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The Future of Tax Privacy

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The Future of Tax Privacy

Abstract - This essay considers the past, present, and future of tax privacy. Regarding the past, it took until 1976 for the concept of tax privacy to be explicitly established in statutory law. Congress established this concept in Section 6103 of the Internal Revenue Code, but has also made it subject to numerous exceptions. In the present, much personal financial information is now accessible out of the tax context and is regulated by other statutes and regulations. This result has made the area of tax privacy somewhat less exceptional today as a regulatory area than in the past. Finally, in the future, tax information in the electronic age will be subject to the same critical issues, such as those involving data security, as other personal information. In conclusion, tax information remains important, but is increasingly subject to the same forces—legal and technical—as other personal information.

INTRODUCTION

The history of tax privacy contains a number of surprises. First, the concept of tax privacy was a contested one throughout much of the 19th and 20th Century. For a period, tax returns were considered to be public documents. At times, they were even posted on courtroom doors or published in newspapers. Nonetheless, there were also advocates for tax privacy and the need for confidentiality of return information.

Second, the imposition of a statutory requirement of confidentiality for tax returns and a shift to a statutory regulation of access to tax returns occurred relatively recently in the history of tax law. The change occurred in the Tax Reform Act of 1976. From a historical perspective, the establishment of this statutory principle of tax privacy occurred as part of the enactment of the most important generation of privacy laws in the 1970s.

If we move from the past of tax privacy to the present, it looks much like other areas of information privacy law. The Tax Reform Act of 1976 abolished the authority of the President to make rules for release of tax information. Its Section 6103 establishes a general rule of confidentiality with Congress to set exceptions by statute. Beginning in 1976 and, subsequently, Congress has enacted an impressive list of disclosure exceptions to Section 6103. Release of tax information is now permitted for purposes such as criminal litigation, civil litigation, child support enforcement, and counterterrorism. The specific disclosure standards vary, but Congress gener-

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ally crafts a given statutory test based on its sense of the necessary benefits and burdens of disclosure in a specific context.

Finally, there is the future of tax privacy. In certain ways, tax information is less important than in the past. The government and curious members of the public have more chances and venues than before to gain access to financial information of the kind that is found in tax returns. At the same time, tax information is more important than in the past. Due to the preparation, filing, and storage of tax returns in electronic form, the security of tax return information is now a critical issue.

Above all, there is the issue of tax privacy exceptionalism. Is personal tax information different than other kinds of personal data? Should tax data be treated differently? Tax information is still exceptional in the narrow sense that it is subject to a specific legal regime of access and use restrictions. To the extent, moreover, that tax returns constitute probably the largest and most detailed set of personal data that an American files under legal compulsion, there is also something exceptional about it, and a widespread desire to keep access to it limited. At the same time, however, beyond tax information, a tremendous variety of personal financial and other information about individuals is available to the government, the private sector and, in some instances, the general public. Questions regarding the legal rules concerning access to this other information have come to take a place of prominence in privacy debates as opposed to personal tax information.

THE PAST

In this section, I examine two topics. The first is the legal development of tax disclosure and tax confidentiality rules for personal tax information prior to the enactment of the Tax Reform Act of 1976. The themes here include how these

rules changed over time, the treatment of Executive Branch discretion to shape disclosure regulations, and the sharing of information within government beyond the Treasury Department. I will also look at public access to corporate tax records. The second topic concerns the different policy arguments made in the past for either tax disclosure or tax confidentiality.

From Public Records to Tax Privacy

The historical record contains a surprise: until relatively recently, namely 1976, statutory law did not establish confidentiality for income tax return information. Rather, the most prevalent approach considered tax return information as a public record, but one open for inspection only pursuant to regulations issued by the Department of Treasury and approved by the President. Sometimes these regulations permitted inspection; sometimes, they did not. In this subsection, I discuss the historical development of income tax privacy as well as the parallel historical discussion regarding corporate tax privacy.

The Civil War Income Tax of 1862, the first income tax in U.S. history, represented an early high point for the publicity of tax information. Pursuant to this statute's regime, tax assessment information was posted on courthouse doors and published in newspapers (Congressional Research Service, 1974, 6-8). The goal of this publicity was to promote compliance with tax law (Department of Treasury, Office of Tax Policy, October 2000, 15). Subsequently, the relative privacy and publicity accorded to tax return information ebbed and flowed until 1976.

In 1870, for example, a Treasury Decision prohibited newspaper publication of annual tax assessments, but permitted public inspection of these lists. The Revenue Act of 1894 formalized the Treasury Decision's policy and prohibited the publication of any income tax return without additional legal authorization (Income Tax

Act of August 15, 1894). Such legal authorization was provided by the Revenue Act of 1924, which required the IRS Commissioner to prepare lists "containing the name and ... address of each person making an income tax return together with the amount of income tax paid by such a person" (Act of 1924). These lists were to be made available for public inspection in "the office of the collector in each internal revenue district."

In 1925, the Supreme Court in *U.S. v. Dickey* upheld this statute, its public inspection requirement, and the publication of the tax assessment information by newspapers. In its analysis, the Supreme Court was obliged to interpret a different and earlier section of tax law, which had made it unlawful to print or publish tax information in any manner "not provided by law." For the Supreme Court, this earlier prohibition against publication was written in a fashion that allowed it to be narrowed over time by creation of "liberalizing exceptions." The Court then considered the policy behind the Revenue Act of 1924. In enacting this statute, Congress did not intend to permit the earlier and general prohibition on publication to block its mandated list of taxpayers and amounts paid. Rather, the 1924 statute explicitly sought to have the Commissioner promote disclosure and publicity. The Commissioner was to draw up a list "[t]o the end that the names and addresses of the taxpayers and the amounts paid by them may be generally known."

In sum, according to the Supreme Court, the 1924 tax statute considered names, addresses, and amount of income tax paid to be "public property." This information could be "passed on to others as freely as the possessors of it may choose." As we shall see in the next section, however, the notion of public access to tax returns was not uncontested. Indeed, there was opposition to the 1924 statute, and a 1927 law, championed by President Calvin Coolidge and Treasury

Secretary Andrew Mellon, narrowed the publicity requirement to require only the posting of a taxpayer's name and address and not the amount of their tax liability.

In 1934 law, Congress enacted its infamous and ill-fated "pink slip" requirement for disclosure. The 1934 law required collection of information from each taxpayer on a "pink slip," that is a pink-colored form (Pomp, 1993). The pink slip, which was to be made available for public inspection, included a taxpayer's name and address, total gross income, total deductions, net income, and other tax information. The pink-slip provision was also to apply to corporate tax information. The opponents of this provision were successful in having it repealed in 1935—before the law took effect. Nonetheless, it was not until 1966 that Congress prohibited publication of tax return information in newspapers, and it was not until 1976 that Congress established the principle of tax privacy in a federal statute.

In addition to these different statutory approaches to openness of tax information, another important historic aspect of tax privacy law concerns Executive Branch discretion. The Revenue Act of 1913 set a general pattern that would stay in place until the Tax Reform Act of 1976. In the Revenue Act of 1913, Congress established a general statutory standard of public access, but one that the President and his Secretary of the Treasury would shape and limit through specific regulations. The Revenue Act of 1913 stated: "[R]eturns ... shall constitute public records and be open to inspection as such: Provided, that any and all such returns shall be open to inspection only upon the order of the President, under rules and regulations to be prescribed by the Secretary of the Treasury and approved by the President." Over the subsequent decades, public access to tax returns then increased and diminished depending upon tax regulations and Executive Branch decisions. The general pattern was, however,

to increasingly limit public access to this information.

From the 1920s on, there was a development of a further element of tax privacy. This dimension concerned disclosure to tax information beyond the Treasury Department. Over time, the Executive Branch, pursuant to the discretion granted to it by Congress, increased the access to tax return information permitted to different parts of government. It considered personal tax information as a generalized asset, which was to be shared with different agencies and with Congress. As one district case from 1989 summarized this period before enactment of the Tax Reform Act of 1976, the IRS served as a "lending library" of personal information for other parts of government (*Crismar v. U.S.*, *4).

In its reports immediately before and after enactment of the 1976 statute, the Privacy Protection Study Commission, a federal blue ribbon panel, indicated its disapproval of this policy of widespread sharing of tax information. The panel summarized the development of the law in this fashion: "the Executive Branch has used its discretion to make tax information available to a steadily increasing number of government agencies through a series [of] Executive orders and regulations. ... Information about individuals maintained by the Internal Revenue Service may also be made available to the President and to Committees of the Congress" (Privacy Protection Study Commission, 1977). Thus, before enactment of the Tax Reform Act of 1976, the declining public access to income tax information had been accompanied by an increasing sharing of this same information within the government.

Finally, these developments regarding the privacy of *personal* income tax information were accompanied by a parallel discussion regarding *corporate* tax data. One of the critical stages in the debate about the general public's access to corporate tax information occurred with the enactment of the Corporate Excise Tax of

1909. This statute has been termed "the ancestor of the modern corporate tax" (Kornhauser, 1990).

The Corporate Excise Tax was a key part of the Progressive Era's drive to limit corporate power. The 1909 law assessed a one-percent tax on the net income of corporations. Yet, beyond its taxing function, a key part of the statute was its "publicity" feature. Proponents of the law wanted more transparency regarding the financial structure of corporations and their transactions. In her historical study of the 1909 Act, Kornhauser (1990) demonstrates how the debate about publicity during the Act's enactment did not consistently distinguish between the government's and general public's access to information about corporations. The distinction is, of course, an important one.

As enacted, the 1909 Corporate Excise Act included inconsistent provisions between publicity and privacy of tax information and left it to the Executive Branch to resolve the issue. This result was the same as the compromise later made in 1911 for personal tax information. First, the 1909 statute provided that corporate returns "shall be public records and be open to inspection as such." Second, it prohibited a federal employee from "making known in any manner any document received, evidence taken or report made, under this section except upon the special direction of the President." The result was that public access to corporate tax return was left to the discretion of the President. Here, again, we see the important historical theme of Executive branch discretion to decide upon access to tax information.

The resulting regulations enacted under the 1909 law drew a distinction between publicly traded corporations and closely held ones. The returns of any publicly listed companies were open to the inspection of any person "upon written application to the Secretary of Treasury." In contrast, the returns of closely held corporations were open only to inspection

by employees of the Treasury Department or by other government employees for proper cause as decided by the Attorney General. The distinction was driven, in part, by the judgment that closely held corporations raised less of threat to the public-as-investors. It also derived, in part, by a belief that greater privacy concerns were raised by access to information about non-public companies; these were frequently small concerns more closely associated with the identities of their proprietors (Kornhauser, 1990).

The debate about access to corporate tax information was, however, also tied to the debate about access to personal tax information. Here is the second chapter of the story regarding access to corporate tax information. The 1934 pink-slip provisions applied to corporate tax information as well as personal tax data. Upon repeal of the law in 1935, access to corporate tax information became subject to the same general rule as personal tax information: public record status plus Executive Branch regulatory authority. As David Lenter, Joel Slemrod and Douglas Shackelford (2003, 813) concisely summarize the ensuing period until 1976, "What precisely this public classification meant in practice varied over time with changes in the rules governing publicity."

The Policy Debate

What were the policy reasons in favor of access to tax returns? What were the arguments against access? In examining the different perspectives, I select one spokesperson, former President Benjamin Harrison, in favor of publicity for tax returns, and another, Secretary of the Treasury Andrew Mellon, for the case against it. The pleas of these advocates for the opposing policies will also be supplemented by additional arguments on either side.

Admittedly, the analysis of the views of the two spokespeople, Harrison and

Mellon, runs the risk of being ahistorical. After all, Harrison expressed his views in 1898, and Mellon in 1925. Different historical and political trends were present in these periods for tax policy. I wish to draw this contrast, however, to illustrate deeper policy currents, that is, ones that were present during both periods, and, indeed, continue to be relevant. Without slighting the differences between 1898, 1925, and today, one is indeed struck by how contemporary many of their arguments sound to modern ears.

For Access

Regarding the arguments in favor of access, former President Benjamin Harrison made a passionate case for public disclosure of tax information before the Union League Club of Chicago in 1898 (Harrison, 1901). Harrison's address came at a time when federal taxes were raised through assessments on personal property, including real estate and securities. These federal taxes were levied, however, only on a limited group of the highly affluent.

At that time, self-reporting was also accompanied by lax enforcement and an inability to achieve fair appraisals of real estate. There was also a lack of a governmental ability to track the personal property on which taxes were levied. Harrison cited a confession of a tax court in Maryland, responding to an inquiry of the state tax commissioner, "We utterly fail in reaching private securities of any description. Here and there only have they been returned by some conscientious holders" (Harrison, 1901, 348).

Harrison identified two policy reasons in favor of access to tax information. First, he pointed to the common interest that all citizens shared in the state's meeting its fiscal goals and their fellow citizens' fulfilling their financial obligations to the state. As a consequence of these interests, there was a general public right to tax

information. Second, Harrison identified a link between tax confidentiality and tax evasion. In general, he argued, "The plea of business privacy has been driven too hard" (Harrison, 1909, 338). These two claims merit examination in additional detail.

Concerning the first point, Harrison fervently spoke of the patriotic and moral duty of all citizens to contribute their just share of public expenses. A kind of partnership existed between citizens, and, as in business, one partner was obliged to another to meet his individual obligations. The partnership concept also meant that each individual had the right to find out how his colleagues were performing. As "members of a great partnership, ... it is the right of each to know what every other member is contributing to the partnership and what he is taking from it" (Harrison, 1901, 356). Each citizen therefore, possessed a "personal interest, a pecuniary interest, in the tax return of his neighbor" (Harrison, 1901, 355).

Concerning the second point, Harrison emphasized the fashion in which confidentiality allowed the wealthy to shirk their proper obligations. Confidentiality allowed cheating on taxes, and the result was—to restate the argument using a modern elocution—a race to the bottom. Harrison described the consequences of widespread cheating of taxes: "One man sees that his neighbor is not making a conscientious tax return, and that if he returns his property honestly he will pay disproportionately. The result is that his conscience finds a salve in saying, 'Everybody does it'" (Harrison, 1901, 349).

Publicity, Harrison assumed, would create social pressure to end improper behavior and assure more accurate self-reporting. It would also prevent worse dangers. In particular, Harrison spoke of his fears that there would be a backlash against the affluent should the wealthy shirk their fiscal duties. In this part of his speech, Harrison drew a curtain back to

reveal some of the tensions of the Gilded Age—a period of the creation of tremendous private wealth as well as one of great social unrest.

Thus, Harrison argued for public access to tax data. Judge Richard Posner would later articulate a general argument concerning how publicity increases social compliance, and privacy undermines it. Just as Harrison worried in 1881 about privacy allowing shirking of full payment of one's taxes, Posner in 1978 warned that "[m]uch of the demand for privacy ... concerns discreditable information, often information concerning past or present criminal activity or moral conduct at variance with a person's professed moral standards" (Posner, 1978, 399). The following decades would only heighten Judge Posner's skepticisms about limits of societal access to personal information (Posner, 2007).

There has also been a recent illustration, and an international one, of the link between publicity and social compliance. In April 2008, the tax authority of Italy briefly posted on its web site the declared earnings and tax paid by every Italian in 2005. According to the country's tax minister, "It's all about transparency and democracy. I don't see the problem" (Stevenson, 2008). Newspaper accounts of the action noted the high level of tax evasion in Italy, and the pledge of successive governments to tackle the problem of tax cheating. The tax authority posted the information without any prior announcement, and it quickly took the information down after a complaint from the country's data protection authority and a flood of public protest.

The publicity about each Italian's tax contributions also led to a moment of glory for Giorgio Armani, the famous Italian fashion designer. In 1996, he was convicted of bribery of a tax official. In 2008, however, it was revealed that he may have paid the most taxes in Italy in 2005: 19 million Euros taxes paid on 44

million Euros in income. Each reader can now take a moment to compare Armani's tax rate to her own.

Beyond the public's access to tax information, as in this Italian example, there is also an important argument for the government's access to tax-related and other financial information. The government's interest in broad access to such information grew along with the rise of the administrative state. In administering programs involving services and benefits, the state realized that it might reduce fraud and its costs by drawing on databases of personal information. As Thomas Beniger, a historian of technology, observes, "Only in the late 1910s and 1920s did bureaucracies begin to realize that the same hardware that processed numerical data might be used to process information more generally and thereby strengthen the control maintained by the entire bureaucratic structure" (Beniger, 1986, 408). In the IRS' own assessment regarding the historical growth of the sharing of tax data, the "1940's, 1950's and 1960's were marked by almost unrestrained growth in the use of tax returns by governmental agencies" (IRS, 2007, Ch 1-7).

Thus, during this time, there was more sharing of information within the government and less with the general public. The law adapted itself to permit and make easier the government's access to such financial information. As an illustration, we might consider the decline of the doctrine of *Boyd v. United States* (1886). In this case, government had issued a subpoena to compel Boyd, a merchant, to produce invoices on cases of imported glass. It wished to use these invoices for proof in a civil forfeiture proceeding; the underlying question was whether Boyd had paid custom revenues on imported plate glass from Liverpool, England. In its *Boyd* decision, the Supreme Court considered the attempt to gather this information tantamount to an attempt "to extort from the party his private books and papers

to make him liable for a penalty or to forfeit his property." The Court found that compelling testimony or seizing private papers to be used as evidence in this fashion violated the Fourth and Fifth Amendments.

In the modern age, the Supreme Court has significantly reduced this holding. It ruled in *U.S. v. Morton Salt* (1950), for example, that the Federal Trade Commission could compel special reports and information disclosure from corporations. It found "corporations can claim no equality with individuals in the enjoyment of a right to privacy" (652). Moreover, agencies could make inquiries into corporate matters so long as they were "within the authority of the agency, the demand is not too indefinite, and the information sought is reasonably relevant" (652).

Regarding individuals, as opposed to corporations, the Supreme Court in *Garner v. U.S.* (1976) ruled on the claim of an individual, a professional gambler, who made incriminating disclosures on his tax return instead of claiming a Fifth Amendment privilege against self-incrimination. The Court found that the defendant was foreclosed against invoking the privilege when the tax return information was later introduced against him in a criminal prosecution. The *Garner* Court stated, "[I]f a witness under compulsion to testify makes disclosures instead of claiming the privilege, the government has not 'compelled' him to incriminate himself" (654). In a similar fashion, "[t]he information revealed in the preparation and filing of an income tax return is, for purposes of Fifth Amendment analysis, the testimony of a 'witness'" (656). Of course, should the professional gambler plead the Fifth Amendment on his tax return, the IRS also has the power to prosecute him for willful failure to make a return and to summon him to appear and produce his records.

At this juncture, we return to the example of the Internet posting of tax returns in Italy. The government's posting of this

tax information can be seen as a clumsy albeit immediate way to supplement the inadequate administrative powers of the Italian tax authority. These shortcomings are as well known as the lack of individual compliance in Italy with tax obligations. As the *Wall Street Journal* summarized the situation, "Eluding the tax man is like an inverted civic duty in Italy" (Kahn and DiLeo, 2007).

Public access to personal tax data speaks to the need for public knowledge in changing otherwise private, or hidden, behavior. As one newspaper described the Italian attitude, "Why should I pay if no one else does?" (Fisher, 2008). Publicity of tax information in Italy was intended to shape norms. In a similar fashion, Benjamin Harrison had hoped that publicity would change the behavior of the rich of his day. The message: we all should be more like Armani. All and all, a successful culture of compliance is a complex creation to establish and maintain. A vicious cycle can be created in which the government's lack of ability to enforce the laws is accompanied by a lack of *compliance* with the law.

Against Access

A quarter-century after Harrison's address, Secretary of the Treasury Andrew Mellon offered a strong voice in favor of tax privacy. When he testified before Congress about tax privacy and other matters in 1925, much had happened since Harrison's speech regarding tax policy. In *Pollock v. Farmers' Loan and Trust Co.*, the Supreme Court, in 1895, had declared the federal income tax to be unconstitutional. The Constitution was amended to overcome the Court's objection, the Sixteenth Amendment became effective on February 25, 1913, and President Woodrow Wilson signed an income tax and tariff bill on October 3, 1913 (Weisman, 2002).

Once again, the resulting income tax was one that only reached a limited

number of affluent tax payers. In the day of Harrison and Mellon alike, most Americans paid their share of the cost of financing the government through tariffs on imports. These kind of taxes were efficient for the government to collect, and relatively difficult to avoid. In contrast, the income tax was an obligation for only the super-rich. In 1895, for example, the income tax applied to only two percent of American taxpayers (Weisman, 2002). In addition, the government's ability to monitor compliance was not improved beyond Harrison's day, and tax evasion was thought to be widespread.

Mellon's support for tax privacy rested on two grounds. One element reflected his general distaste for public access to personal information and strong preference for privacy. Second, Mellon believed that greater compliance would follow from confidentiality than disclosure.

As a matter of social norms, Mellon felt it was wrong for a member of the public to know about someone else's tax obligations. In testimony in 1925 before the House Ways and Means Committee, he argued, "There is no excuse for the publicity provisions except the gratification of idle curiosity and filing of newspaper space at the time the information is released" (Mellon, 1925, 9). This language echoed the concern of Samuel Warren and Louis Brandeis about the press in 1890 in their classic article, *The Right of Privacy*. For these two authors, "[t]he press is overstepping in every direction the obvious bounds of propriety and of decency" (Warren and Brandeis, 1890, 196).

Like Warren and Brandeis, Mellon was also a strong believer in the right of privacy. In his life as businessman and investor, he sought to avoid publicity about his dealings, and in this endeavor, he was largely successful. As David Cannadine, Mellon's biographer, states, he "was a businessman who had preferred to make his money in the shadows rather than in the glare of publicity" (Cannadine, 2007,

302). Later in his life, after a spectacular business career and long public service, Mellon would also have an additional reason to favor tax privacy. As I will discuss below, he became a plaintiff in a spectacular tax trial during the administration of Franklin Roosevelt, and one accompanied by determined Executive Branch leaks of his personal information.

A second element of Mellon's defense of tax privacy was that it would induce compliance. He drew an analogy with confidences shared with one's lawyer, which are, of course, protected from disclosure by attorney-client privilege. Mellon stated: "When the government does not know every source of income of a taxpayer and must rely upon the good faith of those reporting income, still in the great majority of cases this reliance is entirely justifiable, principally because the taxpayer knows that in making a truthful disclosure of the sources of his income, information stops with the government. It is like confiding in one's attorney" (IRS, 2007, Ch. 1-5). A client shares information with her attorney because a lawyer can give assurances of confidentiality—and ones that the legal system will honor. Similarly, Mellon felt that taxpayers would be honest only if the government did not further disclose the information that was shared with it.

There is also a further policy reason for limiting access to tax information, however, and one that has strong resonance today due to the government's increased ability to monitor compliance. Tax information is filed under compulsion— one must report earnings and other information to the government. Here is how the Privacy Protection Study Commission in 1977 discussed this element: "The Service's special powers of legal compulsion give it a unique ability to acquire information" (Privacy Protection Study Commission, 1977, 6). As a consequence, "the individual taxpayer is inherently at a disadvantage vis-à-vis other agencies

that may have access to IRS information about him" (Privacy Protection Study Commission, 1977, 6).

For Mellon, like Warren and Brandeis, there was a right to keep one's information confidential—to be let alone. In contrast, as we have seen, Harrison took the opposite tack: publication of tax information was desirable because it would shame the affluent into heightened compliance with their tax obligations. Mellon questioned this belief: "The publicity is utterly useless from a Treasury standpoint" (Mellon, 1925, 8). He assured Congress that the Treasury Department had carried out a survey "of every supervising internal revenue agent in the different field stations and every collector of internal revenue." Their verdict was unanimous: "no additional tax has been collected due to the publicity provision, and all of them recommend its repeal" (Mellon, 1925, 8).

Today, we have gone from a period, reaching from Harrison's day to Mellon's and beyond, during which the government was poorly equipped to oversee tax compliance. At present, the government in the U.S. has a great ability to track wage income, investments, property sales, and other events with tax implications.

A general debate about publicity and compliance will continue as scholars draw on social norm theory and other disciplines to consider the optimal level of revelation of individual behavior. Recently, Kornhauser even has argued that the time has come to increase public access to personal tax information—albeit not full disclosure, or as she put it, not "the Full Monty" (Kornhauser, 2005). Yet, neither the public nor the government is likely to favor a re-introduction of the pink-slip approach abandoned in 1935. In October 2000, for example, the Office of Tax Policy provided a strong recommendation to Congress against a general publication "of the names of nonfilers or delinquent taxpayers." It found that any benefits from such publication were "speculative at best

and do not warrant taking the risk of inaccuracies or other adverse consequences that may undermine taxpayer confidence in the tax system" (Department of the Treasury, Office of Tax Policy, 2000, 5).

Publicity is entirely not a dead letter in tax law, however, as demonstrated in two areas. First, through press releases, the IRS publicizes its adverse determinations and penalties assessed against individual taxpayers. Such disclosure can be considered as a more targeted approach to the idea that publicity will induce compliance. Here, negative information is intended to stop the public from thinking of tax evasion in these terms: "Everyone does it and gets away with it."

Second, publicity plays a role in the corporate area. As I will discuss below, the IRS now allows access to corporate tax information to shareholders with at least one percent of a company's stock. Moreover, the Securities and Exchange Commission (SEC) makes a wide range of corporate tax information available to the investing public. As a final example, the tax rules for non-profit organizations require public filing of detailed information—including some salary information. This relative greater publicity for corporate tax information is not surprising. There are strong differences in the concepts of "privacy" in the policy debates concerning disclosure for personal and corporate tax information.

To be sure, defining privacy is a notoriously difficult enterprise. Nonetheless, it is fair to say that we associate the concept of privacy most strongly with dignitary, liberty, and/or quasi-property interests of *individuals* as opposed to *corporations*. It is for this reason that the Supreme Court in *Morton Salt*, as we have seen, stated that "corporations can claim no equality with individuals in the enjoyment of a right to privacy."

One might wonder, in fact, why corporations should have any rights against disclosure of their tax information. Here,

Lenter, Slemrod, and Schackelford (2003) provide a useful series of answers. Before noting their answers, I wish to observe that the co-authors ultimately find a compelling case for *increasing* the amount of corporate tax information released to the public—albeit stopping short of advocating full disclosure. Nonetheless, Lenter and co-authors also identify some grounds for granting at least some level of privacy for certain aspects of corporate tax returns. Among these grounds are that disclosure of certain information might reveal valuable business information to competitors and create confusion about accounting and tax practices or corporate activities.

THE PRESENT

Prior to the Tax Reform Act of 1976, federal tax returns were considered "public records," but ones available only upon order of the President and rules and regulations prescribed by the Secretary of the Treasury. As the IRS Disclosure & Privacy Law Reference Guide summarizes this past regime, "Under this scheme, the Executive Branch essentially created all the rules regarding disclosure" (IRS, 2007, Ch. 1-1). By 1976, a consensus view identified two problems with this approach. The first problem concerned the delegation of power to the Executive Branch; the second, the legal default in favor of disclosure unless a regulation required confidentiality.

In the aftermath of Watergate and the Vietnam War, there was widespread skepticism in the U.S. about Executive Branch power. Revelation of widespread misbehavior by the administration of Richard Nixon fueled these doubts. Specific to the context of tax law, moreover, congressional investigations at the time revealed that President Nixon had misused his discretion under the tax code to gain access to the income tax returns of perceived opponents. The Nixon Administration had also

sought to target certain individuals for IRS audits and to gain information from the IRS about certain audits in progress. As a result of these activities, the House's proposed bill of impeachment for Nixon, among its other articles, mentioned his abuse of powers under the tax code (IRS, 2007, Ch. 1–8).

Hearings in the Congress at this time also demonstrated that other Presidents had abused their discretion to gain access to tax returns. Franklin Roosevelt was one of these perpetrators. As David Cannadine states, "Roosevelt relished using both the Bureau of Internal Revenue and the Department of Justice to pursue vendettas against some of his rich antagonists, encouraging them to unleash tax inspectors and prosecutors like crusaders against the 'malefactors of great wealth'" (Cannadine, 2007, 514). In Mellon's case, Roosevelt and his administrators were "determined to pursue Mellon" regardless of any conclusions reached by the Treasury Department (Cannadine, 2007, 514). After a dramatic tax trial, and three months after Mellon's death, the Board of Tax Appeals ultimately delivered a verdict that completely exonerated him of the charges that he had sought to evade payment of income taxes.

Beyond the problem of delegation of power to the Executive Branch, the second problem was with the legal default of disclosure. Congress and other entities, such as the Privacy Protection Study Commission, believed by 1976 that this regime had led the IRS to release too much information with other parts of government. The Tax Reform Act changed this approach. It took power away from the Executive Branch and established a general statutory rule of tax return confidentiality.

Congress enacted the Tax Reform Act of 1976 during the period of its creation of the first generation of modern American privacy statutes. The list of these laws is a long and distinguished one. These statutes include Title III of the Omnibus Crime

Control and Safe Streets Act of 1968 (the Wiretap Act)(regulating electronic surveillance for law enforcement purposes); the Fair Credit Reporting Act of 1970 (regulating credit reporting agencies); the Privacy Act of 1974 (regulating only federal agencies' information practices—despite the expansive title of the statute); the Family Education Rights and Privacy Act of 1974 (regulating access to student records and limiting disclosure of these documents); the Right to Financial Privacy Act of 1978 (regulating banks' and other financial institutions' as well as federal agencies' access to consumer financial information); and the Foreign Intelligence Surveillance Act of 1978 (FISA)(regulating the conduct of "electronic surveillance" for foreign intelligence purposes) (Regan, 1995). These laws collectively reach both private— and public—sector information practices.

In 1976, the Tax Reform Act's privacy provisions altered the previous approach to the confidentiality of tax information. Instead of a default of publicity that confidentiality regulations could modify, this law established a rule of confidentiality to be altered only through statutory exceptions. As Section 6103(a) states, "Returns and return information shall be confidential," and, "except as authorized" by the statute, are not to be disclosed by an officer or employee of the U.S. or any state. In a nutshell, only explicit authorizations enacted into statute can trump the general mandate of the confidentiality of tax return information. Each authorization is also to establish the process under which tax information may be obtained. The idea is that the statute will thereby serve to cabin the government's discretion.

Section 6103 contains a large number of specific disclosure authorizations. In considering the overall picture, we see that Congress has amended Section 6103 over the years to legislate many of the previous kinds of disclosure once permitted through Executive discretion. Congress

has also amended Section 6103 to respond to new concerns, such as allowing access to tax information to combat terrorist activities. Although section 6103 now contains numerous disclosure authorizations, the statute has also considerably narrowed Executive Branch discretion to grant itself access to information.

The list of authorizations in Section 6103 can be characterized as long and extensive. To begin with one set, the IRS can release tax information to Congress and the President. For example, the head of a congressional committee is to make a written request to the IRS for release of the sought-after tax information and fulfill detailed annual reporting requirements regarding requests (Section 6103(f)(1-3)).

As for the disclosures to the President and Executive Branch employees, they require a written request of the President "signed by him personally" (Section 6103(g)). The Executive Branch and executive agency heads can also request a limited subset of tax information about certain Presidential and federal government employees. This information is restricted to whether the potential employee has filed returns in the immediately preceding three years, has failed to pay any tax or was assessed any civil penalties for negligence or fraud, or has been under investigation for criminal fraud. These provisions generally set low substantive bars to disclosure. To limit abuses, this part of the statute relies on a faith in publicity and a paper trail.

Other disclosure authorizations permit the Department of Treasury and Department of Justice to gain access to tax information for purposes of tax administration. Tax returns can also be disclosed for use in judicial or administrative tax proceedings. Beyond tax administration, a federal district judge or magistrate can issue an ex parte order granting access to tax returns to federal officials who are preparing for a proceeding pertaining to "the enforcement of a specifically designated federal

criminal statute (not involving tax administration) to which the United States ... may be a party" (Section 6103(i)). These orders are to be granted when there is reasonable cause to believe both that a specific criminal act had been committed and that the return "is or may be relevant to a matter relating to the commission of such act."

An emergency exception also exists to the general rule of confidentiality. The emergency provisions are limited to circumstances involving either "an imminent danger of death or physical injury" or "the imminent flight of any individual from Federal prosecution" (Section 6103(i)(3)(B)). Should these disclosure preconditions be met, the Secretary of the Treasury is permitted to release return information "to the extent necessary to apprise appropriate" law enforcement officers of such circumstances.

Since 2001, Section 6103 has also permitted the Secretary of the Treasury to release tax return data to inform appropriate officials of terrorist activities. This authority supplements the more general authority of the Secretary, already noted above, to disclose information regarding criminal activities or emergencies. For terrorist activities, the statute sets up a two-part scheme, which turns on whether or not the tax data came from the taxpayer ("tax return information") or from another party ("tax information").

To release tax return information that does not come directly from the taxpayer, the Secretary must find that the information "may be related to a terrorism incident, threat or activity," a low substantive standard. Once this standard is met, the Secretary is permitted to release the data to the head of a Federal law enforcement agency "to the extent necessary" to respond to the threat (Section 6103(j)(3)(C)). To disclose tax return information collected from the taxpayer, the statute obliges additional process: the IRS must seek an ex parte order from a court.

Information filed by a taxpayer can be disclosed if a showing is made to a federal district court that "there is reasonable cause to believe, based on information believed to be reliable, that the return or return information may be relevant to a matter" relating to a "terrorist incident, threat or activity" (Section 6103(j)(7)(C)).

Section 6103 contains a grab bag of other permitted disclosures. For example, the statute authorizes disclosures of tax information, including the address and wage information of taxpayers, to child support enforcement agencies in the states. This information allows the tracking of parents with child support payment obligations, and assists in identifying their employers to permit the garnishing of wages. The statute also authorizes disclosures to the Social Security and Food Stamp Programs, and to federal and state agencies that seek an offset in a taxpayer's refund for debt to another Federal agency or state income tax obligations.

At the same time, however, Section 6103 also blocks the broadest kinds of disclosures allowed under the old regime. The Privacy Protection Study Commission noted of the legal situation prior to enactment of the Tax Reform Act, "Under existing regulations, information about taxpayers may be provided by the Service to the head of any Federal executive agency, for use in 'matters officially before' him or her" (Privacy Protection Study Commission, 1977, 2). Such a "kitchen sink" justification for disclosure is no longer present in the statute.

Finally, a few words should be added about the current status of public access to corporate tax information. Section 6103 allows release of tax information to "any bonafide shareholder of record owning one percent or more of the outstanding stock of such corporation" (Section 6103(e)(1)(D)(iii)). Even more importantly, SEC rules, dating from 1973, require disclosure by publicly traded corporations of detailed information about its federal

income taxes and aggregate data on its state income taxes. This information is filed annually with the SEC on Form 10-K, and is available online as part of the SEC's EDGAR database. As Richard Pomp concludes regarding public access to corporate tax returns, "The SEC has essentially preempted the issue by mandating the disclosure of extensive data by publicly traded corporations" (Pomp, 1993, 412).

In addition, the Tax and Trade Relief Extension Act of 1998 requires public disclosure by non-profit organizations pursuant to their application for tax exemption and annual filing of information with the IRS. The codification of this requirement is found in the Internal Revenue Code at Section 6104(d). Non-profit organizations file this information on IRS Form 990. Among the information required of it, a non-profit organization must list the names and salaries of its five most highly paid employees.

THE FUTURE: TAX PRIVACY EXCEPTIONALISM?

What would a crystal ball show for the future of access to tax return information? One can begin by noting an insight of Yogi Berra, philosopher and member of the Baseball Hall of Fame: "It's tough to make predictions, especially about the future." Nonetheless, and at the risk of going out on a ledge, I wish to predict that the privacy of tax return information will become both more and less important in the future. More helpfully, I predict that different aspects of tax privacy will prove of greater and lesser significance over the next decades.

Less Important

Section 6103 provides a significant and detailed framework that regulates access to tax return information. Nonetheless, this statute is less important than other privacy laws regarding financial infor-

mation. This relative lesser status will continue in the future, and reflects the overall lesser significance of tax return information within the universe of personal information that different entities, public and private, now collect, process, and transfer. In addition, the kinds of personal information available have now come to dwarf even the data found in one's tax return.

Consider the vantage point of 1960: I was not yet filing tax returns, but my parents were, and, at that time, the tax return constituted the single most detailed source of personal information about most Americans in the government's control. Today, there are multiple sources of information about all Americans found in databases of public and private organizations. Some of this information is also available to the general public.

The government now provides convenient online access to some of its databases, which has made it far easier to access this information. For example, property tax information has traditionally been available, but only if one wished to trek down to the registrar at the local county business office. Today, information about the property tax of one's neighbor is usually only a few clicks away.

Regarding the private sector, Zillow and other commercial websites estimate the price of real estate to allow easy satisfaction of the kind of idle curiosity that Mellon deplored. Simple use of a search engine or access to social networking sites provide additional ways to satisfy such curiosity about others. Credit scoring now provides a single numerical point of reference about someone's financial worthiness. Data brokers, such as ChoicePoint, also collect personal information, maintain it in databases, and extract value from it by comparing and combining it with other information and then reselling it (Schwartz and Janger, 2007). These companies gather information from a variety of sources, including public records.

There has also been a steady growth of statutory laws and regulations that set rules for access to financial and other personal information. Section 6103 generally plays a lesser role in the information privacy landscape today than these other laws and regulations. The leading statutes governing access to financial information are the Fair Credit Reporting Act, the Bank Secrecy Act, and the Gramm–Leach–Bliley Act. As an example, banks and other financial institutions must file reports with the Treasury Department about suspicious financial transactions, including those involving relatively small sums. Such reports are filed by financial institutions filed pursuant to the Treasury Department's "Know Your Customer" Rules, enacted under the Bank Secrecy Act. These regulations might also be termed the "Report to the Government on Your Customer" Rules.

As far as the FBI is concerned, National Security Letter provisions in the Right to Financial Privacy Act and the Fair Credit Reporting Act permit it to gain access to certain kinds of financial information without a court order. The FBI must only certify that the sought-after records are relevant to an authorized foreign counterintelligence investigation (12 U.S.C. §§3403(b), 3414).

The consequences of these developments? The government, the private sector, and sometimes even the general public have numerous opportunities to gain access to the same types of information that in the past were found exclusively in tax returns. As a result, Section 6103 is only one of a long list of statutes that regulate the use and disclosure of personal information. And the kinds of personal information available today exceed the data found in an income tax return.

Another trend has been that discretion, once again, is present regarding access to financial information—including the type of information that appears in tax returns. To be sure, Section 6103 has restricted

the Executive Branch's ability to access tax returns and distribute tax return information throughout government. Yet, discretion has re-emerged, for example, in the Bank Secrecy Act of 1970, which requires banks and other entities to maintain records of financial information with "a high degree of usefulness in criminal, tax, or regulatory investigations" (12 USC 1829b(a)(2)). The Act grants considerable authority to the Secretary of the Treasury to promulgate bank recordkeeping and reporting requirements to further this goal.¹

More Important

Thus, Section 6103 is less important than a host of other laws and regulations in the overall scheme for financial privacy, let alone information privacy. In one regard, however, tax privacy is becoming more important than before: threats of data breaches and data leaks now make the security of tax return information a highly significant issue. Data security law is an area of tax privacy that is more important than it has ever been.

The focus of data security law is on preventing unauthorized access to personal information. Today, we live in an age of data hacks and breaches and other losses of personal information—some quite spectacular. The problem is also far from limited to the U.S. In the U.K., for example, the department of Revenue and Customs lost data discs in November 2007 with information concerning 25 million Britons (Hurst and Sherman, 2007).

In the U.S., no such spectacular loss of tax or benefit information has (yet) occurred. The IRS does work, however,

in a data-intensive environment. It has approximately 240 computers systems and more than 1,500 databases. As the Treasury Inspector General noted in a 2007 report, IRS employees "are required to take sensitive taxpayer information out of the office on laptop computers to carry out their audit and collection responsibilities, increasing the risk that information could be lost or stolen" (Treasury Inspector General, 2007b, 2).

The problems of data security for tax information are heightened by four developments of particular significance. First, more Americans file their tax returns with the IRS every year through e-filing. Rather than filing a 1040 form with the IRS via the postal service, the taxpayer or provider uploads an electronic tax return through e-filing to a designated IRS web site. The growth in e-filing statistics has been remarkable; the IRS announced that as of May 2007 almost 60 percent of all tax returns for that tax year were sent to it electronically. Tax professionals filed almost 55 million of these returns, and taxpayers filed more than 22 million from their home computers.

The rise of e-filing also means greater risks for data security. Once a tax return is digitalized, it can easily be shared, transmitted, and breached. Moreover, risks might arise through misbehavior of the e-file provider herself. The Treasury Inspector General has called for improved screening and monitoring by the IRS of e-file providers "to protect both the taxpaying public and Federal Government from losses resulting from actions by unscrupulous [p]roviders" (Treasury Inspector General, 2007a, 5).

¹ One aspect of the discretion concerns the kinds of records to be retained by financial institutions. Another relates to the nature of the identification documents to be supplied by parties. The Secretary is to decide which bank records have a "high degree of usefulness" to the goal of the Act and to require copies of these records to be retained along with identification records of the party into whose account it is to be deposited or collected. The Bank Secrecy Act also allows the Secretary to determine the required retention period for this ID information. The resulting regulations require banks to report information to the IRS on depositors who engage in transactions exceeding \$10,000 or above. The regulations also allow the Secretary to grant exemptions from the requirements of the regulations.

Second, tax preparation software, like other software, is subject to hacking, viruses, data security breaches, software failures, as well as use of online tracking tools by professional tax preparers. A few examples will suffice. In 2000, H&R Block's online tax filing service experienced a technical problem that exposed sensitive client data. Clients who logged on to the H&R Block site were allowed to see other individuals' personal data instead of their own. The problem appeared to have been due to a software glitch rather than an outside attack (Macavinta, 2002). In 2005, the *San Francisco Chronicle* reported that electronic services provided by leading tax preparation firms used Web bugs to track information about online visitor's browsing habits (Lazarus, 2005). A web bug is an object, usually invisible, placed on a web page to allow monitoring of users at that site and beyond.

Third, tax returns may be prepared by U.S. firms that outsource work internationally. Proposed IRS regulations would address this practice of sending tax information around the globe electronically to be processed by workers in low-wage countries.

The proposed regulations provide that tax return preparers must obtain a taxpayer's prior written consent before disclosures to tax return preparers outside the U.S. The IRS explained the policy behind this regulation: "The written consent for disclosure of tax return information outside the United States is needed because it is difficult for the Secretary [of the Treasury] to pursue a criminal action ... against a tax return preparer located outside the United States or to collect a civil penalty" against this party (IRS, 2006, 5, Proposed Sec. 301.7216-2(b)).

Fourth, the IRS already has faced the same problems as the private sector concerning data security. The Treasury Inspector General in an audit report filed in March 2007 reported that "hundreds

of IRS laptop computers and other computer devices had been lost or stolen, employees were not properly encrypting data on the computer devices, and passwords computers were not adequate" (Treasury Inspector General, 2007c, 1). The report also found that backup data stored at offsite facilities were not encrypted and lacked adequate protection. In sum, there are now threats of privacy meltdowns, or dramatic loss of gigabytes of personal information, in a way that was unthinkable in the age of paper tax returns.

The End of Tax Privacy Exceptionalism? The End of Tax Privacy?

Earlier in this paper, I analyzed policy arguments for and against tax disclosure and tax confidentiality. In both approaches, however, there was a shared assumption of a special status for tax information. This shared perspective is that of tax privacy exceptionalism.

From today's perspective, tax privacy remains exceptional in the sense that it is subject to the dedicated sectoral legal regime of Section 6103. Tax information is subject to a specific legal regime of access and use restrictions, and these rules are tailored to fit a series of different processing contexts. It is also exceptional in that it is filed under compulsion—although there is no shortage of personal data about any person, no other set of such detailed information must be filed each year and with such significant legal consequences possibly to follow.

Tax information is no longer exceptional, however, in other ways. The government in its tax administration follows a data-processing model that it uses in other managerial areas. The IRS gathers information about income from employees, investments from financial service companies, outstanding government loans from other branches of the federal government, and a broad variety

of other data points about financial events. Its databases are well stocked, and its electronic systems provide it with a kind of power to oversee taxpayer compliance that was unthinkable in the age of either Harrison or Mellon. The IRS is also likely to continue to seek new ways of collecting and comparing information to narrow the "tax gap" in the U.S. Moreover, much of the essential regulation for personal financial information occurs outside of the tax context. Section 6103 gives personal tax information relatively strong protection, but its regime extends only to "returns and return information" (Section 6103(a)). From this perspective, Section 6103 is just (another) statute about a subset of financial information. In conclusion, one's tax information and tax privacy remain important, but are increasingly subject to the same forces, legal, social, and technical, as other personal information.

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