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TAX PREPARATION AGENCIES: WHAT IS NEEDED FOR THE PUBLIC'S PROTECTION?

Each year, as April 15 approaches, taxpayers are inundated with advertisements urging them to utilize various income tax preparation services. So many taxpayers have heeded the advice that the companies offering these services have proliferated into an expanding industry, an expansion facilitated in part by advances in the computer industry. Obviating the need for personnel thoroughly trained in law or accountancy,[1] these technological changes permit millions of tax returns to be prepared by programming a computer to perform the appropriate calculations and complete the required forms. Moreover, the fact that neither the federal nor any of the state governments have set standards of competency or responsibility for those engaged in the business, unless they are attorneys or public accountants, has also contributed to the rapid increase in the number and variety of tax preparation companies.[2] H & R Block, for example, originated the tax preparation service in 1954, when the IRS ceased preparing returns for taxpayers.[3] Today that company operates over 5,000 offices and franchises in the United States and Canada.[4] It has been joined by a number of competitors who offer one of three basic types of services: personal preparation of the return in consultation with the taxpayer; computer preparations of a return on the basis of data provided by a questionnaire prepared by the taxpayer; and hybrid services utilizing both a client conference and subsequent submission of the data to a computer.[5]

The growth of the industry has been accompanied by a growing governmental concern regarding possible inequitable practices in the solicitation of business and in the preparation of tax returns. Several members of Congress have introduced legislation to regulate the companies by requiring minimum standards of competence for the employees of these firms.[6] In addition, the Federal Trade Commission (FTC) has given notice of intention to file a complaint against H & R Block and Beneficial Corporation for deceptive advertising practices and misuse of confidential information.[7] This comment will examine

1 Illustrative of the fact that sophistication in tax matters is not required is the entry of department stores into the industry—e.g., Sears, Roebuck, J.C. Penney, and Montgomery Ward are in competition for tax return preparation clients. Taxes: Happier Returns, Newsweek, Feb. 23, 1970, at 74 [hereinafter cited as Taxes: Happier Returns].

2 See 117 Cong. Rec. S4749 (daily ed. April 14, 1971) (remarks of Senator Ribicoff).

3 Originally, the brothers Bloch had operated a bookkeeping service in Kansas City, preparing tax statements as a service to their regular customers. H & R Block provides individualized service to each customer, and, by its own estimate, prepares ten percent of the total tax returns in the country. Business Week, March 25, 1967, at 197.

4 Wall Street Journal, April 7, 1971, at 25, col. 3.

5 Taxes: Happier Returns, supra note 1, at 79.

6 Boston Globe, Oct. 11, 1971, at 16, col. 1.

7 Wall Street Journal, July 1, 1971, at 8, col. 1. The FTC has provisionally accepted a consent order prohibiting H & R Block from making certain deceptive claims in adver-

the issues raised by the proposed FTC complaint and the possible improvements which can be made in the industry through enactment of the proposed legislation.

I. The Problem of Incompetence

Three recent surveys[8] indicate the extent of inaccuracy possible in the commercial preparation of tax returns. In each of the investigations, identical sets of data were submitted to several firms which prepared tax returns based on the information supplied. The results were compared to measure discrepancies in preparation costs and to evaluate the precision of the work performed. In one survey, correspondents for *Newsweek* magazine presented to several firms the same hypothetical data based on the income of a mythical taxpayer. When the completed returns were collected, the figures showing tax due varied over a range of $55 and the fee for the services ranged from $9.50 to $22.[9]

In another survey, an Atlanta businessman, with the assistance of a *Wall Street Journal* reporter, compared various tax services in northern Georgia. The taxpayer provided each of five firms with his personal tax information, including data regarding a reimbursement for moving expenses.[10] The investigation revealed that the preparation fees ranged from $15 to $31, with an arithmetic mean of $24. More significant, the standard deviation of the tax computations was $110 from the mean. In other words, two-thirds of the returns showed results scattered over a $220 range, deviating from the mean by as much as $110. When one considers the precision with which tax returns should be calculated, this difference constitutes an extremely wide discrepancy.

Understandably intrigued by these results, the Atlanta surveyist sought the assistance of the Internal Revenue Service. Notwithstanding the fact that the Service no longer prepares returns for taxpayers, the agency agreed to make an exception in this instance because the public would be served by the investigation and its publication. The Service's tax figure was nearly equal to the mean of the amounts com-

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tising and utilizing client personal data without prior permission. FTC, News Summary No. 1 (1972). The provisional acceptance of a cease and desist order by the FTC settles

> a violation or claimed violation of the Federal Trade Commission Act . . . without a formal adjudicative hearing. . . . [T]he decision whether or not this procedure will be utilized is made by the FTC and not a person or company charged with violating the law. Although a formal adjudicative hearing is avoided, the order to cease and desist entered under this procedure has the same force and effect with respect to compliance as an order produced by trial. Civil penalties may be imposed for the violation of such an order.

3 Trade Reg. Rep. ¶ 9595, at 17,096 (1971).

[8] See Wall Street Journal, April 7, 1971, at 1, col. 6; Edwards, The Urban Strategist: Many Happy Returns, New York Magazine, March 15, 1971, at 62 [hereinafter cited as Edwards]; and Taxes: Happier Returns, supra note 1.

[9] Taxes: Happier Returns, supra note 1, at 79.

[10] Wall Street Journal, April 7, 1971, at 1, col. 6.

puted by the five companies.[11] However, considering the high standard deviation in the survey, it is submitted that the similarity between the Service's figure and the mean in no way ameliorates the widespread discrepancies revealed by the survey.

Moreover, the Georgia survey revealed a sizeable variation between two branches of the same company. The total tax due, as computed by one office, exceeded that of the other by $55.[12] Their fees also differed. This intracompany discrepancy was partly due to the fact that the fees were set according to the number of Internal Revenue Service forms utilized; one office had used an additional form. The surveyists also attributed the deviation to clerical errors and to the failure of one consultant to include a medical expense deduction.[13]

Another survey was conducted by a self-employed New York City writer who presented identical tax information to seven tax preparation agencies in New York City.[14] Of the seven firms, Beneficial, a company which utilizes a computer, declined to prepare the surveyist's return because the computer was not equipped to handle the IRS form for self-employed individuals. The remaining agencies surveyed quoted fees ranging from $16 to $125, and two firms offered discounts when the taxpayers appeared reluctant to pay the requested fee. The mean for the preparation charges incurred in this survey was $23.[15] Returns were prepared by four of the firms and their tax computations varied over a range of $245, with a standard deviation of $96.

Other instances of incompetence were revealed in the Georgia and New York surveys: one agency neglected to include a medical expense deduction to which the taxpayer was entitled;[16] another failed to fill in a form for social security assessments for the writer;[17] another entered moving expenses under the travel and entertainment section in order to spare the client the cost of the appropriate IRS form;[18] and several firms did not allow for withheld taxes even though such amounts were noted on the W-2 forms.[19] Although the Georgia survey did not reveal any fraud, one preparer mistakenly entered his company's fee for tax preparation as a deduction.[20] When informed that the taxpayer was not entitled to such a deduction because the pro-

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11 It should be noted that the IRS is not free from error itself. Initially, the Service said that the taxpayer was entitled to a refund of $446.10. Later, when the taxpayer questioned the figure, the IRS agent indicated he had erred in the computation of moving expenses. The correct refund was $400.94. Id. at 25, col. 3.

12 One branch of H & R Block stated that a refund of $487 was due, but another said that the refund should be $542. Id. at 1, col. 6.

13 Id. at 25, col. 3.

14 Edwards, supra note 8, at 62.

15 The discounted fees were used in compiling this statistic.

16 Wall Street Journal, April 7, 1971, at 25, col. 3.

17 Edwards, supra note 8, at 64.

18 Id. at 70.

19 Wall Street Journal, April 7, 1971, at 25, col. 3.

20 Id. at 25, col. 4.

fessional tax advice had not been utilized during the tax year, the preparer attempted to excuse himself by stating that the entry had been mistakenly made for the current year's fee. However, the figures did not support this contention—the amount of the deduction taken was $25, but the actual fee for the current service was $31.[21] Although this discrepancy of itself does not indicate fraudulent activity, it clearly establishes incompetence and places clients in the unenviable position of not knowing whether they are paying an excessive income tax or the absolute minimum required by law.[22]

II. Proposed Federal Legislation

In an attempt to abate the industry's deficiencies as disclosed by the surveys, Senator Abraham Ribicoff has introduced S. 1527, known as the Taxpayer's Protection Act,[23] which would establish a standard of competence for those who prepare tax returns. The proposed legislation would provide for the licensing of those who prepare returns for more than twenty-five taxpayers in a calendar year.[24] Prior to being granted a license, tax preparers would have to meet a predetermined standard of competency and submit to a written examination

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21 Id.

22 "Clients are generally in a position of total helplessness where professional services in tax matters are concerned. . . . Has a disaster occurred because he must pay as much as $10,000 in taxes? Or has he had such fine professional representation that he paid the absolute minimum which the law demands—a mere $10,000?" Rembar, The Practice of Taxes, 54 Colum. L. Rev. 338, 339 (1954).

23 S. 1527, 92d Cong., 1st Sess. (1971).

24 S. 1527, 92d Cong., 1st Sess. § 1(a) (1971) provides:

> Any individual, engaged in the business of preparing returns . . . for others, who meets the standards set . . . by the Secretary . . . may hold himself as a "United States licensed tax return preparer." An individual who prepares more than 25 returns . . . for others, in any calendar year, shall . . . meet the standards set . . . for designation as a "United States licensed tax return preparer."

A subsequently introduced amendment to S. 1527 would exempt attorneys, certified public accountants and enrolled agents from the operation of the law. S. 1527 §1(a), 92d Cong., 1st Sess. (1971).

Although Senator Ribicoff has introduced this exception for the traditional tax professionals, the National Society of Public Accountants (NSPA) has proposed a registration procedure for any person who prepares tax returns for a fee. The NSPA proposal, formulated in response to a request by the IRS for views on the regulation of tax preparers, in substance provides that:

> (1) Every person preparing a return for a fee would be compelled to register with their respective local IRS district director. In addition, each registrant would have to obtain a registration number which must appear on all prepared returns.
>
> (2) Preparing a return for a fee without a valid registration would be punishable as a misdemeanor.
>
> (3) The registration would be valid for a three-year period and renewable upon a showing of continuing technical education in the field of federal taxation.
>
> (4) In order to avoid an implication of government endorsement of registrants, preparers would be prohibited from advertising their registration.

given by the Treasury Department.[25] In addition, the license would be revoked if the licensee engaged in incompetent or unethical behavior.[26] S. 1527 would also authorize the Treasury Department to formulate such standards for preparers of returns as are necessary for effecting the purposes of the Act. Since the effectiveness of the standards to be promulgated by the IRS will determine the success of the program, it is suggested that norms such as those commonly applied to attorneys and public accountants engaged in tax practices would provide a viable standard for nonprofessional tax return preparers.

In the accounting profession, an accountant must exercise diligence in handling the affairs of his client.[27] A public accountant is under a duty to use the due care and caution proper to his calling when employed to supply factual information to an employer, and he must respond in damages if the employer detrimentally relies on the information.[28] In *Bancroft v. Indemnity Insurance Co. of North America*,[29] the liability insurer of a certified public accountant was held liable for the latter's negligent advice in connection with a stock transfer. Specifically, the accountant had advised the plaintiff that no tax liability would be incurred if the plaintiff sold shares of stock to a corporation in which the plaintiff was the principal stockholder. Acting on the advice, the client engaged in two such transactions. Subsequently, a tax exceeding thirty-five thousand dollars was assessed against the plaintiff. In an action to recover this amount from the accountant's insurer, the court held that the insurance company was liable for the loss and that the taxpayer was entitled to compensation for the entire loss occasioned by his reliance on the unsound advice. If a similar standard of diligence were imposed on nonprofessional tax return preparers, low-income taxpayers, unable to afford high-priced professional service, would also be protected against the hazard inherent in relying on unsound tax advice. Thus such taxpayers would be able to recover from the tax preparation agency any additional tax liability incurred because of the agency's mistakes, rather than the currently available relief, which is limited to the penalty or interest the IRS levies on the taxpayer.

(5) The IRS would be empowered to suspend or revoke a preparer's registration for cause. Grounds for suspension would include gross incompetence, fraud, willful misconduct, unethical advertising and similar activities.

8 P-H 1972 Fed. Taxes ¶60,095.

[25] Id. § 1(b).

[26] Id. § 1(c).

[27] Lindner v. Barlow, 210 Cal. App. 2d 660, 665, 27 Cal. Rptr. 101, 104 (Dist. Ct. 1962).

[28] Restatement (Second) of Torts, § 229 A (1965). "If his pretensions are unfounded, he commits a species of fraud upon every man who employs him in reliance on his public profession." 3 Cooley, Torts § 472 (4th ed. 1932). See also Hawkins, Professional Negligence Liability of Public Accountants, 12 Vand. L. Rev. 797 (1959).

[29] 203 F. Supp. 49 (W.D. La. 1962), aff'd, 309 F.2d 959 (5th Cir. 1963).

III. False or Deceptive Advertising

In addition to addressing the issue of incompetence, the federal government has expressed concern regarding advertising practices in the industry. In order to assuage their fear of errors in the compilation of tax data and the completion of tax returns, many taxpayers may rely on advertised representations and decide to utilize a tax preparation service. All the firms investigated in the Georgia survey promised to pay the penalty or interest assessed against the taxpayer as a result of an error on the part of the agency.[30] Many of the firms advertised these warranties extensively. However, in most cases the advertisements are misleading in that taxpayers may be deceived regarding the extent to which the companies are actually bound.

In response to this situation, the FTC gave notice of intention to file a complaint against H & R Block for alleged deceptive advertising practices.[31] Among other representations, Block has advertised that "[w]e guarantee accurate preparation of every tax return. If we make any errors which cost you penalty or interest, we will pay that penalty or interest. That's the H & R Block guarantee."[32] Words to this effect consistently appear in that company's numerous advertisements. The proposed FTC complaint claims that by this advertising H & R Block is representing, directly or by implication, that it will reimburse the client for any tax liability payments required in addition to the originally computed amount, if there was error on the part of the firm.[33] In fact, the company pays only the *penalty* or *interest* incurred and not the additional tax itself; the taxpayer must pay the deficiency. As a result, an unexpected burden is incurred by the clientele H & R Block typically attracts—those with a low, limited income.[34] Typically, these taxpayers pay their taxes or receive a refund, and do not apportion a sufficient sum to adjust a subsequent dispute.[35] If there has been a deficiency in the payment, the govern-

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30 Wall Street Journal, April 7, 1971, at 1, col. 6.

31 New York Times, July 1, 1971, at 57, col. 2.

32 See, Proposed FTC complaint, In re H & R Block, Inc., File No. 712 3433, ¶ 5A6 (announced June 30, 1971) [hereinafter cited as Block Proposed Complaint]; see also, Taxes: The Little Man's Friend, Newsweek, Feb. 10, 1969, at 72.

33 The FTC complaint states that H & R Block's advertisements may be interpreted as meaning that:

> Respondent will reimburse the taxpayer for any payments the taxpayer may be required to make in addition to his initial tax payment, if such additional payment results from an error made by respondent and its representatives in the preparation of the tax return.

But the complaint indicates that:

> Respondent and its representatives [in truth and in fact] do not reimburse the taxpayer for all payments he is required to make in addition to his initial tax payment if such additional payment results from an error made by respondent and its representatives in the preparation of the tax return.

Block Proposed Complaint, supra note 32, at ¶ 7.

34 Most of these taxpayers are in the $5,000 to $15,000 bracket. Taxes: The Little Man's Friend, Newsweek, Feb. 10, 1969, at 71.

35 "[I]t is one thing, in these days of high taxation, to pay a tax which is foreseen

ment will usually assess a penalty against the taxpayer at five percent of the balance due[36] and interest may accumulate at the rate of six percent[37] of the balance. It is at this point that the shocked taxpayer fully realizes that H & R Block has agreed to pay only approximately eleven percent of the client's unexpected liability.

The central issue of the FTC's deceptive advertising allegation is not whether H & R Block advertised an express promise to pay the additional tax, but whether the average taxpayer, seeing and reading the claims, could reasonably believe that H & R Block would pay the difference between the taxpayer's tax liability as erroneously computed by the company and the total amount, including principal and interest, demanded by the government. It is well established that advertising need not be literally false to be restricted from dissemination.[38] Capacity to deceive and not actual deception[39] is the criterion by which advertising practices are judged under the Federal Trade Commission Act.[40] In *P. Lorillard Co. v. FTC*,[41] the Fourth Circuit upheld a cease and desist order issued by the FTC against the plaintiff, notwithstanding the fact that the advertisement involved had contained nothing but truthful statements. The dispute had arisen when Lorillard claimed that a study commissioned by *Reader's Digest* revealed that Lorillard's product, Old Gold Cigarettes, was lowest in tars and nicotine of all brands tested. However, the true import of the article was that one brand of cigarette was the same as any other so

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and provided for, but quite another thing to be faced retroactively, when times have changed, with a large unexpected interest-bearing tax burden resulting from a transaction occurring years before that was unnecessary or was not worth the tax cost." S. Surrey & W. Warren, Cases and Materials on Federal Income Taxation 71 (1962).

36 The Internal Revenue Code provides that "[i]f any part of any underpayment . . . is due to negligence or intentional disregard of rules and regulations (but without intent to defraud), there shall be added to the tax an amount equal to 5 percent of the underpayment." Int. Rev. Code of 1954, § 6653(a). In addition, a 50% penalty is imposed where fraud is involved. Int. Rev. Code of 1954, § 6653(b).

37 Int. Rev. Code of 1954, § 6601(a).

38 FTC v. Sterling Drug, Inc., 317 F.2d 669, 674-75 (2d Cir. 1963).

39 One commentator has stated that:

> The general public has been defined as "[t]hat vast multitude which includes the ignorant, the unthinking and the credulous, who, in making purchases, do not stop to analyze but too often are governed by appearances and general impressions." The average purchaser has been variously characterized as not "straight thinking," and subject to "impressions," uneducated, and grossly uninformed; he is influenced by prejudice and superstition; and he wishfully believes in miracles, allegedly the result of progress in science.
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> The ordinary purchaser is not conversant with the technical cant of the sciences, and he is untrained in the law. Therefore . . . for example . . . [t]he court must only determine whether the public believes that a soap containing [one substance] is better than a soap containing [another substance]. One who subscribes to a book-purchasing plan is ordinarily not qualified to determine the legal rights and benefits of an offer . . . .

Callman, Unfair Competition Trademarks and Monopolies § 19.2(a)(1) (3d ed. 1967).

40 317 F.2d at 674-75, applying Federal Trade Commission Act § 55(a), 15 U.S.C. § 55(a) (1970).

41 186 F.2d 52 (4th Cir. 1950).

far as tar and nicotine content were concerned, and that any differences were minimal.[42] The court found that plaintiff's usage of the study results was a "perversion" which would lead a reader to conclude the antithesis of the *Digest's* findings.[43] The court concluded that in determining whether advertising is false or misleading regard must be given not to "fine spun distinctions" but to the net impression which the claim can be expected to have on the public.[44]

In so holding, the *Lorillard* court relied on the decision in *Charles of the Ritz Distributors Corp. v. FTC*,[45] which had held that there are occasions when the FTC may require total truthfulness in order to protect those who are no more than "fools."[46] Both *Ritz* and a subsequent case, *Ward Laboratories, Inc. v. FTC*,[47] involved advertised claims for cosmetic products. In each case, the court held that the likelihood of deception was so great that the FTC might reasonably exact full disclosure in order to protect the most gullible of consumers. In *Ritz* the court based its holdings on the fact that women are especially susceptible to claims regarding beauty creams;[48] in *Ward*, the court found that men were similarly enticed by the claims for tonics promising increased hair growth,[49] notwithstanding the fact that the claims would be judged patently false by an analytical reader.

For the same reasons that men and women are particularly susceptible to the claims of cosmetic manufacturers, taxpayers may be easily beguiled by the claims of tax preparation companies. The average taxpayer would probably be inclined to accept at face value any promises of assistance in paying his taxes. In fact, the entire theme of H & R Block's commercial messages is that the client can be confident that accurate service has been provided and that, in the "unlikely" event an error has been made, the taxpayer is protected. However, this representation is not completely accurate. Many average readers would not know the technical meaning of "penalty" and thus would not realize the restriction which the term places on the advertised promise: "[w]e will pay that penalty or interest."[50]

FTC complaints are issued for their protective effect: their purpose is to enable the public to rely on representations made in advertisements.[51] For this reason a claim is considered in its entirety and not in piecemeal fashion.[52] Thus, to abate continued use of the alleged

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42 Id. at 57.

43 Id.

44 See note 39 supra.

45 143 F.2d 76 (2d Cir. 1944).

46 Id. at 680.

47 276 F.2d 953 (2d Cir. 1960).

48 143 F.2d at 680.

49 276 F.2d at 954.

50 Block Proposed Complaint, supra note 32, at ¶ 5A3. See also, text at notes 33-38 supra.

51 Goodman v. FTC, 244 F.2d 584, 593 (9th Cir. 1957).

52 Aronberg v. FTC, 132 F.2d 165, 167 (7th Cir. 1942).

misleading claim, the proposed FTC complaint asks that H & R Block be ordered to cease and desist from:

> 1. Using any guarantee without clearly and conspicuously disclosing the terms, conditions and limitations of any such guarantee; or misrepresenting, in any manner, the terms and conditions of any guarantee.
> 2. Representing, directly or by implication, that respondent will reimburse its customers for any payments the customer may be required to make in addition to his initial tax payment. . . .
> 3. Failing to disclose, clearly and conspicuously, whenever respondent makes any representation, directly or by implication, as to its responsibility for, or obligation resulting from, errors attributable to respondent in the preparation of tax returns, that respondent will not reimburse the taxpayer for any deficiency payment assessed against the taxpayer which results from the said errors.[53]

It has been suggested that the allegations of the proposed complaint against H & R Block are applicable to the industry in general.[54]

Federal regulation of deceptive practices is not limited to the area of guarantees. It is also concerned with advertised claims by members of the industry that taxpayers will be represented in subsequent disputes with the IRS stemming from the preparation and filing of tax returns. For example, H & R Block has represented by advertisement that it will provide assistance to clients whose returns are selected for audit by the IRS.[55] The Treasury Regulations allow the individual taxpayer to be represented at an initial meeting before the Audit Division by the person who prepared the return.[56] However, if the dispute proceeds to the District Director's Office, the taxpayer's representative must meet specific standards established by the Treasury Department in order to plead the case.[57] This means that, beyond the audit level, representation would have to be made by attorneys, certified public accountants, or "enrolled agents."[58]

It is unclear whether H & R Block is willing so to represent their clients beyond the audit level. The agency's advertised claim indicates that a taxpayer could reasonably assume that representation would

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[53] Block Proposed Complaint, supra note 32, at 10.

[54] Wall Street Journal, April 7, 1971, at 1, col. 6.

[55] Block Proposed Complaint, supra note 32, at ¶ 5B1. It should be noted that subsequent to the publication of the FTC's proposed complaint against Block, that company now advertises that "if your return is audited we will accompany you, at ***no extra cost***, to the Internal Revenue Service and explain how your return was prepared, ***even though we will not act as your legal representative***." Boston Globe, Feb. 9, 1972, at 30, col. 2 (emphasis added).

[56] Treas. Reg. § 10.7(a)(7) (1966).

[57] Rev. Proc. 68-20, 1968-1 Cum. Bull. 813.

[58] Rev. Proc. 68-20, 1968-1 Cum. Bull. 812 § 3.01.

be provided until the claim is settled by litigation or compromise.[59] However, it is doubtful that Block would incur the expense involved in providing an attorney or certified public accountant as a representative. It is similarly doubtful that Block would provide enrolled accountants. These accountants are highly trained, must pass examinations set by the Treasury Department,[60] and must adhere to the standards of tax practice applied to attorneys by the various state bars, and to accountants by state licensing boards.[61] Moreover, well-trained accountants are probably not attracted to the seasonal employment that tax preparation companies usually offer. In addition, enrolled accountants are precluded from advertising their services, and an association with H & R Block may violate this requirement.[62]

To be sure, H & R Block is not the only allegedly offending tax preparation service, and the FTC plans to move against another member of the industry as well.[63] A proposed complaint against Beneficial Corporation, a large loan company now involved in computerized tax-preparation, includes an allegation of misrepresentation in advertising.[64] Of particular concern to the FTC is Beneficial's promotional material which promises an "instant refund" of money due the taxpayer from the government, if the taxpayer qualifies for a personal loan with the company. If, based on Beneficial's preparation of a client's tax return, the company determines that the taxpayer is entitled to a refund, Beneficial will pay that amount to the client, ostensibly to avoid the delay in waiting for the government's refund check.[65] However, the Commission has alleged in its complaint that the "instant refund" is not a refund at all, but is in reality a personal loan for which the taxpayer is required to pay a finance charge and other costs.[66]

Extensive use of various advertising techniques has generated

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59 One such claim states that Block "will appear with you at an audit without cost to you." Block Proposed Complaint, supra note 32, at ¶ 5B1.

60 Treas. Reg. § 10.4(a) (1966).

61 Treas. Reg. §§ 10.20-.30 (1966).

62 The Treasury Regulations provide:

> No attorney, certified public accountant, or enrolled agent shall solicit employment, directly or indirectly, in matters related to the Internal Revenue Service. For the purposes of this section, solicitation includes, but is not limited to, the advertising of professional attainments or services, the employment of, or the forming of an association or partnership . . . corporation or other organization which solicits in a manner prohibited to attorneys, certified public accountants, and enrolled agents by the provision of this part, or the use of signs, printing, or other written matter . . . .

Treas. Reg. § 10.30 (1966).

63 See Proposed FTC complaint, In re Beneficial Corp., File No. 712 3580 (announced June 30, 1971) [hereinafter cited as Beneficial Proposed Complaint].

64 Id. at ¶ 6.

65 "The instant you sign your return and qualify for an on-the-spot loan, Beneficial advances you the full amount of your refund. So there's no waiting all those weeks and weeks for your check from the government." Id. at ¶ 5(1)(b).

66 Id. at ¶ 7.1.

much of the clientele for tax preparation services. In completing returns for these people, the industry performs a public service by offering inexpensive methods of providing tax advice. However, these companies should not be given an unrestricted license to continue their questionable advertising practices. Unfortunately, the FTC does not have the personnel or resources to supervise these practices on a daily basis.[67] Furthermore, the scope of the Commission's activities is restricted—*i.e.*, a complaint issued by the FTC applies only to the particular firm involved and does not constitute a mandate against industry-wide practices.[68] Even after the FTC decides to move against a firm, the action may not be resolved for several years, especially when the defendant utilizes the full scope of available appellate procedures.[69] Therefore, direct control of the tax preparation industry's advertising practices by the Treasury Department may be more effective.

This control could be effected pursuant to the licensing powers that S. 1527 would grant to the Treasury Department. The threat of license revocation for deceptive advertising practices would, in effect, create a procedure for enforcement of truth-in-advertising within the industry. Furthermore, standards promulgated pursuant to the Treasury Department's regulatory power under S. 1527 could regulate directly the advertising of guarantees in the tax preparation field, and they could be specifically tailored to require freedom from ambiguity.[70]

IV. Misuse of Confidential Information

Beneficial entered the tax preparation industry with the intention of using information obtained from clients for the purpose of promoting the sale of various financial services.[71] Personal data obtained in

[67] "In 1967 the FTC received an appropriation of $14,378,000; of this amount, $6,846,000 was allocated to stopping deceptive practices. This latter figure is less than the combined television advertising budget for Anacin and Bayer during the *first quarter* of 1968." Travers, Foreword to Deceptive Advertising Symposium, 17 Kan. L. Rev. 551, 556 (1969). "It has been pointed out that Procter and Gamble spent $24 million merely to introduce 'Bold,' yet another washday miracle." This amount is almost twice as much as the $14 million the federal government spends annually to operate the FTC. Morse, A Consumer's View of FTC Regulation of Advertising, 17 Kan. L. Rev. 639, 644 (1969). Under such conditions, it is folly to expect the FTC to counteract deceptive practices.

[68] See Comment, Deceptive Advertising, 80 Harv. L. Rev. 1005, 1063-96 (1967), and Travers, supra note 65, at 556-57.

[69] "Lacking preliminary injunctive powers except in the case of false food and drug advertisements . . . the FTC is impotent to prevent deceptive practices until after trial and administrative appeals." Gellhorn, Proof of Consumer Deception Before the Federal Trade Commission, 17 Kan. L. Rev. 559, 560 (1969). See also, Comment, supra note 66, at 1063-96. Illustrative of the time-consuming review procedures which impede the enforcement of FTC orders is Carter Products, Inc. v. FTC, 268 F.2d 461 (9th Cir. 1959). In that case, it took the Commission 16 years to enforce a cease and desist order.

[70] This may be the better solution, particularly since the common law remedies in contract and tort are recognized as being ineffective to meet this problem. See Comment, supra note 68, at 1016-17.

[71] See Business Week, Dec. 20, 1969, at 80:

The refund ploy is, of course, expected to generate a large chunk of tax prepara-

the course of preparing clients' tax returns provided Beneficial with the knowledge and opportunity subsequently to approach these taxpayers with loan offers. As a result of this practice, the FTC has alleged in its complaint that Beneficial preys on the taxpayer's trust by determining a client's financial status in order to sell him a wide variety of financial services.

H & R Block developed a similar plan to sell insurance to its customers in partnership with the Pennsylvania Life Insurance Company of North America.[72] As in its complaint against Beneficial,[73] the FTC has alleged that Block has breached the trust of its clients by using tax information to form lists of names which are segregated according to income brackets. The FTC further alleged that Block uses this list to formulate its own sales programs and then sells the lists to other companies for similar uses.[74] This practice, alleges the FTC, is contrary to the representations made to the taxpayer that the relationship between the client and the firm is a confidential one.[75]

In addition, when an individual or firm is engaged to prepare the income tax return of another, an agency relationship arises.[76] The agent-preparer is then burdened with fiduciary responsibilities. He must act only for the benefit of his principal and, therefore, may not use to the detriment of his principal information acquired in the course of the agency relationship.

In *Chalupiak v. Stahlman*,[77] the defendant-agent was employed by the plaintiff to draw up a deed of sale for land which the latter mistakenly believed he owned. However, the defendant had knowledge that his principal did not have title to the land, and, subsequently bought this property on behalf of his sister. Notwithstanding the fact that the agent had suggested to his principal that title to the land might

> tion business, but it is really a "kicker" to entice people to come in and sign up for a wide range of "family financial services"—especially mutual funds and life insurance—that Benevest's salesmen will peddle after the tax season closes.

Id.

72 Id. H & R Block discontinued its relationship with Pennsylvania Life Insurance Company in January, 1971. A consent order provisionally accepted by Block and the FTC prohibits Block's use of confidential information without the client's prior consent. FTC News Summary No. 1 (1972).

73 The Beneficial Proposed Complaint states: "Respondents . . . retain a copy of each income tax return prepared by them and a copy of a financial profile which is filled out for each customer on the basis of information provided by the customer ostensibly for the respondent's use in the preparation of the customer's tax return." Beneficial Proposed Complaint, supra note 63, at ¶ 8.

74 Id.

75 Block Proposed Complaint, supra note 32, at ¶ 9; and Beneficial Proposed Complaint, supra note 63, at ¶ 9.

76 "Agency is the fiduciary relation which results from the manifestation of consent by one person to another that the other shall act on his behalf. . . ." Restatement (Second) of Agency § 1(1) (1957).

77 368 Pa. 83, 81 A.2d 577 (1951). For differing interpretations of this case, see Note, Agency—Principal and Agent or Master and Servant, 56 Dick. L. Rev. 357 (1952), and Note, 100 U. Pa. L. Rev. 448 (1951).

be vested in the county commissioners, the court ordered the agent to convey the adverse title to the plaintiff. The court reasoned that the agent owed a duty of fidelity to the plaintiff which he violated by the subsequent purchase of the land. Analogously, when an income tax preparation agency elicits financial information from its clients, it acts as a fiduciary. Any information provided by the client in the course of this relationship should not be used to the agent's advantage or the principal's disadvantage.

To curb existing practices which breach fiduciary obligations, legislation has been introduced by Senator Mathias[78] and Representative Gallagher[79] which would greatly circumscribe the purposes for which tax preparation firms may use their client's personal information absent a written release. In pertinent part, this legislation provides:

> Any person who receives any information furnished by a taxpayer to enable such person to prepare or have prepared for such taxpayer a return of the tax imposed by chapter 1 or a declaration of estimated tax required by section 6015 and who—
>
> (1) uses any such information for any purpose other than the preparation of the return or declaration, or makes any such information available to any other person for any such purpose, unless a valid consent . . . to so use such information, or to so make such information available, has been obtained, or
>
> (2) uses any such information, or makes any such information available for a purpose not specified in such valid consent,
>
> shall be guilty of a misdemeanor, and, upon conviction thereof, shall be fined not more than $1,000, or imprisoned not more than 1 year, or both, together with the costs of prosecution.[80]

It is submitted that the legislation's proposed imposition of criminal sanctions to enforce this program will stultify the efficacy of the proposal. Requirements of proof and crowded court calendars will undoubtedly impede the effective court enforcement of the regulations in Senator Mathias' bill. A more practicable approach would be to incorporate the proposed requirement of a client's signed release into the standards proposed by Senator Ribicoff in S. 1527, and to allow for administrative enforcement of the measure. In this way, the ultimate sanction of revocation of the agent's license and intermediate penalties or fines could be imposed, thereby providing a more efficient and prob-

[78] S. 1387, 92d Cong., 1st Sess. (1971).
[79] H.R. 6478, 92d Cong., 1st Sess. (1971).
[80] S. 1387, 92d Cong., 1st Sess. § 2(e) (1971).

ably more effective manner of enforcement. Under such a procedure, both the time-consuming requirement of awaiting judicial adjudication of the dispute and delayed consumer relief are avoided.

Notwithstanding the apparent incompetence and bad faith demonstrated by members of the tax preparation industry, an important practical consideration must be kept in mind by those who pass legislation or promulgate regulations to curb the aforementioned abuses. Use of taxpayer information to sell insurance or loans or similar programs has provided the industry with an added source of revenue. Although actual data is not available, it seems reasonable to assume that this added revenue has accounted in large measure for the industry's ability to keep the cost of tax preparation services relatively low. This low cost enables low-income individuals, unsophisticated in even the simplest tax matters, to afford assistance in the preparation of their returns. What is suggested, then, is not that the industry's deceptions or poor quality be overlooked; rather, it is hoped that the needed legislation and regulations will correct those failures without being overly oppressive, so that costs can remain sufficiently low to appeal to lower-income taxpayers. For this reason, it is submitted that the industry should be required to employ competent personnel with some sophistication in tax matters, but not necessarily high-priced accountants or attorneys; and that tax service agencies should be required to obtain their clients' permission before disseminating confidential information, but not be precluded absolutely from engaging in such a practice.*

CONCLUSION

The questionable competence of tax preparers and industry solicitation practices suggest a need to protect taxpayers who enlist the services of tax preparation firms. Because of the severe penalties imposed for the filing of faulty returns, these taxpayers need protection from incompetent advice and service, and misleading advertising prac-

* On December 10, 1971, Congress enacted the Revenue Act of 1971, Pub. L. No. 92-178, 85 Stat. 529. Section 316 of the Act adds § 7216 to the Internal Revenue Code of 1954. Section 7216 provides, in relevant part:

(a) GENERAL RULE.—Any person who is engaged in the business of preparing, or providing services in connection with the preparation of, returns of the tax imposed by chapter 1, or declarations or amended declarations of estimated tax under section 6015, or any person who for compensation prepares any such return or declaration for any other person, and who—

(1) discloses any information furnished to him for, or in connection with, the preparation of any such return or declaration, or

(2) uses any such information for any purpose other than to prepare, or assist in preparing, any such return or declaration, shall be guilty of a misdemeanor, and, upon conviction thereof, shall be fined not more than $1,000, or imprisoned not more than 1 year, or both, together with the costs of prosecution.

It is submitted that the consent procedure provided for in S. 1387, the Mathias bill, is a more practicable approach. Under S. 1387 the preparer would not be deprived of the added sources of revenue described in the text, provided that he makes full disclosure to clients of the uses to which he will put the confidential information and obtains their "valid consent." See subsection (1) of the Mathias bill in the text at note 80 supra.

tices. Recourse to the courts is available; however, for taxpayers whose income and tax liability is minimal, the adjudicatory cure is worse than the disease. In addition, effective remedial action by the FTC seems doubtful in light of that agency's budgetary and procedural restrictions. Thus effective regulation of the tax preparation industry seems to be a necessity. However, in promulgating such regulations, Congress and the administrative agencies should take care not to place standards so high that the cost of industry compliance would place preparation fees beyond the pocketbook of the average taxpayer. To this end, Senator Ribicoff's proposed legislation, S. 1527, suggests a basic framework within which effective controls may be structured. A federal licensing system, accompanied by standards designed to safeguard the rights of clients, offers a viable alternative to existing practices in the industry.

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