the use of barter exchanges as a tax avoidance device by selecting a high proportion of exchange members for audit.[61] To identify exchange members, the IRS summoned membership lists in the course of exchange audits. These summonses have been resisted on the grounds that the IRS is seeking information about unidentified taxpayers without following the John Doe summons requirements[62] or that the information is for a general research project and therefore contrary to the *Humble Oil* ban on general research summonses.[63]

In *United States v. Constantinides*,[64] a district court enforced a summons for a barter exchange's membership list even though the IRS clearly intended to use the information in connection with a research project. The summons was enforced because the information requested was relevant to a determination of the exchange's tax liability.[65] The summons was not invalid merely because it might also be useful for an IRS research project.[66]

Not all courts agree with the *Constantinides* rationale. In *United States v. Gottlieb*,[67] the court held the IRS must follow John Doe summons procedures whenever they request information about unidentified taxpayers from a third party.[68] The court reasoned that if the IRS could obtain information about unidentified taxpayers while auditing a third party, they would never have to use the John Doe summons procedures.[69]

A Nebraska district court, in *United States v. Barter Systems, Inc.*,[70] followed a rationale similar to *Gottlieb* in concluding that section 7609(f) was intended to make a firm distinction between investigations of identified and unidentified persons. The opinion indicates section 7609(f) was intended by Congress to be a limitation on the broad investigative powers of the IRS.[71] Therefore, a summons issued in the course of an audit must comply with the special John Doe provisions if the IRS intends to use the information for the primary purpose of investigating unknown persons.[72]

The Eighth Circuit reversed, maintaining that the lower court had construed the scope of the IRS summons power too narrowly.[73] The court indicated the IRS summons authority should be upheld unless it was expressly

(codified in scattered sections of 26 U.S.C.). This Act amended I.R.C. § 6045 (West Supp. 1983), making barter exchanges subject to transaction reporting requirements. The Act also amended I.R.C. § 7609(a) (West Supp. 1983) to classify a barter exchange as a third-party recordkeeper.

61. United States v. Constantinides, 80-2 U.S. Tax Cas. (CCH) ¶ 9830 at 85,733 (D. Md. 1980).

62. *See supra* notes 28-29 and accompanying text.

63. *See supra* notes 47-53 and accompanying text.

64. 80-2 U.S. Tax Cas. (CCH) ¶ 9830 (D. Md. 1980).

65. *Id.* at 85,734.

66. *Id.* at 85,735.

67. 82-1 U.S. Tax Cas. (CCH) ¶ 9257 (M.D. Fla. 1982).

68. *Id.* at 83,561.

69. *Id. Contra* United States v. Barter Sys., Inc., 82-2 U.S. Tax Cas. (CCH) ¶ 9707 (E.D. Mich. 1982).

70. 82-1 U.S. Tax Cas. (CCH) ¶ 9127 (D.C. Neb. 1981), *rev'd*, 82-2 U.S. Tax Cas. (CCH) ¶ 9698 (8th Cir. 1982).

71. 82-1 U.S. Tax Cas. (CCH) at 83,094.

72. *Id.*

73. United States v. Barter Sys., Inc., 82-2 U.S. Tax Cas. (CCH) ¶ 9698 at 85,519-20 (8th Cir. 1982).

prohibited by statute or was contrary to substantial policy interests. The court concluded that section 7609(f) is not a limit on IRS use of a general summons during an investigation of a named taxpayer even though the summons requires disclosure of information relating to unidentified taxpayers whom the IRS might also wish to audit.[74]

The IRS experience in enforcing summonses issued in connection with its Taxpayer Compliance Measurement Program (TCMP) also sheds light on the dual purpose summons issue.[75] The TCMP is a research project designed to evaluate overall compliance with tax reporting requirements.[76] Several thousand taxpayers are selected randomly by computer for intensive audits. The ultimate purpose of the TCMP is to increase the IRS efficiency by concentrating enforcement efforts on specific problem areas.[77]

In *United States v. Flagg*,[78] the IRS sought enforcement of a summons served on a taxpayer selected under the TCMP. Although the district court refused to enforce the summons,[79] the Eighth Circuit reversed, maintaining the IRS summons power must be construed broadly to effectuate congressional intent that the IRS insure compliance with the tax laws.[80] The court concluded that *Humble Oil* did not establish that tax records might never be examined for research purposes; *Humble Oil* only held that a summons must be issued pursuant to a "particularized investigation of an individual taxpayer."[81] The TCMP satisfies this requirement because the summonses are issued to determine a particular individual's tax liability.

Interestingly, the Fifth Circuit concurred in this interpretation of *Humble Oil* in *United States v. First National Bank of Dallas*,[82] which involved the enforcement of a third-party summons issued to a bank, requesting records pertaining to a taxpayer undergoing a TCMP audit.[83] Relying on *Humble Oil*, the district court refused to enforce the summons.[84] On appeal, the Fifth Circuit reversed and explained that *Humble Oil* did not hold that a summons could not be enforced if issued primarily for research purposes. A summons may be used to obtain information for research purposes if the summons is issued to determine the tax liability of a specific taxpayer.[85] Thus, the Fifth Circuit stated that the rationale of *Humble Oil* is limited to cases where a summons is issued *solely* to obtain research data.[86]

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74. *Id.* at 85,519.

75. *See generally* Note, *Enforcing Internal Revenue Service Summonses Under the Taxpayer Measurement Compliance Program: The Need for Statutory Reform*, 10 HOFSTRA L. REV. 861 (1982).

76. [3 Audit] INTERNAL REV. MAN. (CCH) § 4861.1(2) (Aug. 27, 1980).

77. United States v. Flagg, 634 F.2d 1087 (8th Cir.), *cert. denied*, 451 U.S. 909 (1980).

78. *Id.*

79. 45 A.F.T.R. 2d (P-H) 80-618, 80-621 (S.D. Iowa 1979).

80. 634 F.2d at 1091.

81. *Id.* at 1092. *See supra* notes 47-53 and accompanying text.

82. 635 F.2d 391 (5th Cir.), *cert. denied*, 452 U.S. 916 (1981).

83. 635 F.2d at 392.

84. 468 F. Supp. 415 (N. D. Tex. 1979). *See supra* notes 47-53 and accompanying text.

85. 635 F.2d at 395.

86. It should be noted that these TCMP cases are not controlling on the issue of whether a dual purpose summons may be used to obtain information about unidentified persons. The TCMP cases are concerned solely with whether the summons was issued for a proper purpose. Issuance of a John Doe summons also requires a determination of whether § 7609(f) restrictions

B. *The Right to "Inspect" Records*

The IRS has attempted to avoid statutory and judicial restrictions on its use of administrative summonses to conduct general research by asserting a statutory right to inspect documents that taxpayers and third parties are required to maintain.[87] The IRS claims such records may be inspected without issuing a summons. Two courts disagree as to whether there is an absolute inspection right. One court, in *United States v. Mobil Corp.*,[88] held that section 6001 did not imply authority to inspect.[89] Another court, in *United States v. Ohio Bell Tel. Co.*,[90] ruled that statutory authority to require records implies an authority to inspect the records.[91]

1. *United States v. Mobil Corp.*[92]

In *United States v. Mobil Corp.*,[93] the IRS requested a permanent injunction to compel production of records which Mobil kept pursuant to section 6001. The information sought concerned the number of personal exemptions claimed by Mobil's employees on their tax withholding forms and reflected the government's concern over the increasing use of unwarranted exemption claims to reduce the amount of tax withheld from wages. The IRS claimed that its right to inspect these records was implied from both the language of section 6001,[94] and its implementing regulations.[95]

Mobil refused the request, contending that the section 6001 recordkeeping provisions should not be utilized to compel a production of records that could not be obtained by a summons.[96] Mobil suspected that the IRS was requesting the information in connection with a general research project, in which case *Humble Oil* indicated that a summons would not be enforceable.

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apply. *See* United States v. Barter Sys., Inc., 82-2 U.S. Tax Cas. (CCH) ¶ 9698 at 85,518 n.10 (E.D. Mich. 1982).

87. The basis for the claim of a statutory right to inspect is found in I.R.C. § 6001 (Supp. V 1981) which provides:

Notice or regulations requiring records, statements and special returns

Every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the Secretary it is necessary, he may require any person, by notice served upon such person or by regulations, to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not such person is liable for tax under this title. The only records which an employer shall be required to keep under this section in connection with charged tips shall be charge receipts, records necessary to comply with section 6053(c), and copies of statements furnished by employees under section 6053(a).

88. 543 F. Supp. 507 (D.C. Tex. 1981).

89. *Id.*

90. 475 F. Supp. 697 (N.D. Ohio 1978).

91. *Id.* at 700.

92. 543 F. Supp. 507 (N.D. Tex. 1981).

93. *Id.* An earlier reported decision in this case by the same court considered Mobil's motion for discovery. 499 F. Supp. 479 (N.D. Tex. 1980).

94. The IRS asserted its right to inspect was inherent in the language of section 6001 that requires "maintenance" of records for tax liability.

95. 543 F. Supp. at 509. In Treas. Reg. § 31.6001-1(e)(1) (1960) the Secretary declared "[a]ll records required by the regulations in this part shall be kept, by the person required to keep them, at one or more convenient and safe locations accessible to internal revenue officers, and shall at all times be available for inspection by such officers."

96. 543 F. Supp. at 508.

Also, if no specific employees were under investigation, the IRS would have to comply with the John Doe summons procedures.[97]

Mobil sought to discover the purpose for the IRS inspection by serving a subpoena *duces tecum* and requesting documents that would reveal the identities of any employees under investigation by the IRS. On an IRS motion to quash the subpoena, Mobil argued that any inspection right conferred by section 6001 is analogous to the summons power granted by section 7602. Thus, it should enjoy all the statutory and procedural rights that would be available in a summons enforcement proceeding.

The district court quashed the subpoena, holding that whatever result would obtain in a summons enforcement proceeding is not dispositive with respect to the scope of discovery under section 6001.[98] A preliminary inquiry into the IRS purpose for an inspection is unnecessary with respect to section 6001 because the inspection causes only a limited disruption and intrusion into the privacy of the inspected party. Conversely, section 7602 provides a far greater reach with respect to the parties, subject matter, and type of testimony that may be summoned. It is this "sweeping and intrusive" nature of the summons power that necessitates the judicial restrictions set forth in *Powell* as well as the requirement that the summons be issued only with respect to specific and well-defined investigations. The court concluded in the discovery order that the government may demand an inspection of records even though its purpose is to avoid statutory and judicial restrictions on the issuance of a summons.

Judge Higginbotham clearly had second thoughts about this discovery order. In granting Mobil's motion for summary judgment, the court held that the IRS derives no inspection authority from section 6001. In order to compel an inspection, the IRS must issue a summons pursuant to section 7602.[99] The court did not find an implied right to inspect because to construe section 6001 otherwise would raise serious constitutional questions.[100] To avoid these constitutional difficulties, the court indicated the IRS was obligated to construe section 6001 narrowly.[101]

2. *United States v. Ohio Bell Telephone Co.*[102]

In contrast to the *Mobil* case, *United States v. Ohio Bell Telephone Co.* provides judicial support for the IRS interpretation of its inspection authority. *Ohio Bell* concerned an IRS investigation into the validity of excise tax exemptions claimed by Ohio Bell customers.[103] Although the tax is paid by the customer, it is collected and paid to the IRS by the telephone company.

97. *See supra* notes 29-32 and accompanying text.

98. 499 F. Supp. at 484.

99. 543 F. Supp. at 519. *See supra* note 14 and accompanying text.

100. *Id.* at 511-16.

101. This construction process begins with an exhaustive analysis of the relevant legislative history, which, the court concludes, presents no clear picture of congressional intent. Without such guidance, the rules of construction mandate that the statute be construed in a manner that avoids constitutional difficulties.

102. 475 F. Supp. 697 (N.D. Ohio 1978).

103. *Id.* at 699.

Certain organizations[104] could obtain exemptions from the tax by submitting an exemption certificate and supporting documents to the telephone company.[105] The regulations require these certificates to be made available for inspection.[106]

In the course of its investigation of Ohio Bell subscribers, the IRS requested access to the exemption certificates and documents. Ohio Bell refused to comply with the request. In an action instituted by the IRS to compel production of the documents, Ohio Bell maintained that the IRS must first issue a summons and comply with the John Doe notice provisions.[107] The court rejected this contention and found that section 6001 authority to require recordkeeping implied a grant of authority to inspect the records without issuing a summons.[108]

3. The Fourth Amendment Issue

The constitutional problem perceived by the *Mobil* court stems from the Supreme Court's decision in *Marshall v. Barlow's, Inc.*[109] In *Barlow's* the Court declared the Occupational Safety and Health Act of 1970 (OSHA)[110] unconstitutional to the extent it authorized the Secretary of Labor to conduct nonconsensual, warrantless, administrative inspections of business work areas. As in *Mobil*, the inspection in *Barlow's* was not initiated in response to a specific complaint, but was the result of OSHA's routine compliance selection process.

The Court held that a warrant, or its equivalent, must be obtained before nonconsensual searches are conducted. This procedure insures that "the inspection is reasonable under the Constitution, is authorized by statute, and is pursuant to an administrative plan containing specific neutral criteria."[111] The warrant requirement also serves to advise the owner of the

104. I.R.C. § 4253 (1976).

105. 26 C.F.R. § 49.4253-11 (1982).

106. 26 C.F.R. § 148.1-4(g) (1982).

107. 475 F. Supp. at 699. *See supra* notes 29-32 and accompanying text.

108. *Id.* at 700. The *Mobil* court rejected this rationale because it found no language in § 6001 to support the conclusion that the statute grants "implicit authority" to inspect records. The requirement that records be available for inspection does not necessarily allow them to be inspected without the protections provided by summons enforcement procedures. Thus, the IRS regulations go beyond the authority granted by the statute. *See* 543 F. Supp. at 511.

109. 436 U.S. 307 (1978). The constitutional questions raised by warrantless administrative searches of business and residential areas have been discussed in a number of excellent articles. *See generally* McManis & McManis, *Structuring Administrative Inspections: Is There Any Warrant For A Search Warrant?*, 26 AM. U.L. REV. 942 (1977); Note, *Administrative Searches and the Implied Consent Doctrine: Beyond the Fourth Amendment*, 43 BROOKLYN L. REV. 91 (1976); Note, Camara, *See and Their Progeny: Another Look at Administrative Inspections Under the Fourth Amendment*, 15 COLUM. J. L. & SOC. PROBS. 61 (1979); Note, *Rationalzing Administrative Searches*, 77 MICH. L. REV. 1291 (1979); *Administrative Search Warrants*, 58 MINN. L. REV. 155 (1967).

110. Pub. L. No. 91-596, 84 Stat. 1590 (codified at 29 U.S.C. §§ 651-678 (1976 and Supp. V 1981). The statute provides that an employer must "make, keep and preserve, and make available" to the Secretary of Labor or the Secretary of Health, Education and Welfare such records as the Secretary of Labor may prescribe by regulation. 29 U.S.C. § 657(c)(1) (1976).

The regulations issued pursuant to this authority authorize inspectors to "review records required by the Act . . . and other records which are directly related to the purpose of the inspection." 29 C.F.R. § 1903.3 (1982).

111. 436 U.S. at 323. In discussing the Secretary's contention that requiring warrants seriously burdens the enforcement process, the Court noted that warrants for administrative

premises of the "scope and objects of the search, beyond which limits the inspector is not expected to proceed."[112]

In *Mobil*, the court indicated that the undefined scope of the warrantless inspection authority claimed by the IRS created constitutional problems similar to those presented in *Barlow's*.[113] The court noted that the IRS interpretation of section 6001 would allow it to "unilaterally determine the scope of its inspection rights."[114] The court interpreted *Barlow's* as rejecting such broad administrative latitude and requiring judicial supervision over agency record inspections.[115]

The court's conclusion in *Mobil* that this judicial supervision necessitates the issuance of a summons is, however, questionable. The *Barlow's* requirement of review by a neutral officer is satisfied by a "warrant or its equivalent."[116] The Fifth Circuit's decision in *United States v. Mississippi Power & Light Co.*[117] suggests the IRS procedures for enforcing record inspections may provide a warrant equivalent. The court in *Mississippi Power* ruled that Department of Labor procedures providing resort to a federal court prior to the inspection are the type of warrant equivalent contemplated by the Court in *Barlow's*.[118]

The court interpreted the *Barlow's* warrant equivalent standard as mandating judicial review of an inspection request *before* an inspection.[119] Under this view, requiring the IRS to obtain an injunction to enforce its inspection right provides adequate constitutional protection because a court will determine the reasonableness of the search before it is conducted.[120]

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searches do not require probable cause in the criminal law sense, but instead require only that reasonable legislative and administrative standards be followed in selecting an establishment for inspection. This category of "administrative" probable cause was created by the Court in the companion cases of Camara v. Municipal Court, 387 U.S. 523 (1967) and See v. City of Seattle, 387 U.S. 541 (1967). The less demanding standard recognized that effective regulatory programs often require the deterrent effect of unannounced, random inspections. An administrative warrant only requires a showing that "a valid public interest justifies the intrusion." *Camara*, 387 U.S. at 539.

In later cases, the Court held that a warrant need not be obtained in all circumstances. In Colonnade Catering Corp. v. United States, 397 U.S. 72 (1970) and United States v. Biswell, 406 U.S. 311 (1972), the Court concluded that valid warrantless searches could be conducted with respect to industries that historically have been pervasively regulated and which require frequent, unannounced inspections for effective law enforcement. Thus, persons in industries such as those involving firearms or liquor are deemed to have impliedly consented to the inspections. *Biswell*, 406 U.S. at 316; *Colonnade*, 397 U.S. at 74-77. The *Barlow's* decision indicates this "implied consent" doctrine will not be extended to permit warrantless inspections merely because an industry engages in interstate commerce or is subject to governmental regulation.

112. 436 U.S. at 323.

113. 543 F. Supp. at 518-19.

114. *Id.*

115. *Id.*

116. 436 U.S. at 325.

117. 638 F.2d 899 (5th Cir.), *cert. denied*, 454 U.S. 892 (1981).

118. 638 F.2d at 907.

119. *Id.*

120. The inquiry into the reasonableness of a particular search is held to require consideration of three elements. *Id.* at 907. The first is whether there is statutory authority for the proposed search. The second is whether the scope of the search is properly limited. The third element requires an examination of whether the standards used by the agency in choosing to initiate a particular search satisfy the fourth amendment standards of reasonableness. The decision must be based upon evidence of an existing violation, upon reasonable legislative or admin-

IV. ISSUING AND ENFORCING JOHN DOE SUMMONSES

A. *Reasonable Basis*

IRS reluctance to use section 7609(f) procedures reflects its uncertainty about its ability to demonstrate a reasonable basis for believing someone has not complied with the tax laws.[121] In most instances where John Doe summonses have been sought, the IRS has asserted two bases for meeting this statutory requirement. The first is that the transaction involved is inherently suspicious as susceptible to tax cheating.[122] The second is that examinations of taxpayers in similar situations indicate a high degree of improper reporting.[123]

Most courts have agreed that either of these circumstances alone can provide the reasonable basis required for issuing a John Doe summons. For example, in *United States v. Pittsburgh Trade Exchange, Inc.*,[124] the Third Circuit upheld a summons demanding production of a barter exchange's membership list and bartering transaction records.[125] The holding was supported principally by a revenue agent's testimony that barter transactions "are inherently susceptible to tax error."[126] Similarly, the Sixth Circuit held that the fact members of barter exchanges "historically, exhibited numerous errors in the reporting of non-cash transactions" constituted a reasonable basis for investigating members of a particular exchange.[127] In *United States v. Island Trade Exchange, Inc.*,[128] the court allowed issuance of a John Doe summons because the IRS met the rational basis standard by establishing that the "unique and nontraditional features of bartering transactions cause taxpayers to omit or improperly report income."[129]

Evaluation of whether the IRS belief in a particular case is reasonable is quite subjective as was illustrated in *United States v. Brigham Young University*.[130] In that case, the IRS asserted a reasonable basis derived from its audit experience with 162 returns of property donors to the university.[131] Every one of the returns revealed substantial overvaluations of the contributed property. Because the vast majority of these overvaluations involved contributions of art objects or silver mining claims arranged by particular dealers or appraisers, Brigham Young University (BYU) offered to identify the donors of such property. The IRS refused this offer and obtained an *ex*

istrative standards, or, the search must be made "pursuant to an administrative plan containing specific neutral criteria." *Id.* at 907 (quoting *Barlow's*, 436 U.S. at 323).

121. I.R.C. § 7609(f)(2) (West Supp. 1983). *See supra* note 13.

122. United States v. Pittsburgh Trade Exch., Inc., 644 F.2d 302 (3d Cir. 1981); United States v. Island Trade Exch., Inc., 535 F. Supp. 993 (E.D.N.Y. 1982).

123. United States v. Brigham Young Univ., 679 F.2d 1345 (10th Cir. 1982), *cert granted*, 103 S. Ct. 713 (1983); United States v. Pittsburgh Trade Exch., Inc., 644 F.2d 302 (3d Cir. 1981); United States v. Maxwell, 81-1 U.S. Tax Cas. (CCH) ¶ 9378 (D. Nev. 1981).

124. 644 F.2d 302 (3d Cir. 1981).

125. *Id.* at 308.

126. *Id.* at 306.

127. *In re* John Does, 671 F.2d 977, 980 (6th Cir. 1982).

128. 535 F. Supp. 993 (E.D.N.Y. 1982).

129. *Id.* at 997.

130. 679 F.2d 1345 (10th Cir. 1982), *rev'g*, 485 F. Supp. 534 (D. Utah 1980), *cert. granted*, 103 S. Ct. 713 (1983).

131. 485 F. Supp. at 536.

parte order allowing it to serve a John Doe summons for the names of *all* persons who donated property.[132]

In the subsequent enforcement proceeding, the court refused to enforce the summons. The fact that many BYU donors overvalued their gifts did not provide a reasonable basis for believing other donors had overvalued their gifts.[133] The court was not persuaded by the IRS statistical argument that the large number of improper deductions discovered made it likely that other donors had also overstated the value of their contributions.[134]

On appeal, the Tenth Circuit rejected the district court's interpretation of the reasonable basis standard.[135] The court compared this case to the cases of *Columbus Trade Exchange*[136] and *Pittsburgh Trade Exchange*,[137] where the IRS statistical experience had been with members of *other* barter exchanges. Supported by these cases in two other circuits, the court concluded that the fact each of the 162 donors examined had overvalued their gifts made it reasonable to believe at least some of the remaining 150 donors had overvalued their gifts.[138]

One issue not explored in *Brigham Young University* is the validity of the statistical evidence upon which the IRS established its reasonable basis. It must be noted that all the determinations about the overvalued contributions were made by the IRS.[139] It is possible that a number of the findings were incorrect and certainly all were subject to challenge in the administrative appeals process or in the courts.

This statistical question was raised in *United States v. Maxwell*,[140] where the IRS sought enforcement of a John Doe summons demanding the membership list of a Nevada barter exchange. To establish a reasonable basis for the summons, the IRS presented the results of two annual surveys of the audits of members of a large Los Angeles barter exchange.[141] The 1976 survey indicated fifty-nine percent of the active members failed to report any income from their barter transactions, while the 1977 survey showed seventy-two percent failed to report. The IRS also asserted that statements made by the exchange's proprietor, to the effect that he knew members were not reporting income, established a second reasonable basis for the summons.[142]

The court straddled the issue, somewhat, in holding that the IRS surveys "may not . . . standing alone" be sufficient to establish a reasonable basis.[143] The court noted "[t]he survey was not an independent study by unbiased researchers," and observed that "the results of any study are only

132. *Id.* at 535.
133. *Id.* at 538.
134. *Id.*
135. 679 F.2d at 1349.
136. 671 F.2d 977 (6th Cir. 1982).
137. 644 F.2d 302 (3d Cir. 1981).
138. 679 F.2d at 1350.
139. 485 F. Supp. at 536.
140. 81-1 U.S. Tax Cas. (CCH) ¶ 9378 (D. Nev. 1981).
141. *Id.* at 87,026-27.
142. *Id.* at 87,025-26.
143. *Id.* at 87,029.

as reliable as the methodology employed."[144] The summons was, however, enforceable because the survey results together with the proprietor's statements established the requisite reasonable basis.[145]

B. *Challenging the John Doe Summons*

A fundamental question about section 7609(f)[146] is whether it created new substantive limitations on the IRS summons power or whether it merely provided additional procedural requirements. Congress directed the district courts to authorize the service of a John Doe summons in an *ex parte* proceeding based "solely upon the [IRS] petition and supporting affidavits."[147] This language has been interpreted to allow the summoned party to challenge the enforcement of a summons by attacking the sufficiency of the IRS showing with respect to issuance of the summons.[148] The effect of this interpretation is to make a sharp distinction between the enforcement standards for John Doe and other administrative summonses. Some courts, however, have maintained that Congress did not intend to create such a distinction, precluding later challenges to the *ex parte* findings.[149]

The disagreement on this issue results from different analyses of the Supreme Court's opinion in *Powell*.[150] If *Powell* is interpreted as being primarily concerned about IRS abuse of its summons powers, then the grounds for challenging enforcement of a summons should be quite broad. In contrast, if *Powell* is viewed as rejecting any probable cause requirement for enforcement of an IRS summons, a taxpayer may not challenge the *ex parte* reasonable basis findings in a subsequent proceeding to enforce the summons. Using this more restrictive interpretation, section 7609(f) only provides a new *procedure* to restrain IRS use of John Doe summonses; under this approach no new substantive ground for challenging a summons has been created.

The practical effect of allowing a summoned party to challenge the issuance of a John Doe summons at an enforcement proceeding is to convert the *ex parte* inquiry into an adversarial contest. In *Brigham Young University*,[151] the Tenth Circuit indicated the Supreme Court mandated such a contest.[152] The court quoted *Reisman v. Caplin*[153] as authority for its contention that a summons enforcement proceeding is an adversarial determination of the issues wherein a "witness may challenge the summons on any appropriate

144. *Id.* at 87,028.

145. *Id.* at 87,029.

146. *See supra* note 25.

147. I.R.C. § 7609(h)(2) (West Supp. 1983).

148. United States v. Brigham Young Univ., 679 F.2d 1345 (10th Cir. 1982), *cert. granted*, 103 S. Ct. 713 (1983); United States v. Island Trade Exch., Inc., 655 F. Supp. 993 (E.D.N.Y. 1982).

149. Agricultural Asset Management Co. v. United States, 688 F.2d 144 (2d Cir. 1982); United States v. Pittsburgh Trade Exch., Inc., 644 F.2d 302 (3d Cir. 1981); *In re* John Does, 541 F. Supp. 213 (N.D.N.Y. 1982).

150. *See supra* notes 15-21 and accompanying text.

151. 679 F.2d 1345 (10th Cir. 1982).

152. *Id.* at 1348.

153. 375 U.S. 440 (1964).

ground."[154] *Powell* is cited as authorizing the courts to "inquire into the underlying reasons" for an IRS investigation.[155] A similar rationale was adopted by one New York district court in *United States v. Island Trade Exchange, Inc.*[156] The court in *Island Trade Exchange* viewed section 7609(f) as encompassed by the requirements in *Powell* that a summons meet all the administrative provisions of the Code.[157]

In re John Does[158] heard by a second New York district court, rejected the view that the *ex parte* findings could be challenged in the summons enforcement proceedings.[159] The court noted that permitting a redetermination of the *ex parte* hearing issues would render the *ex parte* proceeding unnecessary and would interfere with IRS investigatory powers.[160]

The Second Circuit resolved this difference of opinion by holding that the section 7609(f) criteria are not appropriate grounds for challenging enforcement of a summons.[161] An analysis of the statute's legislative history persuaded the court that Congress did not intend for questions about the issuance of summonses to become entangled in adversarial proceedings.[162] To hold otherwise "would make the ex parte proceeding superfluous," a result Congress can hardly have intended.[163]

In *Pittsburgh Trade Exchange*,[164] the Third Circuit also stated that the section 7609(f) criteria cannot serve as an additional substantive basis for challenging summons enforcement.[165] The court's opinion, however, was based on a different and more questionable analysis of the statute's legislative history. This opinion noted that a major portion of section 7609 is concerned with providing notice to taxpayers when summonses regarding their affairs are served upon third parties. From this, the court concluded the thrust of section 7609(f) is to provide procedural safeguards for unidentified taxpayers who cannot be notified.[166] Because the *ex parte* proceeding is essentially a substitute for notice, the criteria used in the *ex parte* proceeding were not intended to create substantive defenses to summons enforcement.[167]

While the court's conclusion may be valid, the legislative history does not support the view that section 7609(f) is primarily concerned with the problem of notice.[168] The placement of this subsection among the general

154. 679 F.2d at 1348 (quoting *Reisman*, 375 U.S. at 449).
155. 679 F.2d at 1348 (quoting *Powell*, 379 U.S. at 58).
156. 535 F. Supp. 993 (E.D.N.Y. 1982).
157. *Id.* at 996.
158. 541 F. Supp. 213 (N.D.N.Y. 1982).
159. *Id.* at 218.
160. *Id.* at 218-19. This reasoning echos that of *Powell*. The Court rejected the probable cause requirement for IRS summonses "because it might seriously hamper the Commissioner in carrying out investigations he thinks warranted, forcing him to litigate and prosecute appeals on the very subject which he desires to investigate. . . ." 379 U.S. at 54.
161. Agricultural Asset Management Co. v. United States, 688 F.2d 144 (2d Cir. 1982).
162. *Id.* at 149.
163. *Id.*
164. 644 F.2d 302 (3d Cir. 1981).
165. *Id.* at 306.
166. *Id.*
167. *Id.*
168. H.R. REP. 658, *supra* note 2, at 307; S. REP. 938, *supra* note 2, at 368.

third-party recordkeeping provisions appears to be more a matter of convenience than affinity. The Committee Reports clearly indicate that section 7609(f) is directed at curbing potential IRS abuse of John Doe summonses.[169]

It is equally clear Congress did not intend to establish a new basis for resisting enforcement of summonses. Congress understood the importance of the John Doe summons as an investigatory tool and did not intend John Doe summons provisions to impose an excessive burden on the IRS.[170] By mandating an *ex parte* proceeding, Congress apparently recognized that permitting an adversarial contest on the reasonable basis question would inhibit the use of John Doe summonses.

V. THE FIRST AMENDMENT ISSUES

The possibility that the government may learn the names of members of controversial political, religious, or similar organizations inhibits participation by some people who might otherwise join or support these groups. In light of this reality, the courts have recognized that the constitutional right to freedom of association depends in great measure upon an ancillary right to privacy in one's associations.[171] Thus, an investigation that would infringe upon associational privacy is permissible only where the government can demonstrate a substantial relationship between the information requested and a compelling state interest.[172]

An illustration of how this constitutional protection may limit the IRS summons power is presented in *United States v. Citizens State Bank*,[173] where an organization of tax protestors, the United States Taxpayers Union (USTU), sought to prevent the IRS from summoning bank records that could reveal the identities of its members and contributors.[174] The summons was issued to a bank during an investigation of a USTU officer who had not filed an income tax return for ten years. The IRS requested all bank records for the officer's personal account and for a USTU account controlled by the officer. The bank did not comply with the summons. In an IRS action to enforce the summons, the officer and the USTU intervened alleging that release of the records would identify members and contributors of the organization. The intervenors claimed that giving the IRS access to USTU records would discourage persons from joining or contributing to the organization out of

169. *Id.*

170. H.R. REP. 658, *supra* note 2, at 306; S. REP. 938, *supra* note 2, at 373.

171. Gibson v. Florida Legislative Investigation Comm., 372 U.S. 539 (1963) (committee request for NAACP membership lists in connection with investigation of Communist Party denied because state did not demonstrate a substantial relation between the information sought and a subject of overriding and compelling state interest); NAACP v. Alabama, 357 U.S. 449 (1958) (state request for NAACP membership lists denied because state could not justify the infringement on right of freedom of association); Pollard v. Roberts, 283 F. Supp. 248 (E.D. Ark.), *aff'd per curiam*, 393 U.S. 14 (1968) (no compelling government interest shown for subpoena requiring production of records identifying contributors to Republican Party). *But see* Laird v. Tatum, 408 U.S. 1 (1972) (Army Intelligence system for surveillance of lawful political activity did not, by itself, have a chilling effect upon constitutional freedoms).

172. Gibson v. Florida Legislative Investigation Comm., 372 U.S. 539, 546 (1963).

173. 612 F.2d 1091 (8th Cir. 1980).

174. *Id.* at 1093.

fear of IRS retaliation.[175] To support this contention, the USTU sought to introduce evidence on the adverse effects such an IRS summons would have on its activities. The district court, however, deemed this evidence irrelevant and enforced the summons.[176]

The Eighth Circuit Court of Appeals reversed, holding that a *prima facie* showing of a first amendment infringement required the IRS to establish an appropriate need for the material.[177] The IRS must demonstrate that there is a rational connection between disclosure of the information and a legitimate and compelling government interest.[178] On remand the district court was ordered to determine whether disclosure of the bank records would adversely affect USTU's freedom of association and, if so, whether the government had a compelling need for the information. The court emphasized, however, that its decision would "only rarely serve to limit the reach of an IRS summons."[179]

Just how rare is illustrated by the Fifth Circuit's decision in *United States v. Holmes*,[180] involving a summons issued during an investigation into the exempt status of a church. Although the court found the summons too broad to meet the restrictive statutory standard of I.R.C. section 7605(c), which permitted examination of church records only to the extent necessary,[181] the likelihood of a subsequent narrower summons impelled the court to consider the constitutional issue.[182] The church asserted that any summons for documents relating to its internal affairs would infringe upon its members' free exercise of religion.[183] The court held, however, that although the summons might create an incidental burden upon religious activities, this burden was balanced by the government's substantial interest in its fiscal integrity.[184]

In the later case of *United States v. Grayson County State Bank*,[185] the same court indicated that religious free exercise cases are distinguishable from the essentially political situation presented in *Citizens State Bank*. The court con-

175. *Id.*
176. *Id.* at 1094.
177. *Id.*
178. *Id.* (quoting Pollard v. Roberts, 283 F. Supp. at 248).
179. *Id.*
180. 614 F.2d 985 (5th Cir. 1980) (*per curiam*).
181. I.R.C. § 7605(c) (1976) *Restriction on Examination of Churches*—
No examination of the books of account of a church or convention or association of churches shall be made to determine whether such organization may be engaged in the carrying on of an unrelated trade or business or may be otherwise engaged in activities which may be subject to tax under part III of subchapter F of chapter 1 of this title (sec. 511 and following, relating to taxation of business income of exempt organizations) unless the Secretary (such officer being no lower than a principal internal revenue officer for an internal revenue region) believes that such organization may be so engaged and so notifies the organization in advance of the examination. No examination of the religious activities of such an organization shall be made except to the extent necessary to determine whether such organization is a church or a convention or association of churches, and no examination of the books of account of such an organization shall be made other than to the extent necessary to determine the amount of tax imposed by this title.
182. 614 F.2d at 88-89.
183. *Id.*
184. *Id.* at 990.
185. 656 F.2d 1070 (5th Cir. 1981), *cert. denied*, 455 U.S. 920 (1982).

cluded that allowing the IRS access to church records did not restrict religious freedom.[186] The court did not, however, discuss the potential chilling effect an examination of church financial records would have on church members and contributors.[187]

VI. CONCLUSION

The controversies surrounding the John Doe summons legislation indicate that the statute has not protected taxpayer privacy interests, but rather has created a tactic for delaying and hindering IRS investigations. This is the result of a congressional failure to recognize the wisdom of the Supreme Court's longstanding view that the IRS power to summon documents cannot be narrowly construed if the tax laws are to be effectively administered.[188]

Section 7609(f) was enacted because Congress believed that the *Bisceglia*[189] decision authorized IRS fishing expeditions and because it approved of the holding in *Humble Oil*.[190] Yet the rationale in *Bisceglia*, is the better reasoned view. The IRS can protect government revenues only by having access to records of financial transactions. In most cases, access to records will not violate legitimate privacy expectations because the records have been voluntarily thrust into the stream of commerce.

For similar reasons, the IRS should be permitted to collect information concerning potential tax evasion. This does not suggest the IRS should be free to roam through records without purpose, but the IRS should be allowed to accumulate information about specific types of transactions. Limited access to records required to be maintained would protect the IRS interest in tax compliance. Given the judicial role in the injunction process, the recordkeeper's fourth amendment rights would also be protected.

The issue of IRS summons infringements on first amendment rights has not been fully developed. As the courts hear more of these cases, the scope of IRS authority to summon records of churches and political organizations will be defined.

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186. 656 F.2d at 1074. In quoting from *Holmes*, the court noted that even if there is an incidental burden on the free exercise of religion, the burden is justified if a compelling government interest outweighs the degree of impairment. *Id.*

187. The position of the Eighth Circuit on the issue of IRS summonses and religious free exercise is not clear. In United States v. Life Science Church, 636 F.2d 221 (8th Cir. 1980) (*per curiam*) the court remanded the case to the district court for a determination of whether a summons for church records was too broad under § 7605(c). The court *also* ordered a determination of the constitutional issues raised by *Citizens State Bank* and *Holmes*. The court did note, however, that the IRS summons probably was an infringement on the first amendment rights of the Life Science Church. 636 F.2d at 224.

The Ninth Circuit, in United States v. Trader's State Bank, 83-1 U.S. Tax Cas. (CCH) ¶ 9131 (9th Cir. 1983) (*per curiam*), refused to enforce an IRS summons for a church's bank records. Citing *Citizens State Bank*, the court found the IRS had shown no rational connection between the documents sought and a legitimate governmental end.

188. *See supra* note 159 and accompanying text.

189. *See supra* notes 35-46 and accompanying text.

190. *See supra* notes 47-56 and accompanying text.