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Federal Income Tax Returns-The Tension Between Government Access and Confidentiality

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FEDERAL INCOME TAX RETURNS—THE TENSION BETWEEN GOVERNMENT ACCESS AND CONFIDENTIALITY

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INTRODUCTION

From 1920 until 1976, the United States government treated individual income tax information as a general government asset.[1] During that period, the Internal Revenue Service (Service) regularly disseminated tax information which could be identified with a particular taxpayer to government officials; frequently, these officials were able to obtain the information without revealing their reasons for requesting it.[2] By the early 1970's, federal agencies requested millions of tax returns each year.[3]

Congress, as part of the Tax Reform Act of 1976, substantially revised the provisions of the Internal Revenue Code concerning tax return confidentiality. The Tax Reform Act of 1976 rejected the concept that tax information is a general government asset. Section 6103 of the Code, which sets forth the general rules governing the disclosure of tax information, was amended to provide that tax return information "shall be confidential" and no one with access to it shall disclose it "except as authorized" by the Code.[4] This fundamental change resulted in part from

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When this Article was written, the authors were members of the Federal Legislation Committee of the Association of the Bar of the City of New York. As committee members, the authors prepared a study which was printed in the May-June 1979 issue of *The Record* of that Association. This Article is an expanded version of that study. The views expressed in this Article are those of the authors, and not those of the Federal Legislation Committee. The authors wish to acknowledge the assistance of Charlynn Goins and Halsey B. Collins, members of the committee, and the committee itself for its opinions and criticism. We especially wish to thank Steven B. Rosenfeld, the committee chairman, for his help in the preparation of the original committee report.

[1] *See generally* REPORT ON ADMINISTRATIVE PROCEDURES OF THE INTERNAL REVENUE SERVICE TO THE JUDICIAL CONFERENCE OF THE UNITED STATES, S. DOC. NO. 94-266, 94th Cong., 2d Sess. 832 (1975) [hereinafter cited as ADMINISTRATIVE REPORT].

[2] *Id.* at 845-46.

[3] *Id.* at 855.

[4] I.R.C. § 6103(a). Section 6103, entitled "Confidentiality and disclosure of returns and return information," provides in pertinent part:

> (a) General rule—
>
> Returns and return information shall be confidential, and except as authorized by this title—
>
> (1) no officer or employee of the United States,
>
> (2) no officer or employee of any State or of any local child support enforcement agency who has or had access to returns or return information under this section, and

Watergate-related events in the 1970's where evidence was uncovered that President Nixon may have had income tax audits and investigations initiated and conducted in a discriminatory manner for purposes unrelated to the collection of taxes.[5] The net effect of the amendments was to limit access by the President, Congress, White House employees, federal agencies, and others to tax information.

This Article analyzes the policy considerations underlying the 1976 amendments to the Internal Revenue Code (Code) that provide generally for confidentiality of information filed with the Service by and about individual taxpayers. We focus on the most important provisions of those amendments which deal with tax information that can be identified with a particular taxpayer, regardless of whether the information is filed directly by that taxpayer.[6]

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(3) no other person (or officer or employee thereof) who has or had access to returns or return information under subsection (e)(1)(D)(iii) or subsection (n),

shall disclose any returns or return information obtained by him in any manner in connection with his service as such an officer or an employee or otherwise or under the provisions of this section. For purposes of this subsection, the term "officer or employee" includes a former officer or employee.

[5] For example, during the hearings before the House Judiciary Committee on the impeachment of President Nixon, it was revealed that the former President had requested and attempted to obtain confidential information contained in income tax returns from the Internal Revenue Service allegedly for political and other purposes not authorized by law. President Nixon had also endeavored to cause income tax audits and investigations to be initiated and conducted in a discriminatory manner. *Statement of Information: Hearings Pursuant to H.R. 803 Before the House Comm. on the Judiciary, Book VIII,* Internal Revenue Service, 93d Cong., 2d Sess. 368 (1974); (transcript of conversation among H.R. Haldeman, John Dean and President Nixon, Mar. 13, 1973); HOUSE COMM. ON THE JUDICIARY, IMPEACHMENT OF RICHARD M. NIXON, PRESIDENT OF THE UNITED STATES, H.R. REP. NO. 1305, 93d Cong., 2d Sess. 3, 141-45 (1974). *See generally* ADMINISTRATIVE REPORT, *supra* note 1, at 830-31. This appears to have been one of the prime reasons which motivated Congress in the Tax Reform Act of 1976 to revise the provisions of the Code concerning tax return confidentiality. *See* S. REP. NO. 938 (PART I), 94th Cong., 2d Sess. 317, *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3746.

[6] This Article considers only tax return information relating to individuals and does not deal with access to such information as it relates to businesses, estates and other entities. Nor does it discuss access by all persons or entities which arguably have some need for tax information. In particular, this Article does not discuss the provisions of the Internal Revenue Code concerning access by (1) the taxpayer or other private persons with a material interest in a taxpayer's return, such as a co-signatory of a joint return (I.R.C. § 6103(e)); (2) the Renegotiation Board (I.R.C. § 6103(i)(5)); (3) the Comptroller General (I.R.C. § 6103(i)(6)); (4) the Social Security Administration and Railroad Retirement Board (I.R.C. § 6103(*l*)(1)); (5) the Department of Labor and Pension Benefit Guaranty Corporation (I.R.C. § 6103(1)(2)); (6) the Department of Treasury for purposes of resolving personnel matters (I.R.C. § 6103(1)(4)); (7) the Department of Healtb, Education and Welfare (I.R.C. § 6103(1)(5)); or (8) federal, state and local child support agencies (I.R.C. § 6103(1)(6)).

I

THE CONFIDENTIALITY OF INDIVIDUAL TAX RETURNS

A. *The Need for Confidentiality*

An individual's federal income tax return contains many intimate details about his personal and financial life. Besides the nature and source of income, the return reveals an individual's assets and liabilities, the identity of business associates, dependents and charities, marital status, alimony payments, political contributions, medical and dental expenses, casualty losses and union membership.

The taxpayer has a legitimate interest in maintaining the confidentiality of such matters.[7] When, however, the government attempts to determine whether the taxpayer has paid the appropriate amount of tax, that expectation of confidentiality must give way. Thus, in civil or criminal investigations of tax-related matters, no policy reason justifies depriving the government of tax information. Problems arise, however, when disclosure is sought for non-tax purposes, for example, by the Department of Justice for investigation of non-tax crimes. When non-tax issues are involved, there are conflicting policy considerations.

In favor of privacy is the personal nature of the return information. The only reason the Service requests such data is to make sure people pay what they ought to. It may be argued, therefore, that no use unrelated to tax collection should be sanctioned.

The individual's interest in privacy is reinforced by the nature of our tax collection system. Returns are not submitted voluntarily to the Service; rather, they are filed under the threat of substantial criminal and civil penalties.[8] If given a choice, most individu-

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[7] The public policy against disclosure of income tax returns has been expressed by one federal court as follows:

> The protection of the data contained in Federal tax returns is an essential part of our scheme of taxation. Individuals and corporations have the right to expect that information contained in tax returns will not be made available by the government to the public. The policy of confidentiality for income tax data encourages the full disclosure of income by taxpayers in that the individual or corporate taxpayer is assured that his neighbor or competitor will not be apprised of the intimate details of his financial life.

Association of Am. Railroads v. United States, 371 F. Supp. 114, 116 (D.D.C. 1974).

[8] *See* I.R.C. §§ 6651-56 (consequences of failure to file); 7201-15 (criminal sanctions concerning obligation to file return and to pay taxes). For example, § 7203 of the Code

als would almost certainly prefer that the information contained in their tax returns not be made available to the public or to government agencies for non-tax purposes.[9] Indeed, most Americans are probably unaware of the availability of tax returns to various persons and governmental entities.[10] This nation's self-assessment tax collection system may work, moreover, only because taxpayers assume that the information they provide is used for computation of taxes, not for other purposes.[11] There is a substantial risk that collections would be adversely affected if taxpayers believed there was widespread improper use of tax information.

Disclosure of tax information may also implicate constitutional concerns. In 1976, the Supreme Court held in *Garner v. United States*,[12] a non-tax criminal prosecution, that an individual has a fifth amendment right to refuse to supply information on a tax return. Once information is disclosed, however, he can not subsequently claim it is privileged.[13] In short, while a taxpayer is not a "volunteer" when he files information[14] and thus is entitled

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which proscribes, *inter alia*, the willful failure to file a return, states:

> Any person required under this title to pay any estimated tax or tax, or required by this title or by regulations made under authority thereof to make a return (other than a return required under authority of section 6015), keep any records, or supply any information, who willfully fails to pay such estimated tax or tax, make such return, keep such records, or supply such information, at the time or times required by law or regulations, shall, in addition to other penalties provided by law, be guilty of a misdemeanor and, upon conviction thereof, shall be fined not more than $10,000, or imprisoned not more than 1 year, or both, together with the costs of prosecution.

In the event an individual fails to make a return, the Service has the right to complete the return administratively, "from [its] own knowledge and from such information as [it] can obtain through testimony or otherwise." I.R.C. § 6020(b)(1). *See also* I.R.C. § 7602 (right to examine books and witnesses for purpose of making return where none has been made).

[9] A recent public opinion poll conducted by Louis Harris & Associates, Inc. stated that 38% of those polled believed that the service asks for too much personal information. Thirty-seven percent of those sampled felt that the service should do more to maintain the confidentiality of personal information. LOUIS HARRIS & ASSOCIATES, INC. AND A. WESTIN, THE DIMENSIONS OF PRIVACY 26, 30 (1979).

[10] ADMINISTRATIVE REPORT, *supra* note 1, at 829, 832.

[11] Our country's self-assessment system of taxation is virtually unique. Widespread use of information a taxpayer provides to the Internal Revenue Service, for purposes unrelated to tax administration, may diminish the taxpayer's willingness to cooperate with the Service by voluntarily filing an accurate tax return. *See* THE PRIVACY PROTECTION STUDY COMMISSION, PERSONAL PRIVACY IN AN INFORMATION SOCIETY 540 (July 1977) [hereinafter cited as COMMISSION REPORT]. In United States v. Bisceglia, 420 U.S. 141, 145 (1975), the Supreme Court stated, "basically the Government depends upon the good faith and integrity of each potential taxpayer to disclose honestly all information relevant to tax liability."

[12] 424 U.S. 648 (1976).

[13] *Id.* at 653-55. *See also* United States v. Kordel, 397 U.S. 1, 7-10 (1970).

[14] *See* 424 U.S. at 652.

to some protection, he must claim that protection at the time of filing.[15] The Court further held that an individual cannot be convicted for failing to file a return if he files one in which he validly asserts his fifth amendment rights.[16]

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[15] The Supreme Court had previously held in United States v. Sullivan, 274 U.S. 259, 263 (1927), that a taxpayer could not refuse to file a return on the basis of his fifth amendment privilege. In that case, Justice Holmes, writing for the Court, indicated in dictum that the privilege could be claimed against specific disclosures required by the return:

> It would be an extreme if not an extravagant application of the Fifth Amendment to say that it authorized a man to refuse to state the amount of his income because it had been made in crime. But if the defendant desired to test that or any other point he should have tested it in the return so that it could be passed upon.

Id. at 263-64.

[16] 424 U.S. at 662-63. Under certain limited circumstances one may refuse to file completely. *See, e.g.*, Mackey v. United States, 401 U.S. 667 (1971); Marchetti v. United States, 390 U.S. 39 (1968); Grosso v. United States, 390 U.S. 62 (1968) (prosecutions for failure to file returns required of gamblers in connection with federal occupational and excise taxes on gambling). As the Supreme Court noted in *Garner*, prior decisions had

> found that any disclosures made in connection with the payment of those taxes tended to incriminate because of the pervasive criminal regulation of gambling activities. *Marchetti, supra,* at 48-49; *Grosso, supra,* at 66-67. Since submitting a claim of privilege in lieu of the returns also would incriminate, the Court held that the privilege could be exercised by simply failing to file.

424 U.S. at 658.

Prior to the enactment of the Privacy Act of 1974, there was no statutory requirement that taxpayers be notified that the Service could disclose tax information to other agencies. Under the Privacy Act, the Service is required to disclose the following information in soliciting the filing of individual income tax returns:

> (A) the authority (whether granted by statute, or by executive order of the President) which authorizes the solicitation of the information and whether disclosure of such information is mandatory or voluntary;
>
> (B) the principal purpose or purposes for which the information is intended to be used;
>
> (C) the routine uses which may be made of the information, as [such uses are] published [in the Federal Register at least annually in a notice of the existence and character of the Service's system of records which includes the categories of user of the records and the purpose of each use]; and
>
> (D) the effects on [the taxpayer] of not providing all or any part of the requested information. . .

5 U.S.C. § 552a(e)(3)(A) to (D) (1976). The "Privacy Act Notice" which was included in the information booklet accompanying the 1978 Federal Income Tax Form 1040 stated:

> The Privacy Act of 1974 says that each Federal agency that asks you for information must tell you:
>
> a. Its legal right to ask for the information and whether the law says you must give it.
>
> b. What major purposes the agency has in asking for it, and how it will be used.
>
> c. What could happen if the agency does not receive it.
>
> For the Internal Revenue Service, the law covers:
>
> • Tax returns and any papers filed with them.
>
> • Any questions we need to ask you so we can—

The fifth amendment protection, however, does not extend to the masses of information provided to the Service by persons and entities other than the taxpayer, such as banks, credit card agencies, and informers. As a general rule, the taxpayer may not claim fifth amendment protection for records that are not in his possession.[17]

All these considerations militate in favor of granting some protection to taxpayers against disclosure of tax information for non-tax purposes. On the other hand, many government agencies—federal, state and local—make legitimate non-tax use

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> Complete, correct or process your return.
> Figure your tax.
> Collect tax, interest, or penalties.
>
> Our legal right to ask for information is Internal Revenue Code sections 6001 and 6011 and their regulations. They say that you must file a return or statement with us for any tax you are liable for. Code section 6109 and its regulations say that you must show your social security number on what you file. This is so we know who you are, and can process your return and papers.
>
> You must fill in all parts of the tax form that apply to you. But you do not have to check the boxes for the Presidential Election Campaign Fund.
>
> We ask for tax return information to carry out the Internal Revenue laws of the United States. We need it to figure and collect the right amount of tax.
>
> We may give the information to the Department of Justice and to other Federal agencies, as provided by law. We may also give it to States, the District of Columbia, and U.S. commonwealths or possessions to carry out their tax laws. And we may give it to foreign governments because of tax treaties they have with the U.S.
>
> If a return is not filed, or if we don't receive the information we ask for, the law provides that a penalty may be charged. And we may have to disallow the exemptions, exclusions, credits, deductions, or adjustments shown on the tax return. This could make the tax higher or delay any refund. Interest may also be charged.
>
> Please keep this notice with your records. It may help you if we ask you for other information.
>
> If you have questions about the rules for filing and giving information, please call or visit any Internal Revenue Service office.
>
> This is the only notice we must give you to explain the Privacy Act. However, we may give you other notices if we have to examine your return or collect any tax, interest, or penalties.

Although this notice responds, in part, to the issues raised in *Garner*, it fails to inform the taxpayer that he must claim his right to fifth amendment protection at the time of filing. We would also suggest that notice should be provided in "plain English" on the income tax form itself.

[17] The elements of possession are complex. *Compare* Couch v. United States, 409 U.S. 322, 336 (1973) (Court refused to permit taxpayer to use fifth amendment to shield papers he had turned over to his accountant) *and* Fisher v. United States, 425 U.S. 391, 414 (1976) (Court held that accountant's work papers which taxpayer had delivered to his attorney were not protected) *with* United States v. Guterma, 272 F.2d 344, 346 (2d Cir. 1959) (taxpayer records stored in safe on premises of corporation headed by taxpayer held within ambit of fifth amendment protection).

of federal tax information. The Department of Justice regularly employs tax return information in the investigation and development of criminal cases involving both revenue and non-revenue offenses; state and local governments use federal tax information to administer and enforce their own tax laws; congressional committees use tax information in connection with the drafting of tax and other legislation; and various statistical gathering agencies, including the Bureau of the Census, use tax return information in conducting demographic, economic and agricultural statistics programs.[18] No doubt our nation is well served by the detection and prosecution of crimes, by statistical studies based on accurate data, and other similar uses of tax information.

In recent years, however, Congress and the public have become increasingly aware that tax returns and tax return information have been used for purposes neither authorized nor intended by Congress.[19] Much attention has been focused on the use of tax information for non-tax purposes and the proper limits on that use. Such concerns have arisen periodically during the development of the United States tax system.

B. *Historical Background*

Congress first provided for an income tax in 1861.[20] Soon thereafter a public debate developed over whether tax returns should be open to public inspection; in 1864, Congress enacted legislation providing for disclosure.[21] Apparently Congress believed that opening tax returns to public inspection would promote the detection of fraudulent returns.[22] In 1870, however, Congress explicitly prohibited publication of tax returns,[23] and abolished the tax itself as of 1872.[24]

In 1894, Congress reenacted the income tax.[25] The new law provided anti-disclosure provisions and also established penalties for unauthorized disclosures.[26] The Act was declared unconstitutional in 1895.[27]

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[18] *See generally* ADMINISTRATIVE REPORT, *supra* note 1, at 875-1002.

[19] *See* notes 4-5 and accompanying text *supra*.

[20] Act of Aug. 5, 1861, ch. 45, § 8, 12 Stat. 292 (repealed 1872).

[21] Act of June 30, 1864, ch. 173, § 19, 13 Stat. 218, 228 (repealed 1870).

[22] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 836.

[23] Act of July 14, 1870, ch. 255, § 11, 16 Stat. 256, 259.

[24] *Id.* § 6. *See* ADMINISTRATIVE REPORT, *supra* note 1, at 838.

[25] Act of Aug. 15, 1894, ch. 349, § 27, 28 Stat. 509.

[26] *Id. See* ADMINISTRATIVE REPORT, *supra* note 1, at 839.

[27] Pollock v. Farmers Loan & Trust Co., 157 U.S. 429, 583, 586 (1895). This case was in effect overruled in 1913 by the sixteenth amendment to the United States Constitution

The income tax was reinstated by Congress in 1913,[28] along with a provision that tax returns constituted public records. Returns would be open to inspection only upon the order of the President or pursuant to rules and regulations prescribed by the Sectretary of the Treasury and approved by the President.[29] These provisions established the basic pattern which governed tax return disclosure until 1976.

Initially, only corporate income tax returns were available for government inspection. It was not until 1920 that individual income tax returns became available.[30] From then until the early 1970's, governmental entities increasingly used individual tax return data pursuant to regulations issued by the Treasury Department or by order of the President.[31]

At first, tax return data were available only to Treasury Department employees. Within a short time, state tax officials, the Department of Commerce, various Senate committees, United States Attorneys, the White House, and others were granted access.[32] Access was so easy that certain government agencies did not have to specify the name of the taxpayer or the reasons for the inspection.[33]

By the early 1970's, federal agencies were requesting millions of tax returns each year. During the first half of 1974, over 20 million tax returns were provided to the Department of Commerce and others pursuant to blanket regulations.[34] Over 15,000 additional returns were provided to the Department of Justice and United States Attorneys for investigative purposes alone.[35]

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which provides that "[t]he Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration." U.S. CONST. amend. XVI.

[28] Tariff Act of 1913, Pub. L. No. 16, § 2, 38 Stat. 114.

[29] *Id.* § 2(G)(d).

[30] ADMINISTRATIVE REPORT, *supra* note 1, at 845. At that time, the Service promulgated regulations providing for certain limited usage of individual tax return data by government entities. *Id. See* T.D. 2961, 2 C.B. 250 (1920).

[31] ADMINISTRATIVE REPORT, *supra* note 1, at 845.

[32] *Id.* at 845-46.

[33] Access to tax information was often granted pursuant to "blanket regulations." ADMINISTRATIVE REPORT, *supra* note 1, at 845-46.

[34] *Id.* at 855. The vast majority of these returns were requested by the Department of Commerce solely for census compilation. *Id.*

[35] *Id.*; Treas. Reg. § 301.6103(a)-1(g) to (h) (1967).

1. *The Privacy Act of 1974*

Congress, by enacting the Privacy Act of 1974,[36] prohibited the federal government from disclosing information without the consent of the individual to whom the record pertained,[37] unless the intended disclosure was covered by one of the Act's exceptions or exemptions.[38] The Act's stated purpose was to protect individual privacy by restricting disclosure of records maintained in federal agency "information systems."[39]

While tax returns appear to be covered by the Privacy Act, the Act's broad exceptions negate any practical effect.[40] Under the Act, a government agency is permitted to obtain individual information for "routine use" (*i.e.*, a use compatible with the purpose for which it was collected),[41] for "investigative purposes" (*i.e.*, a non-compatible use), or for other authorized law enforcement activities.[42] A congressional committee can obtain tax information for any purpose related to matters within its jurisdiction.[43]

At the time the Privacy Act was enacted, Congress recognized that tax returns required special rules governing disclosure. It therefore created the Privacy Protection Study Commission (Privacy Commission)[44] and authorized it to report to the Congress

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[36] Pub. L. No. 93-579, 88 Stat. 1896 (codified at 5 U.S.C. § 552a (1976)).

[37] 5 U.S.C. § 552a(b) (1976).

[38] *Id.* For a general discussion of the conflicting objectives of the Freedom of Information Act, 5 U.S.C. § 552 (1976 & Supp. I 1977), and the Privacy Act, see Karmel & Benedict, *Business Confidentiality Under Attack—Freedom of Information and Privacy,* 1 CORP. L. REV. 72 (1978). Although the Freedom of Information Act has resulted in the publication of taxpayer information not previously available, the Act does not apply to matters that are specifically exempted from disclosure by other federal statutes. 5 U.S.C. § 552(b)(3) (1976). Therefore, the Act does not require the disclosure of "tax returns" and "return information" which may not lawfully be disclosed under § 6103 of the Code. *See* Black, *The Freedom of Information Act and the Internal Revenue Service,* NEW YORK UNIVERSITY, THIRTY-THIRD INSTITUTE ON FEDERAL TAXATION 683; Rosenbloom, *More IRS Information May Become Public Due to Amended Freedom of Information Act,* 45 J. TAX. 258 (1976).

[39] Pub. L. No. 93-579, § 2(b), 88 Stat. 1896.

[40] *See* PRIVACY PROTECTION STUDY COMMISSION, FEDERAL TAX RETURN CONFIDENTIALITY 15 (June 1976) [hereinafter cited as INTERIM REPORT].

[41] 5 U.S.C. § 552a(b)(3) (1976); *see id.* § 552a(a)(7).

[42] *Id.* § 552a(b)(7). The exception specifically pertains to federal, state, and local law enforcement agencies. *Id.*

[43] *Id.* § 552a(b)(9). In addition, the Privacy Act's exceptions permit the disclosure of confidential information concerning an individual—without the knowledge and consent of the individual—to the Bureau of the Census for activities related to census and surveys (*id.* § 552a(b)(4)), and to recipients who have provided assurances that the information will be used solely for statistical research (*id.* § 552a(b)(5)).

[44] Privacy Act of 1974, Pub. L. No. 93-579, § 5(a), 88 Stat. 1896.

and the President on a number of issues, including "whether the Internal Revenue Service should be prohibited from transferring individually identifiable data to other [federal] agencies and to agencies of State governments."[45]

Congress and the Privacy Commission conducted numerous hearings concerning the proper non-tax use of tax return information.[46] In June 1976, the Privacy Commission issued an interim report, in which it recommended more stringent restrictions than those provided by the Privacy Act of 1974[47] or the Internal Revenue Code.[48] Congress, in enacting the Tax Reform Act of 1976, adopted many of the Commission's recommendations, including the fundamental concept that tax returns should be regarded as confidential.[49]

In July 1977, the Privacy Commission issued its final report,[50] which, while endorsing most of Congress' actions, also recommended several additional changes. Since then, an unsuccessful attempt was made to amend the Code to adopt those changes.[51] Further attempts are expected.[52]

2. *The Tax Reform Act of 1976*

The basic premise of the provisions of the Tax Reform Act of 1976 is that there shall be no disclosure of tax returns and return information[53] for uses other than tax administration unless Con-

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[45] *Id.* § 5(c)(2)(B)(ii).

[46] *See, e.g., Hearings Before the Privacy Protection Study Commission* (Mar. 11 & 12, 1976) [hereinafter cited as *Hearings*].

[47] 5 U.S.C. § 552a (1976 & Supp. I 1977).

[48] *See generally* INTERIM REPORT, *supra* note 40.

[49] *See* Tax Reform Act of 1976, Pub. L. No. 94-455, § 1202, 90 Stat. 1520 (codified in scattered sections of 26 U.S.C.).

[50] COMMISSION REPORT, *supra* note 11.

[51] H.R. 8287, introduced by Congressmen Koch and Goldwater on July 13, 1977, incorporated each of the Privacy Commission's revisions. At the expiration of the 95th Congress last November, the bill was still pending before the House Committee on Ways and Means.

[52] Congressman Goldwater has introduced an identical bill, H.R. 354, in the 96th Congress. That bill is currently pending before the House Committee on Ways and Means.

[53] The terms "tax returns" and "return information" have specific limited meanings under the Code. A "return" is defined to mean any tax return, claim for refund, amendment, supporting schedule or attachment filed on behalf of or in respect to any person. I.R.C. § 6103(b)(1). "Return information" includes, among many other things, the taxpayer's identity; the nature, source or amount of income, payments, receipts, deductions, net worth, tax liability, deficiencies, etc.; data received or prepared by the IRS regarding a return; information regarding actual or possible investigations; and any background documents. I.R.C. § 6103(b)(2). Significantly, the term "return information" only includes

gress has enacted specific statutory provisions authorizing such disclosures.[54] The Tax Reform Act also amended section 7213 of the Code to provide stricter penalties for unauthorized disclosure of tax information.[55] Moreover, the Act authorizes a private right of action for taxpayers allegedly damaged as a result of unlawful disclosures.[56]

Section 6103 of the Code, which took effect on January 1, 1977, authorizes the following persons to receive tax information in which an individual's identity is revealed: persons designated by the taxpayer;[57] state tax officials;[58] persons having a material interest (*e.g.*, the taxpayer, a spouse, partners, certain shareholders);[59] congressional committees;[60] the President;[61] White House personnel and the heads of federal agencies in connection with "tax checks";[62] the Treasury Department and the Department of Justice in civil and criminal cases;[63] federal agencies in non-criminal tax cases;[64] and the General Accounting Office.[65] In addition, various other federal agencies, such as the Bureau of the Census, can obtain tax return information for statistical use.[66]

In the remainder of this Article, we shall analyze some of the more important provisions of the Tax reform Act and determine, in each case, whether the government's arguments for access out-

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data in a form which can be associated with, or otherwise identify, a particular taxpayer. *Id.* In this Article, the terms are generally used interchangeably.

For a further discussion of these terms as well as an additional analysis of the Act's provisions, *see* Corey, *Confidentiality of Tax Returns*, in NEW YORK UNIVERSITY, THIRTY-SIXTH INSTITUTE ON FEDERAL TAXATION 1265, 1269-72 (1978).

[54] I.R.C. § 6103(a). In this respect, Congress reversed its long-standing presumption that tax returns were public records which could be made available upon order of the President or pursuant to rules and regulations promulgated by the Treasury Department. *See* text accompanying notes 20-29 *supra*.

[55] *See* notes 261-66 and accompanying text *infra*.

[56] I.R.C. § 7217. *See* notes 269-72 and accompanying text *infra*.

[57] I.R.C. § 6103(c).

[58] I.R.C. § 6103(d).

[59] I.R.C. § 6103(e). While the taxpayer is given unrestricted access to his own returns, his access to information filed about him by others is conditioned on the determination by the Secretary of the Treasury that access would not impair tax administration. Chamberlain v. Kurtz, [1979] STAND. FED. TAX REP. (CCH) (79-1 U.S. Tax Cas.) ¶ 9211 (5th Cir. 1979).

[60] I.R.C. § 6103(f).

[61] I.R.C. § 6103(g)(1).

[62] I.R.C. § 6103(g)(2).

[63] I.R.C. § 6103(h).

[64] I.R.C. § 6103(i).

[65] I.R.C. § 6103(i)(6).

[66] I.R.C. §§ 6103 (j) and (k).

weigh the individual's interest in confidentiality. It is the premise of this Article that tax information should be given only to those persons who have shown a legitimate need and only after adequate safeguards have been established to preserve privacy.

II

INVESTIGATIONS INTO VIOLATIONS OF THE TAX LAWS

An individual is required to file a tax return so that the tax collecting agency may determine whether he is paying the correct tax. Therefore, the Code permits those employees of the Department of Treasury who are charged with making such determinations to have access to tax return information.[67] When tax information is sought for tax-related purposes by other government agencies, such as the Department of Justice for investigation of tax evasion, it is arguable that access should be just as easy. Congress, however, was troubled by this proposition.[68]

The Code provides that tax returns and return information submitted by a taxpayer who is under investigation shall be disclosed to officials of the Department of Justice and the United States Attorneys' offices for use in any civil or criminal (including federal grand jury) proceeding,[69] if that taxpayer's tax liability is at issue.[70] A different rule, however, governs disclosure of re-

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[67] I.R.C. § 6103(h)(1). In this respect, the taxpayer may reasonably expect his return to be scruntinized by such individuals.

[68] The Privacy Commission articulated its concern in terms of the Service's ability to threaten serious punishment if the taxpayer refused to disclose information. COMMISSION REPORT, *supra* note 11, at 537. While not articulated, underlying that concern is the constitutional protection against self-incrimination embodied in the fifth amendment.

[69] I.R.C. § 6103(h)(2)(A) permits disclosure if "the taxpayer is or may be a party to such proceeding." While the Tax Reform Act of 1976 provided that only attorneys working for the Department of Justice could have access, § 503 of the Revenue Act of 1978 permits officers and employees, as well as attorneys, to have access. Pub. L. No. 95-600, § 503, 92 Stat. 2763. Nevertheless, the regulations reinforce the statutory emphasis on confidentiality by providing:

> Disclosure of a return or return information to a person other than the taxpayer to whom such return or return information relates or such taxpayer's legal representative to properly accomplish any purpose or activity described in [the statute] should be made . . . only if such purpose or activity cannot otherwise properly be accomplished without making such disclosure.

Treas. Reg. § 301.6103(h)(2)-1(b)(1) (1978).

[70] The Second Circuit has held that this provision includes the case in which an indictment alleges both tax and non-tax offenses. United States v. Mangan, 575 F.2d 32, 40 (2d Cir.), *cert. denied*, 439 U.S. 931 (1978).

turn information submitted by one taxpayer which pertains to another taxpayer.[71] If the taxpayer who provides the information is not under investigation, the Department of Justice may obtain the information only if (1) the treatment of an item reflected on the return is or may be relevant to the "resolution of an issue" pertaining to the liability of the person under investigation,[72] or (2) there is "a transactional relationship"[73] between the third party and the taxpayer under investigation which affects or may affect the resolution of an issue in the proceeding.[74]

Once tax returns or return information are turned over to the Department of Justice for use in a tax-related matter, they may be disclosed in a subsequent tax-related proceeding if (1) the taxpayer is a party,[75] (2) the information "is directly related to the resolution of an issue in the proceeding,"[76] (3) there is a transactional relationship between a party and the one who supplied the information about the party,[77] or (4) federal criminal discovery rules require disclosure.[78] In exercising its discretion under the criminal discovery rules, a court must "give due consideration to congressional policy favoring the confidentiality of returns and return information."[79] Moreover, no disclosure may be made if

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[71] Typical examples of "third-party" information are bank records, the records of a credit card agency, or the statements of an informer.

[72] I.R.C. § 6103(h)(2)(B).

[73] The legislative history of the Tax Reform Act of 1976 provided the following examples of "transactional relationships": returns of Subchapter S corporations, partnerships, estates, and trusts. S. REP. No. 938 (PART 1), 94th Cong., 2d Sess. 325-26 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3754-56. The Senate Report notes an additional example: a corporation's return showing wages paid to a taxpayer when the issue is whether the taxpayer paid over the proper amount of withholding taxes. *Id.*

[74] I.R.C. § 6103(h)(2)(C). The legislative history of the Tax Reform Act of 1976 states:

> [R]estrictions were imposed in certain instances ... with respect to the use of third-party returns where, after comparing the minimal benefits derived from the standpoint of tax administration to the potential abuse of privacy, the committee concluded that the particular disclosure involved [i.e., total unfettered disclosure] was unwarranted.

S. REP. No. 938 (PART I), 94th Cong., 2d Sess. 325 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3754. It should be noted that Department of Treasury officials are not similarly limited by statute to tax uses, although the seeming disparity may be the result of a belief that a bureaucratic morass would result if IRS officials had to apply for tax information each time they desired it.

[75] I.R.C. § 6103(h)(4)(A).

[76] I.R.C. § 6103(h)(4)(B).

[77] I.R.C. § 6103(h)(4)(C).

[78] I.R.C. § 6103(h)(4)(D).

[79] I.R.C. § 6103(h)(4)(D).

the Secretary of the Treasury determines that "disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation."[80]

The statutory scheme also precludes collateral uses of tax information. Prior to the Tax Reform Act, government attorneys routinely used returns and return information to impeach the credibility of witnesses.[81] The Act apparently precludes such use by permitting tax return information of a third party whose own tax liability is not at issue to be used in a court or administrative proceeding only if it "directly" relates to an issue in the proceeding.[82] This prohibition reflects the congressional belief that the privacy of witness-taxpayers is more important than the possibility that a government lawyer may be able to impair a witness' credibility. Prior practice also allowed the government but not the defense access to tax information. Although this problem could have been avoided by granting the defense equal access, that solution would only have exacerbated the privacy problem by increasing not only the number of persons with access, but also the risk of further disclosure.

III

NON-TAX INVESTIGATIONS

A. *The Department of Justice and U.S. Attorneys' Offices*

Although taxpayers may have a reasonable expectation that their returns will not be used for non-tax investigations, tax return information plays a prominent role in the discovery and prosecution of violations of federal law. Harold Tyler, then Deputy Attorney General, has stated that tax returns are extraordinarily helpful in getting to the facts in so many contexts."[83] The legislative history of the Tax Reform Act of 1976 notes the following contexts: counterfeiting, forgery, loan sharking, mail fraud, interstate transportation of stolen property, illegal payments and loans to labor unions and employees, bribery, illegal

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[80] I.R.C. § 6103(h)(4).

[81] *See* S. REP. NO. 938 (PART I), 94th Cong., 2d Sess. 324 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3754.

[82] I.R.C. § 6103(h)(4)(B). *But see* S. REP. NO. 938 (PART I), 94th Cong., 2d Sess. 326 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3755 ("[T]he return of a third-party witness could not be introduced in a tax proceeding for purposes of discrediting that witness *except* on the item and transactional grounds . . .").

[83] *Hearings, supra* note 46, at 75 (testimony of Deputy Attorney General Harold Tyler on behalf of the U.S. Department of Justice).

kickbacks, bank and investment frauds.[84] Tax information has been a major weapon in the prosecution of organized crime.[85]

A simple example demonstrates the potential importance of tax information. In a case involving the alleged receipt of a bribe, the defendant may claim that he was paid the money for services rendered. It would be probative if his tax return showed he did not declare the money as income.[86]

The Department of Justice's regular requests for tax information are well documented. During a three month period shortly before the passage of the Tax Reform Act of 1976, the Service made over 1,000 disclosures of tax return information to the Justice Department and United States Attorneys' offices.[87] In 1975, the Justice Department and U.S. Attorneys' offices requested nearly 26,000 tax returns of over 6,000 persons.[88]

In sum, tax return information appears to play a prominent role in the discovery and prosecution of violations of federal law. This is, and should continue to be, an important consideration in determining right of access.

Although this extensive use of tax return information poses a potential threat to personal privacy, proponents note that there have been few abuses over the years. Judge Tyler testified in 1976 that there was no "hard evidence of any substantial abuses of tax returns by [Department of Justice] lawyers in all the many, many years . . . ."[89] While we agree that the abuses have been few and far between, the Nixon years exposed the great potential for abuse,[90] an abuse not limited to the White House.

The Tax Reform Act of 1976 places significant procedural limitations on the procurement of tax information for non-tax purposes when the information is sought directly from the Service.[91] As a general rule the Act limits access to the prosecution

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[84] S. REP. NO. 938 (PART I), 94th Cong., 2d Sess. 327 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3437, 3756-57.

[85] *Id.*

[86] *Hearings, supra* note 46, at 75, 79 (testimony of Deputy Attorney General Harold Tyler on behalf of the U.S. Department of Justice).

[87] *See* COMMISSION REPORT, *supra* note 11, App. 2, at 57.

[88] *See* S. REP. NO. 938 (PART I), 94th Cong., 2d Sess. 327 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3757.

[89] *Hearings, supra* note 46, at 56-57. Judge Tyler said there was one instance of abuse by a young Assistant U.S. Attorney who was discharged. *Id.* at 57.

[90] *See* note 5 and accompanying text *supra.*

[91] Government prosecutors may still attempt to obtain tax information directly from the taxpayer or from third parties. *See* Maggio v. Hynes, 423 F. Supp. 144 (E.D.N.Y. 1976).

of crimes;[92] civil enforcement authorities such as the Securities and Exchange Commission are denied access.[93] The Act also provides that tax return information in the files of the Service may be obtained only if a federal district court first approves the disclosure.[94] The procedure is *ex parte*,[95] and only the head of the agency may apply for it.[96] A court may grant an order permitting disclosure if (1) there is "*reasonable cause* to believe, based upon information believed to be reliable, that a specific criminal act has been committed,"[97] (2) the information is "probative evidence of a matter in issue related to the commission of such criminal act,"[98] *and* (3) the information cannot be obtained "from any other source, unless . . . the information sought constitutes the most probative evidence of a matter in issue."[99] The Secretary of the Treasury may withhold information if he certifies that "disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation."[100]

No court proceeding, however, is required to obtain information which the Service has received from third parties.[101] The Secretary of the Treasury must disclose such information upon written request from an agency identifying only the name and address of the taxpayer,[102] the taxable period,[103] the agency's

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[92] I.R.C. § 6103(i)(1)(A).

[93] *See* notes 127-31 and accompanying text *infra*.

[94] I.R.C. §6103(i)(1)(A).

[95] *Id.* The *ex parte* procedure has been upheld by the Second Circuit in United States v. Barnes, No. 78-1040, slip op. at 5621-22 (2d Cir. Apr. 23, 1979). The court refused to imply an exclusionary sanction for violations of the Tax Reform Act since "none appears in the Tax Reform Act itself and since civil and criminal penalties have been expressly provided. 26 U.S.C. §§ 7213(a) (criminal penalties), 7217 (civil remedies in favor of taxpayer)."

[96] I.R.C. § 6103(i)(I)(B). In the case of the Justice Department, the Attorney General, Deputy Attorney General or an Assistant Attorney General may authorize an application. *Id.* In United States v. Mangan, 575 F.2d 32, 39 (2d Cir.), *cert. denied*, 99 S. Ct. 320 (1978), the court strictly construed that Act's requirement that the application be made by the designated officials of the Department of Justice. The court reasoned: "When Congress chooses to speak with such specificity, courts must heed its language." *Id.*

[97] I.R.C. § 6103(i)(1)(B)(i) (emphasis added).

[98] I.R.C. § 6103(i)(I)(B)(ii).

[99] I.R.C. § 6103(i)(1)(B)(iii). As a matter of pure logic this cannot mean that the government must first ask the taxpayer for the information. The obvious reason for the *ex parte* procedure is to avoid notice to the taxpayer, which would be defeated by requiring inquiry of the taxpayer before going to court.

[100] I.R.C. § 6103(i)(I).

[101] *See* I.R.C. § 6103(i)(2).

[102] I.R.C. § 6103(i)(2)(A).

[103] I.R.C. § 6103(i)(2)(B).

statutory authority to conduct an investigation or proceeding,[104] and the "specific reason" why disclosure is material.[105] The request need not be limited to prosecution of a federal crime, one of the limitations set forth for obtaining information submitted by the taxpayer.[106] The Secretary of the Treasury may refuse disclosure of third-party information for the same reasons noted above with respect to information submitted by the taxpayer.[107]

Neither the *ex parte* procedure for obtaining information submitted by a taxpayer nor the written request procedure for the third-party information comport with the Privacy Commission's recommendations. The Commission's basic tenet was:

> [A]uthorizing the IRS to disclose individually identifiable tax information to another agency for a purpose unrelated to the administration of a Federal tax law is seldom defensible unless the Congress would be willing in principle to compel individuals to disclose the same information directly to the agency requesting it from the IRS.
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> . . . .
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> [T]he Commission believes that Federal law enforcement officials should not have easier access to information about a taxpayer when it is maintained by the IRS than they would have if the same information were maintained by the taxpayer himself.[108]

The Commission found no principled distinction between third-party information and information obtained from the taxpayer. The Commission recommended that, in all non-tax investigations and proceedings, the taxpayer receive notice of the request for information and that a federal district court approve the disclosure. Approval was to be conditioned upon a showing of "probable cause" to believe a crime had been committed. The requesting agency would also have to show that the information was "probative evidence" that the crime had been committed and that there was no legal impediment preventing the agency from obtaining the information directly from the taxpayer.[109] The

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[104] I.R.C. § 6103(i)(2)(C).

[105] I.R.C. § 6103(i)(2)(D).

[106] *See* I.R.C. § 6103(i)(2).

[107] I.R.C. § 6103(i)(2). *See* note 100 and accompanying text *supra.*

[108] COMMISSION REPORT, *supra* note 11, at 540-41, 553.

[109] *See id.* at 557. H.R. 354, which was introduced in the 96th Congress by Representative Goldwater, would enact a probable cause standard with notice to the taxpayer and provide a right to contest access with respect to both taxpayer and third-party source information. *See* note 44 *supra.*

Commission further proposed that the court's approval should be a final order subject to appellate review.[110]

1. *Probable Cause and Notice*

"Probable cause" is the phrase which is used in the fourth amendment to govern searches and seizures.[111] "Probable cause . . . exists where the facts and circumstances within the affiant's knowledge, and of which he has reasonably trustworthy information, are sufficient unto themselves to warrant a man of reasonable caution to believe that an offense has been or is being committed."[112] As the legislative history of the Tax Reform Act of 1976 makes clear, reasonable cause "is intended to be less strict than the 'probable cause' standard for issuing a search warrant and this requirement is to be construed according to the plain meaning of the words involved."[113] The Privacy Commission construed "reasonable cause" to mean that a judge must find "some basis to believe that a crime has been committed," a requirement which it thought would be easy to satisfy.[114]

In his testimony before the Privacy Commission, Judge Tyler argued that the probable cause standard would preclude the Justice Department from obtaining necessary information, which would seriously hamper its effectiveness. He testified that it is often impossible to determine whether a white collar crime has been committed until the Department makes a careful financial

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[110] INTERIM REPORT, *supra* note 40, at 62.

[111] The fourth amendment provides:

> The right of the people to be secure in their persons, houses, papers, and effects, against unreasonable searches and seizures, shall not be violated, and no Warrants shall issue, but upon probable cause, supported by Oath or affirmation, and particularly describing the place to be searched, and the persons or things to be seized.

U.S. CONST. amend. IV.

[112] Berger v. New York, 388 U.S. 41, 55 (1967).

[113] S. REP. No. 94-938 (PART I), 94th Cong., 2d Sess. 333 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439,3758.

[114] Commission Report, *supra* note 11, at 555. Some courts have used the terms "reasonable cause" and "probable cause" interchangeably. *See, e.g.*, People v. Blackman, 81 Misc. 2d 12, 14, 364 N.Y.S.2d 704, 707. (Queens Co. 1975); People v. Lombardi, 18 A.D.2d 177, 239 N.Y.S.2d 161 (2d Dep't 1963). The U.S. Supreme Court, however, has interpreted "reasonable cause" to impose "a less stringent requirement than that of 'probable cause'." United States v. Ramsey, 431 U.S. 606, 612-13 (1977). *Ramsey* involved an interpretation of 19 U.S.C. § 482, which permits searches of vessels by certain government officials.

analysis, aided by a review of tax return information.[115] As for giving the taxpayer notice, former United States Attorney General Griffin B. Bell testified that notice could provide an opportunity for delay: "[T]he astute tax evader knows, even a year's delay may spell the difference between a successful and a fruitless investigation."[116]

The comments of former Attorney General Bell and Judge Tyler appear valid. The same can be said of the right to appeal the *ex parte* order—if the taxpayer can appeal, he will have an additional tool to use in interfering with investigations of his conduct which may unnecessarily hinder legitimate law enforcement efforts. In addition, if the probable cause standard precludes access, the government may be forced to indict an individual before it has analyzed all available evidence, including exculpatory evidence, or to forego prosecution of crimes, especially business-related crimes.

The Department of Justice's need for tax return information to detect crimes, while compelling, is not necessarily dispositive. In most instances, local police and other law enforcement officials have just as legitimate a need to search premises for evidence of crimes within their jurisdiction as the Department of Justice has to review tax information. Unquestionably, the probable cause standard results in fewer crimes being detected. Yet the probable cause standard has evolved as the proper balance of the individual's right to privacy and society's need to detect crimes.[117] Moreover, although a taxpayer, having submitted a return, cannot invoke the protection of the fifth amendment,[118] the compulsion inherent in the tax reporting system supports some measure of protection.

Assuming federal judges interpret "reasonable cause" to require some evidentiary showing of a possible criminal violation, the Act's *ex parte* procedure appears to adequately protect the tax-

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[115] *Hearings, supra* note 46, at 81. Judge Tyler was then Deputy Attorney General.

[116] *Administrative Summons and Anti-Disclosure Provisions of the Tax Reform Act of 1976: Hearings Before the Subcomm. on Oversight of the House Comm. on Ways and Means*, 95th Cong., 1st Sess. 5 (1977) (statement of Attorney General Griffin B. Bell); *see Hearings, supra* note 46, at 153-56, 161-62 (testimony of Stanley Sporkin on behalf of the SEC).

[117] *See* Frank v. Maryland, 359 U.S. 360, 363 (1959) ("The vivid memory by the newly independent Americans of [Crown] abuses produced the Fourth Amendment as a safeguard against such arbitrary official action by officers of the new Union.").

[118] *See* text accompanying notes 12-16 *supra*.

payer.[119] Given the novelty of the procedure and the substantial arguments against a higher standard of proof or notice to the taxpayer, the procedure should be permitted at least for a limited period of time so that its workings may be analyzed. It will undoubtedly be easier in the coming years to monitor the *ex parte* procedure to determine if it is being abused, than to determine whether federal prosecutors are being unduly hampered by a probable cause standard or by notice to the taxpayer.[120]

2. *Third-Party Source Information*

The Tax Reform Act of 1976 does not require a court order or notice to the taxpayer before the Service may disclose third-party source information.[121] Congress apparently concluded that fifth amendment concerns are implicated only when information is sought directly from the taxpayer.[122] Third-party information includes not only information supplied by informers, but also bank and credit card records about a taxpayer, and returns and other information filed by persons who are connected to a taxpayer (*e.g.*, trustees or executors) or who have engaged in business with a taxpayer (*e.g.*, suppliers or customers).

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[119] In one of the few reported decisions regarding an *ex parte* application, Judge Nickerson of the Eastern District of New York held that before such an order could be granted, the judge must be permitted to review the requested material *in camera*. He found authority for his holding in the legislative history of the Tax Reform Act of 1976. United States v. Praetorius, 451 F. Supp. 371, 373 (E.D.N.Y. 1978), *citing* S. REP. No. 938 (PART I), 94th Cong. 2d Sess. 329 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3758. This ruling, if followed by other courts, is a healthy sign that federal courts will carefully review government applications for *ex parte* orders.

[120] During a debate on these problems, certain members of the Federal Legislation Committee of the Association of the Bar of the City of New York had recommended a two-tier structure. Initially, the government would have to prove probable cause in an *ex parte* proceeding. If the court holds the government has failed to prove probable cause, the government could be given a second chance, with the taxpayer given notice and the right to contest disclosure. At this second proceeding, however, the government would have to show only reasonable cause. Such a two-tier procedure does have the beneficial effect of recognizing the government's legitimate need for information and the serious risk of giving notice to taxpayers, while at the same time increasing the protection available to the taxpayer by initially requiring probable cause.

[121] *See* discussion at note 101 and accompanying text *supra*. Compare I.R.C. § 7609, which requires that the taxpayer be given (1) notice of any summons served by the Service on a "third-party recordkeeper" requiring the production of records relating to the taxpayer and (2) the right to intervene in any proceeding with respect to the enforcement of such summons. *See* United States v. Desert Palace Inc., [1979 Transfer Binder] STAND. FED. TAX. REP. (CCH) ¶ 9292 (D. Nev. Mar. 12, 1979) (gambling casino which extends credit is third-party recordkeeper); United States v. Exxon Co., U.S.A., 450 F. Supp. 472 (D. Md. 1978) (oil company which issues credit cards not third-party recordkeeper).

[122] INTERIM REPORT, *supra* note 40, at 556.

The Privacy Commission argued that third-party information required protection just as much as information filed by the taxpayer because our society is structured to necessitate maintenance of various records.[123] The Privacy Commission reasoned that while it is a necessary evil for the Internal Revenue Service to have easy access to monitor the tax system, it is quite another thing to provide such information to agencies investigating non-tax matters.[124] Court review may be necessary to ensure that a criminal investigation is not based on inaccurate, outdated or false material, and that the information is sought for a proper purpose.

There are at least two countervailing considerations. As previously discussed,[125] a taxpayer enjoys no constitutional protection with respect to information about him in the hands of others. Further, a requirement of court approval of the many requests for third-party information would impose a substantial burden on the court system. While that burden is mitigated by making the procedure nonadversarial—the applicant should in most cases be able to demonstrate its need for and right to the information—the administrative problem is nevertheless a potentially serious one.

On balance, we agree with the Privacy Commission that third-party source information should be subject to the same protection as information submitted by the taxpayer. The risk of abuse is just as great while the concomitant burden on the government of obtaining an *ex parte* order is no greater. As noted above,[126] the *ex parte* procedure provides the taxpayer sufficient protection from abuse while allowing prosecutors to act without undue hindrance. Congress can deal with the potential burden on the federal courts if that risk becomes manifest.

B. *Civil Investigations—The SEC*

Congress has proscribed use of tax returns and return information by federal agencies for civil litigation purposes, except

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[123] *See* COMMISSION REPORT, *supra* note 11, at 556. For example, a taxpayer-citizen must have bank accounts and access to credit.

[124] *See* COMMISSION REPORT, *supra* note 11, at 556-57. It should be noted that none of the witnesses who testified before the Commission appears to have focused on third-party information.

[125] *See* notes 12-17 and accompanying text *supra*.

[126] *See* notes 119-20 and accompanying text *supra*.

where specifically authorized by the Act.[127] The SEC is not among the agencies so authorized.[128]

Arguably, access is not so essential for the SEC or any other federal agency investigating or prosecuting non-tax *civil* cases that it outweighs the taxpayer's privacy interests. Federal agencies such as the SEC possess adequate investigatory powers to obtain tax returns and other information either directly from the taxpayer via the agency's own investigative subpoena powers,[129] or through third-party sources. If there is enough evidence of a violation, the SEC may commence a civil action and request the tax information under the federal discovery rules.[130] Moreover, the Department

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[127] As a general rule, the Tax Reform Act of 1976 permits disclosure of tax returns and return information for non-tax purposes only upon a showing of "reasonable cause to believe ... that a specific *criminal* act has been committed." I.R.C. § 6103(i)(1)(B)(i) (emphasis added). Prior to the Tax Reform Act, tax information was available to the Department of Justice for defending suits seeking money damages for injury or wrongful death, for instituting civil fraud claims against private parties, and for determining the ability of a party to pay a judgment. Other executive departments and establishments of the federal government could obtain tax information in connection with matters officially before them and for evidence in proceedings conducted by or before a federal agency. The legislative history of the Act points out, however, that such uses of tax information in non-tax civil cases "were not warranted in light of the invasions of privacy involved and the fact of the alternative sources of information available." S. REP. NO. 94-938 (PART I), 94th Cong., 2d Sess. 331 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3760.

[128] In addition to permitting access by the Department of Justice for civil proceedings involving tax administration (I.R.C. § 6103(h)(2)), the Code permits the Renegotiation Board to receive and use such information to implement certain provisions of the Renegotiation Act of 1951, and to disclose such information to the Department of Justice if the Board deems legal action appropriate (I.R.C. § 6103(i)(5)); section 6103(l)(1) authorizes the disclosure of returns and return information to the Social Security Administration and the Railroad Retirement Board in connection with the administration of certain statutory provisions under their jurisdiction; and section 6103(l)(2) sanctions disclosure of returns and return information to the Department of Labor and the Pension Benefit Guaranty Corporation in connection with their civil and criminal administration and enforcement of the provisions of Title I and IV of the Employee Retirement Income Security Act of 1974. The Privacy Protection Study Commission and the Department of Health, Education and Welfare also receive returns and return information for civil purposes pursuant to I.R.C. §§ 6103 (1), (3) and (5). *See* Letter from Charles L. Saunders, Jr., Acting Chief Counsel of the Internal Revenue Service, to Harvey Pitt, General Counsel to the SEC (March 21, 1977) (on file at *Cornell Law Review*).

[129] The Securities and Exchange Commission has power under both the Securities Act of 1933 and the Securities Exchange Act of 1934 to conduct investigations into possible violations of the federal securities laws, including subpoenaing witnesses, taking evidence, and requiring the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry. 15 U.S.C. § 77s(b) (1976); 15 U.S.C. §§ 78u(a), (b) (1976). It may also seek enforcement in any U.S. district court of any subpoena duces tecum issued in the course of its investigations. 15 U.S.C. §§ 77v(b), 78u(c) (1976).

[130] Income tax returns do not enjoy an absolute privilege from discovery. St. Regis Paper Co. v. United States, 368 U.S. 208, 218-19 (1961); Premium Serv. Corp. v. Sperry &

of Justice, not the SEC, has ultimate responsibility for prosecuting criminal violations of the securities laws, and it can obtain tax information by following the *ex parte* procedure outlined above.[131]

The SEC appeared at the Privacy Commission hearings and argued for its continued access to tax return information for use in civil non-tax investigations. Stanley Sporkin, Chief of the SEC's Enforcement Division, testified that a denial of access would seriously hamper the effectiveness of SEC investigations of civil securities laws violations. He stated that while the SEC often obtains leads of possible misconduct, it is not always possible to identify a particular violation of the securities laws; only after other evidence is sifted, including tax return information,[132] can the SEC determine whether a violation has occurred.[133] Mr. Sporkin also contended that there had not been one complaint served against the SEC for having improperly used tax return information.[134] It is clear that a certain degree of duplication of investigative effort will be avoided if the SEC is given access to IRS files.

Section 6103 should be further amended to permit access by the SEC to tax returns and return information upon terms similar to those which govern access by the Department of Justice and

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Hutchinson Co., 511 F.2d 225, 229 (9th Cir. 1975). Many courts, however, have recognized a public policy against the unnecessary public disclosure of tax returns. *E.g.*, Premium Serv. Corp. v. Sperry & Hutchinson Co., 511 F.2d at 229; Cooper v. Hallgaren & Co., 34 F.R.D. 482, 483-84 (S.D.N.Y. 1964); Wiesenberger v. W.E. Hutton & Co., 35 F.R.D. 556, 557 (S.D.N.Y. 1964). One of the factors considered by the courts in determining whether to allow discovery of tax returns is whether the information is readily obtainable by other means or from other sources; courts may also permit access where the taxpayer has put the amount of his income in issue. *See, e.g.*, Federal Sav. & Loan Ins. Corp. v. Krueger, 55 F.R.D. 512, 514-15 (N.D. Ill. 1972); Wiesenberger v. W.E. Hutton & Co., 35 F.R.D. at 557-58; Kingsley v. Delaware Lackawanna & Western R. Co., 20 F.R.D. 156, 158 (S.D.N.Y. 1957).

[131] *See* notes 94-100 and accompanying text *supra*. The Tax Reform Act may permit any federal agency to obtain tax return information if it can demonstrate reasonable cause to believe that criminal violations have occurred. The authors are not aware of any attempt by the SEC to make such a showing.

[132] In 1974 the SEC made 15 requests for information about 82 taxpayers and 360 returns; in 1975, it made 12 requests concerning 21 taxpayers and 121 returns. *Hearings, supra* note 46, at 139 (testimony of Stanley Sporkin, Chief, Bureau of Enforcement, SEC). The three-month study conducted by the Privacy Commission in 1976 shows that the SEC obtained 28 disclosures from the Service during that period. COMMISSION REPORT, *supra* note 11, App. 2, at 57.

[133] *Hearings, supra* note 46, at 152-54. For example, in a case where market manipulation was suspected, but not sufficiently proved, tax return information might provide a link by establishing an individual's dealings in the stock in question. Tax return information is also particularly useful in investigating tax shelter schemes.

[134] *Id.* at 150.

U.S. Attorneys' offices in non-tax criminal investigations.[135] This would include a showing that there is reasonable cause to believe that a specific violation within the SEC's jurisdiction has been committed. Access should also be permitted to other federal agencies responsible for enforcing civil laws, provided they can demonstrate to Congress a compelling need for such information. As with Department of Justice investigations, we believe such a procedure provides the proper balance between an investigating agency's legitimate need for information and the taxpayer's right to confidentiality.

IV

ACCESS BY THE PRESIDENT AND WHITE HOUSE PERSONNEL

A. *Tax Checks*

The President and members of the White House staff have frequently used tax returns and return information to conduct "tax checks" on prospective appointees.[136] The information was often obtained without the consent of the individual to whom the information pertained.

Prior to the Tax Reform Act of 1976, the Internal Revenue Code provided that income tax returns "shall be open to inspection only upon order of the President and under rules and regulations prescribed by the Secretary . . . ."[137] The Code did not specifically provide for disclosure to the President. Under this provision, however, Presidents issued rules and regulations providing for presidential and White House access to tax information for the purpose of investigating prospective presidential appointees.[138]

Since 1961, when President Kennedy first wrote to Secretary Dillon stating that he desired a check of tax records to supplement the character investigations of certain prospective presidential appointees,[139] tax checks have frequently been performed at the request of the President[140] or heads of various federal agen-

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[135] *See* I.R.C. § 6103(i)(1)(B)(i)-(iii). *See generally* notes 90-100 and accompanying text *supra*.

[136] ADMINISTRATIVE REPORT, *supra* note 1, at 981.

[137] I.R.C. § 6103(a) (1975).

[138] *See, e.g.*, Executive Order No. 11,805, 39 Fed. Reg. 34,261 (1974).

[139] ADMINISTRATIVE REPORT, *supra* note 1, at 985 n.608.

[140] For example, the White House requested 547 tax checks in 1966. The number of requests increased to 1045 in 1974. *Id.* at 988.

cies.[141] Checks have been made in connection with the appointment of individuals to numerous kinds of jobs, including postmasters, judges, U.S. Attorneys and White House employees.[142] The ostensible purpose of these requests is to avoid the embarrassment of appointing an individual to an important government post who is in, or has been in, serious tax trouble.[143]

A tax check on a potential presidential appointee is initiated by the White House office as part of a "security and conflicts review." During this review, the Federal Bureau of Investigation (FBI) conducts a "full field investigation" which includes checks with various confidential agencies, including the Internal Revenue Service. Therefore, the inquiry to the Service comes from the FBI rather than directly from the White House. The FBI reports the tax check information to the White House Counsel's Office, which transmits a report to the President.[144]

There have been a few demonstrated abuses of tax information in connection with tax checks. The most notable was the Watergate era revelation of evidence that the White House used the tax check procedure to obtain data to use against Daniel Schorr, a CBS newscaster.[145] Such abuses led to the Privacy Commission's recommendation that tax checks be conditioned on the prospective employee's consent.[146]

Congress disagreed. By amending the Code provisions regarding tax return confidentiality in the Tax Reform Act of 1976,

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[141] These include the Department of Justice, the Department of Treasury, the Department of State, the Department of Commerce, and the Department of Agriculture. *See id.* at 988. The Privacy Commission noted in its *Interim Report* that the Department of Justice requested tax information in 835 instances in 1974 in connection with the consideration of judicial nominees. INTERIM REPORT, *supra* note 40, at 50.

[142] *See generally* S. REP. NO. 94-938 (PART I), 94th Cong., 2d Sess. 322 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3752; ADMINISTRATIVE REPORT, *supra* note 1, at 987.

[143] ADMINISTRATIVE REPORT, *supra* note 1, at 990. It has also been suggested that tax information has some relevance to competence or fitness for a public job. *Id.* This does not, however, justify the need for the disclosure of this information without first obtaining the consent of the taxpayer.

[144] S. REP. NO. 94-938 (PART I), 94th Cong., 2d Sess. 322 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3751-52. If the tax check is "negative," the Service informs the requesting party: "Our records show that income tax returns were timely filed for the [three year period]. There is no record of unpaid taxes, liens, criminal tax investigations, or civil penalties for fraud or negligence. This completes our report." ADMINISTRATIVE REPORT, *supra* note 1, at 986. If the tax check is positive, the department requesting the tax check is so advised. *Id. See* text accompanying notes 149-52 *infra.*

[145] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 991.

[146] *See* INTERIM REPORT, *supra* note 40, at 50.

Congress endorsed the prior tax check practice.[147] Thus, section 6103(g)(2) of the Code now authorizes the disclosure to:

> [a] duly authorized representative of the Executive Office of the President or to the head of any Federal agency, upon written request by the President or head of such agency, or to the Federal Bureau of Investigation on behalf of and upon written request by the President or such head, [of] return information with respect to an individual who is designated as being under consideration for appointment to a position in the executive or judicial branch of the Federal Government.

The Code does, however, require that the Service send written notice to the affected taxpayer within three days of the receipt of the request.[148]

The Code also limits the information which the Service may disclose in a tax check. The Service may only state whether the prospective appointee (1) has filed returns for the immediately preceding three years;[149] (2) has failed to pay any tax within ten days after notice and demand or has been assessed any penalty for negligence within the immediately preceding three years;[150] (3) has been or is under investigation for possible criminal offenses under the Internal Revenue laws, and the results of any such investigation;[151] or (4) has been assessed any civil penalty under title 26 for fraud.[152]

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[147] I.R.C. § 6103(g). It may be argued that Congress cannot constitutionally prevent the President from obtaining access to information gathered and maintained by an agency which reports to him. That issue is beyond the parameters of this article, although we note that article II of the Constitution entitles the President to obtain information from government agencies for purposes of executing the laws. The Supreme Court, however, has held that the President's authority is limited to execution of only those laws which have been enacted by Congress. Youngstown Sheet & Tube Co. v. Sawyer, 343 U.S. 579, 587-88 (1952).

[148] I.R.C. § 6103(g)(2).

[149] I.R.C. § 6103(g)(2)(A).

[150] I.R.C. § 6103(g)(2)(B).

[151] I.R.C. § 6103(g)(2)(C).

[152] I.R.C. § 6103(g)(2)(D). The Code further provides that the tax information shall not be disclosed to any employee of the White House or other federal agency who does not earn a certain salary (I.R.C. § 6103(g)(4)); prohibits employees who receive tax information from redisclosing it to other persons without the personal written direction of the President or head of the requesting agency (I.R.C. § 6103(g)(3)); and requires the President and the head of any agency requesting returns to file a quarterly report with the Joint Committee on Taxation setting forth the names and addresses of taxpayers with respect to whom such requests have been made, the tax information involved, and the reasons for each request (I.R.C. § 6103(g)(5)). The Code requires that the reports be maintained for a

We see no legitimate governmental interest which is served by precluding *prior* notice to the prospective appointee that a tax check will be made.[153] If a prospective appointee does not wish to disclose confidential tax information, he should be afforded an opportunity to say so. If the appointing agency then withdraws the person's name from consideration, at least the choice about revealing the information will have been the candidate's. Moreover, the prospective appointee may have no interest in the particular job, and thus have no reason to reveal his tax return information to anyone.

In its present form, the tax check mechanism has the potential for being unfair. When the Service discloses tax information without the individual's knowledge, the individual has no opportunity to rebut adverse information which may be revealed. Further, as in the celebrated Daniel Schorr incident, tax checks permit the White House to use a prospective appointment as a pretense to obtain potentially embarrassing information about political enemies. Although the after-the-fact notification procedure now incorporated into section 6103(g) reduces the potential for such abuses, it does not eliminate them.

There is also a compelling argument to abolish the tax check procedure altogether. The President or agency may obtain information directly from the prospective appointee at little inconvenience. If a person is anxious to obtain an appointment, he should be willing to disclose such information or authorize the Service to release it. Although the Administration would no longer be able to obtain this information without making the taxpayer aware that he is under consideration for an appointment,

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period not exceeding two years, but prohibits disclosure unless the Committee believes that disclosure would be in the "national interest." Reports are not required with respect to requests for tax information pertaining to current employees of the Executive Branch. *Id.*

[153] Our position is consistent with the Privacy Act of 1974, which, as a general rule, prohibits the disclosure of tax information "to any person [without] the prior written consent of, the individual to whom the record pertains ...." 5 U.S.C. § 552a(b) (1976). Although tax checks made for the purpose of avoiding presidential embarrassment are not compatible with the purpose for which the Service originally collected the information, the "routine use" exception (*see* text accompanying notes 40-42 *supra*) had been interpreted by the Office of Management and Budget to justify the release, without the consent of the taxpayer, of tax information for all uses that were properly made of the information *prior* to the enactment of the Privacy Act. Privacy Act Guidelines, 40 Fed. Reg. 28,949, 28,953 (1975). *See generally* ADMINISTRATIVE REPORT, *supra* note 1, at 868.

the need for secrecy has not been convincingly explained. Indeed, even under current procedures, the Service must notify the prospective appointee within three days after the request for the tax check, whether or not the taxpayer is named for the job.[154]

B. *Other Uses*

While the pre-appointment tax check is the primary use made by the White House of tax return information, the Code allows the President to request information for any purpose. Section 6103(g)(1) permits the Service to disclose to the President, or White House employees designated by him, "a return or return information with respect to any taxpayer" named in a request, without any limitation on what may be disclosed or the use to be made of the information. The section requires only that the request be in writing; personally signed by the President; and specify certain information, including the name and address of the taxpayer whose return or return information is to be disclosed, the kind of return or return information which is to be disclosed, the taxable period or periods covered, and the specific reason why the inspection or disclosure is requested.[155] However, the safeguards applicable to tax checks—prohibitions on redisclosure, restrictions on access, and requirements for congressional reports—also apply.[156]

Prior to the Tax Reform Act of 1976, the Code did not specifically provide for presidential access to tax information. Beginning with the Kennedy Administration, however, such access was provided, for reasons other than tax checks on potential appointees, pursuant to various executive orders and under rules and regulations promulgated by the Secretary of the Treasury.[157] The Service disclosed entire tax returns, parts of returns, and analyses

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[154] I.R.C. § 6103(g)(2). It should be noted that the individual may well have notice of his prospective appointment long before this time because the White House typically consults with an individual's colleagues concerning his reputation, competency, and similar matters prior to requesting tax data.

[155] *Id.*

[156] I.R.C.§§ 6103(g)(3), (4) & (5). It should be noted, however, that the provision requiring post-disclosure notification does not apply to presidential requests which are not made in connection with a tax check. *See* I.R.C. § 6103(g)(2).

[157] *See generally* ADMINISTRATIVE REPORT, *supra* note 1, at 968-71.

of return information.[158] At times, data was provided pursuant to oral requests by White House employees, apparently without the knowledge of the President.[159]

The primary justification offered for such presidential access is that the information is necessary for investigations of "impropriety in connection with government activity."[160] The White House, however, does not normally conduct such investigations; they are within the province of the FBI, the Department of Justice and United States Attorneys' offices. As discussed above,[161] the Code requires that in criminal non-tax situations, federal investigators must first obtain a court order to gain access to return information. Presidential access without such a court order directly conflicts with that procedure.

There is also, of course, the Watergate experience to consider. Investigations revealed evidence that various Presidents had misused tax information. For example, President Nixon allegedly requested tax information concerning the Reverend Billy Graham, John Wayne,[162] and Lawrence O'Brien[163] for improper political purposes. The marginal benefit of allowing the President access to tax information for investigations of "impropriety" is outweighed by the risk that such information may be used improperly. There is, moreover, evidence that such investigative use is unnecessary. Former IRS Commissioner Alexander told the Privacy Commission in 1976 that no one at the White House had asked the Service for tax returns for several years.[164] Under the circumstances, the White House should be hard pressed to justify the need for such information now.

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[158] S. REP. No. 938 (PART I), 94th Cong., 2d Sess. 321 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3751.

[159] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 968-69.

[160] *See* letter from Kenneth E. Belieu, Deputy Assistant to the President, to Senator Russell Long (April 28, 1970), *cited in* ADMINISTRATIVE REPORT, *supra* note 1, at 981 n.595.

[161] *See* notes 94-99 and accompanying text *supra*.

[162] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 970 n.566 (citing *Presidential Campaign Activities*, 93d Cong., 2d Sess. 11223-30 (1974) (testimony of Roger V. Barth)), *reprinted in* 93d Cong., 2d Sess. (1974) (testimony of John J. Caulfield)).

[163] *See* S. REP. No. 938 (PART I), 94th Cong., 2d Sess. 321 n.8 (1976) (citing *Presidential Campaign Activities of 1974: Hearings Before the Senate Select Comm. on Presidential Campaign Activities*, 93d Cong., 2d Sess. 11223-30 (1974) (testimony of Roger V. Barth)), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3751.

[164] *Hearings, supra* note 46, at 48. *See also* ADMINISTRATIVE REPORT, *supra* note 1, at 971.

V

ACCESS BY STATE OFFICIALS

A. *State Tax Administration*

Section 6103(d) of the Internal Revenue Code, as amended by the Tax Reform Act of 1976, permits disclosure of tax returns and return information to "any State agency . . . which is charged under the laws of such State with responsibility for the administration of State tax laws for the purpose of, and only to the extent necessary in, the administration of such laws . . . ."[165] Such disclosure is permitted "only upon written request by the head of such agency . . . , and only to the representatives of such agency . . . designated . . . as the individuals who are to inspect or to receive the return information . . . ."[166] Furthermore, section 6103(a)(2) requires that officers and employees of a state treat the tax information furnished by the Service as confidential.

Disclosure to state tax officials for tax purposes is appropriate, especially where the taxpayer is reporting the same or similar information to both the state and federal taxing authorities.[167] There is considerable evidence that state tax collection is substantially enhanced by allowing states access to federal information.[168] Moreover, the taxpayer has no reason to complain that he did not suspect that federal tax information about him would

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[165] I.R.C. § 6103(d).

[166] *Id.* The chief executive officer of a state is not permitted access. *Id.* The Code also provides for access to tax return information by state agencies regulating tax return preparers. Such information may be furnished only upon written request and only for purposes of licensing, registration or regulation of income tax return preparers. I.R.C. § 6103(k)(5).

[167] This is true regardless of whether the states are permitted access to federal tax information for use in connection with *state* tax administration or, in circumstances where state taxing authorities administer taxes for municipalities in connection with their administration of local tax laws. *See* INTERIM REPORT, *supra* note 40, at 46.

[168] Commissioner James H. Tully, Jr., testifying on behalf of the New York State Department of Taxation, estimated that New York obtains approximately $30 million a year in additional tax revenues as a result of its access to federal tax information. *Hearings*, *supra* note 46, at 438. Similarly, the Governor of Florida estimated that his state would lose some $11 million if they were denied access to this information. *Id.* at 470 (testimony of Marion Lawless, Assistant Bureau Chief for the Florida Department of Revenue). A representative from Wisconsin estimated that in 1975 his state collected over $1 million in additional income taxes as a result of its access to federal tax information. *Id.* at 478-79 (testimony of Daniel Smith, Administrator of Income, Sales, Inheritance and Excise Taxes for the State of Wisconsin).

be disclosed to other taxing authorities.[169] Under the circumstances, we can see little reason why a taxing authority, be it federal or state, should not be allowed to verify that the appropriate tax is being paid.

Although permitting access by state tax officials to federal tax information entails some increased risk of subsequent unauthorized redisclosure,[170] the personal privacy of the taxpayer can be adequately protected by the enactment of safeguards by the states, the imposition of strict penalties by states for unauthorized disclosure, and close scrutiny of state practices by the Service. The 1976 amendments to section 6103[171] are worthwhile efforts to prevent unauthorized disclosure. Additional problems, however, still exist.

1. *Scope of Disclosure*

Section 6103(d) of the Code grants a state taxing authority access to an individual's entire tax return, even though much of the information included may be unnecessary to accomplish the state's purpose in requesting the information.[172] The Code's only limitation on disclosure to state tax officials is that returns and return information be supplied "for the purpose of and only to the extent necessary in, the administration of [state tax] laws . . . ."[173]

The Service should strive to limit access by the states to the specific information actually needed. There is a mechanical problem, however, in limiting access to portions of returns. Traditionally, states, pursuant to agreements with the federal government, have inspected tax returns by examining either the whole return and copying portions in a secured area of the Internal Revenue Service, or by obtaining magnetic tapes drawn from the Services's files.[174] To effectively limit access, the Service will have to cull

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[169] Cooperation between the Internal Revenue Service and officials administering state tax laws allows the taxing authorities involved to verify the accuracy of the information which an individual has reported to each. Disclosure of individually identifiable tax information to state tax administrators is compatible with the purposes for which information from and about a taxpayer is collected, and serves the interest of effective and fair tax administration. *See* COMMISSION REPORT, *supra* note 11, at 546.

[170] The Privacy Commission noted in its *Interim Report* that unlawful disclosures of federal tax information by state officials had been rare. Indeed, the Commission encountered only one instance in which a governor sought to use federal tax information for an unauthorized purpose. INTERIM REPORT, *supra* note 40, at 43.

[171] *See* note 166 and accompanying text *supra*.

[172] *See* INTERIM REPORT, *supra* note 40, at 42.

[173] I.R.C. § 6103(d).

[174] ADMINISTRATIVE REPORT, *supra* note 1, at 993.

only pertinent information from these sources. The necessary modifications will undoubtedly result in additional costs,[175] but, as the Privacy Commission concluded, these costs are justified by the reduced risk of unauthorized use.[176]

The Privacy Commission recommended that the Service be allowed to disclose individually identifiable IRS data to a state agency responsible for tax administration for the sole purpose of determining, validating or enforcing a taxpayer's liability under a general revenue law of the state.[177] States would be unable to obtain federal tax information for use in administering toll collections, licensing or other regulatory laws which require the payment of a fee.[178] The Privacy Commission further recommended that there be at least a general correspondence between the state tax law for which the federal tax information is sought, and the federal tax laws for which the information was collected.[179]

Several witnesses who testified before the Privacy Commission, however, attested to the potential difficulty in deciding when certain state tax laws are similar to federal provisions.[180] Their testimony highlighted the serious practical problems in permitting a state to use federal tax information for administering some, but not all, of its tax laws.[181] In addition, several states may face problems in determining what constitutes a "tax," as opposed to other revenue-raising measures.

These problems could be avoided by permitting state access to federal tax returns, regardless of the nature of the revenue-raising measure. If the goal of permitting access is increased compliance by taxpayers with state tax laws,[182] state tax officials

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[175] The Privacy Commission noted in its *Interim Report* that it had been advised by the Commissioner of the Internal Revenue Service that, to determine, on a state-by-state basis, exactly what data each requesting state would need for the enforcement of their tax laws and to disclose only that data to the requesting state, would cost the Service approximately $72,000 per year. INTERIM REPORT, *supra* note 40, at 42.

[176] *Id.* at 42.

[177] *Id.* at 41.

[178] *Id.*

[179] COMMISSION REPORT, *supra* note 11, at 546.

[180] *See, e.g. Hearings, supra* note 46, at 246-47 (testimony of Sherwin P. Simmons, representing Section on Taxation of the American Bar Association). *See also* ADMINISTRATIVE REPORT, *supra* note 1, at 999.

[181] *See Hearing, supra* note 46, at 372-73 (testimony of Edgar Lindley, representing the Ohio Department of Taxation).

[182] Compliance should be enhanced at both levels of government by increased taxpayer awareness of the cooperation between federal and state tax authorities. *See* ADMINISTRATIVE REPORT, *supra* note 1, at 998.

should not be limited by the type of the local revenue-raising measure. Broader access, however, compounds the risk of improper use and disclosure;[183] the more state officials who have access to such information, the greater the risk of improper use.

2. *Safeguards and Penalties*

The Internal Revenue Code provides certain safeguards against unauthorized disclosure of federal tax information by the states. Section 6103(p)(4) requires that states, at a minimum, must establish and maintain a permanent system for recording all requests;[184] keep the returns in a secure area;[185] and limit access to those persons authorized to receive the information and whose duties or responsibilities require such access.[186] In addition, state tax officials must furnish a report to the Service describing the procedural safeguards established by the state.[187] Moreover, the Service may withhold tax data from state tax officials if adequate safeguards are not established and maintained.[188]

The Code does not require states to enact statutes prohibiting the redisclosure of federal tax information for purposes other than those for which it was originally requested. State tax officials are required, however, to return the tax information to the IRS when they are finished using it, or make arrangements to have it destroyed.[189] In addition, states which require taxpayers to file

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[183] The Privacy Commission further recommended that disclosure of tax information to state agencies be limited to the information on a federal income, estate or gift tax return (*i.e.*, Forms 1040, 1040A, 706 and 709) and accompanying schedules and summary information regarding adjustments to such returns. INTERIM REPORT, *supra* note 40, at 41. Section 6103(d) of the Code, however, provides for disclosure of "returns and return information," thereby including information received by the Service from third-party sources. Neither the legislative history of the Tax Reform Act of 1976 nor the testimony before the Privacy Commission reveals a legitimate need on the part of the states for third-party source material to administer their tax laws. In the absence of a demonstrated need, access to third-party information should be denied.

[184] I.R.C. § 6103(p)(4)(B).

[185] I.R.C. § 6103(p)(4)(A).

[186] I.R.C. § 6103(p)(4)(C).

[187] I.R.C. § 6103(p)(4)(E). The Secretary of the Treasury is required, in turn, to report to Congress concerning the procedures and safeguards established by the states. I.R.C. § 6103(p)(5). Moreover, the Code permits the Comptroller General to monitor the procedures and safeguards established and requires him to furnish an annual report setting forth his findings with respect to any audit conducted. I.R.C. § 6103(p)(6).

[188] I.R.C. § 6103(p)(4).

[189] *See* I.R.C. § 6103(p)(4)(F).

copies of their federal tax returns with their state tax forms must, as a condition to receiving tax information from the Service, enact laws protecting the confidentiality of the federal tax information attached to or reflected on the state tax return.[190]

The safeguards noted above were, in large part, recommended by the Privacy Commission[191] and incorporated into the Internal Revenue Code as part of the Tax Reform Act of 1976. Although these provisions are salutary, additional measures are necessary to protect the taxpayer from unauthorized redisclosure of individually identifiable federal tax information.

States should be required to enact laws prohibiting redisclosure of tax information to persons not listed on the written request submitted to the Service or for purposes unrelated to that request. These laws should also ban the redisclosure of federal tax information attached to or included on state tax returns for purposes other than state tax administration. As presently drafted, section 6103(p)(8)(B) permits disclosure of copies of federal tax returns to state employees for purposes other than state tax administration, provided the federal tax information is attached to or included on the state tax return and redisclosure is specifically authorized by state law.

The penalty provisions for unauthorized disclosure should also be broadened. Although section 7213(a)(2) of the Code makes it a felony for state employees to disclose federal tax information obtained from the Service,[192] there is no penalty provided for unauthorized disclosure of federal tax information which is supplied directly by state taxpayers in connection with their state tax returns. The Privacy Commission[193] recommended that states, as a condition to obtaining individually identifiable data from the Service, enact statutes imposing penalties substantially similar to those of section 7213 for such unauthorized disclosure.[194]

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[190] I.R.C. § 6103(p)(8)(A).

[191] INTERIM REPORT, *supra* note 40, at 44.

[192] Unauthorized disclosure is punishable by a fine of up to $5,000 and/or imprisonment for not more than 5 years. *See* discussion at notes 283-87 and accompanying text *infra*.

[193] INTERIM REPORT, *supra* note 40, at 43.

[194] This proposal would not affect a state legislature's authority to permit the disclosure of state tax information to another state agency. *See* INTERIM REPORT, *supra* note 40, at 43-44. It would, however, alleviate the difficulties that may arise in attempting to prosecute an individual for unauthorized disclosure of federal tax information obtained from the

The threat of either federal or state prosecution for unauthorized disclosure would serve as a substantial deterrent against unlawful disclosures. State enforced penalties have the advantage of placing the burden of prosecution on the state which enjoys the benefit of federal tax information. State prosecution will also lessen the chance that unauthorized disclosures would go unpunished because of the difficulty in determining whether the Service was the source of the federal tax information.[195]

B. *Non-Tax Purposes*

The Code continued past practice by prohibiting access by the states to federal tax information for purposes unrelated to state tax administration without prior consent of the taxpayer.[196] Such use is clearly incompatible with the purpose for which the information was originally obtained. There are a number of legitimate non-tax uses for tax information; for example, state welfare agents could use the information to uncover welfare fraud.[197] If access were granted, Congress would have to develop an *ex parte* procedure similar to that imposed on the Department of Justice.[198] It is highly questionable whether the enormous burden that requests by fifty states would impose on the federal court system is worth undertaking. State review would result in a lack of uniformity in the decisionmaking process. In short, access by states for non-tax purposes is probably best left as it is—forbidden.

Service where that information has been commingled with similar information obtained by the state directly from the taxpayer.

[195] COMMISSION REPORT, *supra* note 11, at 548; ADMINISTRATIVE REPORT, *supra* note 1, at 997. *See* note 194 *supra*. Enactment of appropriate legislation by states may take time, especially in those states where the legislature meets biennially. To obviate that problem, the Privacy Commission recommended that a state be permitted to continue receiving federal tax information for a period of two years after the adoption of the foregoing recommendations by Congress, pending the enactment of the necessary statute by its legislature. If, however, the necessary state legislation has not been enacted by the end of the two-year period, the Service should be required to discontinue the disclosure of federal tax information until the necessary statute is enacted. *See* INTERIM REPORT, *supra* note 37, at 44.

[196] *See* I.R.C. § 6103(d).

[197] *See Hearings, supra* note 46, at 451-52 (testimony of Owen L. Clarke, Chairman of the Board of Trustees of the Federation of Tax Administration and Commissioner of Corporations and Taxation for the Commonwealth of Massachusetts).

[198] *See* text accompanying notes 94-99 *supra*.

VI

Access by Local Governments

Prior to the Tax Reform Act of 1976, local tax authorities were permitted access to federal tax return information for purposes of local tax administration.[199] Tax information was furnished upon written request of the governor to the state tax officials who, in turn, distributed it to local taxing authorities.[200] Although there was no statutory limitation on the amount or type of information which could be obtained,[201] as a matter of practice, the information usually consisted of no more than name, address, social security number and type of return filed.[202] The information was used primarily to identify individuals who may have failed to file their local government tax return.[203]

The Tax Reform Act halted the disclosure of federal returns and return information to local tax authorities. With the exception of information concerning tax return preparers,[204] no information may be disclosed to localities, either directly from the Service or indirectly through state tax authorities.[205] If states permit unauthorized disclosures of such information to local governments, the Service can, among other alternatives, deny subsequent requests for tax information.[206]

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[199] Pre-Amendment § 6103(b) permitted tax information to be "furnished to any official, body, or commission of any political subdivision" of a state "upon written request of the governor." Int. Rev. Code of 1954, ch. 61, § 6103(b)(2), 68A Stat. 753 (repealed 1976). Income tax information, however, was not furnished directly by the Service to local governments. *See* text accompanying note 200 *infra*.

[200] *See* S. Rep. No. 938 (Part I), 94th Cong., 2d Sess. 336 (1976), *reprinted in* [1976] U.S. Code Cong. & Ad. News 3439, 3765; *Hearings, supra* note 46, at 395 (testimony of Edgar Lindley on behalf of the Ohio Department of Taxation).

[201] The Code provided that federal tax information "may be furnished only for the purpose of, and may be used only for, the administration of [the] tax laws [of the locality]." Int. Rev. Code of 1954, ch. 61, § 6103(b)(2). 68A Stat. 753 (repealed in 1976).

[202] Interim Report, *supra* note 40, at 46. *Hearings, supra* note 46, at 396 (testimony of Edgar Lindley on behalf of the Ohio Department of Taxation).

[203] Interim Report, *supra* note 40, at 46.

[204] I.R.C. § 6103(k)(5) permits the disclosure of tax preparer identity information (including name, mailing address, and taxpayer identifying number) to any state or local agency, body, or commission charged with the licensing, registration or regulation of tax return preparers. *See* S. Rep. No. 938 (Part I), 94th Cong., 2d Sess. 339 (1976), *reprinted in* [1976] U.S. Code Cong. & Ad. News 3439, 3768; note 166 *supra*

[205] Nor does the Code authorize the use of federal tax data by state officials in administering local tax laws. The 1976 revisions, however, were not intended to limit the disclosure of state tax returns and return information by state tax officials. *See* S. Rep. No. 938 (Part I), 94th Cong., 2d Sess. 338 (1976), *reprinted in* [1976] U.S. Code Cong. & Ad. News 3439, 3768.

[206] *See* I.R.C. *See* 6103(p)(4); note 200-05 and accompanying text *supra*.

Several witnesses at the Privacy Commission hearings argued in favor of access by local governments to federal tax information. Edgar Lindley, Commissioner of the Ohio Department of Taxation, testified that municipal and local tax administrators would be severely handicapped if they were denied access to IRS files because they do not have names, addresses or social security numbers in their files.[207] Without federal tax information, some localities may be unable to determine who should be paying taxes. One community representative told the Privacy Commission that fifteen to twenty-five percent of its collections would be lost if the community were deprived of federal returns.[208]

Local officials apparently did not abuse the access afforded them prior to 1976. Commissoner Alexander noted in his testimony before the Privacy Commission that there had been some complaints alleging disclosure of confidential information by local officials.[209] However, other witnesses stated that while documented abuses had occurred at the national level of government, they were not aware of any unauthorized disclosures at either the state or local levels.[210] None of the witnesses who testified at the hearings conducted by the Privacy Commission objected to the disclosure of tax information to local jurisdictions, provided confidentiality could be maintained. David Martin, Regional Director of the Administrative Conference of the United States, specifically recommended that the Service be authorized to disclose tax returns to state officials for redisclosure by them to local taxing authorities.[211]

To protect the confidentiality of the tax information disclosed to local governments, the procedural safeguards now required of the states,[212] as well as the additional safeguards noted,[213] should

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[207] *Hearings, supra* note 46, at 374.

[208] *See id.* at 294-95 (statement by David F. Linowes, Chairman of the Privacy Commission). *Accord, id.* at 383 (testimony of Richard E. O'Brien, Chairman of the Tax Committee of the Ohio Municipal League and commissioner of Taxation for the City of Toledo, Ohio); *id.* at 398 (testimony of John R. Urban, testifying on behalf of the Regional Income Tax Agency for the Suburban Cleveland area).

[209] Testimony of Donald C. Alexander before the third meeting of the Privacy Protection Study Commission (September 9, 1975) at 235 (transcript on file at the *Cornell Law Review*).

[210] *See, e.g., Hearings, supra* note 46, at 385 (testimony of John R. Urban on behalf of the Regional Income Tax Agency of the Suburban Cleveland area); *id.* at 393 (testimony of Edgar Lindley on behalf of the Ohio Department of Taxation).

[211] *Id.* at 262.

[212] *See* I.R.C. § 6103(p); notes 184-90 and accompanying text *supra*.

be made applicable to municipalities as a condition for receiving the information. In addition, local officials should be subject to state laws or local ordinances which prohibit the use of the information for purposes other than tax administration, and which impose strict penalties for unauthorized redisclosures.[214]

The Privacy Commission recommended that local governments should be able to obtain federal tax information for purposes of local tax administration,[215] but that the information be limited to a taxpayer's name, address, social security number, and type of return filed.[216] Disclosure of limited amounts of federal tax information is generally compatible with the purpose for which the information was originally obtained—the collection of taxes. Although access to such information provides some increased risk of unauthorized disclosures, the need demonstrated by local governments for this information outweighs the minimal risk that the information will be misused, especially if adequate safeguards are maintained, strict penalties are imposed for unauthorized disclosure, and local practices are closely scrutinized.[217]

VII

ACCESS BY CONGRESS

A. *Tax Committees*

Prior to the Tax Reform Act of 1976, any member of a congressional tax committee could obtain identifiable tax information simply by asking for it. The information could then be used at a

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[213] *See* notes 191-94 and accompanying text *supra*.

[214] For example, ordinances in Ohio contain penalties of $1,000 for each offense. *Hearings, supra* note 46, at 386 (testimony of John R. Urban on behalf of the Regional Income Tax Agency of the Ohio Department of Taxation). *See* 57 OHIO REV. CODE ANN. § 5715.99 (Page 1973).

[215] *See* INTERIM REPORT, *supra* note 40, at 47; COMMISSION REPORT, *supra* note 11, at 548.

[216] Although there was some evidence presented at the Privacy Commission hearings which would indicate that this information would not be sufficient to satisfy the needs of certain municipalities, the primary use of federal tax information by localities appears to be for the purpose of locating taxpayers. In this respect, the recommended disclosures should be adequate. More expansive disclosures, consistent with the principle of disclosure on a need-to-know basis, would necessitate tailoring the information and monitoring system to the needs of each locality—an expense which would appear neither warranted nor necessary. It should be noted that the Code permits access by local government officials to certain federal tax information for use in locating absent parents. *See* I.R.C. § 6103(l)(6).

[217] Access by local governments to federal tax information for purposes other than local tax administration, however, is neither necessary nor justified. Such access is not currently permitted, nor was it authorized by the pre-1976 Code. Moreover, we are aware of no new

public session of the committee.[218] Despite the ease of access, between 1965 and 1975 there apparently were no more than six requests for income tax returns by tax committees.[219] The Tax Reform Act of 1976 nevertheless restricted disclosure and redisclosure of confidential tax information by congressional tax committees. Only the chairmen of the Committee on Ways and Means of the House, the Committee on Finance of the Senate and the Joint Committee on Taxation may obtain tax information.[220] Unless the taxpayer consents, this information may be used only in closed sessions of the committee.[221] Unfortunately, the Tax Reform Act also permits redisclosure of tax information to the full House or Senate without any requirement that confidentiality be protected.[222] Thus, while the committee sessions are closed, the committee report which might reveal identifiable tax information may be publicized. Moreover, an individual member of Congress may place information in the *Congressional Record* which identifies a particular taxpayer.

Conceding that tax return information should be available to congressional committees responsible for drafting tax legislation—and that there is some evidence that various congressional studies of tax reform measures have made important use of tax return data[223]—no compelling argument has been made for giving congressmen information which can be identified with a particular taxpayer.[224] Given the paucity of committee requests over the past ten years,[225] it is clear that they have no real

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persuasive reason which has been advanced in favor of local governments obtaining access to federal tax data for purposes unrelated to tax administration.

[218] Int. Rev. Code of 1954, ch. 61, § 6103(d), 68A Stat. 753 (repealed 1976).

[219] ADMINISTRATIVE REPORT, *supra* note 1, at 960.

[220] I.R.C. § 6103(f)(1). Such disclosure may only be made upon the written request of the committee chairman to the Secretary of the Treasury. Section 6103(f)(2) also permits disclosure to the Chief of Staff of the Joint Committee on Taxation upon his written request to the Secretary of the Treasury. The Chief of Staff may in turn submit the information to a tax committee, provided that if the information identifies a particular taxpayer, the committee is sitting in closed executive session.

[221] I.R.C. § 6103(f)(1).

[222] I.R.C. § 6103(f)(4)(A).

[223] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 968.

[224] The legislative history of § 6103 is largely silent with respect to the need for congressional access to tax returns and tax return information. The Privacy Commission included no study of congressional access in its report, and the *Administrative Report,* which concluded that identifiable information should not be available to Congress, presented no arguments in support of congressional accesss.

[225] *See* text accompanying note 219 *supra*.

need for such information. Considering the risk of disclosure, the public would be better served if congressional tax committees were denied any access to identifiable tax information.

B. *Non-Tax Committees*

Prior to 1976, non-tax committees frequently obtained tax returns and return information pursuant to an executive order from the President and a committee or subcommittee resolution.[226] From the 90th Congress to the 94th Congress, various non-tax committees made 48 requests concerning 634 taxpayers.[227] At least one committee, the House Committee on Government Operations, regularly requested and received a blanket executive order at the commencement of each Congress covering any tax information it might thereafter wish to see, rather than requesting an executive order each time specific tax information was desired.[228]

The Tax Reform Act of 1976 amended the Code to make access to individually identifiable tax information by non-tax committees more difficult. The Service may disclose information only to those committees that have been specially authorized by resolution of the full House or Senate.[229] The congressional resolution must specify the purpose for which the return or return information is sought and stipulate that the requested information is not "reasonably" available from an alternative source.[230]

Tax return information, arguably, can be used beneficially by some non-tax congressional committees. For example, committees which have drafting and oversight responsibility for certain federal subsidy programs might use identifiable tax information to determine whether applicants are concealing income from their application forms. Once applicants are approved, tax information could be used to ascertain whether recipients of federal monies continue to meet prescribed income levels. In fact, investigative use has been the most frequently cited reason for requests of tax return information by non-tax congressional committees.[231]

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[226] S. REP. No. 938 (PART I), 94th Cong., 2d Sess. 319 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3749.

[227] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 960-61.

[228] Letter from Chet Holifield, Chairman, House Committee on Government Operations, to Wilbur Mills, Chairman, House Committee on Ways and Means (July 13, 1973), *cited in* ADMINISTRATIVE REPORT, *supra* note 1, at n.550.

[229] I.R.C. § 6103(f)(3).

[230] *Id.*

[231] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 962-65.

There are, however, substantial arguments against disclosing individually identifiable tax information to congressional committees for non-tax purposes. Such use is incompatible with the purpose for which the tax information was originally submitted to the government. There is also the risk of improper political use, although there appears to be no record of such abuse. Further, there is the difficulty of protecting confidentiality. A 1970 survey by the Joint Committee on Internal Revenue Taxation revealed significant variations in the security measures taken by the committees which had requested tax information.[232]

As previously discussed,[233] Justice Department lawyers seeking identifiable tax information for non-tax purposes must first obtain a federal court order permitting access upon a showing, among other things, of reasonable cause to believe a particular crime has been committed. We see no logic in permitting congressional access by any different means or by any less of a showing.

Alternative means for checking misuse of federal funds exist. For example, an applicant for a federal subsidy could be required to submit his tax returns or to waive the prohibition on disclosure as a condition to obtaining the funds.

One problem has been partially eliminated by the Tax Reform Act. Prior to 1976, a committee which had obtained tax information could submit it to the full House or the Senate.[234] The Service had construed the pre-1976 provision to permit publication of information in a committee report, thereby providing a means of avoiding confidentiality.[235] The problem was partially alleviated by section 6103(f)(4)(B), which provides that when non-tax committees submit tax return information to the full House or Senate, it must be done in "closed executive session" if the information is in identifiable form and the taxpayer has not consented in writing.[236]

While this limitation on the use of identifiable information by congressional non-tax committees is a salutary first step, we believe that tax returns should be disclosed only to congressional tax

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[232] *See id.*

[233] *See* discussion at notes 94-100 and accompanying text *supra*.

[234] Int. Rev. Code of 1954, ch. 61, § 6103(d)(1)(c), 68A Stat. 753 (repealed in 1976).

[235] ADMINISTRATIVE REPORT, *supra* note 1, at 967.

[236] I.R.C. § 6103(f)(4)(B). There would appear to be little reason for distinguishing between tax and non-tax committees in requiring that individually identifiable information be submitted to the full House or Senate only in closed executive session. The privacy considerations are the same regardless of which committee is responsible for transmitting the information.

committees,[237] and even then, only in unidentifiable form. Absent a showing of "reasonable cause"—or its non-criminal functional equivalent—in an *ex parte* proceeding, no congressional committee should be granted access to identifiable tax information.

VIII

Statistical Use of Tax Returns

Prior to 1976, the regulations promulgated under section 6103 specifically provided for the inspection of individually identifiable[238] tax returns and return information by certain government agencies—including the Department of Commerce, the Federal Trade Commission, and the Securities and Exchange Commission—for the purpose of compiling statistical data.[239] The Privacy Commission study concluded that only the Bureau of the Census, a part of the Department of Commerce, had "clearly" demonstrated the need for information about individuals in identifiable form, but that the Department of the Treasury might be able to demonstrate such a need in the future.[240] The Code was subsequently amended by the Tax Reform Act of 1976 to provide the Bureau of the Census[241] and the Department of the Treasury[242] access to identifiable tax return information.

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[237] *See Hearings, supra* note 46, at 172 (testimony of Sheldon Cohen, former I.R.S. Commissioner).

[238] Many government agencies receive non-identifiable tax information for statistical purposes. Such use is outside the scope of this article.

[239] Treas. Reg. § 301.6103(a)-102, T.D. 6375, 1959-1 C.B. 679 (S.E.C.); Treas. Reg. § 301.6103(a)-103, T.D. 6570, 1976-2 C.B. 229 (Advisory Commission in Intergovernmental Relations); Treas. Reg. § 301.6103(a)-104, T.D. 6547, 1961-1 C.B. 698 (Department of Commerce); Treas. Reg. § 301.6103(a)-106, T.D. 6545, 1961-1 C.B. 695 (F.T.C.); Treas. Reg. § 301.6103(a)-107, T.D. 6816, 1965-1 C.B. 537 (Federal Reserve System). All of the above regulations were repealed in 1978. 43 Fed. Reg. 55760 (1978).

[240] Interim Report, *supra* note 40, at 47-49. The Privacy Commission noted that besides the Bureau of the Census and Department of Treasury, only the Bureau of Economic Analysis and the Federal Trade Commission used identifiable tax information. Neither of the latter two, however, used tax information about individuals, only about legal and business entities. *Id.* Pre-1976 Treasury regulations permitted SEC access, but the legislative history of the Tax Reform Act noted that as of 1976 the SEC did not use tax information for statistical purposes because the function for which the SEC had required the information had been shifted to the Federal Trade Commission. S. Rep. No. 938 (Part I), 94th Cong., 2d Sess. 333 (1976), *reprinted in* [1976] U.S. Code Cong. & Ad. News 3439, 3762-63.

[241] I.R.C. § 6103(j)(1).

[242] I.R.C. § 6103(j)(3).

A. *The Bureau of the Census*

Section 6103(j) of the Code provides that the Bureau of the Census may upon written request obtain tax returns or return information "for the purpose of, but only to the extent necessary in, the structuring of censuses and national economic accounts and conducting related statistical activities authorized by law."[243] Regulations promulgated after the enactment of the 1976 amendments preserved the scope of available information but provided that the Service could not disclose the taxpayer's name.[244] A 1978 amendment to the regulation makes it possible for the Bureau to obtain the taxpayer's name "where necessary to evaluate the completeness of census coverage."[245]

The Bureau of the Census has made a convincing argument for access to identifiable tax information. According to the legislative history of the Tax Reform Act of 1976:

> The Bureau uses information from tax returns to assist in preparing the Economic Indicators, the Survey of Minority-owned Business Enterprises, and the Survey of County Business Patterns. The Economic Census (conducted every five years) is used for the Index of Industrial Production (of the Federal Reserve Board), the Index of Wholesale Prices (of the Bureau of Labor Statistics), and the Gross National Product accounts. The Current Economic Indicators include information on retail sales, manufacturers' shipments, orders and inventories, investment, and are used for the Index of Industrial Production (Federal Reserve Board). These statistics are used as a basis for national economic policy, for distributing funds by agencies, by State and local governments in determining their programs, and by private business in forecasting, marketing, investment, etc.[246]

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[243] I.R.C. § 6103(j)(1).

[244] Treas. Reg. § 404.6103(j)(1)-1(b)(1), T.D. 7471, 1977-1 C.B. 380 (amended 1977).

[245] Treas. Reg. § 404.6103(j)(1)-1(b)(1)(i), T.D. 7581, 1977-5 I.R.B. 18. To conduct demographic, economic and agricultural statistics programs, the Bureau of the Census may also obtain limited information from certain schedules accompanying the federal income tax returns filed by individuals. Treas. Reg. § 404.6103(j)(1)-1(b)(2).

[246] S. REP. No. 938 (PART I), 94th Cong., 2d Sess. 331-32 (1976), *reprinted in* [1976] U.S. CODE CONG. & AD. NEWS 3439, 3761. The *Senate Report* also noted that, in 1975, Census obtained 8,400,000 Business Master File Entity Change Records showing employer identification number (EIN), name, address, and zip code; and 21,200,000 Forms 941 showing EIN, total compensation, FICA wages, taxable tips, master file account, tax period, and address change. *Id.* at n.10. *See also* ADMINISTRATIVE REPORT, *supra* note 1, at 881-86; *Hearings, supra* note 40, at 110-11.

The Bureau uses identifiable tax information to correlate data it has gathered with data supplied by the Service. For example, the Bureau collects information on an establishment basis; the Service, however, collects information on a legal entity basis.[247] In order to tabulate data on multi-establishment firms, the Bureau must cull out duplications in the Service information.[248] Because current law prohibits the disclosure of Bureau information to the Service,[249] were the Bureau denied access to identifiable tax information, the Bureau would have to increase its data gathering capability—a costly burden[250] and one duplicative of the Service's efforts.

Such duplication is unnecessary. The Bureau has had an exemplary record in protecting the confidentiality of tax information.[251] Moreover, section 6103 and the regulations promulgated thereunder provide substantial security measures with respect to statistical use of this information.[252] The Bureau's sole function is statistical tabulation and analysis; it should be neutral and objective.[253] In addition, the Bureau does not have a functional relationship with other subdivisions of the Department of Commerce.[254] It is therefore probable that the information will remain within the Bureau. There is little to be gained in further hindering the Bureau's access to information.

B. *The Department of the Treasury*

The Privacy Commission noted that while the Department of the Treasury appeared to use tax information for statistical purposes, the Commission could not determine whether that department needed *identifiable* information for those purposes. The Commission recommended that the department should be granted identifiable tax information only if it could show a clear need.[255]

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[247] ADMINISTRATIVE REPORT, *supra* note 1, at 1070 n.251.

[248] *Id.*

[249] 13 U.S.C. § 9 (1976).

[250] The Bureau of the Census at one point estimated that it would cost an additional $30 to $65 million to prepare the five-year Economic Indicators if it were denied access to individually identifiable federal tax information. ADMINISTRATIVE REPORT, *supra* note 1, at 882.

[251] INTERIM REPORT, *supra* note 40, at 48.

[252] *See* I.R.C. § 6103(p)(4).

[253] *See* ADMINISTRATIVE REPORT, *supra* note 1, at 885.

[254] *See id.* at 879-86.

[255] INTERIM REPORT, *supra* note 40, at 49.

The Tax Reform Act permits such disclosure "for the purpose of, but only to the extent necessary in, preparing economic or financial forecasts, projections, analyses, and statistical studies and conducting related activities."[256] Because the request for such information must be in writing and must set forth the "specific reason or reasons why such inspection or disclosure is necessary,"[257] it is likely the requesting party will ask only for truly necessary information. As the Privacy Commission concluded, "[d]ependence upon written requests with articulated objectives should deter unjustified disclosures."[258]

Written requests, coupled with the Tax Reform Act's provision prohibiting redisclosure of identifiable information,[259] and the imposition of criminal sanctions for such redisclosure, should prevent any serious problem.[260] However, given the almost total absence of any indication from the Department of the Treasury as to why it needs identifiable information, its requests for tax data in the future should be monitored to determine whether there is such need.

IX

REMEDIES FOR UNAUTHORIZED DISCLOSURE

A. *Criminal Penalties*

Prior to the enactment of the Tax Reform Act of 1976, section 7213 of the Code provided that it was a misdemeanor punishable by up to a $1,000 fine or one year in prison or both (1) for an officer or employee of the United States to divulge or permit inspection of certain information about a taxpayer's income without authority; or (2) for an officer or employee of a state or local government to make an unauthorized disclosure of information furnished to the government pursuant to section 6103 of the Code.[261]

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[256] I.R.C. § 6103(j)(3).

[257] *Id.*

[258] COMMISSION REPORT, *supra* note 11, at 549.

[259] I.R.C. § 6103(j)(4).

[260] *See* I.R.C. § 7213. In addition, the Treasury Department should, like the Bureau of the Census, be required by statute to establish safeguards as a condition of receiving such information.

[261] Int. Rev. Code of 1954, ch. 75, § 7213, 68A Stat. 855-56, *amended by* Pub. L. No. 85-866, 72 Stat. 1666 (1958), Pub. L. No. 68-778, 75 Stat. 940-41 (1960) (repealed 1976). The Privacy Act of 1974 made the following persons liable for a maximum jail term of one year and/or a fine of $5,000:

The Tax Reform Act increased the offense under section 7213 from a misdemeanor to a felony, punishable by a $5,000 fine or five years in prison or both.[262] The statute now applies to the unauthorized disclosure of all information about an individual, whether filed by that individual or collected by the Service from third parties.[263] The revisions make additional persons subject to the criminal penalties: former employees of federal, state and local governments; agents (including contractors) of the federal government; and local child support officials.[264] The Tax Reform Act preserved the prior requirement that a federal officer or employee be discharged upon conviction of the crime.[265]

The increase in the potential penalty for unauthorized disclosure reflects the strong congressional policy in favor of confidentiality. The Privacy Commission, which had chastised Congress for not enacting all its proposed confidentiality provisions, had argued against increasing the penalty to a felony because felony treatment "might present practical problems in obtaining convictions."[266] The irony should not be lost: the Privacy Commission was worried that juries would not be as concerned with confidentiality of their tax returns as Congress thought they should be.

B. *Civil Remedies*

It was not until the Privacy Act of 1974 that a civil action could be brought against an agency making unauthorized disclosure of taxpayer information.[267] If the agency is found to have

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(1) Any officer or employee of an agency, . . . who knowing that disclosure of the specific material is prohibited, willfully discloses the material in any manner to any person or agency not entitled to receive it . . . .

(2) Any officer or employee of any agency who willfully maintains a system of records without meeting the notice requirements . . . .

(3) Any person who knowingly and willfully requests or obtains any record concerning an individual from an agency under false pretenses . . . .

5 U.S.C. 552a(i) (1976).

These provisions are undercut, however, by the Privacy Act's broad exceptions. *See* text accompanying notes 40-43 *supra*.

[262] I.R.C. § 7213(a)(1).

[263] Section 7213(a)(1) prohibits the unauthorized disclosure of any return or return information, as those terms are defined by section 6103(b) of the Code. *See* note 53 *supra*.

[264] I.R.C. §§ 7213(a)(1) to (3).

[265] I.R.C. § 7213(a)(1).

[266] COMMISSION REPORT, *supra* note 11, at 559. The Privacy Commission, however, agreed with the increase in the maximum amount of the fine from $1,000 to $5,000. *Id.*

[267] 5 U.S.C. § 552a(g) (1976). The Privacy Act provides that individuals who have been adversely affected by a federal agency's failure to comply with tbe Privacy Act, including

acted intentionally or willfully, the United States is liable for actual damages in an amount of not less than $1,000, together with costs and attorney's fees.[268] The minimum award reflects the difficulty an aggrieved taxpayer may have in proving actual damages.

The Tax Reform Act added section 7217 to the Code. This section establishes a civil remedy for any taxpayer damaged by an unlawful disclosure.[269] It provides that any *person* who knowingly or negligently discloses any taxpayer return information in violation of section 6103 is liable for damages in the same amount provided under the Privacy Act (not less than $1,000), but is not liable for attorneys' fees.[270] The violator may also be liable for punitive damages where the disclosure was willful or the result of gross negligence.[271] A subsequent amendment to section 7217 offers greater protection to the malfeasor by providing that disclosures resulting "from a good faith, but erroneous, interpretation of section 6103" are not actionable.[272]

CONCLUSION

Each of the confidentiality provisions of the Tax Reform Act of 1976 must be viewed in light of the varying and competing policy considerations. Not every governmental request for tax information can or should be treated identically.

The Tax Reform Act of 1976 went a long way toward recognizing that tax information should be viewed as confidential by stopping the relatively free availability of federal tax returns to a wide variety of government agencies for an even wider variety of uses. Additional reforms are still necessary, however, to ensure that tax information is used primarily for its intended purpose of revenue collection, and that the reasonable privacy expectations of the individual taxpayer are respected.

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unauthorized disclosure of information, may bring a civil action against the agency. 5 U.S.C. §§ 552a(g)(1)(D) and (4).

[268] 5 U.S.C. § 552a(g)(4) (1976).

[269] I.R.C. § 7217.

[270] I.R.C. § 7217(a).

[271] I.R.C. § 7217(c)(I).

[272] Pub. L. No. 95-600, 92 Stat. 2763, 2923 (1978) (codified at I.R.C. § 7217(b)).